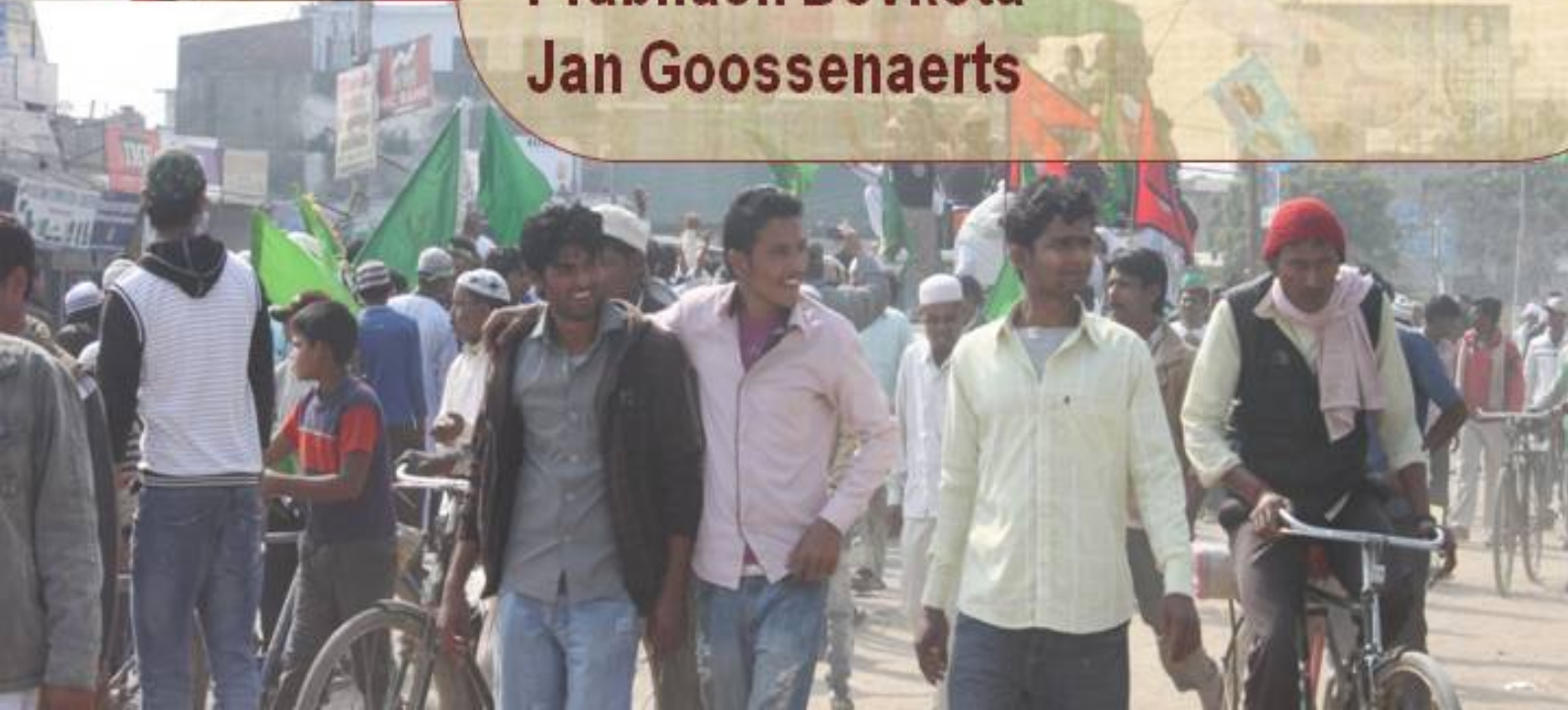




Foreign Aid and the making of Democracy in Nepal

Edited by
Prabhash Devkota
Jan Goossenaerts



Foreign Aid and the making of Democracy in Nepal

Prabhash Devkota and Jan Goossenaerts

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Preface

This study covering foreign aid direct investment in Nepal within the last 5 decades was conducted with an aim to bring some critical issues around aid politics and its direct link up with democracy, democracy making in Nepal, the role of foreign aid as a positive or negative catalyst of democracy, and issue based impacts on health, education, forestry amongst others. Moreover, the aim of the study was to initiate a discourse on aid governance and politics from the larger arena of Political Economy and to find the gaps in the democratizing of our institutions, the institutionalization of democracy from the family to the country system. AAMN believes that in democratic systems and governance there is the political space of the unheard, neglected and socially excluded. There are marginalized, women, Dalit, indigenous who should also enjoy the dignified life. Growing dissatisfaction with the development models the country is going through and the realization of vast gaps between haves and have nots made AAMN and its likeminded to think over the polity minutely. The likeminded of our network realized that something has to be done outright as time for it is in our forefront, the country is in transition. Nepal, has a politically federal democratic government without having any indicators of democracy. AAMN conducted a series of interactions with the likeminded about what exactly can be prescribed in this deteriorating time. AAMN published several e-bulletins that seek to promote a wider discourse on the subject. It created pressure among many stakeholders. Even the government high officials choose the sensitive topics. No one hesitated on saying that a knowledge initiative was needed as part of a wider discourse. So the network and likeminded institutions promised to address the topics within their area of work and intellectuals/think tanks became ready to write their papers, with in return a minimal remuneration for stationary. ActionAid International Nepal financed the initiative and publication; and AAMN generated a small supporting fund. The efforts of many people delivered the book that is in your hand today. AAMN wants to make sure it continues its journey. On the road we are walking and where many individuals from foreign nations also walk together with us. In the meantime we want to accept the reality that the book may not be of the standard of your choice but we say proudly that it is better than the previous one. Similarly the challenge of improvement is always there so we promise for that. In this series AAMN is publishing another book as the first one reaches your hand. All together 35 papers were contributed to our study, and if compiled in one volume that would have been bulky and not user-friendly so we decided to make part two with thematic papers.

Personally AAMN expresses its sincere thanks and gratitude to the country director of ActionAid International Nepal Mr. Bimal Kumar Phnuyal whose regular suggestions and advices have enriched our study and the resulting book, similarly to Ganga Duttaa Awasthi, Dwarika Nath Dhungel, Dev Raj Dahal, and the entire team of AAMN. Jan Goossenaerts and Melody Smith, and the authors became strong pillars of our initiative. The continuous efforts of Prabhash Devkota in completing the complete task are highly recognized and AAMN expects his energetic efforts in future endeavors too.

Our special thanks go to all the other unseen hands that make it happen. Many authors have conducted focus group discussions, interviews and surveys - so all the respondents and participants are deeply thanked. Overall the contribution of Mr. Birkha Pun of AAMN became instrumental to make it happen.

Prof. Dr. Keshab Raj Khadka

Chair-person Alliance for Aid Monitor Nepal

November, 2013

Some words

Has ‘development aid’ worked for a developing country like Nepal to prosper; added value towards democratization of its governing institutions; contributed to empower the marginalized sections of its population; and, enabled to stand as a responsible member of the international community in the contemporary world? These are some of the most basic and pertinent questions to be deliberated upon in the present context of ‘Aid and Development’ discourse in Nepal. Experiences across the world show that any particular ‘aid-package’ in itself cannot be termed ‘good’ or ‘bad’, unless we evaluate the impacts of those aid packages in the light of above four questions. ActionAid, internationally, has been advocating for ‘Real Aid’, which can positively respond to above key questions, with the aim of progressively reducing ‘aid dependency’ on the part of developing countries; as well as engaging with bilateral and multilateral development agencies to devise transparent, accountable and effective aid governing mechanisms both at donor and host country level.

First of all, ‘development aid’ must be looked at from the perspective and spirit of ‘international cooperation’, rather than through the typical conventional lens of ‘donor-recipient’ charity attitude. The historical global level report prepared by the remarkable group of international statesmen and leaders led by Willy Brandt, the former German Chancellor, back in 1980, called “North-South: A Programme for Survival” had stated that “To help conquer poverty and hunger and to create a more just and a more effective international economic system, fundamental structural changes must be made in the markets in which developing countries are suppliers – of commodities, of manufacturers, of labour – and in which they are customers – for capital and technology”. The report also highlighted that such changes were also required in the mechanisms and institutions which generate and distribute international finance, investment and liquidity. It has been absolutely clear that “Aid is means, and not an end in itself”. A bad ‘aid-package’ even exacerbates the social, political and economic environment of a recipient country, at the same time giving bad experience to the resource providing agency or country. Therefore, there is a huge need for deeper deliberations on dominant models of aid mechanisms, development effectiveness of such aided projects, and their overall impacts amongst policy makers, international development partners, academics, civil society actors and social movements in the present context of Nepal. We hope that this publication will add some positive value towards that direction.

