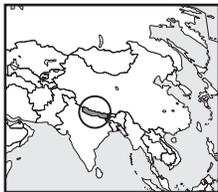


# The urgent need to mobilize public resources to finance development



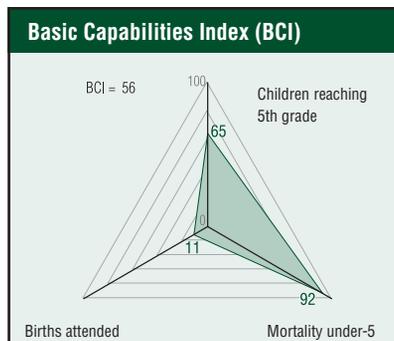
The trend to increasingly allocate the country's scarce resources to security and debt servicing has led to diminishing financing for social and economic development and poverty alleviation in Nepal. With the recent return to multi-party rule and the start of peace talks between the Government and Maoist insurgents, there is hope for a renewed focus on pro-poor and participatory development processes.

## Rural Reconstruction Nepal

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Nepal's political crisis – which deepened from 2002 to 2006 with the transfer of power from a series of weak elected governments to King Gyanendra<sup>1</sup> – reached a new transition point in April 2006, when the King was forced to restore power to an elected parliament after mass popular demonstrations. But even before the King usurped control and further stalled development, Nepal – already categorized as one of the world's least developed countries – was suffering under the burden of a Maoist insurgency and a feudalistic socio-economic system. The insurgency began in 1996 after people became dissatisfied with the country's elected leaders, following the advent of representational democracy six years earlier.<sup>2</sup>

Since then, the conflict has caused thousands to be wounded and disabled, and resulted in the death of more than 12,000 civilians, the abduction and displacement of an estimated 64,000 people, and the destruction of billions of rupees of government and private infrastructure (HMG/N Office of the Prime Minister and Council of Ministers, 2006, p. 27). Additionally, a leading newspaper recently reported that the Government's spending capacity in development activities has also been collaterally damaged (Khanal, 2006). As a result of political and governance problems, quality of life has deteriorated and the economic growth of the country has been negatively affected.<sup>3</sup> Those who have been the worst hit are the marginalized communities and indigenous

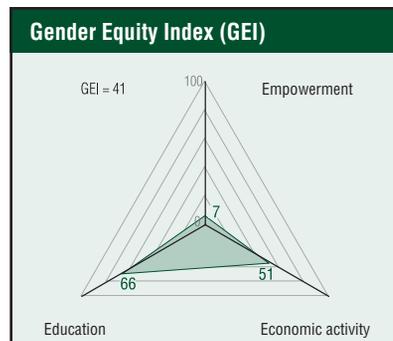


people, who historically have been the most deprived of economic, social, political and human rights.

## Domestic budget processes and macroeconomic policy

Nepal's macroeconomic policies have been ineffective in addressing poverty alleviation issues, and have been particularly unable to promote pro-poor growth and equitable income distribution. This is largely because macroeconomic policies are structured according to international liberalized financial and trade regimes. The current national development plan, the Tenth Plan (2002-2003 to 2006-2007), mainly focuses on poverty alleviation through liberalization of the economy and concentration of government resources on physical and social infrastructure. Although the Government has declared that under the Ninth Plan, the percentage of people living in poverty decreased from 41% to 32%, many have questioned these figures and the structures and effectiveness of such policies in truly addressing poverty (GCAP Nepal, 2005).

The State has also been unable and unwilling to incorporate a pro-poor and inclusionary approach in its budget-making processes. Women, Dalits ("untouchables"), Janajati (indigenous) and other ethnic groups and the disabled have rarely been given the chance to play a role in policy decisions and in the formulation and monitoring of national development plans and policies. In fact, the United Nations Development Programme (UNDP, 2004, p. 11) evaluation of the country's governance structures in relation to poverty has identified the ab-



sence of citizen participation in the decision-making processes as one of the foremost weaknesses in the system. Furthermore, disruptions caused by the civil war have now made public consultations impossible in the many districts where rebels maintain effective control.

