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NEPAL AND THE EUROPEAN COMMUNITY

CO-OPERATION STRATEGY

2002-2006

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LIST OF ABBREVIATIONS

ADB	ASIAN DEVELOPMENT BANK
AEPC	ALTERNATIVE ENERGY PROMOTION CENTRE
ALA	MANAGEMENT COMMITTEE ON ASIA AND LAT. AMERICA
APP	AGRICULTURAL PERSPECTIVE PLAN
BIWMP	BAGMATI INTEGRATED WATERSHED MANAGEMENT PROGRAMME
BPEP II	BASIC AND PRIMARY EDUCATION PROGRAMME
CBOs	COMMUNITY-BASED ORGANISATIONS
COPE	COMMUNITY-OWNED PRIMARY EDUCATION PROGRAMME
CSP	CO-FINANCING SUPPORT PROGRAMME
DANIDA	DANISH INTERNATIONAL DEVELOPMENT ASSISTANCE
DDCs	DISTRICT DEVELOPMENT COMMITTEES
DFID	DEPARTMENT FOR INTERNATIONAL DEVELOPMENT
DGM	DONOR GROUPS MEETINGS
DKK	DANISH KRONER - DOE DEPARTMENT OF EDUCATION
DPCP	DECENTRALISED PLANNING FOR CHILD PROGRAMME
EC	EUROPEAN COMMISSION
ECHO	EUROPEAN UNION HUMANITARIAN OFFICE
EIB	EUROPEAN INVESTMENT BANK
EIDHR	EUROPEAN INITIATIVE FOR DEMOCRACY AND HUMAN RIGHTS
ESAP	ENERGY SECTOR ASSISTANCE PROGRAMME
EU	EUROPEAN UNION
FDI	FOREIGN DIRECT INVESTMENT
FYP	FIVE-YEARS PLAN
GARDP	GULMI & ARGHAKHANCIRURAL DEVELOPMENT PROJECT
GDP	GROSS DOMESTIC PRODUCT
GNI	GROSS NATIONAL INCOME
GNP	GROSS NATIONAL PRODUCT
ha.	hectare
HMG/N	HIS MAJESTY'S GOVERNMENT OF NEPAL
HR	HUMAN RIGHTS
IBRD	INTERNATIONAL BANK FOR RECONSTRUCTION & DEVELOPMENT
IDA	INTERNATIONAL DEVELOPMENT ASSOCIATION
IDP-MWR	IRRIGATION AND DEVELOPMENT PROJECT OF THE MID-WESTERN REGION
ILO	INTERNATIONAL LABOUR ORGANISATION
ILO/IPEC	INTERNATIONAL PROGRAMME ON THE ELIMINATION OF CHILD LABOUR
IT&C	INFORMATION, TECHNOLOGY AND COMMUNICATION
JC	JOINT COMMISSION
JDPC	JOINT DISTRICT PEOPLE'S COMMITTEES
KVMP	KATHMANDU VALLEY MAPPING PROJECT
LDC	LEAST DEVELOPED COUNTRIES
LGP	LOCAL GOVERNANCE PROGRAMME
LSA	LOCAL SELF-GOVERNANCE ACT
MTEF	MEDIUM-TERM EXPENDITURE FRAMEWORK
NCP	NEPALI CONGRESS PARTY
NDF	NEPAL DEVELOPMENT FORUM
NEWAH	NEPAL WATER FOR HEALTH (NGO)
NGO	NON-GOVERNMENTAL ORGANISATION
NCHR	NATIONAL HUMAN RIGHTS COMMISSION
NOVIB	NGO (Netherlands)
OIE	OFFICE NATIONAL DES EPIZOOTIES (France)
OPEC	ORGANISATION OF PETROLEUM EXPORTING COUNTRIES

p.a.	per annum
PAF	POVERTY ALLEVIATION FUND
PDDP	PARTICIPATORY DISTRICT DEVELOPMENT PROGRAMME
P.M.	PRIME MINISTER
PRSP/10 TH FYP	POVERTY REDUCTION STRATEGY PAPER / 10th FIVE-YEAR PLAN
PESP	PESTICIDE ENVIRONMENTAL STEWARDSHIP PROGRAMME
REDP	RURAL ENERGY DEVELOPMENT PROGRAMME
RETs	RENEWABLE ENERGY TECHNOLOGIES
RGB	ROYAL GOVERNMENT OF BHUTAN
RJS	REFORM OF JUSTICE SYSTEM
RRM	RAPID REACTION MECHANISMS
SAARC	SOUTH ASIAN ASSOCIATION FOR REGIONAL CO-OPERATION
SPS	SANITARY AND PHYTO-SANITARY STANDARDS
T.A.	TECHNICAL ASSISTANCE
TRIPS	TRADE-RELATED ASPECTS OF INTELLECTUAL PROPERTY RIGHTS
TRTA	TRADE-RELATED TECHNICAL ASSISTANCE
UK	UNITED KINGDOM
UML	UNITED MARXIST-LENINIST
UN	UNITED NATIONS
UNCTAD	UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT
UNDP	UNITED NATIONS DEVELOPMENT PROGRAMME
UNHCR	UNITED NATION HIGH COMMISSIONER FOR REFUGEES
UNICEF	UNITED NATIONS CHILDREN FUND
UNPF	UNITED NATIONS POPULATION FUND
US	UNITED STATES
USA	UNITED STATES OF AMERICA
VDCs	VILLAGE DEVELOPMENT COUNCILS
vs	versus
WFP	WORLD FOOD PROGRAMME
WHO	WORLD HEALTH ORGANISATION
WTO	WORLD TRADE ORGANISATION
WUA	WATER USERS ASSOCIATION

Executive summary

The Kingdom of Nepal is inhabited by 23 million people, 86% living in rural areas, and 50% in the hills and mountains. Agriculture employs 80% of the population. Nepal remains an LDC (GDP per capita \$250), ranking 142nd in the UNDP's Human Development Index, despite the huge potential for exporting hydropower and tourism.

In 1990 Nepal began a new **democratisation** process, when a constitutional monarchy was established, incorporating a multi-party system with a legislature and locally elected bodies. After the Royal tragedy in June 2001, the situation in Nepal rapidly deteriorated. Conflict with the Maoists and the dissolution of Parliament (May 2002) led to the creation of a caretaker government headed first by PM Deuba, and then by PM L.B. Chand. New elections, scheduled for November 2002, were postponed because of security concerns. At present, Mr S.B. Thapa is the last P.M. designated by the King.

Since the proclamation of the ceasefire on 29 January 2003, both Government and rebel forces initiated peace process. The 27 August 2003 the truce was unilaterally interrupted by the Maoists and the negotiations collapsed. The main political parties in Nepal are feeling marginalised, complaining of the unconstitutional nature of the present government.

EC assistance to Nepal dates back to 1977 and totals €130 million. Current aid activities operate within the 1996 **EC-Nepal Framework Co-operation Agreement**. Development aid has been granted in areas such as irrigation and watershed management, animal health, reproductive health, primary education, refugees, and institutional capacity building.

The 2002-2006 EC strategy supports HMG/N development efforts as defined in the Agenda of Priority Reform Actions and the PRSP/**10th Five Year Plan (2002-2007)**. Addressing Nepal's foremost objective of **poverty reduction** involves: **broad-based economic growth** (development of agriculture, infrastructure, macroeconomic stability), **social sector development** (effective delivery of social services like education, health, culture) and **targeted programmes** (in favour of socially disadvantaged people), and **good governance** and **decentralisation**.

The EC's **co-operation strategy** will be **linked** to the economic and political situation in Nepal through appropriate initiatives in favour of the country's lasting development. **Long-term** support for the rural sector will focus on the Mid-Western Regions while the development of renewable energy (photovoltaic) will concern Nepal's rural areas with no access to electricity. Considering Nepal's present situation, special attention will be given to the finalisation of a coherent **Poverty Reduction** and **Conflict Mitigation Strategy** aimed at consolidation of democracy. While support for sustainable development remains the **long-term objective**, conflict mitigation and **consolidation of democracy** emerge as important corollaries of the long-term strategy, with **short-term** (RRM-Rapid Reaction Mechanism) support of local communities, local media and conflict monitoring and

medium-term initiatives (extension of RRM, support for **the Judicial system and promotion of Human Rights**). Assistance for the legislative elections is, for the time being, on standby until December 2003 and humanitarian assistance for refugees will also be considered on ad hoc basis.

Other areas of co-operation will include Nepal's integration into the International Economy with provision of technical assistance to facilitate Nepal's accession to the **WTO**, and to promote **trade** and **economic** activities

The EC's overall allocation to Nepal over the next five years is estimated at **€70** million.

A previous EC strategy document expired in 2001. In order to have a coherent presentation of the overall EC new strategy, the period covered by this document is 2002-2006¹.

Throughout the proposed strategy, the major concern will be **poverty reduction**, with due attention paid to cross-cutting themes of improving **governance** and enhancing the participation of the most disadvantaged social groups in development process. Similarly, promotion of the rule of law and human rights will help to sustain the national **reconciliation** process, and thus contribute towards the ultimate goal of peace and renewed confidence in the Nepalese political system.

1. EU CO-OPERATION OBJECTIVES

EC assistance to Nepal dates back to 1977. In June 1996, the EC-Nepal Framework **Co-operation Agreement** came into force, outlining the general conditions for providing EC technical assistance and co-operation. The Agreement is based on Nepal's respect for human rights and democratic principles. The objectives of the Agreement are **(i)** to develop two-way trade; **(ii)** to support sustainable economic development and improve the living conditions of the poorest strata of the population; **(iii)** to enhance mutual interests, economic co-operation and support the current move towards a market economy; and **(iv)** to support environmental protection and regional co-operation.

The general objectives of the EC Country Strategy are fully consistent with existing EU Treaties and Regulations. The **Treaty of the European Communities** (Article 177) sets out areas for co-operation such as the promotion of sustainable economic and social development, the promotion of trade between EU Member States and third countries, and the campaign against poverty. The **"ALA" Council Regulation**² of February 1992 states that respect of human rights, fundamental freedoms and democratic principles are preconditions for durable economic and social development (Article 2).

¹ Funds in support of the renewable energy sector have already been committed in 2002.

² Council Regulation (EEC) No 443/92 of 25 February 1992 on financial and technical assistance to, and economic cooperation with, the developing countries in Asia and Latin America, OJ L 52 of 27 February 1992, p. 1

“With poverty reduction as the central objective of the European Community’s development policy”³ the EC clearly stated the principle of sustainable, equitable developments to enhance the rules of economies of LDCs countries. **EC Development Policy**⁴ emphasises the link between trade and development, through support for:

- Institutional capacity building, particularly in the area of good governance, the rule of law and the implementation of macro-economic policies
- Regional integration and co-operation
- Transport, food security and sustainable rural development.

EC Co-operation objectives take into account the conclusions of the **Nepal Development Forum** (NDF) (Kathmandu-Pokhara, 4-7 February 2002), which underlined the importance of implementing poverty alleviation strategies, in response to a situation that has dramatically deteriorated over the last two years in political and economic terms.

EC Development Policy has also identified human rights and democratisation, gender and the environment as major cross-cutting issues. Considering the particular climate of instability in Nepal, the importance of democratic participation and reforms to relaunch economic growth has to be stressed.

Progress on economic and social development is largely dependent on political stability. In seeking to reduce poverty, mitigate conflict, consolidate democracy and integrate Nepal into the international economy, EC co-operation with Nepal is complementary to Nepal’s own development agenda (Section 2). EC co-operation is also co-ordinated with the efforts of other donors and Member States (Section 5.3), as required by the communication on EC Development Policy.

The EC objective of reducing poverty should at the same time address the main causes that have contributed to political instability. This strategy is therefore based on the Communication from the Commission on Conflict Prevention.⁵ In countries where there is the potential for conflict, there is a need to focus external aid on the "re-emergence of a favourable political environment", and on the root causes of the conflict with appropriate development initiatives.

2. NEPAL'S POLICY AGENDA

Nepal’s overriding development challenge remains to **reduce poverty**. HMG/N acknowledges this fact, and has incorporated its **Poverty Reduction Strategy Paper** into its key development programme – the **PRSP/Tenth Plan 2002-2007**. The Government’s approach to overall development is based on a **four-pronged** strategy.

³ COM (2002)429 Final, (Summary)

⁴ COM (2000) 212 Final

⁵ COM (2001) 211 Final

1) Broad-based Economic Growth

Poverty reduction is not possible without rapid economic growth which is both broad-based and sustainable. HMG/N will therefore act in favour of:

Accelerating growth in the agricultural sector, through improving the access of the poor to the market, to basic agricultural resources, and to domestic and foreign capital and technology.

Increasing Competitiveness through market-oriented policies, privatisation, deregulation and liberalisation, thus encouraging inflows of foreign capital into Nepal's economy.

Improving Infrastructure through promoting private sector investment, especially in the hydropower sector and areas with high employment potential.

Ensuring Macroeconomic Stability and Predictability through co-ordination of fiscal policies, and strengthening the capabilities of agencies dealing with the financial and corporate sectors.

2) Social Sector and Rural Infrastructure Development.

The priority for this sector is the effective **delivery of basic goods and services in:**

Education, with the focus on a more efficient school system; improving enrolment levels, especially of girls; and developing opportunities for vocational education.

Health, providing better management and an improved institutional framework, focusing on the participation of communities, NGOs and the private sector.

Social harmony: HMG/N also pursuing programmes to underpin the respect of cultural traditions and social harmony.

Women empowerment, gender equality and gender mainstreaming

3) Targeted Programmes for the most vulnerable social groups

In order to facilitate social integration and economic participation, HMG/N will focus on initiatives in favour of the most vulnerable segments of the population (people living in remote areas, the extremely poor, women, etc.) in particular, **employment generation programmes** will be promoted through the Poverty Alleviation Fund.

4) Governance

HMG/N is committed to improving governance in Nepal. Initiated in 1992 with the Decentralisation Act, and strengthened with the Local Self-Governance Act in 1999, **decentralisation** remains a priority area for HMG/N. The Tenth Plan pledges to enhance the efficiency of public services through a more equitable sharing of responsibilities and resources with local government units, and to improve the transparency, accountability and responsiveness of local institutions. **Corruption** is being addressed through the enhancement of the legislative framework and judicial system. The **Commission for the Investigation of the Abuse of Authority**, established as a watchdog in the public service, has already brought some persons holding different public positions including politicians to book for corruption.

The following aspect of Nepal's policy agenda as set out in the 10th Plan are also of particular interest in the context of EU-Nepal Co-operation:

- **Trade:** Nepal has replaced an import substitution strategy with one geared to promoting exports, and has taken a number of measures in this direction. Nepal has submitted an application for full membership of the **WTO**, and welcomes donor support in the technical preparation of its accession and afterwards.
- **Investment:** HMG/N has already enacted necessary legislation and as further pledged to make Nepal's foreign investment policies more liberal and transparent in order to attract more foreign investment into the country.⁶
- **Land reform and management:** HMG/N's land management policies will seek to maximise the productivity of land in Nepal, while increasing the access of the poor to land resources. HMG/N proposes to safeguard land records, to discourage keeping fallow land, to develop a National Geographic Information System, and to promote income generation activities for formerly bonded labourers.
- **Human Rights:** With the intensification of the conflict, human rights situation deteriorated. Though Nepal is party to more than 18 international human rights instruments, the implementation proved to be rather difficult. The **10th Plan** commits the government to strengthening the protection of human rights, and running projects to raise popular awareness of human rights.
- **Protection of the environment:** HMG/N acknowledges the importance of *sustainable* development. Special attention will be paid to the protection of the environment when utilising natural resources and developing infrastructure. One of the advantages of developing Nepal's hydropower potential will result in less wood consumption.

