



NEPAL
ECONOMIC
FORUM

nefport

A SPECIAL ISSUE ON
**TOURISM AND HOSPITALITY
PERSPECTIVES AND PROSPECTS**

DOCKING NEPAL'S ECONOMIC ANALYSIS

TOURISM AND HOSPITALITY SPECIAL

ISSUE 28 | MARCH 2017

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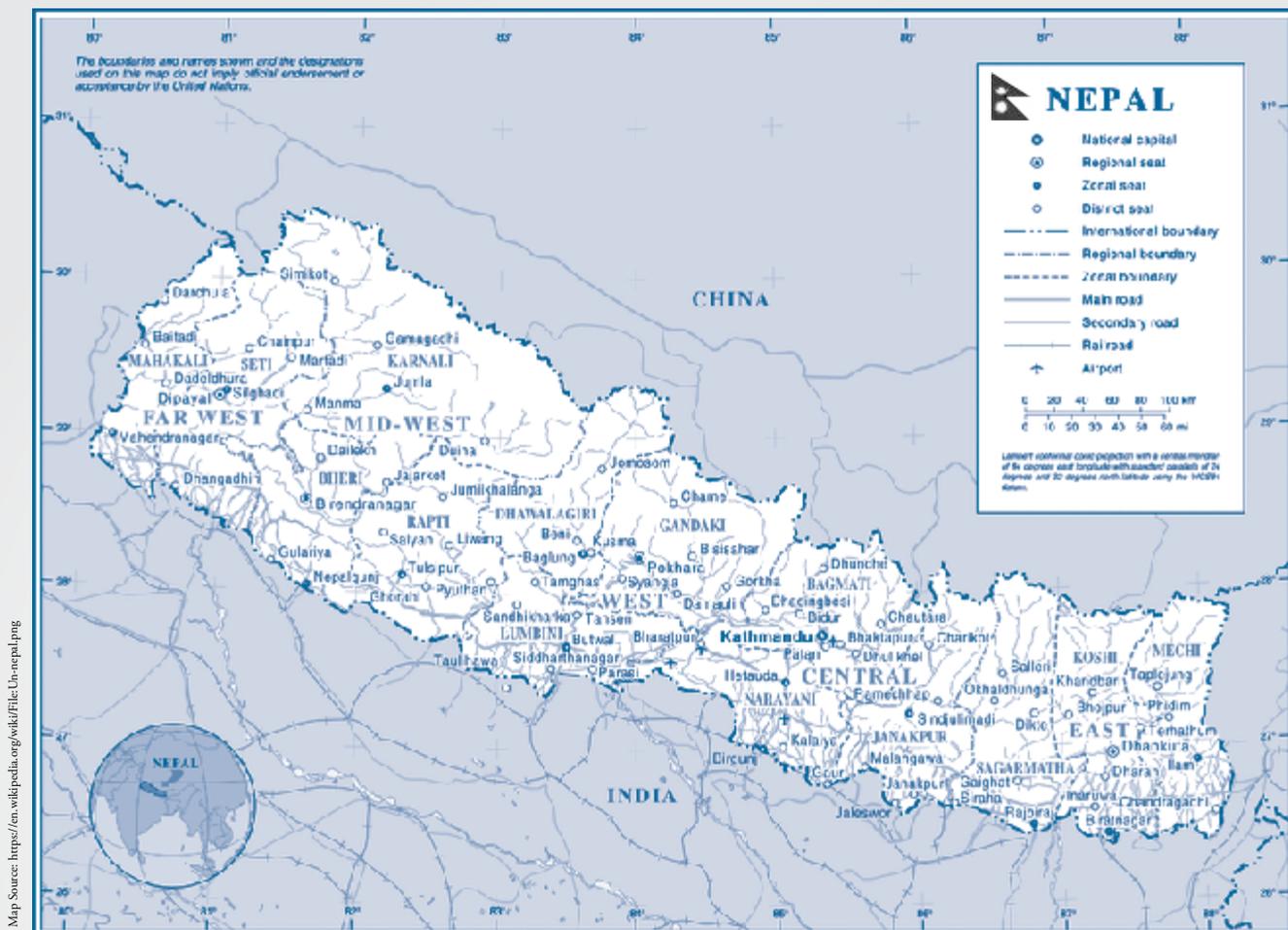
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FACTSHEET

NEPAL FACTSHEET



KEY ECONOMIC INDICATORS

GDP	USD 21.15 billion	GDP Growth rate (%)	0.77
Rank	104	Inflation (annual %)	10.2
GNI per capita (Atlas)	USD 730	Agricultural growth rate (annual %)	1.3
Rank	196	Industrial growth rate (annual %)	-6.3
GNI (PPP)	USD 2,500	Service Sector growth rate (annual %)	2.7
Rank	187		
Gross Capital Formation (% of GDP)	28%		
HDI	0.548		
Rank	145		

Sources:

Left Table - The World Bank; HDI figure from Human Development Reports of the UNDP; Right Table - Economic Survey Fiscal Year 2015-16 - Ministry of Finance, May 2016



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EDITORIAL

One of the big updates for Nepal Economic Forum (NEF) this quarter was its feature in the list of Top Think Tanks in Southeast Asia and the Pacific (84/100) in the 2016 Global Go To Think Tank Index Report released by the Think Tanks and Civil Societies Program under the University of Pennsylvania. We are very thankful for the support from different stakeholders as well as members of our distinguished advisory board; which has been crucial in NEF's growth.

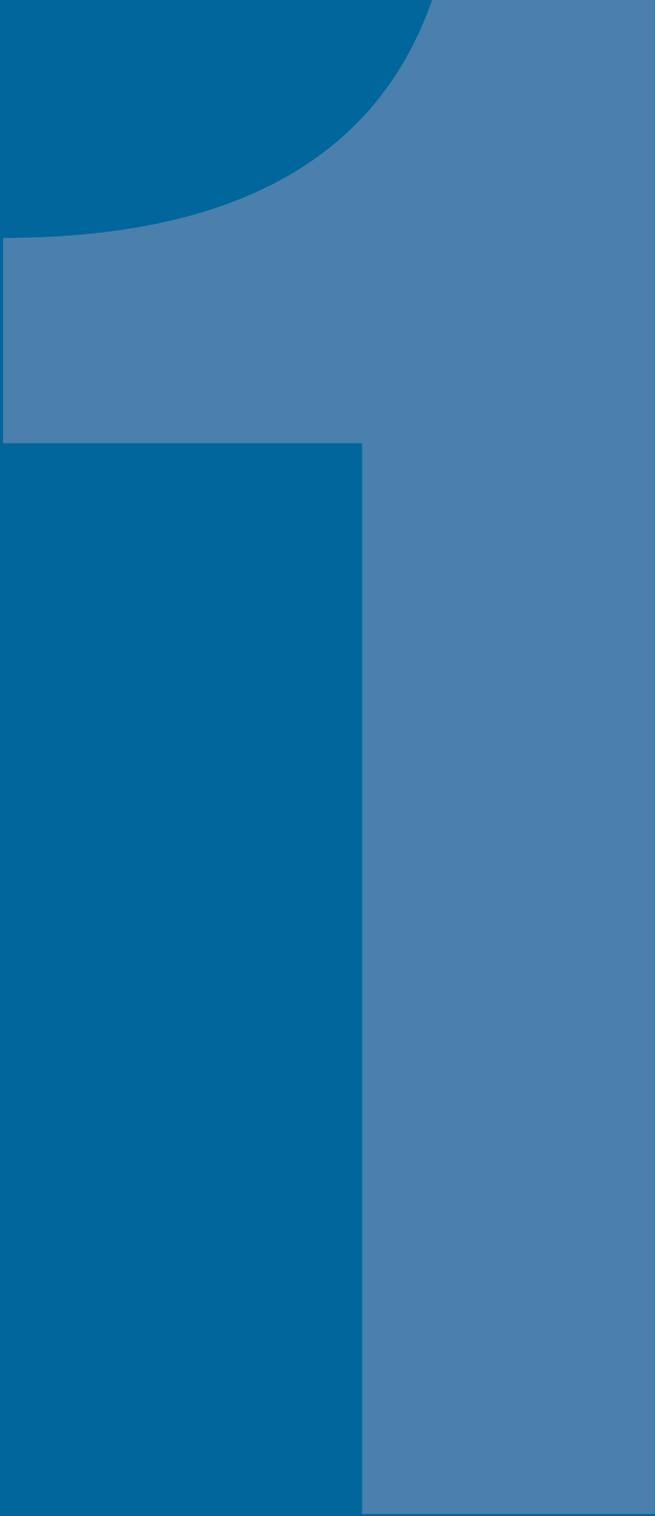
This quarter NEF continued to collaborate with partners on events for instance the panel discussion forum on the "Economic Development of Landlocked Countries" with the Embassy of France which explored the issue of whether being landlocked is an impediment or rather a mind-set which requires looking at development through land linked lenses.

The quarter was also marked with many pieces of legislation being approved by the parliament. The criticism on unspent capital expenditure has made the government rethink its spending of the budget and will provide the impetus for better administering of the budget. The announcement of local elections after 19 years also provides an opportunity for economic growth, and a move towards local levels with more accountability and transparency. Meanwhile the relief from power cuts after a decade is also showing a positive impact on economic activities.

While there will be changes in government in the next quarter, we expect that some key portfolios may remain unchanged and provide continuity to specific endeavours of key ministries.

This issue focuses on hospitality and tourism which continues to be a big contributor to Nepal's economic growth. We would like thank all the individuals who have provided their time to meet the team and provide their perspectives. As always, we remain eager to receive your valuable feedback on how to make future issues of nefport more useful and user friendly. Please email us your suggestions at info@nepaleconomicforum.org.

Sujeev Shakya
Chair, Nepal Economic Forum

A large, stylized number '1' graphic in a lighter blue shade, positioned in the upper right quadrant of the page. It has a curved top-left corner and a vertical stem.

GENERAL **OVERVIEW**

GENERAL OVERVIEW

POLITICAL OVERVIEW

Constant delays to formulate election-related laws have not only created widespread confusions regarding the legislative framework for polls but have also raised doubts over proposed election dates. Although the government has vowed to hold local level elections on May 14, 2017 it still faces obstructions from the Samyukta Loktantrik Madhesi Morcha (SLMM). Further, the Election Commission (EC) has continuously expressed concerns due to slow preparations and planning as regular obstructions have slowed the process of preparing election-related laws. Lack of consensus and prolonged delays have now raised questions regarding the successful completion of not only local polls but also provincial and federal level elections that need to be held by January 2018.

Local election dates finalized: After a gap of two decades since 1997, the cabinet has finally approved the government's proposal to hold local elections, approving the proposed date of May 14, 2017. Although the Election Commission (EC) had initially proposed to hold the elections in two phases - on May 15 and June 4 - however the main coalition partner of the current government; Nepali Congress, was in favor of completing the election by the end of the first month of the Nepali calendar- Baisakh; resulting in the proposal of completing polls on May 14 itself. Ministry of Finance (MoF) is releasing a budget of NPR 10.29 billion (USD 94.56 million) to hold the election while the election commission is seeking finalization of the electoral laws to expedite the

implementation process. Moreover, the Cabinet has also activated the Federal Commission to ensure the rights of Madhesis, Tharu, indigenous communities and women.¹

Constitution amendment delays approval of election-laws: The government has not been able to create consensus over the constitution amendment proposal, impacting the approval of election-related laws. As opposition parties continue to rally against the constitution amendment bill, the government has failed to formulate election-related laws. While Madhes-based political parties have announced a boycott of the election if the amendment bill is not endorsed, the opposition party alliance led by the Communist Party of Nepal (Unified Marxist Leninist) CPN-UML have

opposed the government's move to register the constitution amendment bill in parliament. With agreement over the constitution amendment bill looking far out of reach, the government has failed to formulate the required election-related laws in a timely manner.²

Disagreements persist over LLRC report: Following recommendations made by the Local Level Restructuring Commission (LLRC) to register 719 village and municipal councils in the new federal-setup, the government has struggled to tabulate the report for approval. Amidst fears of antagonizing the Madhes-based parties and Samyukta Loktantrik Madhesi Morcha (SLMM); which has objected to the report, the government has formed a task force to further review

LLRC's recommendations.³ Although the Cabinet has decided to increase the number of local units in Terai focusing on the population density, there are still frustrations arising on the government's inability to facilitate the approval of the LLR report.

The CPN-UML has also discouraged making any revisions to the report saying it would violate constitutional provisions. Although the EC has clearly stated that the report must come into force at least a 100 days prior to local polls, negotiations have failed to outline a clear path of action to implement the report.

Role of EC unclear: Due to regular delays in the endorsement and passing of election-related laws, the EC remains unclear about its roles. The EC has urged the government and parliament to finalize five election-related bills to properly outline the necessary laws to hold elections as per the new constitution. The EC has also expressed doubts over the likelihood of three levels of elections being held by January 2018 - when the term of the incumbent parliament ends. Continuous obstructions in

the Parliament have resulted in the government's failure to authenticate necessary election laws with poll dates approaching fast. While the Act Related to the Election Commission, Voter List Act and the Election Offence and Punishment ACT has been formalized, the EC is awaiting the Act on Political Parties.⁴ The EC has expressed concerns over the lack of a detailed plan to organize elections as the government continues to fail to announce election dates and formalize the new administrative centers as recommended by the LLRC report.

Right to reject provision dropped: The government has dropped the EC's proposal to include a 'right to reject' option for voters during the local polls. The EC had proposed to include a 'none of the above' (NOTA) option for voters explaining that a 'right to reject option' would maximize the democratic right of voters. The Prime Minister's Office and political parties however opted for removing the provision stating that such a provision could further complicate elections in a fledgling democracy like Nepal. In South Asia, India and Bangladesh have implemented NOTA provisions

during elections while Pakistan too reversed such a provision following non-cooperation by political parties.⁵

Ambassadors nominated: The Cabinet has recommended 14 people as ambassadors in various diplomatic missions abroad. The recommendation came on a pro rata basis with Nepali Congress recommending six ambassadors and CPN Maoist Centre recommending three. In the current scenario, 13 diplomatic outposts are without any ambassadors.⁶

Nepal falls in Corruption Perceptions Index: Nepal slipped one spot down to 131 in the Corruption Perceptions Index 2016 survey compiled by Transparency International (TI). Despite gaining two points in this year's index from 27 points in 2015, Nepal fell one spot to occupy the 131st position jointly with Iran, Kazakhstan, Russia and Ukraine. Denmark and New Zealand occupy the top position in the index with 90 points.⁷ Among the SAARC nations, Bhutan stands at 27th position with 66 points and India at 79th position with 40 points.⁸

“ OUTLOOK

Failure to reach consensus over the constitution amendment bills and LLRC report have resulted in continuous obstructions in Parliament proceedings. As the proposed dates of local level polls near, the slow preparation of election-laws has now put the government and EC under tremendous time constraints. Public confidence and support for the government continue to recede as authorities also face pressure to organize provincial and federal level polls by January, 2018 as per the constitutional deadline. The credibility of the political parties hinges on how the local elections are going to be conducted. The local elections will be important to shift the focus away from Kathmandu and with local political leaders elected there will be more accountability in the funding and implementation of government programs. We need to recall that in 1997 a similar move occurred; but as the Kathmandu political elite started to lose control, they dissolved the local governments and it has taken 19 years for another election to happen. The change of guards should take place smoothly at the federal level and with some of the Ministers from Nepali Congress to continue, we may see some sense of continuity in the otherwise very short lived governments and appointments.

GENERAL OVERVIEW

INTERNATIONAL ECONOMY

Uncertainty looms large in world economies today especially after US President Donald Trump officially took the oval office in January. Meanwhile, the situation is exacerbated with the UK pushing hard for an official Brexit and oil prices in the world market remaining unstable. Amidst all this, Chinese President Xi Jinping has called out to world leaders to not lose faith in globalization during the Davos World Economic Forum. In addition, India's newest budget announcement provides an optimistic outlook in terms of development.

President Donald Trump takes office: United States President Donald J. Trump officially took the oval office on January 20, 2017. Since then, he has signed several executive orders that have invited major criticisms and outcry from the general public. The Trans Pacific Partnership (TPP); a trade deal with 11 countries in the Pacific rim was the first to be scrapped, and there have been talks to renegotiate North American Free Trade Agreement (NAFTA) with its neighbours, Canada and Mexico.⁹¹⁰

Another major move has been the reinstatement of Mexico City Policy; also referred to as the global gag rule, wherein a ban has been placed on provision of funding to International Non-Government Organizations (INGOs) that either perform abortions or provide information about them. The global gag rule also

prohibits funding for groups that lobby for legalization of abortion. Executive orders have also been signed to allow construction of projects such as the Dakota Access pipelines; initially blocked by the Obama administration over environmental concerns.¹¹ Meanwhile an executive order has also been signed that denies refugees and immigrants from certain Muslim majority countries into the United States.¹²

Official Brexit draws closer: Last June, people of the United Kingdom (UK) voted to leave the European Union in a historic referendum. However, for the UK to officially end terms with the Union, it needs to invoke Article 50 of the Lisbon Treaty; signed by the heads of state and governments of EU member countries; which gives the associated parties two years to agree to the terms

of the split. However, according to the UK high court's ruling in November, the government first needs a vote from the parliament to trigger Article 50.

The Brexit Bill was passed through the House of Commons on the first week of February and was overwhelmingly approved by a majority of MPs.¹³ British Prime Minister Theresa May intends to trigger the process by the end of March on approval from the House of Lords, which means that the UK will be expected to have left the EU by the summer of 2019. The government will also enact a Great Repeal Bill that will end EU law in the UK.

US Federal Reserve increases interest rate: In a highly anticipated move, US Federal Reserve – the central bank of America, raised short-term interest rates in December 2016, the

second hike since 2006. The interest rates were raised by 25 basis points (quarter of a percentage point) to between 0.50% and 0.75%.¹⁴ The move comes at a time when the US economy is on the verge of full employment and inflation is almost reaching the central bank's target point of 2%; thus, a valid step for the US Federal Reserve. Janet Yellen, chairman of the Federal Reserve System, expressed that such a move reflects confidence on the progress and resilience of the US economy on the Federal Reserve's part. She also made onlookers wary about looming uncertain economic climate as changes in various fiscal and economic policies are expected from the new Trump administration. The Federal Reserve is expected to announce interest rate hikes again in 2017.¹⁵

WEF Davos held: The World Economic Forum annual meeting for 2017 was held from January 17-20 in Davos, Switzerland under the theme 'Responsive and Responsible Leadership' where business, political, academic and other leaders from around the world attended to discuss various pertinent issues in the global economy.

A major highlight was Chinese President Xi Jinping's speech defending globalization. According

to President Xi Jinping, globalization has fuelled global economic growth and facilitated movement of goods, capital, and interaction among people, alongside technological spillovers. Therefore, it is wrong to blame globalization for all the problems the world faces today. President Xi Jinping however did acknowledge that globalization also benefits certain groups; leaving behind others, and subsequently advocated for inclusive development and growth. Other major topics discussed at the forum were Brexit, poverty and the implications of Trump's administration's policies.

2017 Union Budget announced in India: Union Budget for the new FY 2017-18 was presented by Indian finance minister Arun Jaitley on February 1, 2017. It was broadly categorized into 10 themes – agriculture, rural employment, youth, poor and the underprivileged, infrastructure, financial sector, digital economy, public service, prudential fiscal management and tax administration.

One of the most prominent features of the newest budget is the focus on agriculture for development. The government has pledged an increased investment in irrigation

projects through various schemes and provision of easy credit worth NPR 16 trillion (USD 147 billion) to farmers at lower interest rates; along with implementation of other measures like crop insurance schemes and model laws on contract farming. The government also launched a new scheme called Trade infrastructure for Export Scheme (TIES), to create better infrastructure for export promotion at the state level. Moreover, with the new budget, the government is taking a liberal stance when it comes to Foreign Direct Investment (FDI). It has abolished the Foreign Investment Promotion Board (FIPB) which required prior approval for foreign investment, to ease FDI inflows.

In the new budget, India has also pledged to increase financial aid to Nepal by 17% at NPR 6 billion (USD 55 million), with the aim of encouraging development in the nation. India has also proposed to lower interest rates from 1.75% to 1%, on soft loans to Nepal. India had recently extended NPR 79.5 billion (USD 730 million) in soft loans to help with post-earthquake construction.

Oil prices on upward trend: After hitting the lowest point in January

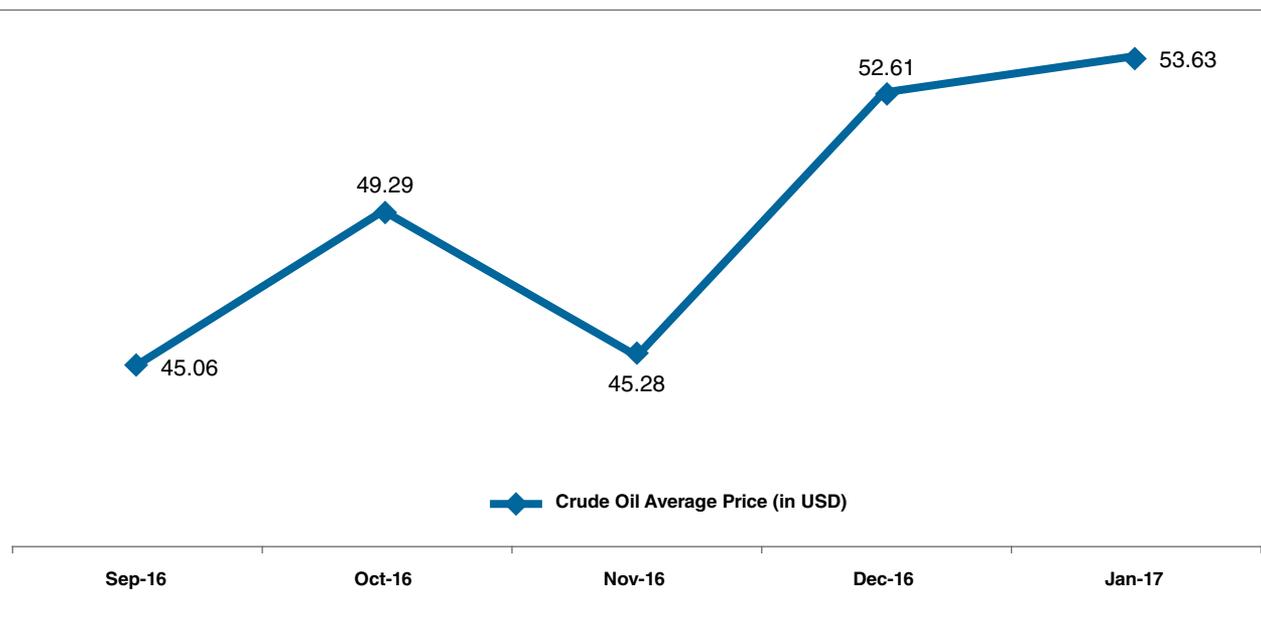
2016 in several years, crude oil prices in the global market have been on a fairly increasing trajectory. The last two quarters witnessed consistent increase in prices, notwithstanding the slump in November. Despite talks to freeze output to keep prices artificially low, members of the Organization of the Petroleum Exporting Countries

(OPEC) ended up pumping oil at record-high levels in November leading to decreased prices.¹⁶

As of January 2017, average crude oil prices stood at USD 53.63 (NPR 5838) per barrel up from USD 45.28 (NPR 4927) per barrel in November. This shows that OPEC member

countries are finally conforming to oil freeze agreement; however, markets still remained uncertain about the supply and demand dynamics over the compliance issue. Meanwhile, the Trump led administration has also added new sanctions against Iran; that could obstruct oil exports from the country furthering oil price instability.