The book has tried to draw and analyze the linkage of aid within various aspects of people’s lives. The policy analysis and the evidences from grounded reality have been presented coherently which will be helpful to understand the macro and micro context of aid politics. An idea behind these efforts is of course to map out the given context, contribute to deepen the discourse on aid at different levels, and to explore more progressive modalities of aid paradigms. The chapters seem to have raised pertinent questions around aid effectiveness and democracy, politics of informal economy, culture of dependency, fiscal policy issues, poverty alleviation and contextual innovations etc. I hope, this will be a useful document for social thinkers, academia, policy makers and human rights activists in understanding the pros and cons of ongoing foreign-aided development practices.

We are very much thankful to expose the fact that, this is an outcome of constructive collaboration of ActionAid International Nepal (AAIN) and Alliance for Aid Monitor Nepal (AAMN) in grounding the aid discourse. AAMN has established itself as a vibrant common platform and resource organization on the aid sector. I would appreciate the efforts made by all the paper contributors who supported from equal footage in shaping articles for this book. My special gratitude goes to AAMN, especially to Mr. Prabhesh Devkota and his team, and also to Dr Keshav Khadka for his guidance and leadership to AAMN. I would

also like to convey my special thanks to all AAIN colleagues, especially to Mr. Govinda Prasad Acharya and team for their regular support and engagement. Finally, I would like to remember all those who have contributed from their respective capacities to make this great achievement.

Bimal Kumar Phnuyal

Country Director
ActionAid International Nepal

November, 2013

List of Abbreviations

AAA	Accra Agenda of Actions
ADB	Asian Development Bank
AIC	Akaike Information Criteria
AMP	Aid Management Platform
AMMAA	Agreement on Monitoring of the Management of Arms and Armed Personnel
APTA	Asia-Pacific Trade Agreement
BIMSTEC	Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation
BPfA	Beijing Platform for Action
CA	Constituent Assembly
CAC	Citizen Awareness Center
CASU	Constituent Assembly Support Unit
CRB	Central Revenue Board
CBOs	Community Based Organizations
CBS	Central Bureau of Statistics
CEDAW	Committee on the Elimination of Discrimination against Women
CFUGs	Community Forestry User Group
CIAA	Commission for Investigation of Abuse of Authority
CPN-UML	Communist Party of Nepal- United Marxist and Leninist
COFSUN	Community Forestry Supporter Networks Nepal
CPA	Comprehensive Peace Agreement
CSF	Countercyclical Support Fund
CSOs	Civil Society Organizations
DANIDA	Danish International Development Agency
DANIDA/HUGOU	Danish International Development Agency/Human Rights and Good Governance Advisory Unit
DC	District Council
DDC	District Development Committee
DDP	District Development Plan
DFID	Department for International Development
DIMC	Decentralization Implementation Monitoring Committee
DOF	Department of Forests
DPs	Development Partners
EC	European Commission
EFA	Education for All
EPZ	Export Promotion Zones
ESCAP	United Nations Economic and Social Commission for Asia and the Pacific
ESP	Enabling State Programme
EU	European Union
FA	Foreign Aid
FACD	Foreign Aid Co-ordination Division
FAO	Food and Agriculture Organization of the United Nations
FECOFUN	Federation of Community Forestry Users Nepal
FDI	Foreign Direct Investment
FSSS	Financial Sector Strategy Statement
FY	Fiscal Year
GAAP	Governance Accountability Action Plan
GCF	Gross Capital Formation

GESI	Gender Equality and Social Inclusion Policy
GDP	Gross Domestic Product
GNI	Gross National Income
GON	Government of Nepal
GRP	Governance Reform Programme
HCR	Head Count Ratio
HKH	Hindu Kush Himalaya
ICA	Investment Climate Assessment
ICOR	Incremental Capital Output Ratio
IDA	International Development Assistance
IFAD	International Fund for Agricultural Development
IFC	International Financial Cooperation
IGEG	Inter-Governmental Expert Group
IIDEA	International Institute for Democratic and Electoral Assistance
ILO	International Labour Organization
IMF	International Monetary Fund
INGOs	International Non Governmental Organizations
IPCs	Integrated Planning Committees
IPL	Income Poverty Line
IPFC	Integrated Plan Formulation Committee
ISN	Interim Strategy Note
JICA	Japan International Cooperation Agency
LGCDP	Local Governance and Community Development Programme
LGBs	Local Governance Bodies
LGP	Local Governance Programme
LSGA	Local Self Governance Act
LSGR	Local Self Governance Rule
MC	Municipal Council
MC	Management Committee
MDGs	Millennium Development Goals
MoAC	Ministry of Agriculture and Cooperatives
MoF	Ministry of Finance
MoFALD	Ministry of Federal Affairs and Local Development
MoWR	Ministry of Water Resources
MPFS	Master Plan for the Forestry Sector
MTEF	Medium Term Expenditure Framework
NAG	Nepal Aid Group
NC	Nepali Congress
NDF	Nepal Development Forum
NDCM	Nepal Donor Consultation Meeting
NEFIN	Nepal Federation of Indigenous Nationalities
NGOs	Non Governmental Organizations
NORAD	Norwegian Agency for Development Cooperation
NPC	National Planning Commission
NPL	National Poverty Line
NRB	Nepal Rastra Bank
ODA	Official Development Assistance
OECD-DAC	Organization for Economic Co-operation and Development- Development Assistance Committee
OGA	Office of the Auditor General
OPEC	Organization of the Petroleum Exporting Countries
PD	Paris Declaration on Aid Effectiveness
PDS	Peace and Development Strategy
PDDP	Participatory District Development Programme

PERC	Public Expenditure Review Commission
PMO	Prime Minister's Office
PPP	Public Private Partnership
PRGF	Poverty Reduction Growth Facility
PRSC	Poverty Reduction Support Credit
PRSP	Poverty Reduction Strategy Paper
PSC	Public Service Commission
REFLECT	Regenerated Freirean Literacy through Empowering Community Technique
ROSA	Rest of South Asia
SAARC	South Asian Association for Regional Cooperation
SAB	South Asian Bank
SAFTA	South Asian Free Trade Area
SDC	Swiss Agency for Development and Cooperation
SDF	SAARC Development Fund
SDGs	Sustainable Development Goals
SEZs	Special Economic Zones
SMEs	Small and Medium Enterprises
SNV	Netherlands Development Organization
SWAPs	Sector-Wide Approaches
TA	Technical Assistance
TER	Tax Effort Ratio
TYIP	Three Year Interim Plan
TYIDP	Three Year Interim Development Plan
UCPN-Maoist	United Communist Party of Nepal-Maoist
UC	User's Committee
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
UNESCO	United Nations Educational, Scientific and Cultural Organization
UNFPA	United Nations Population Fund
UNMIN	United Nations Mission in Nepal
UNS	United Nations Systems
UNSCR	United Nations Security Council Resolution
WCF	Ward Citizen Forum
VAT	Value Added Tax
VCDP	Vulnerable Communities Development Programme
VDC	Village Development Committee
VLCF	Village Level Citizen Forum
WB	World Bank
WFS	World Food Summit
WHO	World Health Organization
WTO	World Trade Organization

Introduction

In the political and development climate that Nepal currently experiences, an in-depth analysis of the political economy of the country can make a valuable contribution. If policymakers and development planners hope to meet the expectations of the Nepalese citizens they will need to understand the problems and their causes as fully as possible. Democracy and development failures have been very common in countries that have gone through major political conflicts and governance transitions and are ethnically rich and diverse. Being land-locked also implies particular challenges as a country wishes to join the global economy.

The June 2013 Nepal Democracy Survey jointly conducted by the Nepal chapter of State of Democracy in South Asia, and International Institute for Democracy and Electoral Assistance (Sweden) shows that respondents overwhelmingly (94%) approved of a system of government led by the people's elected representatives, yet they have a certain level of frustration and disillusionment due to the expiration of the Constituent Assembly (CA) without promulgating a new constitution and due to the present state of state of affairs which is perceived as 'undemocratic' by 47% of the respondents. Other favorable signals from the survey include (i) the respondents' understanding of democracy, their awareness of the major national agendas and their participation in public affairs; (ii) the perceived improvement in the condition of the excluded groups (acknowledged by 72% of the surveyed citizens) with an overwhelming majority (80–98%) of citizens surveyed listing women, Dalits, Janajatis, Madheshis and Muslims, along with people from backward regions as groups deserving preferential treatment from the government; and (iii) the attitudes towards identity, state restructuring, federalism and governance, where opinions on dividing topics show more convergence and less division than in the 2007 survey.

For several reasons these favorable signals should not make donors, policy makers and the elected representatives complacent.

Regarding the institutional foundations of a democratic Nepal the CA-II is likely to address the constitution drafting in a more favorable climate as also political parties are more committed to multi-party competition and accepted democratic values and norms, and as polarized opinions and expectations on solving all problems simply by restructuring the state and introducing federalism have slowly made room for a more realistic and multi-faceted agenda for discussion. On the other hand the challenge to draft a constitution amidst the various forces, democracy gaps and issues remains an enormous challenge.