The PRSP/10th FYP is substantial and ambitious. However, in the past HMG/N has often found it rather difficult to implement its reforms effectively. It is intended that EC support will assist HMG/N in seeking to achieve its development goals while avoiding frequent inconsistency between development priorities, as determined by Nepal, and the priorities of donor countries and institutions. Projects and programmes excessively driven by donor demands, and with little domestic 'ownership', will inevitably reduce the effectiveness of external assistance. The EC has taken care to ensure that the present strategy is complementary to both the development priorities outlined in HMG/N's Tenth Plan and the objectives of the main development stakeholders in Nepal.

⁶ It has endorsed a paper prepared and published by the United Nations Conference on Trade and Development (UNCTAD) and the International Chamber of Commerce (ICC) entitled, 'An Investment Guide to Nepal'.

3. Country Analysis

3.1 Political Situation

3.1.1 Internal Situation

- **The Constitution of the Kingdom of Nepal, 1990**

Since November 1990, the Kingdom of Nepal has been a **constitutional monarchy** and a multi-party democracy. His Majesty King Gyanendra Bir Bikram Shah Dev is currently the Head of State of Nepal. The constitution established a two-tiered legislature, the National Council (60 members) and the House of Representatives (205 members). The members of the House of Representatives are directly elected for five years. The King appoints the leader of the party which commands a majority in the House of Representatives as Prime Minister. Other constitutional organs include the **Council of Ministers**, the **Council of State (Raj Sabha)**, which advises the King, the Supreme Court, the Public Service Commission, the Attorney General, the Auditor General, the Commission for the Investigation of Abuse of Authority and the Election Commission. The King is the Supreme Commander in Chief of the Royal Nepal Army.

- **History of the Maoist insurgency**

In 1996 the Maoists, originated following the split in the parental United People's Front, decided to abandon the democratic process and declared a '**People's War**'. Their initial goal was to remove the constitutional monarchy and parliamentary democracy and replace it with a Maoist 'people's republic'. Since 1996 over seven thousand Nepali people have been killed in the conflict.⁷ For five years, the Maoist guerrillas waged a low intensity, mainly rural war. In 2001, there were three rounds of peace talks between the Maoists and the Government, but these broke down in November when the Maoists pulled out of the talks and resumed conflict on an unprecedented level. For the first time, the Royal Army was used to contain Maoist insurgency following the declaration of a state of emergency (November 2001). The Maoists claim to have set up bases in some districts in Nepal, particularly in the Mid-Western region where the insurgency is strongest along with the designation of people's local bodies and no-go area for security forces.

- **Causes of the insurgency**

The **proximate causes** of the Maoist insurgency were rural poverty, uneven development between urban and rural areas, endemic corruption, persistent socio-economic inequalities and the frustration at the delivery of public goods and services from the governments. The Maoists leadership found its followers in rural parts of Western Nepal where the conflict originated mainly because of poverty, lack of basic amenities and perceived social discrimination.

The EC Conflict Prevention Assessment Mission in January 2002 identified the following contributory factors:

⁷ International Crisis Group Asia Report No 50, 10 April 2003

- **Uneven Development between Kathmandu valley and rural Nepal** – Despite decentralisation measures, power remains centralised in Kathmandu.
- **Endemic Corruption** – Corruption has intensified inequities.
- **The caste system** in Nepal maintains and strengthens socio-economic inequalities.

The Royal tragedy of June 1, 2001 threw Nepal into shock and contributed to worsen the political situation that also included the resignation of the Koirala government.

• **Political Instability**

In the 1990s, although Prime Ministers changed frequently, the constitutional democracy was never seriously endangered or rejected. However, with the intensification of the Maoist 'People's War', the political situation rapidly deteriorated. In August 2001 Sher Bahadur Deuba replaced Prime Minister Koirala. Following the failure of the peace talks with the Maoists on 23 November 2001, the King declared the State of **Emergency** on the recommendation of the Council of Ministers, which was adopted by an overwhelming majority of the House of Representatives. When the Government proposed a renewal of the state of emergency, there was a division of opinion in the ruling Nepali Congress Party. The lack of consensus in the ruling party finally led the Prime Minister to recommend to the King the dissolution of the House of Representatives. The King dissolved the House of Representatives and asked Mr. Deuba to act as '**caretaker**' Prime Minister until new general **elections** planned in November 2002. In the meantime, political parties suggested that the security situation in the country was not favorable for general elections. Following this development Prime Minister Deuba recommended to the King to take necessary action under Article 127 of the Constitution (removal of obstacles) for the postponement of the elections, since he found it impossible to hold elections within the constitutionally mandated period (six months). In October, the King removed P.M. Deuba from office for his inability to hold general elections as scheduled and replaced him with L.B. Chand.

Present Situation

A **ceasefire** was declared on 29 January 2003, first by the Maoists and quickly followed by the Government.⁸ Hopes that this ceasefire might herald real progress were buoyed by the signing of a common **Code of Conduct** (The 22 "Peacestones") on 13 March, to be implemented by both sides during the ceasefire. Both sides have pledged to seek a peaceful solution through dialogue, and to stop violent and aggressive activities. On the whole, the terms of the ceasefire have thus far been upheld.

One of the major problems still faced is that the political parties remain highly suspicious of the current negotiations, from which they have excluded themselves despite several HMG/N's attempts to accommodate their views through consultations at an all-party meeting. To translate cease-fire into a permanent peace, it is important to have cooperation from all walks of national life.

⁸ The Minister of Physical Planning and Works, Narayan Singh Pun, played a pivotal role in facilitating contacts between the Palace and the Maoists.

The present **truce** remains very fragile. Ending such a volatile political scenario requires further major efforts to progress with the present **confidence building** phase between negotiating parties⁹.

On 30th May 2003, Prime Minister L.B. Chand resigned and was replaced by the four times Prime Minister, Mr S.B. Thapa.

3.1.2 External Situation

The Kingdom of Nepal is a **landlocked** country in the Eastern Himalayas, bordered by the Tibetan region of China in the north and by India. In the East, West and South. Nepal has been pursuing a foreign policy that is based on and guided by the principles of **non-alignment**, Panchsheel (or Five Principles¹⁰), UN Charter, International Law and World Peace. Since early 50s, Nepal has been trying to develop country's external relations in both economic and political spheres.

Nepal's relations with **India** are comprehensive which have been marked by goodwill, understanding and cooperation despite disparity in size, population and economic development.¹¹

Nepal has friendly relations with **China** and it recognises Tibet as an integral part of China. The Tibetan refugees who came to Nepal in the past have been settled in different parts of the country.

Relations with **Bhutan** became problematic when approximately 93, 000 of Nepalese origin fled Bhutan and entered Nepal as refugees,¹² in early 1991. The refugees are at present in seven camps in the districts of Jhapa and Morang in Southeast Nepal. Recent figures indicate that the population has increased, mainly by natural growth, to over **100 000** people.¹³

In March 2001, negotiations (ongoing since 1993) between HMG/N and the Royal Government of Bhutan resulted in the **verification** process, a first step towards the

⁹ At the moment of the requested adoption by the European Commission of the CSP/NIP Nepal (2002-2006) and following the interruption of the truce the 27 August 2003, the conflict between HMG/N and Maoists goes on.

¹⁰ (a) Mutual respect for each other's State; (b) non-aggression; (c) non-interference in each other's internal affairs; (d) equality and mutual benefit; (e) peaceful co-existence

¹¹ Following the ratification of the historic Mahakali Treaty between India and Nepal in June 1997, the two countries concluded a **power trade** agreement, which provides for the participation of the private sector of both countries in the development of this essential source of Nepal's revenue. The 1991 Treaty of Trade between HMG/N and India sets up the conditions for facilitating trade through multilateral/mutually agreed concessions.

¹² UNHCR, December 1997

¹³ The EU has since covered most of the cost of the care and maintenance of the refugee camps via the UNHCR and the WFP.

solution of the refugee problem. Further progress has recently been made, but more resources and determination are required to achieve concrete results. The EC and other donors have repeatedly expressed their willingness to support a satisfactory solution and to provide assistance in the repatriation and settlement of refugees.

The basic objective of Nepal's **security** policy is to preserve Nepal's independence and **territorial integrity**. Nepal's armed forces number about 50,000 in total.

Nepal is one of the strongest advocates of **SAARC**. The presence of the SAARC **headquarters** in Kathmandu increases the strategic importance of Nepal as a focal point for South Asian Co-operation.

This organisation, while offering a potential platform for the countries of South Asia to accelerate the process of economic and social development, has not achieved its major goals due to persistent political internal difficulties. Any attempt to progress towards economic and commercial integration should be encouraged in particular to allow smaller Member States like Nepal to strengthen their competitive position and economic performances in relation to their neighbouring regional markets.

Nepal is fully committed to the principles of the UN Charter. It has also been actively engaged in UN activities, contributing highly reputed military personnel to UN peacekeeping operations in various places worldwide. Nepal is party to the international agreements on Bio-diversity and Climate Change, and has signed but not ratified the Comprehensive Test Ban Treaty and the Cartagena Protocol on Bio-safety.

3.2. Economic and Social Situation

3.2.1 Structure and Performance

Despite four decades of development efforts, Nepal remains one of the poorest countries in the world, a **Least Developed Country** with an estimated per capita GNI of about **€255** (2002).¹⁴ Nepal is the poorest country in South Asia. It has a total land area of 147 181 km², split into three topographical areas: the high mountains, the hilly regions and the low-lying Terai, which contain 7%, 44% and 49% of the population respectively.

The **UNDP Human Development Index**¹⁵ of 2003 ranks Nepal **143rd** out of 173 countries. Nepal has improved its ranking in recent years but further improvement in its standing will depend on the political environment to effectively implement the reforms envisaged by HMG/N. The population below the poverty line is about 37.7 %. One extensive survey in 1996 (NLSS) estimated this figure to be 44% while the same is 23 % in the urban areas.

Nepal is predominantly **rural**. Only 14.20% of the total population of 23.6 million (2001) live in urban areas, and around 80% of the population is directly involved in agriculture. Besides **subsistence agriculture**, significant areas of Nepal's economy are an important tourism sector, a small industrial sector (garments, carpets, etc.) and remittances

¹⁴ World Bank (2002)

¹⁵ UNDP – Human Development Index 2003

generated by migrant workers. Since 1990, policy changes have led to accelerated growth (6.5% per annum) in areas other than agriculture, particularly in the manufacturing and utilities sectors.

The performance of the agricultural sector, which generates about 40% of the national income, has been **disappointing**. Agricultural output grew at 2.5% per annum on average during the 1990s, compared to 4.0% during the 1980s. This reduced growth rate was due, among other things, to the declining quality of the environment, inadequate infrastructure, weak irrigation, and highly fragmented land ownership.

The rapid growth of the **energy** sector has diminished the share of income generated by agriculture. Water and hydropower are Nepal's most important natural resources. There are about 45 000 km of rivers and streams and an estimated power potential of 83 000 megawatts, of which 50% is economically viable but only 0.5% has so far been exploited. **Forests** occupy about 39% of the landmass and host a large diversity of flora and fauna. Deforestation, which is progressing at an estimated rate of 4% p.a. due to increasing domestic use and human settlements, has become a matter of major concern.

- **Trade**

India was Nepal's biggest import and export partner in 2001. The EU is the second biggest exporter to Nepal, and the third biggest importer of Nepali goods, after the USA.

The bulk of Nepal's **imports** consists of petroleum products, machinery and transport equipment, electrical goods, telecommunications and computer equipment, chemicals and drugs. Nepal's principal **exports** are carpets, garments and pashmina products, which accounted for about 39% of total exports in 2000. Also in FY 2001/2, export of garments and carpets accounted for about 29.5% of total exports.

Current account balance stands about US \$ 255.8 million for FY 2001/02. However, the current account balance for 2000 was US \$ 285.1 million.

Forex reserve for 2001/02 was US \$ 1388.49 million which was sufficient to cover the import of 11.93 months

Foreign grants amounted to US\$149 million in 2000.

Nepal benefits from the treatment granted by 'Everything But Arms' (EBA), and the ongoing Accession process to WTO is proceeding smoothly, even if the impact of adopting multilateral trade rules is matter of concern for the weak Nepali economy.

Lack of human resources in trade-related expertise, analytical and negotiating skills, product development and marketing could hamper the proper integration of Nepal into the multilateral trading system. Nepal undoubtedly appreciates EBA potential benefits but is also aware of its lack of competitive advantages to effectively compete with other LDC in the region.

- **Fiscal and Monetary Policies**

Foreign assistance (more often as grants) is the main source of funds for much of the HMG/N's capital budget, while the recurrent budget in recent years (1996-2001) has been

totally self-financed. Developing revenues to enable effective implementation of the PRSP/10th FYP (2002-2007) is a fundamental issue faced by HMG/N.

Since 1992, Nepal has had a fixed exchange rate with the Indian rupee

Interest rates in Nepal are on the decline. The prime lending rate came down from 11.5% in 1998/99 to 9.5% in 2001/02. **Inflation** (rise in consumer price index) is broadly determined by India's price fluctuations, and was estimated to be in the range of 2.9% in 2002.

The Nepalese authorities are trying to pursue a **rigorous** fiscal policy, but with difficulty. This is due partly to increased expenditure on defence, and partly to a decline in government revenues as a result of both the global recession and domestic instability. Foreign exchange reserves amounted to nearly US\$1.4 billion in mid-July 2001, or about 11 months of imports. **External debts** (US\$2.7 billion) represented 49.1% of GDP in July 2001.

- **Private sector development**

Since 1994, HMG/N has been making great efforts to promote private sector initiatives and to privatise state-owned enterprises. However, although HMG/N is opening all sectors of the economy for private sector participation, private investors are mainly interested in power development and telecommunications. Recently, HMGN has taken several measures to ensure level playing field to the private sector. These include significant changes in the Nepal Water Supply Corporation Act to open up the involvement of a private sector operator in the water supply. A new Bankruptcy Bill is being drafted to boost the confidence of investor and a Court Management and Judicial Administration Act has been enacted to improve the regulatory framework. The latter measure is expected to have a direct impact on the business and investment climate through enhanced efficiency of the judiciary. HMGN has also initiated reforms in corporate and financial governance.

3.2.2 Social Development

Nepal has not achieved any significant results with its poverty reduction policy. At the Nepal Development Forum (February 2002), the issue of poverty was extensively debated in the following key areas:

- Nearly 10 million people lived below the national **poverty line** in 1999. Poverty remains a predominantly rural problem, and the situation has worsened dramatically among ethnic minorities and marginalised people. In the context of social discrimination the situation of disadvantaged Dalits is of paramount importance.
- **Income** distribution is highly distorted. In 1999, the poorest 20% of the population earned less than 8% of national income, while the richest 20% earned nearly 50%.
- **Access** to social services, especially primary **health** care, is still critical. The fall in **infant mortality** rates has slowed markedly in recent years to about 70 deaths

per 1000 births. Lack of medicine is listed as a major problem, followed by poor health facilities. **Life expectancy** increased from 49.5 years in 1990 to 57.6 years in 2001, but it is still about 4 years lower than the average for South Asian countries.

- Among South Asian countries, Nepal ranks relatively highly in public **education**: the literacy level increased from 39.6% in 1991 to 57.6% in 2001. In 1995, nearly 90% of Nepalese households lived within a 30-minute walk of a primary school. Nevertheless, drop-out rates and the quality of education are still major causes of concern, especially in rural and isolated areas.
- Access to **water** rose from 24% in 1985 to 71.5% in 2001. A major issue is the poor quality of drinking water (very high levels of e.coli are systematically reported).
- Another matter for concern is the high **population growth** rate of 2.27%. Considering that over 86% of the Nepalese population live in rural areas, the present rate will have a considerable impact on social sector expenditure.
- The strengthening of central government capacity (education, health) has often been counterproductive, reinforcing resistance to decentralisation, which is considered necessary for improved social development.

