OCCASION

This publication has been made available to the public on the occasion of the 50th anniversary of the United Nations Industrial Development Organisation.

DISCLAIMER

This document has been produced without formal United Nations editing. The designations employed and the presentation of the material in this document do not imply the expression of any opinion whatsoever on the part of the Secretariat of the United Nations Industrial Development Organization (UNIDO) concerning the legal status of any country, territory, city or area or of its authorities, or concerning the delimitation of its frontiers or boundaries, or its economic system or degree of development. Designations such as "developed", "industrialized" and "developing" are intended for statistical convenience and do not necessarily express a judgment about the stage reached by a particular country or area in the development process. Mention of firm names or commercial products does not constitute an endorsement by UNIDO.

FAIR USE POLICY

Any part of this publication may be quoted and referenced for educational and research purposes without additional permission from UNIDO. However, those who make use of quoting and referencing this publication are requested to follow the Fair Use Policy of giving due credit to UNIDO.

CONTACT

Please contact publications@unido.org for further information concerning UNIDO publications.

For more information about UNIDO, please visit us at www.unido.org

UNITED NATIONS INDUSTRIAL DEVELOPMENT ORGANIZATION
Vienna International Centre, P.O. Box 300, 1400 Vienna, Austria
Tel: (+43-1) 26026-0 · www.unido.org · unido@unido.org

07213

Distr.
LIMITED

ID/WG.234/7
8 November 1976

ENGLISH

United Nations Industrial Development Organization

Intergovernmental Expert Group Meeting on the
Industrialization of the Least Developed Countries

Vienna, Austria, 15-24 November 1976

Agenda Item 1

SPECIAL PROBLEMS FACING LDCs IN PROMOTING INDUSTRIAL DEVELOPMENT

WAYS AND MEANS TO OVERCOME VARIOUS OBSTACLES TO THEIR INDUSTRIALIZATION 1/

Country Paper

NEPAL

by

Ajit Narayan Singh Thapa*

1/ The views expressed in this paper are those of the author and do not necessarily reflect the views of the Government of Nepal or UNIDO. This document has been reproduced without formal editing.

* Executive Chairman, Industrial Services Centre, Nepal.

id.76-5930

We regret that some of the pages in the microfiche copy of this report may not be up to the proper legibility standards, even though the best possible copy was used for preparing the master fiche

TABLE OF CONTENTS

1. Conditions in Nepal's Industrial Sector

Nepal's Gross Domestic Product (GDP) estimates show that the industrial sector accounts for 11 per cent of total GDP at market prices including contribution of 6.68 per cent from Cottage and Village Industries. An analysis of the census figures presents a picture of a highly skewed industrial sector, whether measured in terms of size, product or locational distribution.

Size: the average sized manufacturing establishment in Nepal employs 20 workers, produces Gross Value Added (GVA = Net Output + Depreciation) of Rs. 136,000 and uses fixed assets valued at Rs. 105,000. However, the majority of firms are considerably smaller than this, since 80% of the establishments employ less than 10 workers.

Product:

Most industry in Nepal is simply an extension of the agricultural sector. Rice and oil mills account for 76% of the total number of establishments and 50% of the net output. Productivity in these firms is extremely low, the net output per worker averaging only Rs. 8,100 for the year. Other agro-based industries contribute 9 per cent of the sector's net output. Agro-industries other than grain and oil milling are thus likely to produce about the same net output as the next largest category, bricks and tiles, which contributes 11 per cent. Otherwise only wood-based industries at 6 per cent and printing at 3 per cent are worth mentioning, though it should be mentioned that the Miscellaneous group accounts for 17 per cent and some of operations which are presumably included in this category, such as brewing and distilling and cigarette manufacture, are probably equally large.

Location:

The degree of concentration of industry in the Central and Eastern Regions of Nepal is shown by the following table:

Percentage Distribution of Manufacturing

	Central	East	West	Far West
No. of establishments	54%	21%	14%	11%
Gross Value Added	49%	28%	18%	5%
Employment	52%	33%	10%	5%

Rs.12.5 = US$ 1.00

Thus, 77 per cent of industrial activity as measured by GVA and 85 per cent of employment is in the Central and Eastern Regions. A latitudinal classification of location would show even more marked concentration, since apart from Kathmandu Valley, Hetauda and, to a limited extent, Pokhara, all industry is virtually confined to the Terai.

Industrial productivity is extremely low. Overall the average GVA per worker is approximately Rs. 7,000 and net output Rs. 6,500, which is even lower than the figure for grain and oil mills quoted above. The reasons for this low level of productivity can also be explained by the labour intensity of most industrial operations since the value of fixed assets per worker is only Rs. 5,400 and the capital/output ratio is below unity at 0.82. However, low capitalization is not the sole cause of low productivity, important contributory factors being the high incidence of temporary closures and poor management.

