AN ANALYSIS OF BUDGETARY SYSTEM IN NEPAL

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By

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LETTER OF RECOMMENDATION

This thesis entitled **An Analysis Budgetary System in Nepal**has been prepared by **Mr. Ganesh Raj Upadhayay**under my supervision. I hereby recommend this thesis for examination by the Thesis Committee as a partial fulfillment of the requirements for the Degree of Master of Arts in Economics.

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Prof. Dr. R.K. Shah

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Date: 03/01/2074 B.S.

LETTER OF APPROVAL

We certify that this entitled**An Analysis Budgetary System in Nepal** submitted by **Mr. Ganesh Raj Upadhayay** to the Central Department of Economics, Faculty of Humanities and Social Sciences, Tribhuvan University, in partial fulfillment of the requirements for the Degree ARTS in ECONOMICS has been found satisfactory in scope and quality. Therefore, we accept this thesis as a part of the said degree.

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ABBREVIATIONS/ACRONYMS

ADB	:	Asian Development Bank
ADRL	:	Autoregressive Distributed Lag
AG	:	Auditor General
GoN	:	Government of Nepal
GDP	:	Gross Domestic Product
FY	:	Fiscal Year
MoF	:	Ministry of Finance
WB	:	World Bank
LDCs	:	List Developed Country
IDS	:	Integrated Development Studies
NRB	:	Nepal Rastra Bank
CEDA	:	Center for Economic Development and Administration
CBS	:	Central Bureau of Statistics
NPC	:	National Planning Commission
VAT	:	Value Add Tax
RC	:	Resources Committee
IMF	:	International Monetary Fund
RCC	:	Revenue Consultative Committee
DDC	:	District Development Committee
MPS	:	Member of Parliaments
FCGO	:	Financial Controller General Offices
VDC	:	Village Development Committee

AGO	:	Auditors General Offices
PCO	:	Project Coordinators Offices
DTO	:	Districts Treasury Offices
SOEs	:	State Owned Enterprises
CDF	:	Constinuity Development Fund
SAP	:	Structural Adjustment Program
ESAF	:	Enhanced Structural Adjustment Facility
IPA	:	Immediate Action Plan
MTEF	:	Medium Term Expenditure Framework
SAFTA	:	South Asian Free Trade Agreements
WTO	:	World Trade Organization
CAP	:	Comprehensive Peace Agreement
PER	:	Public Expenditure Report
GNP	:	Gross National Products
PCI	:	Per Capita Income
DE	:	Development Expenditure
TE	:	Total Expenditure
RE	:	Recurrent Expenditure
CE	:	Capital Expenditure
PR	:	Principal Repayment
TYIP	:	Three Year Interim Plan
$	:	Dollar

CHAPTER I

INTRODUCTION

1.1Background of the Study

The budgetis an instrument through which the government controls the entire economy where as budgeting is the budget a process of preparing, negotiating and agreeing a quantifier and specific plan for an organization, normally for a year. The budget has been defined by different writers in various ways. Some of writers are in the view that budget is a statement forecasting revenue and expenditure during a certain period of time. The word 'budget' is derived from French word "Baguette" which means small leather bag of pouch. It was used first in England to describe the white leather bag, which held the seal of medieval Court of Exchequer. Later known 'Budget' contained proposals of financial plan of government expenditure. But word budget has now been used in all countries and in many languages. The term budget is now commonly understood as a government document. In pact it is a proposal of proposed means of financing them for the approval of legislature (Bhandari, 2014).

Budget is also a financial resource that plays a pivotal role in the functioning of the state. Whether a budget is balanced, in surplus or in deficient, directly influences the state's operation. A budget dose not only establishes a linkage with the existing policies but also addresses the demands of citizens. The local level organization, local representatives and parliamentarians have a vital role in advocating for certain programs or projects that meet the needs of their constituencies. Therefore, a budget represents an allocation of resources based on the demands and needs of the citizens (Sigdel, 2014).

Budgeting is important because Market mechanism only cannot perform the functions of the economy. Public policy is needed to guide and supplement to the economic function as a whole. The budget plays vital role to solve the problems like, to secure the condition government interfere is essential, to solve problems of externalities. Support to government policies through market operation, problems of discounting in future, price stability, high unemployment, distribution of income and wealth etc. (Khanal,2013).

Nepal is not new to the concept of budgeting with detailed guidelines, policies and law as in place. Nepal, government plays an important role for the socio-economic development of the country. The issue of significant proportion of the capital expenditure being unspent is indicative of the underutilization of the resources in the country. Budget expenditure has always been a problem with majority of the spending taking place towards the end of the fiscal yearIn the developing country like oursprivate sectors in weak to participate in the economic development. Due to lack of capital and private sectors is not encouraging. By budgetary policy with the means of tax, exercise, customs etc. government can motivate private sector to cope (manage successful) with development activities in developing countries due to very immature stage of private sectors, government has to motivate and give suitable infrastructure for making private sectors active. Then only control and direction becomes the secondary phase of the government to deal with private sector.The budgeting plays a vital role in the mode of economic development of a country. As the world environmental is becoming more and more complex, budgeting has becomes very important and technical as well(Dahal, 2008).

The origin of the budget is said to have from the French word ‘Bougget’which refers a small leather bag or pouch. It was first used in England to describe the white leather bag, which held the seal of Medieval Court of Exchequer. Later known budget contained proposal of financial plan of government expenditure. But word budget has now been used in all countries and in many languages. The term budget is now commonly understood as a government document. In fact, it is a proposal of proposed expenditure for a given period of time and means of financing them for the approval of legislature (Lekhi, 2008).

Nepal is least developed and centralizedgoverning systems. ThusThe presentation of budget to the legislature-parliament appears to be unified one. The presentation of the budget to the parliament is mandatory by law. According to the Interim Constitution of Nepal: 2007 (Article 93, clue 1 and section 9) for each financial year, the Finance Minister must present the estimation of budget to the legislature-parliament for its approval (GoN, 2007).Thus the formulation, presentation and implementation of the budget is constrained by the constitution and Financial Act in Nepal(Bhandari,2014).

In general, the background of budget in Nepal defines as “the government annual plan and programs to accomplish national goals and objectives defined by periodic plan that consist: projection of next fiscal revenue collection, projection of next fiscal year government expenditure and actual progress report up to the tenth month of current fiscal year on revenue collection and expenditure" (Acharya, 2009).

Budget becomes more important in managing government finance mainly after the introduction of planned development process in 1956. The concern over the status and efficiency of budgetary systems of GON increased specially after the political change of 1990.Growing challenges encountered in relation to the rising expectation of people have promoted the government to become serious as to the means and the use of the scarce resources in a more organized and effective manner(Dahal, 2008).

Budgetary experience after the restoration of multiparty democracy in 1990/91 within the framework of Constitutional Monarchy based heavily on the adoption of the various policies of liberalization, globalization and the privatization of the economy. Budgetary programs policies and the priorities of the GoN budgets presented by the various short lived government have also undergone change to that direction since the very first budget 1991/92 of Rs 26.7 billion (budget speech ,1991/92) presented by the majority government of Nepali Congress(NC). This was the first budget in direction towards the liberalization of the Nepalese economy in true sense. It gave a new vision to encourage participation of the private sectors in the productive areas (Bhandari, 2014).

Only the sound understanding of the existing problems in budget process facilitates better planning and executing of state-level programmers. Budget correlated to planning .Planning involves the combination of many aspects of programmers. The pattern and structure of budget differs from country to country in France, the budget is presented twice a year. So it could be said that the mode of the budget differs from the policy dimension of a country. Therefore, the budget depends upon the political nature of a country(Sigdel, 2014).

During the first half of the 1990s Nepal went through a period of fiscal consolidation as an integral part of an economic liberalization and reform program. Nevertheless the expansionary fiscal policy adopted by a succession of short lived government during the latter half of the 1990s resulted in an increase in deficit financing, debt stock and debt-servicing obligation (Adhikari, 1990). It is because of this study focuses the trend of the budgetary componentsvia govern expenditure, revenue, deficit financing and the debt of the government budget after the Restoration of multiparty Democracy in FY 1990/91.

1.2 Statement of the Problem

The budget in developing countries is of recent origin Nepal also has short experience of budgeting. The budget was oriented towards spending under different heads such as salaries, furniture, goods, building. Vehicle and equipment travels etc. which are need for control and accountability over the expenses mode. Gradually budget has been prepared with the objective of meeting national plan and programs.

Nepal is a country facing a major macroeconomic crisis, indeed; in many respectsits macro economy is reasonably sound, with an improving balance of payment, adequate foreign exchange reserve, relatively modest inflation, fiscal deficits financed largely by external aid relatively low levels of domestic borrowing. However, it is stuck in a low level equilibrium, with decaling investment, modest economic growth, high population growth and widespread poverty. Fiscal management has been participatory weak and fiscal stability is being maintained largely at the expenses of development activity, although public spending averages at around 18 percentof GDP a rate which should be sufficient to provide a reasonable level of basic public services in most countries - in Nepal there is little to show for it, particularly in rural areas, leading to wide spread perceptions of misuse and waste of scarce public resources.

The policies aid down in the budget can play a vital role in the national economy. As an annual policy and program document of the government, budget is a primary means to accelerate the pace of overall economic situation of country. Basically, a single budget which is generally formed for only one fiscal year cannot solve the entire existing economic, social and other problems at once. But the budget should be the necessary momentum and appropriate guidance to the economy towards its basics vision, objective and goals in sequential manner. In our budgetary practice, it is frequently observed that there is very poor consistency between the objectives of long range plan and the priority of short range budget of the same periods. The congruence between the budgets of the chronological periods also seems to be missing.

There are no simple explanations for the apparent ineffectiveness of public spending in Nepal .Given its land- locked and difficult terrain, development projects are inherently more costly and take longer to implement in Nepal. This is however only part of the story. A complex web of systematic factors, which cut across virtually all sectors and projects/programs, has consistently contributed to poor implementation and development results.

The effectiveness of the budget could be visualized in the economic indicators such as GDP growth price stability, employment generation, socio-economic, infrastructure development, improved domestic resources mobilization and reduced dependence on foreign investment financing, current account and balance of payment improvements, poverty reduction, fiscal welfare improvements, better law and security environments, etc. but none of these indicators are found to be satisfactory in our national development exercise despite the implementation of ten ‘five year plan and three ‘Three Year Plan ‘about 65 annual budgets. Keeping this situation in mind, this study tries to explore budgetary system in Nepal.

Nepalese government has not been able to address its economic problem properly although it is issues. Regarding budget, it doesn't include all stakeholders during its complete cycle. Policies and their implementation are not fully consistent with each other. In the case of Nepal, non-budgetary express are significantly increasing. Dependency on foreign resources has still been seen.

In Nepal the finance ministers introduced the first budget in the year 1951 for economic development. However in Nepal budgets seems to have been characterized by uncertainties. Allocation of resources usually made with optional expectations. Due to such phenomenon several programs have to be left out. It may be noted have that greater proportion of the total development budget is finalized by foreign aid and lone keeping this situation in mind, this study tries to explore budgetary situation in Nepal.

1.3Objectives of the Study

The general objective of the study is ‘an analysis the budgetary system in Nepal after the royal rule finished up to formulation of new federal constitution begins. (FY2005/06 to FY2014/15).

But the specific objectives of the study are as follows:

(1) To identify the expenditure and revenue pattern of government of Nepal.

(2) To identify problems and prospects in Nepalese budget.

1.4 Research Question

i) What is the majors problems and prospective of the Nepalese budgetary system?

ii) What is the expenditure and revenue pattern of government of Nepal?

1.5 Significance of the Study

The government is responsible for welfare of the people. In the developing countries there is a problem of resource gap. High rate of inflation, high rate of unemployment, lack of capital, underutilization of resources. Corruption and high public debt. Etc. In the context government's fiscal instrument have a direct and immediate influence on the national economy. As the governments make decision in the national interest, attention has to be paid to the process by which public revenue is collected and public expenditure is determined, allocated and controlled. Customary that these processes are expressed in terms of budget. Since the government has no right to collect revenue and to spent this without the permission of national legislature.

Nepal is a least developed country with per capita income less the $750 and very low GDP growth rate 4.6 (MoF, 2012). Many other developed countries of the world including our neighbors have taken a quantum leap in the economic development by achieving double digit economic growth, our nations could not achieves the rate a desired owning mainly due to political instability has been the main cause of budgetary uncertainty since along.

Demand of the Nepalese society is the rapid socio-economic development Present of the country Present. This is possible only through the development expenditure in the large scale. It is therefore, necessary bon the part of the state to assume the responsibility of creating infrastructure needed for of country like Nepal lies in increasing growth rate, raising income and status of the people reducing inequalities of income and wealth, removing regional imbalance, promoting initiatives progress, stability and assume the responsibility of creating infrastructure needed for progress, stability and the growth of the economy. Importance of the government expenditure in economic development and maintaining macroeconomic stability.

As the government makes decision to the national interest attention has to be focused on process by which the public revenues are collected and the public expenditure aredetermined, allocation and controlled. It is customary that these processes are expressed interims of the budget components; expenditure, revenue, deficit financing and the debt of the government.

Thus, the study of the trend of budgetary components in the developing country like in Nepal has of Great significance. Formulation of the future budget on the basis of past experiences is very important aspect of the government budget. Learning the lesson from the post experiences can be utilized in formulating the future course of the budgeting so that the better budgetary policies of the government can be carried out in order to fit the budgetary expenditure, revenue, deficit financing and debt of the government at the desired level of the economy. Although there are some dissertations regarding Nepalese budget and government of Nepal finance, yet the critical assessment has not been made on the "Trends of Budgetary components of the government of the government budget in Nepal after the restoration of democracy". Therefore, this study makes an additional contribution to some extent for the assessment of the trends of the government expenditure, revenue, deficit financing and debt of the government in 2010/11.

1.6 Limitations of the Study

The main limitations of the study are as follows:

1. This study covers the periods from FY2005/06 toFY 2014/15 only.
2. This study based on the published secondary data and desk research. No attempts are made to examine the reliability of the available secondary data since the related authorities officially release them.

1.7 Organization of the Study

There are seven major chapters in the study; each chapter further divided into various subsections. The first chapter which is the introductory portion gives a general overview of the whole study and helps reader to know what and how of the study.

The second chapter presents the reviews done on different literatures. This chapter is divided into two units. The first unit presents the theoretical review and the second unit is based on the empirical review in the context of Budgetary Trend in Nepal.

The research methodology constitutes the third chapter, which provides information regarding the types and sources of data used in to study.

The Nepalese budgetary system has been analyzed in fourth chapter. It includes historical background, budget formulation process, and budgetary reforms and polices and the sizes and objectives of the GoN budget from FY 2005/06 to FY2014/15.

The fifth chapter deals with empirical analysis to see the trend of revenue, expenditure and deficit budget and public debt and relationships among the variables under study.

Finally summary, conclusion and the recommendation of the study made. Recommendations made based on such study that might be helpful in preparing and implementing the budget of Nepal. References presented after the last chapter closes the study.

CHAPTER II

REVIEW OF THE LITERATURE

2.1 Theoretical Review

2.1.1 Conceptual Background

The concept of budget is normally associated with national government and internal-external sources. A government budget is framed in the shape of a financial plan it is a statement of income and expenditure relating to the various economic and other activities that the government intends to perform in the coming period, usually a year .A long with the proposed revenues and expenditure relating to these activities, a budget present the financial accounts of the previous year, the budget and resaved estimates of the current year and the budget estimates of the coming financial year. In the context of budget, several publications are published in the form of booklet, book, journal, article etc. Likewise there are several books, booklets, journals and articles written by Nepalese budget. Similarly, studies have been made to allocate the resources for different activities. The reviewed relevant past works are present below:

2.2 International Review

2.2.1 The World Bank

The World Bank had reviewed public expenditure pattern of Nepal in 1999. In this study, WB has pointed out that fiscal management is week reinforcing in widespread perceptions of misuse and waste of scarce public resources. The review further found that budget preparation is divided in to two branches with the ministry of finance preparing the, regular budget,and the national planning commission preparing the development budget without well integration.Scarce resources are found to be allocated in an incremental basis rather than on resources needs of projects and programs.Because of political pressure to accommodate new projects, the budget, particularly development is heavily over-programmed so that many projects derive away too little resources. There is even weak link between plans and annual budget without having rolling public expenditure programs.

As the study pointed out, institutional weakness' was the result of over-staffing, low salaries, political interferences in appointments and, transfer inadequate recognition of efficiency and performance, which lead to poor public expenditure management. The study has noted that Nepal is at major cross roads in its economics and political development.

The study conducted by W.B. has suggested some solution to improve public resources management. Some of them are as (a) reexamination of the role of public sector in the economy, (b) focus limited resources on key priority areas where such resources can be put to most effective use, (c) ensure good governance and transparency, (d) desire action to formulate an anti-corruption agenda, (e) strengths the institutional capacity for caring development activities.

2.2.2 International Monetary Fund(IMF)

Fishcher(1990) followed result in his study of the economics of the government budget constraints the macro economic analysis that has outlined is a useful starting point for examining the economics of budget deficit. However, it takes more than a single indicator to judge fiscal policy, the macro economics of deficits. The more efficient are taxes and spending. The higher is the public deficit then can be sustained, since growth will higher.