3.2.3 Women in Nepal

Nepali women continue to face **discrimination** in various aspects of life. In Nepal, women's **life expectancy** is very low, while, according to Tenth Plan document (2003), only 34.6 % of women in Nepal were literate, one of the lowest female literacy rates in the world. Women are under-represented in government institutions and in most social development programmes. As a cross-cutting objective, gender equality will be advanced by all EC-funded co-operation initiatives, by promoting the participation of women in the projects, and by ensuring that the projects benefit women equally.

3.2.4 Population and Culture in Nepal

Nepal's population is a mixture of Indo-Nepalese and Tibeto-Nepalese groups. The majority of the Nepali people (80%) are Hindus, while 10% are Buddhists, 4% Muslims and 6% people of other faiths. The official language is Nepali (of Sanskrit origin), although English is spoken by about 11% of the population. Around 50 different languages are spoken in total.

3.3 Sustainability of Current Policies

Existing structural and institutional barriers – such as fragile agricultural, industrial and financial sectors and an inefficient public expenditure system – make it extremely difficult for HMG/N to ensure the **sustainability** of its policies. HMG/N efforts to alleviate poverty are also impaired by the rapid growth in population, the high degree of illiteracy, and low growth in agricultural productivity. Without a breakthrough, Nepal's development will remain unsustainable, with a major risk of further damaging local socio-economic and environmental conditions.

HMG/N is yet to develop strong policies on population growth, agricultural incentives, energy development, and natural resource conservation. Due to frequent changes in government, weak institutional framework and traditional cultural patterns, Nepal's Governments have found it increasingly difficult to reconcile the imperatives of economic growth with the respect for social rights, environmental protection and a fairer distribution of income.

3.3.1 Environment

HMG/N's responses to environmental challenges are generally fairly diverse and consistent within Nepal's legal framework and international commitments. Unfortunately, these responses have been ineffective, with very little success in **halting** environmental degradation and restoring the "carrying capacity" of the eco-system due to lack of resources.

Serious threats to the environment emerge in particular in three areas:

i) Nepal's **agriculture**, unable to achieve higher growth rates, is now expanding to include land which is less productive and environmentally fragile. Without successful land use and land tenure policy, agricultural performance will continue to decline, with serious environmental and social consequences.

ii) Environmental degradation in **urban** and **peri-urban** areas has become a matter of serious public concern, particularly in the **Kathmandu Valley**. Its population, estimated at 1.5 million people, is growing at an annual rate of about 10%. Existing infrastructure facilities are unable to cope with such a rise. The high use of harmful chemicals, the lack of solid wastes facilities and increasing fuel emissions following mass imports of and plying of old vehicles are a growing danger to public health.

iii) In the mid-1990s, the liberalisation of **industrial** policy led to the haphazard establishment of industries in urban areas, with few health and environmental safety measures taken.

3.4 Challenges in the Medium Term

Nepal urgently needs to address the issues of **political stability, domestic security and conflict mitigation**, which obstruct poverty reduction and economic growth.

A successful **peace-building** process would facilitate the implementation of policy reforms, which in turn could help prevent future conflict by reducing poverty. As long as a situation of **volatility** persists (curfew, strikes or bandh), there will be little chance of economic recovery or of a policy of sustainable development being implemented.

On the **economic and social** front, the main challenge for HMG/N will be to increase the performance of the agricultural sector. In particular, poor farmers need both encouragement to change their practices (for example, to diversify their crops) and

improved access to agricultural infrastructure and facilities such as water and credit. Basic social services in the rural areas should also be urgently improved.

The challenge of **environmental degradation** needs to be tackled through the **enforcement** of the environmental laws that have already been enacted. Targeting polluting industries and assisting in their relocation are priorities.

Improving **governance** and diminishing **corruption** is also a major requirement for enhancing Nepal's development. Good governance is an essential precondition for a fairer and more successful development policy based on comprehensive civil service reforms to increase efficiency and accountability both at central and at local level.

Improving respect for **human rights**, particularly in the context of ongoing peace process, is also a challenge, which requires immediate action to rebuild confidence in the Nepali governance.

Private sector contribution to growth needs to be enhanced to create conditions more conducive to new investments, while progressing towards a gradual integration of the Nepalese economy into the global market.

4. Overview of Past and Ongoing EC Co-operation

4.1 Overview

Foreign aid plays an important role in Nepal's development, representing about 5-6% of GDP per annum and financing over 25-30% of total government expenditures. In recent years the nature of foreign assistance has significantly changed. Grant aid has declined in comparison to loans, which now account for about 75% of the total. Bilateral assistance has also declined to around a quarter.

The 1996 EC-Nepal Co-operation Agreement is the institutional basis for EC relations with Nepal.¹⁶

Dialogue with HMG/N authorities has been expanded and improved since the creation of an EC Delegation in Kathmandu (April 2002). The EC's portfolio for co-operation needs to be carefully managed and monitored, alongside HMG/N's reform programme. Given the amount of funds allocated to Nepal, an increase in organisational capacity and resources of this Delegation is indispensable, particularly in order to consolidate EU links with Nepalese civil society and local NGOs and to allow full participation in donor co-ordination and dialogue.

4.2 Past and Ongoing Co-operation

To date, the EC has committed more than €130 million of aid to Nepal since 1977, 59% of which has been committed since 1994, at an annual average close to €10 million.

EC aid has, on the whole, consistently responded to the needs and priorities of Nepal. The most successful projects have been those based on the active participation of local beneficiaries and strong management. The principle of **co-responsibility** and close interaction with local administration has so far minimised the risk of resource **dispersal**.

Recent lessons learned from various evaluation and mission reports have also pointed to the need of reinforcing the on-going co-operation strategy with a broader operational framework in order to address fast emerging and critical issues facing Nepal such as security, good governance, the environment and conflict mitigation. Furthermore, reforms in Nepal are now charting complex paths and are also subject to political and administrative uncertainties. Therefore there is also a need to implement the new EC strategy in a balanced and appropriate manner in relation to local and national interests.

¹⁶ EC-Nepal discussions on multiple aspects of co-operation are held regularly within the framework of the **HMG/N-EC Joint Commission (JC)**; (3rd JC, Kathmandu - 19 March 2002). Only recently, the JC's work was complemented by previous meetings of the **EC-Nepal Sub-Commission on Development Co-operation** (10 October 2001) and the **EC-Nepal Working Group on Economic and Trade Co-operation** (19 July 2001), which provide the appropriate forum for updating Government policies, monitoring ongoing activities and addressing technical issues.

EC development co-operation has covered the following areas:

- **Rural development**

The three ongoing projects - **GARDP/P2** (rural development), **IDP-MWR** (irrigation) and **BIWMP/P2** (watershed management) - are being carried out successfully, with a high degree of "**acceptance**" by the local communities. Local conflict has sometimes resulted in delaying implementation but it has not prevented projects from reaching their targets and obtaining full support from the local beneficiaries. In the future additional efforts should be made to further integrate rural development activities within the local (decentralisation) and national context, to ensure real "**ownership**" and ultimately sustainability. Planners and managers of future EC-funded activities should fully capitalise on prior experience, such as the lessons learned from working in Maoist-affected areas.

At community level, planned activities must be based on a non-discriminatory approach, and should be systematically monitored.

The participation of farmers' groups and women's organisations should be promoted through appropriate training. Post-conflict dynamics and security guidelines should be fully explained and applied, putting social and political interaction with local development initiatives in the right perspective.

- **Animal health**

The strengthening of veterinary services for livestock disease control contributed to the elimination of Rinderpest, which was achieved in February 2002.¹⁷ This successful project highlighted the importance of close interconnection with government management, and of collaboration between key stakeholders (government and livestock owners). The conclusions of past activities still indicate the need for consolidation and extension of the results achieved.

- **Reproductive health**

The EC-funded Asian Regional Initiative on Reproductive Health has helped Nepal to make some progress towards making reproductive health services more accessible and more utilised. The second phase of this initiative will address the need to consolidate results and to enhance the capabilities of local agents. The main lesson learnt is that management and accountability of government service delivery must definitely be improved through involving recipient communities more directly.

- **Education**

The EC funds a core investment **programme** through a multi-donor arrangement with four other contributors.¹⁸ **The Basic and Primary Education Programme** (BPEP II)

¹⁷ Certification delivered by the "Office International des Epizooties" (OIE)

¹⁸ Denmark, Finland, Norway, IDA and EC

will improve both enrolment levels and learning, while strengthening institutional capacity at national, district and community levels. Major efforts still have to be made in upgrading the DOE's capabilities in areas such as auditing, planning and programme implementation. Collaboration with ministries, public institutions and civil society should be intensified to ensure better, workable solutions for delivering education services, especially in the districts affected by the insurgency. The main lesson learnt is that the management of schools should be transferred to local communities. Donors have followed too "centralised" an approach, often resulting in poor training of teachers, unsuitable curricula and teaching methods and little parental involvement.

- **Institutional Capacity Building**

The EC has contributed to two projects aimed at developing institutional capacity, the **Kathmandu Valley Mapping Project** and the **Population and Housing Census 2001**. Developing the capacity of the Kathmandu Metropolitan City Planning service was required in order to address the long-standing problem of uncoordinated development of urban areas. The development of a National Geographic Information Infrastructure will provide local authorities with a first reliable geo-information base for all types of development activities.

- **Civil Aviation**

The main objective of this regional initiative is to stimulate co-operation and business linkages between the EU and the Aviation sector in South Asia and South-East Asia. Awareness of EU industry practices, including airworthiness and safety regulations and standards, should make for an improvement in quality and generate new market opportunities.

- **Refugees**

Through the UNHCR, local NGOs and the WFP (World Food Programme), the EC is providing essential humanitarian assistance to Bhutanese refugees living in the camps in Eastern Nepal. ECHO support (food aid) via the WFP has ensured the necessary continuity of food supply to the most vulnerable categories of refugees.

4.3 EU Member States and other donors' programmes

4.3.1 EU bilateral donors

Member States' assistance to Nepal is mainly concentrated on poverty reduction. The areas of intervention that absorb most MS resources are: rural development, including infrastructure and energy; natural resources management; health and good governance. For the past four years (1999-2002), the bulk of EU bilateral donors in Nepal came from three MS, i.e. UK, Germany and Denmark. On the average, UK, which is the main development partner for Nepal, spent about € 30 million per annum. The funds for co-

operation committed by Germany, which is the second biggest EU donors, amounted to about € 28.5 million per year. And Denmark, which is the third largest EU donors, provided yearly around € 18.5 million to Nepal. All EU aid to Nepal is in the form of grants. As a whole, EU aid to Nepal represents a significant percentage of bilateral grant development assistance. Available information indicated that in 1999, EU share was about 40%. The detailed breakdown by sectors of MS aid to Nepal is as follows¹⁹:

- **Denmark** allocated €20 million in 2002 to support ongoing co-operation with Nepal, which remains a focus "Programme Country". Danish development co-operation concentrates on four areas: **(1)** education, **(2)** natural resources management, **(3)** rural energy, and **(4)** human rights, good governance and decentralisation. Over the next five years, Danish-Nepalese development co-operation will be implemented within the framework of the 10th FY Plan/PRSP.
- **Finland's** ongoing co-operation includes actions in areas such as energy, mapping, primary education, environment, and rural water supply and sanitation, to a total amount of €6.3 million. Finland also contributes to activities in good governance, democratisation and human rights areas.
- **French** co-operation focuses on three main areas: scholarships for Nepali students, cultural co-operation and food security. Starting from 2003 (and for three years), a new programme of rural development will be implemented and funded through counterpart funds generated from French food aid (8 000 t of wheat are expected in 2003). In 2000, France committed about €0.35 million, which does not include contributions to multilateral organisations.
- The priority areas for **German** co-operation with Nepal are: **(1)** health and family planning, **(2)** promotion of local self-governance and civil society, and **(3)** the promotion of renewable energy. Between 1996 and 2001, German financial co-operation with Nepal amounted to €43,3 million. The commitment for the period 2002/2003 totals €27.8 million. These amounts do not include contributions made through multilateral organisations (€11.7 million in 1999).
- The **Netherlands' aid** focuses on two areas: **(1)** bio-diversity and energy with the emphasis on natural resource management and the environment, and **(2)** good governance concentrating on support for state programming, decentralisation and women's rights. €9 million has been committed for 2002, which is an increase compared to past years.
- Through Sida, **Sweden** is supporting the Melamchi Water Transfer Project, which is the largest infrastructure project in Nepal. The Asian Development Bank is the lead donor agency. The Swedish contribution is €21.9 million.

¹⁹

Sources: HGMN/Ministry of Finance – UNDP; Nepal's Development Partners, Profiles of Cooperation Programmes, April 2002. Royal Danish Embassy in Nepal, Federal Republic of Germany in Nepal and DFID in Nepal.

- The **UK** allocated around € 86.9 million to co-operation with Nepal over the period FY 1999/00-2001-02. The UK Development Assistance aims to help the Government of Nepal to significantly reduce poverty and achieve measurable progress towards the Millennium Development Goals. The UK is committed to promoting reform and development in order to address the root causes of poverty in Nepal. It gives priority to support for economic opportunities and essential services to poor and disadvantaged communities, including those currently affected by conflict, and to social justice and governance reforms.

4.3.2 Non-EU bilateral donors

Outside the EU, the main countries co-operating with Nepal²⁰ are Australia, Canada, China, India, Japan, Norway, Switzerland and the United States. **Australia's** development co-operation programme covers forestry, food aid and education. **Canada's** key areas of co-operation include infrastructure, basic human needs, the private sector and gender issues. **China's** co-operation with Nepal is in health, transport and social development services. **India** provides assistance in the sectors of transport, health and education. **Japan's** main interests are tourism and civil aviation, education, debt relief and transport. **Norway** is active in the field of district development and education. **Switzerland** is active in three priority sectors: transport, occupational skills and enterprise development, and natural resources management. The **USA** is active in the field of poverty reduction, focusing on the sectors of health and family planning, agriculture and forestry, women's empowerment and hydropower.

For non-EU bilateral donors, only Japan and Norway provided some loans to Nepal. Over the last four fiscal years, the shares of loans in the total bilateral grants and loans ranged from 0% in 1999/00 to 6% in 2001/02 ²¹

4.3.3 Multilateral donors

In 2001, **Asian Development Bank** (ADB) assistance to Nepal amounted to about € 113.9 million (96% loans). Agriculture and natural resource development represented the largest component (46%), followed by energy (26%), transport and communication (13%) and social infrastructure (8%). In 1999, the **World Bank's** loan disbursements to Nepal amounted to € 52.4 million, these being for agricultural and irrigation development, human resources, transportation and energy. The **UNDP** is active in the sectors of governance, poverty alleviation and sustainable livelihood, gender equality and environment. Other key players on the Nepal co-operation scene are: **UNHCR**, whose dominant activity is addressing the issue of refugees from Bhutan; **UNPF** in the field of reproductive health; and the **WFP**, which provides food assistance to primary schools, refugees, and food-for-work projects. The **ILO** medium-term co-operation programme focuses on four areas: (1) poverty alleviation through employment promotion, (2) improvement of industrial relations, (3) elimination of child labour, and (4) improvement of working conditions. **UNICEF's** priorities in Nepal are the promotion of human rights for women and children, in accordance with the CRC²² and the CEDAW²³ treaties. **WHO**

²⁰ In alphabetic order

²¹ Source: HGMN, Ministry of Finance. Economic Survey, Fiscal Year 2002/2003.