Figure 1: Monthly average prices of crude oil (Brent, WTI and Dubai)



Source: World Bank Commodity Price Data (The Pink Sheet)

OUTLOOK

The United States of America under the new Trump administration has been mired by one uncertainty and controversy after another. The recently reinstated gag rule stands to affect Nepal as well; as funding to organizations providing counselling on reproductive health and contraceptive uses are cut short. Moreover, protectionist policies can be expected from the Trump administration, which will severely affect other economies through trade restrictions and various tariff measures.

Moreover, the focus of the newly announced Union budget of India on the agricultural sector is all set to make the Indian agricultural sector more competitive in the global market. Nepal ought to take prudential steps to stand up to the competition that cheaper Indian agricultural and manufactured goods pose. It should also reap maximum benefits through scrupulous spending of increased aid flows.



MACROECONOMIC
OVERVIEW

MACROECONOMIC OVERVIEW

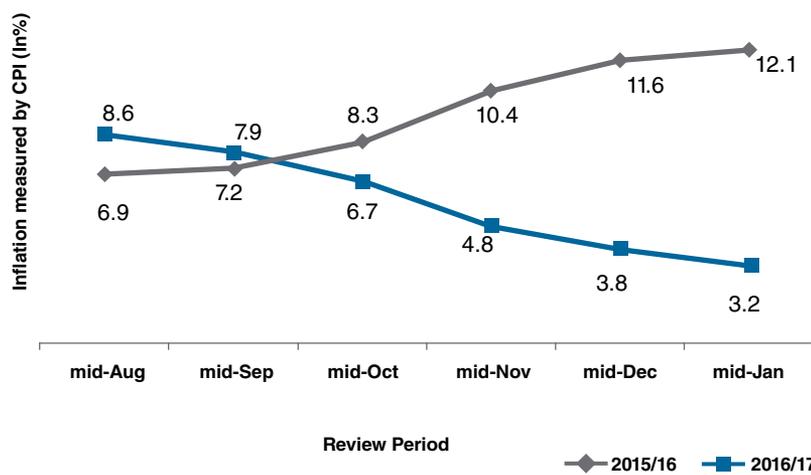
Inflation level has receded to a record low at 3.2% over the past three months of FY 2016-17; thus taming the inflation within the targeted level of 7.5%. On the other hand, Nepal's trade deficit continues to widen while government expenditure levels are lagging behind, forcing the Ministry of Finance to revise their estimation on expenditure.

Inflation: Inflation rate, measured by Consumer Price Index (CPI), dropped to its lowest level in 12 years at 3.2% as of January 2017; as shown in Figure 2. It stood at a peak of 12.1% over the same period the previous year. Food inflation moderated to 0.7%, which was caused by a decline in price for vegetables, meat and cereals. Non-food inflation also moderated to 6.2% on the back of declining prices of clothes, housing and education.¹⁷

The massive drop in inflation rates can be attributed mainly to an improved supply situation and a deceleration in the Indian inflation rate. Prices in Nepal have moderated after the end of the border blockade, as supply has not been impeded. During the blockade, major supply disruptions caused domestic prices to rise rapidly as Nepal depends on India for more than 60% of its total imports.

Furthermore, inflation has also been moderating in India as a result of Indian Prime Minister Narendra Modi's demonetization program, which severely impacted money supply in the country. A possible fall in money supply could have led prices to decline, thereby causing a major downward pressure on inflation rates in India. As Nepal is an import based

Figure 2: Year on Year inflation measured by Consumer Price Index (CPI) for three months of FY 2015-16 & 2016-17



Source: Current Macroeconomic Situation of Nepal (Based on the six month data of 2016/17), Nepal Rastra Bank

economy -with India being a major importing partner - the direct effect of demonetization was also observed in the Nepali economy. As such, the inflation in Nepal shrank to 3.2% in January 2017 compared to 12.1% in the previous year.

Inflation Wedge between Nepal and India: Inflation wedge, measured as the year-on-year change in CPI of India and Nepal has fallen to zero, as shown in Figure 3. Over the same period last year, the

inflation wedge between India and Nepal stood at 6.4% as shown in Figure 4. Inflation wedge between the two countries narrowed from 5.2% in July to 3.5% in August. The wedge narrowed further to 3.6% in September, 2.5% in October, 1.2% in November and 0.4% in December. An improved supply situation between the two countries and a deceleration in the Indian inflation rate can be cited as the main reasons for the reduction in inflation wedge.

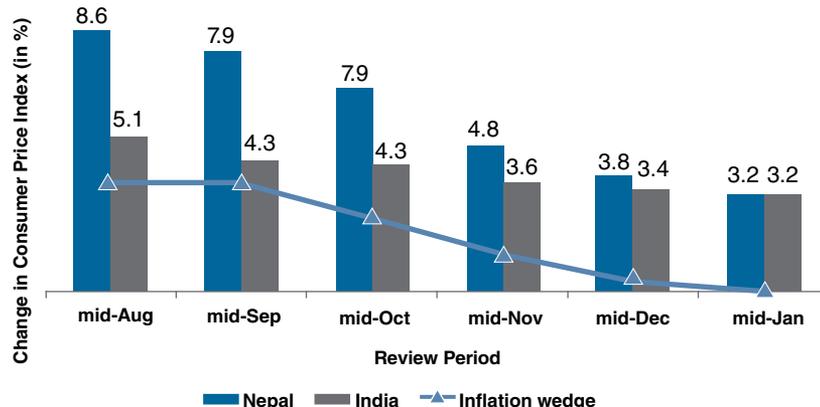
Import-Export and trade deficit:

Merchandise imports have increased by 67.3% to NPR 464.61 billion (USD 4.27 billion) in the first six months of FY 2016-17, as shown in Figure 5. During the same period in the previous year, merchandise imports had deteriorated to -25.7%, due to effects of the border blockade. Imports have been increasing on account of an increase in import of vehicles, petroleum products and machinery. Nepal's imports from India increased by 95% in comparison to the same period last year; it shows a greater dependency on its neighbour.

While merchandise imports have shown a drastic increment, merchandise exports have grown at a sluggish pace in comparison to imports. In the first six months of FY 2016-17, merchandise exports increased by only 14.8% to NPR 36.27 billion (USD 333 million), in comparison to a drop of 27.2%, as shown in Figure 6. A lack of growth in the industrial sector can be attributed to the lack of any substantial growth in exports. Similarly, wholesale price indices (WPI) of agriculture commodities and domestic manufactured goods showed a growth of 2% and 4.8% respectively. Such increment in WPI could have made our domestic export more expensive thereby leading our export to shrink.

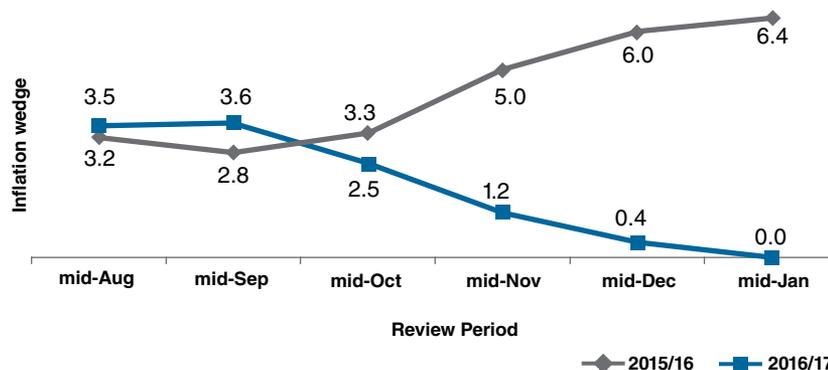
As a result of the widening gap between imports and exports, Nepal's trade deficit increased to 74%, compared to a contraction of 25.5% in the same period in the previous year, as shown in Figure 7. Nepal's trade deficit now stands at NPR 428.33 billion (USD 3.94 billion). Nepal's propensity to import goods from India and the lack of growth in

Figure 3: Year-on-year percentage change in CPI in Nepal and India and the inflation wedge in the corresponding period for FY 2016-17



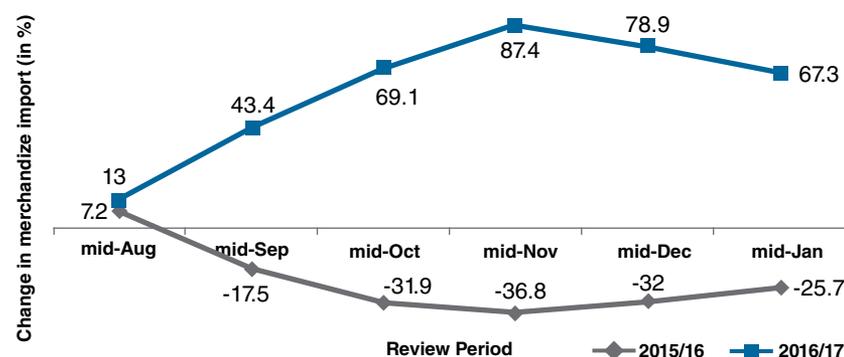
Source: Current Macroeconomic Situation of Nepal (Based on the six month data of 2016/17), Nepal Rastra Bank

Figure 4: Year-on-year change in inflation wedge (based on CPI) between Nepal and India in FY 2015-16 and FY 2016-17



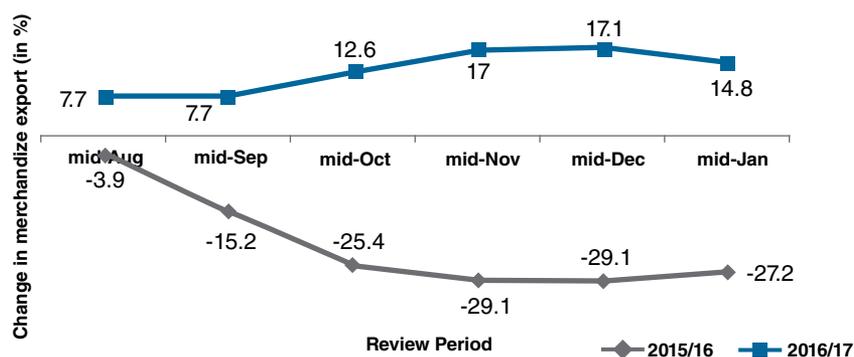
Source: Current Macroeconomic Situation of Nepal (Based on the six month data of 2016/17), Nepal Rastra Bank

Figure 5: Year-on-year percentage change in merchandise imports in review periods in FYs 2015-16 and 2016-17



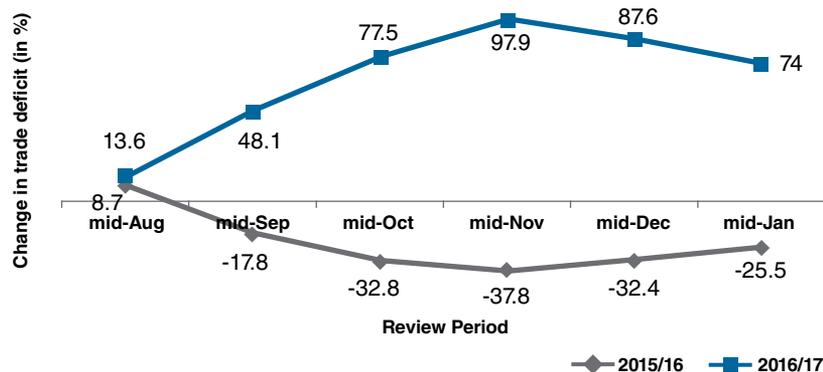
Source: Current Macroeconomic Situation of Nepal (Based on the six month data of 2016/17), Nepal Rastra Bank

Figure 6: Year-on-year percentage change in merchandize exports in review periods in FYs 2015-16 and 2016-17



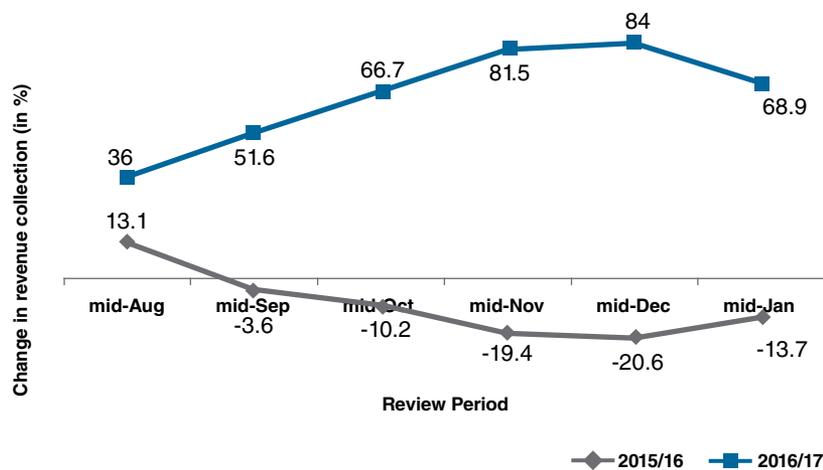
Source: Current Macroeconomic Situation of Nepal (Based on the six month data of 2016/17), Nepal Rastra Bank

Figure 7: Year-on-year percentage change in trade deficit in the twelve months of FYs 2015-16 and 2016-17



Source: Current Macroeconomic Situation of Nepal (Based on the six month data of 2016/17), Nepal Rastra Bank

Figure 8: Year-on-Year percentage change in revenue collection during the review periods for FY 2015-16 and 2016-17



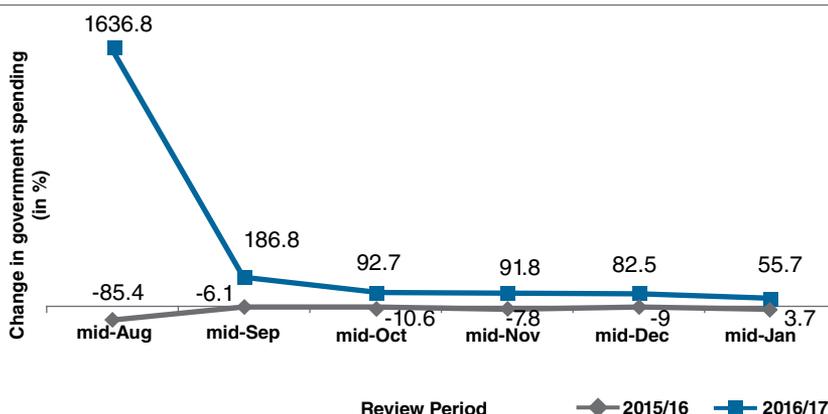
Source: Current Macroeconomic Situation of Nepal (Based on the six month data of 2016/17), Nepal Rastra Bank

domestic producers can be attributed to the widening trade gap. With the government unable to boost exports and support the development of the domestic industrial sector, the trade deficit will continue to worsen, as imports grow at a substantial rate.

Government Revenue: Government revenue collection increased by 68.9% amounting to NPR 277.57 billion (USD 2.55 billion) against a drop of 13.7% in the corresponding period of the previous year as shown in Figure 8. Increase in collection of government revenue can be attributed to the higher growth rate of value added tax, income tax and customs. While government revenue collection is increasing; the new directive of NRB to reduce debt equity ratio of auto loan financing to 50% is expected to hit government revenue collection; however, the restriction is only for private auto loan financing. Since duties on automobile imports make up a significant portion of government tax receipts, a decrease in vehicle imports induced by reduced auto-lending will impact revenue collection for the government. In fact as of March 3, 2017 the collection of revenue has already decreased by 7% to NPR 8.43 billion (USD 75.5 million); the targeted collection was NPR 9.7 billion (USD 89.15 million).¹⁸

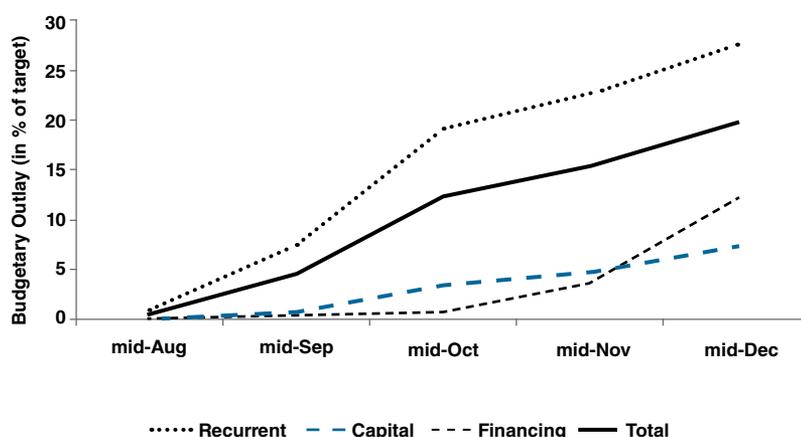
Government Expenditure: Total government expenditure increased by 55.7% to NPR 248.20 billion (USD 2.28 billion), compared to an increase of 3.7% in the corresponding period of the previous year, as shown in Figure 9. This was on account of both recurrent and capital expenditure rising to NPR 196.47 billion (USD 1.81 billion) and NPR 30.97 billion (USD 285 million) respectively. Recurrent and capital expenditure

Figure 9: Year-on-year percentage change in government expenditure during the review period for FY 2015-16 and 2016-17



Source: Current Macroeconomic Situation of Nepal (Based on the six month data of 2016/17), Nepal Rastra Bank

Figure 9: Budgetary outlay trend over the three months of FY 2016/17



Source: Ministry Wise Budget Expenditure Status for various months, Financial Controller General Office

stood at NPR 126.01 billion (USD 1.16 billion) and NPR 13.63 billion (USD 125.3 million) respectively in the corresponding period of the previous year.

While both recurrent and capital expenditure have increased in comparison to the corresponding period of the previous year, the Ministry of Finance (MoF) have revised capital expenditure targets for FY 2016-17 to 84% of the allocated amount of NPR 311.95 billion (USD 2.87 billion). The

MoF mentioned weak performance of ministries in mobilizing the budget as a major reason for this revision. For instance, Ministry of Physical Infrastructure and Transport has spent only a quarter of their allocated budget within the six months of FY 2016-17. In addition, recurrent expenditure is also expected to stand at 91% of the total allocation amounting NPR 617.16 billion (USD 5.67 billion). Figure 10 shows the monthly outlay in terms of percentage of the target achieved for government spending.

VAR MODEL BASED ANALYSIS ON RELATIONSHIP BETWEEN INDIAN AND NEPALI INFLATION

As shown in **Table 1**, 'L' signifies lagged values of respective coefficients. The output confirms that Inflation of Nepal is more dependent on Inflation of India as lagged values – except for L3 - are statistically significant at 5% significance level. However, most lagged inflation coefficients of the Nepali economy are not statistically significant at 5% significance level. Therefore, the statistical findings conclude that inflation of Nepal is influenced by the inflation levels of India.

In contrary, inflation of India is affected by its own lagged values rather than inflation of Nepal as shown in the **Table 2**. The statistical coefficients of Indian lagged inflation - except for L3 - are statistically significant at 5% significance level; whereas, the lagged inflation coefficients of Nepali economy are not statistically significant. Thus, inflation in Nepali economy doesn't actually influence the Indian inflation. The possible reason could be minimal contribution of Nepali export in the Indian economy.

This analysis has been done considering yearly inflation data of Nepal and India from FY 1965 to FY 2015.¹⁹ As per the Augmented Dicky Fuller (ADF) test, data was found to be stationary at 1% significance level; thus Vector Autoregressive Analysis (VAR) was performed to determine the relationship between inflation of Nepal and India by considering the lag order of 4 (Baysian Information Criteria has been used to confirm the lag order of 4). Further econometric analysis shows that the above VAR model is stable as all eigen values lie within the unit circle. Likewise, residuals of VAR are not correlated as confirmed by the Multivariate Portmanteau Test or autocorrelation function (ACF) of residuals.

Table 1: Vector Autoregressive (VAR) output

		Coefficient	P values
Nepal	Nepal		
	L1	-0.017	0.917
	L2	0.062	0.653
	L3	0.041	0.767
	L4	0.498	0.000
	India		
	L1	0.345	0.034
	L2	-0.506	0.001
	L3	0.246	0.106
	L4	-0.586	0.000
	Constant	7.712	0.000

Table 2 Vector Autoregressive (VAR) output

		Coefficient	P values
India	Nepal		
	L1	0.074	0.676
	L2	0.213	0.146
	L3	0.983	0.504
	L4	0.522	0.000
	India		
	L1	0.344	0.046
	L2	-0.644	0.000
	L3	0.096	0.553
	L4	-0.612	0.000
	Constant	6.955	0.000

Author's computation based on the data from World Bank

OUTLOOK

Inflation levels are expected to remain relatively low in the country, with the only threat to inflation coming from changes in global oil prices. Nepal's trade deficit will continue to widen, increasing the need for strengthening domestic industries in order to make Nepali exports more competitive in the global market. Since the current account deficit is a product of consumption binge in case of Nepal; therefore, the government should use deficit financing for investment purposes. If the borrowed foreign funds are not utilized for making investments with a higher return than the interest rate; the ability to repay the debts may come into question. Lastly, revision of capital and recurrent expenditure targets has compounded fears of the government being unable to spend the entire allocated budget for FY 2016-17.

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SECTORAL
REVIEW

AGRICULTURE

The International Monetary Fund has projected that Nepal's annual gross domestic product will grow at 5.5% in FY 2016-17 due to increased agricultural output following plentiful monsoons. The government has taken initiatives such as the agriculture modernization project, yield-base insurance schemes, and supply of improved seed varieties to boost the agricultural economy. However, measures such as year-round irrigation facilities, modernization of farming techniques, and timely supply of agricultural input for the sustainable agricultural growth still remain inadequate.

10 year PM agro program launched in Dhading:

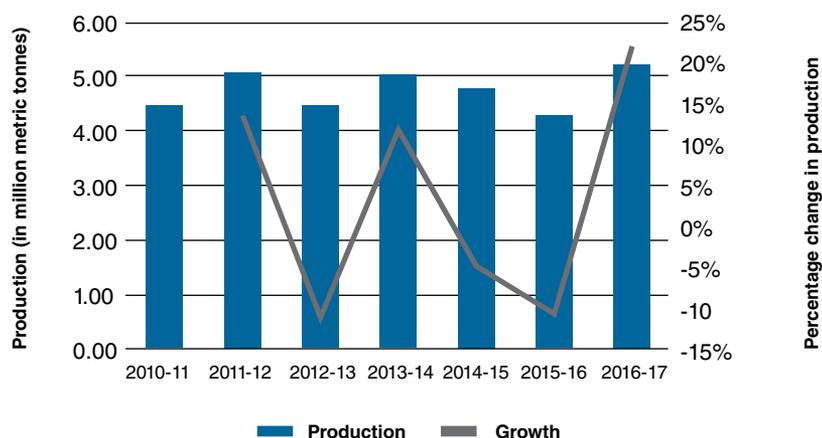
The District Agriculture Development Office (DADO) of Dhading, has launched a 10-year Prime Minister Agriculture Modernization Project as envisioned in fiscal budget of 2016-17. This 10 year national project aims to create 2,100 pocket areas of 10 hectares each, 150 blocks of 100 hectares each, 30 zones of 500 hectares each and seven super zones of 1,000 hectares each to achieve self-sufficiency in food-products through the adoption of modern technologies and mechanization in the farming sector throughout the country. In Dhading, the project has planned to spend NPR 19.2 million (USD 0.18 million) within FY 2016-17. DADO has identified 25 pocket areas, each consisting of at least 10 hectares of farm land, where each pocket area will specialize on one product. The proposed agricultural products for the project are vegetables, banana, lemon, large cardamom, paddy, maize and bee keeping.²⁰

Rise in paddy production: Paddy production in Nepal has surged to an all-time high of 5.23 million tonnes this FY 2016-17; a growth of 22%

as compared to the previous fiscal year when total production stood at 4.3 million tonnes. Such growth has been attributed to favourable monsoons, increased plantation area and productivity. According to the Ministry of Agriculture Department, the productivity of paddy has increased to approximately 3,300 kg per hectare compared to 2,900 kg per hectare recorded in previous years; due to usage of highly improved

seeds. As shown in Figure 11, the previous highest paddy production was in FY 2011-12, which was 5.07 million tonnes. In FY 2015-16, paddy production managed to reach 4.3 million metric tonnes despite the border blockade; that resulted in supply crunch of seeds and fertilizers and subsequent fuel crisis. As a result, the increasing trend in paddy production is expected to result in a decreased import of rice.