Felipe and Klaus (1991) conducted in Zimbabwe, during the study period of 1980/81 to 1988/89, found that the public sector deficit has grown from less than 10 present of GDPin initial period of study (1980/81), but it is raised up to 14 percent of GDP over 6 year span. From which nominal interests on domestic debt and foreign debt output ratios were continually rising. But due to the starting of fiscal adjustment program in 1987/88 and it was continuously decreasing. The study shows that among macro-economic variables, real import and real exchange deviation had a negative impact on public sector deficit. On the country, increase in the domestic real interest rate, domestic inflation and foreign nominal interest rate tends to boost the deficit in decreasing rate. The impact analysis shows that if real GDP has to be increased by one percentage that translates the fiscal deficit should be increased by 16 percentages. For this, the foreign real debt increased by 3 percentage and domestic by 5 percentage where the domestic inflation increased by 31 percentage. This whole finding shows that fiscal deficits have to be reduced for attaining the goals of sustainable development of the economy

Chowdhury (2004) suggested that fiscal actions do not have any perceptible influence on the exchange rates of the sampled countries except Nepal where increased government expenditure tends to appreciate the Nepali currency. This is a non-conventional result such a result can be theoretically explained by the monetary theory of exchange rate determination. The results obtained in this study have enormous policy implications of LDCs. The result will be always fears among policy planners in LDCs about the alleged deleterious effect of fiscal actions. Thus, more and not less of fiscal actions is recommended for accelerating growth in LDCs.

Huynh (2007)conducted his study while collection data from the developing Asian countries for the period of 1990 to 2006. He concluded that there is negative impact of the budget deficit on the GDP growth of the country while simply analyzing the trend in Vietnam. Furthermore, he conclude the crowding-out effect surfaces as the budget deficit burden increase. There is a strong, significant and positive relationship between the budget deficit and the long-term nominal rate of interest in a study conducted for the periods 1971to 1984 on the United States of America (Cebula, 1988).

Saleh (2003) on the basis of previous researches, which are conducted by economists regarding the impact of budget deficit on different economic variables, concluded that budget deficit has diverse impact on different economic variables.

Sriyana(2011)made that budget deficit is an important factor in increasing government spending, but also for development spending. This finding described that the government has created the fiscal trap in the long run, where an expensive fiscal policy was followed by higher deficit. This result recommends that the government allocate its spending into sectors that are more productive.

Fatima, Ahmed, andRehman(2012)analyzed the relationship between budget deficit and economic growth. For the propose, an application of unit root test and OLS model using home country data set of budget deficit and output growth for the periods 1978 to 2009. The negative impact of the budget deficit on the economic growth is because governments are short of the resources to meet their expenses in the long run. Their savings as well as revenues are not enough to meet their expenses. Different development projects started by the governments on the one hand increase their growth, but on the other hand make the administration in jeopardy to meet the actual expenses (including some unforeseen expanses).

Rise is suffering from many deficiencies which contract the scope and effectiveness of budget regarding the better allocation of resources. Pointing out the budgetary system in developing countries. "Many of the deficiencies of budgetary system of developing countries are explained by the fact that the budget is dominated by one function control and accountability of expenditure. A budget structured in this manner, however, provided little information about the government's objectives and its programs and makes the evaluation of alternative expenditure activities particularly difficult" (Beyer, 1978)

No government can afford to take taxation, borrowing, expenditure and other fiscal decision at random. On account of their inter-connection, all decision and policies decision at random. On account of their inter-connection, all decision and policies must from a part of its overall set of objectives. The whole approach has to be quite systematic if chaos and wastage are to be avoided. In general, a budget shows financial accounts of the previous year, the budget and revised estimates of the current year. And the budget estimates for the fourth coming year. In addition, the estimates for the forthcoming year are split up to two parts – those based upon the assumption that existing taxes and their rates would continue, and those based upon the proposed changes there in. a budget, in this sense, become both a description of the fiscal policies of the government and the financial plans corresponding to them (Bhatia, 2006).

Budgetary structure ,simply means the items of objectives of budget, either these are in expenditure sides or in the revenue side, which a budget incorporate within it to facilities better understanding on various ways in which the public sector transactions can take places.

The modern government has to be in position to take decision which can be crucial for the stability of country’s economy in the present and for its growth in the future. They have accepted new and wider range not only for the balance and growth of their economy but also for the social welfare of their people. This emerging phenomenon’s stresses lay emphasis on the structural reform of the budget that serves to asses at the needs arising from those new responsibilities for economic and social policy (Gupta, 1967).

A budget structure of modern government involves essentially the dewing of suitable function and programs format of the budget, but it also encompasses issues concerning the extent to which the budget reflect government and public activity.

2.2.3National Review

Beyer (1973) conducted a research on the topic "budget innovation in developing countries, the experience of Nepal". In the study he pointed out, the budgeting system of developing countries continue to be dominated by the traditional objectives of control and accountability rather than a concern for allocating limited public sector resources to well defined programs and projects that are intended to serve a set of national objectives. He came to the conclusion that, there has been no formal earmarking of revenue in Nepal. The extension of the budget coverage has involved a combination of formal and informal incorporation of expenditure activities; formal extension of the budget has involved only two relatively small expenditure activities. One is the incorporation in to the budget of the lending operation of Nepal government to its employees, which had traditionally been handled outside the budget the other formal extension involved the incorporation of foreign assistance programs, which were previously outside the budget. In short, the traditional budgeting systems are the antithesis of planning the allocation of scarce resources.

Malla(1999) made a research work on the topic "Study on Planning and Development Budget in Nepal". He was attempted to examine the allocation of development expenditure on the various sectors according to the order of priority, which is known as expenditure pattern. He remarks that expenditure allocation for various were very rough. Foreign assistance was the main sources on development financing and deficit financing is in increasing order.

He further clarify that budgeting and planning formulation and implementation is bounded by various inherent problems such as lack of the co-ordinations and co-operation between planning and budgeting agencies and sacrifices of the people, lack of the trained manpower in planning and budget sector, lack of the stable and honest administration, absence of higher mutual character and imbalance between agricultural and industrial sector.

The World Bank (2000) found that many factors have contributed in varying degrees to the lack of effectiveness of public spending in Nepal. There is little doubt that intuitionalfactor (including deficiencies in the planning, budgeting and expenditure monitoring process, as well as weakness in institution, particularly the civil-service/administration) have played a key role in the over-programming of the budget , its lack of focus and prioritization and implementation problems. The eagerness of external donors to help has also encouraged over-programming and lack of prioritizations of the public expenditure program. The lacks of ownership of project/ program at various levels and the absence of accountability, have also undermine the quality and effectiveness of public spending.

In Nepal, exercise regarding the economic classification of the budget was started from FY 1962/63. However, this classification was not without any deficiencies. As Singh S.K. has expressed the views in his book 'Fiscal systems of Nepal; "The main deficiency of this exercises was that it was based on the budget estimates rather than actual figures, since, large difference between the actual and budget figure exists; classification based on them cannot reflect the true impact of government transactions" (Singh).Beyer says, 'The measurement of a government performance through the annual budget is a fundamental component of any budgeting systems' (Beyer,2005, p. 24).

Concerning the mobilization of internal resources the revenue is most reliable source. It has been realized that on the revenue side taxation is the without the review of literature no any research work can be done. So we should deeply study the different articles, published/unpublished previous reports, bulletin, magazine etc. Literature review helps to find out new things about the related subjects.

Before 1956 budgeting in Nepal was limited on scope within the control over the public expenditure and its accountability. In this context Mr. Pant has wrote, "In the classification of the budget for the fiscal year 1951/52 and the following years, the number of items used was between eighty and ninety. Though it served quite impressively to establishes a tight control over expenditure by the ministry of finance, it also limited sharply the discretion of government officials responsible for implementing various programmers (Pant, 1970).

But, unfortunately, the budgetary system in developing count potential source of financing the public expenditure in developing countries like ours. Taxes, in general, have two major objectives in developing countries i.e. generating revenue. For meeting government expenditure and creating incentives for socio-economic development for accelerating the race of economic development Regarding the role of taxation in developing countries like ours, M.K. Dahal puts the things in sound manners, "In any country like ours where there are no discovered mineral resources, no coastal routes for the expansion and diversification of international trade, in signification industrial development and where the agriculture sectors is largely at subsistence level, taxation has a critical role to play in acceleration the pace of economic development (Dahal, 1985).

As Amatyasuggested that Nepal continues to rely of foreign budgetary grants without which its budget and balance of payments would not be viable unless the present structure is reformed and new taxes are realized, Nepal's public finance will be continue to be heavily dependent on foreign assistance for many year (Amatya, 1986, p. 105).

The above discussion makes clear that many attempts have been done to promote budgetary systems. However, Government of Nepal does not seem to be active as it is required. If proper attention is note paid in time, budgeting system have to confront serious problems in years to come.

Very few researches have been made in this area in Nepalese context: but no research is available analyzing the budgetary policy framework adopted after the restoration of democracy in 1990. Whatever the research has been made are also not in depth and details. A few dissertations have been submitted to TribhuvanUniversity thesis which is somehow related on this area. An attempt has been made to review some of these dissertations.

Singh (1977) carried out a study under the title of “the fiscal system of Nepal”.He analyzed the trend of revenue and expenditure during the period from FY1954/55-1974/75 and concluded that the expenditure/GDP ratio had increased substantially; this ratio was only 2.44 in 1955 and increased to 10.57 percent in 1975. Another notable finding of it was the rise in the development expenditure /GDP ratio. Which increased from 4.07 percent in 1996 to 6.77 percent in 1975 the growth rate of regular expenditure was comparatively slower, rising from 2.13 percent in 1966 to 3.82 percent in 1975. Integrated development studies (IDS), a renowned research center in Nepal, had carried out a study on financing of the public sector expenditure in Nepal in 1987. The study covered a period of decade from FY1974/75 to 1984/85. IDS repotted that government expenditure had grown more rapidly than that of the country, s GDP. Moreover, IDS found that a major feature of government expenditure in Nepal was the dominance of regular expenditure over development expenditure.

Ranjitkar (1987) made a research entitled “budget innovation in Nepal” in 1987. She has attempted to identify the budgetary problems and suggested some remedial measure to them. It included some theoretical aspects of budget innovation in developed countries. It has focused on the structure and the pattern of budget in Nepal. It has used secondary data published by government of Nepal and has analyzed in a meaningful manner using some common statistical tools. In this study it has attempted to examine the revenue and expenditure and make a critical assessment of the budgetary policy of government of Nepal. She has also tried to analyze the share of external and internal borrowing in the budget of Nepal.

2.3Empirical Review

2.3.1International Review

The World Bankcarried out an another study on “public finance in development” in 1998 and had drawn the conclusion that in most developing countries the share of central government spending in GDP remained below that of industrial countries; in developing countries the public sector tended to pay greater role as an investor then in industrial countries, and in most developing countries, account for important shares both of total spending and of GDP.

ADB (2005) revealed that the Nepalese economy remains well inside its production possibilities frontier, which makes future acceleration of the growth rate perfectly feasible. With 71 percent of its labor force in agriculture and underemployed, Nepal can hasten its transformation from an economy based primarily on agriculture to one based primarily on services and industry. If labor incentive services and industry grow and pull even a quarter of the rural labor force into more productive employment, the economy can be expected to grow much faster. Simultaneously, the accompanying reduction in the population pressure on farmland will help rise agriculture productivity and wages.

The World Bank (2010) found that many factors have contributed in varying degrees to the lack of effectiveness’ of public spending in Nepal. There is little doubt that institutional factors (including deficiencies in the planning, budgeting and expenditure monitoring process, as well as weakness in institution, particularly the civil-services/administration) have played a key role in the over-problems. The eagerness of external donors to help has also encouraged over-programming and the lack of prioritization of the public expenditure program. The lacks of ownership of projects/programs at various levels and the absence of accountability, have also undermined the quality and effectiveness of public spending.

Hayatiand Rahaman (2012) discussed that on the relationship between budget deficit and economic growth. While Keynesian economies claimed that these two series are positively related. The neo classical economic claimed the opposite Meanwhile, the Ricardian equivalence hypothesis argue that there is neutral relationship between budget deficit and economic growth. The objectives of this paper are to investigate the relationship between budget deficit and economic growth from Malaysia's perspective. Four variables were used namely real GDP, government's debt, productive expenditure, and non-productive expenditure. ARDL approach is used to analyze the long run relationship between all series it can cater for small size. By using quarterly data from FY 2005 to 2015, it was found that there is no long run relationship between budget deficit and economic growth of Malaysia, constant with the Recardian equivalence hypothesis. However, productive expenditure has positive long run relationship with the economic growth. In case if there is a shock in the Malaysian economy, the only variable that can help to coverage the economy to its equilibrium is the change in GDP and productive expenditure. For future recommendation, it is suggested that other researcher will enhance this research by including other developing countries as the sample analyses.

Government expenditure and inflation are positively related. It is generally believes that higher government spending leads to higher inflation as the government seeks additional sources of revenue. In this reference,Vegh had performed a comparative study of relationship between government spending and inflationary finance in a public finance context in 1996. In this theoretical study, Carlos found the following effects of government expenditure.

- The higher level of government expenditure, the larger the increase in nominal interest rate that results from a given increase in government spending.

- The more inefficient the tax collection system is, the higher is the optional nominal interest rate for a given level of government spending. And
- The share of revenues of the inflation tax is a decreasing function of government spending

From the policy perspective this theory is more useful:"especially in developing countries, a reduction in government spending should lead to reduction in an inflation tax. Because the ultimate reason for the existence of a high inflation- tax lies in the fact that the government need for revenue co-exists with increasing marginal costs of collection alternatives taxes."

Beyer (1973) conducted a research on the topic"Budget innovation in Developing countries The Experience of Nepal. This study pointed out that. The budgeting system of control and accountability rather than a concern for allocating limited public sectors resources to will be defined programs and project that are intended to serve a set of national objectives The conclusion that, there has been no formal earmarking of revenue in Nepal. The extension of the budget coverage has involved a combination of formal and informal incorporation of expenditure activities. Formal extension of the budget has involved only two relatively small expenditure activities. One is the incorporation into the budget of the lending operation of Nepal Government to its employees, which had traditionally been handled outside the budget. The other formal extension involved the incorporation of foreign assistance programs, which were previously outside the budget. In short, the traditional budgeting system is the antithesis of planning the allocation of scarce resources.

Olabisi andFunlayo (2012) showed that the relationship between the composition of public expenditure and economic growth in Nigeria. Government expenditure is expenditure is expected to be means of reducing the negative impact of market failure on the economy. However allocation of public expenditure with lack of consideration for the urgent needs of the country may engender greater distortion in the economy which may be detrimental to growth, to this end, they have analyzed therelationship between public expenditure compositions from 1960 to 2008 on economic growth using the vector Autoregressive model (VAR). The finding shows that expenditure on education has failed to enhance economic growth due to the high rate of rent seeking in the country as well as the growing rate of unemployment. They also noted that expenditure on health and agriculture should be encourage due to their positive contribution to growth while future studies is necessary to identify empirically why public expenditure on water and education are negatively related with growth.

2.3.2 National Review

Sharma (1988) made a research about the Nepalese Budgetary Structure. His research clarifies that the pattern of government expenditure has followed more or less the uniform course throughout the reference period. It is observed that government expenditure and revenue both have increased in absolute and relatives terms. Government expenditure and revenue both have increased in greater trend then the revenue. This pace has not been enough to cope up with the development objectives and targets as preceded by periodic development plan. There is inadequate mobilization of domestic resources through government revenue .Thus, he points out a serious problem of widening resources gap existing since the inception of the budget history in Nepal.

Malla (1996) conducted that a research work on the topic “Study on Planning Development Budget in Nepal”. This study attempted to examine the allocation of development expenditure on the various sectors according to the order of priority. This is known as expenditure pattern. It is remarked that expenditure allocations for various sectors were very rough. Foreign assistance was the main sources of development financing and deficit financing is in increasing order.

It is further clarified that budgeting and planning formulation and implementation is bounded by various inherent problems such as lack of the co-ordination and co-operation between planning and budgeting agencies and sacrifice of the people, lack of the trained manpower in planning and budget sector, lack of the stable and honest administration, absence of higher mutual character and imbalance between agriculture and industrial sector.

Pathak (1999) suggested that a research work on the topic”A Study on Deficit Financing in Nepal.” This study pointed out that, the main problems of the Nepalese economy is proper domestic resources mobilization. Domestic resources can be mobilized properly, if there is progressive taxation and effective borrowing system. Commodity taxation in Nepal is very popular which is said to be a regressive type of tax as compared to the income tax. Similarly, the fact is that there is chance of tax evasion and corruption resulting from administrative inefficiency and tax law. Therefore, deficit financing has becomes a necessity to some extent.

Poudel(2002) analyzed a research entitled “A Study on budgetary Pattern of Nepal”. This study covers the time span of the twenty years. In this study the pattern of government expenditure shows a significance difference between receipt (revenue and grants) and expenditure. The gap between development expenditure and revenue surplus is widening due to the growth of government expenditure as compared to the growth rate revenue mobilization. Thes Study conduct by Poudel has suggested some recommendations to improve budgeting systems in Nepal some of them are as:

a) Proper coordination between National Planning Commission and Ministry of Finance should be maintained.

b) Budget should be prepared depending upon economic prosperity.

c) Expenditure on unproductive sector should be reduced and

d) Transparency in earning and spending should be enhanced.