²² Convention of the Rights of the Child

concentrates its efforts on: prevention and control of communicable diseases (leprosy, polio, etc); family and community health; promotion of healthy environments; mental health; health technology; and pharmaceuticals.

For multilateral donors, loans represented a major share of the aid commitment. For the last four fiscal years, the percentage of loans in the total multilateral grants and loans ranged from 59.1% in 2001/02 to 99.9% in 1998/99 ²⁴

5. EC Co-operation Strategy for 2002-2006

5.1 Principles and Objectives

The overarching objective of EC co-operation is to support Nepal's efforts to **improve the living conditions of its people**, particularly among the rural poor, and to enhance the performance of its economy. To reach this goal, it is also essential to support new initiatives to help **consolidate democracy in Nepal**.

HMG/N urgently needs to re-build the basis for more durable development, to put an end to the persistent state of **political uncertainty** and to concentrate on decisive and well-focused initiatives that tackle the root causes of the conflict.

Because of the complex matrix of socio-economic factors related to poverty, political instability and insurgency, the concept of Conflict Mitigation will be central to EC initiatives. **A common denominator** of the EC strategy will be close integration of **poverty reduction** and **conflict mitigation** activities to be implemented over a long-, medium- and short-term period. The emerging **peace process** in Nepal should have positive implications for future co-operation. The objectives of the present strategy, in line with the conclusions of the EC-Nepal Joint Commission, will be monitored with a certain degree of **flexibility**. In particular, the impact of the situation in Nepal on EC funded activities will be regularly assessed in order to optimise the use of available resources and to comply with cooperation priorities.

Based on the extrapolated "indicative Multi-annual allocation of resources" of **€ 70 million** for Nepal, the average foreseeable annual amount for the period **2002-2006** is **€ 14 million** (budget lines: B7-300 and B7-301).²⁵

EC funds are allocated to implement a strategy along the lines of the National Indicative Programme (NIP), focusing on the following **three concentration areas**, divided into 6 sub-sectors of **action**:

Concentration area 1: Nepal's Poverty Reduction	€ 58.0 M
Action 1: Renewable Energy and the Environment	€ 15.0 M
Action 2: Strengthening Rural Development and Governance	€ 43.0 M

²³ Convention on the Elimination of All Forms of Discrimination against Women

²⁴ **Source: HGMN, Ministry of Finance. Economic Survey, Fiscal Year 2002/2003.**

²⁵ However, this does not pre-empt EC budgetary authorities decision-making procedures

Concentration area 2: Consolidation of Democracy	€ 8.0 M
Action 1: Conflict Mitigation Package I:	
Support for Local Communities and Civil Society Voice	€ 3.0 M
Action 2: Conflict Mitigation Package II:	
Support for the Judicial System and Human Rights	€ 5.0 M
Concentration area 3: Integration into the International Economy	€ 4.0 M
Action 1: Trade Policy (Accession to WTO)	€ 2.0 M
Action 2: Economic Co-operation, Export Promotion and Capacity Development	€ 2.0 M

Development activities will be subject to detailed identification and appraisal undertaken by the Commission, full consideration being given to the following criteria:

- **Sectoral and regional concentration** of resources
- **Complementarity** with activities funded by EU Member States and co-ordination with other major donors
- **Participation** of civil society, community-based organisations and non-governmental organisations.

Nepal's new **policy mix** has benefited from the existing cooperation between EU members states and other donors which has allowed resources to be spent not only on poverty alleviation programmes but also on emerging issues such as good governance, democratization and conflict.

This cooperation strategy will be consistent with objectives and priorities of EC policies directly related to the chief areas of cooperation with third countries. The combination of development, trade and economic cooperation with a global projection of democratic and social justice values should contribute to growth while facilitating political stability. In this context, the Doha Development Agenda, strongly supported by Member states, calls for its rapid implementation in particular for LDC countries such as Nepal.

Particular attention has been paid to coherence with the EC Development Policy²⁶ and strategic activities and objectives recommended for Nepal largely reflect its orientation policy.

Poverty alleviation in rural areas of the Western Region and in particular support to rural development aims to create job opportunities and provide an enhanced social environment that encourage people to reduce migratory flows. Furthermore, this region will receive particular attention as one of the poorest in Nepal, also known for its conflictuality.

Priorities proposed in the agriculture, energy and environment sectors are integrated with conflict mitigation objectives given that development tools are the most powerful instruments for treating the root cases of the conflict. The main principles of the Conflict Prevention Commission's Policy will apply to Nepal as the present political situation

²⁶ COM (2000) 212 Final of 26.04.00

urgently requires a better level of security for all citizens. At the same time, a higher degree of protection of human and civil rights will also determine further advances in cooperation areas.

The consolidation of a democratic environment in Nepal is urgent and in line with the conclusion of the EU Council on the EU's role in promoting Human rights and democracy in third countries and the activities proposed by this strategy should facilitate progress towards peace.

Moreover, assistance provided to uprooted people, will contribute to conflict mitigation as well as to the survival of the hundred thousand people in the camps of Eastern Nepal.

This longstanding assistance has been complemented by urgent humanitarian services in line with ECHO policy in favour of this "forgotten crisis" and in view of a possible future exit strategy (integration of refugees' families).

It has to be stressed that the present strategy is centred in particular on expanding on results achieved with previous development activities (i.e. Mid-Western region). Moreover future EC initiatives will capitalise on past experience and knowledge of the beneficiary population while broadening the scope for development through local reforms and better governance.

EU co-operation with Nepal will depend on HMG/N demonstrating a real commitment to good governance, decentralisation, and building durable peace. Manifestation of this commitment should be clear progress made on these issues.

5.1.1 Cross-cutting Issues

In the Nepali context, cross-cutting issues such as gender and civil society, good governance have brought to light specific complexities. These need to be addressed within a proper framework as they have an important role to play in bringing **cohesion** to the EU Response Strategy. Furthermore, they also provide substantive bridges or links between thematic concentration areas.

Particular attention will be paid to cross-cutting issues that complement the focus of the EC strategy in Nepal, which is aimed at improving the social, political and economic conditions of local people, mitigating conflict, and supporting sustainable development. Cross-cutting issues to be taken into account in the design of future co-operation initiatives, as summarised below, will be integrated into development activities as complementary components.

- **Good Governance**, an indispensable factor for promoting transparency, accountability, ownership and full community participation.
- **Human Resources Development**, an important corollary of good governance, enabling both the public and private sectors, as well as NGOs and civil society, to respond more efficiently to development objectives.
- **Gender and Civil Society**, the creation of an appropriate environment to ensure the fullest participation of women in economic and social life in Nepal.

- **Environmental Protection**, more careful consideration of natural resources in Nepal's development process to halt further degradation.
- **Conflict Mitigation**, an urgent new specific requirement to gear co-operation activities to eliminating the causes of the conflict and consolidating the peace process.

5.2 Main Areas of Concentration

The EC's development co-operation assistance for the period **2002-2006** will be set within **three** main areas of concentration: **Poverty Reduction**; **Consolidation of Democracy and Conflict Mitigation**; and **Integration into the International Economy**.

Each of these areas covers two sub-sectors of action.

5.2.1 Concentration area 1: Poverty Reduction

The present strategy paper recommends concentrating new resources on Poverty Reduction, focusing on **Rural Energy** and **Rural Development**.

Providing rural communities with access to **energy** for the first time will bring major benefits in terms of improvement in the socio-economic conditions of people living in poor districts and strengthening local capacities to effectively manage a renewable resource.

Expanding and consolidating agricultural activities through **irrigation** in areas of Mid-Western Nepal will have major consequences that go beyond an increase in production and better living standards. Special focus on good governance and land tenure issues should help to limit local beneficiary participation to insurgency activities.

Action 1: Renewable Energy and the Environment²⁷

HMG/N has given great emphasis to the development of rural energy systems using local available resources and developing the technology to reduce the external dependency for energy supply.

Only 15% of Nepal's population currently has access to electricity (this percentage drops to 5% in the countryside), and Nepal is one of the five least energy-consuming countries in the world.²⁸ **90% of the rural population** depend exclusively on firewood and biomass for cooking, illumination and space heating. Alternative energy (photovoltaic) in rural areas not yet serviced by hydropower or the national grid will alleviate the level of poverty, by providing a modern form of energy that saves foreign currency (by substituting imported fuels) and contributes to a cleaner environment. Access to **renewable** energy resources will provide local communities with sufficient energy for domestic use for the first time, while improving **health**, **educational**

²⁷ The Renewable Energy Project - Nepal (NPL/B7-3000/AIDCO/2000/2244) was approved by the Commission on 4th October 2002 (PE/2002/1855)

²⁸ 15 GJ per capita

facilities and encouraging small rural **enterprises**. Solar photovoltaic technology will be evaluated against the availability and cost-effectiveness of other types of energy

Action 2: Strengthening Rural Development and Governance

The **rationale** of the EC strategy is to channel resources towards the most needy areas, because the Ninth Plan (aimed at achieving broad-based growth) has failed to reach large segments of the rural poor, especially in conflict areas. Recommendations for increasing agricultural outputs, enhancing agricultural services (livestock), providing food security and higher income and employment are clearly complementary to HMG/N policy as indicated in the Agricultural Perspective Plan (APP). The **guiding criteria** for the selection of targeted areas and beneficiary communities will be: a high incidence of poverty in areas long neglected, and poor irrigation infrastructures despite good potential for increasing crops production.

Some 75% of people in the Western Region own either no land or small farms of less than 2.7 hectares. By increasing rural production of mainly rain-fed land, the EC will offer this region a real chance to enhance the livelihood of the population, thus attempting to mitigate local political tensions. In parallel, the EC will pursue two important corollary goals:

- In relation to **Good governance**: EC-funded activities will give special attention to people's mobilisation, local community empowerment and strengthening of local administrations as essential conditions for achieving the main development targets. Without a strong commitment to decentralising functions, resources and responsibilities, and to combating **corruption** at all levels, poverty reduction and development initiatives will not be sustainable. These components will be fully integrated in the Western Region strategy without excluding collateral initiatives (support to social services) to accompany the main infrastructure works.
- In relation to **Land Reform**: in conflict-torn areas there is a need to obtain a clear picture of the configuration of land ownership and profiles of land use. These elements are essential for finding practical ways of implementing the new Land Legislation (2001-2002) at local level.

5.2.2 Concentration area 2: Consolidation of Democracy and Conflict Mitigation

The situation faced by the Nepalese people, whose vulnerability has been increasingly worsened by the conflict, requires **urgent** contributions to facilitate national **reconciliation**. Short-term **Rapid Reaction Mechanism** activities have been recently implemented to pave the way for future EC development activities. In parallel to poverty reduction, initiatives to consolidate democracy, to reduce the impact of the conflict and to enhance the role of civil society will form an integral part of this strategy.

Within the context of the same policy framework, mention is made of the European

Initiative for Democracy and Human Rights (**EIDHR**), EC support for the **electoral process** and support for the **refugees**.

Short-Term – Rapid Reaction Mechanism (RRM) ²⁹

*At the end of 2002, the EC approved four **short-term RRM** pilot initiatives for the duration of six months. The follow-up to these activities will be **consolidated** in the medium term under Action 1. (Conflict Mitigation Package I - Support for local communities and Civil Society Voice), using the resources of budget line B7.300.*

*The four areas covered by the **RRM** are:*

I. Socio-Economic Development for Kamayas.

The Kamaya system (bonded labour) was abolished in July 2000, but the labourers were 'liberated' without any preparation in terms of training, provision of assets or social protection. These groups need urgent resources to develop sustainable livelihoods and to facilitate their social integration.

II. Socio-economic Development for communities affected by refugees.

*The unexpected long-term presence of refugee camps in Eastern Nepal has created a **competitive** environment with regards to locally available resources.*

The impact of refugees on the indigenous population could be reduced through a series of micro-interventions to provide local communities with socio-economic aid and facilitation support, thus reducing local political instability.

III. Media - Radio Broadcasting.

The main objective of disseminating non-partisan information about issues affecting the daily life of Nepalese society is to address the local population with conflict mitigation messages and to promote a far-reaching discussion forum. This initiative is aimed at promoting the necessary awareness of ways to build consensus during the national reconciliation process.

IV. Conflict Assessment:

A good understanding of the situation is crucial to ensuring that co-operation activities are impartially monitored and secured by a conflict specialist. This is achieved through close interaction with the government, local authorities, civil society, development partners, project managers and co-operation beneficiaries. This expertise also offers appropriate guidance for future co-operation activities in conflict-affected areas.

²⁹ The RRM decision (RRM 2002-2006) to allocate € 615000 to short-term pilot initiatives in Nepal was taken in August 2002. Under Council Regulation (EC) No 381/2001 of 26 February 2001- OJ L 57 of 27 February 2001 p. 5, resources can be mobilised "**to respond**" in a rapid and flexible manner to crises involving a threat to the rule of law and escalating into armed conflict likely to jeopardise co-operation policies and activities

Action 1. Medium-Term: Conflict Mitigation Package I: Support for local communities and Civil Society Voice.

As mentioned above, the Commission Decision to implement RRM short-term initiatives aimed at bringing a quick response to the repercussions of the conflict in sensitive areas of Nepal.

The objective of implementing a Medium-Term Conflict Mitigation Package I is to extend support in favour of the communities in the Mid-Western and Eastern regions of Nepal and to sustain the role of local media.

The (first) short-term pilot RRM phase just began in conjunction with the proclamation of the “truce” (January 2003), while the Medium-Term Conflict Mitigation Package I will pursue the following objectives:

- to further involve community-based organisations (CBO) in long-term development through mobilisation of local beneficiaries;
- to coordinate NGOs network while improving communication to decrease local political, ethnic and caste antagonism;
- to sustain the voice of civil society through national broadcasting and to challenge the resurgence of violence with more suitable means (dialogue) to consolidate the peace process.

The initial six months of RRM support in the critical geographical areas of Mid-Western and Eastern Nepal will therefore be **consolidated** over a **Medium-Term** period. This approach should help to remove the greater obstacles for future development of pro-poor initiatives, taking into account the weakness of local communities, often victims of social exclusion and therefore prone to **radical** demands.

To make people’s **voice** heard through independent media (**broadcasting**) is recognised as an important aspect of civil society participation in the ongoing peace building process. To allow people to listen to a variety of conflict-related subjects broadcast for a fairly long period and nationwide (such as traditionalism versus modernism, parental/family authority, property rights, pollution, corruption, unemployment, etc.) will create new forums for public awareness debating on alternatives to conflict.

Action 2: Medium-Term – Conflict Mitigation Package II: Support for the Judicial System and Human Rights

- From the beginning of the “people’s war” (1996), the number of cases where members of both insurgency and counterinsurgency forces act with **impunity** has increased. To adequately support the peace process it is necessary to strengthen the existing mechanisms protecting human rights, and extend their capacity to investigate and handle a whole range of complaints. Dealing with cases of abuses according to a clear set of rules will help to break the culture of violence and the vicious circle of rebellion and repression.

Key issues faced by the present **Legal and Judicial** System in Nepal include better **access** to justice; enhancing the quality of the legal regime; and modernising the existing structures with adequate resources. EC initiatives should aim to help the government **decentralise** judicial functions and upgrade the provisions for **legal assistance**, especially in favour of people without the financial means or information needed for proper access to the justice system. In this context, the **Nepal Bar Association**, with of its experience and reputation, is the most suitable interlocutor to accomplish this type of mission.