Only after the constitutional question has been resolved, empowered and legitimate national government and local government units can fully dedicate themselves to addressing the most important national and local problems regarding basic amenities essential to meet family needs (most important local: 81%; national: 43%) and economic issues (local: 10%; national: 32%). The June 2013 Nepal Democracy Survey shows that respondents of the survey have high expectations regarding the family needs that government should address: employment (most important for 21%; highest rate by Madheshi community: 26%; and highly educated: 25%), water (19%; senior 60+: 25%, Pahadi: 23%), roads (18%; Madheshi ethnicity: 22%; Madheshi community: 21%), education (16%; highly educated: 22%; Madheshi: 21%), electricity (13%; excluded groups: 14%) and health care (13%; highly educated: 16% and women: 14%).

For delivering on these expectations, the Government of Nepal will continue to need foreign aid. And that foreign aid will have to meet effectiveness criteria to the fullest extent.

Alongside having delivered many genuine contributions to Nepal's development, many of these are also acknowledged in the papers of this volume, foreign aid has also failed in many instances, with reduced

effectiveness as a result. Several trends of the past decades must be reviewed by donors. Democracy and aid failures may result from a variety of interacting factors. When conducting their next aid-effectiveness review, policy makers and donors need to understand problems as fully as possible and discover the root-causes that underlie those problems and the mechanisms that feed vicious circles draining development resources.

Before introducing the themes addressed by the contributors to this volume, let us first note that foreign aid's impact on the development of democracy in recipient countries is generally difficult to achieve. The key policy messages of (OECD Development Assistance Committee, 2011) start by stating that: *"There is increasing recognition that much of this support (donors spending over \$10 billion annually on governance support of which accountability is a common component) has made inaccurate assumptions about the nature of democratic and institutional transitions. This has translated into commitments to Western models and technical approaches that use blueprints, templates and best practice approaches"*.

Context and evidence

Each paper in this volume has been written by a close observer of foreign aid and/or democracy in Nepal and makes a contribution to the in-depth understanding of a theme.

Together the papers address background, evidence and recommendations via varying themes. Well aware of their area of expertise, and the piecemeal bit of evidence each can bring to the "foreign aid and democracy problem solving" mission, the contributors have avoided the "prescription before diagnosis" trap, and rather have proposed recommendations on the basis of the evidence they have presented in their papers.

Using the metaphor of a puzzle, it is not surprising that these pieces do not fit together neatly. Yet, any reader of this volume, and anyone interested in a peaceful and prosperous future of Nepal may like to know which institutional decisions of the forthcoming legislature, and which foreign aid decisions by donors would best (i) reflect awareness of the integral evidence and (ii) take into consideration the integral recommendations put forward by experts and observers.

To facilitate such a wish for comprehension we have made an effort to fit the pieces together as well as we could within the little time available, and indicate in which paper is which evidence and which kind of recommendations. In this introduction, for the clarity of the emerging collaborative diagnostic and prescriptive hypotheses we have separated the diagnosis-related evidence from the prescription-related recommendations. After all, each paper will bring its own train of reasoning connecting both aspects. Contradictions in the evidence would indicate errors, and these should be corrected. Where recommendations diverge, decision makers and donors should further analyze the supporting evidence and the issues at hand. Even convergent recommendations should be handled with care, yet very strong arguments had better be present when putting these aside.

We have ordered papers in accordance with their thematic focus or the major area of evidence they address.

On the Historical and political context of foreign aid to Nepal

A first set of papers address the historical and political context of foreign aid to Nepal

In "Aid and Democracy in Nepal," Himalay Shumsher J.B. Rana, a long retired senior governance and development practitioner, offers a general and succinct description of the results of multilateral and bilateral technical assistance to Nepal. He challenges the Nepalese administrators to channel foreign aid to the development of Nepal, which is sustainable and protective of the country's deteriorating environment.

In “Aid Politics and Democracy,” Bharat Pokharel draws together observations and conclusions from the realms of development studies, political science, international relations and economics concerning the roles of foreign aid in politics. The author concludes that Nepal’s foreign aid policies need to be put into the perspective provided by the aid practices, both past and present, of Western industrialized nations, as well as the context of Nepal’s own domestic political forces.

In “Challenges of State Building and the consequences of External forces in Nepal,” Chandra D. Bhatta explains and analyzes internal and external factors that are at the origin of a current political process that seems incapable to bridge the “sovereignty gap, the authority gap, and the legitimacy gap” in post-conflict Nepal.

In “Poverty alleviation Status in South Asia during 1990-2015 and options,” Y B Thappa, a former member of the National Planning Commission of Nepal, compares the poverty trends in Nepal with those in other South Asian countries. The paper offers an assessment of the Millennium Development Goals (MDGs) and the the SAARC Development Goals (SDGs) indicators’ livelihood pillars. Then it turns to the member-states’ approaches to economic growth and their inclusive development activities. The study concludes with some methods to augment the regional resources, products and services for achieving targets of poverty alleviation, economic growth and endowment enrichment.

Democratic institutions at the local level

Two papers focus on the experience with democratic institutions at the local level. This experience may offer a partial explanation for the high rates of respondents’ understanding of democracy, their awareness of the major national agendas and their participation in public affairs as observed in the 2013 Nepal Democracy Survey.

In “Deepening Democracy at the local level” Dwarika Nath Dhungel, Mahendra Raj Sapkota and Pradyumna Prasad Regmi describe the working of the local governance bodies that have been very familiar for the Nepalese people for more than five decades: the Village Development Committee (VDC) in rural areas, the municipalities in urban areas, and the District Development Committee at the district level.

In “Community forestry: A model of grassroots democracy - Nepal’s own innovation and the role of development aid” Bharat K Pokharel provides an analysis of Nepal’s community forestry at the grassroots level from which one can learn the concepts, processes, methods and tools related to local democracy for resource governance. The paper describes some opportunities to transform Nepali society by capitalising the best practices of community level democracy.

Evaluating the contribution of foreign aid to democracy in Nepal

Many of the papers in this volume provided evidence and analysis regarding the contribution of foreign aid to democracy in Nepal.

As an input for a diagnostic hypothesis regarding which aspects of foreign aid need improvement in order to put in motion the virtuous circles of inclusive development and democracy in Nepal, we summarize analysis and evidence from the papers by classifying it with respect to these four “consensus” common principles:

- **Focus on results:** public sector and development investments and efforts must have a lasting impact on eradicating poverty and reducing inequality, on sustainable development, and on enhancing developing countries’ capacities, aligned with the priorities and policies of developing countries themselves. Under this heading we also pay attention to failures and to undesired effects of foreign aid.

- **Inclusive development partnerships:** Openness, trust, and mutual respect and learning lie at the core of effective partnerships in support of development goals, recognising the different and complementary roles of all actors.
- **Ownership of development priorities by the target constituency:** Partnerships for development are much more likely to succeed if they are led by the target constituency, reflecting their collective value orientations, and implementing approaches that are tailored to country-specific situations and needs.
- **Transparency and accountability to each other:** Mutual accountability and accountability to the intended beneficiaries of our co-operation, as well as to our respective citizens, organisations, constituents and shareholders, is critical to delivering results. Transparent practices form the basis for enhanced accountability.

Failures, undesired effects and results

Failures

In his paper “External forces and international cooperation in the context of current constitutional instability and development in Nepal” Ganesh Dutta Bhatta summarizes the history of constitutional law in Nepal before describing the failure of the Constitution assembly and a constitution drafting process in which major international interests were involved directly or indirectly. The author offers a detailed analysis of the weaknesses in the mobilization of international aid in this failed constitution drafting process.

Uddhab Pyakurel in “Foreign Aid in Nepal’s Democracy Struggle” mentions that a Finance Ministry official admitted recently that there had been no progress in enforcing international aid guidelines. Though international agreements made by donors were aimed at making foreign aid more efficient, coordinated, and effective through increased donor engagement with government agencies, parliament, and civil society, the author calls it unfortunate that no one witnesses a ray of hope in Nepal.

Devraj Dahal in “Politics of Informal Economy” indicates that in the context of growing youth population, declining public budget, rural push of poverty and foreign pull of opportunity, the Nepalese state often lagged in providing a supportive policy framework for their productive employment. Naturally, this population has to engage in informal sectors. Informal sector continues to grow in direct proportion to the decline of formal economy owing to the elites interest in privatization and denationalization of industries and de-regulation import laws, negative effects of the global economic crisis, protracted political instability and the democratic deficits in the country.

In “Fiscal Policy Issues in Nepal,” Madan Kumar Dahal describes the fiscal situation in Nepal and compares it with that in other South Asian countries. He then addresses the major problems in Nepal’s fiscal policy including the poor implementation of revenue policies, an extremely limited tax base due to erosion in the legal based and the numerous tax shelters, huge leakages in tax collection due to a lack of transparency and simplicity in procedures; and the lack of computerized tax systems, records of property (land and building) and business transactions with the Inland Revenue Department.