As the provision of basic services is necessary to reduce poverty and move the development process forward for the rural poor, the conflict situation has further compounded the financial vulnerability of the marginalised population. The Government has continued to increase its security-related expenditures at the expense of social and economic service expenditures, and the poor have subsequently become increasingly poorer and unable to access social services. In fiscal year 1997-1998, for example, the total security expenditure rose steadily and accounted for 9.03% of the budget. By 2003-2004, the allocated budget for security increased even further to a startling 16.58% of the total budget (GCAP Nepal, 2005, p. 9).

Meanwhile, budget expenditure for social development and economic development dropped from 18.40% and 31.90%, respectively, of the total budget in the year 1997-1998, to 14.98% and 18.74% in the year 2003-2004 (GCAP Nepal, 2005, p. 9). This decrease in the development budget has compromised the content, range and reach of government programmes and services and this has been detrimental to those who need them most.

At the same time, a large proportion of the allocated budget for social services and development goes under-utilized due to the non-release of the

1 King Gyanendra seized absolute power in February 2005. His rule curtailed fundamental human rights and crushed any political and development progress made until that point.  
2 After a series of unresponsive governments failed to deliver on their promises – specifically and significantly along the lines of caste, gender, ethnicity, social exclusion – the Maoist armed insurgency began to take form and gain power.  
3 The country's economic growth, which stood at about 5% on average during the 1990s, dropped to 2% in 2004-2005 against estimated growth of 4.5%. In 2005-2006 growth is expected to be the same and per capita income will decline as in 2004-2005. Nepal's Civil Society Report, 2006, p. 10.

budgeted amounts. The *Kathmandu Post* has estimated that 48% of development budget allocated for the 2006 fiscal year will not be spent by the end of the year. In the health sector, of the allocated NPR 7.68 billion, only 34.5% was distributed, and in the education sector only 54% of the allocated NPR 21.05 billion was spent. In some projects, such as the "Education for All" project, this figure dropped to 11% of the budget (Khanal, 2006, p. 7).

As regards gender budgeting, it is primarily the Ministry of Women, Children and Social Welfare (MWSCW) that conducts this kind of analysis. Although the MWSCW develops its own programme budget that integrates key elements of the Convention on the Elimination of All Forms of Discrimination Against Women (CEDAW) and is responsible for ensuring that gender equality is engrained in those of other ministries, it has little influence on the latter's programme budgets. Considering inflation, the 2003-2004 budget of the MWSCW has actually declined in comparison with past years as a result of volatile funding. This kind of uncertainty and the under-utilization of the budget has led to the inefficient programming of government-funded projects (MPEG, 2003).

### Access to credit

Access to credit sources is important in upgrading the socio-economic status of the marginalized and poor sectors of society. However, less than 20% of the population have access to institutional credit, and small, marginal and landless households have practically been barred from institutional borrowing, as 86% of formal credit is provided against the collateral of land and property.

Moreover, Nepal's formal financial system caters largely to the urban population. As agriculture is instrumental in reducing poverty, the lack and high cost of credit has resulted in its stagnation. For instance, none of the expectations of liberalization, such as the extension of the organized credit market to more rural areas, increasing access for small capital borrowers, or more efficient and productive use of financial resources have been achieved even partially (Acharya *et al*, 2003).

### Lack of transparency, inefficiency and corruption

State efficiency, accountability and transparency are prerequisites for addressing poverty, and there is much work to do in these areas. Development projects implemented with both loans and grants, for instance, have been highly affected by corruption, unaccountability and non-transparency (Thapa, 2004 as cited in GCAP Nepal, 2005, p. 43). This is particularly reflected in "excessive political interference at key appointments in the project cycle, increasing corruption and leakage, politicization of the civil service and insecurity among the public officials which leads to either delaying sensitive decisions or passing even the routine matters to higher levels." (Acharya *et al*, 2003)

Capital flights have also been attributed to the State's inefficiency and corruption in managing its affairs. Historically, many of the companies with access to foreign accounts have also been the ones with the most links to the royal regime, so that many have supposedly transferred money out of the country before they can be caught and brought to trial. During the royal takeover, the palace gave itself a blank cheque to the State's financial resources, and began siphoning as much as possible into its private bank accounts abroad. The State's inability to influence financial transfer transactions also includes the financial impunity of the ruling classes; the role of India in influencing tariff setting and financial management; the lack of experience and understanding among successive governments about the impact of international trade treaties on Nepal's economy; and the huge amounts of red-tape that discourage inward investment.