- The main difficulties so far encountered include monitoring the human rights situation and ensuring proper functioning of the judicial system, particularly in remote areas. Enhancing the capacity of the **National Human Rights Commission (NHCR)** to investigate cases of Human Rights violation outside Kathmandu is a primary objective to be pursued with determination. Support activities will be funded within the context of the NCHR Strategic Plan 2003-2005, prioritising activities that promote the protection of human rights in government policy and practice.

Other complementary activities:

- ***ECHO :***

Humanitarian support was provided to the people affected by the conflict through protection and dissemination of International Humanitarian Law activities (implemented by ICRC) and through basic primary health care in the Far West. The total indicative amount for these activities in 2002-2003 will be of € 3,6 Mio.

Future Dipecho program 2003-2004 for South Asia includes Nepal. Call for proposals (June 2003) will select operation with focus on training, early warning and mapping

- ***EIDHR :***

In addition to the Conflict Mitigation Package II, it has to be mentioned that the European Initiative for Democracy and Human Rights (EIDHR) has included Nepal among its focus countries. The EIDHR supports objectives such as conflict dialogue, freedom of expression, strengthening of human rights organisations and the rule of law. A detailed action programme is under preparation, which takes into account other donor activities and is closely co-ordinated with the strategic objectives set in this document for initiatives to be funded by the co-operation budgetary instruments.

- ***Elections***

Following the dissolution of the Nepalese Parliament (May 2002), early **general elections in Nepal** were scheduled for 13 November 2002 and subsequently

postponed **sine die**. The decision taken by the EC in mid 2002 to finance an EU Electoral Observation Team will remain **valid** until the end of 2003. Member States and the donor community have firmly supported this initiative though expressing high concern for a free and fair electoral process. The EC position is that new general elections should be held as soon as possible, but this will depend on the outcome of the peace process. An additional contribution from the EC to support the role and the mandate of the Election Commission of Nepal could be envisaged both at National and local levels.

- **Refugees**

The presence of over 100 000 refugees in Eastern Nepal since the early 1990s has generated growing local tensions. In the absence of a solution, the EC will continue to provide care and maintenance assistance to the camps via the UNHCR, NGOs and through ECHO contribution of food aid via the WFP. The slow process of negotiations between Nepal and Bhutan has increased the need for humanitarian help. A sudden interruption of aid in the absence of a political solution would have further destabilising effects in the region.

5.2.3 Concentration area 3: Integration into the International Economy

The EU Council on General Affairs on 19 November 2002 emphasised the importance of integrating trade-related assistance into a coherent strategy, with particular reference to the provision of assistance for WTO accession and the support of initiatives to enhance private sector capacity and economic performance.

Action 1: Trade policy (Accession to WTO)

Nepal needs urgent assistance in adapting its existing regulatory framework to a multilateral one in preparation for its accession to the WTO, and in formulating its trade policy. Planned action to help Nepal implement WTO rules will take account of its economic situation and in particular the constraints of an LDC country.

Nepal's **accession** to the WTO has been a slow process (it applied in 1989), because of the complexity of the issues to be handled by the HMG/N administration and the expertise required to pass several phases of negotiations.

European TA could be made available in relation to **sanitary** and **phyto-sanitary standards** (SPS) and **Technical Barriers to Trade** (TBT) as well as **customs evaluation**. The SPS sector is of particular concern for HMG/N, considering Nepal's potential for developing competitiveness in some agricultural products. Areas to be covered include processing technologies, national regulatory bodies, training and equipment.

Equally important will be to implement measures to protect **Intellectual Property Rights** system so as to encourage technology transfer to Nepal.

Action 2: Economic Co-operation and Capacity Development

HMG/N's plans for stronger market-oriented reforms are constantly frustrated by the high incidence of poverty and by a weak know-how and institutional capacity, despite new budget objectives aimed at improving the environment for investment and facilitating access to productive resources. New initiatives that could facilitate trade and investment promotion have often been jeopardised by a) the **absence** of a proper information strategy, and b) the **lack of contact** between Nepalese traders/manufacturers and potential partners outside Nepal.

- EC support for **economic co-operation** should be extended alongside government efforts to encourage **foreign investment** in areas of comparative advantage. **Obstacles to economic co-operation** must also be removed in order to improve corporate governance, transparency and efficiency.³⁰
- Concerning the **export sector**, Nepal continues to face problems of a narrow export base and limited country focus. HMG/N's efforts to promote a sustainable export strategy in conjunction with the private sector should also be supported, with a view to increasing the competitiveness of Nepali products in particular.
- It is also important to stress the importance of Nepal's **diplomatic missions** abroad and the need to promote the training of diplomats in economic affairs. **Economic diplomacy** should play a more active role, together with the private sector, in promoting, facilitating and monitoring economic activities abroad.
- **Business-to-Business** contact would help expand trade relations between Nepal and the EU. In this context, the **Nepal-EU Economic Forum**,³¹ established under the Federation of the Nepalese Chamber of Commerce and Industry (FNCCI), can play an important role in improving interaction between Nepal and EU entrepreneurs. Constant changes in the business environment suggest that professional organisations need to offer information that is often not accessible to individual entrepreneurs.
- Another area that also deserves greater attention is the dissemination of information concerning EC Regional Programmes (**Asia Invest, Asia Link, Asia Urbs, IT&C**). These regional instruments can offer a whole raft of **opportunities** in various areas that could stimulate Nepalese private sector activities through new initiatives, business contacts and transfer of know-how.
The **Guide Book for European Investors in Nepal** (2001 - implemented by EU/Asia Invest Programme) has been the most advanced initiative to promote business-co-operation, but the conclusions of the Guide Book have been very

³⁰ Ongoing project support (ADB) for Corporate and Financial Governance has done the groundwork for future private sector growth in business activities.

³¹ This embryonic entity should be further developed and supported with EC funding to capitalise on a previous and rather positive experience of a minor scale, the **Technology of Trade Information Promotion System (TIPS)** (1997). TIPS mainly focused on Business Offers and Requests Collection and Abstracts preparation and support for the FNCCI executive committee on European affairs.

narrowly exploited. Also, recent UNCTAD studies promoting FDI and detailing success stories have been made available to potential foreign investors.

5.3 Complementarity within the EU and with Other Development Partners

The EC will make a particular effort to ensure that future development activities are complementary to the strategies of Member States and other development partners active in Nepal. Donor co-ordination is carried out at two different levels:

- At a **political** level, major donors meet regularly (two months) at '**Donor Group Meetings**' (DGM) sponsored by the World Bank and the UNDP. Donor dialogue ensures that a comprehensive discussion is followed up on HMG/N's development strategy, and provides a forum for discussing new ideas and mechanisms in support of development in Nepal. The DGM has significant political leverage, and can call on the competent national authorities to discuss priority issues. The EC also has regular consultations with all the relevant development partners, including Member States, in the identification and appraisal stages of the project cycle to ensure complementarity.
- At a **technical** level, there are **twelve thematic** groups that seek to monitor donor activities and discuss sectoral strategies and priorities.³² The convenors of these meetings are responsible for updating the monitoring system of donor activities, and preparing the agenda for the group meetings. The EC Delegation participates in the group meetings on Good Governance and Public Sector Management; Child Labour; Health and Population; Education; Agriculture/Rural Development; Natural Resource Management and Environment; and Transport and Telecommunications. Participants in these meetings consist mainly of experts, advisers, and middle officials from HMG/N.

Responding to the need for better co-ordination among donors, the UNDP has recently prepared a document profiling donors' co-operation programmes, which provides useful guidance and facilitates the complementarity of development efforts among the various donors in Nepal. Finally, a recently established **Peace Support Group** aims to provide a co-ordinated aid effort to accompany the peace process in Nepal. So far, the relatively small 'donor community' active in Kathmandu has ensured that, as regards the strategies and activities of the main development partners, most are mutually well informed. Generally, the EC encounters no difficulties in harmonising its development aid agenda with those of Member States and other donors in Nepal.

³² The twelve groups are as follows: Good Governance and Public Sector Management; Macroeconomic Management, Financial/Private Sector and Trade; Child Labour; Gender and Development; Health and Population; Education; Agriculture/Rural Development; Natural Resource Management and Environment; Energy/Power; Transport and Telecommunications; Urban Development (including Urban Water and Environment); Disaster Preparedness.

SOCIO-ECONOMIC INDICATORS¹, NEPAL 2001

Poverty and social	
GNI (former GNP) per capita (<i>Atlas method, USD</i>)	250.0
GNI (<i>Atlas method, USD billions</i>)	5.8
GDP (<i>USD billions</i>)	5.6
GDP (<i>average annual growth %</i>)	4.8
Population, mid-year (<i>millions</i>)	23.6
Population (<i>% of average annual growth, 1995-01</i>)	2.4
Labour force (<i>% of average annual growth, 1995-01</i>)	2.5
Poverty (<i>% of population below national poverty line</i>)	42
Urban population (<i>% of total population</i>)	12
Life expectancy at birth (<i>years</i>)	59
Infant mortality (<i>per 1000 live births</i>)	74
Child malnutrition (<i>% of children under 5</i>)	47
Access to improved water source (<i>% of population</i>)	81
Illiteracy (<i>% of population age 15+</i>)	57
Gross primary enrolment (<i>% of school-age population</i>)	126 ²
Gross primary enrolment, male (<i>% of school-age population</i>)	140
Gross primary enrolment, female (<i>% of school-age population</i>)	112
Government finance (<i>% of GDP, includes current grants</i>)	
Current revenue	11.4
Current budget balance	0.2
Overall surplus/deficit	-4.5
Structure of economy (<i>average annual growth %</i>)	
Agriculture	4.3
Industry	2.5
Services	6.6
Trade (<i>USD millions</i>)	
Total exports (fob)	942
Total imports (cif)	1774
Balance of payments (<i>USD millions</i>)	
Exports of goods and services	1359
Imports of goods and services	1984
Resource balance	-625
Net income	9
Net current transfers	774
Current account balance	158
External debt and resource flows (<i>USD millions</i>)	
Total debt outstanding and disbursed	2700
IBRD	0
IDA	1127

¹ Source: World Bank

² These figures for gross primary education are to be explained by the fact that there are more pupils enrolled in primary education than there are children of school age (6-11 years). In Nepal, there are pupils older and younger than this who are enrolled.

**OVERVIEW OF ONGOING EC FINANCED PROJECTS IN NEPAL
(B7-300,301)**

Project/Sector	Year	EC cost € million
Development co-operation		
Strengthening of the Veterinary Services for Livestock Disease Control	1994	8,7
Gulmi Arghakhanchi Rural Development Project	1996	14.7
Irrigation Development Project-Mid Western Region	1997	8.1
BAGMATI Integrated Watershed Management Programme	1997	12.2
Greater KATHMANDU Valley Mapping	1998	5.6
Basic & Primary Education Programme	1999	20.5
2001 Population and Housing Census	2000	2.4
Renewable Energy Program	2002	15
Total		87.2

Other ongoing projects

Sector	Committed total (€)
Humanitarian Aid (B7-210)	3 675 000
NGO –Co-financing (B7-6000)	7 353 649
HR and Democracy (B7-701)	1 871 213
Tropical Forests (B7-6200)	999 446
Aid to Uprooted People (B7-302)	2 900 000

SECTORAL MATRIX / DONORS CO-ORDINATION

Sector	EC	MS	Other donors	Comments
Rural development	X	UK (on-going) D (2000-2004) FR (2002-2005) UK (on-going) D (1996->2006) UK (on-going) D (2000-2004) UK (on-going)	AUS ADB WB ADB, UN CH ADB WB ADB ADB, UN JAP, US	
Infrastructure Energy Transport & communication				
Irrigation Tourism Rural finance Special cultures	X X			
Governance		NL (on-going) UK (on-going)		All donors
Conflict prevention	X	UK (on-going) D (2001> ongoing)		
Human rights		DK (1999-2009) UK (on-going)	AUS, CH	
Environment	X	DK (1985-2009) D (1992-2006) UK (on-going) DK (1988-2004) UK (on-going) DK (1988-2004) UK (on-going) DK (1988-2004) NL (1994-1996)	ADB, CAN, N, JAP, WWF WB, AUS, CH, JAP, US CH ADB, N, CH UN	Environment is considered a priority sector by many donors. N.B.: <i>Ensure environmental sustainability is one of the Millennium development goals for Nepal.</i>
Forestry				
Water conservation				
Environmental standards and policy				
Natural resources				
Biodiversity				
Social sector		UK (on-going) UK (on-going)	ADB, CAN, US, UN ADB, WB, N, UN	Poverty reduction is the target common to all donors. Gender is considered as a priority horizontal issue by many donors. N.B.: <i>Eradicate poverty and promote gender equality are two of the Millennium development goals for Nepal.</i>
Gender issues				
Water & Sanitation				
Health		D (2001-2003)	WHO, IN ADB, AUS, JAP	N.B.: <i>Reduce child mortality, improve maternal health and combat infectious diseases are three of</i>
Primary level				

Reproductive and child health AIDS and other infectious diseases control (tuberculosis...)	X	UK (on-going) D (2001-2003) UK (on-going) UK (on-going)	WB, US, UN AUS, JAP, UN	<i>the Millennium development goals for Nepal.</i>
Education Primary/secondary education Technical and vocational training Scholarship	X	UK (on-going) DK (1980-2008) FR (on-going)	IN ADB, WB, N CH	N.B.: <i>Achieve universal primary education is one of the Millennium development goals for Nepal.</i>
Economy sector Financial sector Power & energy (inc. renewable) Transport & communication SMEs	X	UK (on-going) NL (1997-2003) D (1996-2006) DK (1999-2004) FIN (2000-2003) DK (1996-2003)	ADB, WB WB, CAN, N, US WB, CH, IN CH	
Urban development		D (1987-2006)	UN	
Regional co-operation			ADB	
Support NGOs		UK (on-going) D (1995-2005)		All donors

*Austria, Belgium, France, Luxembourg and Sweden provide ODA to Nepal, but no data available on sector distribution

ADB: Asian, Development Bank

WB: World Bank

UN: United Nations (UNDP + UNICEF+UNFPA)