Undesired effects

Meena Vaidya Malla in “Foreign Aid and Democratization in Nepal: Culture of Dependency” addresses the culture of economic and psychological dependency that Foreign Aid has induced in Nepal: Nepal’s historical economic dependency on foreign aid has now transcended into the social and political aspects: the political actors substantively interact with and depend more upon the donors than their domestic constituency. The donors have bypassed the state sovereignty in policy decisions in the name of engaging civil society and grassroots organizations. The dependency thus imbues governance with the values of

status quo and, consequently, makes it unresponsive to citizens' concern. If this situation continues, the condition of nation and citizens are sure to worsen and political culture and behaviour to suit the present democratic polity hardly develops.

Kashi Raj Dahal, in "A strong legal regime, a necessity for the effectiveness of foreign aid" first summarizes observations from international experts who are critical about the effectiveness of foreign aid in many receiving countries. The latter are often getting poorer and poorer in spite of receiving more foreign aid. This is also the situation in Nepal which has a low capacity to utilize the aid it receives. A lasting impact on eradicating poverty and reducing inequality is unlikely as political interference and corruption have severely debilitated the poverty relief efforts in Nepal. Another results-eroding factor is that donor countries and INGOs provide assistance based on their vested interest, which do not necessarily coincide with the sovereignty, integrity, national interest, and the greater welfare of the people.

Results, but...

Govind Prasad Kusum in "Foreign Aid and Democracy" addresses the donor communities' role in establishing peace and restoring public properties in post conflict Nepal. He notes that the promotion of economic growth and the reduction of poverty is only partially successful due to the poor performance of the country's bureaucracy and corruption.

Sohan Kumar Karna in "Foreign Aid: a hot button issue" gives a detailed overview of the impact of foreign aid on the Nepalese economy, the magnitude and trend over the past decades of grants and loans, the evolution of foreign aid commitment and disbursement, and a sector wise composition of foreign aid. He notes that almost all the highways and communication networks, public industrial enterprises, agricultural and rural development projects, and development institutions are the result of foreign aid.

In "Does Foreign Aid cause Gross Domestic Product? Empirical evidence" Kamal Raj Dhungel describes the fiscal policy trap in which poverty leads to low public investments and low public investments reinforce poverty. At the beginning, aid in the form of grants played an important role in the construction of infrastructure projects and establishment of some of the key basic industries. But foreign assistance in the form of grants has been changing over time. Grant at large is being replaced by loans as bilateral donors are gradually changing into multilateral. In this context, the author investigates the causal relationship between GDP and foreign aid in the short and long run. After the peace process started in 2006, Nepal has received more foreign aid than ever. Unfortunately the foreign aid has not been utilized in any of development activities but rather in solving political disagreements. This has led to a lack of opportunities in the country. Businesses hesitate to invest as the future is uncertain and the risk is high. The author concludes that more than anything the country needs stability. Aid that is not delivering this, as more aid implies greater economic imbalance and higher debt, is not working for Nepal. Without prosperity from economic activities it is impossible to achieve growth. Foreign aid (in its past forms) is not the answer to the growth of Nepal.

Research in 2011 about the Efficiency of Development Actors in Good Governance by Ganesh P. Adhikari and Prabhash Devkota is reported about in "Donor Obligation for Public Sector Reform in Nepal." It shows that respondents considered local authorities as the best performer and donors as the least performer in demonstrating good governance. The lowest level of donor efficiency indirectly indicates that turn-key projects executed by donor agencies are not effective in terms of good governance, particularly from the recipient's perspective.

Inclusive development partnerships

Meena Vaidya Malla in "Foreign Aid and Democratization in Nepal: Culture of Dependency" laments that a large number of populations are economically, socially and politically excluded from the mainstream of development. They have physically participated in political and development process but neither they

are able to put their view nor are their voices heard. Periodic development plans spanning a period of six decades have failed to make a significant change in the living standard of people. Over the past decade, the inequality between rich and poor has increased considerably. Any country whose democracy is installed without acquiring economic prosperity is likely to risk falling prey to its enemies, the worst being increasing poverty and decreasing participation.

Uddhab Pyakurel in “Foreign Aid in Nepal’s Democracy Struggle” indicates that in spite of Nepal being one of the most agriculture-dominated economies in Asia, the agriculture and rural sector continue to be neglected by the government. The vulnerability and rising poverty levels are worst in the more remote areas where development efforts have been ineffective or nonexistent. Owing to low productivity and the deteriorating rural economy coupled with lack of employment, Nepalese people increasingly depend on remittances from relatives working abroad. The dependency on development aid is because of the country’s inability to raise sufficient domestic revenue and because of a lack of necessary resources, especially its incapacity in harnessing its natural resources.

Devraj Dahal in “Politics of Informal Economy” raises that the informal economy is the biggest employer of the Nepal’s workforce, yet it is deliberately excluded from statistical monitoring, protection and regulation by the state authorities. This exposes the informal sectors and their workforce to multidimensional vulnerabilities to the abuse of their rights, absence of entitlements, remuneration, paid leisure, maternity leave, health and safety, pension and adequate living wage for sustainable livelihood. This author writes about the “urban bias” in development policies and resource allocation of the donors, the state, employers and even labor unions as development is seen until recently as improved economic growth, not the amelioration of structural injustice through liberation, entitlements and fairer justice for individuals, communities and the state.

Ownership of development priorities by the target constituency

In “Community forestry: A model of grassroot democracy - Nepal’s own innovation and the role of development aid” Bharat K Pokharel recognizes that the encounter between change agents and traditional forces, social structure and feudal organisational culture tends to hinder the change process that is taking place in terms of the practice of sustainable management of forest resources, inclusive, pro-poor and gender responsive forest governance at the grassroot level. Although community forestry is a model of grassroot democracy and local governance, a foundation for the transformation of Nepali society from the bottom, it faces many challenges because it has to operate within the forestry sector, the larger government’s bureaucratic set up and within a difficult national context of unstable transitional political environment and feudal social structure.

In “Deepening Democracy at the local level” Dwarika Nath Dhungel, Mahendra Raj Sapkota and Pradyumna Prasad Regmi describe the activities related to demand-strengthening and citizen empowerment, especially the marginalized sections of the society in the planning process of the LGBs, are the important components of this program. The Ward Citizen Forum (WCF) and the Citizen Awareness Center (CAC) are institutional arrangements made at the VDC and Municipality under this component. The WCF and CAC have been dealt with in the context of the planning process of the LGBs.

Govind Prasad Kusum in “Foreign Aid and Democracy” raises (i) that the democratic system is too weak to handle the modalities of aid, a situation which creates comforts for corruption and fraudulence; and (ii) Aid conditionalities reduce the space for national political decision making and its proper implementation; and (iii) the ineffective monitoring system of the Government creates a congenial environment to the INGOs to play with policy lacunas.

In “Aid Effectiveness and Country Ownership: Need of Democratic Governance in Nepal” Vidyadhar Mallik focuses on the origin of this principle and how it has been addressed in Nepal’s foreign aid

policy. Surveys conducted in the context of the monitoring of the Paris Declaration show limited progress in Nepal and highlight major challenges in aid effectiveness. The author describes the impact on development effectiveness and public financial management and corruption of the present situation in Nepal without elected institutions, and without properly working accountability structures and judiciary.

Tara Dahal in “Civil Society as a Democracy-Building Project in Nepal” claims that the bulk of Nepalese civil societies bear the potential to carry out an impulse of virtuous society to democratize, civilize and reduce social, economic and political gaps across various sections of people through righteous public action. The plurality of civil society in Nepal reflects the diversity of Nepalese societies’ needs and conditions and, therefore, multi-dimensional level of action from advocacy, education, communication to relief, livelihood, rehabilitation and relationship-building measures. Yet, owing to the inability of the Nepali state to enforce security, the rule of law and protect the rights of citizens, the international donor community treats it as a fragile state and designed its aid policies accordingly.

Meena Acharya in “Democracy and Foreign Aid – disconnect between democratic aspirations and free-market policy prescription” answers four questions in the context of 60 years of Nepal’s political history since 1951. To the question whether the volume of foreign aid changed with the system of governance in the country, the answer is that available information does not show any such connection. On the questions whether the institutional and policy packages that accompanied the aid flow were democratically discussed, their fitness and sustainability evaluated in the specific country context, and whether the aid packages and the policy recommendations matched the needs and aspiration of the people in the country, the answer is that until about the late 1990s, foreign aid packages were rarely contextualized to Nepal’s political or economic realities, nor did they match the needs and aspirations of the people. The answer to the question whether the economic packages introduced were discussed by the political representatives and voted by the people in Nepal is that until the late 1990’s these were not discussed or voted by the people or by their political representatives. Though the situation has started to change with MDGs, PRSP, and Aid Effectiveness Agenda, the policies and programs are still based on the assumption of the primary role of the private sector as the engine of growth, and an unsustainable model of capitalist or social democratic models, which themselves are facing multiple crises.

