

## Nepal's Statement on LDC Graduation for 2021 Triennial Review

### 1. Introduction

Nepal has been included in the Least Developed Country (LDC) category since 1971. In line with the outcomes of the subsequent LDC Conferences, the priority areas including productive capacity, agriculture, food security, trade, social development, environmental risks, and development finance continue to remain an integral part of Nepal's national policies and programs. Implementation of the 2030 Agenda and aspiration to graduate from the LDC category underpin Nepal's development efforts.

The Constitution of Nepal includes provisions that foster good governance, development, justice and prosperity. New laws and regulations have also been enacted to cater to the needs of the vulnerable segments of society. Nepal has been currently implementing the 15<sup>th</sup> Periodic Plan (Fiscal Year 2019/20-2023/24) along with a Long-Term Vision 2043, under the national aspiration of 'Prosperous Nepal, Happy Nepali'. The Government of Nepal is committed to sustainable graduation of the country from the LDC category.

Our efforts have yielded some good progress in socio-economic development such as poverty reduction, education, and health. The average economic growth rate for FY 2016/17- 2018/19 was 7.3 per cent.

During past decades, the incidence of multi-dimensional and headcount poverty has reduced significantly. The prevalence of undernourishment, stunting and wasting among children has also decreased remarkably. In health sector, the maternal mortality rate has declined to 239 per 100,000 live births. The net enrolment rate in primary education has reached 97.2 per cent. Also, the basic water supply coverage has reached 91 per cent and the basic sanitation coverage has reached 99 per cent. Similarly, the access to electricity has reached 90 per cent

of households while the per capita annual electricity consumption has increased to 260 kilowatt hour.

With affirmative action, women's participation at decision-making levels in both private and public sectors has increased remarkably. Women's representation in elected bodies and civil service has reached about 41 per cent and 24 per cent, respectively. The social protection coverage has been expanded to about 17 per cent of the population. The Government of Nepal has ensured fiscal federalism based on capacity, expenditure needs, equity, and balanced development at provincial and local levels.

The GNI per capita income of Nepal was US\$ 745 against the graduation threshold of US\$ 1230 in the last triennial review. The gap in per capita income against the threshold level remained about 40 per cent. The gap between the threshold and current status has declined, however it is still below the threshold level. The recent CDP estimates for 2021 triennial review show GNI per capita US \$ 1027, HAI 75 and EVI 24.2. However, the COVID-19 pandemic has posed tremendous challenges to sustain and accelerate the achievements.

Nepal met the graduation thresholds for two out of three criteria, in the triennial reviews of 2015 and 2018. Nepal was also the first and only country being considered then for graduation without meeting the income criterion. Besides the low GNI per capita, the earthquake in 2015, border disruptions in 2015/16, and other disasters including floods in 2017 hampered the economic growth. Further, as Nepal had met HAI and EVI thresholds by only a small margin, the question of sustainability of graduation without relapsing into the LDC category loomed large. In that context, Nepal requested the CDP in 2018 for the deferral of its consideration for graduation to the triennial review of 2021.

## 2. [Impact of COVID-19 in the National Economy](#)

The COVID-19 pandemic has had adverse impacts on the lives of people and the socio-economic condition of the country. Tourism, transport, and manufacturing

sectors are hardest hit by the pandemic. Education, construction, agriculture, trade, and supplies have also been severely affected. In addition, the production of goods and services, supply chain and service delivery have been disrupted.

According to the preliminary assessment, the economic growth was estimated to be about 2.3 per cent against the target of 8.5 per cent in FY 2019/20. Revenue mobilization, capital expenditure and private sector investment have been affected by the measures and interventions undertaken to prevent, control and mitigate the pandemic.

During the last fiscal year, inflation remained at 6.15 per cent, imports decreased significantly by 15.6 per cent while exports increased slightly by 0.6 per cent. The further impacts due to shocks in both demand and supply sides have been witnessed in the economy.