WHO: World health organisation

WWF: World wildlife found

SNV: The Netherlands Development Organisation

AUS: Australia

CAN: Canada

CH: Switzerland

IN: India

JP: Japan

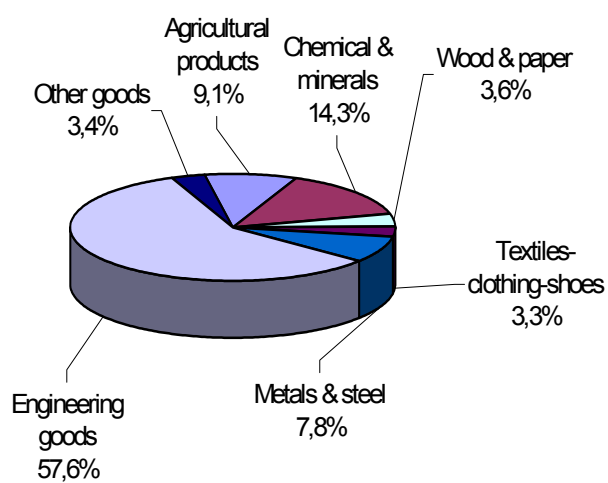
N: Norway

US: United States of America

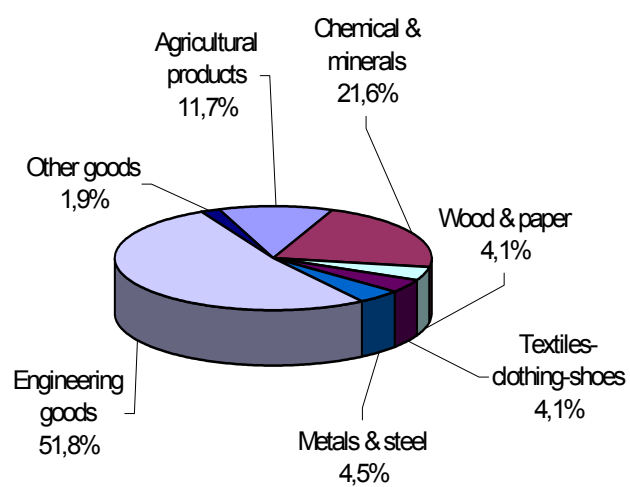
EU-NEPAL TRADE

EU EXPORTS TO NEPAL

2000

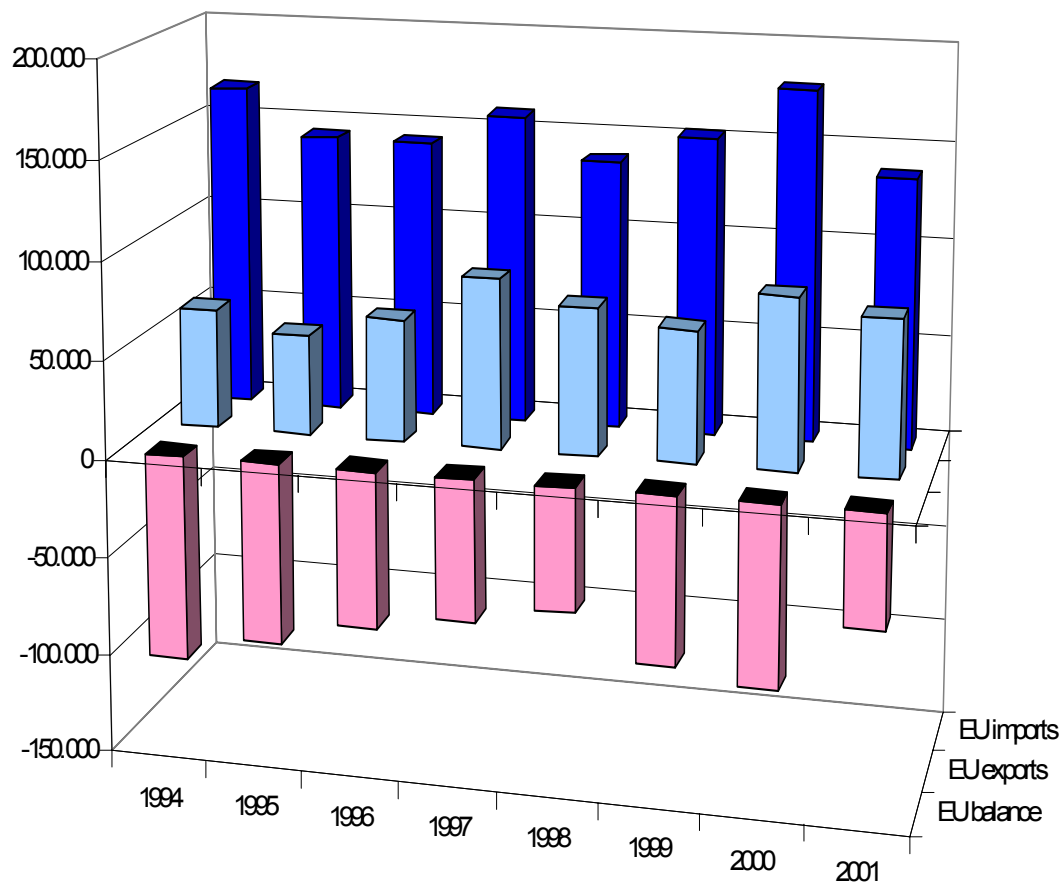


2001



EU – NEPAL TRADE

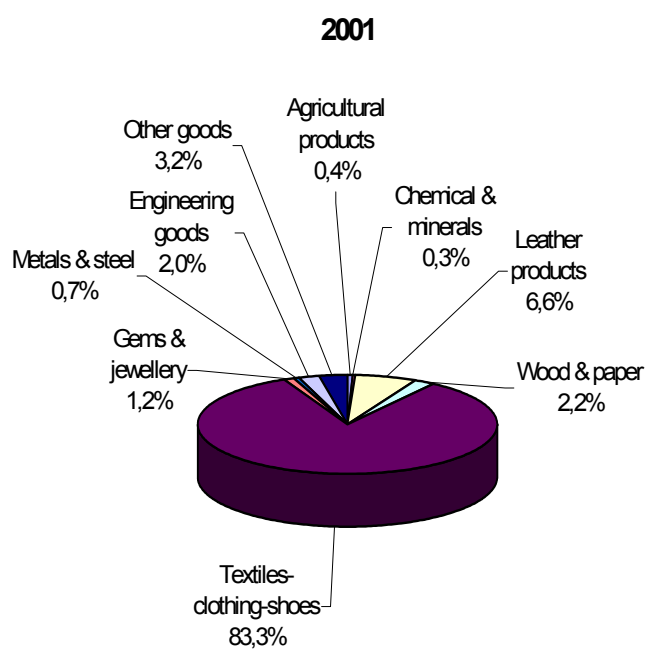
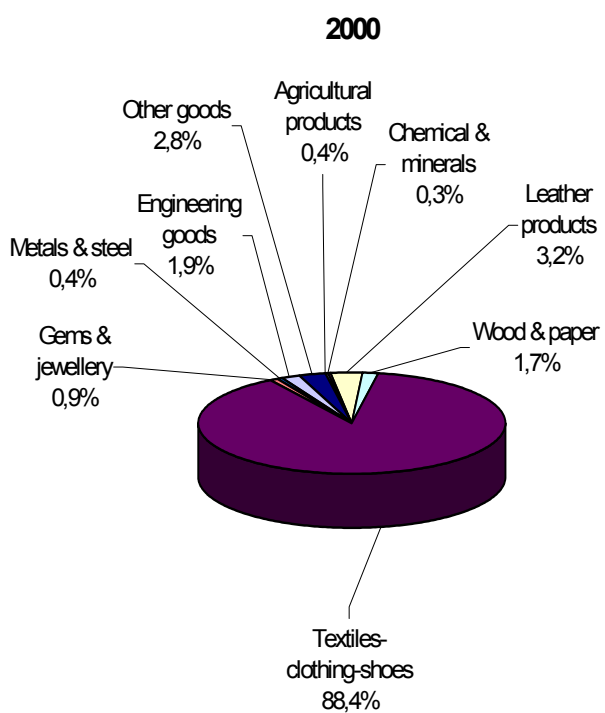
Evolution of EU-15* trade with Nepal — 1994-2001
In ECU (EURO from 1999) thousands



*Until 1994=EU 12, since 1995=EU 15

	1994	1995	1996	1997	1998	1999	2000	2001
EU balance	-104.851	-91.848	-79.453	-71.979	-62.443	-85.077	-91.496	-57.358
EU exports	61.421	51.175	62.815	86.683	75.195	67.381	87.329	79.623
EU imports	166.273	143.023	142.268	158.663	137.637	152.460	178.946	136.981

EU IMPORTS FROM NEPAL – COMPARISON 1999 – 2000



MAP OF NEPAL



NATIONAL INDICATIVE PROGRAMME (2002-2006)

NEPAL

Country/Region	: NEPAL
Budget Years	: 2002-2006
Budget Line	: B7-3000, B7-301
Legal Base	: ALA Council Regulation (443/92 of 25 February 1992)
Cost of Order	: € 70m
Programming Service	: DG RELEX H3
Head of Unit	: Laurence Argimon-Pistre
Co-ordinator	: Mario Ferrucci

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1. EC-Nepal Country Strategy

The EC-Nepal Country Strategy Paper (2002-2006) takes account of the goals of European Union co-operation policy, the Nepalese policy agenda, the country analysis, as well as past and ongoing experience. The CSP states that the *overarching objective of EC co-operation will be to support Nepal's efforts to improve people's living conditions, particularly the rural poor, and to improve economic performance*. The three main areas of concentration for EC co-operation will be to promote Long-term **Poverty Reduction**, to consolidate democracy through **Conflict Mitigation** and to support Nepal's integration into the **International Economy System** by strengthening the domestic economy.

Horizontal issues such as gender equality, environmental protection, human rights (particularly of vulnerable groups), good governance, and anti-corruption, among others, will be mainstreamed into all EC assistance to ensure that they are adequately addressed and integrated into co-operation design and implementation.

Furthermore, coherence with EU policies and complementarity within the EU and with other donors will be pursued in all areas of co-operation. In particular, the present indicative programme will aim to complement and support projects, where appropriate, which are financed by EU Member States.

Specific project selection will be subject to detailed identification and appraisal to be undertaken by the Commission. Special consideration will be given to the specifications of project's objectives, purposes and results in order to focus on "measurable" and "comparable" achievements to enable the identification of progress and outcome of implementation. Objectively, verifiable indicators will form an integral part of the feasibility studies foreseen for the accomplishment of the NIP 2002-2006 and in parallel with a significant contribution to support monitoring and evaluation activities at different stages of projects' implementation. In the preparation of EC assistance, special efforts will be made to ensure that the socio-economic objectives of Nepal, as stated in the 10th Five-Year Plan, are taken into account in the project-programme design and its follow-up, so as to make for maximum impact on Nepal's own development goals.

EC assistance will be conditional upon Nepal's continued commitment both to a development strategy that addresses the root causes of the Maoist conflict and the necessary reforms and to demonstrable progress in the field.

A previous EC Strategy document expired in 2001. For reason of a coherent presentation the period covered by the overall new EC strategy is 2002-2006.

2. Summary of the Strategy and Priorities

Concentration area 1: Assistance to the poorest sectors of society includes underpinning rural development and developing renewable sources of energy in rural areas. Additional provisions for good governance and land reform are also among the long-term development targets.

Concentration area 2: Assistance to the process of consolidation of democracy through Conflict Mitigation Packages designed to defuse the conflict and to prevent more violence from further impinging on the Nepalese people's livelihoods and rights. Legal and judicial reforms and promotion of Human Rights will also be an essential part of the Conflict Mitigation Package.

The co-financing possibilities will be explored subject to an analysis of public finance management. In this context particular attention will be directed towards the issue of endemic corruption/governance as an over-arching concern of our co-operation.

Concentration area 3: Assistance to trade and investment and integration into the international economy comprises trade sector policy formulation and training to strengthen Nepal's capability to negotiate its accession to WTO and to implement the rules of the multilateral trade system. Support for initiatives from the private sector to activate and consolidate contacts between Nepalese trader-manufacturers and potential partners outside Nepal is an essential component of the economic co-operation project.

From the EC's perspective, an integral aspect of all Community co-operation will be to raise the EU's profile – concept, values, culture – and visibility in Nepal. A special effort will be made to combine traditional development co-operation initiatives with economic co-operation approaches, promoting a more harmonious sectoral strategy that takes both developmental constraints and the economic opportunities offered by international trade into account.

3. Indicative Budget

During the period covered by the National Indicative Programme, from 2002 to 2006, a total EC grant of **€ 70m** can be committed to support the overall budget for EC-Nepal co-operation activities. The following is a breakdown of this aggregated grant (more details in Annex 1):

3.1 Concentration area 1: Nepal's Poverty Reduction **€ 56.0m**

Action 1: Renewable Energy and the Environment	€ 15.0m
Action 2: Strengthening Rural Development and Governance (SRD+G)	€ 41.0m

3.2 Concentration area 2: Consolidation of Democracy and Conflict Mitigation **€ 10.0m**

Action 1: Conflict Mitigation Package I	
Support for Local Communities and Civil Society Voice	€ 3.0m
Action 2: Conflict Mitigation Package II	
Support for The Judicial System and Human Rights	€ 7.0m

3.3 Concentration area 3: Integration into the International Economy **€ 4.0m**

Action 1: Trade Policy (Accession to WTO)	€ 2.0m
Action 2: Economic Co-operation and Capacity Development	€ 2.0m

4. Priority: *Nepal's Poverty Reduction*

4.1 Strategy Context and Justification

Poverty reduction through development is the overriding objective of the 10th FYP (2002-2007), as confirmed by the Nepal Development Forum (NDF) (February 2002). HMG/N and donor community conclusions also took full account of the Poverty Reduction Strategy Paper (PRSP)/10th Plan objectives and HMG/N's Agenda for Priority Reform.

Consistent with HMG/N's goal of poverty reduction, EC development co-operation will continue to subscribe to the campaign against poverty. The CSP explicitly identified pro-poor areas of intervention, such as rural development and sustainable use of natural resources.

The CSP mentions that support will be geared towards decentralisation and people empowerment, through capacity building at community level and greater ownership by beneficiaries of project initiatives. Geographical focus will be narrowed down and achievements of existing projects will be consolidated and extended.

4.1.1 Development of Renewable Energy and Environment Strategy Context and Justification

Within the context of poverty alleviation, developing the **Rural Energy Sector** in Nepal will stimulate community-based initiatives (and investments) by providing decentralised energy services in an attempt to build a sustainable system increasingly autonomous from donor or government incentives in areas not easily serviceable by traditional sources of energy. Only 15% of Nepal's population currently has access to electricity (this percentage drops to 5% in the countryside) and Nepal is one of the five least energy consuming countries in the world. The most disadvantaged rural poor should benefit from **photovoltaic** energy infrastructures aimed at facilitating income generation, along with access to improved social services (health, education, safe water supply, etc.), both at the Village and District Development Committee (VDC/DDC) and at national level.

Moreover, Nepal's rural energy situation is characterised mainly by the fact that presently only 5% of the rural population has access to electricity, and that traditional fuels, such as firewood, account for 98% of energy consumption, resulting in large-scale unsustainable harvesting practices. HMG/N has placed the emphasis on the promotion of renewable energy technologies for their role in rural development since the early 1980s. Support for this sector was institutionalised in 1996 with the establishment of the **Alternative Energy Promotion Centre** (APEC), which is the country's first government institution fully dedicated to the promotion of renewable energy technologies in Nepal. The goals for solar energy with the current Five-Year Plan (1997-2002) are to install 38 000 solar home systems in remote areas not accessible to the national grid of micro-hydro supply. APEC's Renewable Energy Perspective Plan (2000-2020) calls for increased investment in the renewable energy sector in the coming years and accelerated promotion efforts. REPP forecasts 5 000 kW of solar PV and 500 000 m² of solar thermal collectors at the current rate.

4.1.2 Strengthening Rural Development and Governance in the Mid-Western Region. Strategy Context and Justification

The Ninth Five-Year Plan (1997-2002) stressed the leading role of Agriculture in poverty alleviation, given that about 80% of the population is engaged in this sector and some 40% of GDP relies on Agricultural outputs. The Agricultural Perspective Plan (APP) is the main basis for augmenting production, providing food security and increasing employment and income. The main emphasis is placed on the expansion of irrigated agriculture, agricultural support services, with special attention to the livestock sector and land management systems. Development of irrigation in the Mid-Western Region, through a substantial increase in mainly rain-fed land, will greatly benefit the local population, which in this area still lives (70%) below the poverty line. Besides irrigation infrastructure and land management, these activities should be accompanied by collateral activities which are of particular significance in the local context. Good governance (local capacity building and decentralised administrative reforms), Land Reform (pilot studies and schemes implementing the new legislation) and rehabilitation of social services will represent the entry points in these politically sensitive zones.