Transparency and accountability to each other

Govind Prasad Kusum in “Foreign Aid and Democracy” contrasts the external and internal, hidden, intention of donors and laments that the latter threatens the security and weakens the governments of developing countries, including Nepal.

Vidyadhar Mallik conjectures that any efforts by the development partners (donors) for capacity building or supply side strengthening ultimately support and strengthen only petty interests of unaccountable bureaucrats and hand-picked politicians while fear of investments in demand side/voice mobilization with grass-root level communities constantly keep weakening the initiatives of community organizations and that of civil society.

The Way forward

The survey on the impact of foreign aid on democracy in Nepal by the editors of this volume was based on the contents of OECD DAC studies on the topic. The survey results show that respondents were rather supportive of the range of topics that were proposed as enablers for democratic and institutional transitions:

- Make support to the accountability system long-term

- Promote citizen access to media and mobile technologies as well as citizens' media literacy
- Ensure that accountability support efforts strengthen the parliament
- Ensuring local ownership of development aid projects
- Ensure that accountability support efforts complement one another
- Encourage links between media institutions and the rest of civil society
- Support independent, sustainable, and capable local media
- Technical assistance to political parties
- International elections assistance

Our authors go a long way in translating these rather generic propositions into more concrete recommendations.

Democratic values

The below key recommendations should be considered as inputs for a prescriptive hypothesis for improving the contribution of foreign aid to democracy in Nepal.

The Ward Citizen Forum (WCF) and the Citizen Awareness Center (CAC) described in Dhungel's paper are institutional arrangements made at the VDC and Municipality that should be further strengthened in an approach to more inclusive determination of development priorities. Nearly all Nepalese people are familiar with their local governance bodies.

In "Community forestry: A model of grassroots democracy - Nepal's own innovation and the role of development aid" Bharat K Pokharel proposes the community forestry institutions as a model of grassroots democracy and local governance, a foundation for the transformation of Nepali society from the bottom. Here society has experience with the encounter between change agents and traditional forces, social structure and feudal organisational culture, and this experience has yielded champions which could support replicating the experience in other areas of the Nepalese society.

Vidyadhar Mallik calls for two compacts guided by the principles of a democratically owned 'peace and development' strategy:

- a first one between the government of Nepal and society at large represented by plethora of civil society organizations, intelligentsia, media, NGOs, local governments, community organizations like Ward Citizen Forums (WCFs) and Community Awareness Centers (CACs), PAF – COs, local peace committees, forestry user groups, irrigation user groups, school and hospital management committees, rights bodies, human rights institutions, women and children organizations and their associations/federations; and
- a second one between the development partners/donors and the government of Nepal.

In the present transition, development partners/donors should encourage, engage and actively support (with enough funding and capacity building) dialogues and deliberations between the government and society at large, including community based grass-root institutions: the fear of 'demand mobilization' should give way to more such exercise for voice and choice mobilization of communities till the elections of local and national governments are held and Nepal stabilizes with a new popular constitution.

Govind Prasad Kusum calls upon political groups to work for the underpinnings of democracy in a cohesive manner.

Institutional foundations

Devraj Dahal in “Politics of Informal Economy” raises that there is a need to bridge the gap between development theory and contextual knowledge and its outcome for human development.

Tara Dahal in “Civil Society as a Democracy-Building Project in Nepal” request civil society to create the favorable conditions for Nepal’s society and the state to adapt to universalistic norms and act to abolish the tradeoff between political power where leaders indulge in life-and-death-struggle and democratic values that moderate their appetites to move to extreme directions incubating the source of violence and vicious conflicts.

Specifically for the constitution drafting process Ganesh Dutta Bhatta calls for a proper evaluation of all the weaknesses of the past constitution assembly and the formulation of policies and guidelines that help the foreign aid for the drafting of a future constitution become more transparent, effective and accountable. He calls for being cautious for those people and organizations that might again be active to grab the international aid and use it against the Nepal’s dream of creating a democratic constitution through elected members from the constituent assembly.

In “Fiscal Policy Issues in Nepal,” Madan Kumar Dahal describes a strategy for taxation with the purpose to speed up reforms in the tax system and improve the tax administration ensuring a competitive tax structure primarily to attract FDI for sustaining a high level of economic growth, and promote indigenous investment in cooperation with private sector for reducing absolute poverty. His paper contains detailed reform recommendations.

Govind Prasad Kusum advices the Government of Nepal to send skilled negotiators to foreign aid negotiations, they must take care of how far the conditionalities are compatible with the national interest. If the terms and conditions set forth by donors are against the public interest, against government policy and against national security, such aid must be rejected.

The government should have a master plan on how the country can be sustained financially and economically.

Involve the informal and private sector

Devraj Dahal in “Politics of Informal Economy” calls for an inclusion of the informal sector. He conjectures that a sustainable solution of the problem of informal sector lies in the legislation of proper laws, building of participatory culture whereby societal interests prevail over private greed and gain, reinvesting of economic surplus on production process, promotion of subcontracting with intermediary and large business, strengthening of inter-sectoral linkages, legal protection and encouragement of workers to become shareholders of the business enterprise and low-cost cooperatives.

Sohan Kumar Karna in “Foreign Aid: a hot button issue” emphasizes several challenges both for donors and recipients. In spite of reported huge aid inflows, there remains a large gap between the need and aid availability due to mis-targeting, emergency situations, aid diplomacy and unfair trade. Donors’ political and economic interests coupled with their disharmonising aid policies have made aid inadequate, inefficient and ineffective. But provided the recipients ensure good governance, aid has immense potentiality. Nepal’s absorptive capability should be strengthened beyond the government by involving the private sector.

Ever since the government began to receive aid, the capacity to utilize the committed amount of aid productively continues to remain as a crucial problem. This shows low absorptive capacity resulted in political instability, lack of commitment of ruling authorities, bureaucratic delays and absence

of institutionalization of development administration, corruption and lack of proper management of development projects.

Also Uddhab Pyakurel in “Foreign Aid in Nepal’s Democracy Struggle” points at the inability to utilize aid as the key obstacle in addressing people’s expectations for a better life through aid-oriented priority projects. Encouraging the private sector to handle foreign aid resources, with the government functioning as a facilitator, may bring about an increase in the efficiency of foreign aid. This would increase the efficiency of aid disbursement by reducing the tendency of aid to strengthen the government sector and curbing the government behaviour of using foreign aid to pursue socially non optimal agenda. The government should streamline its institutions, prepare personnel (both through training of its staff and through spending in the social sector to equip the population in providing skilled manpower), ensure an open environment for entrepreneurship and commit itself to maintaining a healthy economic climate. Such actions that strengthen the private sector and bolster macroeconomic management will not only pay dividends in an increased willingness of the donor countries to disburse more capital in the form of foreign aid, but also increase the effectiveness of the institutions and process that determine the efficiency of foreign aid already disbursed.

Priorities and the role of foreign aid

Research about the necessity of donor-support for various issues of democratic governance by Ganesh P. Adhikari and Prabhash Devkota shows a top three of strengthening local authority strengthening civil society organizations, and controlling corruption. As to the kind of donor-support that is appropriate for civil service reform in these areas, when given the options policy advice, financial support and technical assistance. More than fifty percent of respondents were in favor of each of the three kinds of donor-support for corruption control (56.9%, 57.3% and 50.2%). In the case of strengthening local authority and citizen-centered service delivery, nearly 83 and 69 percent respondents respectively were in favor of financial support.

Meena Vaidya Malla in “Foreign Aid and Democratization in Nepal: Culture of Dependency” concludes that aid, should, primarily be used as catalyst-sometimes to help generate other resources or gain access to them-sometimes to help create domestic capacity or manage conflicts resulting from various forms of unsustainable development. At this juncture, what is required is special focus on aid policy which creates social harmony, political stability and peace-the preconditions for democratization in Nepal.

The role of donors

Govind Prasad Kusum calls upon donors to take into consideration the country’s vulnerable situation, and pay greater attention to the myriad factors that contribute to and underpin transition, and even more complicated, consolidation. The country needs a huge amount of resources to achieve poverty reduction alongside democracy strengthening by investing in people’s health, education, food and infrastructure, including in rural areas as was also confirmed in the June 2013 Nepal Democracy Survey.

Meena Acharya in “Democracy and Foreign Aid – disconnect between democratic aspirations and free-market policy prescription” calls for the adoption of a more holistic economic model, which takes into account both market and non-market activities, is socially more sensitive and is based on environmentally more sustainable resource use.

Further refinement of diagnostic and prescriptive hypotheses

We conclude our introductory chapter with the hope that this volume will provoke further analysis in support of sound and responsive decision making and aid delivery that better meets the consensus common principles of effective aid, in Nepal and in other countries in transition.

This book is published both in print form in Nepal, and as an e-book via leanpub for readers around the world.