The remittances that constitute about 25 per cent of GDP decreased by 0.5 per cent in FY 2019/20, against 16.5 per cent increase in the previous year. Additionally, the number of Nepali workers receiving approval for foreign employment decreased by 96.8 per cent in the first quarter of 2020/21 against 3.7 per cent decrease in the same period of previous year. This may not only drastically plummet the inflow of remittances in the future but also exacerbate the problem of unemployment in the country.

The pandemic has also severely impacted the industry sector. The actual investment from the newly registered industries was far below the expectation in FY 2019/20. The agriculture sector has also been adversely affected due to the disruption in supply chain, and obstruction in plantation and seasonal harvesting.

A significant number of workers, particularly seasonal and temporary workers, workers in small and cottage industries and internal migrants, have lost their jobs during the pandemic. Due to the pandemic, highly vulnerable people are likely to fall back into poverty.

The travel restriction has severely affected the tourism sector. Also, the government had to roll back the flagship campaign 'Visit Nepal 2020' that had an

aim to bring 2 million tourists into the country. This resulted in job loss in the formal and informal sectors associated with it.

As of 31 December 2020, a total of 260.5 thousand individuals have tested positive for COVID-19 and 1856 lives have been lost. The pandemic has created new challenges in health, education, livelihoods, and overall economic activities amidst various pre-existing vulnerabilities arising from being landlocked, natural disasters and deepening climatic crisis, among others. The pandemic severely hit the health sector due to inadequate health infrastructure, and lack of equipment and human resources to handle the increasing number of cases in the country. The outpatient department services have decreased during the lockdown and regular health services have been disturbed which has had a negative impact on nutritional programs and services leading to an increased vulnerability of the poor, pregnant and new mothers, children, senior citizens, and people with disabilities.

Due to the pandemic, about 35 thousand schools have been closed and about 8.7 million students have been directly affected. Most of the educational institutions across the country had been used as quarantine facilities. School closure may result in an increased school dropout rate in the short run and create major human capital losses in the long run thereby widening the existing gaps in education.

Operationalization and completion of most of the National Pride Projects and Game-Changer Projects have been delayed due to the pandemic. It will pose cost and time overruns in these projects resulting in low capital formation in the economy. The impacts of COVID-19 pandemic combined with natural disasters and climate change will severely hit the most vulnerable segment of the population.

### 3. Recent Government Initiatives

Considering the impact of COVID-19, the Government of Nepal has concentrated its efforts towards controlling and mitigating the pandemic through appropriate plans, policies, and programs.

The Government also introduced relief packages including social protection measures targeting daily wage earners, the poor and other vulnerable people. Likewise to address the mounting economic crisis, the government provided tax rebates and facilities of delayed payment of taxes to the business and industrial community. Concessional loan facilities have also been provided to the severely affected sectors.

The Government has prioritized health, employment, agriculture, infrastructure, and social development in the annual budget of the current fiscal year. The budget has given priority to people's safety through the protection of citizens from all kinds of disaster and diseases. It has also focused on reviving the economy, enhancing social welfare, and building a resilient economy.

Furthermore, the 15<sup>th</sup> Periodic Plan has envisioned a long-term vision with 10 national goals. Besides that, national strategies, drivers of transformation and enablers as well as National Pride Projects, Game Changer Projects, major programs, and projects under the public private partnership have been identified in the Plan. Also, the national level result indicators as well as the provincial level indicators have been identified in the results framework of the Plan.

#### 4. Possible Impacts of Graduation

LDC graduation is a milestone for a country moving towards sustainable development. It will impact access to concessional development finance and trade preferences, which are the enablers of development of the country.

Nepal's exports comprise primarily of light manufacturing based on imported raw materials, such as readymade garments, textile, yarns, iron and steel, and domestic agricultural and agro-processed products. There is high trade cost of being a landlocked country with poor infrastructure, inadequate transport, logistics and trade measures. After graduation from the LDC status, Nepal would face challenges in diversifying markets and products, as the existing market would face higher tariffs and stringent rules of origin.