Figure 11: Paddy production volumes and percentage change in production over seven consecutive fiscal years



Source: Ministry of Agriculture Development

Government requests India to supply fertilizer: The Government of Nepal has requested India's Ministry of External Affairs to provide 30,000 tonnes of urea to prevent a possible shortage of farm input for winter crops. Urea is mostly used for winter crops such as vegetables, wheat, maize and spring paddy (Chaite Dhan). The annual demand for fertilizer is 700,000 tonnes, out of which demand of fertilizer for the winter crop is 90,000 tonnes. Currently, the Agriculture Input Company, a government entity responsible for sales and distribution, has 6,000 tonnes urea in stock. As per the Nepal-India treaty signed in 2009, India has to sell 100,000 tonnes of chemical fertilizers to Nepal annually at the international parity price.²¹

Yield-based insurance scheme for spring paddy: The Insurance Board has introduced a new policy for spring paddy (Chaite Dhaan) under which policyholders can seek compensation based on the project yield. This is the second agriculture related insurance product that covers the risk based on anticipated yield, enabling policyholders to demand for compensation if actual harvest fails to meet the yields projected at the time of purchasing the insurance scheme.

This scheme will be issued only to the groups of cultivators based on information made available by the district agricultural development offices. Spring paddy is planted in 35 districts in between mid-March and mid-April. However it is not common as it requires better irrigation facilities.²²

Rise in rice imports hits mill industry of eastern region: A large number of rice mills in the Eastern Terai region of the country have closed down while the rest have transformed into packaging plants importing rice from India and selling them under different brand names. Industrialists are opting for this modality as the custom price for importing paddy is higher (8%) than that of rice (5%), making the import of rice more beneficial than paddy. In the Mechi and Koshi Zone, there are more than 100 rice mills of which majority are involved in packaging rice under different brands. As per Mechi customs office, in the last fiscal year, rice imports amounted to NPR 463.36 million (USD 4.26 million) while the import of paddy amounted to NPR 105.77 million (USD 0.91 million). However, in the first five month of this fiscal year, the import of rice from Mechi customs

has already been recorded at NPR 463.32 million.²³

Poultry owners hit hard due to foreign investment: Poultry entrepreneurs in Chitwan; especially small investors, are facing existential crisis due to increasing foreign investment in the poultry sector. Lately, various investors from India and China have invested in poultry and feed industries in collaboration with Nepali business people. Currently, there are two feed manufacturing companies in Chitwan, established with Chinese and Indian Investment, while an additional company is being constructed with Chinese investment. These companies are well-equipped and technologically sound making it difficult for local firms to compete. As per the chairperson of Poultry Entrepreneurs' Forum, Government of Nepal has offered subsidies for foreign investors that have created uneven competition between Nepali Investors and Foreign investors. Accordingly, Nepali Investors are of the opinion that foreign investment should be banned in the poultry sector so as to create an investment friendly environment to encourage Nepali entrepreneurs.²⁴

OUTLOOK

The sector is showcasing various positive developments with continuous efforts by the government to increase agriculture production in the country. This is a positive indication of the governments' commitment to achieve self-sufficiency in agri-produce. The government should put concentrated efforts on delivery of programs ideated by them regarding irrigation facilities, agricultural mechanization, timely supply of improved seeds etc. suitable according to the various terrain of the country.

ENERGY

The past couple of months have seen Kathmandu Valley relatively load shedding free. With completion of the Khimti-Dhalkebar Transmission Line, Nepal Electricity Authority (NEA) expects to continue this trend with much greater ease. The current onset of the dry season though has led to an increase in energy imports. Furthermore, crackdowns on corrupt NEA officials and announcement of competitive Power Purchase rates have cast a sense of optimism in the hydropower sector. Meanwhile, Independent Power Producers (IPP's) continue to perform efficiently and are set to be a larger power generator than the NEA by the end of the year.

Electricity imports increase by 23%:

Electricity imports increased by 23%, to 785 million units, over the first six months of FY 2016-17. Energy imports had stood at 636 million units in the corresponding period of the last fiscal year. While energy imports increased, NEA's import bill only grew by 12% as they prioritized cheaper energy imports through the Dhalkebar-Muzaffarpur Transmission Line. The cost of energy imports through this line stands at NPR 5.76 per unit (USD 0.05). NEA has stated that energy imports will be unavoidable until domestic production can satisfy demand. NEA however, expects energy imports to decrease once the wet season starts as run-of-river (ROR) projects will then be able to work at a higher capacity.²⁵

NEA to save NPR 1 billion a year by curbing power leakages:

NEA has managed to cut down electricity leakages by 2%, and by doing so has reduced its financial losses by NPR 1 billion (USD 9.2 million).²⁶ NEA stated that leakages went from 25.78% of total electricity supply in July 2016 to 23.78% at the start

of January 2017. The major causes of leakages are theft and loss during transmission and distribution. The reductions in leakages are a result of a strict crackdown on NEA staff members who were accused of electricity theft and the recent completion of the Khimti-Dhalkebar Transmission Line.

As of January 22, 2017, NEA with the assistance of Nepal Police arrested 16 people including a NEA supervisor on electricity theft charges.²⁷ Others arrested include businessmen and industrialists who colluded with NEA staff members to conduct electricity theft. NEA Managing Director Kulman Ghising stated that NEA would push ahead with reducing leakages and plans to reduce leakages by 3.5% by the end of the current fiscal year. By doing so he expects to save NPR 1.75 billion (USD 16 million) for NEA.

LPG prices on the rise: The Nepal Oil Corporation (NOC) has increased the cost of Liquefied Petroleum Gas (LPG) by NPR 25 (USD 0.23) per cylinder as of February 1, 2017.²⁸

With this price revision, a cylinder of cooking gas will now cost NPR 1,350 (USD 12.4) in the country, except in the Western region where it will cost NPR 1330 (USD 12.2). NOC in its formal statement has stated that it has been compelled to increase prices due to price revisions by the Indian Oil Corporation (IOC). IOC has increased LPG prices by NPR 102 (USD 0.94) per cylinder, forcing NOC to revise its own price in the process.

NEA plans power tariff hike on industrial sector:

The Nepal Electricity Authority (NEA) is seeking a hike in tariff rates for electricity supplied to the industrial sector in order to curb the growing disparity in purchasing and selling rates. Currently, the average rate for consumers in the industrial sector is NPR 9.66 per unit (USD 0.088), while the cost of supplying electricity stands at NPR 12.13 per unit (USD 0.112).²⁹ The loss of NPR 2.47 per unit (USD 0.0227) has thereby worsened NEA's precarious financial situation. The proposed tariff hikes have drawn considerable criticism

from the industrial sector as the hike will make it even more difficult to compete with Indian and Chinese goods. As such the private sector has urged the NEA to adjust power tariffs so that high load industries are encouraged to operate at night when the demand for power is low.³⁰

India agrees to trade electricity through its territory: India has agreed to permit electricity trade through its region, allowing Nepal to export surplus energy to Bangladesh, according to Bangladeshi State Minister for Energy and Power, Naisrul Hamid. Furthermore, Bangladesh has also shown renewed interest in investing in the hydropower sector of Nepal, with their most recent admission coming during the 9th South Asian Economic Summit in October 2016.³¹ During the course of the event the two countries signed an agreement to construct two hydropower projects capable of generating 1,600 MW. The proposed projects are the 1,110 MW Sunkoshi II

and 536 MW Sunkoshi III located on the Sunkoshi River in central Nepal. As per the agreement, the electricity generated by the two hydro projects will be exported to Bangladesh via India through the Bangladesh Bhutan India Nepal Initiative (BBIN).

Khimti-Dhalkebar transmission line completed: Khimti-Dhalkebar Transmission Line has begun commercial electricity transmission from 19 January 2017. Construction of the 220 kV transmission line started in 2003; scheduled to be completed in 2009, but was stalled following disputes on land Baacquisition and compensation.³² The project was finally completed with the help of a NPR 1.15 billion (USD 10.6 million) grant from the World Bank. The completion of the project is expected to ease electricity supply to Kathmandu and Pokhara. The double-circuit transmission line is expected to supply 700 MW and extends to about 73 km. It also enables Nepal Electricity Authority (NEA)

to import additional electricity from India, if the need arises.³³

MoE announces new purchase rates for hydropower projects: The Ministry of Energy (MoE) has proposed new Power Purchase Rates (PPR's) for dry and wet seasons for different types of hydropower projects as a part of the National Energy Crisis Reduction and Electricity Development Decade plan. Rates vary according to whether the project is a reservoir or run-of-river (ROR) based. According to MoE, a reservoir project can sell electricity per unit at NPR 12.44 (USD 0.114) during dry seasons and at NPR 7.10 (USD 0.06) during wet seasons. Likewise, ROR projects will be able to sell electricity per unit at NPR 10.55 (USD 0.097) in dry seasons and at NPR 4.80 (USD 0.044) in the wet seasons. MoE has stated that higher rates have been proposed in order to attract more foreign investment into the sector.³⁴ Meanwhile the rates will also be raised by 3% annually for a span of eight years.

IPP'S SET TO SURPASS NEA IN POWER GENERATION

Independent Power Producers (IPP's) are set to surpass NEA in terms of total power generation by the end of 2017. Currently, Nepal has a total installed capacity of 960 MW to which NEA contributes 530 MW and IPP's contribute 430 MW. IPP's are set to complete six hydropower projects, as shown in Table 3, with a total capacity of 200 MW by the end of 2017 to bring their total generation to 630 MW. NEA on the other hand has two projects; 30 MW Chameliya and 14 MW Kulekhani III in the pipeline. With the addition of these projects, total generation of NEA is set to increase to 574 MW.³⁵

The main reason behind IPP's surpassing NEA in terms of power generation is the efficiency of IPP's in finishing projects on time to avoid adverse cost effects which directly hamper profits. On the other hand, NEA projects face lengthy delays and are hampered by bureaucratic hurdles.

While increased power generation is boon for the country, the current situation is likely to further increase scrutiny on NEA; which has been plagued by financial problems in the past decade. Recent calls for reforming the NEA have yet to be implemented. Meanwhile the World Bank has suggested that massive reforms are needed in NEA if Nepal is to realize its goal of generating 1000 MW hydroelectricity in 10 years.³⁶

Table 3: Hydropower projects to be completed by IPP's by end of 2017

Hydropower Project	Capacity
Khani Khola 1	40 MW
Dordi Khola	27 MW
Kabeli B1	25 MW
Upper Dordi A	25 MW
Chaku A	22 MW
Sikles	10 MW

Source: *The Himalayan Times*

“ OUTLOOK

The country has taken massive steps forward in terms of hydropower development over the past quarter. The completion of the Khimti-Dhalkebar Transmission Line will further add impetus to keep Kathmandu Valley and Pokhara load shedding free with Birgunj next in line to be load shedding free. Energy imports are expected to continue rising till the arrival of the wet season during the month of June. With IPP's generating electricity at a faster rate than NEA, calls for reforming NEA have gained more ground. Furthermore, while NEA has improved its performance since the change in management, massive reforms and changes are still required within the NEA to pull it out of decades of underperformance.

INFRASTRUCTURE

The Infrastructure sector is one of the major driving agents of the Nepali economy with the government announcing various infrastructure projects as national priority projects over the past several budgets. However, implementation of such infrastructure projects has been a major issue due to continuous political interferences and instable governments.

SPV for construction of fast track expressway:

The committee formed for recommending modalities for construction of the NPR 108.81 billion (USD 1 billion) 76 km Kathmandu-Terai expressway has been submitted to the Prime Minister's Office. The report recommends setting up of a Special Purpose Vehicle (SPV) to build the project. Other recommendations include the purchase of the detailed project report (DPR) carried out by a consortium comprising of Infrastructure Leasing and Financial Services Transportation Networks, Infrastructure Leasing and Financial Engineering and Construction and Suryavir Infrastructure Construction. The report is scheduled to be presented before the cabinet; to choose the most appropriate type of SPV. The SPV set up for the purpose could be a company, a development committee or an authority.³⁷

Protest against Mid-Hill highway plan:

Locals of Myanglung, Tehrathum district have demanded that the plan to open the 1 km track through Myanglung Bus Park to Jirikhimti and onwards to Halimela road be re-routed. Residents claim the current route could leave 200 families homeless.³⁸ The Mid-Hill highway which began from Panchthar's Chiyobhanjyang has now reached close to Myanglung.

Obstruction in expansion of major road section in the Valley:

As per the Kathmandu Valley Development Authority (KVDA) more than 200 km of roads still remains to be widened within the valley. The delay in expansion is attributed to the strong protests and cases that have been filed against the road expansion campaign. It is estimated that only 25% of road expansion has been completed till date; and with the current obstructions the expansion project is not likely to be completed even within the next five years.³⁹

Mobilization of army to open road track linking to China:

The Government of Nepal (GoN) has decided to mobilize the army for building the 120 km road from Hawa Danda (Lapu VDC) to Sama Gaun in Gorkha district. Currently about a 60 km road stretch from Benighat to Hawa Danda has been completed.⁴⁰

Vehicle Fitness Test Center to come into operation:

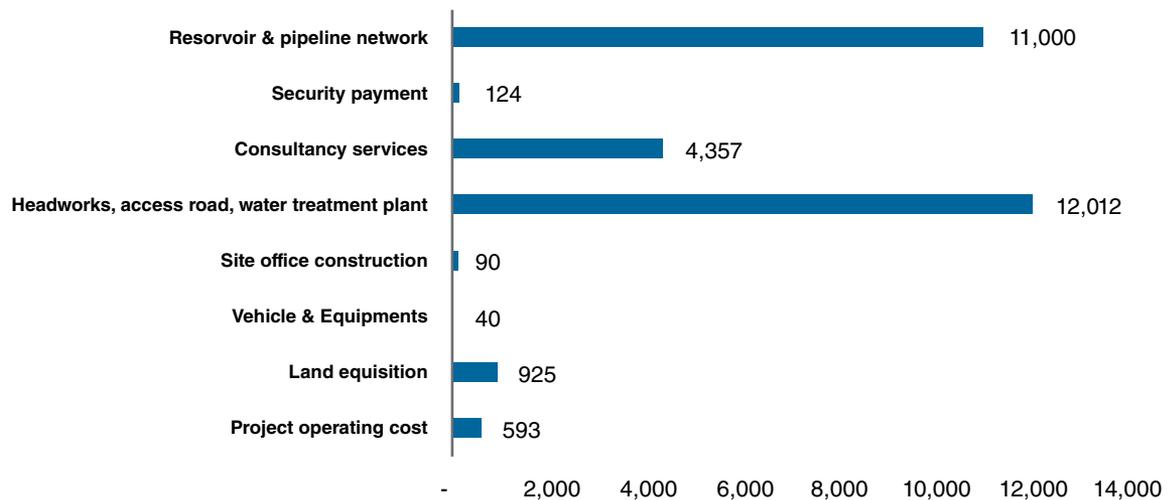
The NPR 60 million (USD 551,420) worth Vehicle Fitness Test Center (VFTC) is expected to come into operation by mid-April this year.⁴¹ The VFTC was constructed in 2012 but failed to come into operation due to lack of coordination among different government agencies on fixing standards for vehicle tests and checking.

Possible delay in Melamchi water supply:

Considering the pace of tunnel excavation, installation of distribution networks, and other construction work it will most likely be difficult for the Melamchi Water Supply Development Board (MWSDB) to meet its October 2017 deadline.⁴² Currently, 4.5 km of tunnel is yet to be excavated which must be completed by July; to meet its October 2017 deadline. At the current pace of excavation it is impossible to complete excavation by July 2017. Once completed, the project will supply 510 million liters of water per day to the Kathmandu Valley. The amount spent in Melamchi water project until December 2016 amounts to NPR 29 billion (USD 266.5 million). The cost break up is shown in below.

On-going construction of Jayanagar-Janakpur-Bardibas railway:

The NPR 8.77 billion⁴³ (USD 80.5 million) Jayanagar-Janakpur- Bardibas rail project is being constructed in three phases. The first phase of the project (29 km Jayanagar – Janakpur) is expected to be completed by November 2017. The second phase includes the 22 km railway between Janakpur and Bijalpur, while the 20 km Bijalpur – Bardibas railway constitutes the third phase. Although construction work for the first and second phase is moving ahead the contract for the third phase is yet to be signed.

Figure 12: Melamchi Water Supply Project Cost (In NPR millions)


Source: Ministry of Agriculture Development

OUTLOOK

A major challenge for constructing mega size projects is the allocation of such projects to a qualified contractor; as A-class contractors in Nepal lack the financial and technical experience of undertaking large size projects. As such there will be a need to hire international contractors to fill the experience void as larger projects come through. Mega projects demand high financial resources; therefore besides fiscal budget allocations the government should also employ instruments such as development bonds and promote policies attractive for foreign investment.

The road expansion plan which began in 2011 has moved at a snail's pace mainly due to local protests and inefficiency of government agencies. While the road expansion is a means to solve the valleys congestion and bring in a new era of development in the valley; in the quest of development certain cultural landscapes of the valley have been destroyed.

There are no substitutes for infrastructure development and there are no shortcuts for faster economic growth. Unless Nepal prioritizes and invests in all elements of infrastructure development, growth in this sector will continue to be slow.

INFORMATION AND COMMUNICATION TECHNOLOGY

In the review period, the ICT sector of Nepal has witnessed some major developments such as the introduction of 4G mobile services in Kathmandu and Pokhara by Nepal Telecom (NT). As such 4G services are now available to both prepaid as well as postpaid users. According to NT, 400,000 subscribers have switched to the 4G network. Besides NT, Ncell has also sought permission to deliver 4G services to its users. The user base is likely to increase substantially in the near future as the service will soon be made available in other areas of Nepal as well.

NT to collaborate with China Telecom to provide IP service in Nepal:

An agreement has been signed between China Telecom Global (CTG) and Nepal Telecom (NT) to provide Internet Protocol (IP) service in Nepal with Terrestrial Cable Route (TCR); connecting Nepal and China via Jilong (Rasuwa) gateway. This agreement provides additional connectivity to Nepal, whereas this route can also be used as a transit hub for the country to connect worldwide.⁴⁴

NTA considering issuing genuine IMEI numbers for fake mobile phones:

In order to control the grey market, Nepal Telecommunications Authority (NTA) is planning to issue genuine International Mobile Equipment Identity (IMEI) numbers to fake handsets to ensure that all mobile sets sold in the market is registered. In order to issue IMEI numbers to mobile phones, the regulator of the telecommunications sector is yet to collaborate with the authorized international firms. The new IMEI numbers for mobile sets can only be issued by four firms

from India, United Kingdom, United States of America and China. NTA plans to use SMS and NTA website to help mobile phone users to check if their IMEI numbers are fake or genuine. More than six million units of mobile phones have got their IMEI numbers registered at NTA after it was made mandatory for importers to register the IMEI numbers of mobile phones.⁴⁵

NTA calls for proposals for launching satellite:

Nepal Telecommunication Authority (NTA) had called for proposals to launch a satellite in the orbital position allocated to Nepal by the International Telecommunication Union (ITU). A total of 20 proposals have been received from countries like United States, India, China, Singapore, Thailand, Canada, France, Japan, South Korea, Saudi Arabia, Russia and Israel. A committee will be formed to shortlist six companies, and detailed proposals regarding financial and management plans will be provided by the shortlisted companies. Following this the Ministry of Information and Communication will forward this

list of proposals to the Cabinet to select one company. After its launch, the Ministry is also coming up with guidelines to make it compulsory for telecommunication service providers, radios and televisions to use the satellite services.⁴⁶

4G mobile services launched:

Nepal Telecom (NT) launched the fourth generation (4G) mobile service in Kathmandu and Pokhara on January 01, 2017.⁴⁷ In order to operate the 4G network, NT upgraded its 308 Base Transceivers Stations (BTS) in Kathmandu and 25 stations in Pokhara. Currently, 4G users can use data up to the speed of 32.4 Mbps which will eventually be upgraded to 100 Mbps.⁴⁸ This service was available to prepaid users from February 04, 2017.⁴⁹ In addition, NT has now signed an agreement with Apple to enable its users to use 4G services by introducing a beta version.⁵⁰ According to NT, since the launch of 4G services in January 01, 4G network has been subscribed by 90,000 postpaid users and 310,000 prepaid users.⁵¹

Online mobile application for taxis to be launched:

Nepal Meter Taxi Association (NMTA) has taken permission from the Department of Transport Management to launch online mobile application for taxis. With this application, passengers will be able to hire taxis that are within two kilometres from their location; which will be tracked through Global Positioning System. These taxis will be rated from one to five. The app allows passengers to determine the distance travelled as well as the fare. Therefore, once this app is launched, taxi drivers will not be able to overcharge passengers.⁵²

Telecom service providers required to take permission from NTA to change share structure:

In order to effectively regulate the telecommunication industry of Nepal, the High-level Monitoring Committee formed under the Telecommunication Policy, 2004 has decided that telecom companies will now have to take permission from Nepal Telecommunications Authority (NTA) before making any changes in the share structure. Until now, telecom companies were able to make changes in the share structure after fulfilling the legal requirements of Department of Industry (DoI) and the Office of Company Registrar (OCR) without

having to inform the regulatory body. NTA is now looking forward to make necessary amendments in the telecommunication policies to implement this decision of the government.⁵³

Ncell overtakes NT in terms of active SIM users and revenue:

According to Nepal Telecommunications Authority (NTA) data, Ncell has almost 4 million more active SIM (Subscriber Identity Module) users compared to Nepal Telecom (NT). As of date, 15.7 million SIM cards has been distributed by NT while only 14.9 million SIM cards has been distributed by Ncell. However, Ncell has more number of active callers even though it has distributed less SIM cards compared to NT. In the last fiscal year, NT was able to generate revenue of only NPR 40 billion (USD 367 million) using frequencies under different bandwidths. On the other hand, even though the government has assigned limited frequency to Ncell, it was able to generate a revenue of NPR 56 billion (USD 514 million) in the same year.⁵⁴

MVAS providers to get separate license from NTAs:

With the view to regulate the Mobile Value Added Service (MVAS) sector, an operating license will soon be required from

Nepal Telecommunications Authority (NTA) for MVAS providers in Nepal. Besides the standard voice calls and fax transmissions, MVAS includes all non-core telecommunication services like mobile banking. As of now, these service providers are operating in association with telecom partners. NTA permission is to be taken by telecom operators before allowing MVAS firms to provide their services. In order to make it compulsory for MVAS firms to take operating license from NTA, the telecom sector regulator has prepared a consultation paper on licensing provisions. Once this provision comes into effect, the current MVAS providers have to obtain the license within a year and will be penalized if they fail to do so.⁵⁵

Ncell asked for a roll out plan by NTA before awarding 4G license

4G service license has not been provided to Ncell by NTA for not settling the capital gain tax for the shares it had sold to Malaysian company Axiata last year. In this scenario, NTA has asked Ncell to submit a roll out plan. Ncell is yet to pay capital gain tax of around NPR 23 billion (USD 211 million) from the buyout deal. The Public Accounts Committee (PAC) has given three months' time period to the Ministry of Finance to recover the capital gains tax from Ncell.⁵⁶

“ OUTLOOK

The ICT sector of Nepal seems to be moving in a positive direction with new developments. Besides the launch of 4G service, Nepal Telecom (NT) has been exploring various lines to expand internet service. Therefore, more people will now be getting access to faster internet and internet based services are also expected to increase. Furthermore, NTA is seeking to come up with regulations to make the growth of ICT sector more sustainable. However, the involvement of regulators is justifiable to the extent that it supports growth and innovation in the sector.