4.2 Action: Renewable Energy and the Environment¹

4.2.1 Objectives

The overall objective is to create a renewable energy infrastructure in rural areas which will facilitate income generation, sustainable growth and delivery of social services, thus alleviating poverty. More specifically, and in accordance with the EC-Nepal Co-operation strategy, the project will help to:

- alleviate poverty in rural areas;
- improve the environment at local and global level;
- strengthen public agencies and policy reforms, mainly by encouraging HMG/N's continuing policy of democratisation and decentralisation;
- intensify the industrialisation process by developing the energy sector in the form of community-based enterprises on a comparative and competitive level;
- increase the security of energy service supply of specified Nepalese Districts; and
- facilitate implementation of the HMG/N's Plan of Rural Energy Supply.

4.2.2 Expected Results

The project is expected to deliver three main types of results:

- **End user** applications resulting from energy supply for communities in VDCs consisting of at least 2.2 MW of PV systems of different size and solar thermal systems for supply of process heat, hot water supply for health posts and the tourism industry and solar cookers in institutions like clinics, schools, etc.
- **Energy services** provided for improving standards of living, public services and capacity building/job creation. In health posts and rural clinics, examples of end uses include: light, vaccine refrigeration, laboratory testing, water purification, battery charging, hot water and steam sterilisation. In primary and secondary schools: light, AV instruction, training and entertainment, computing/internet service, air flow cooling by fan, lantern charging and cooking for pupils. For safe water provision: water

¹ The Renewable Energy Project - Nepal (NPL/B7-3000/AIDCO/2000/2244) was approved by the ALA Committee on 18 July 2002

pumping and water sterilisation (ozonisation) and packing. For general community energy services: lighting, audio/video entertainment, and computing. And for agro processing: milk chilling, tea withering and drying, drying of handmade paper and drying of crops and spices.

- **Institutional development**, both at community and district as well as at central level.

At community and **district level**:

- technically and business-trained community organisations (COs), which would progressively transform into community-owned legal business entities;
- qualified staffed District Technical Offices;
- operational district energy with appropriate funds, qualified in fund management and accounting capacity.

At **central level**:

Alternative Energy Promotion Centre; Solar Energy Test Station; Banking system; a revolving fund and a management information system.

4.2.3 Activities

The main project activities will be to:

- establish and support social mobilisation activities, aiming at sustainable energy service demand through Community Energy Service Providers;
- create technical, financial and business management competence in Community Energy Service Provider groups through training;
- set up a sustainable system for tendering, purchasing, installation and after sales services for energy service equipment and end user applications;
- establish a sustainable system for financing and (partly) subsidising capital and working capital investments of community energy service providers;
- promote and create awareness of uses and schemes for end use applications through energy service provision;
- set up a Project Management Unit for management, planning, promotion and control;
- contribute to capacity building within AEPC and DDCs, particularly at peripheral levels;
- add to the development of measures for quality assurance of solar and other renewable energy products and services.

4.2.4 Implementation

The Executing Authority (EA) is the AEPC. The EA will establish a **Project Steering Committee** (PSC) for policy guidance and co-ordination between all institutions involved in the project as well as a Project Management Unit (PMU). The PSC will meet twice a year and will assist the EA by providing guidance on policy and strategy for the project. The PSC will review and endorse the PMU's six-monthly reports, as well as the policy and strategic implications of the Project Work Plans and budgets drafted by the PMU before they are sent to the EA and EC for approval. The PSC will be chaired by the Executive Director of AEPC and membership will include senior representatives of the parties and project stakeholders concerned as well as the beneficiaries. EC representatives will be invited to PSC meetings as Observers with the right to speak. The project co-directors will provide the secretariats of the PSC. The PMU will be based in the offices of HMG/N. The PMU will be jointly headed by

a full-time Nepalese Co-director appointed by the Executing Authority and endorsed by the Commission, and an EC Co-Director appointed by the Commission and endorsed by HMG/N. Both Co-Directors will have joint and equal authority for managing the project and co-signing all technical and financial documents.

Other PSC functions include the decision on Technical Advisory Committee (TAC) recommendations. TAC is composed of the European and Nepalese co-directors of the PMU, plus representation by project managers of collaborating agencies (UNDO and the World Bank for REDP, UNDP for COPE, DANIDA for ESAP, SNV for BSP, UNICEF for DCDP, DFID for NEWAH, etc.), representations of the solar industry in Nepal through the solar association SEMAN, DDC chairpersons in participating districts and invited observers (NGOs). TAC will meet quarterly, review project progress, responsiveness and compliance and will screen proposals and present recommendations to the PSC.

Within the framework of the overall and annual work plans and disbursement schedules approved by the EA and EC, the PMU will have operational autonomy to cover the technical, administrative, financial and human resources aspects related to Project co-ordination, implementation and management.

4.2.5 Risks and Assumptions

Improved energy service benefits the poorer segments of the population and replaces rather than complementing the present uses of fossil fuels. A policy of decentralisation is adopted in the 10th Five Year Plan, and decentralisation is supported by a shift of technical line responsibility and funds to VDCs/DDCs. The lack of energy service in the agricultural sector and other small industry is a major constraint to productivity and economic viability. Institutional and end user groups pay dues for energy service. Reliable information about future grid extension and hydro potential is available. The EC equipment procurement process is sufficiently flexible to ensure local market competition. Collaborating agencies maintain current projects and strategies. Responsive financial agencies are available. Tariffs are affordable for end use institutions. Risks include major political disturbance in the VDCs/DDCs concerned and the lack of security in the project's areas. Industry does not respond to demand.

4.2.6 Performance Outcome Indicators

Annual statistics of VDCs/DDCs, project results (improved energy available) reported by PMU. Number of sustainable operational Community Solar Energy Groups, and amount of end use energy provided at decentralised levels. PMU evaluation reports, payback rates of respective loans. Number of requests to AEPC for subsidies for institutional systems increases. Increased sales and revenue generation. Product certified according to appropriate protocols at appropriate testing facility. Verifiable PV module and solar battery import statistics. Volume of financial transactions through subsidy, endowment and loan scheme. Availability of products in the solar thermal manufacturing sector. Institutional end users (schools, health posts, etc.) are equipped with functional products which support the provision of good quality education or health services, etc.

4.2.7 Financial Allocation

The EC grant amounts to **€15m**, and HMG/N's contribution is € 0.675m.

4.2.8. Indicative timeframe

Preparations were made in 2002, for commitment the same year. The duration of the programme is from 2003 to 2008.

4.3 Action: Strengthening Rural Development and Governance in the Mid-Western Region (SRD+G)

4.3.1 Objectives

By providing **irrigation** facilities to the command area of about 36 000 ha, the SDR+G project located in the Banke District aims to increase the cropping intensity from the present 130% to a future 179% after full development of the project. Besides significant infrastructure implications, the SDR+G project also aims to provide the Mid-Western region with a real chance to enhance the livelihoods of long neglected rural populations. By contributing to the release of local socio-economic tensions that have been the causes of the conflict, the SDR+G project represents tremendous added value in terms of Conflict Prevention through Long-Term Development activities.

Taking into account the present degree of acceptance of the EC's ongoing project by all political forces (including the Maoists), it is also considered important to implement collateral activities within the framework of SRD+G. The project encourages full implementation of agricultural support activities (including livestock development) plus a study of local pilot schemes in relation to the new legislation on Land Reform. The project also looks at the issue of good governance initiatives at local level, which is a central aspect of decentralisation policy.

4.3.2 Expected Results

At the end of the project, the irrigation infrastructure will comprise the following principal works:

- A gated concrete dam across the Rapti on the East of the West Highway.
- Headworks for the main feeder canal.
- An offtake for diversion for the supply of water on the left bank of the Rapti.
- A 34 km line feeder canal to serve the main command area of about 34 000 ha. net.
- 18 km lined main canals and 75 km secondary canals flanked by hard surface inspection roads with appropriate control, measurement and auxiliary features.
- 360 km of unlined tertiary canals flanked by tracks with appropriate structures for control measurement.

Concerning the support services sector, the following results are expected:

- Formation of a Water User Group (WUG) at tertiary level.
- Formation of a Water User Association (WUA) at secondary level.
- Formation of a Water User Central Committee (WUC) at project management level.

4.3.3 Activities

The project's activities will cover the construction of the required irrigation infrastructure as well as the provision of support services for agriculture development, establishment and training of WUAs and improvement of land management. Support for the livestock sector will also help to increase rural incomes.

The situation regarding the main social services in the project's rural areas will be carefully assessed and, whenever required, duly rectified in order to improve the living conditions of rural families.

The main collateral activities will be carried out in the following three sectors:

- **Good Governance/Decentralisation**

Nepal's pressing problem of poverty reduction will not be sustainable without a commitment to decentralise functions and responsibilities and to combat corruption. EC-funded development activities in the Mid-Western region should encourage self-government and people's empowerment at local level, as envisaged by the Local Self-Governance Act of 1999 (LSA). Mobilisation of non-governmental institutions, participation of users groups, and training of local institutions (VDCs, DDCs) to create full accountability and impartiality in the management of resources will imply intensive training and capacity building activities.

Local corruption and little or no public transparency should be counteracted by enhancing the performance and resources of the local administrations involved.

HMG/N has implemented the Local Governance Programme (LGP) (with assistance from the UNDP), in an attempt to enhance decentralised management of local development efforts. EC-funded activities in the Mid-Western Region should pursue the same objective of sustaining social mobilisation teams through small local funds, to promote the formation of community organisations (including men and women of lower caste groups),

The main indicators of success for these activities will be the percentage of households in village-based community organisations, the number of schemes/projects operated by local organisations, participation of women in the decision-making process, local authorities' capability to use resources from financial institutions, and the number of community-managed service centres (on health, agriculture, veterinary, etc.).

- **Land Reform**

Land is the source of livelihood for almost 80% of the population in Nepal. Haphazardly scattered and unevenly sized parcels, lack of basic infrastructure, unplanned and subsistence farming practices are some of the reasons for low productivity of land and the deteriorating condition of farms. Poor land records and the cadastre system have been another **barrier** to efficient land management and land administration. Most of the cases pending in the civil court are related to land. Land Reform Legislation was approved in 2001-2002. A new land Reform Programme cannot be properly implemented due to the lack of expertise, technology, data and adequate resources. Development of the Mid-western Region could build on a set of studies capitalising on EC assistance already provided in

support of a National Geographic Information Infrastructure Programme and Information services. In this context, land use planning at district level could be started and district and village land use maps produced.

The EC contribution will not take into consideration the issue of land acquisition, but it will help to provide the necessary transparency for ownership-related issues in a limited number of areas. A proper method of channelling this information is an essential prerequisite for preparing a realistic land distribution strategy. Liberated bonded labour (Kamaiyas) has resulted in an acute problem of squatter farming and public land encroachment (Forest), in particular in the Mid-Western region. Future EC involvement in this region should take account of the present situation of landless people in order to facilitate their legitimate access to agricultural resources.

- **Livestock Sector Development**

Improvements in animal health and in nutrition and marketing are inseparable and complimentary components of productivity in the livestock sector. Animal health services must be capable of meeting the demands of the agricultural sector when increased offtake is targeted.

The outstanding importance of livestock in the area where the SRD+G Project is located makes it essential for a holistic approach to be taken to rural development, including the livestock sector, if poverty alleviation in the region is to be achieved.

EC-funded development activities in the Mid-Western region should encourage the development of the livestock sub-sector, as it offers considerable potential for rural employment and income generation, particularly for women, in addition to providing adequate protein content to cover family nutritional requirements, which is especially important to children and nursing mothers.

The main components of the livestock sub-project should comprise: surveillance systems, disease investigation and diagnosis, extension packages, zoonotic disease surveillance, marketing and movement surveillance, food safety and training.

4.3.4 Implementation

Assuming that all the required preparatory work can be carried out during FY 2003/04, the implementation period would be 6 years starting from August 2004. The construction period is estimated to be 4 years, and 2 years will be required for O&M support, strengthening of WUGs and WUAs and intensive agricultural support, assistance in farm water management, including the development of a field channel system, and land management/land consolidation

4.3.5 Risks and Assumptions

Besides the risk of insecurity linked to insurgency activities and considering the slow start of the peace process, no other major risks have been identified. The project would co-ordinate the required intensification of agricultural support activities with the Department of Agriculture

(DoA) and would provide support for specific agricultural services in the irrigated area. This would include the provision of improved planting materials, field trails, demonstration, training and selected equipment/motorcycles. Specific attention would be paid to agricultural support for women and women's groups. In view of the post-conflict situation in the region, project planners should avoid the risk of discrimination among beneficiary groups because of their political affiliation.

4.3.6 Performance Outcome Indicators

Verifiable increase in cropping intensity, viable farming arrangements, acceptance of the project by local rural authorities and among rural communities, active participation of farmers and officials in the relevant administrations who have received training would be a general key indicator of the impact of the project.

The following project outcomes will be particularly relevant:

- Number of surface irrigation scheme constructed and/or rehabilitated in the project areas.
- Number of WUG and WUA formed, duly registered and trained.
- Number of WUA assuming the responsibility for O&M of the completed irrigation scheme.
- Number of farmers participating in agricultural demonstration and training activities.
- Number of committees formed to discuss cropping intensity and agricultural issues.
- Number of facilitators promoting and managing transparency for landownership-related issues
- Level of increased awareness, understanding and dialogue by local people with respect to good governance.(e.g. based on feedback forms)
- More indicators will be developed during the formulation mission.

4.3.7 Financial Allocation

The total EC grant is estimated at € 41m.

4.3.8. Indicative timeframe

Preparations should be started in 2003, for commitment in 2004. The total duration of the programme should be seven years: 2004-2008 (construction); 2008-2010 (O&M)

5. Priority: *Consolidation of Democracy and Conflict Mitigation*

5.1 Strategy Context and Justification

The EC strategy for 2002-2006 places great emphasis on initiatives for the Consolidation on Democracy and Conflict Mitigation. Recent historical developments fully justify the inclusion of specific activities that, in parallel with development co-operation, will help to enhance the livelihoods of local communities and civil society rights and to promote the rule of law in Nepal.

5.1.1 Conflict Mitigation Package I - Support for Local Communities and Civil Society Voice

Nepal has experienced a protracted conflict over the last seven years, with serious negative impact on the country's socio-economic development. Activities designed to support local communities and civil society voice aim to strengthen the peace process or mitigate conflict in the event that there should be a resurgence of violence by sensitising the public to conflict-related issues and addressing some of the root causes of the conflict, such as political and socio-economic inequalities. The CSP identifies conflict mitigation as one of the important areas in Nepal's long-term development. The success of the current peace process is greatly dependent on consolidation at grass roots level.

The key priorities are those areas where people are prone to be drawn into the conflict due to social and economic inequality. The critical areas identified for intervention are the **liberated bonded labour** camps (ex-Kamaiyas), where the government fails to provide them with even the most basic opportunities, and other surrounding communities without means (Dalits and landless).

The second priority is in relation to the **communities** surrounding the Bhutanese refugee camps in Eastern Nepal, who face instability due to the large number of refugees housed in the camps. Both are areas with potential for conflict.

The third priority is a **media** component through which a large part of Nepal's population can be reached and made aware of conflict issues, as well as giving a voice to civil society.

To provide a quick response to the same problems the EC has already funded, a six-month pilot action under the Rapid Reaction Mechanism scheme² and a new phase of consolidation is therefore included in this NIP.

5.1.2 Conflict Mitigation Package II - Support for Judiciary System and Human Rights

Key issues of the Nepalese Justice System concern access to justice, quality of justice and the existing legal regime. Customary laws predating the British influence in the subcontinent are still a central part of the system.

The development of a justice system which is seen to be fair, impartial and independent will underpin good governance, and form the basis for tackling corruption and social injustice. At the same time, denial of impunity for human rights violations requires a decisive strategy for strengthening and modernising the present justice system.

EC Conflict Prevention experts have strongly recommended formulating an Action Plan for the Reform of the Justice System, with a view to developing an EU flagship programme in conjunction with the Nepal Bar Association, the Chief of Justice and the International Commission of Jurists.