Due to loss of access to trade related special and differential treatment after graduation, Nepal could face challenges of developing export capacity. While the graduation may have no impact on trade with India (Nepal's major trade partner with around 63% of trade) as it is through duty free market access that is not contingent on Nepal's LDC status, it will have an impact on trade with the United States and the European Union. After graduation, Nepal will lose preferential market access available under the European Union's Everything But Arms (EBA) scheme and concession granted under Generalized System of Preference (GSP). Among preference giving countries and regions, the United States and the European Union account for 11.2 per cent and 10.45 per cent of the exports, respectively. LDC graduation would result in the loss of around 3.7 per cent export to these countries with more than half of the export loss on trade with the European market.

Moreover, export loss from preferential market access accounts for more than 10 per cent and it impacts the top 10 products. Also, loss of preferential market access and increased competition in the international market would disproportionately impact export-oriented small and medium enterprises and employment generated by them. This loss could affect agricultural and industrial sectors and its impact would be on the poor, vulnerable and marginalized groups of the population due to low investment in public goods and loss of employment opportunities. The loss of preferential treatments will also hamper the prospects of Nepal's trade diversification.

As a WTO member and an LDC, Nepal receives flexibility in applying many WTO rules and these flexibilities will not be available after the graduation. Nepal will lose flexibilities on the Trade-Related Aspects of Intellectual Property Rights (TRIPs) agreement for promoting infant industries, use of Trade-Related Investment Measures (TRIMs) for pharmaceutical products, and access to provisions on export subsidies and other agreements made for LDC during the Doha round.

LDC graduation entails phasing out of access to LDC-specific international support measures provided to overcome structural impediments to growth and sustainable development such as targeted Official Development Assistance (ODA) for LDCs that includes concessional financing, and technical assistance and other support measures. In Nepal, foreign assistance has a notable importance on the fiscal system as ODA flow in relation to GDP was about 5 per cent in 2019/20. ODA has significant role in financing the capital and development expenditure as its share is more than 60 per cent. However, the proportion of ODA on the domestic budget has decreased from 15.1 per cent in FY 2015/16 to 11.2 per cent in FY 2019/20. Hence, the government expects to receive more ODA which could be affected after graduation. However, the multilateral development partners make ODA decision based on the income category. Nepal is at the cusp of ‘dual transition’, with graduation from low-income country status to lower-middle income country in addition to the graduation from LDC category. Moreover, specific instruments designed for LDCs such as Least Developed Countries Fund (LDCF), Enhanced Integrated Framework (EIF), and Technology Bank for the LDCs and United Nations Capital Development Fund (UNCDF) would no longer be available.

On a positive note, LDC graduation would increase the country’s creditworthiness and boost foreign direct investment as Nepal would be branded as a potentially competitive destination leading to an opening of new avenues for private investment inflows.

## 5. Nepal’s Readiness for Graduation

Despite being the first and only country set to graduate without meeting the income threshold, Nepal is looking forward to the graduation process with a belief that it will be accorded with all possible measures to ensure sustainable graduation and smooth transition. Graduation from the LDC category is not an end in itself, but an important milestone in the development trajectory. Despite the loss of the specific benefits and privileges, graduation can be expected to bolster Nepal’s self-confidence, and incentivize robust mobilization of resources, for realizing the

national aspiration of ‘Prosperous Nepal, Happy Nepali.’ Graduation has remained an integral component of national ambition and plan documents, backed by the commensurate political will.

The consideration for graduation was deferred in 2018, citing the concerns over the sustainability of progress as well as the fallout of disasters including the 2015 earthquake. In the ensuing years after the last triennial review, the progress has been made across all three criteria. The income growth saw a sustained trend, while the progress was seen in HAI and EVI as well. While anticipating the positive trend to further continue in the future, Nepal takes this as an encouraging sign to dispel the apprehension about the sustainability of the graduation.

Nonetheless, Nepal is aware of the up-front costs associated with the loss of LDC status –especially with the end of LDC-specific international support measures as well as challenges posed by COVID-19. As the country is at the cusp of dual transition from the low-income category as well as LDC category, the loss of access to concessional financing could be further accentuated. Meanwhile, the avenues opened by innovative financing tools including blended finance, support from the private sector partnerships, growing interest in impact investment among others provide a wider menu to choose from. If allowed with adequate preparatory time, Nepal could better navigate the alternative sources for financing its development.