REAL ESTATE

The concept of real estate and housing in Nepal; which began in the 1990s with the availability of housing finance from BFIs, has been transforming from owner built systems to organized housing development projects. However, most housing developers are catering only to very high income groups. Options for affordable housing is needed that can meet the demand of low income groups as well.

Increased revenue collection amid increased taxes: Land Revenue Offices (LROs) across the country collected NPR 9.81 billion (USD 90.2 million) in registration fees in the first six months of the FY 2016-17; thereby achieving 70% of their annual revenue collection target of NPR 14 billion (USD 128.7 million).⁵⁷ The increase in revenue collection during the first six months is mainly on account of increased tax on land transactions. The land registration tax in metropolitan cities was increased from 4.5% to 5% while taxes in sub-metropolitan cities were increased from 4% to 4.5%. Likewise, land registration taxes in municipalities and village development committees were increased from 3.5% to 4%.

Banks halt credit to real estate: All 28 commercial banks in the country have decided to halt loans to real estate amidst the liquidity crunch faced by banks.⁵⁸ Meanwhile commercial banks have decided to float loans based on deposit growth; with credit to be extended to the productive sector as defined by the Nepal Rastra Bank.

Lack of credit to real estate sector would mean diminished growth of the sector; which has been recovered from a long slowdown in real estate prices and transactions.

Monitoring of houses under-construction underway: The Kathmandu Metropolitan City (KMC) office is inspecting houses under construction to verify whether they are built as per the building bylaws or not.⁵⁹ The move aims to ensure that ongoing construction projects meet the new building bylaws. Post-earthquake the Ministry of Federal Affairs and Local Development issued basic guidelines on settlement development, urban planning and building construction; which stipulates standards for construction of new buildings.

Strict action by KMC against non-standard houses: The Kathmandu Metropolitan City (KMC) has released the Building Construction Certification Procedure 2016 which provides guidelines for certification of building structures by KMC. As

per the procedure KMC will depute technicians to verify whether the details submitted are authentic before sending documents to the building permit approval department for approval.⁶⁰

Development of satellite city: According to the current year fiscal budget the government plans to build a satellite city near Kathmandu Valley; with the plan likely to be endorsed by the Kathmandu Valley Development Committee by mid-march. As per the plan, in the first phase the government is looking to develop a satellite city on approximately 100,000 ropanis (5087 Hectares) land on the fringes of Kathmandu Valley.⁶¹ The exact location and size of development will be determined by the Detailed Project Report. In the second phase a satellite city will be built in Lalitpur which will be spread across 10,000 ropanis (509 hectares). The Kathmandu Valley Development Authority (KVDA) has already received NPR 160 million (USD 1.5 million) for the Detailed Project Report (DPR) of the first phase.⁶²

“ OUTLOOK

The Nepal housing market has gained momentum, after years of slowdown with a significant growth in the number of property transactions; resulting in a rise in property prices. The growth in the housing market has been driven by falling interest rates and latent demand for housing which was postponed due to earthquake and economic blockade. Interest, as low as 8%, per annum has been the major driver for increasing realty transactions. However with the current liquidity crisis facing the economy, BFI's have stopped disbursing home loans, and as a result housing transactions are now expected to slow down briefly, which in turn will ultimately effect government revenue collection; which currently contributes a significant amount to government revenue through land registration fees, etc.

EDUCATION

Following many public and community schools failing to enrol the desired number of students from local communities in rural and urban areas, the Ministry of Education (MoE) has allowed concerned District Education Offices to merge certain schools. At the government level, efforts are currently underway to enhance the quality of education in public and community schools. Meanwhile, MoE is planning to take the Grade 10 examinations down to the provincial level and hold School Leaving Certificate (SLC) exams at Grade 12 under the Central Examination Board.

Sajha Prakashan also to print textbooks:

Janak Education Materials Center (JEMC); the main publishing authority of textbooks for public schools in Nepal has been able to print only 60% of textbooks required for the next academic session. The Ministry of Education (MoE) has therefore decided to give the responsibility of printing the remaining school textbooks to Sajha Prakashan to ensure that there is no shortage of required textbooks for the coming academic year. As such other private publishers will also be involved, if Sajha Prakashan is unable to manage the task. Meanwhile MoE is also looking to develop a master plan which to adjust textbook prices and print them at the regional level.⁶³

Earthquake struck schools yet to be restored:

Of the 8000 schools destroyed in the 31 earthquake affected districts; only 1049 schools have been completely reconstructed so far. Meanwhile the Ministry of Education (MoE) has limited resources to build only 2807 schools; and as such is facing problems in building the remaining 4,067 schools due to the lack of various resources

such as budget constraints, skilled manpower, reconstruction materials, supervision and monitoring, and coordination among the stakeholders. The Post-Disaster Recovery Framework prepared by the National Reconstruction Authority (NRA) estimates that NPR 180 billion (USD 1.65 billion) will be required to rebuild the schools damaged by the earthquake.⁶⁴

Initiative to boost girls to enrol in schools:

The Department of Education in collaboration with Search for Common Ground, have initiated a project in three Terai district of Dhanusha, Mahottari and Siraha to encourage girls to enrol in schools. The programme will initially be focused in 42 secondary schools and later expand to 60 other schools in the area. The project aims to improve the quality of education and increase management capability of principals and teachers through good social and educational governance methods. A school management committee and parents teachers union will be formed to encourage involvement of the local community and to ensure good governance of schools. The

project will also foresee a policy level expansion through strategic and practical interactions in the districts, to have good educational governance at the central level.⁶⁵

Urgent need for Braille textbooks:

Visually impaired students from the ninth grade are facing difficulty in understanding their lessons due to lack of Braille textbooks. The Ministry of Education (MoE) has not printed Braille textbooks for class nine since the syllabus was changed. Hence this has created discontentment amongst visually impaired students with the oncoming examinations as these students have been grasping their lessons based on what they hear in the class.⁶⁶

No records maintained of students returning from abroad:

Annually, an average of 30,000 No Objection Certificates (NOC) are issued to students by the Ministry of Education (MoE), permitting them to go abroad to complete their higher studies, as shown in Table 4. While the government maintains a record on the outflow of students, it has not maintained any record of students

returning to Nepal after completion of studies; or on activities of students in foreign countries following completion of education. Neither the MoE nor the Ministry of Foreign Affairs (MoFA) have taken any initiative to maintain comprehensive records or developed any policy for retaining students once they have completed their studies. Recently, records of medical students, who are going abroad under government scholarships have been maintained. As per regulation some students return to the country, while the remaining opt for permanent residency status abroad.⁶⁷

Delay in implementation of education regulation: The Ministry of Finance (MoF) has delayed the endorsement of the new educational regulation formulated by the Ministry of Education (MoE). The approval of the regulation by MoF is essential for implementation of the amended Education Act; which aims to restructure the school education system. According to the regulation, all educational institutions will be required to operate schools in two levels - pre-primary to Grade VIII and Grade IX to XII. The regulation

also emphasizes the reconstruction of schools destroyed by the earthquake.⁶⁸

The MoF has estimated a cost of NPR 27 billion (USD 248.1 million) for the implementation of the regulation and will not be able to provide the funding for FY 2016-17. Meanwhile the regulation has also made a provision for temporary teachers to either apply for a permanent position or accept a golden handshake. It is estimated that a cost of NPR 5.5 billion (USD 50.5 million) will be incurred on the golden handshake for around 14,000 temporary teachers and NPR 7 billion (USD 64.33 million) would be spent on around 30,000 female volunteers annually; who would eventually graduate as teachers both at Early Childhood Development classes and the basic education programme. MoF is therefore sceptical about endorsing the new regulation as it would entail an additional financial burden on the national coffers.⁶⁹

Table 4: Total number of students going abroad

Fiscal Year	Number of students
2010/11	11,982
2011/12	10,324
2012/13	16,504
2013/14	28,126
2014/15	30,696
2015/16	32,489

Source: Ministry of Education

OUTLOOK

The Ministry of Finance has set aside USD 241.2 million (NPR 26.25 billion) from the total budget of NPR. 1,048.9 billion (USD 9.63 billion) for FY 2016-17 to improve the educational sector. It is essential that the Government of Nepal prioritizes education both in terms of policy and practice. Meanwhile it is critical that the Department of Education also increases the supply of qualified teachers as well as focus on reforming the curriculum as well as lecture delivery mechanisms. At the same time an initiative should be taken by the private educational system to collaborate with youth and other groups to strengthen the importance of education within local communities.

HEALTH

The health sector of Nepal is plagued by lack of health infrastructure especially in rural areas. The government has come up with various programs to improve this sector by ensuring that every citizen gets access to basic health facilities; however the strategies are yet to be effectively implemented. Meanwhile Kathmandu Valley; where a large segment of the population resides, has been facing severe dust pollution which has become a major issue due to unmanaged road expansion; resulting in a sharp increase in respiratory problems within the valley.

Bill to regulate alcohol consumption

drafted: In order to regulate the supply and consumption of alcoholic drinks, a committee comprising representatives from the Ministry of Home Affairs, Ministry of Finance, Ministry of Commerce, security agencies and other stakeholders has been formed to finalize the draft of National Alcohol Regulation and Control Bill. The bill has been drafted considering the health and social consequences of consuming alcohol to both the drinker as well as the society.⁷⁰ The new liquor law will include various policies such as barring alcoholic drinks in private parties, discouraging pregnant women and people below 21 years of age from purchasing alcohol.⁷¹

National Ambulance Policy drafted:

In order to regulate ambulance service in the country, a National Ambulance Policy has been drafted by the government. The Ambulance Guidelines 2016 drafted by Ministry of Health classifies ambulance service under A, B and C category based on their service capacity and colour codes. Category 'A' ambulances are red coloured state of art ambulances that have major life support equipment

and a medical professional as well. Category B ambulances are yellow coloured advanced ambulances with emergency medical services and other required manpower. Meanwhile NGOs and other charity organizations usually operate the green coloured ambulances. The ambulances will be registered and monitored by a district ambulance coordination committee formed under the leadership of chief district officer.⁷²

Government doctors required to take approval before private practice:

Approval from the Ministry of Health (MoH) is mandatory for government doctors to practice at any private clinics or hospitals by the second week of March. Approvals will need to be taken from the MoH if they are to work before or after duty hours. Government doctors are also not allowed to work in private clinics from 9am to 3pm. In addition, MoH's approval is also required for private health facilities that are to employ any government doctors. These facilities will be subject to strict actions if they do not follow the Ministry's directives.⁷³

Government targets to make Nepal leprosy-free:

The Government of

Nepal (GoN) has set the goal to make the country leprosy-free by 2020. Research shows that 200,000 new leprosy patients are reported yearly worldwide with 3,000 reported from Nepal. Globally, 175,000 leprosy patients are undergoing treatments with 2,500 such patients receiving treatments in Nepal. While there has been a decrease in the number of leprosy patients worldwide, the numbers have not decreased in Nepal since 2010.⁷⁴

Ineffective implementation of health insurance program:

The Ministry of Cooperatives and Poverty Alleviation (MoCPA) has not yet distributed ID cards that distinguishes "too poor", "poor" and "marginalized" category of impoverished people. As per the Social Health Security Program (Operating) Regulations, 2015, under the ongoing health insurance program, an insurance premium fee of NPR 2500 (USD 23) will be waived for people identified as "too poor", 75% premium will be waived for "poor" category and 50% premium will be waived for the "marginalized" category. However, due to failure in issuing the ID cards, the government has not been able

to effectively implement the health insurance program.⁷⁵

Serious health risks to traffic officers in the Kathmandu Valley:

Traffic officers in Kathmandu Valley are facing serious health risks due to the high exposure to dust caused by ongoing road expansion projects and the subsequent increase in pollution levels. As a result traffic officers are exposed to higher risk of respiratory and cardio vascular diseases. Research indicates that traffic officers have higher chances of varicose veins; i.e. swollen, twisted or lengthened due to poor circulation from standing for long hours, and also experience a lot of coughing and eye itching problems. On the other hand, female traffic officers were more likely to have urinary tract infections.⁷⁶

Government hospitals to provide free Pap smear tests:

The Ministry of Health has issued a directive stating that all public hospitals across the country are to provide free Pap smear tests to women. Such tests are done to screen for cervical cancer which is one of the most common types of cancer in women. Women of 35 – 60 years of age should take this test at least once a year.⁷⁷

Increase in respiratory related patients within the valley:

The number of patients suffering from respiratory problems in Kathmandu Valley has increased by more than 20% in recent months. The increase in dust pollution can be attributed to delays in the road expansion project, unorganized digging of roads and ongoing work on the Melamchi Drinking Water Project. People living in areas where road expansion is on-

going; are the ones most affected by dust pollution; while infants, young children and elderly people have been suffering the most.⁷⁸

Free immunization program launched:

Currently, free vaccinations to children have been provided by the government for 11 diseases such as diphtheria, polio, measles, rubella, and Japanese encephalitis. However, almost 13% of the children have not been immunized against any of these diseases. In order to ensure that all the children are immunized, the Children Health Division under the Ministry of Health has started a campaign to provide free vaccination services to all children in the country. The free immunization program aims to promote health of children by preventing them from contracting various diseases and hence reducing the child mortality rate.⁷⁹

MoH mandates registration of health facilities:

The recently amended “Guidelines on Standards of Health Facility Establishment, Operation and Upgradation, 2014” has mandated that all non-government health facilities; and their subordinate bodies, need to be registered with the Ministry of Health (MoH) by the first week of February 2017, with unregistered facilities to be shut down and penalized. Health facilities registered with the Department of Industry (DOI) will also have to register with the MoH. The provision also applies to those facilities that have sought approval but are yet to renew their operating licenses.⁸⁰

Urban Health Promotion Centres to be set up by MoH:

The Ministry of Health (MoH) has been in discussions

with the Kathmandu Metropolitan City and other stakeholders to set up urban health promotion centres at 10 different locations in Kathmandu. The promotion centres will promote public health inspections; comprising of inspection of food, meat and water quality, provide information on non-communicable diseases; adolescent and reproductive health, and provide basic laboratory tests. According to World Health Organization (WHO), by 2050, more than 70% of the population all over the world will be living in urban areas. MoH has come up with such a move since WHO states that these areas are facing triple threats of infectious, non-communicable diseases and violence and injuries.⁸¹

Climate change and diarrhoea epidemic:

Research from the National Health Research Council (NHRC) indicates climate change as one of the major reasons behind the diarrhoea epidemic in Nepal. The study done on the trends of climate change and diarrhoea from the year 2002 to 2014 shows how rising temperatures due to climate change has resulted in the facilitation of pollution of water sources; leading to diarrhoea. The frequency of diarrhoea epidemics has increased by 4.39% in the last 12 years in Nepal.⁸²

Government to implement national strategy to reach the unreached:

In order to strengthen the various components of the health system and achieve universal health coverage of the country, the government has come up with a ‘National Strategy for Reaching the Unreached’. The strategy aims to address inequalities

in access to health services by 2030, with the view of helping people reach health institutes from remote areas. The plan seeks to come up with better emergency transportation services including cycle ambulances. The various groups of people targeted by this strategy comprises of people living in rural areas, the underprivileged, migrant workers, people living in the slums, HIV infected, lesbian, gay, bisexual, transgender and intersex (LGBTI), and female sex workers.⁸³

Liver transplantation service to be available in Nepal: With the endorsement of the Human Organ Transplantation Regulations, 2016, liver transplantations can now be

performed in the country. Nepali doctors were assisted by senior South Korean doctors to perform their first liver transplant on a 41-year-old man at the Human Organ Transplant Centre in Bhaktapur on December 9, 2016. Patients will now be able to access such transplantation services for around NPR 1.5 million (USD 13,785) which would otherwise cost more than NPR 10 million (USD 91,903) in India and other countries.⁸⁴

Introduction of free medical service program: The Government of Nepal (GoN) has come up with a free medical service program in order to ensure that patients - including the elderly, disabled and single women - who cannot afford

medical treatment in private health facilities get access to basic health services. The Ministry of Health has recently decided that 10% free health care services to these economically weak admitted patients need to be provided in all health facilities including private and nursing homes from December 16, 2016. In order to implement this decision, a circular has already been issued to all private medical colleges, hospitals, nursing homes and community hospitals. They will be receiving such facilities upon showing their ID cards to prove their status. According to the MoH an effective monitoring mechanism will be introduced to ensure that all the health facilities have followed this provision.⁸⁵

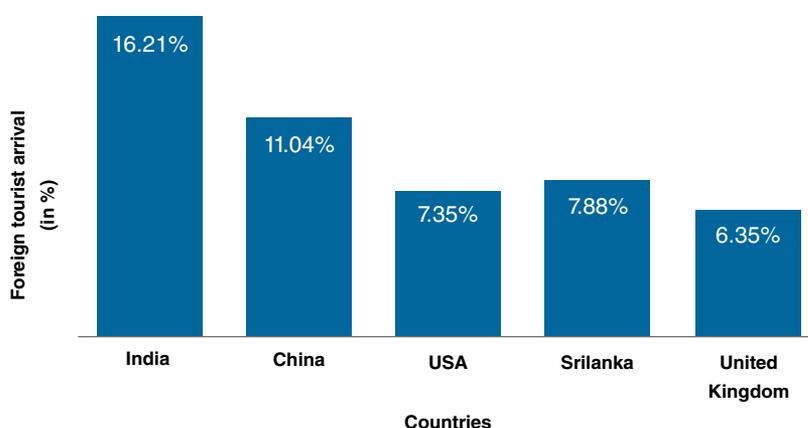
“ OUTLOOK

Despite continued efforts to improve the health sector of the country, very little has actually been translated into action. Although the government has come up with various programs, there have been major issues of delayed implementation. For instance, the government has not been able to effectively implement the health insurance program due to lack of timely issuance of ID cards that distinguishes categories of impoverished people. Therefore, providing basic health facilities to the underprivileged still remains a key problem in the country. In addition, bureaucratic red tape has become a major hindrance in the development of the health sector.

TOURISM

According to the Nepal Tourism Board, foreign tourist inflows to Nepal stand at 729,550 for the year 2016; an increase of 32% from the previous year; with the increase expected to continue in 2017 as well. The highest tourist inflows are from India (16.21%), followed by China (11.04%), United States (7.35%), Sri Lanka (7.88%) and United Kingdom (6.35%) as shown in Figure 13. Meanwhile Nepal; recognizing its potential for religious and adventure tourism is also working towards making Nepal a safe destination and increasing tourist inflows in these areas.

Figure 13: Top 5 Foreign Tourist Arrival in the 2016



Source: Nepal Tourism Board

Trade Unions demand full service charge: The trade unions of - Nepal Tourism and Hotel Labourers Association, Nepal Independent Hotel, Casino & Restaurant Workers' Union, All Nepal Hotel, and Casino and Restaurant Workers' Union - have demanded that employees should get the full service charge amount which hotels and restaurants add to bills. The Unions have filed a joint memorandum to the Hotel Association of Nepal (HAN), Restaurant and Bar Association of Nepal (REBAN) and Fast Food Association Nepal. Currently, the

service charge is divided among the management and employees at 32% and 68% respectively, as per the agreement signed between HAN and the trade unions in 2006. The mandatory service charge system came into force on January 1, 2007. Since then, hotel and restaurant customers have been paying 23% extra tax on the advertised prices, of which 10% is service tax and 13% is value added tax (VAT).⁸⁶

ABC and EBC to get free wifi soon: Nepal Telecommunication Authority (NTA) has planned to set

up free Wi-Fi zones along the trekking trails of Lukla-Everest Base Camp (EBC) and Annapurna Base Camp. This project is in its initial stage and will help promote tourism in these areas. The initiative will also provide easy flow of information during disasters; as these areas are avalanche prone and have seen many incidents where climbers have been trapped on slopes and rescue teams have been unable to reach them. This initiative therefore also ensures that tourist feel safe to trek in the mountains. The service will operate on the Okamura Model, which suggests use of low-cost optical cable for high-speed internet.⁸⁷

Chitwan set to boost tourist inflow: There has been a tremendous increase in tourist inflow at Chitwan National Park (CNP), with more than 63,199 tourists visiting in the first six months of the current FY 2016-17.⁸⁸ With Nepal's tourism sector slowly gathering momentum after the earthquake and blockade, the number of tourist arrivals have doubled in Chitwan compared to the last fiscal year. In order to attract high end tourists and tap into the tourism potential, the Ministry of Forest and Soil Conservation, has also approved

luxury resorts to start operations once again inside the national park. However, hotels will have to meet the present standards to start operations inside the park. A detailed guideline will also be prepared for the hotels to follow, to ensure that the ecology of the park is not disturbed and animal habitation remains protected.⁸⁹ Elephant safari, which is the most popular jungle activity in Chitwan, will be extended to another four buffer zones inside the CNP that includes Batuli Pokhari, Dakshinkali, Nawajyoti and Bandevi community forests. This initiative would also help stimulate job creation as well as involve local communities in wildlife conservation.⁹⁰

Nepal Airlines in first position: Nepal Airlines Corporation (NAC) has bagged the number one position among international passenger carrier in Nepal; by flying 275,701 travellers in the first nine months of 2016. NAC has shown a tremendous growth of 74.63% compared to the same period in 2015, while Qatar Airways has secured the second spot with a percentage growth of 3.69% followed by Air Arabia in the third position with a growth of 24.62%.⁹¹

NAC introduced two new Airbus A320 aircrafts last year serving eight international destinations. NAC is currently planning to buy two wide-body and two narrow-body aircrafts over the next two years, and plans to serve long haul destinations like Australia, Japan, South Korea, Saudi Arabia, Dammam, Colombo, Yangon and London.⁹²

NTB launches “Visit Nepal-Europe 2017” campaign: Nepal Tourism Board (NTB) has launched a ‘Visit Nepal-Europe 2017’ campaign in order to promote Nepal as a tourism destination in Europe. The campaign aims to increase tourist inflow from European countries by 30 to 40% in the current year compared to 2016. It would also provide an impetus for promoting Nepal tourism all over the world for the ‘Visit Nepal Year 2018’. NTB will work in collaboration with Nepali missions in Europe, Nepali diaspora and travel and tour operators in Europe in order to initiate the campaign; and has planned tourism promotion programs in Ireland, United Kingdom, Switzerland, Russia, the Netherlands, Belgium, Spain and Denmark. It has designed various programs under the campaign, such

as talks on mountaineering, photo exhibitions, ‘send a friend to Nepal’ campaign, tourism promotion through Nepali restaurants, Nepal Day, Buddha Jayanti, Everest Day celebrations and training the Nepali diaspora in Europe to promote Nepal Tourism.⁹³

India grants new air space for Nepal: The Government of India has decided to provide additional air routes to Nepal and develop the Trans-Himalaya 2 air route and redefine the Kathmandu-Mahendranagar-Delhi (L626) route as a bi-directional route. Once the Trans-Himalaya 2 air route becomes operational, it would become the shortest air route for the flights to enter the Nepali airspace from the Gulf countries and from South Korea, Japan as well as Hong Kong. India has also decided to approve bi-directional facility for the Lhasa-Kathmandu-Bharatpur-Bhairahawa-Delhi B345 route and the Kathmandu-Jaleswor-Patna G335 route, but so far there is no entry permission through these routes as of yet. These cross border routes will allow better connectivity between India and Nepal, and will also facilitate flights between Pokhara and Bhairahawa which in turn would save cost and time of air travellers.⁹⁴

NEW CIVIL AVIATION BILL SENT TO MINISTRY

Trekking Agencies’ Association of Nepal (TAAN) has allocated approximately NPR 100 million (USD 0.919 million) from the annual budget for FY 2016/17, to maintain and develop infrastructure in the existing trekking trails in the Himalayan region in addition to exploring new trails. The fund will also be utilized to promote Nepal’s trekking routes in the domestic and international markets. TAAN has selected 63 trails; from the Kanchenjunga region in eastern Nepal to Api Himal in the far-west, for maintenance, infrastructure development and promotion. It has also set aside a considerable amount to build the Tourism Memorial Park in Timal, setting up mobile washrooms in tourist bus parks, developing cycling trails, installing solar street lights in Thamel, constructing a bridge over Mardi Khola and implementing the Khaptad Development Programme.