For Human Rights, the conflict is likely to continue to impact negatively and conflict polarisation will increase the number of cases of impunity on both sides of the insurgency and counterinsurgency forces. The risk of abuses during the ceasefire and the difficulty in monitoring the situation in remote areas, in terms of both human rights protection and proper functioning of the Judicial System, mean that the existing mechanism for handling a whole

² The RRM decision (RRM 2002-2006) to allocate € 615 000 to short-term pilot initiatives in Nepal was taken in August 2002. Under the Council Regulation of 26 February 2001, resources can be mobilised "**to respond**" in a rapid and flexible manner to crises involving a threat to the rule of law and escalating into armed conflict likely to jeopardise co-operation policies and activities - Reg. (EC) No 381/2001

range of complaints needs to be geared up. Enhancement of the National Human Rights Commission's capacity (NHRC) to ensure a proper level of investigation and examination of cases of Human Rights violation is a primary objective.

5.2 Action: Support for Local Communities and Civil Society Voice

5.2.1 Objectives

- Undertaking community development in critical/conflict-prone areas (in the Mid-western region where the EC will concentrate its future efforts, focusing activities in and around the camps of former bonded labour, in the Eastern region around the Bhutanese refugee camps).
- Supporting the poorest members of society in critical areas through the delivery of basic services from which they have been deprived because of the conflict and social exclusion.
- Enhancing socio-economic development in critical areas.
- Raising awareness among Nepali people on conflict issues and on possible strategies for managing/mediating conflicts at different levels.
- Strengthening civil society in reconciliation, conflict prevention and resolution matters.

5.2.2 Expected Results

- A leading role for local communities behind social and economic development.
- Increased number of deprived people achieving sustainable livelihoods.
- Increased access to basic services for deprived people.
- Increased opportunity for civil society to access media and voice their opinion.
- Increased awareness among Nepali people on conflict-related issues.

5.2.3 Activities

Four activities are planned under support for local community and civil society voice (although they will be further defined during the formulation stage).

The first activity focuses on increasing and building on the capacity of local communities, in terms of both conflict situations and their awareness of self-development.

The second activity will aim to increase and create livelihood opportunities and sustainable deployment for working people in critical areas through training and awareness.

The third will provide basic services, health care and formal and non-formal education to marginalised people through community involvement.

The fourth activity aims to increase awareness of conflict resolution mechanisms in local communities, both through training and media campaign/nationwide broadcasting.

5.2.4 Implementation

The methods of implementation will be detailed during the formulation phase. Given the current unstable situation, where the government cannot intervene at grass roots level in certain parts of the country, it is suggested that NGOs be used as implementing partners.

5.2.5 Risks and Assumptions

The assumption is that the current situation will not deteriorate to the extent that it is not possible for NGOs to work in the field and that the government will not oppose local community mobilisation and networking.

The project is dependent on the transparency of the implementing organisations in the Maoist-affected areas. Field-level activities are highly dependent on the support of local communities.

5.2.6 Performance Outcome Indicators

Detailed performance and outcome indicators will be defined at the formulation stage. Many project aspects related to the peace-building process are not tangible. However, a cost-analysis can be formulated as regards livelihoods components. At the same time, information on measurable physical achievements (work training sessions, outputs, etc.) will be detailed both in the work plans and in the progress reports.

5.2.7 Financial Allocation

The EC grant is estimated at € 3m, to be committed from 2003 to 2006.

5.2.8. Indicative timeframe

Assistance should be implemented over a period of 3 years, starting at the end of 2003.

5.3 Action: Support for Judiciary System and Human Rights

5.3.1 Objectives

The general objective of the programme is two-fold: on the one hand, to support Nepal in its efforts to implement the decentralisation of functions of justice while upgrading the legal assistance mechanisms, especially for people with less chance of benefiting from a fair level of protection; on the other, to provide assistance to the National Human Rights Commission (NHRC) in the development of the institution's capacity to ensure an appropriate level of protection of Human Rights through a smooth functioning complaints and investigation mechanism.

5.3.2 Expected Results

Focusing on areas considered to be bottlenecks that hold back progress on reform, this action is expected to result, on the one hand, in a more transparent, effective and efficient legal administration and, on the other hand, in a stronger National Human Rights Commission. Specific policy, legislation, regulation or administrative instructions will be identified during the preparatory stage for each of the main activities described below. Other results include enhanced capability both of the District Courts and of branch offices for NHRC and the Nepal Bar Association.

5.3.3 Activities

The main activities covered by this action aim to respond to the various potential areas described in point 5.1.2 and could tentatively include (non-exhaustive list):

- Training of trainers for lawyers and human rights officials
- Provision of legal texts and practices, translations
- Provision of equipment
- Provision of scholarships
- Training for the Attorney General Departments and Public Prosecutors
- Training in the delivery of Free Legal Assistance/Aid.

Detailed activities and the selection of geographical areas would be subject to further review and priority screening during the formulation phase.

Specific assistance under this action could aim at public sector administration and at civil society entities such as associations and leading NGOs. Assistance could take the form of one of:

- **Policy advice and institutional support.** Technical assistance for the preparation of legislation and regulations at both central and district levels.
- **Capacity building and training.** To support reform and ensure smooth implementation of new policies, regulations and guidelines, assistance could be provided for skills upgrading, through training, seminars and workshops.

5.3.4 Implementation

The methods of implementation will be defined during the formulation phase.

There is plenty of scope for co-operation in this sector, and it is recommended that the Reform of the Judiciary System and support for the National Human Rights Commission Action Plan and the Nepal Bar Association should be closely co-ordinated with the Member States (UK, Denmark), Norway and the UNDP, in order to ensure the dovetailing of ongoing actions.

5.3.5 Risks and Assumptions

In terms of supporting the judiciary system and NHRC, the main risks to be considered could be:

- Delays in approval of guidelines/procedures
- Conflicting attitude between Executive and Judiciary
- Politicisation of the Bar
- Low response to accountability of judicial functions
- Political changes in government policy
- Conflict escalation.

5.3.6 Performance Outcome Indicators

The main indicators will be:

- Number of functioning courts at district level
- Number of judges/lawyers trained

- Number of offices for the Free Legal Assistance Scheme
- Number of cases dealt with under the Free Legal Assistance Scheme.
- Number of cases dealt with the Courts
- Number of complaints received and handled by NHRC
- Production of new texts/translations
- Establishment of guidelines and procedures
- Increased effectiveness of monitoring human rights violations, including local situations
- Increased transparency and public accountability of the reform of the judiciary system

5.3.7 Financial Allocation

The total EC grant is estimated at € 7.0m.

5.3.8. Indicative timeframe

Preparations should be made in 2003 for commitment in 2004. The duration of the programme should be four years.

6. Priority: Integration into the International Economy

6.1 Strategy Context and Justification

The EC has identified the need to interlink trade and development policy in order to achieve the objectives related to poverty reduction. Thus, for the EC, trade-related technical assistance to developing countries is a high political and operational priority (Doha Development Agenda). It is clear that important **prerequisites** for achieving sustainable economic growth are an open trade regime and a business-friendly environment of law, tax and public policy for enterprises.

One of the most important ways by which a business-friendly environment can be provided and sustained is through increased **economic openness**. A key feature of such openness is a country's integration into the global trading system. The CSP identifies facilitating Nepal's integration into the flow of international trade as a main area for co-operation.

The CSP has also identified potential areas for targeting in support of Nepal's efforts to facilitate trade and investment promotion, which have often been jeopardised by the absence of institutional capabilities, and to establish a proper information strategy to activate contacts between Nepalese trader-manufacturers and potential partners outside of Nepal. Key priorities in this context include: **(a)** the establishment of a **business information** service centre at the Federation of Nepalese Chambers of Commerce and Industry to promote a sustainable export strategy in conjunction with the public sector, **(b)** support for initiatives which advance the concept of **economic diplomacy**, as recognised by HGM/N in its efforts to encourage foreign investment in areas of comparative advantage, and **(c)** assistance to the Nepal-EU Economic Forum, established under FNCCI, to promote **interaction** with their European business counterparts and to enhance economic and trade activities.

6.2 Action 1: Trade Policy (Accession to WTO)

6.2.1 Objectives

The overall objective of the action is to help Nepal to establish and improve the basic conditions for stable and sustained economic growth. The specific objective of the programme is to support Nepal in its efforts to **integrate** into **international trade** and investment flows. This support includes specific assistance in preparing for accession to WTO and managing obligations arising out of the adoption of the multilateral agreement.

6.2.2 Expected Results

The action is expected to result in enhanced integration of Nepal's economy into the global community through:

- Nepal's entry into the WTO;
- increased knowledge among Nepalese officials about international trade policy-related matters in a free trade environment;
- greater expertise on WTO provisions, rules and disciplines;
- improvements in the legal and regulatory framework and greater administrative capacity to ensure compliance with WTO requirements.

6.2.3 Activities

Actions will include:

- Technical Assistance in the areas of SPS, TBT and customs valuation
- Specific Technical Assistance on international trade-related matters, including the drafting of trade-related regulations and legislation. Actions could include support for skills upgrading through training, seminars and workshops, plus transfer of know-how by European experts
- Institutional strengthening to ensure implementation of WTO-related regulations and legislation
- Dissemination of information with the aim of enhancing awareness and understanding the consequences and benefits of WTO membership for Nepal.
- Training, seminars, conferences, workshops, think tanks coordinating private sector with national policy-decision makers
- Trade and Investment-related research.

6.2.4 Implementation

EC activities will need to be co-ordinated with the relevant activities of the other donors involved (UNCTAD) and designed with the assistance of DG Trade. Particular attention should be paid to co-ordination and complementarity with the "Integrated Framework for Trade-Related Technical Assistance to LDCs".

6.2.5 Risks and Assumptions

To make for optimum results, trade sector strategy reform should be addressed through a comprehensive and integrated approach. This will require a firm commitment from HMG/N and co-operation between major donors and agencies.

6.2.6 Performance Outcome Indicators

- Number and extent of WTO regulations/legislation adopted and implemented
- Number of government officials and organisations participating in various activities (e.g. training, seminars, workshops, etc.)
- Level of increased awareness, understanding and dialogue by participants in the various activities (e.g. based on feedback forms)
- Information/advocacy material produced
- Number of research reports produced
- Quantifiable dissemination of information materials.

6.2.7 Financial Allocation

Expected EC contribution: € 2.0m.

6.2.8. Indicative timeframe

Given the major challenges Nepal faces in its accession to WTO, an Identification Mission should be undertaken in 2003 to formulate a programme in full consultation with the other donors involved in this sector. Implementation should be scheduled before the end of 2003.

6.3 Action 2: Economic Co-operation and Capacity Development

6.3.1 Objectives

The general objective of this action is to **foster a business environment** which is conducive - to enhancing EU-Nepal economic relations, - to creating a dynamic private sector in Nepal, thus helping to develop employment and sustainable small and medium-sized enterprises, and to supporting HMG/N in its efforts to promote "Economic Diplomacy".

6.3.2 Expected Results

The Economic Co-operation and Capacity Development Programme should result in:

1. improved implementation by Nepal of its commitments/obligations under the WTO;
2. improved capacity of Nepal to manage its integration into the global economy;
3. enhanced information services to facilitate capacity establishment, consolidation and international exposure of small and medium-sized companies;
4. strengthened and expanded economic relations with the EU and international institutions in the areas of trade (mainly exports), tourism, private investment, and technical and economic co-operation.

6.3.3 Activities

Activities under the programme would generally fall into two categories: capacity building and advocacy. Examples of activities that may be undertaken under each category are given below. A flexible approach to implementation (see below) is recommended, with the possibility of rapid reaction as needs arise. Potential activities would have to be examined in detail at the programme appraisal stage.

1. Capacity Development – *Strengthening key private and public institutions involved in trade, investment and finance*: Actions could include support for *skills upgrading* through training, seminars and workshops, and provision of *advisory services* by European experts, with the aim of enhancing the ability of government organisations to design and implement a regulatory and policy environment conducive to business. Particular attention could focus on those institutions dealing with key issues (e.g. customs procedures, standards, sanitary and phyto-sanitary-related issues, intellectual property protection, etc.), and on professional organisations which help Nepali business to cope with challenging issues (e.g. product competitiveness, market trends, rules and standards, etc.).
2. Advocacy campaign – *Enhancing awareness, understanding and dialogue through*:
 - actions which may include training, seminars, conferences, workshops, etc., to promote broad-based awareness, improved understanding, and dialogue among the relevant key players in the country, especially between the business sector and government on economic and trade-related issues; and
 - support for the Nepal-EU Economic Forum, which has already been established within the context of the Federation of Nepalese Chambers of Commerce and Industry (FNCCI). This embryonic entity should be further developed and supported by EC funding, and also be open to co-operation with neighbouring countries. Assistance will also be channelled into the development of HMG/N's capability for "Economic Diplomacy", to be managed by Nepali officials trained to promote trade, foreign investment, tourism, development co-operation, and access to business co-operation opportunities with economic operators outside Nepal.

6.3.4 Implementation

Implementation of the Programme will be defined during the formulation stage. A possible management arrangement to be explored consists of the possibility of setting up a co-ordination unit in charge of implementing and monitoring programme activities.

6.3.5 Risks and Assumptions

The activities planned under this action are highly dependent on the progress made in legal and policy reform and the political climate and willingness of the Government of Nepal to develop a fair and competitive market economy. Risks and assumptions regarding these activities are again linked to the peace and order situation, the functioning of institutions, and the effective possibility of benefiting from the incentives and "attractiveness" measures already in place.

6.3.6 Performance Outcome Indicators

Activities initially identified are only indicative and a programme appraisal mission should review and upgrade the following indicators:

1. Capacity Development - *Strengthening key private and public institutions involved in trade, investment and finance:*
 - Number of government officials and organisations participating in various activities (e.g. training, seminars, workshops, etc.)
 - Number of issues where skills have been enhanced or advice provided (e.g. based on reports on the activities)
 - Level of skills improvement and quality of advice provided (e.g. based on feedback forms)
 - Number of market and promotional strategies adopted by diplomatic representations.
2. Advocacy campaign - *Enhancing awareness, understanding and dialogue:*
 - Number of government officials, individuals and organisations participating in various activities (e.g. training seminars, conferences, workshops, Nepal-EU Economic Forum, etc.)
 - Number of issues where awareness, understanding and dialogue have been enhanced or even resolved (e.g. based on reports on the activities)
 - Level of increased awareness, understanding and dialogue by participants in various activities (e.g. based on feedback forms)
 - Information/advocacy materials produced.
 - Number of files opened for access to EC-funded regional programmes.

6.3.7 Financial Allocation

Expected EC Contribution: € 2.0m.

6.3.8. Indicative timeframe

Preparations should be made in 2004 for commitment the same year. The duration of the programme should be four years to allow for both short-term and some longer-term assistance, depending on needs.

NATIONAL INDICATIVE PROGRAMME (2002-2006)

NEPAL

INDICATIVE TIMETABLE

Action (NIP Point) / € Million to be committed in year	2002	2003	2004	2005	2006	Total
1.1 (4.2.7) Renewable Energy and the Environment	15					15
1.2 (4.3.7) Strengthening Rural Development and Governance in Mid-West.			41			41
2.1 (5.2.7) Support for Local Communities and Civil Society Voice		3				3
2.2 (5.3.7) Support for Judiciary System and Human Rights			7			7
3.1 (6.2.7) Trade Policy (Support for WTO Accession)		2.0				2
3.2 (6.3.7) Economic Co-operation and Capacity Development				2.0		2
TOTAL						70