Trade will be another area with a considerable impact of graduation. While the large bulk of trade of Nepal is limited with India, the terms of which are not contingent upon the LDC category, other large trading partners including the EU and the US accord preferential trade measures which will be lost upon graduation. Unfortunately, Nepal has not been able to make the best utilization of the LDC specific measures on trade and thus, as indicated in DESA’s Ex-Ante Impact Assessment, the loss from current base will not be largely pronounced. Nepal is aware of the imperative to make the best use of the LDC-specific preferential markets as well as further diversify its trade by increasing supply-side

competencies. Therefore, a longer preparatory period would, allow Nepal to minimize the costs ensuing from the loss of preferential trade measures.

While we express our readiness for graduation, the impact of COVID-19 on the economy is a significant driver of some element of doubt. The extent of such impact has not yet been made available due to the time lag in data as well as the chain effects of the current measures on near term and longer-term prospects of the economic growth and human development. Despite the setback by the pandemic, Nepal is hopeful of a quick rebound after the situation stabilizes hopefully in 2021, and thus is considering the option to graduate favorably.

It is in this context, that Nepal is ready to start the preparations for graduation from the LDC category, with a just expectation that the CDP will recommend for providing Nepal a longer preparatory period of 5 (five) years. Such an extension of the preparatory period will allow Nepal to work towards diversifying the options for financing as well as utilizing the trade measures and bolstering the readiness of business sector for competitive trade after the graduation becomes effective, taking into account the smooth transition measures that would be available after graduation in a phased manner.

## 6. Expected Support Measures

During the transition phase, Nepal will require generous support from the international community in economic and social sectors particularly in infrastructure development, productive employment, increasing production and productivity for the sustainable graduation. Also, upgrading health-related infrastructure, enhancing the quality of education, sustainability of social security scheme will be of utmost priority. Moreover, international support will be needed to improve information communications technology, reduce the digital divide, and develop the human capital.

International support measures will be required for productive transformation and safeguarding the economic activities and financing huge gaps for achieving the SDGs. Moreover, during post-graduation, preferential market access should be

continued to promote international trade and increase exports. As a WTO member, Nepal seeks export subsidies on pharmaceutical products among others, which could be protected through patent as well.

## 7. Commitment and Conclusion

The Government of Nepal will prepare a transition strategy in consultation with all stakeholders. The strategy would analyze short and long-term effect following graduation and respective institutions will be approached for the continuation of concessional financing and other facilities received as an LDC. The institutional arrangement required for preparedness of upcoming graduation is significant. To prepare for replacement of preferential access in export, the Government of Nepal will carry out capacity development in international trade and Nepal's Special and Differential Treatment (SDT) will be further deliberated in the obligations of WTO. Meanwhile, improvement in economic governance will be emphasized.

To prepare the transition strategy, the Government of Nepal will coordinate and consult with its bilateral and multilateral development and trading partners, to adjust their development assistance over the transition period considering its level of development and existing international support measures. The transition strategy will focus to facilitate a smooth transition without any disruption in the development path and with an emphasis on the sustained momentum. It should involve gradual 'phasing out' arrangements as opposed to a sudden loss of concessions, as these are deemed vital to the country.

For sustainable graduation and beyond, Nepal will strive to develop productive capacities through investment on human capital, infrastructure, and universal health coverage, promote entrepreneurship, reduce inequalities, and build resilience. So, the Government, along with increasing its capital expenditure, will focus on improving the productive capacities through both public and private sector investments and achieve multiplier effects of employment creation and economic growth.

In conclusion, the Government of Nepal is optimistic about graduation from the LDC status with the preparation of a robust transition strategy. Nepal requests the Committee for Development Policy to recommend a longer preparatory period of 5 (five) years to enable adequate preparation for ensuring a smooth, meaningful, irreversible, and sustainable graduation.