Khanal(2005)observed that government expenditure, revenue and their components are linearly related and it has forecasted the components of budget using the linear trend up to the year 2015/16.it is future observed that growth rate of recurrent expenditure is more than capital expenditure.

Panday(2005) conducted that a thesis of :”An analysis of Budget structure of Nepal 1990/91 to 2002/03”remarks “the pattern of government expenditures show significance difference between receipt (revenue and grants) and expenditure .Total receipt of government has covered 68.26% of the annual government expenditure in the view period. Government expenditure recorded 18.84% to GDPwhereas revenue was11.13% to GDP in average. The percentage of regular expenditure to total expenditure is increasing whereas the percentage of development expenditure is declining.

As a percent economic survey carried out inFY 2012/13it was pointed out that:

1. Gap between expenditure and revenue collection needs to be minimized for the fiscal balance, however, the increase in revenue is not keeping pace with the increase in expenditure. It therefore, calls for prompt actions towards

gearing up revenue mobilization, improvement in current expenditure management and expansion in capital expenditures.

Adjustment made in the customs duties and excise, positive change observed in tax paying attitude, increase in non-tax revenue collection, to mention a few, have provided a breathing space due to positive change in revenue collection this year compared to the past performances. To maintain this momentum, the task of tracking and plugging leakage in tax revenue lies ahead.

2. Measure to make the tax administration fully automatic, to make the customs evaluation system more objective through administrative reforms, to simplify the income tax procedures and to reduce the tax exemption callings should receive priority attention.

3. Tax revenue has an important role in revenue generation. To further reap its to enhance taxpayer awareness through tax education should go a long way in increasing tax revenue.

4. Burden of foreign debt servicing on internal revenue has been raising due to the increasing use of foreign aid in the development works. To keep the foreign debt servicing liability within sustainable limit special focus to increasing national saving rate, avoiding as well as containing unproductive current expenditure, and making the development expenditure more productive is warranted.

5. In foreign aid, grant element needs to be enhanced and its use needs to be prioritized. Overall, rational utilization of foreign aid should be a matter of constant review (MoF,2013/14).

2.4 Research Gap

All the research work mentioned above are basically related to the budgetary structure, innovation and trend etc. These studies have found different results and have been drawn different conclusions in global as well as Nepalese context. Some of this research concentrated on the area of expenditure management and some, in contrast, on public resources management. Likewise, some research works have been done on public investments and growth and some on public expenditure and civil liberties, the relationship between government expenditure and revenue, GDP and the like. However, these all studies cover only some sectors of the budgeting system.Problem and prospects of budgetary system in afterrepublic and political change in Nepal.

In the Nepalese context, as mentioned above, very few studies have been out. Some of them are deeply concerned on the trend and pattern of government expenditure in Nepal and some are guided by the perspective of taxation. Finding of these research states only the features, structure and trend of existing budgeting system.

None of the available works analysis budgetary situation in Nepal especially after liberalization of Nepalese economy, which in fact is a challenging issue among the Nepalese planner's policy makers, and social scientists hence a clear gap is seen among the research works available in the area of Nepalese budgetary system. This study entailed "An Analysis of Budgetary System in Nepal" has attempted to fulfill this research gap and to suggest some policy recommendations for the future budgetary practice.

CHAPTER III

RESEARCH METHODOLOGY

3.1Research Design

The study is primarily based on secondary dataand descriptive, analytical as well as quantitative approach is developed to examine the issues. The study is an examination and evolution of the budgetary policies as incorporated in the budget documents presented by the democratic government in Nepal after the restoration of multi-party democracy system in 1990. Therefore, the study is mainly related with the various budget documents have been tabulated and presented in meaningful order. Among them trend analysis has been made extensively .The research is mainly based on secondary data. The presentation of trend and pattern of budget and relationship between the variables is the main concern of the study. The available data will be reclassified. Regrouped and analyzed in order to make them useful in examining the objectives of the studyto make the information easily understandable and visible. Then the information easily understandable and visible, the data will be presented in graphs and figuresbesidethis qualitative aspect of the budgetary policies their implementation and actual outcomes.

Linear Regression Analysis

Linear regression linear fitted between the variables based on the observed data if it is felt that the linear relation between two variables exists. The independent variable is denoted by x and dependent variables is denoted by y in such case the relationship between y and x is given by

Y=a + bx

Where a and b are constant to be obtained from the regression analysis. Value are estimated by

$$b = \frac{\sum xy - n.\bar{x}\,.\bar{y}}{\sum x^2 - n.x^{-2}}$$

a = $\bar{y}$- b$\bar{x}$

And degree of fitness between the variables under consideration is evaluated by the coefficient of determination R^2given by

$$R^2 = \frac{\sum xy - n.\overline{x}.\overline{y}}{\sqrt{\sum x^2 - n.x^{-2} \times \sum y^2 - n.y^{-2}}}$$

3.2 Nature and Sources of Data

This research is mainly based on secondary data published by various Government Organizations like CBS, GoN, MosF, NRB, CEDA etc. they are : GoNMinistry of Finance (MoF): Various issues of Budget Speeches Economic Surveys ,National Planning Commission (NPC): Three year plan (067/68-069/70), Nepal RastraBank (NRB), : various issues of QuarterlyEconomic Bulletin, Economic Report and Current Economic Situation of the Nation, Central Bureau of Statistics (CBS): Various issues of Statistical Yearbook and Statistical pocket book and Center for Economic Development and Administration (CEDA).

3.3 Tools and Technique of Data Collection

This study is based on the secondary data collection as stated above in 'nature ofsources of data collection.' The data information and policies extracted from the budget documents have been tabulated and presented in meaningful order.The presentation of trend and pattern of budget and relationship between the variable is main concern of the study. To make the information easily understandable and visible the data will bepresentation in figure and table.

3.4 Presentation and Analysis of Data

This study is based on the secondary data. Data collection as started above in sources of data information. Processing of data has been done in computer using application programs like MS WORD, MS EXCELetc. Some mathematical and financial tools have been applied in analysis and interpretation. Presentation has been made in from of table and figures etc.

3.5 Selection Period

The period taken for the study is from FY 2005/06 to FY 2014/15. That is the analysis is basically for the periods since the economic reforms. Started country in 1990, democracy was restored on the country, the governments then formed center this periods is supposed to be the appropriate to analyzed trend and pattern of budget in the country.

CHAPTER IV

BUDGETARY SYSTEMIN NEPAL

4.1 Introduction

Nepal’s budgetary evolution spanned more than six decades since 1951 when the budgetary process initiated.GoN, after the restoration of multi-party democracy, adopted the open and liberal economic policy and, in the process has been repealing the prevailing restrictive rules, regulations, laws and directives governing the economic policies one after another with great zeal and vigor. Budgetary policy has also undergone change to that direction since the very first budget of the multi-party democratic government. Growing challenges encountered in relation to rising expectation of the people have encouraged government to reconsider the mines that could manage scarcest resources in a more organizes and effectiveness manner. GoN has been responding to these expectation in various ways including strengthening program, budgetary practices, delineation of budget, classification of income and expenditure heads to make it more comprehensive and informative, clear enunciation of objectives pursued by the particular budget, its linkage with national development objectives an compatibility with the policy of liberalization. Budget is a part of economic plan. Therefore, while formulating budget it is necessary to determine resources allocation in conformity with the objectives, programs and strategist setting plan documents.

Now for the further structural reform of fiscal management and expenditure control, the GoN intends to undertake wide ranging reform to rationalize the expenditure program and improve budget planning by prioritizing both donors supported and fully government funded projects, strictly controlling fund releases, strengthening the administration of project implementation and improving projects monitoring.

4.2 Historical Background

Nepal’s has not very old story to tell about the intuition of systematic budgetary system in the country. It has been only six decades after the Rana regime was overthrown in 1951 the first budget was formulated. For convenience, the historical background of budget of Nepal has been divided in three different phases:

4.2.1 Before 1951

During the period before 1951, the state treasury was under the sole control of the Rana Prime Ministers. The country remained isolated from the outside world and the few ruling elites had no concern of the well-being of the country and its people.

The treasury offices in different district headquarters were responsibilities for collection of revenue and disbursement expenditure. The central levels office responsibilities to control the whole exercise was Kumari-Chowk, the state treasury offices, therefore, the amount of the government expenditure was limited. Any budgeting systems and economic development through planning were not implementation at that time.

4.2.2 After 1951

After the political change of 1951 in Nepal, the responsibility of the government to launch different programs increased. For these purposes, discussions that are more practical appeared in the planning sector. In 1952, first national budget was pronounced and after this. The national budget is formulated every successive year.

In those days, the budget used to conation just the revenue estimates from different sources and the expenditure needed for different heads. Later on in 1958 as the development planning started, the government being to increase the budget size and the customary budgeting process was changed. The budget started to have two portions i.e. regular budget and development budget. The former to deal with the ordinary expenditure of the government and to maintain the law and order while the later to deal with the expenditure as provided for the development plans. In fact, the first development plan was introduced in the FY1958/59 under the heading of “plan account”.

In the budget history of Nepal, FY1962/63 is of much importance because some structural change in the budget took please from that fiscal year. In 1962, a functional classification scheme was introduced and it has been prepared in continuous basis from that year with some reform measures. Economic classification of budget was also taken place in the budgetary system to the country since them.

Nepal incurred large fiscal deficits following the 1980 referendum, the verdict of which went in favor of the party less panchayat system against the multiparty systems. Successive governments formed after the referendum followed an expansionary fiscal policy. The widened deficits put pressure on the balance of payments leading to a deficit for three consecutive years FY 1982/83 to 1984/85. It was this crisis on the external front that forced the government to initiate economic reforms. The types and contents of economic reforms were largely the result of negotiations conducted with the IMF and the World Bank for financial assistance.

4.2.3 Budgetary Experienceafter1990

Government of Nepal, after the restoration of democracy, adopted the open and liberal economic policy and, in the process, has been repealing the prevailing restrictive rules, regulations, laws and directives governing the economic policies one after another with great zeal and vigor. Budgetary policy has also undergone change to that direction since the very first budget of the multiparty democratic government. Many reform measures in the fiscal sectors were introduced and initiated on both the revenue and the expenditure side. It is because of this study focuses the budgetary trend only after the year 1990/91.

During the first half of the 1990s, Nepal went through a period of fiscal consolidation as an integral part of an economic liberalization and reform program. Nevertheless, the expansionary fiscal policy adopted by a succession of short-lived governments during the latter half of the 1990s resulted in an increase in fiscal deficits debt stock and debt-servicing obligations.

Two measures were taken to widen the tax base. The first was reduction in both the tax rates and slabs of various taxes prior to the reform, tax rates were as high as 300percent.An excessively higher rate encourages tax evasion and act as a disincentive for further production. Consequently, revenue mobilization falls below the potential levels. Under the circumstances, rising revenue lowering tax rates with a view to widening the tax base and improving tax collection, Nepal lowered the tax rates. Similarly, the number of tax slab of earlier years that have made tax administration too cumbersome. However, it has been realized that lowering the tax rates without the commensurate improvement in revenue administration and an orderly tax systems does not produce the intended results. As such, reforms n revenue administrations were also introduced.

In direct tax which was domination in the Nepalese tax system had exemption and loopholes. The systems did not cover all commodities and services produced and distributed within the economy. As such, it had a narrow base. Realizing this and under the advice of multilateral agencies such as the IMF and the World Bank, Nepal introduced the VAT, a unified indirect tax instruments. However, because of the opposition from the business community, the introduction of VAT was frequently postponed before it was finally implemented.

4.3 Preview of Budget System

The budgetary process in larger governmental unites involves four steps: preparation and submission of the budget to legislative body, enactment of authorization and appropriations legislation, execution and audit. Responsibility for preparation of the budget usually rests with the executive branch of government-assisted; in larger government by special budgetary experiences that handle the work of preparation, under the jurisdiction of the chef executive. The first cycle of budget takes several months for preparation, but developing countries budget is prepared with in a period of few weeks. Budget is formulated at a time for two consecutive years in developed countries ensuring continuity in policies and programs and providing effectively delivery of goods and services to the people.

4.3.1 The Formulation Process

The budget formulation consists of the four steps or phases, which are also known as budget cycle:-phase 1) Preparation, phase 2) Enactment/Legislation, phase3) Execution, Phase4) Auditing

4.3.1.1 Preparation

The process of budget formulation beings with resources estimation. Activity starts at ministry of finance (MoF) with the Resources Committee (RC).comprising Vice-Chairperson of National Planning Commission (NPC), financial Controller general and MoF Secretary. The RC determines the size of the budget by analyzing overall economic situation of the country with the help of macro-economic indicators. Resources estimates comprise estimate of revenue, foreign lone, grant and domestic borrowing. Upon accomplishing resources estimation the Resources Committee sets the ceiling for budget for the next fiscal year. The budget ceiling is fixed considering availability of both internal and external resources. The NPC sets out the priority and policy goals with respect to plans and programs for forth coming fiscal year and provide necessary guidelines to the concerned Ministry and Ministry of finance, prior to sending of the circular for preparation of budget (Budget Manual, 2000). In the mid- fiscal year, the ministry of finance issues budget circular to all sector's Ministries and Constitutional Bodies directing them to prepare the budget with following information:

- Ceiling of funds including external assistance available for each ministry for various budget funds.
- Formats to be used for various estimates and instructions to be followed in preparing the estimates.
- Policy guidelines to be followed in prioritizing activities.

Immediately upon receiving the circular, budget preparation at the ministry levels beings form the project levels to be followed by a detailed discussion and scrutiny in the planning division of the ministry. Estimation of foreign aid on the following basis:

- Review of project documents including project agreements, minutes of Understanding (MoF), staff Appraisal Report, Master plan of Operation, and so on.
- Discussion and interaction with the counterpart donors held at the Ministry to identify whether their commitments along with the governments counterpart funds are correctly reflected.
- With all this information, the respective Ministry submits the budget proposal and the annual program-one each to NPC and MoF in the beginning of third trimester of the fiscal year.

The first round of budget discussion takes place at NPC in the case of capital/ development budget in April/may participated by the line agency staff along with NPC and MoF staff, when the proposed program is critically examined in the perspective of policy guideline and the circular and the Mof staff assess the aid-involved projects in the context of the confirmed and unconfirmed commitments of the respective donors. The discussion at NPC refers to,

- Projects to be funded under external assistance are retained as far as possible.
- There are some cuts and adjustments when grants assistance needs counterpart funding.

- Projects not supported by firm commitment or those, which depends upon availability of funds, are taken out.

Although no donors are invited in the budget discussion at NPC, they get all these feedback from their counterpart staff. If the discussion goes against the interest of donors, they can influence the process at the policy level. The final round of discussion takes place at MoF, representatives by the concerned ministries/ departments/projects and NPC staff.

- Interaction takes place with the concerned projects/ministries/departments to confirm donor's commitment to the project.
- Projects needing counterpart finding are examined critically when MoF often makes unilateral cuts, reduces government counterpart funding budget and raises aid portion without information the respective donors.
- Donors keep an open eye on those cuts and some donors may pressure through the concerned ministries and secretaries not to deviate from the original proportion and maintain at least the counterpart funding specified in the project document.

In view of all these factors specified above, MoF prepare a statement. Of expenditure (Red Book) containing description of all estimated expenditure for each sector, ministry, which would be ready by June/July. During these periods, considerable pressure may come from the politicians, particularly the MPs and DDC Chairman, to adjusted development programs to their constituencies resulting in bigger size of budget in excess of available resources.

The role of revenue consultative committee (RCC) set up mat national level under MoF is also significant particularly in the context of attaining growth, equity and stability objectives of taxation. The RCC is an apex body to provide recommendations for designing policies, determination tax base and tax rates, setting the level of exemptions and personal and business deductions.

4.3.1.2 Legislation/ Enactment

Enactment/Legislation is the second step of budget formulation. The phase enactment beings with budget speech by the finance minister at the joint session of parliaments in the second or third week of July. It is followed by a brief discussion of the underlying budgetary principles and policies. The minister also submits an appropriation bill is accompanied with a description of programs and their regional distribution, the discussion in parliament lasts for one and half to two months, when subjects are analyzed item wise, followed by a voting on the bill in parliament in September. After about one to two weeks from the date of parliamentary approval of the bill, the bill gets the royal assent to become an Act.

Government of Nepal and donors to the respective programsafter the presentation of appropriation bill, the finance minister presents the advances bill seeking authorization to release certain fixed amounts to the government till the budget is passed.

The appropriation bill is accompanied with a description of programs and their regional distribution (Red Book). The discussion in parliament lasts for one and a half to two months, when subjective are analyzed items wise, followed by a voting on the bill in parliament in September. After about a one two weeks from the date of parliamentary approval of the bill, the bill become the Act.