Moreover, transparency issues have been one of the major problems plaguing Nepal since the advent of democracy in 1950. Even before this historical date, the feudalistic nature of Nepal lent itself to a feeling that the country and its assets belonged to its rulers. At present, transparency is still a problem with detailed programme costs difficult to verify within the relevant government ministries.

Lastly, as regards corruption, Nepal's trade and investment have been negatively affected by the whimsical changes in decisions made by corrupt politicians. Corruption has affected the implementation of some of the most important development projects in the country, including the Kali Gandaki 'A' (KGA), Nepal's largest hydroelectric project (Chintan, 2004, cited in GCAP Nepal, 2005, p. 43). The Index of Economic Freedom, published by the Heritage Foundation, gives Nepal a very poor rating on such issues as inefficiency and pervasive corruption. The impact of corruption on the poorest also has direct negative repercussions, as those who cannot afford to pay bribes are denied rights such as citizenship papers and land registration.

### Susceptibility to global economic factors

As one of the world's least developed countries (LDCs), Nepal is easily susceptible to adverse effects from economic policies imposed upon it, particularly those related to liberalization-oriented reforms. The liberalization process has intensified the process of impoverishment and is increasing the disparity of income and access to resources. A vicious circle of poverty-powerlessness-poverty has resulted, and few of the 'poverty alleviation' strategies have actually made a difference in terms of promoting opportunity, facilitating empowerment, enhancing security and increasing "people's participation" (Acharya *et al*, 2003).

Nepal's accession to the World Trade Organization (WTO) in 2004, as the first least developed nation to join, alongside Cambodia, has not yet resulted in any putative benefits. This can be primarily traced back to the two types of commitments

that are required for a country to receive WTO membership: (1) reducing trade barriers and (2) regulations and processes in the domestic economy. Nepal lacks the institutional capacity, understanding of the issues at play and money needed to carry out these measures.

Nepal's products – which are handicapped by a lack of human, technological, as well as financial resources – have a difficult time meeting the standards required for competitive trade as set by WTO. When looked at from the perspective of the poor, meeting such standards may actually hurt them. Additionally, other WTO agreements also limit both the incentives necessary for promoting small and medium enterprises, and the country's ability to impose conditions on foreign investors for using local materials. According to the UNDP, "all in all, failing to mitigate such impacts through policy interventions can disempower people and widen the development gap." (UNDP, 2004, p. 42)

### Foreign aid and debt

External financial assistance has contributed greatly to the Nepali national economy, especially to the development and agricultural budgets. In 2003-2004, foreign grants and other aid accounted for 57.65% of the development budget and 3.82% of the GDP, at market prices (MoF/HMG/N 2005 as cited in GCAP Nepal, 2005, p. 38). The share of assistance to the social sectors has also been relatively high, although when one considers the integral relationship between access to the social sectors and poverty alleviation, it is not substantial enough.<sup>4</sup>

Gradually, Nepal is falling into a debt trap with the accumulating foreign debt being increasingly offset by debt service liabilities and worsening rates of internal revenue mobilization. Fresh loans are now being taken to service past loans: the proportion of debt service to net annual borrowing increased three-fold between 1989-1999, when it was 43.78%, and 2002-2003, when it reached 121.43%. In other words, debt service payments actually exceeded net annual borrowing (GCAP Nepal, 2005, p. 41). In fact, within the eight years after the restoration of multiparty democracy, public debt increased seven-fold, forcing the country to put aside 3% to 4% of the GDP and 15% of the annual budget for debt servicing (Sharma *et al*, 1998 as cited in SAAPE, 2003, p. 128). It is currently estimated that more than half of the annual government revenue goes to foreign debt servicing (Pradhan, 2000, as cited in SAAPE, 2003, p. 128).

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<sup>4</sup> In the education sector, the share of aid was calculated at 22.03% of the total expenditure in 2003-2004.