Moreover, NPR 9 million (USD 82,713) has been allocated for exploration of new trekking trails and NPR 8.79 million (USD 80,783) for development of infrastructure, maintenance and promotion of existing trekking trails. TAAN will also be investing on promotion and tourism marketing in the international market and has allocated NPR 2.4 million (USD 22,57) for United States, NPR 3.2 million (USD 29,409) for Russia, NPR 2 million (USD 18,380) for South Asia, and NPR 800,000 (USD 7,352) for Middle East and Australia and NPR 1.2 million (USD 11,028) for Asian markets. It has also set aside NPR 2.4 million (USD 22,056) to organise a cycling competition on the Lukla-Salleri-Patale-Okhaldhunga-Sindhuligadhi-Namobuddha-Dhulikhel route. Furthermore, NPR 1.2 million (USD 11,028) has been reserved to promote Overland Way to Everest (Kavre-Namobuddha-Sindhuli-Sindhuligadi- KhotangHalesi-Okhaldhunga-Siddhicharan Park-Okhaldhunga-Salleri-Surke- Chaurikharka-Everest Base Camp).⁹⁵

“ OUTLOOK

Since 2018 has been identified as the “Visit Nepal 2018 Year”, the government should expedite the process of constructing the new international airport, so that there is easy and more inflow of foreign tourists from long haul hubs. The government should also take initiative to provide loans at low interest rates to the small tourism private entrepreneurs in famous trekking trails, to facilitate better accommodation facilities and services. Meanwhile focus should also be placed on promoting the trans-national Buddhist circuit from India to Nepal, to tap tourists from Southeast Asian nations.

TRADE AND DEBT

The country's import during the first six months of FY 2016-17 increased greatly against a modest growth in export. Heavy dependence on imported goods from both India and China continue to lead to an incline in imports.⁹⁶ Subsequently a widening trade deficit due to a large mismatch between import and export growth rates is likely to affect economic growth.

Foreign trade scenario: Table 5 shows the foreign trade scenario of Nepal for the first six months of FY 2016-17. Merchandise exports improved by 14.8%, with total exports amounting to NPR 36.27 billion (USD 333.33 million) compared to a drop of 27.2% during the same period of the previous fiscal year. Exports to India increased by 17.1%, while exports to China saw a considerable rise of 54.8%. Exports to other countries grew by 10.1%, contributing NPR 14.96 billion (USD 137.48 million) to the country's total exports.

On the other hand, imports have increased substantially by 67.3%, as total imports skyrocketed to NPR 464.61 billion (USD 4.27 billion), compared to NPR 277.79 billion (USD 2.55 billion) in the corresponding time period of the previous year. Imports from both India and China rose considerably compared to a decrease in the previous year; a result of the trade embargo with India. Imports from India more than doubled, increasing by a significant 95% while those from China saw an increment of 34%.

Top imports and exports: Import of vehicles and spare parts from India rose considerably by 217% amounting to NPR 44 billion (USD

Table 6: Foreign Trade Statistics for the FY 2016-17 (in billions)

In NPR billions	2014-15	2015-16 R	2016-17P	Percent Change	
				2015-16 ^R	2016-17 ^P
TOTAL EXPORTS	43.39	31.59	36.27	-27.2	14.8
To India	27.16	17.41	20.39	-35.9	17.1
To China	1.57	0.60	0.93	-61.8	54.8
To Other Countries	14.66	13.58	14.96	-7.3	10.1
TOTAL IMPORTS	374.00	277.79	464.61	-25.7	67.3
From India	236.98	156.79	305.71	-33.8	95.0
From China	53.96	46.20	62.05	-14.4	34.3
From Other Countries	83.06	74.80	96.85	-9.9	29.5
TOTAL TRADE BALANCE	-330.61	-246.20	-428.33	-25.5	74.0
With India	-209.82	-139.38	-285.31	-33.6	104.7
With China	-52.39	-45.60	-61.13	-13.0	34.1
With Other Countries	-68.40	-61.22	-81.89	-10.5	33.8
TOTAL FOREIGN TRADE	417.39	309.38	500.88	-25.9	61.9
With India	264.15	174.20	326.10	-34.1	87.2
With China	55.52	46.79	62.98	-15.7	34.6
With Other Countries	97.72	88.39	111.80	-9.6	26.5

Source: NRB Report- Current Macroeconomic Situation (based on six months data of FY 2016-17)

404 million) in contrast to a decline of 33.8 % during the first six months of the previous fiscal year. Import of petroleum products also saw a huge

rise of 140% amounting to NPR 49.98 billion (USD 459.33 million) compared to a fall of 63.3% during the corresponding time period last

year. Likewise, MS Billet worth of NPR 23.35 billion (USD 214.59 million) was imported from India, registering a significant increase of 234.3% in stark contrast to a 48.2% decrease during the first six months of FY 2015-16. Import of telecommunication components from China recorded a growth of 48.5% while gold imports from other countries registered a small increment of 0.3 % compared to an increment of 514.5% during the same review period last fiscal year.

The export of polyester yarn continued to drop with a decline of 15.6% during the first six months this fiscal year. Cardamom exports amounted to NPR 1.74 billion (USD 15.99 million) registering a decline of 26.7% against a growth of 61.2% during the first six months of the previous fiscal year. Further, the export of readymade garments, zinc sheets, ginger and vegetables also decreased in the first six months of FY 2016-17. In contrast, export of juice amounted to NPR 2.35 billion (USD 21.59 million), registering a significant growth of 181.4%. Likewise, metal and wooden handicraft products - the country's main export to China, increased only by 15.2% compared to a rise of 79.9% during the corresponding period of FY 2015-16.

Trade Deficit: Total trade deficit in the first six months of FY 2016-17 substantially widened by 74% reaching NPR 428.33 billion (USD 3.93 billion) in contrast to a contraction of 25.5% during the same period of the previous fiscal year. Likewise, export-import ratio dropped to 7.8% from 11.4 %. Considerable surge in imports compounded by a sluggish

growth in exports has substantially increased the country's trade deficit.

BOP surplus: The overall Balance of Payments (BOP) registered a surplus of NPR 45.02 billion (USD 413.75 million) at the end of the first six months of FY 2016-17 compared to a surplus of NPR 139.75 billion (USD 1.28 billion) in the same time period of the previous fiscal year. The current account registered a deficit of NPR 1.08 billion (USD 9.9 million) in comparison to the surplus of NPR 157.52 billion during the same review period last year owing to a substantial surge in imports. Continuing the previous trend, BOP surplus despite current account deficit, can be mainly attributed to remittance inflow and grants inflow for earthquake recovery efforts.

DOC implements Export-Import Code: The Department of Customs (DoC) has introduced an Export-Import (ExIm) code for traders with the aim of addressing the under-invoicing of imports and making customs clearance processes more efficient. To be eligible for trade from the next fiscal year, all export and import firms will have to acquire an ExIm code - a government identification number - by the end of this fiscal year. The ExIm code raises the paid-up capital requirement for both importers and exporters to NPR 2 million (USD 18,380) while also making it mandatory for import firms to submit bank guarantee slips of NPR 1 million (USD 9,190).⁹⁷ The implementation of the ExIm code intends to track unregistered importers and traders who are involved in under-invoicing of imports to evade Value Added Tax (VAT) payments.

Further, the use of the code also aims to facilitate digitization of Customs Transit Declaration (CTD) at the Kolkata port and Visakhapatnam port as the DoC prepares for electronic data exchange with Indian customs.

India imposes and then withdraws 4.5% service tax on third-country imports of Nepal: India had levied a 4.5% service charge on the transport of Nepal's third country imports. The Indian government had imposed the service tax on ocean freight of goods which enter Nepal's market via Indian ports - making third-country imports more expensive.⁹⁸ Around 8,000 containers come to Nepal from different countries through the Kolkata Port every month, bringing cooking oil, coal, iron, steel and fertilizers to Nepal's market.⁹⁹ The Nepali government had requested the Indian counterpart to remove the service tax imposed on ocean freight as per the Article 11 of World Trade Organization's (WTO) Trade Facilitation Agreement. Nepal and India as a member of WTO are expected to comply with the agreement which states that traffic in transit shall not be conditioned upon the collection of any fees or charges imposed in respect of transit. Accordingly the Indian government has decided to discontinue the service tax in the case of Nepal.¹⁰⁰

Nepal ratifies Trade Facilitation Agreement: Nepal has submitted a report to the World Trade Organization (WTO) to ratify WTO's Trade Facilitation Agreement (TFA) - becoming the 108th WTO member to do so. The TFA will come into force once two-thirds of WTO members formally approve

the agreement. The agreement endorses provisions for expediting the movement and clearance of goods in transit and establishing measures for effective cooperation between customs and appropriate authorities to enhance trade facilitation. Further, the WTO agreement also contains provisions for technical assistance and capacity building to improve trade mechanisms in developing and least developed countries (LDCs). With the implementation of the TFA, the WTO hopes to support trade in developing and least developed members by reducing trade costs by

an average of 14.3% and the time taken to import and export goods by over a day and a half.¹⁰¹

Reduced bank lending shrink imports and revenues: Imports of luxury automobiles and industrial raw materials have dropped due to tightened bank lending following a reduction in supply of loanable funds. As auto imports are a major source of government revenue, the decrease in imports have caused a drop in revenue collection at the Birgunj Customs Office with revenue collection tallying to NPR

8.42 billion (USD 77.38 million) – which is NPR 650 million (USD 5.97 million) short of the target set for mid-January to mid-February. Further, a decrease in demand for double-cap pickups, auto rickshaws, mini buses, auto accessories and lubricants – due to reduced bank lending – has also impacted government revenue. The Sirsiya Customs Office – one of the main gateways for the import of raw materials for iron and steel industries – has also reported a drop in revenue for the period of mid-January to mid-February.¹⁰²

“ OUTLOOK

The easing out of trade embargo and unrest in Terai region resulted in a sharp rise in imports; as traders sought to recover for the duration that they were not able to import, and meet domestic demand. Persistent imbalances between imports and exports are likely to widen the country's trade deficit. On the positive side, the government-imposed ExIm code is expected to significantly affect trade activities including exports. As trade experts emphasize the importance of diversifying export products and export markets, the TFA could help the country improve its trade capacity, as predicted by the WTO.

FOREIGN AID

In order to finance ongoing development projects, foreign aid commitment has increased by 40% in the first six months of the current FY 2016-17. For instance: in order to support Nepal's post-earthquake reconstruction work, different aid agencies including Asian Development Bank (ADB), World Bank, Government of Japan, and Government of India have pledged to increase the size of available funds to NPR 152.3 billion (USD 1.40 billion). The amount was NPR 108.5 billion (USD 1 billion) during the first six months of FY 2015-16.¹⁰³ However, the impact of aid on long term growth (also referred as aid-growth relationship) remains an interesting topic for future study.

ADB to increase its support to USD 1.2 billion:

The Asian Development Bank (ADB) is increasing its support by 42.12% to NPR 130.57 billion (USD 1.2 billion) in the period of 2017-19. This additional allocation of NPR 38.73 billion (USD 356 million) will be disbursed over a period of three years for projects contributing to regional cooperation, integration and reduction of disaster risks and fragility; subject to the performance of the Government of Nepal (GoN). ADB is also interested in providing financial assistance for the second Melamchi Project thereby extending tunnel to Yangri and Larke rivers. The support is directed towards helping Nepal become a prosperous middle-income country by 2030.¹⁰⁴

Japan offers grant assistance:

The Government of Japan (GoJ) has committed to provide NPR 4.53 billion (USD 41.62 million) to the Government of Nepal (GoN) for the Improvement of Water Supply Project in Pokhara. The project will directly benefit the residents of Pokhara as GoN aims to improve their living

standard by providing clean water supply. At the same time, the project also aims to increase the revenue of Nepal Water Supply Corporation by reducing the water leakages, minimising the unaccounted water ratio and improving the collection of water tariffs.¹⁰⁵ The project will have the capacity to filter 40.2 million litres of water every day, and is expected to reach completion by 2022.¹⁰⁶

Likewise, the GoJ has pledged NPR 5.25 million (USD 0.49 million) for the reconstruction of school buildings in earthquake affected areas of Rasuwa and Nuwakot districts. The buildings will be reconstructed with earthquake-resilient technology. The motive of the project is also to increase awareness and educate people of Rasuwa and Nuwakot districts regarding disaster risk management. In this regard, Shanti Volunteer Association and Community -an international nongovernmental organisation based in Japan- will work with Rural Development Society Nepal (CARDSN) -Nepali partner nongovernmental organisation- to implement the project.¹⁰⁷

Switzerland pledges USD 9.19 million for improving road access:

The Government of Switzerland has agreed to provide financial assistance of NPR 1 billion (USD 9.19 million) to improve road access across the country. The fund will be used by the Government of Nepal (GoN) to accelerate construction of bridges through Phase III of the Motorable Local Road Bridge Programme. The three and half years project starting from March 2017 is expected to benefit four million people across the country through improved access to services, markets and employment.¹⁰⁸

Japan provides support for medical kids and food security:

The Government of Japan (GoJ) has pledged a grant of NPR 1 billion (USD 9.19 million) to the Government of Nepal (GoN) for execution of a project for the Improvement of Medical Equipment at Tribhuvan University Teaching Hospital (TUTH) and the food security programme. As per the agreement, Japan International Cooperation Agency (JICA) will provide NPR 692 million (USD 6.24 million) to TUTH for improvement

of medical equipment, service and education, whereas the GoJ will provide NPR 321 million (2.95 million) to support the government's food security programme.¹⁰⁹

World Bank to support Health Sector Management Reform Program:

In addition to DFID support of NPR 11.98 billion (USD 111 million), the World Bank has also pledged NPR 16.32 billion (USD 150 million) to support the Nepal Health Sector Management Reform Program. The project is expected to run for the period of four and half years starting from January 2017. The fund will be granted to the Government of Nepal (GoN) and the project is expected to improve public resources management system of Nepal with the major focus being on managing development results, health system performance, public expenditure, financial management and procurement.¹¹⁰

Earlier DFID had pledged NPR 11.98 billion (USD 111 million) to support Nepal Health Sector Management Reform Program for four and half

years. The support would be used to restore essential health services in areas affected by the earthquake and improving the quality and governance of health services across the country.¹¹¹

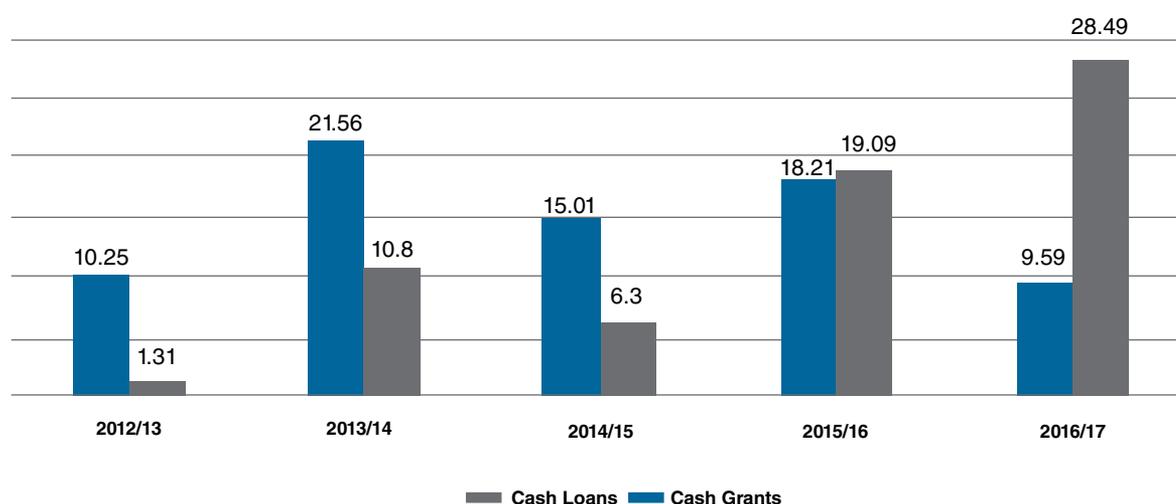
ADB promotes private sector solar power investment:

The Asian Development Bank (ADB) is providing a grant of NPR 2.18 billion (USD 20 million) in order to spur private sector investment in utility scale solar energy sector in Nepal. The fund will be provided to potential bidders having best off-take prices. The project is expected to ensure installation of at least 25 MW of solar power by 2018. The project is based on the concept of 'viability gap' funding; whereby a subsidy will be provided to private investors if there exists a difference in cost of producing the solar power and selling it to Nepal Electricity Authority (NEA). The mentioned approach of 'viability gap' funding will provide financial security to the private investors thereby attracting more private investment and reducing government finances in the energy sector.¹¹²

Overview of foreign cash loan and foreign cash grant:

As shown in Figure 14, foreign cash loans have shown an increasing trend except for FY 2014-15. In fact, foreign cash loans in FY 2016-17 have increased 20.74 times as compared to FY 2012-13 with an annual average growth rate of 233.75% over a period of five years. The size of foreign cash loans have increased in order to finance the development projects; which includes the projects like improving transport connectivity, strengthening social system, and developing infrastructure among many others. In contrary, foreign cash grants have a random trend with an annual average growth rate of 13.49% over a period of FY 2012-13 to FY 2016-17. Meanwhile foreign cash grants decreased marginally by 6.44% in FY 2016-17 as compared to FY 2012-13. The possible reason for decrement in foreign cash grant could be the ineffective mobilization of funds. As such, donor countries including The United Kingdom, Switzerland, Norway and Denmark have even requested a refund on unspent amount.¹¹³

Figure 14: Comparison of Foreign Cash Loans and Foreign Cash Grants in the first six months over the past five years



OUTLOOK

Foreign aid commitment has increased by 40% to NPR 152.3 billion (USD 1.40 billion) in the first six months of the current FY 2016-17. The corresponding amount was NPR 108.5 billion (USD 1 billion) during the first six months of FY 2015-16.¹⁰³ Increasing dependence on foreign aid is likely to affect sustainable economic growth of Nepal as the economy moves away from the notion of endogenous growth; where economic growth is a function of the internal economic system, and not a force that impinges from outside. As such, donor agencies and INGOs will tend to have significant influence in law making process thereby questioning the sovereignty of Nepal. The Government of Nepal (GoN) should therefore focus on industrializing the economy rather than relying on a comprehensive investment packages from donor countries; as such increasing use of foreign aid will only create more dependence and promote corruption.

REMITTANCE

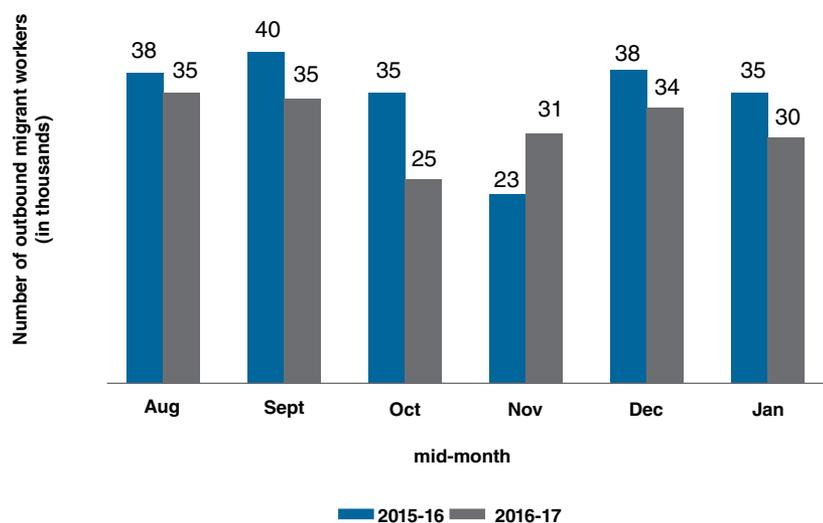
The declining growth trend of remittance inflow since the beginning of 2016 is a matter of concern as it is considered as one of the major reasons behind the liquidity crunch currently plaguing the financial sector in Nepal. There has been prolonged contraction in departure of migrant workers due to economic stress in the destination countries. Amid such situation, various positive developments for the welfare of outbound migrants are being considered such as mandating insurance of migrant workers family and exploring prosperous European countries as potential foreign employment destination.

Continuous decline in remittance growth rate:

Remittance inflow rose by 5.7% to NPR 342.23 billion (USD 3.15 billion) in the first half of FY 2016-17 compared to a growth of 17.3% in the corresponding period of the previous year.¹¹⁴ The fall has been attributed to a decline in the number of outbound workers seeking foreign employment along with demonetization of Indian bank notes.

According to Department of Foreign Employment (DoFE), the number of Nepali workers seeking work abroad in the first six months of FY 2016-17 is 189,433 which is a year-on-year decline of 9.93%. Such a decline can be attributed to the economic slowdown in gulf countries thereby resulting in fewer job opportunities in the gulf region; one of the major destination countries for foreign employment. Furthermore with the Government of Nepal's stricter regulations to safeguard migrant workers; including enforcement of "Free Visa, Free Ticket", manpower companies are now more cautious about sending workers for employment haphazardly.

Figure 15: Comparison of the number of outbound migrant workers in FY 2015-16 and 2016-17



Source: Current Macroeconomic Situation, Nepal Rastra Bank

Nepal top remittance recipient economy:

As per Asian Development Bank's Asian Economic Integration Report 2016, Nepal has topped the chart among the top 10 inward remittance economies in Asia Pacific in 2015; as proportion of Gross Domestic Product (GDP, 31.5%). This has been attributed to a spike in

inflow of remittance to the country post-earthquake, where otherwise countries such as Tonga and Tajikistan were the highest receipt in terms of GDP in 2005 and 2010. The report looked into the top 10 remittance economies in Asia Pacific in 2005, 2010 and 2015 wherein India topped in nominal terms 2015, Tonga topped

in per capital terms and Nepal topped in proportion to GDP terms. The report highlights that on an average, remittance in 2015 accounted for 1% of GDP at USD 271.1 billion in the Asia Pacific region; while South Asia and Central Asia regions are most dependent on remittances.¹¹⁵

Manpower agencies exploring European job market as a potential destination: With Nepali migrant labourers facing job insecurity due to sluggish economic growth in the gulf region; manpower agencies are now exploring new destinations in Europe and Baltic regions. The Ministry of Labour and Employment has recommended Lithuania as a new foreign employment destination for Nepali workers; which will be added as foreign employment destination on approval by the cabinet. European countries to be added to the list of

foreign employment destinations include Netherlands, Turkey, Latvia, Estonia, Ukraine, Portugal and Belarus. Manpower agencies are now exploring more prosperous European countries such as Belgium, Germany, France, Italy and Switzerland. However, European countries could potentially be reluctant in allowing the entry of migrants for fear of overstay and exploitation of the liberal legal rules. Currently, Nepali people are working in 170 countries; out of which 110 countries are permitted by the government while 55 countries are based on migrants working on through individual permissions.¹¹⁶

Insurance policy coverage for migrants' family members: The government is planning to mandate the purchase of insurance coverage of family members of outbound

migrant workers; for migrant workers to be eligible for a work permit. This mandate is likely to come into effect once the Social Health Insurance Act, 2073 is endorsed in Parliament. The policy is expected to benefit dependents of an estimated 3 million migrant workers in various countries (except India) and will also help fulfil the governments' dream to provide insurance coverage to all Nepali people. According to the Ministry of Labour and Employment, discussions with stakeholders are currently underway to set up a mechanism for implementation. This policy will be applicable for both aspiring workers as well as workers already working abroad. As such the Insurance Board has already asked Insurance companies to contact families of outbound migrant workers to cover their families through the payment of an additional amount.¹¹⁷

“ OUTLOOK

Given the declining trend of remittance inflow, significant growth is required in the days ahead; which will otherwise create pressure and disequilibrium on macroeconomic factors of the country such as balance of payment, domestic liquidity and widening trade deficit. As such the government need to devise a clear way forward to respond to exogenous shocks; and mitigate adverse effects, considering the excessive dependency of economy on remittance.