We welcome our reader's views and comments on the papers and on this introduction. These can be sent to us directly, or posted on the social media platforms. Using Spundge we will curate comments or links posted on Google+, Facebook, Twitter and other social platforms if they are tagged with #nepalmaprajatantra (Democracy in Nepal) or #nepalmabaidesiksahayog (Foreign Aid in Nepal)

On the basis of those comments, and additional canvassing of the related literature and evidence we hope to review and strengthen the diagnostic hypothesis and the derived recommendations. Also we want to hear from you if you have implemented recommendations, and with what effect.

Prabhash Devkota

Jan Goossenaerts

1. Aid and Democracy in Nepal

Himalaya SJB Rana

Internationally, aid for strengthening and sustaining democracy commenced after the end of the Second World War with the Marshall Plan for the reconstruction of Europe. Establishment of the International Bank for Reconstruction and Development (later known as the World Bank), the International Monetary Fund and subsequently the Asian Development Bank followed soon after. As a complementary measure, United Nations and Specialized Agencies launched technical assistance/cooperation programmes for capacity and institution building in developing countries, later venturing into pre-investment assistance. Side by side, bilateral aid programmes like USAID were launched in many developing countries like Nepal. Foreign aid appeared in the development scenario of Nepal after the advent of democracy in February 1951.

My active involvement in the governance of Nepal has been mainly in the financial sector as the first Finance Secretary and the first Governor of the Nepal Rastra Bank (Central Bank) for altogether some ten years in the 1950s. Then, for some twenty-four years I worked in the development sector of the United Nations in numerous capacities including Resident Representative of the United Nations Development Programme in three countries. I retired from UN service in 1986, some twenty-seven years back. I regard myself as a date expired development practitioner. As such, my short piece on the subject will be of a general nature unlike scholastic articles focusing on different facets of aid in Nepal contributed by eminent authors.

In my view Nepal's non-alignment policy and international relations did not influence Nepali politics and infrastructure development, as foreign aid was received both from the First World and Second World countries. Sir Ivor Jennings then mainly drafted the constitution promulgated and accepted by all democratic political parties. The Westminster Model recommended by him was in many respects similar to the model enshrined in the constitution of India. As far as I know the Government of India was consulted, but there was no pressure from the South on the salient features of the King Mahendra Constitution.

Multilateral and bilateral technical assistance to Nepal have greatly contributed to laying an appropriate foundation for and improving the governance in Nepal in tune with democracy. During the last six decades, hundreds of Nepalese administrators and technicians have participated in observation and training programmes in developed countries. Due credit has not been given by the development rapporteurs to the notable result that Nepalese administrators and technicians are now capable to conceive, plan and implement projects and programs and deliver good governance to people as well as their counterparts in the neighboring countries.

Concurrently, grants and concessional loans from multilateral development banks and friendly countries for infrastructure and other projects during sixty years have immensely facilitated the growth of the country's economy. Initially, quite a few factories were assembled and some arterial highways were constructed under the aegis of the Russian, Chinese, Swiss and Indian bilateral aid at a notably low cost. Then followed numerous projects in the power, telecom, industry and other sectors funded by the World Bank, ADB, Japanese, German and other bilateral aid. The cost of implementing these projects tended to be high not only due to the comparatively high remuneration and payments made to the foreign consultants and contractors but also to the Nepalese commission agents – a new breed that emerged and has been growing and thriving. The latter development is one dark spot in the annals of aid to Nepal.

Indian-Chinese relations have moved from adversarial to negotiating mode. USA, as the number one donor, promoting democracy in order to contain communism, delivered massive aid to Nepal from the fifties to mid-seventies in various sectors. Their interest in Nepal then flagged and revived as a component of countering terrorism. The USSR delivered sizable aid to Nepal in the fifties and sixties following the state visit of King Mahendra, as counterpart to aid from USA. However, the USSR was unable to continue matching aid from USA in the years that followed.

After the re-instatement of multi-party democracy in Nepal, aid to the social sector from INGOs has remarkably increased. Their role in highlighting the need of greater equity and inclusiveness in the Nepalese society is welcome. However, there are complaints that their unbridled activities have promoted ethnic divisions and unrest in Nepalese society. As such, their role should be monitored by the Government in the interest of national amity.

For decades, foreign aid focused on infrastructure development, augmenting agricultural and industrial production and capacity and institution building. Of late, protection of environment has appeared as one of the main concerns. It is high time that the sociological impact should also be taken into consideration.

I do not agree with commentaries tended to regard aid as evil. Foreign aid became donor driven to some extent and unwittingly fostered a new breed of commission agents, not to speak of the lordly living style of aid officials, both foreign and national. If the recipient government has well defined national priorities and manages to channel aid to such priorities foreign aid can make a yeoman's contribution to socio-economic development of the country. Certainly, most countries can survive without foreign aid like North Korea. But socio-economic growth will be accelerated with judicious utilization of foreign aid.

In conclusion I would say that foreign aid makes significant contribution to the socio-economic development of a country where development programmes are clearly chalked out and aid is channeled to such programmes. The challenge to our administrators is to channel foreign aid to development of Nepal, which is sustainable and protective of our deteriorating environment.

2. Politics of Informal Economy in Nepal

Dev Raj Dahal

2.1 Introduction

Informal economy has become a source of income for economically active poor many developing countries and Nepal. Informal economy involves those economic transactions that are not fully accounted, protected and regulated by the state authorities. This deliberate exclusion exposes informal sectors and their workforce to multidimensional vulnerabilities to the abuse of their rights, absence of entitlement, remuneration, paid leisure, maternity leave, health and safety, pension and adequate living wage for sustainable livelihood though this sector is the biggest employer of the nation's workforce. The labor-capital ties in informal sector, except in the cases of those run by family members, are beleaguered by one-way dependency of workers and decision-making by the owner of capital and enterprise. For migrant Nepalese working abroad in informal labor market, they have to rely on the goodwill of their employers and are not entitled to many of universal labor rights. Those working as servants and slaves are in the heartbreaking perils expecting better hope only in the next life.

Informal sector in Nepal is huge and this space is mostly preoccupied by those at the bottom of development statistics—poor women, wage workers, dispossessed and those who stand between the capital and the labor. In the context of growing youth population, declining public budget, rural push of poverty and foreign pull of opportunity, the Nepalese state often lagged in providing a supportive policy framework for their productive employment. Naturally, this population has to engage in informal sectors. Informal sector continues to grow in direct proportion to the decline of formal economy owing to the elites interest in privatization and denationalization of 34 industries and de-regulation import laws, negative effects of global economic crisis, protracted political instability and democratic deficits in the country.

New technology has marginalized the real and formal economy by expanding the space of flexible and highly specialized symbolic economy with the growth of financial capitalism, banking business, service and technological sector production from craft-oriented specialization to computer service. Its decentralized nature fits well with the diverse needs of Nepalese people strewn in diverse topography and resource location having the resiliency to withstand the challenges of globalization. But, one can clearly see the “urban bias” in development policies and resource allocation of the donors, the state, employers and even labor unions as development is seen until recently improved economic growth, not amelioration of structural injustice through liberation, entitlements and fairer justice^[1] for individuals, communities and the state. There is a need to bridge the gap between development theory and contextual knowledge and its outcome for human development. This paper poses fundamental questions about informal economy and narrates the characteristics of informal economy, upcoming challenges for this sector, status of Nepal's informal sector, exigency of people-centered development and draws a short conclusion.

2.2 Fundamental Questions

The crucial questions are: How to provide property rights to the poor in an informal economy and expand labor market opportunities at home so that they become equal stakeholders of democracy,

human rights and good governance? Is minimum wage sufficient to guarantee the basic rights of workers for their essential human needs and freedoms? Under the condition of liberalization and globalization where the roles of state have been downsized how can the government address the workers' demand for social accountabilities in the vast informal sector? Does the private sector seem willing to undertake this responsibility? How to establish a complementarity of interest between informal and formal economies and workers and build solidarity through policy measures, concrete programs and collective action? What are the essential legal and practical measures to transcend local customary rules for the creation of efficient market for informal sector progress? Is there a possibility for small-scale informal sector entrepreneurs and workers to become joint enterprise holders able to compete in a competitive neighborhood and global economy? How far workers' collective experience of neglect by the government helps them to act rationally in terms of maximizing profits and redeploying economic surplus for expanding the scale of political economy?

2.3 Characteristics

Informal economy is too diverse to compress into a single definition. In Nepal, it may be described as small-scale, decentralized, indigenous, agricultural sector, self-employed in artisan activities, street selling and casual and part-time works. Some informal economic sectors are owned by families and engaged in non-market networks of diversified production of public goods nourishing the livelihoods of a bulk of poor and ensuring their social and financial security. Skills and apprenticeships in such enterprises are provided by families themselves. For them, the scope of citizenship, access to and identification with the state is far-off. Other micro enterprises, employing less than ten persons, use local pools of knowledge, management, resources, workers, technology and market access and are considered economically very efficient in production, supply, pricing and appropriation of profits. By economizing the limited capital, their operations are near perfect competition, which helps to keep prices down so that poor people can afford to buy goods and services in the market.

