E-Seminar Title: First NSC E-Seminar No 1, 2007: The State's Role in Private Sector Development in New Nepal
Subject: Designated Discussant's Comment on Ms. Mallika Shakya's Paper
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The Background

Nepal experienced significant all-round improvements in economic and human development between 1995-96 and 2003-2004. The incidence of poverty fell from 42 to 31 percent. Health and education outcomes improved, particularly for girls and people living in remote areas[1]. Such findings, of the National Living Standard Survey of 2003/04, show that Nepal made considerable economic progress even during the twelve years of conflict. However, Nepal's economy grew only by 2.7 to 3.8 percent between 2003 and 2005, compared to 7.7 to 7.9 percent average for South Asia, and by the declining rates of 2.7 percent in 2004/05 and 1.9 percent expected in 2005/06.[2]

The recent peace accord with the Maoists provides new hopes to move ahead more vigorously. Most countries have accelerated growth through private sector development (PSD). What are the main hindrances and the opportunities for Nepal?

Main Issues

Political Factors. Conducive political climate is a fundamental prerequisite. Ms. Shakya's paper recognizes this but seems much more optimistic than might be warranted. The Maoists' participation in competitive politics could prove to be a HUGE wishful thinking. The first question is how will the Maoists behave if they lost the next election considering that they went to the jungle when they lost the last time? Secondly, what will be the Government's attitude if Maoists came to power or shared power in a coalition? The Maoists have been openly announcing that the agreement with other parties was only a stepping stone to achieve a full-fledged communism. Their leaders have denounced private ownership of properties. Will a Maoist Government behave like the Chinese, the West Bengal Communists or the Cubans? Will there be other possible political conflicts, like the recent Madhesi protests?

Institutional and Governance Factors. A recent story in the Economist (February 3-9, 2007) starts as follows: *Once upon a time, not so long ago, there was a poor continent. Its name was Europe. Then it discovered three things: the free market, the rule of law and science-based technology. Now it is rich....simplistic perhaps, but the same thing happened in North America, with the same consequences, and it is now happening in Asia...*

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[1] *Resilience Amidst Conflict*, the World Bank, Asian Bank and DFID, 2006.
[2] Economic Survey 2005/06, Ministry of Finance.

Ms. Shakya cites that Nepal ranked 100 out of 175 countries in Ease of Doing Business Index. The Government too admits that: *Investments could not be attracted due to lack of legal and institutional framework for the protection of investments, inflow and repatriation of capital, flexible labor policy, and standard accounting and auditing system in place for ensuring good governance in the private sector*[3].

Nepal can radically alter the situation and stand out in the area. All South Asian countries lag significantly in dealing with private sector. Nepal, as a smaller country, has advantage over larger countries. India's experience can greatly help in developing institutional framework or rules. I wonder if an internationally participated watch-dog body could be established in Nepal to guarantee efficient implementation of a trustworthy PSD mechanism which will be fair and completely free from red tape. This could provide Nepal with that "niche factor" needed to compete in the global market, attracting entrepreneurs from India and other countries. (Of course, there could also be other potential niche products like hydro-power, tourism, tea, herbs, etc.)

India/China Factor. I agree with Ms. Shakya that Nepal could benefit immensely by acting like a *jholunge* (bridge) between two economic giants, shining India and roaring China, instead of maintaining the old thinking of *yam between rocks*. Nepal could largely meet her quest for FDI and technology transfer without turning too far. But Nepal must make efforts to maximize FDI and technology transfer through smart fiscal policies, no red tape PSD environment and continued good economic relationship with neighbors. For example, competing with India will be more difficult in most areas but Nepal can involve influential Indian entrepreneurs in her private sector and use their goodwill to preserve Nepal's interests just like US traders lobby for overseas suppliers.

Manpower Export. Manpower export and remittances will continue to be extremely important for Nepal for the foreseeable future. This is important for employment, income generation for relatively poor populations, to meet Nepal's balance of payments and for the liquidity needs of the economy. This can also prepare workers for more productive work when they return. In recent years, manpower export to third countries (other than India) has grown very significantly, especially to the Middle East and East Asia. The remittances have grown from 3 percent in 1995/96 to over 12 percent in 2004/05. The following data <u>during the first eight months of 2004/05</u> demonstrate the importance[4]:

Workers remittances:	NRs 36,060 million
Gorkha remittance:	NRs. 1,996 million
Total goods export:	NRs 36,948 million

Export of manpower must, therefore, be facilitated properly through the establishment of training facilities to enable better income, through improved recruitment management to prevent exploitation by bad contractors, and by establishing efficient and trustworthy remittance facilities to prevent cheating by unscrupulous middlemen.

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[3] Economic Survey, 2005/2006, Ministry of Finance.
[4] Economic Survey, 2004/05, MOF.