MARKET
REVIEW

FINANCIAL MARKET

Net profit of commercial banks has surged by a whopping 47.3% at the end of the second quarter of the current FY 2016-17 as compared to the same period of the corresponding fiscal year.

Key Indicators

Deposit and credit mobilization

As per the macroeconomic and financial situation report based on the first six months data of FY 2016-17 published by the Nepal Rastra Bank (NRB), deposits at Banks and Financial Institutions (BFIs) increased by 7.2% compared to an increase of 6% in the same period of the previous year. Of the total deposits at BFIs, the share of demand deposits, saving deposits and fixed deposits remained at 8.2%, 42.1% and 32.7% respectively in mid-January 2017. Such shares were 8.6%, 43.8% and 29.2% respectively in the corresponding period of the previous year.

In the review period i.e. in the first six months of FY 2016-17, credit extended to the private sector by BFIs increased by 12.9% compared to an increase of 5.8% in the corresponding quarter of the previous year. Credit mobilization of commercial banks and development banks increased by 14.8% and 6.2% respectively while that of finance companies decreased by 5.2%. Of the total outstanding credit of BFIs, 60.6% is against the collateral of land and building and 14.3% is against the collateral of current assets such as agricultural and non-agricultural products.

Likewise, in terms of credit exposure, the outstanding credit of BFIs to real estate sector stood at 15.1% in

Table 7: Loan portfolio of BFIs in some key areas (In NPR billions)

Type of loan	Mid-Jan 2016	Mid-Jan 2017	% change
Overdraft	259.2	343.1	32.4%
Real Estate and Home Loan	219.0	286.3	30.7%
Hire Purchase	85.1	142.6	67.6%
Margin Nature Loan	27.6	40.8	47.8%

Source: Nepal Rastra Bank

mid-January 2017. Similarly, BFIs' total credit to Small and Medium Enterprises (SMEs) was only 2.7% of the total credit exposure. Similarly, as per NRB's policy-provision which requires commercial banks to disburse 20% of their total credit to designated productive sectors, as of mid-January 2017; the exposure of commercial banks stood at 15.9% i.e. NPR 254 billion (USD 2.33 billion).

Liquidity Management

In the review period, NRB used various instruments to inject liquidity in the banking system. NRB injected liquidity of NPR 15.40 billion (USD 142 million) through repo auction while it further injected net liquidity of NPR 219.35 billion (USD 2.02 billion) through the net purchase of NPR 222 billion (USD 2.04 billion) from the foreign exchange market (commercial banks). In the corresponding period, net liquidity of NPR 234.13 billion (USD 2.15 billion) was injected through the net purchase of USD 2.23 billion.

Likewise, in terms of absorption, NRB mopped up NPR 101.10 (USD

0.93 billion) through open market operations. Under this system, NPR 29.80 billion (USD 0.27 billion) was mopped up through 14 days deposit collection auction under the corridor system, NPR 7.05 billion (USD 64.79 million) under 90 days deposit collection auction and NPR 64.25 billion (USD 0.59 billion) through reverse repo auction on a cumulative basis.

Similarly, NRB also purchased Indian currency (INR) equivalent to NPR 224.30 billion (USD 2.06 billion) through the sale of USD 1.98 billion and Euro 95 million. INR equivalent to NPR 140.99 billion (USD 1,295 million) was purchased through the sale of USD 1.34 billion in the corresponding period of the previous fiscal year.

Foreign Exchange

Gross foreign exchange reserve stood at NPR 1,088.85 billion (USD 10 billion) at the end of the second quarter of FY 2016-17; an increase of 4.8% compared to NPR 1,039.21 billion (USD 9.6 billion) in mid-July 2016. Out of the total foreign

exchange, the reserve held by NRB increased by 4.7% to NPR 928.74 billion (USD 8.53 billion) while reserve held by BFIs increased by 5.2% to NPR 160.11 billion (USD 1.47 billion). The share of INR in total reserves stood at 21.9% as of mid-January 2017.

Based on the imports of the first six months of current fiscal year, foreign exchange holdings of the banking sector is sufficient to cover the prospective merchandise imports of 14.3 months, and merchandise and services imports of 12.4 months. The ratio of foreign currency reserve-to-GDP, reserve-to-imports and reserve-to-M2 stood at 48.5%, 103.5% and 44.9% respectively as at mid-January 2017.

Interest Rates

Taking into consideration the weighted average, the 91-day Treasury bill rate increased to 1.74% in the review period from 0.68% a year ago. Likewise, inter-bank transaction rate among commercial banks increased to 2.71% from 0.26% in the previous year, and inter-bank rate among other financial institutions increased to 5.53% from 1.21% in the previous year. Meanwhile, interest rate spread between deposit and lending rate of commercial banks decreased to 5.33% in the review period compared to 5.97 in the previous year. The average base rate of commercial banks increased to 7.1 % from 6.82% a year ago.

Balance of Payments (BOP)

In terms of BOP, the current account fell into a deficit of NPR 1.08 billion (USD 9.90 million) in this quarter from a surplus of NPR 157.52 billion (USD 1.45 billion) in the same period of the previous fiscal year. However, the overall BOP had a surplus of NPR 45.02 billion (USD 413.70 million) in the review period compared to a

surplus of NPR 139.75 billion (USD 1.28 million) in the same period of the previous year. In the review period, Nepal received capital transfer of NPR 7.93 billion (USD 72.87 million) and Foreign Direct Investment (FDI) inflow of NPR 7.39 billion (USD 68 million) compared to transfer of NPR 7.41 billion (USD 68.10 million) and NPR 1.93 billion (USD 17 million) respectively in the same period of the previous year.

Second Quarter Performance Analysis of Commercial Banks

As per the unaudited second quarter financial results of commercial banks as shown in Table 8, the operating profit margin of commercial banks grew by 46.1% and the net profit margin grew by 43.7% compared to the same quarter of the corresponding fiscal year. Amongst all commercial banks, Nepal Bank was able to post the highest net profit of NPR NPR 1.89 billion (USD 17.4 million), followed by Nabil Bank at NPR NPR 1.74 billion (USD 15.9 million), and Nepal Investment Bank at NPR 1.58

billion (USD 14.5 million) at the end of this quarter. During the period, deposit mobilization increased by 25.5% while credit mobilization by commercial banks increased by 39.2%.

The average Non-Performing Loan (NPL) of banks has gone down from 1.9% to 1.5% in the review period compared to the corresponding period. Likewise, the average cost of funds of commercial banks has increased slightly to 3.8% from 3.7% during the review period. Similarly, the average base rate of commercial banks stood at 7.1% at the end of second quarter, the highest being 10.3% of Agriculture Development Bank and the lowest being 4.3% of Nabil Bank.

Key Developments

Mid-year review of Monetary Policy

The central bank came out with a half yearly review of its monetary policy on February 21 which aims to aid the economic growth target set by the government.

Table 9: Key achievements of monetary policy as on Mid-January 2017

	Target/Objectives of Monetary Policy 2016/17	As on Mid-January 2017
1	Containing annual average Consumer Price Index inflation rate to 7.5%	Average inflation rate stood at 5.8 % during the period
2	Domestic credit is projected to grow by 25%	On year over year (y-o-y) basis, total domestic credit increased by 24% in mid-January 2017
3	The growth rate of broad money will be contained within 17%	On y-o-y basis, broad money increased 18.5 % in mid-January 2017
4	Private sector credit is projected to grow by 20% in 2015/16	On y-o-y basis, private sector credit grew 30.9 % in mid-January 2017
5	Maintaining foreign exchange reserve sufficient to cover import of goods and services for at least 8 months	The foreign exchange reserve stood at NPR 1,088 billion (USD 9.99 billion), based on average import rate, the reserve is estimated to cover import of goods for 14.3 months and goods & services for 12.4 months

Source: Nepal Rastra Bank

Some of the key highlights, revisions and provisions outlined by the mid-year review of the monetary policy are as follows:

- BFIs can calculate Credit to Core capital-cum-deposit (CCD) ratio by deducting 50% of loans extended to productive sectors at the end of this fiscal year. As per existing provision, BFIs have to extend 20% of its loan portfolio to the productive sector. This provision will be valid until mid-July 2016.
- BFIs can issue foreign currency-denominated letters of credit for a period of 90 days. Likewise, it has allowed banks to issue trust receipt loans and other similar loans for a period of up to 150 days from the existing 120 days; also effective till mid-July 2017.
- Interest on call deposits should not exceed interest of normal savings deposit.
- To discourage multiple banking loans, those availing credit worth NPR 1 billion (USD 9.19 million) and above from multiple BFIs have to convert into consortium financing. BFIs that are unable to do so will be categorized under the 'watch list'.
- Personal overdraft loans have been reduced by 25% to NPR 7.5 million (USD 0.068 million) from the existing NPR 10 million (USD 0.091 million). Those that have already issued such loans need to reduce to the stipulated level by the end of the current fiscal year.
- Credit extended to borrowers who have submitted different financial statements at different institutions – such as BFIs and revenue offices, should be categorized as 'bad loans'.
- The period for commercial banks to meet the direct deprived sector lending (2%) by the end of this fiscal year has been extended till next fiscal year. As such commercial banks will not be penalized if they are not able to meet the lending criteria by the end of the year.

“ OUTLOOK

The banking sector has got some respite after the central bank made some key revisions via mid-term monetary policy revision. However, the impact of liquidity crunch seen in the banking sector is likely to impact borrowers in the days to come. The interest rates on key loan products have already seen significant changes as BFIs have started to offer interest of up to 12% on its fixed deposit products to attract and retain deposits. The mismatch of funds – largely due to lower deposit growth aided by sluggish remittance growth, swelling trade deficit, lower government spending - amidst aggressive lending by BFIs to 'unproductive sectors' like real estate, stock market and automobiles are some of the primary reasons for the current liquidity crunch in the banking sector. Such situation has brought Credit to Core capital-cum-deposit (CCD ratio) of most BFIs above the limit i.e. 80% outlined by the central bank, thus limiting BFIs' lending capacity and bringing interest rates up on both lending and deposit products.

There is a tendency of tightening liquidity in the banking system at the end of the second quarter of each fiscal year as corporates file first instalment (40%) of their yearly tax liability while banks tend to expedite their lending post key festivals - Dashain and Tihar. Moreover, key participation of investors in primary market instruments such as Further Public Offering (FPO), Initial Public Offering (IPO) and Right shares could be other reasons; as they dry up savings accounts in the banking system, thus adding additional pressure to maintain the CCD ratio.

Since prolonged crisis has the potential to affect numerous sectors and hinder economic growth, the central bank should take pro-active measures rather than a reactive or control oriented regulator. Similarly, it is imperative that banks come out with innovative savings products in advance rather than at the eleventh hour. Moreover, BFIs should start investing in data and research; as the volume of bank businesses increase, which could subsequently jeopardize the whole banking system and evoke systematic risk.

TABLE 8: UNAUDITED 2ND QUARTER RESULTS OF COMMERCIAL BANKS-FY 2016-17 (FIGURES IN NPR TEN MILLION)

Bank	Paid-up Capital	Reserve & Surplus	DEPOSIT			LOANS AND ADVANCES			OPERATING PROFIT			NET PROFIT			NPL (%)			COST OF FUND (LCY)			BASE RATE (%)
			FY 16/17	FY 15/16	% Change	FY 16/17	FY 15/16	% Change	FY 16/17	FY 15/16	% Change	FY 16/17	FY 15/16	% Change	FY 16/17	FY 15/16	% Change	FY 16/17	FY 15/16	% Change	
			2 QTR	2 QTR		2 QTR	2 QTR		2 QTR	2 QTR		2 QTR	2 QTR		2 QTR	2 QTR		2 QTR	2 QTR		
Nabil Bank	618.3	715.7	10,837.2	10,837.2	11.5	9,030.0	6,500.6	38.9	262.8	190.2	38.2	174.7	135.1	29.3	0.9	1.7	1.9	2.4	(0.6)	4.3	
Nepal Investment Bank	870.6	916.6	9,808.1	9,808.1	18.9	9,670.9	7,748.2	24.8	232.4	143.9	61.5	158.4	107.8	46.9	0.7	1.1	3.5	3.2	0.3	5.7	
Standard Chartered Bank	374.9	451.4	5,788.0	5,788.0	7.1	3,510.6	2,577.2	36.2	112.0	87.8	27.6	74.0	61.2	20.9	0.3	0.4	1.3	1.5	(0.2)	4.6	
Himalayan Bank	647.6	400.2	9,109.8	8,113.7	12.3	7,556.7	5,899.7	28.1	160.9	126.1	27.6	102.7	80.2	28.1	0.9	3.2	2.7	2.5	0.3	6.0	
Nepal SBI Bank	388.3	385.2	7,759.9	5,835.9	33.0	5,977.2	4,181.8	42.9	116.4	92.7	25.6	75.8	62.3	21.7	0.1	0.2	2.5	2.7	(0.2)	6.5	
Nepal Bangladesh Bank	401.1	225.2	3,960.3	3,550.1	11.6	3,620.1	2,917.1	24.1	74.0	48.0	54.2	54.0	36.8	46.7	1.0	1.1	4.4	4.5	(0.0)	7.3	
Everest Bank	460.6	487.9	9,043.6	7,604.5	18.9	7,261.8	5,504.0	31.9	148.6	117.3	26.7	97.1	75.3	29.0	0.7	0.7	2.8	2.4	0.4	5.5	
Bank of Kathmandu Lumbini	562.9	267.1	7,000.0	4,181.1	67.4	6,278.8	3,228.6	94.5	86.5	50.0	73.0	60.1	32.9	82.7	1.5	3.9	4.2	4.2	(0.1)	7.1	
NCC Bank	467.9	230.3	5,546.8	2,663.5	108.3	4,842.2	2,172.6	122.9	7.6	23.4	(67.5)	7.7	24.6	(68.7)	1.8	1.3	5.3	4.5	0.7	8.3	
NIC Asia Bank	581.9	264.7	7,907.1	5,831.8	35.6	6,642.2	4,627.1	43.5	76.3	61.5	24.1	72.1	50.2	43.6	0.7	1.4	4.5	4.9	(0.4)	7.4	
Machhapuchhre Bank	466.6	242.3	5,824.0	4,454.2	30.8	5,185.3	3,738.9	38.7	84.9	60.3	40.8	57.5	40.1	43.4	0.4	0.4	3.8	4.2	(0.4)	7.0	
Kumari Bank	269.9	164.3	3,994.6	3,453.1	15.7	3,365.9	2,750.5	22.4	35.9	29.5	21.7	27.9	21.0	32.9	1.1	2.6	4.7	4.7	0.0	8.1	
Laxmi Bank	303.9	362.6	5,555.4	4,110.7	35.1	4,671.0	3,341.3	39.8	48.9	40.4	21.0	40.6	30.3	34.0	1.3	1.1	5.3	4.0	1.2	7.6	
Siddhartha Bank	523.5	247.1	7,493.5	4,863.8	54.1	6,265.9	4,030.0	55.5	87.1	59.4	46.6	72.6	48.7	49.1	1.5	1.4	4.2	4.1	0.1	6.8	
Global IME Bank	715.0	246.1	8,412.6	6,382.5	31.8	7,151.6	5,498.4	30.1	117.6	104.5	12.5	90.6	76.2	18.9	1.6	1.6	4.1	3.1	1.0	7.1	
Citizens Bank International	553.7	191.5	5,274.9	4,003.4	31.8	4,678.2	3,355.6	39.4	68.2	37.0	84.3	63.1	41.8	51.0	1.3	2.4	5.2	4.5	0.8	7.8	
Prime Commercial Bank	494.0	243.7	5,500.6	4,230.6	30.0	4,605.2	3,411.8	35.0	73.4	58.5	25.5	55.9	46.9	19.2	1.4	1.5	4.5	4.5	(0.0)	7.3	
Sunrise Bank	530.1	145.2	5,730.0	3,722.4	53.9	4,922.3	3,108.0	58.4	82.0	40.5	102.5	60.9	36.3	67.8	1.4	2.3	4.6	4.9	(0.3)	7.6	
NMB Bank	543.0	454.4	6,879.7	5,248.8	31.1	5,893.6	4,276.4	37.8	82.0	46.8	75.2	70.1	42.1	66.5	1.9	1.7	4.0	4.3	(0.2)	7.5	
Prabhu Bank	588.1	141.2	7,021.6	4,798.1	46.3	5,652.9	3,179.5	77.8	93.4	31.9	192.8	111.2	40.5	174.6	4.9	5.5	-	-	-	6.4	
Janata Bank Nepal	230.7	33.2	2,556.4	2,313.7	10.5	2,297.8	1,850.2	24.2	15.9	18.4	(13.6)	16.1	13.8	16.7	2.6	1.4	4.6	4.9	(0.4)	8.1	
Mega Bank	401.2	130.7	3,851.7	2,352.7	63.7	3,401.1	2,046.3	66.2	52.7	25.2	109.1	37.0	22.3	65.9	0.7	1.1	4.5	3.9	0.5	8.5	
Civil Bank	458.3	142.8	3,293.4	2,693.1	22.3	2,950.5	2,304.9	28.0	0.02	9.95	(99.8)	16.7	15.6	7.1	4.5	2.1	5.6	5.7	(0.1)	8.8	
Century Commercial Bank	368.9	83.5	3,267.5	2,407.7	35.7	2,901.6	2,084.3	39.2	32.7	23.4	39.7	22.3	16.0	39.4	0.5	0.7	5.4	4.5	0.9	8.2	
Sanima Bank	530.5	141.6	5,179.1	3,909.6	32.5	4,692.1	3,329.0	40.9	95.3	62.7	52.0	62.2	40.8	52.5	0.0	0.1	4.1	4.2	(0.1)	7.0	
Public Sector Banks																					
Nepal Bank	649.9	226.3	8,483.3	8,022.0	5.8	7,081.5	5,513.1	28.4	138.3	64.3	115.1	189.5	104.8	80.8	2.9	3.9	2.0	2.2	(0.2)	6.3	
Rastriya Baniya Bank	858.8	123.4	13,829.6	12,842.3	7.7	9,390.6	7,719.4	21.6	115.5	88.8	30.1	121.7	107.1	13.6	2.8	3.4	1.3	1.9	(0.7)	5.4	
Agriculture Dev. Bank	1,037.4	494.1	8,765.9	8,254.0	6.2	8,705.7	6,757.9	28.8	68.4	26.5	158.1	90.6	38.7	134.1	3.8	5.4	4.8	5.2	(0.3)	10.3	
Total	14,897.6	8,156.3	191,181.9	152,276.6	25.5	58,203.3	113,652.4	39.2	2,569.7	1,769.0	45.3	2,083.1	1,449.4	43.7	1.5	1.9	3.8	3.7	0.1	7.1	

CAPITAL MARKET

The NEPSE index is in a bearish trend with the market already losing 506.87 points since early October 2016; when it was hovering above 1800 points.

Secondary Market Performance

The Nepal Stock Exchange (NEPSE) benchmark index (18.26%) went down by 293.27 points to close at 1313.01 points during the review

period (21 November, 2016 - 26 February, 2017). Total market capitalization stood at NPR 1,478 billion (USD 13.60 billion). As shown in Table 10: Performance of sub-indices, all sub-indices ended

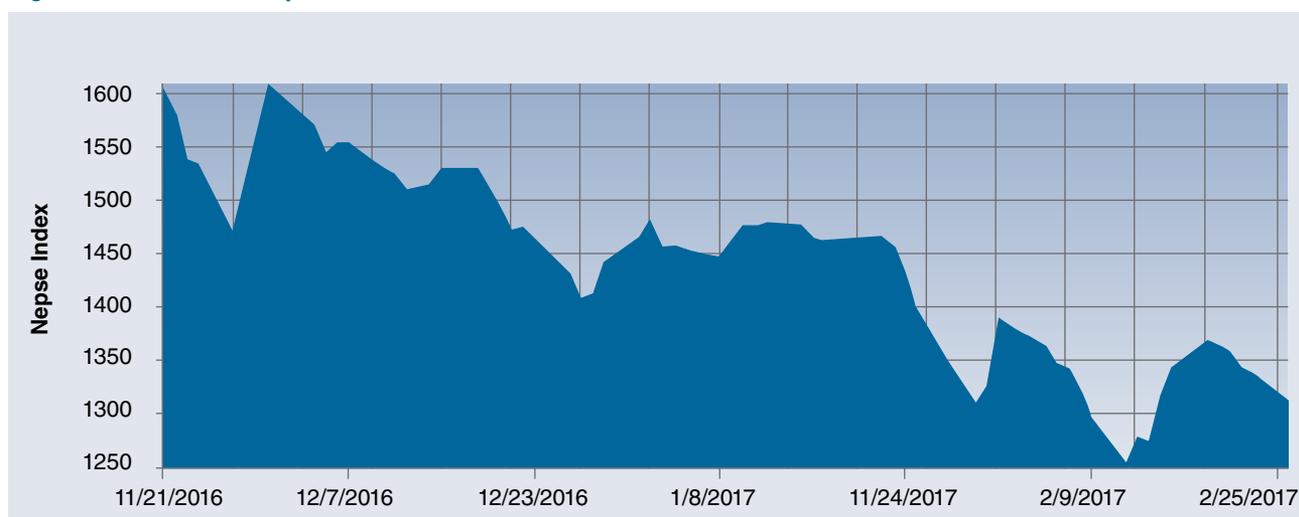
in the red zone. The Insurance sub-index (-30.90%) was the biggest loser; as selling pressure mounted in the market. This was followed by the Hydropower sub-sector (-24.30%) and the Hotel sub-index (-22.12 %).

Table 10: Performance of sub-indices

Indicators	21-Nov-16	26-Feb-17	% change
Nepse Index	1606.28	1313.01	-18.26%
Commercial Bank Index	1499.37	1255.57	-16.28%
Development Bank Index	1667.8	1439.41	-13.69%
Finance Index	778.9	607.45	-22.01%
Insurance Index	8229.93	5686.49	-30.90%
Hydropower Index	2023.24	1531.61	-24.30%
Manufacturing & Processing Index	2242.34	2137.93	-4.65%
Hotel Index	2152.99	1676.69	-22.12%
Others Index	763.24	658.84	-13.68%

Source: NEPSE

Figure 16: NEPSE Index performance



Source: NEPSE

Key developments

Primary Market

During the review period, the primary market witnessed the issuance of one Further Public Offering (FPO) and two Initial Public Offerings (IPO). Nepal Life Insurance Company Ltd. issued FPO worth NPR 4,412.41 million (USD 40.55 million); i.e. 3.09 million equity shares at NPR 1,425 (USD) per share including a premium of NPR 1,325 (USD) per share. The FPO received rating of Grade 3+ from ICRA Nepal, indicating above average fundamentals. The FPO issue received overwhelming response from investors and was oversubscribed by over 12 times; collecting a total of NPR 54.70 billion (USD 502.71 million) from 250,000 investors.