A surprisingly high proportion of Nepal's manufacturing production is exported, viz. Rs.840 million out of a total gross output of Rs. 1.76 billions or 48 per cent. However, 93 per cent of these exports are from the grain and oil milling industries whose export sales are virtually confined to India. The remaining 7 per cent are almost entirely made up of jute and jute products and export from other manufacturing industries are negligible.

Thus although the jute industry is Nepal's principal source of convertible foreign exchange earnings after tourism - Indian currency being non-convertible outside India - it only accounts for 3 per cent of the gross output of manufacturing industry which is sold outside the Indian and Nepalese markets. Moreover, the heavy dependence (60 per cent of its gross output) of the grain and oil milling industry on the Indian market, while probably safe enough for the time being, does place this industry in a strategically weak position in the event of India approaching closer to self-sufficiency in food grains or finding cheaper sources of supply, such as PL 480 sales from America. Hence the importance of improving and modernizing the basic food processing industries and of expanding activities into the production of more highly processed food products, with a view to overseas export.

2. Problems of Industrial Development in Nepal

The basic problem faced in developing manufacturing industry in Nepal is the small size of the domestic market and locational handicap of being land-locked and situated far away from the nearest sea-port. Although the population is larger than in many developing countries, the cash purchasing power is at most less than £$ 50 per head per year. Two-thirds of the population live in the hills which are difficult of access and where monetary transactions are peripheral, the people's basic needs being met from their own production. The market for manufactures is thus limited to the 10 per cent of the population which lives in towns and to the more accessible parts of the Terai.

As regards exports, apart from grain products to India they have been inhibited by Nepal's geographical position and the absence of easily exploitable natural resources and lack of skilled personnel. Even the jute industry has needed artificial support and it is only recently that the potential of other industries to produce for the world market, such as sugar, and tea, has been appreciated.

Against this background there has been little private initiative directed to the industrial sector and such capital and enterprises as has been forthcoming has been mainly concentrated in other sectors, notably trade and tourism. Furthermore there has been little effective institutional support for industrial development and uncertainty over the future of Indo-Nepal Trade and Transit Treaty greatly affects the industrial sector.

3. Objectives of Industrial Development

In the fifth five year plan His Majesty's Government of Nepal (HMG) has allocated approximately 16% of total planned outlay to the Industrial Sector, including power, and has the following objectives:

i) Making available to the maximum number of people some of the essential goods and services such as textiles, construction goods and consumer goods,

ii) gradual reduction of present dependence on imports by establishing industries designed to substitute imports,

iii)to provide the growing labour force, heavily dependent on agriculture, with expanded opportunities for new jobs.

iv) to strike a regional balance in development by establishing industries in less developed areas of Nepal,

v) to develop export-oriented industries wherever possible to improve the balance of payments position,

vi) to bring about both quantitative and qualitative improvements in industrial production and productivity.

4. Industrial Development Strategies

In order to alleviate the problems encountered by the Industrial sector, a number of steps have been taken by HMG. The fragmentation of the market is being slowly reduced by investment in surface and air communications; the monetisation factor is being raised by encouraging the production of cash crops and by the spread of financial institutions into rural areas; and much greater emphasis is being placed on industry at the macro-economic planning level. In 1974 HMG published its new Industrial Policy ,which lays down clear objectives for the sector, clarifies the position of the private sector and provides a number of fiscal incentives for activities in the priority areas. Financial support has been provided since 1959 through the Nepal Industrial Development Corporation (NIDC), but this by itself proved insufficient to generate the desired level of industrial investment since it was not strongly supported by good project studies. This deficiency was remedied two years ago by the formation of the Industrial Services Centre (ISC). The volume of requests for feasibility studies now coming forward has out-stripped ISC's capacity, indicating that there is no lack of potential projects, and HMG is now seeking outside assistance in order to accelerate the preparation of 'bankable' industrial proposals. At the risk of over-simplification, the strategy can be summarized as the maximum expansion of import-substitution industries, both at cottage and village scale and small, medium and large scale, while at the same time paying attention to industries with an export potential, which require large investment to bring in economies of scale and competitive in export markets.

5. Measures taken by HMG of Nepal to Overcome the Constraints

5.1. Investment Allocation

In view of the reluctance by private investors to provide capital for industrial ventures, the Government has assigned an important rôle to the public sector. Thus out of the total planned investment outlay of Rs. 1000 million in the industrial sector, it is expected that the public sector will contribute Rs. 531 million and the private sector about Rs. 400 to Rs. 500 million.