4.3.1.3 Execution (Implementation)

Implementation is also called the procedure of releasing budget. The process of fund release starts with the approval of the budget by the parliament. After the parliament approves the budget, the budget implementations require two future steps. They are:(i)finalization of work programs consistent with the ratified budget for each spending unit by the respective line Ministries and their approval by NPC, and (ii) the formal delegation (through official notification) of authority to spend by the secretary of finance to sectors Ministries and then to project managers. These procedures unnecessarily hold up implementation for several weeks, and very little work is carried out in the first trimester of the fiscal year. Immediately after completion of the discussion on the underlying principles and policies, the Finance Ministries puts before the parliament the Vote on Account Bills, which authorizes the government to spend a specified amount in advance. The process for releasing budget is given below.

a. Whereas up to one-third of the previous year's 'expenditure was often released under the advance bill before, the government can advance up to one –third of the budget for core projects, two-third or one-sixth for remote projects and one-sixth for regular and other programs, Subsequent release can follow after the Appropriation bill gets of the Head of the State assent.

Budget release will be made on a monthly basis. In the past, trimester budget release was in practice. However, the Financial Controller General Office (FCGO) has maintained the trimester and lump sum system for subsides (DDC,VDC,Education, health, Public Corporation, Companies),controlled budget (Medical Care, Gratuities) and others.

b. For donor-funded projects, budget will be released on a pre-funding (donors have to put deposit to GoN, treasury in advance) and reimbursement basis (applied for loan-financed projects and to some extent for bilateral donor-financed projects depending upon the agreement.)

c. The system of impress account and Special established under ADB and World Bank-financed projects have also been maintained under which the project authority can withdraw directly from the said account.

The budget release system, however, is not automatic. Its release is subject to the following conditions;

After the approval of the Appropriation bill, MoF will inform the entire sector Ministries on the project details of the approved budget, and send the Sources Book onForeign Aided projects and letter of authority for all expenditures to all ministries, FCGO and Auditors General‘s Offices (AGO). Line ministries also forward such budget details and authority latter for expenditure through their concerned Department/project coordinator Offices (PCO) to the district line agencies with copies to the FCGO and each District Treasury Offices (DTO).

- The department/PCO prepares the unit/wise program supported by budgetary details both source-wise and items-wise and forward it so the NPC and line agencies. In that process, the central levels projects will be approved by the NPC and the district level project by the ministries concerned.
- After the approval of the program as maintained in (a), the Dept. / PCO make available to each unit under it the program and budgetary detail. Then each project unit and PCO submit the monthly release respects from a long with

copies of the approved program and authority letters giving budgetary details to the nearest DTO.

The FCGO and DTO play important role in the budget release process. The DTOs process all request and will release the funds requested to respective agency's bank account. DTOreleases the fund upon the receipt of the following documents.

(a) Authority letter from the concerned ministry,

(b) Release order to DTO by FCGO.

(c) Project/program duly approved by NPC and document In the budget,

(d) The FCGO release funds on a monthly basis, provided the above mentioned condition are fulfilled and the budget requests tally with the sources book,

(e) DTO release the fund only after receiving the statement of expenditure of the previous month from the requesting agency,

(f) DTO is also empowered to release the donor portion budget on a reimbursement basis, if so provisioned in the sources book,

(g) In the case of pre-funding arrangement in the sources book, budget is released to the extent of donor contribution available.

4.3.1.4 Auditing

The final phase of budget cycle is auditing. This is the overall responsibility of the Auditor General (AG) to prepare the annual report after accomplishing auditing of all government transaction. The AG presents its annual report to GoN , which is later forwarded to parliament for discussion and implementation. Unfortunately, financial irregularities are found at staggering magnitude, which is indicative of growing corruption in government organizations. Stringent condition with server punishment is required to check financial irregularities. In many state-owned enterprises (SOEs) and DDCs auditing is pending for many years, yet there is no action against form the center there is also growing demand from the civil society that political parties too audit their account by the Office of the Auditor General and publish in media.AG submits the report to government and presented in parliament for discussion and implementation of the suggestions.

4.4 Historical Overview of Annual Budget in Nepal

4.4.1 Review of Annual Budget

The Fiscal policy of government is translated practice by the budget. Thus the budgetary policy occupies an important place in the overall economic policy of the Government. Any change in the socio-political regime remains incomplete unless the budgetary policy of the government also is changed accordingly. The government of Nepal, after the restoration of multi-party democracy has adopted the open and liberal economic policy and in the process it has been repealing the existing restrictive rules, regulations, laws and directives governing the economic policies one after another with a great zeal and vigor. Budgetary policy has also undergone changes to that direction through the very first budget FY 1991/1992 of the multi-party democratic government. In this context, it seems pertinent to study the budget objectives .government commitments and the budget policies to know the trend and direction of fiscal policy .An attempt has been made to review these major aspects of the budget as incorporated in the budget speeches for the period after the restoration of multiparty democratic system in 1990.

Budget 2005/06

Mr. MadhukarShumsher J.B. Rana, the finance minister of the government presented the budget of the kingdom of Nepal for the FY 2005/06 the actual expenditures of the government of the expenditures totaled Rs.110 billion 889.2 million, of which the recurrent expenditures were Rs 67 billion 17.8 million, capital expenditures were Rs.67 billion 17.8 million, capital expenditure Rs.29 billion 606.6 million & repayment of dept principal Rs.14 billion 264.8 million.

The medium term vision of this budget was to create foundation for prosperous new Nepal, within three years, by contributing to the political, Social and economic sectors and by reducing the level of poverty, mainly in the period of three years:

1. Peace would be restored,
2. Economic stability would be maintained in order to attained higher economic Growth rate,
3. Representative political institutions would be developed to make Nepal transiteconomic between India & China.

The main mission of this budget of this budget was to put into a respectable positionin the country of the nations by restoring peace, achieving prosperity and reactivatingdemocracy by means of pursuing market oriented policy and protecting people's lives& property level to below percent & meeting the MillenniumsThe Development Goals(MDGs)

Main objectives of this budget were as follows:

1. To invest for the restoration of the peace,
2. To pave for stabilization of private sector in a leadership role in the developmentof economic sector, and
3. To improve the economic, human and social indicators of the ultra-poor anddeprived groups.

It was estimated to achieve the macro-economic growth of 4.5% with an increase in4.0% in agriculture & 4.8% in non–agricultures sectors in FY 2005/06. Similarly, would be expected to remain inflation narrow money supply and broad money supply at his rate of 4.9% 12% % 13% respectively .Revenue mobilization would beexpected thus at 14.10% of the Gross domestic product after policy related changes inthe revenue % the administrative reforms

Sources: Economic Survey, FY 2005/06, MoF, Kathmandu

Budget 2006/07

Finance minister Dr. Ram Sharan presented coalition government in the house ofrepresentative at the strength of people's movement after a parliament vacuum of thefour years. The budget for FY 2006/07 was of Rs. 131 billion 851 million of whichrecurrent expenditure would reach Rs 80 billion 331.1million, capital expenditureRs.36 billion 379.9 million and repayment of dept principal Rs 15 billion 140 million.

Following were the objectives & priorities of this budget:

1. To institutionalize the democratic system;
2. To develop economic infrastructures
3. To improve investment climate;
4. To make economic programmed pro-poor and inclusive;

5. To implement programmers’ for relief, rehabilitation and reconstruction: and
6. To increase capital investment & productivity by containing consumptionexpenditures.

   Sources: Economic Survey, FY 2006/07, MoF, Kathmandu

Budget 2007/08

Dr. Ram SharanMahat, finance Minister of the interim government after second historical people's revolution & the peaceful commitment process between Nepal govt.& Maoists , presented the budget for FY 2007/08 to the interim parliament. The 168 billion & 995.6 million budgets included Rs 98 billion 172.4 million and 91 thousand has been expected for recurrent expenditure and Rs.55 billion 261.6 million & 82 thousand for capital expenditure. And Rs.15 billion 561.4 million and 27 thousand for principal repayment. This estimate is higher by 17.14 % as compared to total allocation of FY 2006/07 & 28.2% higher than revised estimate of the same period. The revised expenditure as compared to estimate 22.2 higher in recurrent expenditure and 51.9% in capital expenditure, & 2.8 in repayment of the principal .

Of the total expenditure of Rs.93 billion 743 million and 45 thousand has been earmarked for general administration, & Rs.75 billion 252.5 million and 55 thousand for development programs.

Out of the total estimated expenditure Rs.900 billion 605.9 million and 56 thousand will be borne from current source of revenue, Rs. 27 billion 460.9 million & 14 thousand from foreign grant & Rs.017 billion 367.4 million 44 thousand will be mobilized from foreign aid. However, despite resource mobilization from these two sources, there will be difficult of Rs.24 billion 561.3 million.

The budget of the FY 2007/08 had the following objectives:

1. The sustainable peace, stability & strengthening of the Democratic system,
2. Poverty Alleviation & Economic prosperity
3. Investment Promotion;
4. Human Development; and
5. Reconstruction, Rehabilitation & Relief.

   Sources: Economic Survey, FY 2007/08, MoF, Kathmandu

Budget 2008/09

Dr. BaburamBhattrai, finance minister of Maoists lead government after the electionof constitutional assembly presented his budget on constituent assembly on 19th September, 2008 for the FY 2008/09. The Maoist lead government is also acoalition government, thus his budget also on the base line of Dr,Mahat budget andnothing extra ordinary on it because the main objectives of the budget is to maintainpeaces and security throughout the nation by setting down Maoists combatants.

The government expenditure in the FY 2008/09 totaled Rs. 219,661.9 million.Out of that total expenditure, revenue mobilization financed 65.3 percents, foreigngrants 12.0 percents, and foreign loan 4.5 percent, and foreign loan 4.5 percent, domestic borrowing 8.4 percents whilechange in reserves shared 9.8 percent. The recurrent expenditure in the FY2008/09 totaled RS.127738.9 million, which is 39.7 percent higher than that of theprevious year, which was RS.91446.9 million for the previous fiscal year. Of the totalrecurrent expenditure in the FY 2008/09, major portion of such expenditure(RS.47437.9 million) was on health, education, drinking water, local development andother social services

Capital expenditure in the FY 2008/09 rose by 36.6 percent compared to theprevious fiscal year totaling Rs.73, 089.0 million. Such expenditure in its precedingyear was Rs.53, 516.2 million. And in the FY 2008/09, interest repayment onprincipal stood at Rs.18, 834.1 million. Such expenditure was Rs.16, 386.9 million inthe previous fiscal year of the total principal repayment expenditure, the share ofprincipal repayment against domestic borrowing remained at 46.3 percent and that offoreign loan 53.7 percent in the FY 2008/09 .when compared to the previousFY, principal repayment in the FY 2008/09 against domesticborrowings has increase by 2.3 percent while that of foreign loan has decrease by34.9percents.

The budget of the FY 2008/09 had the following objectives:

1. Making democracy more people centered with the institutionalization of thefederal democratic republic.
2. Sustaining peace in the country by bringing to logical conclusion the peaceprocess on the basis of the Comprehensive Peace Accord (CPA) agreed betweenthe Nepal Communist Party (Maoist) and the seven political parties.

3. Accelerating the process of economic and social transformation to accomplish thegreat mission of building just, advanced and prosperous new Nepal.
4. Achieving higher economic growth that comes along with geographical andregional balance, social justice and employment opportunities.
5. Providing immediate relief to the people to make them feel that the country hasreally become a republic.
6. Erecting foundation of a self-reliant and independent economy through optimallymobilizing the national capital and indigenous resources.

   Sources: Economic Survey, FY 2008/09, MoF, Kathmandu

Budget 2009/10

Mr.SurendraPanday, finance minister of the coalition government presented hisbudget in the constitutional assembly for the FY 2009/010 on Monday 13thJuly 2009.He has nothing change in his budget due to coalition government. The totalexpenditure of Nepal government in the FY 2009/10 was Rs.259.69 billion. Ofthis.58.2 percent was recurrent and 34.7 percent capital expenditure while 7.1 percentaccounted for repayment of principal.

The government expenditure in the FY 2009/10 totaled Rs.259.69 billion. Outof that total expenditure, revenue mobilization financed 69.3 percent, foreign grants14.8 percent; foreign loan 4.3 percent domestic borrowing 11.5 percents while changein reserves shared 0.02 percent. The recurrent expenditure in the FY 2008/09total Rs.151.19 billion which is 18.2 percent higher than that of the previous fiscalyear, as compared to Rs.127.74 billion. Of the total recurrent expenditure in the FY 2009/10, major portion of such expenditure (RS.62.43 billion) was on education,health, drinking water, local development and social services

Capital expenditure in the FY 2009/10 rose by 23.5 percent compared to theprevious fiscal year totaling RS.90.24 billion. Such expenditure in its preceding yearwas RS.73.89 million and in the FY 2009/10, interest repayment on principal stood at RS.18.43 billion. such expenditure was Rs.18.83 billion in the previous FY of the total principal repayment expenditure, the share of principal repaymentagainst domestic borrowing remained at 14.7percent and that of forging loan 58.4percent in the FY 2009/10 .when compared to the previous FY,principal repayment in the

FY2009/10 against domestic borrowings hasdecrease by 11.8 percent while that of foreign loan has increase by 6.2percent.

Main objectives of the budget were:

1. To facilitate promulgation of the new constitution as per the people'sexpectations and bring the peace process to an end
2. To create employment by encouraging roles and investments of the co-operatives, private and public sector pursuant to the concept of inclusive development
3. To emphasize the development of large physical and economic infrastructure forrapid economic growth.
4. To intensify the relief, reconstructions and rehabilitation for the conflict affected,and
5. To provide relief to the people by controlling prices and facilitating supplysystem.

Sources: Economic Survey, FY 2009/10, MoF, Kathmandu

Budget 2010/011

Mr. SurendraPandey, finance minister of coalition government delivered his budgeton the constituent assembly on 12 July 2010 regarding the special arrangement forrevenue and expenditure for the FY 2010/11.Total expenditure of NepalGovernment in the FY 2010/11 were Rs 295.36 billion. Of this, 57.7percentwas recurrent, and 36.5percent capital expenditure while 5.8 percent accounted forrepayment of principal.

The total government expenditure that increased by 18.2 percent in the FY 2009/10 compared to its preceding FY grew by 13.7 percent in the FY 2010/11. Of this, recurrent expenditure had increased by 18.2 percent in the FY 2009/10 while this category of expenditure grew by 12.8 percent in the FY 2010/11.The capital expenditure in the FY 2009/10 had increased by 23.5percent in the previous fiscal year, which recorded a growth of 19.5 percent in FY 2010/11. The principal repayment had decreased by 6.6 percent in the FY2010/11 in comparison to its decrease of 2.1 percent in FY 2009/10.

Government expenditure in the FY 2010/11 totaled Rs 295.36 billion .out ofthat total expenditure, revenue mobilization financed 67.7 percent, foreign grants 15.5percent foreign loan 4.1 percent domestic borrowing 14.4 percent while change inreserves stood at -1.7 percent. Recurrent expenditure in FY 2010/11 totaled Rs170.29 billion, which is higher by 12.8 percent compared to the previous fiscal year.Recurrent expenditure in FY 2009/10 was Rs 151.02 billion. Of the totalrecurrent expenditure incurred in the FY 2010/11 education, health, drinkingwater, local development and other social services absorbed largest share (Rs 70.54billion).

Capital expenditure in the FY 2010/11 rose by 19.5 percent as compared to theprevious fiscal year totaling Rs 107.81 billion. Such expenditure in FY 2009/10 was Rs 90.24 billion. In the FY 2010/11, principal repaymentexpenditure stood at Rs 17.22 billion. Such expenditure was Rs18.43 billion in theprevious FY. Of the total principal repayment expenditure, the share ofprincipal repayment against domestic borrowing remained at 34.9 percent and that offoreign loan 65.1 percent in the FY 2010/11. When compared to the previousFY, principal repayment in the FY 2010/11against domestic borrowinghas decreased by21.9 percent while that of foreign loan has increased by 4.4 percent.

Sources: Economic Survey, FY 2010/11, MoF, Kathmandu

Budget 2011/12

- Honorable finance minister, Mr.Bharat Mohan Adhakari presented the budget at the constitution assembly hall for the FY 2011/12. On Friday July 2011. Budget Rs 384.90 billion for FY 2011/12.

This budget has not most important for the policies and programs of budget

- Establishment of peace, formulation of consultation & sustainable resolution of conflict,
- Reform in public services delivery &supply system to provide relief to general public,
- Social justice & inclusive development,
- Highly remote & backward area development program and gender equality empowerment.

- Ownership and access enhancement of poor &disadvantage land,
- Transforming agriculture sectors & its commercialization,
- Promotion & expansion of cooperatives as a main pillar of the economy,
- Road ,bridge & other infrastructure development ,
- Youth self-employment generation through public, cooperatives & private s
- Good governances & administration reforms.

During FY2011/12, the total government expenditure was Rs. 339167.48 million, which constitutes 88.12% of the initial estimates. Recurrent expenditure Rs. 66613 million as a percent 69.27%, capital expenditure Rs.72607 million as percent 18.86% and financing Rs.45680 million as a percent 11.87%. The total expenditure is increased by 14.83% as compared to the previous FY total expenditure of FY 2010/11 was Rs. 295363 million.

Sources: Economic Survey, FY 2011/12, MoF, Kathmandu

Budget 2012/13

Finance ministerMr.,ShankarPrasadKoirala presented the budget FY 2012/13 in an April 2013.The size of the budget Rs. 404.82 billion of the FY. This budget focused for the to achieve broad based high economic growth, economic stability, infrastructure development, agriculture sectors development, energy sectors development, good governances and political stability these are the main objectives of the FY2012/13 budget.