Forward Community Microfinance Ltd. issued IPO worth NPR 60 million (USD 0.50 million) i.e. 600,000 equity shares at NPR 100 per share. The issue received rating of Grade 4+ from ICRA Nepal, indicating below average fundamentals. Likewise, Samata Microfinance Limited floated its primary share worth NPR 9.80 million (USD 90,000 dollars) i.e. 94,800 equity shares at NPR 100 per share. Both primary offerings were oversubscribed by multiple folds.

United Modi Hydropower Ltd. is coming up with IPO worth NPR 17 million (USD 0.15 million), by issuing 1.70 million equity shares at face value of NPR 100 (USD 0.92) each from 2 March, 2017. The issue has received rating of Grade 3+ from

ICRA Nepal, indicating average fundamentals.

Other Developments

Odd lot transaction allowed on a regular trading day

NEPSE has come up with a new regulation allowing small-volume transactions (less than 10 units) on a regular trading day i.e. Sunday to Thursday; which previously used to be traded only on Friday, with an aim to facilitate small investors. However as per NEPSE such transactions will not be taken into account while calculating the index value.

Stock Brokers expanding their services outside Kathmandu Valley

NEPSE is preparing to provide additional Remote Work Station (RWS) available to stockbrokers to open their branches outside Kathmandu Valley. Currently, there are 8 RWS in operation. NEPSE is seeking permission from Securities Board of Nepal's (SEBON's) to allow an additional 41 stockbrokers to conduct transactions from outside the Valley. However, SEBON has asked NEPSE to initiate the process only after considering the risk settlement measures that stockbrokers will adopt after expanding beyond the Valley.¹¹⁸

CDS Regulation and Clearing & Settlement by laws amended

SEBON has amended Central Depository Service (CDS) Regulation, 2073 and Clearing & Settlement Bye Laws, 2073. The amendment has deducted the restriction on trading

by the stock broker to 3 days from previous 7 days. If a broker is unable to do clearing and settlement within prescribed days i.e. T (Transaction) +3 days or if it fails to submit documents as required by SEBON, they will be restricted from trading for three days. Further, the amendment also requires all depository participants' to make arrangement for the Investors to view their account statement online.

Key Directives by SEBON

Some of the key directives issued by SEBON during the review period are as follows:

- Considering the current liquidity situation and the shortage of loanable funds; SEBON has scrapped a rule which required money collected from Initial Public Offerings (IPO) or Further Public Offerings (FPO) to be parked in the Nepal Rastra Bank (NRB) for at least 6 days.
- SEBON has directed Standard Chartered Bank (SCB) to hold its FPO; as it is likely to worsen the ongoing liquidity crunch in the banking system. SCB was set to float 2.5 million shares at NPR 1,290 per (USD 11.85) share from 20th February 2017.
- SEBON has directed all companies, other than Banking and Financial Institutions (BFIs) and Insurance companies, to get approval of their plans and strategies from the company's annual general meeting regarding the implementation of funds raised through issuance of rights shares and FPO.

“ OUTLOOK

In the past few months, a bearish trend has been prevailing in the secondary market, causing a free fall in the NEPSE index. Investors panicked due to margin calls from Bank and Financial Institutions (BFIs) that obliged them to offload their shares; amid the ongoing situation where BFIs are tightening their funds. According to the current macroeconomic and financial report based on first six months data of FY 2016-17 prepared by Nepal Rastra Bank (NRB), BFIs' total margin lending extended against the collateral of shares, stood at NPR 40.08 billion (USD 368.30 million). Moreover, as BFIs are offering attractive interest rates on saving schemes, investors seemed less tempted to invest in this bearish stock market.

Furthermore, despite attractive second quarter results posted by listed companies; especially BFIs at the end of second quarter, the market has not been able to attract investors as Earning Per Share (EPS) of these companies have diluted due to increased paid-up capital of these institutions. BFIs need to meet additional capital requirement as stipulated by the central bank by the end of current FY 2016-17. This has minimized the prospect of receiving stock dividend from next fiscal year and has resulted in mounting selling pressure of these companies. Nonetheless, the index has showcased some improvements lately, as investors have been lured by cheaper stock prices along with the expectation of positive political developments and ease in the banking liquidity.

A large, stylized number '5' is the central graphic element. It is rendered in a light blue color against a darker blue background. The '5' is composed of several overlapping rectangular and circular shapes, giving it a modern, geometric appearance. It occupies the upper two-thirds of the page.

**A SPECIAL ISSUE ON
TOURISM AND HOSPITALITY:
PERSPECTIVES AND PROSPECTS**

A SPECIAL ISSUE ON

TOURISM AND HOSPITALITY: PERSPECTIVES AND PROSPECTS

TRAVEL AND TOURISM: THE BEGINNING

The opening of Nepal to the world in the 1950s heralded the beginning of the tourism and hospitality industry in Nepal with high end travellers coming to Nepal in search of a “*Shangri La*”; closed to the world until then. The end of the World War, a new world order, an independent India and the fall of colonial rule in Asia therefore heralded a new wave of change globally, with greater air connectivity facilitating travel across countries. As such, this gave way to the development of a travel and tourism industry with individuals looking to venture into previously unexplored locations. In Nepal, this culminated in the issuance of Nepal’s first tourist visa to Boris Lissanevitch; a Russian hotelier, who paved the way for tourism in Nepal and opened the country’s first hotel – The Royal Hotel. Shortly after hotels such as the Soaltee Crowne Plaza and Hotel Annapurna were started by the then royal family, marking the onset of luxurious hospitality sector in Nepal.

Shortly after the issuance of tourism visas in Nepal, the first five year plan on tourism was released by the National Planning Council identifying tourism as an important tool for the country’s development. This was followed by the establishment of the Nepal Transportation Department; paving the way for civil aviation, and the Tourism Development Board in 1957 which culminated in the establishment of the Nepal Tourism Board in 1998. In order to promote tourism Nepal subsequently took on memberships in the World Tourism Organization (WTO), and the Pacific Area Travel Association (PATA) in 1963.¹¹⁹ Shortly after, the 70’s saw an influx tourists; mostly backpackers visiting Nepal. However tourist arrivals dropped drastically shortly after following the period of conflict and political turmoil; stemming from the Maoist insurgency against the government.

TOURISM AND HOSPITALITY OVERVIEW

The growth of the tourism and hospitality industry in recent years can be attributed to the end of the decade

long insurgency; following the Maoist party entering mainstream politics, and a moderately stable political environment. This in addition to a rising middle class, increase in international tourist’s arrivals and promotion of tourism friendly policies has contributed to the industry’s growth. The tourism and hospitality industry is an important sector that contributes to foreign exchange reserves of the country. This sector emerges as the largest source of foreign exchange and employment generation within the country, directly contributing NPR 85.3 billion (USD 784 million) to the country’s GDP; comprising 4% of total GDP in 2015. This is projected to grow by 5% per annum from 2016 to 2026 and eventually reach NPR 149.4 billion (USD 1.4 billion) (4.7% of total GDP) by 2026.¹²⁰ Likewise, the travel and tourism sector contributed 426,500 jobs in 2015, which is 3.2% of total employment. This figure is estimated to grow annually by 3.8% by 2026 and create 654,000 jobs directly.⁹

Hotels are foreign exchange earners, employment generators and tax contributors. Therefore, the government needs to support hotels, as they are one of the key contributors to the economy of the country.

*Pralhad R. Kunwar, Chief Operating Officer/
General Manager, Hotel Himalaya*

Meanwhile the hospitality industry forms the backbone of any tourism industry; with airlines and transportation services as key auxiliary function. Nepal today, has moved a long way from the nascent development of the tourism and hospitality industry and is now a multi-billion dollar

industry with many different segments; from high end luxury and heritage hotels to the more common motels, bed and breakfasts, and other lodging businesses. While most people associate the hospitality industry with just hotels, a key segment also comprises of the food and beverage industry including restaurants, fast food chains or any establishments that provide food and beverage; located in either hotels or as standalone restaurants. Likewise the hospitality industry also comprises of travel and tourism businesses that provide a variety of services to their customers. A total number of 1,105 hotels are registered with the Department of Tourism as of mid-December-January 2017, out of which 120 were star category hotels while 985 were non-star hotels.¹²¹

TOURIST ARRIVAL STATISTICS

While tourism arrivals did see some recovery and reached relatively stable levels following the sharp decline during the period of insurgency, the 2015 April earthquake led to another sharp drop in tourism numbers by 31.78% as indicated in Figure 17 below. Meanwhile the 1 million tourist target set since the Visit Nepal Year 1998, 20 years ago, is still an elusive figure.

As per government statistics, during the peak tourist season of October and November 2014, hotels recorded its highest occupancy rates at 73.02% and 86.33% respectively, with average occupancy rate of five star hotels at 61%. However the 2015 earthquake saw a drop in tourists; particularly Indian and European, barring a few Chinese tourists visiting Buddhist sites like Lumbini.

According to the Lumbini Development Trust, total visitor numbers in Lumbini has gone up by 71.81% to reach 1.28 million in the year 2016. Foreign visitor numbers stood at 136, 253 with an increase of 5.48% compared to 2015, whereas Indian visitors were the highest at 134,269, up 3.08% compared to 2015. Average occupancy rates of hotels post April 2015 earthquake was 30-35% dropping down to under 20% after the Terai unrest, economic embargo and subsequent fuel crisis, with the tourism and hospitality sector hit the hardest during this time; particularly five star hotels that have relatively high operating costs.¹²² However, occupancy rates of hotels have now gradually increased from the average occupancy rate of 35% in 2015 to around 65% in the year 2016.¹²³

CONTRIBUTION TO GDP

When considering the contribution to GDP, hotel and restaurants have contributed approximately 2%¹²⁴ of the total GDP annually during the last three years from FY 2013-14 to FY 2015-16. As can be seen in Figure 18, the hotels and restaurants business picked up in 2016 compared to 2015. Deluxe, 5 star, heritage and budget hotels are doing well, while Meetings, Incentives, Conferences, and Events (MICE) and Food and Beverage (F&B) sectors have been the biggest revenue contributors to hotels. Meanwhile there has also been increased average spending per visitor per day, which witnessed an increase of USD 28.6 (NPR 3112) from USD 39.9 (NPR 4342) in 2010 to USD 68.5 (NPR 7453) in 2015 thereby driving up the revenue of hotels.¹²⁵

Figure 17: Total tourist arrivals - land and air - from 2010 to 2016

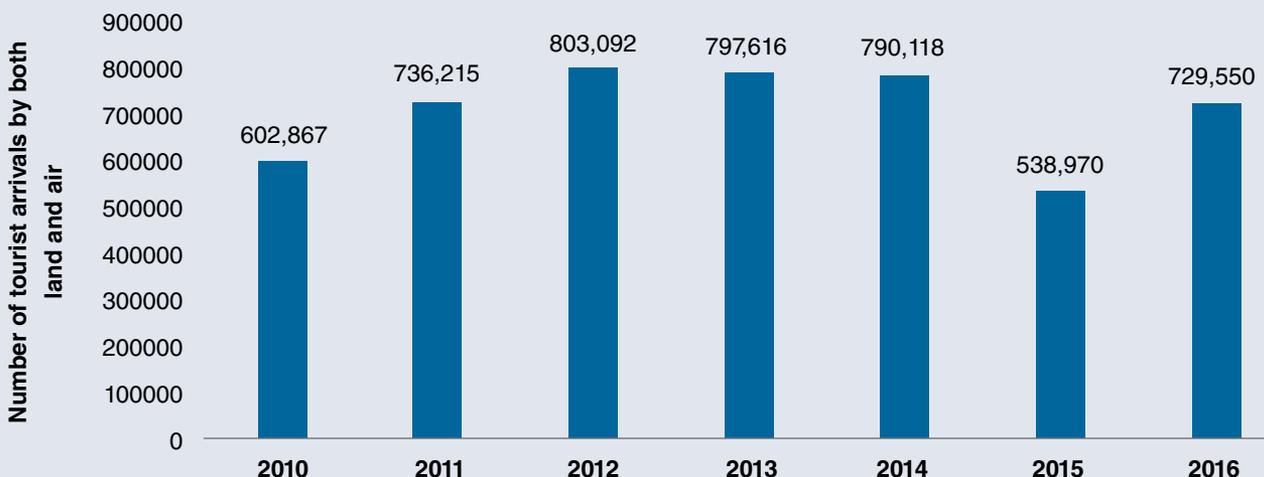
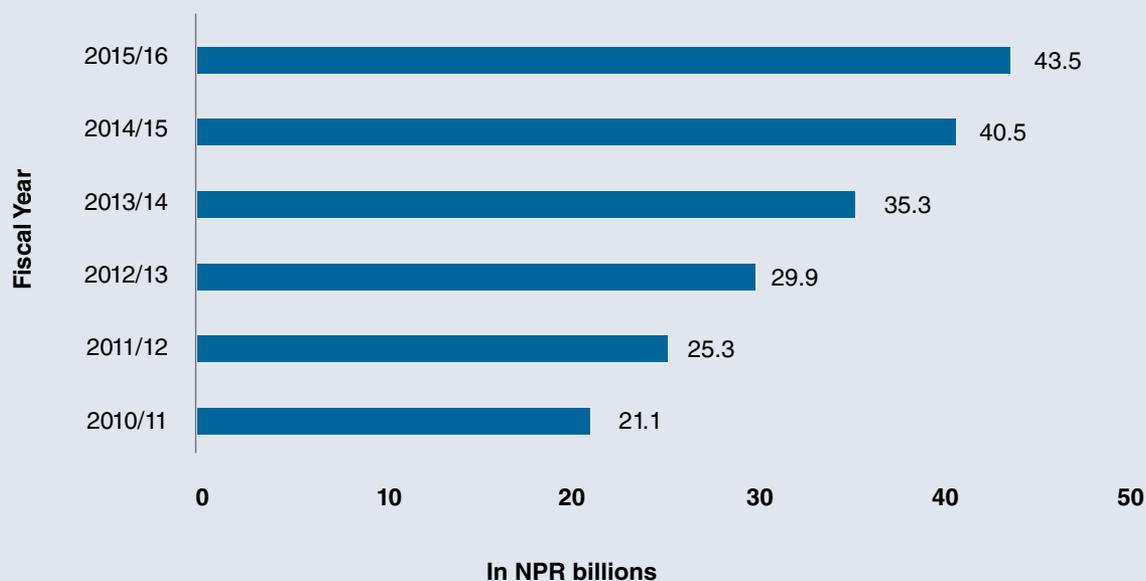


Figure 18: Contribution by hotels and restaurants to GDP (current prices) 'In NPR billions'


Source: Nepal Economic Survey Fiscal Year 2015-16, Ministry of Finance

RISE IN DOMESTIC TOURISM

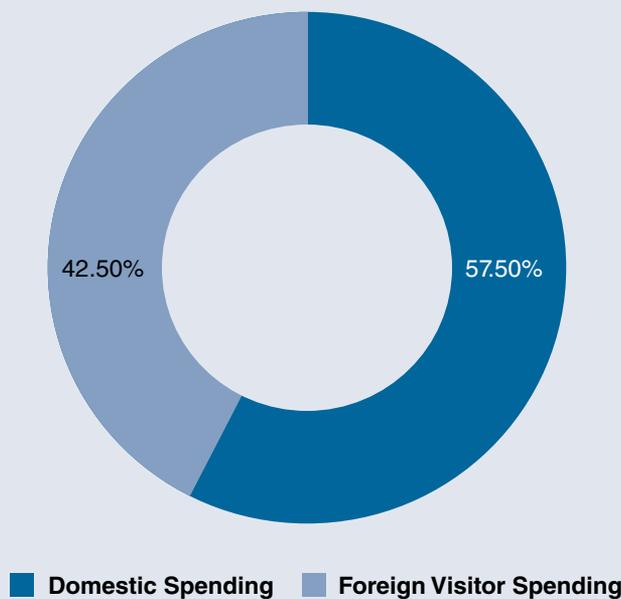
There has been a significant growth in domestic tourism over the years that has bolstered the growth of the hospitality sector. This has helped to boost demand for hotels rooms and food and beverage post-earthquake and economic blockade. As shown in Figure 19, domestic travel spending generated 57.5% of direct travel and tourism GDP in 2015, compared to 42.5% from foreign visitor spending. Better connectivity of roads, increased private vehicle population, improved lifestyle choices and mushrooming of nuclear families over the years has led to more domestic travel in Nepal. Meanwhile, the exponential rise of social media also helped the domestic population discover and share various facets of their own country across different digital and social media platforms. As such, the hospitality industry has responded with tourism packages targeting domestic tourists such as lodgings with basic amenities, availability of a variety of food, etc. to encourage traveling within the country.

Nepal continues to be urban centric in its growth; with continued internal and external migration and displacement of people on a large scale. This therefore brings about a new wave of travellers visiting friends

and families or attending religions or social functions within the region. The mobility of the average Nepali had improved considerably, especially post conflict; when travel was difficult and dangerous due to the ten year insurgency. Meanwhile increased acceptability of traveling as a form of recreation among the new generation has also pushed domestic travel with these trends expected to continuously grow at rapid pace.

Domestic tourism is a life saver. If not for domestic tourists, most of the hotels would have shut post-earthquake and economic blockade. Nepali people travel a lot and on an average spend more than the foreigners.

*Yogendra Sakya, Chairman,
ACE Hotels and Resorts*

Figure 19: Domestic versus foreign spending in 2015

Source: *Travel and Tourism Economic Impact 2016 Nepal*, World Travel and Tourism Council

Nepali tourists mainly travel to Pokhara and Chitwan and are found to spend more on food and beverage compared to international tourists. Besides domestic tourism, the country has also seen a growth in outbound tourism; with travel agencies have coming up with attractive outbound tour packages, and a greater number of Nepali people traveling abroad in recent years.¹²⁶ Meanwhile, the easing of visa regulations to travel to Indonesia through a visa on arrival program has also seen thousands of Nepalis visiting popular holiday destinations such as Bali.

HOTEL AND MONETARY POLICY

One of the main objectives of the monetary policy for FY 2015/16 of Nepal Rastra Bank (NRB) is to channelize financial resources towards productive sectors of the country such as agriculture, energy, tourism, small and cottage industries, as well the deprived sector. As per the existing requirement of Nepal Rastra Bank (NRB), it is mandatory for commercial banks to disburse 20% of their total credit in the specified productive sectors. Likewise development banks and finance companies are required to allocate 15% and 10% respectively of the total credit to the specified productive sector. As such, there is also provision of refinance facilities to establish luxury hotels in tourism

development potential areas such as Pathivara, Maipokhari, Halesi, Lamtang, Swargadwari, Upper Mustang, Gadhimai, Janakpurdham, Rara and Khaptad. The policies laid down by NRB shows that a lot of investment will be coming in the tourism and hospitality sector which is expected to grow in the near future.

Tourism and hospitality is one of the most productive sectors of the economy. Therefore, banks must support it as it contributes to employment generation and supports other SMEs as well.

*Sunil KC, Chief Executive Officer,
NMB Bank Limited*

SWITCH TO OTA'S FOR INCREASED REVENUE

With widespread proliferation of technology in today's world, there has been a shift from travel service providers; in booking hotels, trips and air tickets, to online travel

agents (OTA). Many travellers worldwide now make travel bookings through OTAs based on reviews and online research. Marketing and branding of tourism destinations and businesses have therefore been exposed to a new dimension of managing their businesses – from ensuring that they have online marketing channels covered to maintaining standard service delivery; to avoid negative online reviews. According to industry experts, in the year 2015/16, 70-80% of hotel bookings were done online via OTAs such as booking.com and agoda.com. While OTAs typically charge commission of 15%, they have become good source of business to the hotels in the recent years.

The current trend is a shift towards internet, Google and TripAdvisor recommendations. Hotel bookings are now mostly done online through OTAs like TripAdvisor.

*Sagun Pradhan, Director,
Swotha Traditional Homes*

TERAI TOURISM SCENARIO

The Terai region in Nepal has seen a growing revenue base through tourism, due to a growing number of Indian tourists; particularly from the bordering Indian states, taking advantage of the open border between the two countries. With Bihar being declared an alcohol free state by the Indian government, the Bihar populace often travels to Nepal via the open border, giving rise to liquor tourism and the proliferation of small casinos in the region. Subsequently budget hotels have seen a surge in their occupancy rates in the border areas; with occupancy at 85-90% on most days. Likewise, pubs and bars are also doing very well. Subsequently, this has also led to a rise in room rates in popular tourist areas in the Terai. For instance lodge owners in Janakpur have increased their room rates by over 30% to capitalize on this trend.¹²⁷ Consequently the Hong Kong based Silver Heritage Group is now developing a 100 room five star casino resort in Bhairahawa targeting the large volume of potential Indian tourists living across the border; including Delhi, Uttar Pradesh, Bihar and West Bengal.¹²⁸

Besides the popularity of the Terai region for liquor tourism and mini casinos, major cities of Terai; such as Nepalgunj,

are also gaining popularity as a destination for Indian weddings. With a view of targeting this group of Indian tourists, Soaltee Crowne Plaza is developing an 81 room, four star hotel in Nepalgunj.¹²⁹ There is a huge potential for the hospitality and tourism sector in Nepalgunj, as it is a gateway for the Mount Kailash and Mansarovar trek, with the Nepalgunj-Simikot-Hilsa route being a popular one for tourists.¹³⁰ Meanwhile Nepalgunj is also a transit hub for trekking to the Dolpa, Jumla and Mugu regions.¹³¹

BOUTIQUE HERITAGE HOTELS

Due to homogeneity of services provided in the tourism and hospitality sector across the world, a key differentiating factor for Nepal has been its ability to provide a rich cultural heritage experience to its tourists. With more and more tourists seeking such immersive experiences, various traditional homes in Kathmandu, Patan and Bhaktapur have now been converted into hotels or lodges; providing unique cultural experiences to tourists. The main focus of these establishments is to provide an authentic traditional Nepali experience with modern comforts. For instance, Swotha Traditional Homes in Patan has been built; preserving and renovating a 70 year old Newari home. Similarly various Rana residential buildings have also been converted into hotels and lodges; such as the Hotel Kaze Durbar in Kamalpokhari - a heritage hotel built by renovating a Rana dynasty building – thereby preserving its original European neoclassic design.

Nepal has never been about high rises. Tourists look for authentic Nepali experience.

*Sagun Pradhan, Director,
Swotha Traditional Homes*

Tourism has to be sustainable. It has to take into consideration heritage and conservation issues.

*Karna Shakya,
Founding Chairman, KGH Group of Hotels*

SERVICED APARTMENTS

The serviced apartments segment in the hospitality sector is an emerging one in Nepal. These apartments usually target guests that stay for long durations; and are usually larger than hotel rooms and are fully serviced. With a growing expat community within the country, there is significant scope for fully serviced apartments in Nepal. For instance, the Aloha Residence in Jawalakhel that charges USD 1500 (NPR 163,215) per month for a three bedroom apartment including 1 Mbps dedicated internet, 24 hours hot and cold water, gas, health club facilities and 200 units of free electricity,¹³² has been doing relatively well. In addition, with increased Foreign Direct Investment (FDI) inflows into the country, the demand for fully serviced apartments is projected to increase.