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The trend to increasingly allocate the country's scarce resources to security and debt services has stalled the progress made in achieving the Millennium Development Goals by 2015 and made the goals seem practically impossible to attain. It seems ironic that the rationale for acquiring debt is to address development needs in order to alleviate poverty. On the contrary, however, as millions of dollars are being spent to pay off the foreign debt, the fight against poverty has made little headway. Over the years, "the poor in whose name foreign aid has been provided became poorer and those who ruled became richer." (GCAP Nepal, 2005, p. ix)

In essence, foreign aid has failed to alleviate the country's poverty. This is largely due to the following factors: the lack of good governance and political will of the governments; the pursuance of donors' own strategic interests rather than bringing about meaningful social and economic development; political interference in bureaucratic functioning causing frequent changes in project management; and ineffective monitoring and feedback systems (SAAPE, 2003, p. 128). The non-sustainability of foreign aid projects has also been a problem. In order to ensure effectiveness, sustainability and prioritization of key areas for foreign assistance, it is recommended that foreign aid development programmes be initiated, formulated and implemented with local participation (Acharya *et al.*, 2003).

### Solutions proposed by civil society

According to the Asian Human Rights Charter, development means the realization of the full potential of the human person and rights of people, including the right to participate in the affairs of the State and the community (Taiwan Association for Human Rights, 2006). The State has an obligation to ensure that its development aid approaches are reflective of these rights. In fact, the Nepali Constitution states that the government will "pursue a policy which will help promote the interests of the economically and socially excluded groups and communities by making special provisions with regard to their education, health and employment." (Article 26, HMG/N Ministry of Law, Justice and Parliamentary Affairs, 2004) The current intra- and inter-state policies do not yet strive to meet this goal.

Civil society organization (CSO) coalitions have been outspoken over such violations of the rights of the marginalized and poor. Civil society is actively engaged in campaigns that advocate total unconditional cancellation of Southern debts.

Many CSOs have also taken up the fight over the disproportionate expenditures allocated to the military and police, and the collapse of state interventions in the education, health and infrastructure sectors. Their specific solutions reinforce the political line advocated by the political parties and the Maoists, to realign spending and policy priorities to meet the peoples' needs. A more decentralized and pro-poor framework – one that effectively addresses

the problems of exclusion, discrimination and disempowerment – is envisioned to replace the current centralized, elite-driven state apparatus.

Civil society should increase lobbying efforts to ensure that such a debate does not get pushed off the table. Lobbying efforts would advocate to ensure that the voices and presence of the country's women, disadvantaged and poor be allowed to prevail in national policy formulation debates. Furthermore, such efforts could call for a more pro-poor framework to be integrated into the market system, with more built-in incentives helping to expand small and medium enterprises.

The championing of good governance through administrative reforms, reduction in discretionary authority and a sound economic system based on competition and rule of law, could also help the country's trade and economic growth. Policy-making processes must undergo capacity building enhancement in order to be more responsive to the people's needs and include an institutional structure facilitating power-sharing for women and the marginalised and poor sectors, as well as a better feedback system from the grassroots level. Glaring corruption must be checked alongside the progressive opening of the economy to international capital (Acharya *et al.*, 2003).

With the return to multi-party rule in April 2006, and the start of peace talks between the Government and Maoists, there is hope that there will be a renewed focus on pro-poor and participatory development processes. Civil society can be instrumental in this effort by being pro-active in engaging in national debate and focusing discussions on the needs and rights of the marginalized, women and poor sectors of society. ■

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## PARAGUAY

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- Development of human capacity and the reduction of poverty are not achieved by merely raising the level of resources available. Efforts must be oriented toward eliminating inequalities.
- Poverty requires structural actions, economic and social reform and actions focused on inclusion and capacity development in the most vulnerable sectors.
- The development of information systems and mechanisms that assure transparency in public administration is fundamental.
- Social investment impacts growth. Poverty limits national possibilities of growth and development. Reducing inequalities is as necessary as economic growth.
- The problem is not merely coverage but equity. Access to government and public services is one of the principal causes of social exclusion. ■

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