Out of these Rs.279.1 billion or 68.92% allocated for the recurrent expenditure, Rs. 66.13 billion or 16.34% for capital expenditure and Rs. 59.67 billion or 14.74% for the financing provision. The total expenditure is increased by 5.74% as compared to the previous FY 2011/12 was Rs. 339167 million.

The main objectives and priorities of this budget is given below,

- To achieve broad based high economic growth to graduate Nepal from least developed to developed country status to the level of developing countries by 2022,
- To maintain economic and fiscal stability,

- To make the economy dynamic by conducting the economic activities of the nation through public private and cooperatives partnerships sectors development,
- To make public services and easily accessible,
- Development extension and promotion of hydropower and energy sectors,
- Increase in Agricultural productivity and its commercialization and marketization,
- Construction of physical infrastructure,
- Easy access and qualitative, improvement in education, health, drinking water & sanitation,
- Tourism promotion,
- Import substitution and export promotion and

  Improvement in public good governances and services delivery.

  Sources: Economic Survey, FY 2012/13, MoF, Kathmandu

Budget 2013/14

Mr. ShankarPrasad Koirala,Finance minister of the government delivered his budget on the 14 July 2013 regarding the special arrangement for revenue and expenditure for FY 2013/14. The total expenditure of Nepal government FY 2013/14 was, Rs. 517.24 billion for the implementation of the policies and programs of the budget for the FY2013/14 Out of this Rs. 353.42 billion or 68.33% for recurrent expenditure Rs. 85.10 billion or 16.45% for capital expenditure, Rs. 78.72 billion or 15.21% for financial expenditure. Allocation is 39.75% higher than the revised estimates of the current fiscal year of the total allocation proposed Rs. 241.58 billion or 46.7% for the development expenditure and Rs. 275.66 billion or 53.3% for general administration.

The main objectives and priorities of this budget given below,

- To help conduct the election of constituent assembly scheduled for 19 November 2013, in a free, fair and credible manner,

- To achieve broad based high economic growth to graduate Nepal form least developed country to developed country status to the level of developing countries by 2022,
- To maintain economic and fiscal stability,
- To make economy dynamic by conducting the economic activities of the nation through public, private and cooperatives sectors,
- To increase the coordination private sectors by creating investment friendly environment,
- To focus for sustainable, balanced and employment oriented inclusive development,
- To make public services simple and easily accessible,
- Development, extension and promotion of hydropower and energy sectors,
- Increase in agriculture productivity and its commercialization,
- Contribution of physical infrastructure,
- Easy access and qualitative improvement in education, health, drinking water and sanitations.
- Creating investment friendly environment for the development of private sectors,
- Import substitution and export promotion, and tourism promotion.

  Improvement in public service delivery and good governances.

  Sources: Economic Survey, FY 2013/14,MoF, Kathmandu

Budget 2014/15

Finance minister Dr. Ram SharanMahat presented full annual budget of Rs. 618.10 billion (PY517.24 billion) of Sunday, Ashad 29, 2071 (July 13, 2014) for the financial year 2071/72 (2014-15) through finance Act, 2071.

This budget has been given utmost important to Energy sectors, Agriculture sectors and infrastructure sectors. Out of the total budget, Rs.398.98 billion (64.50%) as against previous year budget of Rs. 353.42billion (68.33%) will go to recurrent expenditure's Rs. 166.76 billion (18.90%) previous year Rs. 85.10 billion (16.45%) to capital expenditure and Rs 102.39 billion (16.60%) previous year Rs. 78.22 billion (15.22%) for financing provision (i.e. principle repayment of lone).The size of budget is 19% previous year 28% more than previous year's budget.

The budget aims to collect Rs. 422.90 billion (PY Rs.354.50 billion) from revenue, Rs.73.39 billion (PY Rs. 69.54 billion) from foreign grants, Rs 49.52 billion (PY Rs. 43.70 billion) from foreign lone, Rs. 1 billion (PY Rs 5.5 billion) from repayment of principle and Rs. 52.75 billion (PY Rs. 44 billion) from internal loans.

The GDP growth is estimated at 6% (PY5.5%) and inflation rate at 8% (PY 8%). The direct tax provision contained in the finance Act, 2071 (2014) will generally apply to the financial year ending Ashad 32, 2072 (July 16, 2015) unless specifically stated otherwise. The indirect tax provision shall apply immediately on its announcement.

Focusing on the economic reforms, energy sectors, infrastructure, and others, the government announced the budget for the FY 2014/15 incorporating few new programs, including the Constituency Development Fund (CDF).

This budget gives continuity to most of the programs included in the previous year's budget.

The hike in the salaries and allowances to the civil servants has significantly tacked up recurrent expenditure.

The objectives & priorities of the budget

- Energy sectors,
- Agriculture sectors,
- Infrastructure sectors,
- Petroleum products,
- Textile industries,
- Services industries ,
- Telecom,
- Government vehicle, and general

Sources: Economic Survey, FY 2014/15MoF, Kathmandu

Conclusion

The budgetary policy measures taken by the coalition government during the periodof transition adopts the policy towards liberalization along with providing peace andsecurity to the people of the nation. But these policies are quite inadequate in terms ofdesired results due to instability caused by Maoists insurgency.

The each and every government in this decade try to establish long term sustainablepeace, harmony, investment friendly environment along with prosperous Nepal. Butthese objectives of the government could not achieve due to frequent change ingovernment and lack of common minimum agenda in politics (Especially in the fieldof economic policies focused on budgetary policy).

Looking at the expenditure trend of this decade, the share of recurrent expenditure in total expenditure remained close to 60 to 62 percent between FY 2005/06 and 2010/11 while such ratio has declined in subsequent years, which is considered as positive from public financial management perspectives.

During the past one decade after the restoration of the multi-party democratic system, the democratic government also seems unable to introduce new, bold and brilliant measure to mobilized domestic resources. Recently a major feature of budgetary development has been growing dependence on foreign lone for deficit financing. Around 70 percent of the development expenditure has been proposed to be financed through the foreign sources. This is not a happy situation for the country like ours which has already borne its development expenditure upon foreign assistance (grants and lone) could not be broken even by the democratically elected government. So much remains to be done in the area of budgetary elected government. So much remains to be done in the area of budgetary policy if it has to be made consistent with the overall macro-economic policy some suggestion has been presented in the last i.e. Summary, Finding and Recommendations.

Budget is an important aspect of government activities. It is one of main instrument of fiscal policy. Budget incorporates many public policy and figure of government expenditure, revenue and deficit financing. It is essential and appropriate to study budgetary policies as well as quantitative outcome of the budget.

4.5 Government Budgetary Operation

For a number of years budget in Nepal was classified under two categories: regular and development. However, this has been adjusted to international classification of current budget and capital budget from FY2004/05. The major heading under current budget is expenditure on consumption expenses, office operation and services, grants and subsidies, services and production expenses, contingency expenses, principle and interest payments on domestic and foreign loans, likewise, items falling under capital expenditure are capital transfer, capital formation, investment in share and lone and capital grants.

The NPC determines the size of capital/development expenditure conformity with the policies programs and priorities envisaged in the national plan and also by considering the extent of external borrowing both bilateral and multilateral grants and loans as well as domestic borrowing available to treasury during the given fiscal year. The capital development budget includes all the expanses of development project on going and new. Expenditure on capital projects, training research exploration and projects/programs activities supported by external assistance are also reflected in the development budget. The magnitude of current/regular expenditure is estimated on financial ceiling provided by MoF and NPC (financial management projects, 1995). There is limited scope to expand the size of current budget in a resources scare economy where tax elasticity and voluntary compliance on the part of tax payers are very low.

Tax revenue constitute of both direct and indirect taxes. The premier direct tax are on net income, property and capital gains and major indirect taxes include domestic taxes on goods and services like VAT, excise etc, tax on international; tread and transactionslike export and import duties. Non tax-revenues constitute fines and penalties and royalties.

A budget therefore, should be designed to facilitate determination of governmental activates in the light of the preference of society by ensuring the comparison of conflicting programs and methods in the attainment of the goals. The budget should also aid in attaining greater efficiency in the use of governmental resources.

4.6 Budgetary Reforms and Policies

Every democratic government makes vigorous efforts for maximizing the welfare of the community in the modern times. In order to achieve, the government takes in hand various socio- economic activities. This requires proper manipulation of the budgetary policy of the government. In Nepal, after restoration of democracy government initiated the economic strategy of maximizing public participation by promoting the role of the government from a controller to facilitators for the economic development of the country. Liberal and market oriented economic policy is followed against the inward looking and controlled economic policy for the attainment of sustainable higher growth rate in non-agricultural sector.

Budgetary policies of Nepal government during the nineties were directed towards economic liberalization, privatization, poverty reduction and decentralization. Policies and programs of the budget during Nineties were essentially concerned with agriculture, moderation, employment promotion, women empowerment, financial sector reform,government expenditure management, tax reform, good governance, social service and the development of the basic and physical infrastructure. The budgetary policy measures adopted by the first two budgets deserve appreciation at least interim of the direction towards liberalization throw they were still in adequate in interim of achieving the desire result (Adhikari, 2004/05).

Developed and developing economies needs to design economics policy that facilitate implementation of structural reform and should also be flexible enough to achieving sustainable and broader economic growth (economics survey 2004/05)

4.6.1 Structural Adjustment Program (SAP) and Enhanced Structural (ESAF)

The government adopted a stability program supported by the IMF Standby arrangement and a Structural Adjustment program in 1987 and in 1989 financed by the World Bank Structural Adjustment Credits and by an IMF Structural Adjustment Facility. The specific objectives of the adjustment program in Nepal were:

- Macroeconomic Stabilization,
- Increased resource mobilization,
- Enhanced investment efficiency,
- Improvement in financial management of public enterprises,

- Increased productivity and employment in the agriculture, forestry, trade and industry.

Nepal entered into another agreement with IMF under the Enhanced Structural Adjustment Facility in 1992 after second SAP expired in 1990. The objectives were:

- Raising GDP growth to about 5 percent per annum in the next three years,
- Reducing annual inflation to 5 percent and limiting current account deficit to 9.6 percent of GDP,
- Reducing fiscal deficit to 7.8 percent of the (before grant) with domestic borrowing limited to 0.2 percent of GDP by the end of the program period (1994-95).

4.6.2 Immediate Action Plan (IPA) and Medium Term Expenditure Framework (MTEF)

In June 2002, Nepal Government adopted the IAP that was designed to expedite reforms in immediate three critical areas-prioritizing public expenditures, improving service delivery and strengthening anti-corruption and accountability measures. Main IAP actions as regards public expenditure include:

- Setting a realistic budget ceiling and eliminating a number of low priority projects.
- Implementing public procurement and financial accountability reforms.
- Public posting of budget information and tracking of expenditures.

Based on the recommendation of the 2000 Public Expenditure Review and thework of the Public Expenditure Review Commission in 2001, and prompted by theworsening fiscal situation, Nepal Government decided to introduce MTEF starting inFY 2002/03. Overcoming the entrenched tendency to seek increased foreign aid tocope with fiscal stress, the reform minded NPC and MoF used the fiscal pressure to motivate serious adjustment in budget allocations.

4.6.3 12thThree Year Plan (2010/11 to 2012/13)

After coming to an end of Three Year Interim plan (2007/08 to2009/10) NPChas formulated and implemented the Three year plan (2010/11 to 2012/13). This plan,being prepared at prevailing a special moment in the country's history, is expected togive continuity to previous achievements, and to address issues specific to thetransitional period in a post-conflict situation. This Plan puts special emphasis onincreasing public expenditure to assist relief and generate employment as well as onpeace building, state restructuring, rehabilitation, reintegration, inclusion, andrevitalization of the economy and state of transition to ensure the completion writingof the constitution of the Federal Democratic Republic of Nepal. Following budgetaryreform policies have been envisaged in this plan:

4.6.3.1 13th Three Year Plan

4.6.4 Expenditure Policies

a) In the past, there was negative impact on national income growth and other economic indicators as the regular expenditure was more than targeted anddevelopment expenditure far less than targeted. The following policies will be adopted in order to improve public expenditure management.

b) Additional efforts will be made to increase efficiency in public expenditure tostrengthening fiscal system, and maintaining fiscal discipline in order to helpmaintain macroeconomic stability. Additional measures will be adopted toreduce the imbalance between current and capital expenditure.

c) Medium Term Expenditure Framework will be reviewed andinput/outcome/impact system will be adopted in a concrete manner for newmethods of scrotal prioritization and investment effectiveness.

d) Budget release and control system will be reviewed and improved.

e) Unproductive expenditure will be gradually reduced, and auditing enforced tomaintain fiscal discipline.

f) Feasibility study will be carried out to implement a zero-based budgetingsystem.

g) Gender accountable budget system will be institutionalized.

4.6.4.1 Tax Policies

a) The system of collecting and mobilizing taxes will be made transparent andsimple by reviewing existing tax system and acts

b) Revenue leakage will be controlled by strengthening revenue administrationcapacity.

c) Value Added Tax system will be made more effective

d) The tax base will be gradually broadened.

e) Customs rate and other tax systems will be adopted in line accordance with Nepal's commitment to international and regional organizations like World Trade Organization, and SAFTA.

f) Domestic revenue mobilization will be strengthened by broadening reintegration and inclusive development.

The projection of government budget for the three year's plan following.

Table:4.1

BudgetExpenditure for the Three Year Plan (2010/11-2012/13)

(Rs in millions)

FY	Current	Capital	Principal Repayment	Total
2010/11	177680 (56.80%)	114000 (36.44%)	21100 (6.74%)	312780 (100%)
2011/12	195450 57.42%)	121300 (35.63%)	23640 (6.94%)	340390 (100%)
2012/13	211080 (57.54%)	129040 (35.17%)	26710 7.28%)	366830 (100%)
Threeyear's total	584210 (57.27%)	364340 35.71%)	71450 (7%)	102000 (100%)

Source: Three Year Plan: Approach Paper (2010/11-2012/13)

Table: 4.2

Sources of Financing in the Three Year Plan (2010/11-2012/13)

(Rs in millions)

FY	Revenue	Grant	Foreign Loan	Domestic Loan	Total
2010/11	20598 (65.85%)	55030 (17.59%)	20470 (6.54%)	31301 (10%)	312790 (100%)
2011/12	228430 (67.10%)	58330 (17.13%)	23120 (6.79%)	30510 (8.96%)	340390 (100%)
2012/13	243580 (66.40%)	61830 (16.85%)	30520 (8.31%)	30900 (8.42%)	366830 (100%)
Three year's Total	674990 (66.46%)	175190 (17.17%)	74110 (7.26%)	92720 (9.09%)	1020010 (100%)

Sources: Three Year Plan: Approach Paper (2010/11-2012/13)

4.7Size and the Objectives of GoN Budgets After 1990

The size and the objective of the GoN budget have been changed remarkably after the political change of 1990. The magnitude of the budget presentedsizes the and by the Interim government formed after the establishment of the multipartydemocracy in 1990/91 was Rs. 19.8 billion. The main objective of the budget was toextend all possible supports from economic front towards the task of formulating newconstitution and establishing the popularly elected democratic government in thedeference to the wishes and expectations of the people's movement. This budgetidentified the vital significance of the role of the private sector and accordinglyadopted the privatization concept. Moreover the budget was so designed as to providethe ensuing government a solid foundation for eradicating the disparities anddistortions inherent in the economy and that its major thrust was to lessen thehardship of the people.

FY 1991/92, Nepali congress (NC) secured the absolute majority in the generalelection held after the restoration of multiparty democratic system. The NCgovernment presented the budget of Rs. 26.74 billion to the first session of theparliament. In true sense, this was the first budget in the direction towards theliberalization of the Nepalese economy. It gave a new vision to encourageparticipation of the private sector in productive areas. In this budget, it was realizedthat the government role in the industrial and other enterprises should gradually bedecreased with corresponding increased participation of the private sector. Thereafter,especially the objectives of the democratic budgets presented by the various governments were motivated by fulfilling the desires and the needs of the commonNepalese people. However, some new objectives like peace restoring, reconstructionsand rehabilitations etc. We are adjusted in the frequent presentations of the democraticbudgets especially after 1996 due to an ensuing ten-year civil war between Maoistextremists and the government forces until 2006. The size of the budget presented forFY 2006/7 was Rs. 143.91 billion as it was 13.75 higher than the budget presented inthe FY 1990/91. Sizes and the Objectives of GoN Budgets After 1990

However, the signature of the comprehensive Peace Agreement (CPA) in 2006between Maoist and the government officials brought a halt to the immediate violenceand the Interim Constitution of Nepal 2007 announced Nepal to be a Federal Democratic Republic. Following a Nationwide election in April 2008, the newly formed constituent Assembly declared Nepal as a Federal Democratic Republic whichabolished the monarchy at its first meeting the following month.

As Nepal made a historic 'U' tern-the end of the era of feudal monarchy in2008, the first Mega budget of the Republic Nepal presented by the Finance MinisterBhattrai (2008), under the Maoist led government amounted to Rs. 236.15 billion.This Mega budget was 39.7 percent higher than that the budget of the FY 2007/8. Inwas stated that "this Mega budget is needed to move ahead and take a giant leapforward". The major thrusts of this budget were the institutionalizing the FederalDemocratic Republic and the socio-economic transformation for building just,advance and New Nepal by the promulgation of the new constitution. Thereafter allthe Republican budgets have been guided by the promulgation of the newconstitution, bringing

Peace process into logical end, relief, reconstruction andrehabilitations and the rapid growth of the economy. The information regarding thesizes, objectives and the names of the Finance Ministers who delivered each financial year's budget to the legislature parliament during two decades after FY 2005/06 to 2014/15have been mentioned in the Appendix-1.