The gradual shutting down of over 30 state-run industries in Nepal can be attributed to excessive rent-seeking, mismanagement, financial losses, bloated political bureaucracy, dislocation of politics and inflexibility of leadership in attitude change regarding the attainment of common good through suitable economic policies. The fatal attraction of post- 1990 governments to neo-liberal policies further created a disjunction between local development discourse and global imperatives that inescapably pushed Nepalese economy to informal sector growth. It has, therefore, stifled the prospect for a substitute for developing a low-cost way of creating employment. The innocent optimism of new republic has given way to sordid exhaustion of national economic strength. Exchange of political power for money strained the possibility for the investment in the modernization of informal sectors. The post-republic order corresponds to a state of nature where the struggle of informal sector workers for dignity continues to contest the utility of hegemonic discourse for the upliftment of the poor.

Informal sector does not mean that it is often backward based on what Karl Marx called "petty commodity trade" of independent producers (1972: 82) or modernization theorists dubbed "anti-development" due to its traditional method of production (Muenkner and Walter, 1996: 87). Development expert Goran Hyden calls informal sector an "economy of affection" (1983:15) because of its proximity to family, community and neighborhood, pro-poor, labor -intensive and environment-friendly nature. Lord Buddha long ago and Karl Marx later, referred to an economy based on the "need of society" than on the insatiable greed of individuals which has become a base of discourse of E. F. Schumacher in defense of "small is beautiful" (1999:5). An attentive society requires caring of the environment and the people. In a rapidly changing consumer markets, there is greater incentives on the flexibility, adaptability and innovation that only informal sector and small scale industries can provide. Referring to the enormous cost of human civilization incurred by capital-intensive and techno-centric development, Jeffrey Sachs said that

creation of “mindful society” requires adopting the golden mean and going back to the ethics underlined by Gautam Buddha, Aristotle and Immanuel Kant who had advocated non-violent, ecologically and humanely sustainable economic policies. Informal economy can contribute better if the state provides sound policy framework to upgrade its technology, information, raw materials and market access for products and overcome three-fold deficit of its macro-economy—public budget, foreign trade and internal and external debt. A harmonious life cannot be possible without addressing these deficits and striking a balance between material and ethical basis of liberty and representative public order. Economic survival of democracy also requires a strong middle class who not only pays tax for social welfare benefits for the poor but also mediates the interest of society and allows reformist politics in the context of power shift.

2.4 Upcoming Challenges

The raw materials were basic fuels of agriculture-dominated society. Energy was the vital element of industrial revolution. And, information technology remains the motor of post-industrial development. In the industrial society, the state mediated the interest of the capital and the labor and managed production, exchange and distribution, international trade, commerce and communication. The most significant effect of information revolution is the globalization of capital, resource and energy-intensive political economy which is highly inflationary in nature. Ironically, the impacts of inflation in the life of poor are less calculated by mainstream economists. For the least developed countries like Nepal, unable to compete in the competitive market, this globalization process is undermining the historical “social contract” between the capital and the labor, inverted the historical convergence between the state, economy and citizenship and generated more poverty, unemployment and inequality. The government - shepherded free market advertised by conformist intellectuals, media and private business empires and mainstream politicians has eroded the power of Nepali state to formulate and implement appropriate policies, laws and rights, weakened national economies and societies, the support base of the vulnerable population and the political capacity of trade union movement to compete for the “dignity of work” through the promotion of labor rights, citizenship rights and human rights embedded in the Interim Constitution 2007.

The corporate global world’s demands for “labor market flexibility,” aiming to reduce minimum wage and workers’ protection, is at conflict with the workers on welfare measures, science over climate change and environmental issues and art over the commercialization of spiritual and human life. It is recklessly commodifying nature, labor, education, health and culture. (Stiglitz, 2006: 17; Galbraith, 2006:23). As a result, all goods and services are reduced to their monetary values and made them to respond the code of price. Many of the demands are generated by men of inner circle of power without face through media advertisements. To check this trend, “the market forces require a stronger counterweight from an effective state” (Bofinger, 1999:3). Only then a system of inclusive politics beefed up by democratic redistribution of power and wealth can overcome the darker instincts of life, restore the balance of society and contributes to social justice and peace. But for Nepal linked to regional and global market there is a Catch-22 situation: brining social justice to markets requires the regulation of business institutions but the nexus of business-bureaucracy-political elites often escape democratic constraints on their wealth and political power.

Newly digitized symbolic economy has created a new social stratification producing multi-class workers, self-employed and dispossessed without solving the old division between capital and labor and altering the nature of wealth production, exchange and distribution. There is a neo-liberal “paradigm shift” first, in the nature of economy from real to symbolic and in the mode of wealth creation—production, circulation, distribution and investment within the country. Second, it has opened better labor market opportunities abroad under foreign rule than at home. It has provided global mobility of Nepal’s labor force in tune of over 3 million, emigration of 300,000 annually out of 450,000 youth force who annually enter into job market. Third, due to heavy jobs layoffs following closure of state industries, majority of labor force are forced to shift from organized to informal sector to satisfy their livelihoods. It is their

remittance which has become lifeblood of Nepal's development. But the migration of youth has also reduced the level of productivity of agriculture turning 3.5 million people food insecure and converting the nation from the net exporter of food grains to gross importer. Suddenly, small-scale entrepreneurs in Nepal are exposed to national and international competition with the effect of losing safety valve in deregulated and denationalized system of laws and corroded the source of income for the poor. Still, Nepalese economy is sputtering and is producing more losers of economic game. The employer's recourse to flexible employment contracts has further lowered job security for the workers, undermined their positions and their unions in free collective bargaining restraining the rationalist program of reforming labor market relations and perverting the country's historical traditions of golden mean in ethical business practices governed by *shuva lav*.

The expansion of social rights and the conception of social welfare state based on the fulfillment of human rights, core labor standards and social security have been well up beyond the capacity of the Nepali state to attain them. Especially, for women, artisan caste (Dalits), marginalized and geographically isolated people, only the informal sector continues to contribute to their food security in rural areas. It also provides job security in the marginal cash economy of urban areas and safety valve for the disaffected young population that make up the majority of the nations' population. The role of national level unions is great in solidarity building, policy mediation and human development. Unfortunately, they are also seen unable to cope with the problem of workers' layoff, deteriorating working condition, declining job market, growth of child labor, forced labor, denial of rights to workers, poor health and safety provisions and even appropriation of social security and social protection money by local government officials.

Informal sector is socially embedded, favorable to the production of "economic commons." This shows that economy is not an isolated system where private sectors can free ride beyond corporate accountability—evasion of tax, bank defaulting, capital flight and building links to criminal source of money. This amoral trend will eventually minimize the resources for productive investment and intensify hunger, deadly disease, famine and resource conflicts (Dahal, 2011:45). Survival of informal sector economy rests on its own internal dynamics of human development and the environment which provides skills, raw materials, technology and markets. It is deeply rooted in local, national, regional and global power relations. In an informal economy, social aspect of transactions (kinship, language, localism and other affinity) provides necessary backward (agriculture) and forward (trade) linkages of the economy, garners broader forms of social capital and creates social safeguard for development that is fairly just, redistributive and sustainable. But, in Nepal, the government's orientation to revenue rather than production-oriented development has weakened the linkage of informal with formal sector and undermined economic basis of the state to promote collective welfare. Owing to the slow entry of trade unions into informal, agricultural and small-scale entrepreneurs' sectors existing at the unorganized realm, informal sector remains outside the sphere of "collective bargaining" in the domain of profit maximization, co-determination of policy that affects them and peaceful collective action. Democracy has given the informal sector workers political power whose conscious exercise can become attendant for their economic empowerment and reconciliation between the capital and the labor.

2.5 Nepal's Informal Sector Workers

Informal sector in Nepal is defined as having family enterprise, unregistered or a registered company with 10 workers at work. In this informal sector, a trade union federation can be organized with 500 or more workers engaged in the same nature of work. In the case of self-employed workers and agricultural workers they were granted the right to unionize under an amended Act 1999. The association of 5000 agricultural workers, covering at least 20 districts and with a minimum of 100 members in each of the district is entitled to constitute a national federation in agricultural sector.

Nepal Living Standards Survey 2010-11 reveals the condition of Nepalese workers' engagement in varied activities where 73.9 percent of workers are in agriculture and forestry sector followed by manufacturing 6.6 percent, wholesale, retail and trade 5.9 percent, construction 3.1 percent and rest of others are in mining and quarry, hotel and restaurants, transport and storage, financial intermediaries, real estate and renting, public administration and defense, education, health and social work and private and community works. Over 30 percent of its economically active population is totally unemployed. Nepal's society, economy and politics are predominantly informal: society because of the predominance of "unwritten transcript" of society on the life of workers; economy because of vast unorganized sector living in subsistence economy, low production base, poor tax ratio, huge contribution of remittance, low human development and vicious poverty and structural injustice reinforcing multidimensional conflicts; and politics because of personalized dominance of leaders over the impersonal public institutions of the state and polity. When political leaders are comfortable with weak institutions and fear the development of depersonalized institutions, rules and processes of the state, it is hard to address the root causes of the poverty, create joint development projects between perpetrators and victims of conflict and generate sufficient political will in the democratic transition towards a constitutional state, democratic polity, transformational leadership and legal-rational legitimacy for governance springing from bottom up.