HOMESTAYS IN NEPAL

Another tourism service that has gained popularity in Nepal has been the private or community based homestays in Nepal; initiated first in Sirubari and Ghalegaon.¹³³ Homestay programs provide tourists with the opportunity to experience local cultures; meanwhile also providing an alternative source of livelihood for the rural Nepali population. Homestays often have a positive impact in the environment. For instance Dallagaon village in Bardia used to be very dirty with people throwing garbage in the

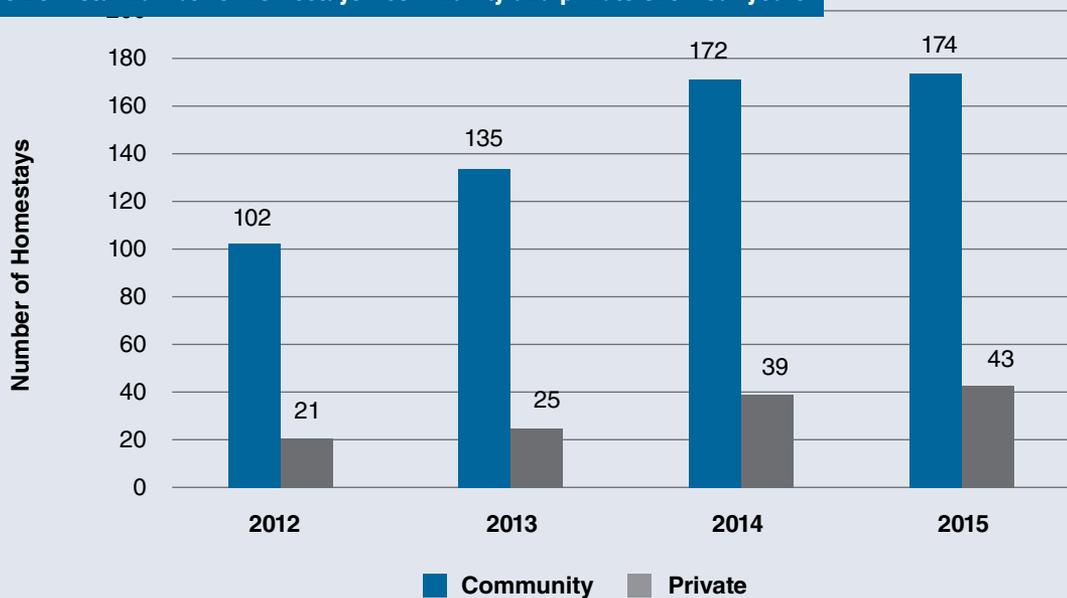
streets. However after the launch of homestay programme people started keeping the streets clean.¹³⁴

Besides environmental impact, homestays also help in preserving the art and culture of the village. For instance Bhusse Village of Bhulbhule VDC in Lamjung has recently started a homestay program to revive Tamang art and culture.¹³⁵ Likewise Chitlang, Makwanpur has seen a rise in both domestic and foreign tourists which has encouraged them to expand homestay facilities. The number of homestays in Chitlang has increased from 4 to 12 since the first time it opened homestays in 2011.¹³⁶ According to the Department of Tourism, there is increasing number of homestays in Nepal - both community and private, with a total of 353¹ homestays all over Nepal as of 2016.

A person preferring to stay in a five star hotel will definitely go for that category hotel and not a homestay.

*Yogendra Sakya,
Chairman, ACE Hotels and Resorts*

Figure 20: Total number of homestays - community and private over four years



Source: Nepal Tourism Statistics 2015, Nepal Tourism Statistics 2013

¹ The figure comprises of both community and private homestays all over Nepal including data from tourism office of Kakarvitta, Namche, Janakpur, Birgunj, Bhairahawa, Pokhara and Kohalpur.

NEPAL HOSPITALITY SUPPLY OUTLOOK

According to Hotel Association of Nepal (HAN), 4,000 hotel rooms will be added across hotel by 2018-19. Within the next three years, 16,000 room nights is projected to be added; which could accommodate nearly 6 million tourists per year. As per the Department of Tourism the current total number of beds is shown in the Figure 21.

Figure 21: Total number of beds in star and non-star category hotels



Source: Department of Tourism

A number of international hotel chains have signed management contracts with Nepali entrepreneurs to expand their branches in Nepal.¹³⁷ Several global brand hotels including Aloft by Marriott Starwood, Doubletree Hilton by Hilton Hotels and Resorts, Fairfield by Marriott, Sheraton by Marriott Starwood, Holiday Inn by InterContinental Hotels Group, Zinc City, are scheduled to make their presence in Nepal. Therefore, approximately 1,000 rooms are expected to be added into the hospitality industry by 2020; through these global hotel brands.

CHALLENGES AND RECOMMENDATIONS

The tourism industry has never been regarded as an independent industry on its own but is generally clubbed with the aviation as well as hospitality industries. For the development of an effective tourism brand of Nepal, a major overhaul is needed for the tourism and hospitality industry to unleash its full potential. Meanwhile there are many lessons to be learned from countries who were in similar situations in the 1990s in terms of arrivals - be it Cambodia or Malaysia – but have now been able to make tourism a backbone of their economies. Meanwhile Bhutan is another country that has opened up to tourism relatively late, but has been able to position itself as a high end destination.

AIRPORT MANAGEMENT

The current status of Tribhuvan International Airport (TIA) is one of the key bottlenecks to growth in the hospitality industry. There are major issues within the airport management ranging from infrastructural to service delivery; such as airport immigration systems, service quality or control of national carriers. With airports being

one of the first touch points for travellers, its management and service delivery is key for tourism. With tourism being a strong pillar for economic development it is therefore essential to scale up the international airport infrastructure as well as in terms of for efficient management.

With tourist arrivals expected to increase in the coming years, passenger handling capacity of the TIA also needs to increase simultaneously. Currently the airport is ill equipped to deal with heavy passenger inflow. For instance, if multiple flights land at the same time, the current number of conveyor belts are insufficient to handle the luggage. Meanwhile, value addition is also very important to high end tourists such as improvement in flight services or crisis management at the airport. As such efficient management and maintenance of the upcoming airports including Gautam Buddha airport (6 million passenger per year), Pokhara International Airport (1 million passenger) and Nijgadh International Airport (15 million passenger per year) can pave a way for tourism and hospitality development of Nepal.

Nepal needs to focus on 4 A's:

- 1) **Attraction:** Nepal as a country is attractive for the tourists because of its natural beauty and cultural heritage.
- 2) **Accessibility:** Since Nepal is a land locked country and has only one international airport, it is one of the biggest challenge for the country. Moreover airfares to Nepal are relatively expensive which makes Nepal a costly destination. Nepal therefore needs to focus on upgrading the current airport and come up with additional international airports.
- 3) **Accommodation:** Good standard hotels are only limited to Kathmandu and Pokhara. Nepal should focus on establishing good hotels in other destinations of Nepal as well.
- 4) **Activities:** Nepal should promote new destinations and come with innovative product offerings.

*Prachanda Man Shrestha,
Freelance Tourism Consultant*

AVIATION WOES

Nepal's national flag carrier; previously the Royal Nepal Airlines and now Nepal Airlines (NA), used to reach the world's top cities including Frankfurt, London and Osaka.¹³⁸ A lot of tourists from these country; mostly belonging to the high spending category used to visit Nepal. Because of the presence of this connectivity, airfare used to be cheaper for travellers visiting Nepal. However in the present context, air connectivity of Nepal is only good with countries where migrant workers travel such as Malaysia and Middle Eastern countries including Doha and Dubai. Currently, NA has direct flights to only to the following international destinations – Delhi, Bangkok, Kuala Lumpur, Doha, HongKong, Bengaluru, Mumbai and Dubai. With the revival of the national carrier and expansion of its air routes and other international private airlines coming in the picture like Himalaya Airlines; with direct flights to international destinations including Colombo and Doha, this will facilitate in expanding global connectivity while also reducing airfare.

INFRASTRUCTURE IMPROVEMENT

Besides airport infrastructure, road infrastructure is also a major issue in Nepal. Dust pollution and traffic congestion due to inefficient management of road expansion projects and water pipeline projects have acted as major deterrent to tourists visiting Nepal. Meanwhile road networks from Kathmandu to other tourist destinations such as Pokhara, Chitwan, etc. also need to be developed to reduce travel time. Furthermore development of roadside infrastructure and businesses such as restaurants and rest houses also need to be facilitate to ease traveling within the country. As such, ongoing road expansion projects and water pipeline projects therefore need to be more effectively managed to reduce dust pollution and traffic congestion in the valley.

RESEARCH AND DEVELOPMENT IN THE PRODUCT OFFERINGS

Research and development in product offerings is required to facilitate greater tourist inflow in the coming years. As of yet, Nepal has not been able to change its itinerary for the tourists with trekking being the key value proposition for tourists. Nepal therefore needs to develop tourism destinations, products and services in a planned way by maximizing its potential. For instance since Nepal is popular for its traditional heritage, better urban planning of such tourism destinations is important to conserve them.¹³⁹

The current infrastructure of Nepal will not be able to support the increasing number of tourists. The development codes need to be more conducive for building hospitality projects while also being sensitive to safety issues. Policies need to be favourable to investors as well as the tourism sector as a whole. A holistic introspection and action is necessary if we wish to make the most of our tourism potential.

Rahul Chaudhary.

Executive Director, CG Hotels and Resorts

Countries such as Thailand have been able to develop various destinations and products for tourists to capitalize on its tourism potential; making it one of the most visited Asian destinations. Similarly Nepal should also work towards developing various attractive packages. For instance, a tourist help desk at the airport or information centres around major tourist locations providing a list of tourist activities, can facilitate greater revenue for the tourism sector. As such tickets to these various tourist location can be bundled and sold to tourists to increase visitation to certain tourist sites. While tourists benefit through discounted bundled prices and hassle free ticket procurement, lesser known tourist sites are also able to generate revenue on being packaged with better known sites.

In terms of product of destinations, hoteliers have a huge opportunity to invest in the mid and far western regions of Nepal since they are easily accessible to Indian tourists. Tourists travelling from New Delhi to Shuklaphanta National Park located at Kanchanpur district have to drive only 350 km. Likewise it is only a four hour drive from Lucknow to Bardiya National Park. Therefore, adequate research and development in these areas will therefore further facilitate increased revenues through the tourism and hospitality segments.¹⁴⁰

Most visitors to Nepal are trekkers, therefore service standards in trekking accommodations should be markedly improved. More hotels with better service standards should come in rural destinations while existing lodges should enhance service delivery.

*Sumit Baral, Tourism Portfolio Manager,
Samarth-Nepal Market Development
Programme*

ACCESSIBLE TOURISM AS AN OPPORTUNITY FOR NEPAL

According to industry experts, there is a huge opportunity for Nepal to tap in to accessible tourism. Like Nepal has been regarded as a welcome destination for the LGBT community, the same could be extended to the physically challenged community. As per World Health Organization (WHO), around 15% of the world's population have some form of disability. Therefore, it is an opportunity for businesses in the tourism industry to facilitate travel for such people. The government also needs to come with policies on infrastructural developments to cater to the needs of these tourists. Hotels and restaurants need to come up with proper ramps and facilities to support this differently abled category of tourists.

RESOLVING HUMAN RESOURCE ISSUES IN HOSPITALITY SECTOR

The efficiency of human resources in hotel industry is very low in Nepal. The staff to room ratio in general is about 2:1 in Nepal, which is double the current international benchmark of 1:1. One of the major reasons behind this high ratio is due to lack of staff training. Hotels in Nepal generally do not have a policy of providing ongoing training and therefore severely lacks investment in human capital. Furthermore, Nepal also does not have a strong labour law in terms of hiring and firing policies, due to which staff generally tend to work in the same organization for a long period of time despite performance. As a result, more benefits and medical facilities have to be provided for such senior staffs which increases the hotel costs.

In the present context, it is estimated that there are about 1,200 hotel management graduates every year from over 27 hotel management schools in the country. The current number of hotels cannot accommodate the employment of the number of graduates. Therefore, most of the skilled graduates go abroad for better work prospects. In addition, staff turnover is very low in the hotel sector of Nepal resulting in decreased job prospects for new entrants.

The hospitality industry will therefore need to focus on providing both initial as well as ongoing training to their staff; associated with strict monitoring to improve the quality of human capital in the industry. Meanwhile technological innovations can also be leveraged to further increase efficiency of staff. With the increase in 4000 hotel rooms by 2020, it is also an opportunity for fresh hotel school graduates to work with the international hotel chains.

Traditionally trekking was more attractive for the tourists. However, now, holiday makers are inclined to cultural experiences. People visit Nepal for bird watching, wildlife and agro experiences, spiritual awakening, meditation, wellness and spa. Senior citizens are travelling in significant number. Special interest travellers are increasing. Accessible tourism is the upcoming trend globally. Nepal has a huge potential to tap into this segment. Therefore, hotels and tourism operating sectors should design their products and amenities focusing on the special need of these travellers.

Pankaj Pradhananga, Director - Four Season Travel and Tours

Many skilled hotel management graduates go abroad as the current number of hotel rooms cannot accommodate the number of graduates. Upcoming international brand hotels is a better prospect for Nepal as fresh graduates of Nepal will have opportunities to work in the country itself.

Samir Thapa, Executive Chairman, Silver Mountain School of Hotel Management

SERVICE AS DIFFERENTIATOR

Brand Smile has always been Nepal's key differentiator in tourism with warm hospitality being a hallmark of all Nepalis. This therefore needs to be leveraged to provide an outstanding tourism experience to visitors to the country. However political interference in unions and associations have resulted in poor service delivery across the hospitality industry. Similarly nepotism and lack of stringent quality checks and measures within the industry have fostered

poor service delivery; with union associated employees failing to meet delivery standards. Increased politicization within these industries have therefore resulted in skilled members of the tourism and hospitality sector leaving Nepal in search of greener pastures. Productivity based emoluments, acknowledging seasonality of working hours, allowing 24 hours operation of establishments and allowing employers to hire and fire employees easily are some of the major reforms that are required.

GLOBAL TOURISM & HOSPITALITY SCENARIO

Globally the hospitality and travel industry has expanded and diversified to become one of the largest and fastest growing industries. As a result many countries are embracing and investing in tourism resulting in the development of many new travel destinations; leading to subsequent growth in the hospitality industry.

INTERNATIONAL TRAVEL ON AN UPWARD TREND

Despite geo-political issues, terrorism and economic volatility; the global tourism industry has shown resilience with travel and tourism on the increase. Globally international tourist arrivals grew by almost 76% from 674 million in 2000 to 1.2 billion in 2015. It is estimated that international visitors around the world grew by 3% in 2016. Countries such as Japan, South Korea, Vietnam, Spain, Portugal and Ireland recorded double digit growth. Meanwhile terrorist attacks negatively impacted tourist arrivals in few of the countries such as France, Belgium and Turkey.¹⁴¹

According to World Travel and Tourism Council (WTTC), in 2015 travel & tourism directly contributed USD 2.2 trillion (NPR 242.6 trillion) to the world's GDP (3%). This figure is forecasted to grow by 4.2% annually from 2016 to 2026 to reach USD 3.5 trillion (NPR 377.5 trillion) in 2026 (3.4% of world's GDP). In 2015, a total of 107 million jobs (3.6% of total world employment) was directly supported by travel & tourism; and is forecasted to increase by 2.1% annually to 135 million jobs by 2026 (4% of total world employment).¹⁴²

INCREASED ASIAN OUTBOUND TRAVEL

According to Pacific Asia Travel Association (PATA) report, in the year 2015, the Asia Pacific region witnessed 577 million international visitors. In terms of annual percentage growth in international tourist arrivals, the top five performing destinations in this region included Japan, Chile, Thailand, Sri Lanka and Myanmar; with Myanmar taking the lead with a growth of almost 52%. At the beginning of 2016, 35 out of the total 44 destinations in the Asia Pacific region showed a collective increase of 8.4

million international arrivals. In early 2016, China showed the highest outbound growth patterns in Asia Pacific.¹⁴³ It is estimated that arrivals from China to Asia Pacific destinations will be more than 150 million by 2020, and China will generate about 23% of all arrivals to Asia Pacific destinations by the end of this decade.¹⁴⁴

INCREASED BRAND MERGERS AND ACQUISITIONS

The hospitality industry has seen flurry of activity in the trend towards mergers and acquisitions (M&A) among global hotel brands since 2015. For instance, the San Francisco based Kimpton Hotels and Restaurants have been acquired by the Intercontinental Hotels Group and Fairmont Raffles Hotels international (FRHI) Hotels and Resorts by France's Accor Hotels. Meanwhile, Marriott International's acquisition of Starwood Hotels and Resorts in 2016 have also made headlines. Other noteworthy M&A include purchase of parent companies such as, HNA Tourism Group Co. Ltd.'s purchase of Carlson hotels and their announcement of a significant stake acquisition in Hilton Worldwide.

Recently the strategic way for global brands to grow has been through the acquisition of tourism and hospitality operators with management and franchise contracts; a result of natural attrition in properties and limitation to new supply growth. Equity analysts are also found to favour businesses that have a full range of offerings; in terms of service levels and geography. Furthermore, with growth in revenue per available room slowing across mature markets, brands and management companies are looking to boost EBITDA (earnings before interest, tax, depreciation and amortization) and boost efficiency by adding properties.

TRANSFORMATION IN HOTEL DISTRIBUTION CHANNELS

Traditional distribution channels are slowly and steadily losing market share while new channels particularly those that allow bookings via online portals such as Online Travel Agents (OTAs) are growing in popularity. The OTA segment is emerging as a strong distribution channel

and has grabbed a substantial share from traditionally contracted booking channels; mainly wholesalers, tour operators and direct bookings.

Initially OTA's; which have been around for almost two decades, were seen as a convenient distribution channel through which hotels and airlines could sell extra inventory. However the relationship between hotels and OTAs have gone somewhat sour. This is because OTAs have been eroding the hotel revenue and profits by charging 15-30% from hotels for their services. However, with OTA's share of online sales increasing year over year, dependency of hotels on OTAs for bookings are also increasing.

The deployment of massive marketing budgets by OTA's have also allowed them to gain a high level of market dominance over direct hotel sales. For example, in 2015 Priceline spent USD 2.8 billion (NPR 305 billion) on online advertising and another USD 215 million (NPR 23.4 billion) on offline channels such as television and billboards. Likewise Expedia spent USD 3.3 billion (NPR 359 billion) on advertisement.¹⁴⁵ In order to counter OTA's, hotels are now pushing direct sales through their websites. For example, in 2016 Hilton Worldwide and Marriott International launched their "Stop Clicking Around" and "It pays to book direct" marketing campaigns respectively to counter OTAs.

TRAVEL BRANDS EMBRACING ONLINE BOOKABLE TOURS AND ACTIVITIES

Online travel companies such as TripAdvisor, Airbnb, Google, Expedia and Booking.com have now forayed into online booking tours/packages; such as sightseeing, day trips, etc., which signals the growth in this business segment therefore becoming a major attraction point for many OTAs. This is illustrated by TripAdvisor's non-hotel segment; which recorded a revenue of USD 101 million (NPR 11 billion), a growth of 35% in the third quarter of 2016. Similarly TripAdvisor's hotel segment which is three times the size of its non-hotel segment declined by almost 6%.¹⁴⁶ The decline in growth of the hotel segment for OTA's is a result of hotels starting to fight back against the dominance of OTAs and pushing direct sales through their own websites.

NEW DEMOGRAPHIC TARGET MARKET

Research indicates that the fifties age group has emerged as the new demographic target market for the tourism and hospitality industry. This is because this fifties demographic have higher spending capacity than the millennials and have a clear preference for value over luxury. One of the

key drivers for targeting this segment; by international travel brands, is that the fifties demographic provides a bridge between the boomers and Gen-X; and therefore have a keen insight from Gen-Y (their kids). This holds particularly true for the United States (US) market as it is estimated that in 2017 nearly 50% of the US adult population will be age 50 and older and will control 70% of the country's disposable income.¹⁴⁷

HOSPITALITY INDUSTRY VULNERABLE TO ECONOMIC CONDITIONS

Travel and hospitality industry is highly vulnerable to economic conditions. This is because the hospitality sector operates in a globally inter-connected and consumer led environment. For example the North African hotel market recorded a steep decline in revenue during the Arab Spring movement in 2010. An economic downturn is one of the most challenging demand shocks from an operational and investment perspective, as it typically has a protracted impact on revenues and capital expenditure.

CHANGING CONSUMER MIND-SETS

The rapid and exponential growth of mobile usage among customers has meant that customer are increasingly switching to smart phone technology to research travel and bookings. It is estimated that 85% of leisure travellers decide on activities only after they have reached their destination. Further 50% of international travellers rely on mobile services to make spontaneous decisions on what to do.¹⁴⁸

The hospitality industry has witnessed a move from B2B to B2C selling; with consumers directly interacting with service providers. Meanwhile popularity of online travel portals; like TripAdvisor, has necessitated personalized responses to consumers. As with the advent of social media, one bad review can mean loss of business. Whereas word of mouth; a key source of business has now been institutionalized through social media. Changing consumer expectations and travel behaviour will therefore be one of the key issues that the hospitality sector will need to focus on with consumers starting to value personalized services. Meanwhile, the rapid growth of Airbnb shows that there is a huge market for various travel products besides basic offerings. Revenue of hotels will therefore depend on the speed at which hotels are able to capitalize on changing customer expectations.

GLOBAL OUTLOOK

In the year 2017, the travel and hospitality industry globally will need to focus on leveraging technology to

add value to their offerings. Customer experiences should be enhanced by making travel easier through the use of various technologies; such as artificial intelligence and mobile applications. While basic Wi-Fi services have become mandatory, hotels will need to come up with more

innovative ways to meet changing consumer expectations, for instance access to a number of options and services via mobile applications for hotel guests. In addition use of smart phones as - room keys, television remotes, and thermostat controls – are also expected to gain popularity.¹⁴⁹

A great example of technology and innovation in meeting changing customer experiences is Uber's partnership with a variety of apps; including hotels, restaurants and trip planning services, to simplify the travel experience. With this partnership, travelers can now get information across different service providers through one platform. For example, Hilton being one of the partners of Uber, the customer would be able to use the Uber app to check their stay details at the Hilton.

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NEF PROFILE

Nepal Economic Forum (NEF) is a premier private-sector led economic policy and research organization that seeks to re-define the economic development discourse in Nepal. Established in 2009 as a not-for-profit organization under the beed (www.beed.com.np) umbrella, NEF is a thought center that is working to create positive transformations in policy reforms. NEF stands out in being able to make significant strides to bring the private sector perspective and engage with both the public and private sectors in the development discourse. NEF is currently a recipient of the Open Society Foundations' Think Tank Fund.



NEF works in partnership with many Nepali and international institutions in its quest to mainstream the discourse on the Nepali economy, which has not been given the necessary space it deserves.

NEF has partnered with the Himalayan Consensus Institute (HCI) to facilitate the development of alternative development paradigms and successfully held the first Himalayan Consensus Summit 2016 in March 2016.

NEF BROADLY WORKS UNDER THREE AREAS:

BPRC

The Business Policy Research Center (BPRC) engages in research, dialogue and dissemination relating to pertinent economic policy issues. BPRC has been producing nefport, a quarterly economic analysis publication, nefsearch, a periodic research publication and conducting nefstalk, a platform for policy discourse.

PPCP

Through the Center for Public, Private and Community Partnerships (PPCP), the partnerships discourse is further elaborated through addition of the community dimension to existing models of public private partnerships. Apart from standalone interventions, the PPCP perspective is integrated in the work that NEF and beed initiate.



NEF operates in the domain of Development Consulting through its devCon division in conjunction with beed management.. It works with a variety of bilateral, multilateral, national and international NGOs in the areas of policy research, economic analysis, value chain analysis, enterprise development, sectoral studies and public private dialogue.



We are striving to ensure financial sustainability for NEF to complement the support it currently receives from beed management and the Open Society Foundations. If you are interested to support NEF, please do get in touch with sujeev.shakya@beed.com.np or shayasta.tuladhar@beed.com.np



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