CHAPTER V

TREND AND PATTERN OF GOVERNMENT BUDGET

5.1 Introduction

Actually after the political change of 1951/52 in Nepal the responsibility of the government to launch the different programs has been increasing progressively. As an increase in the responsibility of the government there was simultaneous increase in the government expenditure and its revenue as well which can be clearly seen in its annual budget? However due to lack of resources, there was tremendous shortage offunds. Because of this financial constraint the government has no other option but tointroduce deficit financing which was first used in the first national budget of thecountry in 1951/52 to meet the growing requirements of funds for developing works.Since then the government has usually been continuing to introduce deficit financingquiet frequently in Nepal.Budget being the main instrument of economic policy incorporates policies,programs and activities related to government expenditure, revenue and other sourcesof financing. The main aspect of budget is expenditure, sources of revenue andfinancing of deficit. Tax and non-tax revenue plays vital role in collection of revenuefor meeting the requirement of government expenditure. Foreign grants are alsoincluding in the sources of finance. Any difference between government expenditureand government receipts is financed through external (foreign loan) and internalsources (banking, non-banking and cash surplus/deficit. As government activities andobligations are increasing, deficit financing is the common phenomenon of everybudget.

This chapter presents an analysis of the trends of budgetary components of theGoN budget like the government expenditure, revenue, deficit budget and debt ofgovernment during the period of FY 2005/06 to FY 2014/15.

5.2Components of the Nepalese Budget

The Structure of Budget includes various components incorporated withinbudget. Nepalese budget not only comprises of expenditures and revenue but alsoheavily depends on foreign grants and loans. The main components of NepaleseBudget can be divided in to the following main headings:

i. Government Expenditure

ii. Government Revenue

iii. Foreign Grants

iv. Loans (Internal and External)

As per international classification, Government Expenditure is classified asrecurrent expenditure, capital expenditure and principal repayment expenditure fromFY 2004/05. Public Revenue can be divided into tax revenue and non-tax revenue aswell.

5.2.1 Government Expenditure

Government expenditure refers to the expenses incurred by the government forthe maintenance of the government and to preserve the welfare of society as a whole.In other words, it refers to the expenses made by public authorities i.e. (StateGovernment, Central Government and Other Local Bodies) to satisfy the commonwells of the people. It is for protecting the citizens for promoting the common andsocial welfare. Government expenditure was classified into two headings: RegularExpenditure and Development Expenditure till FY 2003/04. From the year 2004/05 thesame has been classified as Recurrent Expenditure, Capital Expenditure and PrincipalRepayment Expenditure.

Nepal being a developing country, there is an urgent need of expendingdevelopment expenditure. However, there is also a growing financing expenditurerequirement in revenue collection. Situation of revenue receipts determines theamount necessary for foreign assistance and internal borrowing. The growth ofgovernment expenditure in Nepal has been phenomenal as evident from the fact thatevery finance minister ever since the beginning of the budgeting system in 1951 haspresented a publicexpenditure program larger than that of the previous year(Adhikari, 2004). As the data is available from the FY 2005/06 as per newclassification, trend of public expenditure will be analyzed for the period FY 2005/06 to2014/15. The main components are as follows.

1. Recurrent Expenditure

Recurrent expenditure is one of the major components of total expenditure which is the current expense. Recurrent expenditure is made of various components. It`s main components are expenditure on general administration, social services, defense, economic services, loan, and interest payment etc. Under the heading of miscellaneous other smaller components are included.

2. Capital Expenditure

Capital expenditure is the public investment and desirable also from the development perspective. This category is of particular importance for the developing countries like Nepal. Capital expenditure is also made of different components.

3. Principal Repayment

It is the share of internal loan payment and external loan payment. Its share is nominal while comparing with the whole budget as compare to capital and recurrent expenditure. But the repayment of principal in absolute amount is in gradual increasing trend in Nepal. Nepal being a developing country, there is an urgent need of expanding development expenditure. However, there is also growing compulsion to maintain law and order as well as debt servicing. Financing expenditure requires increment in revenue collection. Situation of revenue receipts determines the amount necessary for foreign assistance and internal borrowing. The growth of government expenditure in Nepal has been phenomenal as evident from the fact that every Finance Minister ever since the beginning of the budgeting system in 1951 has presented a public expenditure program larger as that of the previous year. (Adhikari, 2004)

5.3 Trend of GovernmentExpenditure

Total expenditure of Nepal government in FY 2014/15 was Rs.5359.0million. Of this, 64.5% was recurrent, and 18.9% Capital expenditure while 16.6%accounted for repayment of principal. Looking at the expenditure trend of the pastyears, the share of recurrent expenditure in total expenditure remained close to 60 to62 % between FY 2009/10 and 2014/2015 which such ratio has declined insubsequent years, which is considered as positive from public financial managementperspective. The share of capital expenditure in total expenditure was about 36.51%between FY 2010and11 and 2014and15 while it showed gradual improvementin the subsequent years reaching 18.9% in FY 2014/2015.

Table 5.1 reflects the amount of regular, development, capitalexpenditure, principle repayment and total expenditure during the review period. In FY 2005/06 the total expenditure was only Rs.110889.20 million that amounted up to Rs. 53598.0 million in FY 2014/15. This clearly depicts the steady and increasing trend of expenditure in Nepal.

Table 5.1also shows that the amount and percent share of recurrent and capital expenditure in total expenditure during the period of FY 2005/06 to 2014/15.

The percent share of recurrent expenditure in total expenditure has increase from 60.44in FY 2005/06 to 64.5 in2014/15. Its total amount and percentage share in total expenditure is in increasing trend during review period. When expenditure is analyzed, recurrent expenditure could not be controlled by government as compulsion of increment in employee among others together with the expansion of government machinery leads recurrent expenditure to increase every year. ,

Similarly total amount and percentage share of capital expenditure in totalexpenditure has been increasing from 26.7 in FY 2005/06 to 18.9 in 2014/15. Thetotal amount of capital expenditure has also been increasing, however, relatively lessthan that of recurrent expenditure because of the compulsion of expandinginfrastructural facilities, social services, economic services etc. The percentage shareof developing expenditure in total expenditure is in increasing trend during the reviewperiod except FY 2005/06, 2006/07 and FY 2007/08.

The FY 2006/07 in which the percentage share of recurrent expenditure in totalexpenditure is the greatest than that of capital expenditure in the study period whichshows the consumption nature of government.

In the same fashion, recurrent expenditure heavily increased during the review period.In absolute term it has risen from Rs. 67017.80 to Rs. 39895.0 million in FY 2014/15.The percentage share gives clear idea of the very trend of recurrent expenditure.However, small fluctuation is seen in the share of recurrent expenditure to totalexpenditure. The capital expenditure of government has increased slowly as comparedto recurrent expenditure. In absolute term, it has moved up from Rs. 2960.66millionto Rs. 11675.0 million from FY 2005/06 to 2014/15. The percentage shareof capital expenditure to total expenditure shows a continuous decreasing trend up to FY2007/08. Then it has also a fluctuating in nature. The annual percent change of totalexpenditure, capital expenditure and recurrent expenditure is also shown in table 5.1 all these expenditure heads have fluctuating trend. But in capital expenditure there isalso have negative annual percentage change in the FY 2005/06 and 2006/07.Such types of allocation of budget in development slow down the developmentactivities. Such scenarios of expenditure took place in the Nepalese budgetary historybecause of insurgency and political instability in the country. But such negativegrowth rate of capital expenditure has not been taken place since FY 2007/08.In the final fiscal year of review period the annual growth rate of budget indevelopment is19.5percent.

Table 5.1

Government Expenditure

(Rs in millions)

Fiscal Year	Recurrent Expenditure	Annual %of Change	Capital Expenditure	Annual % Change	Principle Repayment	Annual %of Change	Total Expenditure	Annual % of Change	% Share of Total Expenditure			
2005/06	67017.80	8.92	2960.66	8.3	1426.48	5.4	110889.20	12.35	R.E.	C.E.	P.R.	T.E.
2006/07	77122.40	10.17	3972.99	34.2	1675.23	17.4	133604.60	23.31	60.44	26.7	12.86	100
2007/08	91446.90	18.57	5351.61	34.7	1632.69	-2.2	161349.90	19.66	57.72	29.74	12.54	100
2008/09	12773.89	39.69	7308.90	36.6	1883.41	14.9	219662	37.83	56.68	33.17	10.15	100
2009/10	15101.91	18.22	9023.77	90.4	1843.23	-2.1	259689	21.35	58.15	33.27	8.57	100
2010/11	21016.8	11.70	4732.8	19.5	600.2	-6.6	295363.4	10.68	58.15	34.75	7.1	100
2011/12	24346.0	12.6	5139.1	15.5	662.7	-7.9	30147.8	15.21	57.66	36.51	5.83	100
2012/13	24745.5	15.8	5459.8	6.24	2094.0	6.74	32299.3	16.23	71.8	15.2	13	100
2013/14	30353	22.66	6669	140.63	2515	7.28	39537	21.98	69.0	15.2	15.8	100
201415	39895	31.44	11675	66.89	2028	7	53598	11.85	69.82	15.94	14.24	100
									64.5	18.9	16.6	100

RE refers to Recurrent Expenditure, CE refer to Capital Expenditure, PR refers to Principle Repayment, TE refers to Total Expenditure

Sourcs: Economic Survey,FY 2011/12 and 2014/15, MoF, Kathmandu,

Recurrent Expenditure

According to the budgetary classification of public expenditure, expenditure can be divided in two heads i.e. recurrent expenditure and capital expenditure. Hence recurrent expenditure has also various components. The main functional components are constitutional organs, general administration, revenue administration, economic administration and planning, judicial administration, foreign service, loan and investment, loan repayment and miscellaneous. The table shows that the composition of recurrent expenditure they are loan repayment and interest, social service sector, general administration ,defense, miscellaneous and economic service sector the larger share of recurrent expenditure is made the share of these sectors are given respectively. In Table 5.2 the expenditure on general public service reached to Rs.137770.7 million in FY 2014/15from Rs.7529.80 million in FY 2005/06. The expenditure on defense sector reached to Rs.25817.3 million in FY 2014/15 from Rs.25382.6 million in FY 2005/06.economic affairs was to Rs.60599.3 million in FY 2014/15 from Rs.6158.70 million in FY 2005/06.the expenditure on social services was Rs 15920.0 million in FY 2014/15. From Rs.9269.50in FY 2005/06.

The expenditure on interest payment was Rs.17410 million in FY 2010/011 from Rs.9706.00 in FY 2005/06then the recurrent expenditure heads change from FY2011/12 government the recurrent expenditure pattern new series. .The expenditure on miscellaneous was Rs.21009.8 million in FY 2010/011 from Rs.6006.80 million in FY 2005/06 .The expenditure on others million in FY 2010/11 from Rs.7127.0 in FY 2005/06 Similarly the expenditure on others was to Rs.5073.2million. The GoN adopted the new policy and new pattern of recurrent expenditure in different heads environmental protection FY2014/15 Rs 3825.5million in FY 2011/12 Rs. 465.1 million. The expenditure on housing and community amenities was Rs.3221.8 FY 2014/15Then the Rs.3234.1million FY 2011/12. The expenditure on recreation, culture and religion was Rs.3393.8 million FY 2014/15 in FY 2011/12 Rs.1864.2 million. The expenditure health was Rs.3393.8 million FY2014/15 in FY2011/12 Rs.19495.4 million. The expenditure on education was Rs. 85860.1 million FY2014/15in FY2011/12 Rs 61914.2 million. The expenditure public order and safety was Rs.29854.1 million in FY 2014/15 in FY 2011/12 Rs.36075.3 million. In this way from the given table 5.2 we can see that the recurrent expenditure on different heads has been increasing.

Table 5.2

Structure of Recurrent Expenditure in Different Heads

(Rs in millions)

Fiscal Year	General Public Services	Defense	Economic Affairs	Social Services	Interest Payment	Miscellaneous'	Others
2005/06	7529.80	25382.6	6158.70	9269.50	9706.00	6006.80	5073.2
2006/07	8384.80	29497.60	6164.00	11079.00	10128.90	7900.50	5712.1
2007/08	9200.7	35073.22	6373.68	10564.94	10564.94	11677.99	6423.8
2008/09	12052.6	47437.9	8154.2	13748.4	13748.4	24513.2	4972.1
2009/10	14927.3	62394.7	9981.3	16576.0	16576.0	21599.2	5966
2010/11	17789.2	70541.7	12737.1	17410	17410	21009.8	7127

New series

Fiscal Year	General Public Services	Defense	Public Order Safety	Economic Affairs	Environmental Protection	Housing and Community Amenities	Health	Recreation, Culture and Religion	Education	Social Services
2011/12	54550.4	20779.8	36075.3	34736.8	465.1	3234.1	19495.4	1864.2	61914.2	103344.7
2012/13	60523.6	18476.9	34832	35964.9	291.6	2306.5	18918.3	2255.9	62290.7	11595.0
2013/14	62685.5	25778.2	39854.1	50680.8	1521.4	6046.4	23362.0	3606.4	77699.3	12297.7
2014/15	137770.7	25817.3	29854.1	60599.3	3825.5	3221.8	3393.8	3393.8	85860.1	15920.0

Source: Economic Survey, FY 2011/12 and 2014/15, MoF, Kathmandu

Capital Expenditure

The capital expenditure has also various components. i.e. general administration, economic administration and planning, social services, economic services and miscellaneous now government Nepal adopted the new series of heading of the budget FY 2011/12.then adjusting the new series,general public services, defense, public order and safety, economic affairs environmental protection, housing and community amenities, health, recreation culture and religion and education others as the table 5.3 shows that expenditure on economic services was Rs.45615.3 million in FY 2010/11. It is declined to Rs.14797.1 in FY 2005/06 the rate of expenditure is not stable in different Fiscal Year. The expenditure on economic administration and planning reached Rs.169.2 in FY 2010/011 from Rs.20.3 million in FY 2005/06.The expenditure on Social service was Rs.45591.1 in FY 2010/011 from Rs 10151.8 million in FY 2005/06.The expenditure on General administration reached to Rs.1776.2 million in FY 2010/011 from Rs.1181.7 million in FY 2005/06.The expenditure on miscellaneous was Rs.3495.6 in FY 2010/011 and Rs.13.60million in FY 2005/06.now a day's FY 2011/12 government of Nepal change the heading of capital expenditure the heading is general public services expenditure was Rs 67107.5 million in FY2014/15 from Rs. 1254.4 million FY 2011/12. The expenditure of defenses Rs. 5541.3 million for FY2014/15 from Rs.1877.7 millionFY 2011/12. The expenditure of public order and safety for Rs.5016.3 million for FY2014/15 from Rs. 3190.4 million FY2011/12. The capital expenditure of economic affairs for Rs.109599.0 million for FY2014/15 then the Rs.33879.2 million FY2011/12. The capital expenditure of environmental protection Rs. 6965.8 million for FY 2014/15 then the Rs. 452.1 million FY2011/12. The capital expenditure of housing and community amenities Rs. 19120.6 million FY 2014/15 now Rs. 6784.5 million for FY 2011/12.the expenditure of health Rs.4676.4 million FY2014/15 then the Rs.3374.7 million for FY2011/12. The capital expenditure on recreation culture and religion Rs.587.8 million for FY2014/15 then the Rs.201.9 million for the FY2011/12.and the last series of government capital expenditure education Rs.173.9 million FY2014/15 again Rs.138.9 million FY 2011/12 this type of data shows the table 5.3.

Table 5.3

Structured of Capital Expenditure in Different Heads

(Rs in millions)

Fiscal Year	Economic Services	Economic Administration and Planning	Social Services Sectors	General Administration	Constitutional Organization	Miscellaneous
2005/06	14797.1	20.3	10151.8	1181.7	96.1	13.60
2006/07	17938.9	26.8	15529.3	4512	45.3	223.1
2007/08	20840	79.8	20283.6	1773.5	96	906.3
2008/09	31999.9	47.2	34056.8	1781.7	84.7	3002.9
2009/10	42968	86.8	36495.2	2006.6	71.6	3563.7
2010/11	45615.3	169.2	45591.1	1776.2	105.3	3495.6

New Series

Fiscal Year	General Public Services	Defense	Public Order and Safety	Economic Affairs	Environmental Protection	Housing and Community Amenities	Health	Recreation Culture and Religion	Education	Social Protection
2011/12	1254.4	1877.7	3190.4	33879.2	452.1	6784.5	3374.7	201.9	138.9	236.9
2012/13	2096.3	2422.3	2930.9	36291.0	329.4	7085.1	2953.4	156	139.1	195.0
2013/14	46845.8	6588.0	5114.2	59868.2	1050.8	8228.2	3156.4	305.9	126.4	236.5
2014/15	67107.5	5541.3	5016.3	109599.0	6965.8	19120.6	4676.4	587.8	173.9	360.2

Source: Economic Survey, FY 2011/12 and 2014/15, MoF, Kathmandu

5.4 Government Revenue

To meet the requirement for day to day administration and development, government collects resources through various sources. The principal among them are tax and non-tax revenue sources. But limited growth of economy with low level of income as well as the rate of saving in Nepal makes the exercise of collecting tax revenue insufficient for government expenditure. Besides high taxation often adversely affects the private enterprises and contributes to a decline in the investment capacity and thereby in employment of the economy.