5.2. Sub-Sectoral Programme

The Fifth Plan (FFP) includes a programme for the re-organization, modernization and expansion of a number of public sector industries, viz. Agricultural Tools Factory, Leather and Shoe Factory, Tobacco Development Co. and Tea Development Corporation, start-up of production from five industries (cotton textiles, agricultural and industrial lime, vegetable ghee, bricks and tiles and vegetable oil) which were started during the last 4th Five Year Plan; establishment of two mineral-based industries - magnesite and cement - and two forest based industries - rosin/turpentine and pulp and paper. Private Sector has been given equal importance in the Industrial Policy of HMG/N. Areas and Projects have been identified for private investment and various support services are being extended. FFP has an explicit programme of assisting in re-organization of 'sick' industries and promising industrial ventures in the private sector will be supported to strengthen their operation and expansion. In addition every support required to set up 50 agro-based, 13 mining-based, 12 forest-based and 52 miscellaneous industrial ventures in the private sector will be extended by Government institutions and departments.

5.3. Priorities

As per the strategies, the Government has clearly outlined the priorities in the industrial sector with a view to making the country self-reliant in essential consumer goods and gradually making available development goods based on local natural resources. This approach is expected to develop import substitution as well as export-oriented industrial ventures. The details are as follows:

1. Committed projects under implementation. These include Brick and Tile, Cotton Textiles and Vegetable Ghee.

2. Projects designed for increased production of articles of daily necessities and producing construction goods of developmental needs. These include Cement, Sugar, Ghee, Flour, Woollen Garments, Iron and Steel.

3. Projects primarily based on indigenous raw materials and natural resources such as matches, catechu and tanning, resin and turpentine, hardboard, slate, pulp and paper, magnesite, tea etc.

4. Medium and small-scale industries as well as village and cottage industries producing ancillary goods, and also large-scale industries not falling within the above category but necessary due to economies of scale, will be accorded priority.

In terms of sub-sectoral priorities, top priority goes to the development of agro-based industries in keeping with the present dominance of agriculture in the economy and the need to expand processing and preservation capacities of agricultural products.

5.4. Facilities and Support Services

The 1974 Industrial Policy clearly defines the type and extent of investment promotion facilities to be extended to both local and foreign investors. It delineates both the types of projects and the regional areas in which the government seeks participation from the private sector in order to encourage industrial growth in a desired pattern and to improve the regional economic balance.

The facilities extended include term loan guarantee facilities, foreign exchange allocation to import inputs, relaxation on direct and indirect taxes and provision of required utilities and services at nominal rates through the government institutions. Further, HMG has attractive foreign currency capital and profit repatriation policies for foreign investment which allow the foreign investor a guarantee of repatriation of 10 per cent of the equity capital invested and 25 per cent of profits attributable to such capital.

Also HMG/N welcomes and provides every support and facility as above for foreign investment in the projects requiring investment from Rs. 1 million and above either in collaboration with private parties or on a joint sector basis with HMG, particularly where advanced technology is needed.

5.5. Industrial Districts

There are only few places such as Kathmandu, Biratnagar and Birgunj where the basic infrastructure for the establishment of industrial units is adequately available. It is therefore important to create such facilities outside these three cities as well.

HMG started in the early 1960's to remove these constraints by way of establishing industrial districts in the different parts of the country, where industries can be located. In the initial years, the districts have experienced low utilisation ratio of sheds and utilities but later this was significantly improved and presently two estates are fully occupied and area and capacity of utility services is different in various parts of the Kingdom. There are two in Kathmandu (Balaju, and Patan) and one each in Hetauda, Dharan, Pokhara, Butwal and Nepalgunj. The facilities available in these districts are developed plots of land, industrial buildings, regular and adequate supply of power and processed water. The rental charges on these utilities and facilities are nominal.

5.6. Institutional Services

In order to strengthen and re-organize the functioning of the public sector enterprises, HMG/N has already established the Corporation Co-ordination Council (C.C.C.). So far the Council has completed management and operational studies of many public enterprises, including manufacturing units. Findings of these studies are being used to improve their performance. Similarly the industrial extension and pre-investment feasibility services provided by ISC have contributed to the healthy promotion, expansion and implementation of industrial ventures.

5.7. Institutional Financial Support

Financial support of the industrial sector is provided through commercial banks and other financial institutions. NIDC is supporting both private and public sectors by providing long and short-term loans and equity participation, the emphasis is however for the private sector. Commercial Banks finance primarily loans for working capital, but recently in conjunction with the Cottage and Village Industries Department the Commercial Bank began to make term loans for small-scale industries; they are required to invest 70 per cent of their total deposits in cottage industries and agriculture. To meet these requirements NIDC and the Agriculture Development Bank are supported by lines of credit from various sources such as the USA, Japan, India, Germany, Britain, IDA, ADB etc. Local currency support is provided by Nepal Rastra Bank and HMG/N. To meet the specific needs of a particular industry, such as tea, tobacco, jute etc. and for absorbing bilateral assistance from donor countries, HMG is operating public sector companies. Financial support is also being provided by the recently formed Stock Exchange Company, which will underwrite share issues by manufacturing and commercial ventures, and by the Credit Guarantee Corp. which will guarantee loans for small and cottage industries.

E - 267

77. 06. 28