Out of population of 27 million about 90 per cent of the Nepalese work in the informal economic sector. Total workforce is 11.77 million. In organized sector 1.99m workers are employed while in informal sector the number is 9.78million. The average monthly minimum wage for workers is US \$ 87.32 which is barely enough even for a small family given average annual inflation rate of 12 percent. Daily wage for industrial worker is \$3.25 while for agricultural workers it is yet to be decided. The annual per capital income of \$645 puts Nepal in the bracket of least developed country. Informal sector's contribution to national economy is more than 50 percent. Poor working conditions, gender discrimination, lack of social protection, low productivity, hazardous work, non-recognition of work done, poor income, long working hours, unsafe working environment, meager benefits, no leave or holidays, inadequate social security benefits, and poor unionization to protect the rights of workers are the basic features of informal sector in Nepal. These challenges pose problem in unionizing the informal sector. Violent conflicts have further affected this sector causing the alienation youth force from its social roots and, consequently, depriving the society of its dynamic, critical masses of social and cultural transformation. New social movements have, therefore, precisely taken anti-institutional turn.

Low level of literacy, lack of modern skills for bulk of work force, poor nutrition and health facilities contribute to their low productivity. Investment in social sectors is, therefore, absolutely essential to improve the productivity of workforce. Likewise, high population growth relative to economic growth has increased demands for social services and basic infrastructures facilities while the quality and coverage of health services up to the village levels are grossly insufficient. Why did this happen? Obviously, problems were not seen through the eyes of people and policies were not conceptualized to attune to local needs and conditions. If economy does not work for the people, it will generate a dynamic tension between policy discourse, state institutions and social classes and politics ultimately loses its legitimacy to defend public and national interest.

Social deprivation remains very high in the country despite some improvement in health care, regular immunization campaign against communicable diseases, literacy and quantitative growth of education. Majority of people in both urban and rural areas are still without safe drinking water and sanitation and face rising pollution where polluters don't pay. The costs have to be subsidized by the general society. Welfare outcome of the social expenditure of the government is highly skewed because of urban bias in planning and development. The working environment, medical facilities and conditions of work are so poor that they also militate against the protection and security of informal sector workers. Irresolution of root causes of violent conflict has decreased economic activities, reduced the value of workers and even flexibilized the working environment incubating the ruggedness of life. Without social competence

economic efficiency cannot be achieved. Legal property rights do not exist for the poor in Nepal despite the constitutional recognition of the fact that sovereign power lies with the people. Political stasis at the top level of leadership defies the possibility to create self-governing polity at the grassroots level favorable for the modernization of informal sector economy.

2.6 Exigency of People-Driven Development

With the microfinance revolution and other positive efforts, attitude towards informal economy is slowly changing. There is recognition that these economic activities can become an entry point for fulfilling basic needs and freedom. It is expected to promote social and economic development and initiate silent social transformation of Nepali villages in line with gender, social and inter-generational equality. Ethical desire to lead good lives for oneself justifies a moral reason for concerns to others (Dworkin, 2011:1) where the role of state is vital. Nepali state is under “an obligation to provide all its citizens with equal opportunities in life, and to grant equal access to public goods—education and culture, health and natural resources, internal and external security” (Thierse, 2009:11). Sustainable solution of the problem of informal sector lies in the legislation of proper laws, building of participatory culture whereby societal interests prevail over private greed and gain, reinvesting of economic surplus on production process, promotion of subcontracting with intermediary and large business, strengthening of inter-sectoral linkages, legal protection and encouragement of workers to become shareholders of the business enterprise and low-cost cooperatives.

Informal sector economy has to respond to the legitimate aspirations of workers constituted as citizens and human beings and cluster around networks with like-minded enterprises for production, supplies and market services so that it can achieve financial stability, economies of scale and social support. Due to its closeness to society and local self-governance institutions, it can evenly distribute employment benefits to the people. But, the local self-government has the responsibility to offer training, financing and other services to this sector so that it can increase its productive functions. Only productive jobs can ensure them the necessary conditions of freedom, equity and dignity. Election of local bodies can reduce official corruption on the distribution of social security and social protection measures and implement citizen charter. Civil society, NGOs and private sectors can add the resources of modernization into their efforts to upscale the scale of political economy of informal sectors. The diversity of Nepal’s demography and topography offers various resources which can be synchronized and utilized through decentralized, labor-intensive and eco-sensitive policies.

2.7 Conclusion

Informal sector economy of Nepal holds tremendous potential to guarantee livelihood, mitigate poverty, reduce inequality and provide sustainable basis of democratic development if the state and private capital provide technology, resources, information and market access for its products. Implementation of the ILO Declaration on Fundamental Principles and Rights at Work has made important contribution to the new architecture of social and economic development. The ILO Convention N0 189 on Decent Work for Domestic Workers has yet to enter into effect. On this architecture extension of social security schemes, implementation of laws on fair wages and incomes and development of mechanisms by which workers in the informal economy can possibly be provided access to and control over productive assets and resources. The new solidarity of informal sector should be built on a system of global rule, designed around a single fundamental human right—the right to what Hannah Arendt calls “human condition” (Ree, 2006: 28). The role of state in redistributive justice is essential as market does not show equal concern to all (Dworkin, 2009: 470) citizens while civil society groups are relativized by their plural mandates. The challenge is

to find ways to ensure the voice of workers in income generating activities through the constructive engagement of community with the state policy makers and increase livelihoods and small-scale business enterprises.

The cohesiveness of unions counts a lot to exert pressure for policy reforms, organization, solidarity, communication and collective action on behalf of its members and the society at large. Other issues are: implementation of minimum wage in all sectors, inter-movement solidarity of unions, contribution-based social security, reform in labor market, management of foreign jobs, elimination of child labor practices, rights-oriented campaign, collective bargaining, etc (Bhattarai, 2011: 51-55). It is also important to attract the attention of national policy makers on the plight of informal sector workers– Kamaiyas, child laborers, Dalits, dispossessed, domestic servants, conflict-victim groups and define a viable strategy of formulating an integrated approach to peace building. There is a need to make “taxation more progressive in order to offset the economic forces increasing inequality” (Stiglitz, 2006:20). The coordination of the roles of various social partners working to foster “decent work” in the informal sector of Nepal equally presupposes the expansion of the sphere of social and gender justice through equality of opportunity and right-based and procedural distribution of resources through laws that guarantees their livelihoods and freedoms. There is no hope of peaceful progress of Nepal if economy is divorced from democratic principles and profit is placed before good life of ordinary people. The morality of public interest provides suitable “framework condition” for the good life of all people-formal and informal ones and overcome the instinctive leadership desire for selfish ends with almost negative democratic outcome. Modernization of informal sectors is expected to alter structural conditions for the emancipation of Nepali people and transforming them into citizenship with equal rights and equal responsibilities.

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[1] A fair justice is relative to any number of models: "equality of distribution (one person, one object), equality of opportunity, procedural distribution, rights-based fairness, need-based fairness, scalar distribution, equal distribution of responsibility, equal distribution of power, etc (Lakoff and Johnson, 1999:297).

3. Contributors

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Blogs at: Just Aid-<http://aidmonitor.org.np/blog/>

Alliance for Aid Monitor Nepal (AAMN) is a public forum towards bringing voices, perspectives and critical discussions on the issues related to foreign AID in Nepal. Nepal is no exception to AID realities. However, AID, which in a way intends to influence the future of every citizen, has been an issue of debate of certain government, political and intellectual elite. It has not been able to be a part of public debate in Nepal. At a time when the country is marching towards transformative politics, it is high time to ensure that citizens have rights to access information about aid and that they have their say on aid politics. With an aim to engage and initiate a discourse on aid

within people's politics, this forum aims to open up a creative and critical space. *Connecting Global to local on Governance, Democracy and Aid Issues in Nepal by Engaging Academia, Media, Professionals, Researchers, Campaigners, Community People and Development workers. A Think Tank and Research Base*



ActionAid International Nepal is an anti-poverty, human rights-based organisation established in 1982. We are an associate member of the ActionAid International federation, and we aspire to become a full affiliate at the beginning of this strategy period. ActionAid International is active in over 45+ countries across Asia, Africa, the Americas and Europe, with international secretariat in Johannesburg, South Africa. We have worked in partnership with more than 250 civil society organisations, social justice movements and people's organisations in 42 districts to fight against poverty and injustice.

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