For developing countries like Nepal, the problems of development are enormous and complex in nature. A government needs income for the performance of a variety of functions and meeting its expenditure. Dalton has defined the revenue in two senses; it includes all the income and receipts, irrespective of their sources and nature, which the government happens to obtain during any period of time. In the narrow sense, it includes only these sources of income of the government which are described as revenue sources.

So, it is widely recognized that government revenue is the major source of resource for financing the public expenditure of developing countries. Nepal has also realized this fact. Therefore, Nepal has been making constant effort to increase the revenue in her every budget. The public revenue in Nepal has been increasing continuously but only marginal increase has been evident.

5.4.1 Composition and Trend of Government Revenue

Table 5.4 below shows the total revenue (tax revenue plus non tax revenue) during the review period. According to table total revenue in absolute term has increased from Rs. 72282.1 million in FY 2005/06 to Rs. 424751.56 million in FY 2014/15. From the trend diagram, it can be seen that it is increasing all the way in the nominal term.

Similarly, table 5.4 shows the trend of tax revenue, which in absolute term has increased from Rs. 57430.4million in FY 2005/06 to Rs.355955.77 million in FY 2014/15. Non tax revenue, in absolute term has increased from Rs. 14851.5 million in FY 2005/06 to Rs.49910.74 million in FY 2014/15. It is, as a whole is fluctuating in nature. Table 5.4 shows that the absolute amounts of both sources are increasing annually.

In the initial study period the tax revenue was 87.72 percent of total revenue whereas non tax revenue was only 12.30 percent FY 2014/15 of the total revenue. The percentage distribution of tax and non-tax revenue in total revenue is both in fluctuating trend. Revenue mobilization through tax remained satisfactory in the last two year of the study period. To give continuation to this, challenges are to control the tax leakages especially in VAT and income tax, the two major contribution of the tax revenue. Areas such as expansion of tax base and change tax rates should be reviewed revised and implemented them in addition to developing programs related to tax education and tax awareness so as to increase revenue mobilization. Similarly, the services delivery by the tax administrator to tax payers needs to be improved. Revenue leakages through the rampant and illegal use of the duty free goods need to be controlled.

Table 5.4

Composition of Government Revenue

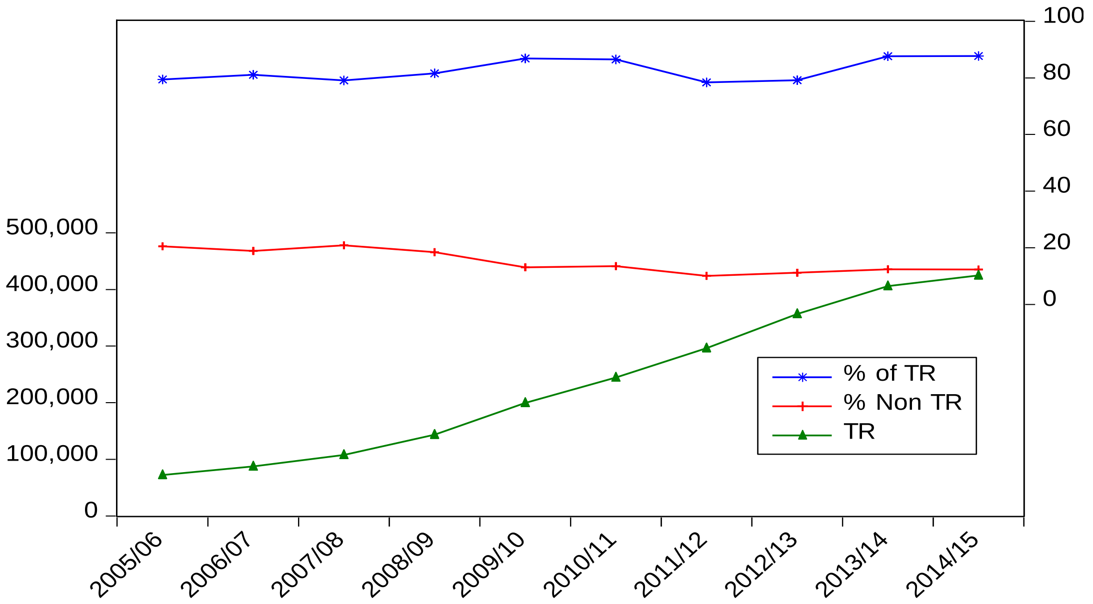
(Rs in Millions)

Fiscal Year	**Total Revenue**	**Tax Revenue**		**Non-tax Revenue**	
		Amount	**% of Tax Revenue**	**Amount**	**% ofNon Tax Revenue**
2005/06	72282.1	57430.4	79.45	14851.5	20.55
2006/07	87712.1	71126.7	81.09	16585.4	18.91
2007/08	107622.5	85155.5	79.12	22467	20.88
2008/09	143474.5	117051.9	81.58	26422.6	18.42
2009/10	199819	156294.9	86.86	23650.9	13.14
2010/11	244561.1	172777.6	86.47	27041.7	13.53
2011/12	296189.0	211722.6	78.41	32651.5	10.09
2012/13	356620.78	259573.0	79.16	36156.5	11.24
2013/14	405865.74	312441.26	87.61	44179.52	12.39
2014/15	424751.56	355955.77	87.72	49910.74	12.30

Source: Economic Survey, FY 2011/12 and 2014/15, MoF, Kathmandu

Figure5.1

Composition of Government RevenueFY (2005/06-2014/15)



Source: Researcher's Calculation through Excel

5.4.2 FiscalDeficit and Budget Deficit

Fiscal deficit is defined as the difference between total expenditure and total revenue including capital receipts and excluding borrowing and other liabilities. The total revenue is subtracted from total expenditure and the gap between the two is known as fiscal deficit. In formula form, Fiscal deficit = total expenditure-total revenue the total revenue and foreign grants is subtracted from total expenditure of government and the gap between is known as budget deficit. Budget deficit is financed through the mechanism of internal and external borrowing, which is called deficit financing. In formula form,

Budgetary Deficit=Total Expenditure-Total Receipts (Total revenue + grants)

So, the fiscal deficit is greater than budget deficit. Fiscal deficit is covered by grant portion to some extent.

In table 6.5 the absolute amount of fiscal deficit and budget deficit are both increasing from initial to the final year of the study period. But the implement is in fluctuating nature. The absolute amount of fiscal deficit reached to Rs. 19520.0 million in FY 2014/15 from Rs. 39861.10 million FY 2005/06. Similarly budget deficit reached to Rs. 3315.2 million in FY 2014/15 from Rs. 24779.6 million in FY 2005/06. The controlled increase in government expenditure accompanied by constantly low level of revenue realization has been mainly responsible for acceleration in government fiscal and budgetary deficit.

Grants received by the government from friendly countries, in absolute term have increased from Rs.13827.10 million in FY 2005/06 to Rs.73388.0 million in FY 2014/15. Foreign grants have been increasing continuously but it does not have steady growth rate. The government receipt is not increasing in proportion to the increase in public expenditure, although, both government expenditure and receipt are increasing continuously. So we always get an existing gap between the receipt and expenditure.

The trend of total revenue, total expenditure foreign grants fiscal deficit and budget deficit following the graph in government budgetary operation demonstrates that the fiscal and budget deficit have been widening almost every year during the review period. Causes of deficit are quite clear from the above trend analysis of government revenue and expenditure. The trend shows that the level of government expenditure has been higher than the level of revenue including foreign grants. The gap between revenue sources and total expenditure was widened significantly during the review period. It amply demonstrates the fact that the government has not been able to raise resources to meet the growing expenditure. This means government has been living beyond its means.

Table 5.5

Fiscal Deficit and Budget Deficit

(Rs in millions)

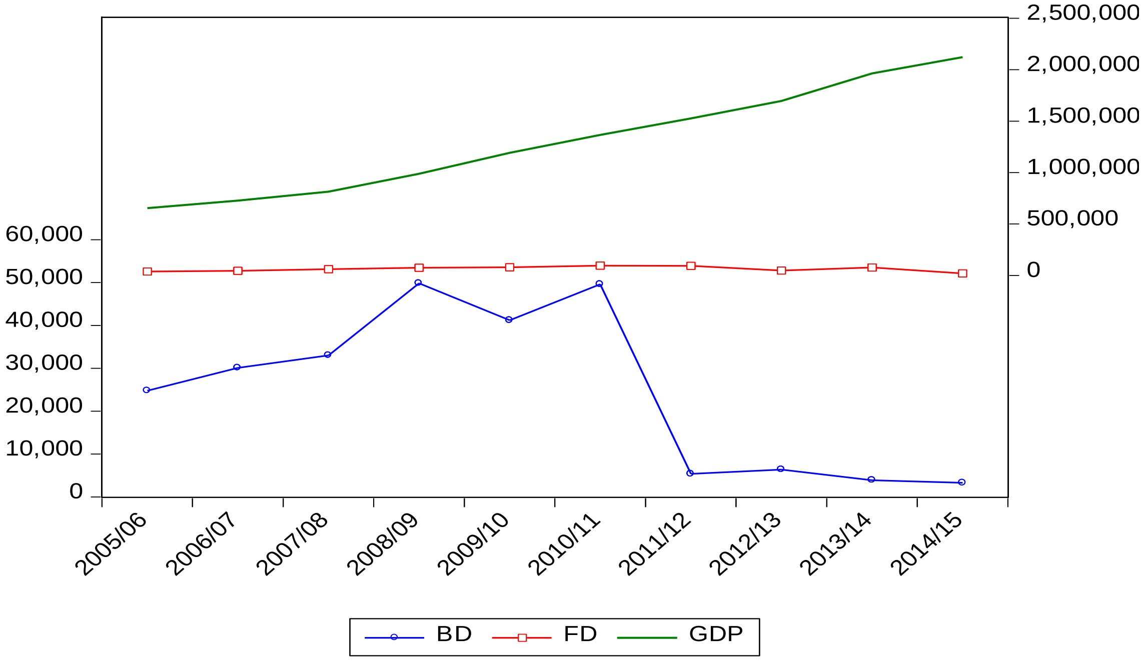
Fiscal Year	Total Expenditure	Total Revenue	Fiscal Deficit	Foreign Grants	Budget Deficit
2005/06	110889.2	72282.1	39861.10	13827.10	24779.6
2006/07	131851.0	86135.5	45037.7	15946.0	30091.7
2007/08	168995.6	103667.3	60875.8	27469.1	33031.2
2008/09	219662	143474.5	76187.5	26382.8	49804.7
2009/10	259689.1	179945.8	79743.3	38545.9	41197.4
2010/11	295363.4	199819	95544.4	459922.2	49622.2
2011/12	33916.75	24437.41	94793.4	40812.2	53.79.61
2012/13	33863.8	28960.49	49033.1	35229.9	6383.55
2013/14	43505	35662	78430.0	33969.0	3895.66
2014/15	61810.0	42290	19520.0	73388.0	3315.2

Source: Economic Survey, FY 2011/12 and 2014/15, MoF, Kathmandu

The trend of total revenue, total expenditure foreign grants fiscal deficit and budget deficit following the graph in government budgetary operation demonstrates that the fiscal and budget deficit have been widening almost every year during the review period. Causes of deficit are quite clear from the above trend analysis of government revenue and expenditure. The trend shows that the level of government expenditure has been higher than the level of revenue including foreign grants. The gap between revenue sources and total expenditure was widened significantly during the review period. It amply demonstrates the fact that the government has not been able to raise resources to meet the growing expenditure. This means government has been living beyond its means.

Figure 5.2

Trend of Fiscal Deficit and Budget Deficit FY (2005/06-2014/15)



Source: Researcher's Calculation through Excel

5.4.3 Sources of Budget Deficit

Most of the countries in the world practice the budget deficit. Theoretically the volumes of expenditure surpass the revenue in such situation. As such gap between the expenditure and revenue need to be managed with various instruments. In other words, the budgetary deficit ought to be financed. In the Nepalese context, as elsewhere, budgetary and fiscal deficit is financed with the medium of internal and external sources. External sources include foreign assistance, particularly loans and grants where internal sources includes internal loan along with borrowing and cash surplus. In forgoing analysis revealed that there persists the budgetary deficit in budgetary system of Nepal. The gap between the revenue and expenditure need to adjust in order to balance the financial position. To meet overall deficits, particularly fiscal deficit, an external source sources of financing i.e. loan and grants are found is heavily used. Therefore, it can be noted that external sources of financing have crucial role in the Nepalese economy.

Table 5.5explains the figure of financing budget deficit where foreign loan and internal borrowing are major sources of it. The major portion of financing deficit seems to be internal sources. In the FY 2005/06 the external source of financing budget deficit was 33.15 percent of the total budget deficit but the percentage share of external loan in budget is only 32.22 percent in the final year of the study period.

The average share of foreign loan in budget deficit is 33.94 percent in the study period. The table 5.6 further shows that the contribution of internal borrowing plus cash balance was 79.66 percent, highest in the FY 2011/12 of the study period and lowest 48.66 percent of the budget deficit in FY 2007/08. The average share of internal source of financing in total budgetary deficit is 66.60 percent.

Table 5.6

Budget Deficit and Sources of Financing

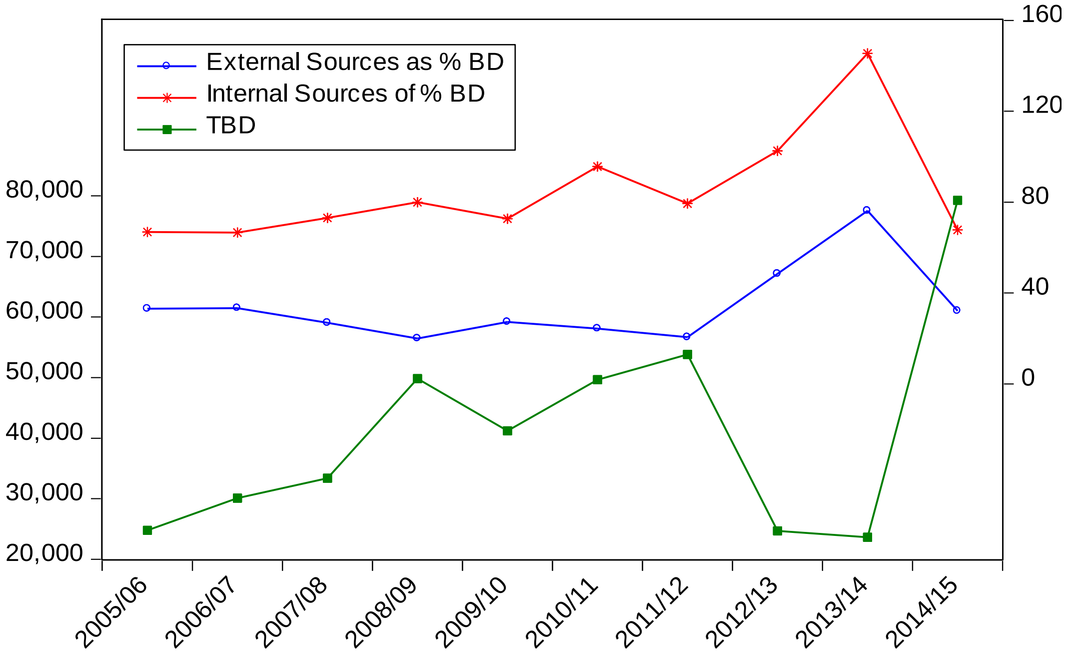
(Rs in millions)

Fiscal Year	Total budget Deficit	External Sources(Foreign Lone)		Internal Sources (Borrowing+ Cash Balance)	
		Amount	%Budget Deficit	Amount	% Budget Deficit
2005/06	24779.6	8214.3	33.15	16565.3	66.85
2006/07	30091.7	10053.5	33.40	20038.2	66.60
2007/08	33406.7	8979.9	26.88	24426.8	73.12
2008/09	49804.7	9968.9	20.01	39835.7	79.99
2009/10	41197.4	11223.4	27.24	29973.9	72.76
2010/11	49622.2	12075.6	24.33	47484.9	95.67
2011/12	53796.1	11083.1	20.60	42713.1	79.40
2012/13	24710.5	11969.1	48.43	25344.3	102.56
2013/14	23618.8	17998.8	76.20	34344.9	145.4
2014/15	79235.8	25531.3	32.22	53704.6	67.77

Source: Economic Survey, FY 2011/12 and 2014/15, MoF, Kathmandu

Figure 5.3

Budget Deficit and Sources of FinancingFY (2005/06-2014/15)



Source: Researcher's Calculation through Excel

5.5 Impact of Budget Deficit in GDP Growth Rate

In developing countries, like Nepal private sectors is not well developed. So the public expenditure increases with its government increasing activities. When market works perfectly, price mechanism will solve the basic economic problem of what, how and to whom to produce. Government intervention however does not necessarily provide a guarantee that society willsbenefited from such action. Government intervention however does not necessarily provide a guarantee that society will benefit from such action. Government total expenditure is increasing every year and total revenue also increase, but increasing rate of total expenditure is greater than increasing in total revenue. This increase the gap between total expenditure and total revenue. To fulfill the gap between total expenditure and total revenue, budget deficit also increase.

The impact of budget deficit on GDP can be analyzed by establishing some model (linear regression model, log linear model). Through each model carries its own merits and demerits, emphasis is given to the simple linear regression model. To do so the regression is carried out with 11 year of data from FY 2005/06 to FY 2014/15.

The fitted equation of the regression model is as following that the estimates are based on constant data series of the variables. However, no attempt has been made to correct the problem of series correlation. In all statistical analysis, figures in present these below the coefficients for independent from computer via SPSS programmers. All of variable name, label and formation of regression can be seen by appendixes. The regression equation is given on each heading.

5.6 Regression Analysis

1. Contribution of Budget Deficit on GDP

The ordinary least square (OLS) estimation of the relevant equation given the following result:

BD = 56157.9 + 0.02406 GDP

$R^{2 =}$ 0.434, Adj.R^2= 0.363, t = -2.467, D.W 1.299

In the above equationBD depends GDP linearly. There is positive relationship exists between BDandGDP.In the equation explained above shows that one million increments in GDP, BD increase by 0.0246 million on an average per-annum. The value of R^2reveals the fact that about 43.4 percent change in GDP is extend by the change in budget deficit, which shows the goodness of fit of the regression line. Here, calculated value of t (7.868) is grater then tabulated value of t(-2.477) at 5% level of significant; it means there is positive relationship between budget deficit and GDP. The DW value is 1.299 suggested that there is uncertainty of autocorrelation at 5 percent level of significance.

2. Contribution of Total Expenditure on GDP:

The OLS estimation of the relevant equation gives the following results:

TE = -53941.8 + 0.259GDP

R^2= 0.9830, Adj R^2 = 0.9809, t = -3.217, DW = 1.5131

In the equation TE depends on GDP linearly. There is positive relationship between TE and GDP. In the equation explained above shows that one million increment in GDP, BD increases by 0.259 million on an average per-annum.It shows the values of $R^2$0.9830 and Adj $R^2$0.9809 are very high, it represents the high goodness of fit of regression line. That is the value of R^2 is high enough to justify that 98 percent change in GDP is explained by the change in the change in the total expenditure. Here, calculated value of t (3.217) is greater than tabulated value of t (21.56)at 5% level of significance. So, t value is significant, it means there is negatives relationship between total expenditure and GDP. The DW value of 1.5131 suggests there is negative auto correlation at 5 percent level of significance.

3. Contribution of total Revenue on GDP

An attempt is made to analyze the impact on GDP by total revenue. The OLS estimation of the relevant equation given following results:

$$TR = -83372.0 + 0.2253\ GDP$$

$$R^2 = 0.9866,\ Adj.R2 = 0.9850,\ t = -6.45,\ D.W = 0.6353$$

In this equation shows that there is positive relationship between GDP and TR.TR depends on GDP linearly. As explained above, it is concluded that one million increment in GDP, TR increases by 0.2253million on an average per-annum. As the value of $R^2$0.9866. Adj.$R^2$0.9850is very high. It represents the overall goodness of fit of the model. That is the value is R^2high justify that 98.5percent. So it is significant, it means there is positive relationship between total revenue and GDP. The DW value 0.635 suggests that there is positive auto correlation at 5 percent level of significance.

4. Contribution of Fiscal Deficit on GDP

The ordinary least square (OLS) estimation of the relevant equation given the following

$$FD = 64568 + 0.000510\ GD$$

$$R^2 = 0.000110,\ Adj.R^2 = -0.1248,\ t = 2.694,\ DW = 1.263$$

Above equation shows that there is positive relationship between GDP and FD.FD depends on GDP. In the equations explained above shows that one million increment in GDP, FD increase by 0.000510 million on an average per-annum. The value of $R^2$0.000110 and Adj.R^2-0.1248 are very high. It represents the overall goodness of fit of model. That is the value of R^2 is highly enough to justify that0.000510 percent change in GDP is explained by the change in fiscal deficits have positive auto correlation at 5 percent level of significance. Here calculated value of t (2.694) is grater then tabulated value of t (0.029) at 5 percent levels of significance. So, t value is significant, it means there is positive relationship between fiscal deficits and GDP.

5.7 Problems of Nepalese Budget

Deficient infrastructure in basic infrastructure, and with political confusion, Nepal has given priority to building the physical so as to spread the gains and linkages of the development strategy within the country, to integrate domestic markets and above all, to speed up rural development. The need for basic infrastructure is also justified for diversifying the economy and its export base which tends to be narrow and consists of a few primary and manufactured productsonly.

With the advent of the democratic political system in 1951A.D the budgetary system as applied by the first elected government in 1958/59 spread the gains and linkages of the development strategy within the country, to integrate domestic markets and above all, to speed up rural development. The need for basic infrastructure is also justified for diversifying the economy and its export base which tends to be narrow and consists of a few primary and manufactured products only.

Given such circumstances is the first scientific budget. The regular expenditure and development expenditure consist of General Administration and Constitutional Bodies, Economic Administration and Planning, Social Services, Economic Services, Communication, Transport, Electricity, Other Economic Services and Miscellaneous.

The average annual growth rate of development budget is less compared to the regular budget during the past three decades. The increasing trend of regular expenditures on unproductive sectors and the decreasing trend of development expenditures indicate the minimization the average annual growth rate of development budget is less compared to the regular budget during the past three decades. The increasing trend of regular expenditures on unproductive sectors and the decreasing trend of development expenditures indicate the contemplation over the status and effectiveness of budgetary system of the government increased specially after the political change of 1990. Increasing challenges encountered in relation to the rising expectations of people have prompted the government to become serious as to the means and the use of the minimization of the pace of development. Budget, however, became more significant in managing government finance the scarce resources in a more organized and effective manner.

Estimation Over

The resources estimation in Nepal is mostly based on accounting trend and intelligent judgment. Sometimes it leads as much as 25 percent differences between the estimated and the realized revenue. With weak estimation, whole expenditure planning becomes a failure.

Political Intervention

Budget in Nepal is driven by more political objectives rather than social and economic objective of the government. The Nepal Public Expenditure Report (PER) 2000 points out that the development budget is heavily over programmed. Because of the political pressures, the size of the budget is set at levels, which are not consistent with the actual availability of resources and institutional capacity. The consequence is that the limited resources are spread to thinly among too many projects.

Lack of Participatory Approach

Local ownerships of the projects may improve the effectiveness of public spending. Budget formulation is not participatory in real sense, which explains why there is lack of ownership of projects and program by local communities, it results into poor performance.

Not Performances Based or Zero Based Budgeting

Zero based or performance based budgeting system is effective to cut down expenditure. It is not practiced in Nepal, although it is recommended from various quarters that the government should introduced it past performance is not revived while formulating budget and it follows incremental approach.

No Earmarking of the Funds

There is no practice of earmarking the certain revenue for the certain purpose only. Earmarking of funds can help better achieving the budgetary goals.

Donor's Pressure

Some projects are kept under first priority just because they are donor financed. Like ADB, The World Bank, IMF and other development partner NGOs, INGOs. Foreign Aid policy is to be brought out as per our national interest and priorities. **A** national action plan on Aid effectiveness should be implemented to improve the effectiveness of the foreign assistance. Strong monitoring system should be developed to enhance the aid effectiveness and utilization capacity

Budgetary Uncertainty

Since for a long time, Nepal has been suffering from political instability. Political initiatives like Bandh, Strike, Highway Obstruction, and road block and Gherao that obstruct the economic stability, there is lack of political consensus on national economic agenda which has been main caused to make irregularity in the presentation of the budget. Due to the absence of timely revision on revenue policy and rates as per the necessity of the economy, revenue growth is continuously decelerating. The revenue growth rate declined also due to the slackness in economic activities caused by budgetary uncertainty.

5.8 Prospects of Nepalese Budget

Developing Countries have adopted government budgetary system as a tool to accelerate the pace of economic development and annual budget is considered sine-quo-none of the modern government. The budgetary process is widely accepted as an efficient strategy to accomplish the development goals of the nation. The concept of effect of annual budget implies the supply side of the development process.

At the course of trend analysis, the various variables have been brought to examine the macro pattern. Among these variables agricultural GDP, manufactured GDP, total GDP, GNP, PCI are taken as the macro development indicators along with capital formation. The trend of DE, RE, TE and its GDP ratio have been found satisfactory. The planning mechanism in the country has been substantially non-effective and therefore it is necessary to fix the targets on the basis of empirical programs rather than on the basis of ad-hoc decisions. In fulfilling the objectives and targets, since institutional factors play critical role policies have to be simultaneously evolved in reforming institutions in order to implement programs effectively. It is necessary to envisage the projects and programs in conformity with the production targets in a more operational and more realistic way. In view of the major chunk of internal resources primarily utilized in financing consumption type of expenditures, it is equally necessary to standardize the project planning. Though foreign aid is an exogenous and externally determining factor, a part of it goes towards non-productive consumption activities; its utilization pattern has to be drastically corrected. The overriding trend on regular expenditure reflects alarming situation with regard to fiscal discipline and the overall development program of the country. The government should establish an appropriate environment to open the various sectors for private investment. A nominal role of internal borrowing and internal revenue in the economy and the excessive dependence on foreign aid has led the country for heavy debt service obligations every years forcing for additional tax burden. Therefore, other domestic sources mobilization prospects and opportunities should be sought with full venture by the government. The development activities are highly influenced by the open border of neighboring countries. Therefore, it is necessary to introduce some control measures on the borders between two countries in the larger economic interests of the county and people.

CHAPTER VI

SUMMARYOF FINDINGS, CONCLUSION AND RECOMMENDATIONS

6.1 Summary

Budget is guideline of annual programmed and policy of a government. Moreover, it isthe main instrument of economic policy, incorporates policies, programs and activities relatedto government expenditure, revenue and financing of deficit. Tax and non-tax revenue plays avital role in collection of revenue for meeting the requirement of government expenditure.Foreign grants are also included in the sourced financing. Any difference betweengovernment expenditure and government receipts is financed through external (foreign loan)and internal sources (banking, non-banking and cash surplus/deficit). As governmentactivities and obligations are increasing, deficit financing is the common phenomenon ofevery Fiscal Year's Budget.

After reestablishing democracy in 1990/91 and even after announcing Nepal as aFederal Democratic Republic in FY 2005/06, Governments of Nepal has attempted to increase theamount of expenditure and revenue which is clearly seen in its annual budget. The presentstudy entitled on "An Analysis of the trends of Budgetary Components of the GovernmentBudget in Nepal after Restoration of Democracy" covers actual figures of the period of 10years (2005/06-2014/15). This study has tried to show the trend of government expenditure,revenue, and foreign aid, deficit financing and public debt in Nepal as well. The budgetary policy measure taken by the coalition government during the period of transition adopted the policy towardsliberalization along with providing peace and security to the people of the nation. But these policies are quite inadequate in terms of desired results due to instability caused by Maoists insurgency.

In Nepal, it has been found that the government expenditure is increasing fast compared to revenue. Among the expenditure, regularexpenditure probably has been increasing readily due to growing burden of debt service payments, maintaining law and order and providing salary to civil servants. Growing regular expenditure has become major concern to policy makers because it has been reducing the revenue surplus necessary to finance development expenditure. There is, on the other hand, decreasing the developing expenditure. It is because of numerous in project implementation resulted from frequent change in government. During the recent years, because of political instability, the development expenditure stood even below the regular expenditure. Obviously, such decaling situation of development expenditure would erode the productive capacities of economy through lack of basic socio economic infrastructure.

Following are the major findings of the study. These findings are based on the analysis of the budget data for the FY 2005/06 to FY 2014/15. Budget data for the expenditure and its components are analyzed for the period FY 2005/06 to FY 2014/15 as the data for the previous years are not available as per the new classification brought out from FY 2010/11. Looking at the expenditure trend of review periods, Government expenditure has accelerated from Rs. 110889.20 million in FY 2005/06 to Rs. 295363.40 million with an average annual growth rate of 12.35 percent. The growth rate of recurrent expenditure in total expenditure has been 8.92percent; capital expenditure in total expenditure has been 8.3 percent.

Summary of Findings are as follows:

1. Unrealistic Budgeting Process

Nepal's budgeting process has been highly unrealistic in recent years. In almost all the years inthe review period, the budget targets have been set at unduly high levels, particularly fordevelopment revenue and foreign aid. This cover estimation of resources in turn has led thegovernment to set similar unrealistic targets for the development budget and to accommodate toomany new projects. However, the actual budget outcome had fallen significantly short of theseoptimistic expectations every year. And, since there is little scope for cutting back regularexpenditures, the brunt of fiscal adjustment has been made through cutbacks in developmentspending.

2. Development budget is heavily over-programmed

The budget, particularly its development component is heavily over-programmed. Because ofpolitical pressures to accommodate new projects, there are unmanageable projects fordevelopment budget. There is a concrete lack of cost-benefit analysis and prioritization of development projects.

3. Decliningbut Still High Deficit

Despite a series of fiscal reform, both in revenue and expenditure fronts, the budget deficits stillremained above the six percent of GDP. This may be partly due to ascendant impact ofdevelopment expenditure which was dominated by a few but popular and even costlyentitlements like social services, rural infrastructure, and power generation, generally tied withdemographic and economic factors. In order to finance these entitlements revenue policy hasbeen skewed, making it more difficult to meet resource gap through increased taxes.

4. Increasing Burden of Debt Servicing Charges

There has been a increasing trend towards loans rather than grants in the composition of theforeign aid in Nepal. This has imposed the growing burden of debt servicing charges and interestpayment. Debt servicing burden in Nepal, though not acute and alarming as yet is increasing fast.Unless the government takes certain measures to alleviate the situation, it will not only bringinstability in the economy but will also slow down the pace of development and will thusproduce consequences economically.

5. Lack of Co-ordination between Regular and Development Budget Formulation

The budget document presented to the parliament appears to be a unified one. But in reality theregular budget and the development budget are normally prepared different procedures. TheMoF prepares regular budget on the basis of past experience and historical accounting whereasNPC prepares the development budget targeting to fulfill the development need of the nation. Insuch cases, difficulties are frequently encountered in meeting macro objectives where the twobudgets are prepared without full co-ordination, or on different economic assumptions.

6. Over Reliance on Foreign Aid and lack of Proper Foreign aid Policy

There is no concrete foreign aid policy. However, the government has made draft for this in2002.Lack of proper foreign aid policy has resulted in haphazard flow and uses of foreign aid.Such a situation has been creating aid dependency syndromes in the Nepalese economy. Overreliance on foreign aid has been creating the situation of lose in self-dignity.

7. Lack of Monitoring Mechanism

There is a lack of monitoring mechanism during the budget execution. That's why there is awidespread leakage of resources and tardy pace of project implementation. There is also lack ofco-ordination between government organizations.

8. Lack of Multi Year Planning

There is severe lack of multiyear planning in Nepal. As such, there is a lack of coordinationbetween necessary budget required and budget allocation for the many development projects.Because of lacking such a planning, many development programs are in under-finishedconditions and their implementation condition is gloomy.

9. Lack of Commitment

There is also a lack of commitment from the government as well as civil staff. There is no anyeffective reward and punishment System. Therefore, there is an excessive leakage of thegovernment resources and weak performance. No one takes the responsibility of the projectfailure. In this way, there is lack of public responsibility and accountability. In other words, thereis an absence of good governance that is resulting in the weak fiscal management of thegovernment.

10. Inconsistencies between Tax Policies and Programmers

To fill the resources gap from domestic front, government has introduced various tax policies with multiple objectives. In substance, the revenue related objectives of government stated in annual budget speech are hardily achieved to increase the share of direct tax for reducing economic inequality in the society, to reform the tax administration in order to increase the domestic resources mobilization, to reduce the tax rate which contributes for liberalization and provides relief to the people at large, to provide long term direction to revenue policy by making tax composition appropriate to consolidate tax revenue with economic activities and to make it elastic.

6.2 Conclusion

During the decades after the restoration of multiparty system in 1990, the democratic government, despite their serious attempts, saw unable to mobilize adequate domestic resources as evident from the less than expected revenue/GDP ratio, higher fiscal deficit/GDP ratio, narrowing revenue surplus, and large outstanding government debt/GDP ratio. Recently, a major feature of the budgetary development has been the growing dependence on foreign loans for deficit financing. Around 66 percent of the development expenditure has been purposed to be financed through the foreign sources. This is not a happy situation for Nepal.

GoN, during the Nineties and even after the Nineties, followed the vigorous policy of liberalization, privatization and globalization, giving primary focus on private sector activities. Although there was a series of changes of the governments on a frequent basis, there has been no major diversion during the period over study at least in the major policy framework of the government. However, despite GoN adopting the policy to boost the private sector, in actual sense, private sector has not been able to come up as expected since frequent changes of government created since frequent changes of governments created policy confusion and uncertainties in the economy such political instability resulted in the lack of commitment to pursue, in a smooth and coordinated scheme development activities due to excessive political interference for party politicizing. As a result, most of the development projects were halted without completion. Although the number of projects increased on a account of the political pressure, there was a sever in effectiveness in the implementation of these project.

GoNfailed to contain the growth of recurrent expenditure because of the increasing liability of the maintain law and order, debt service payments, salary increment and other overhead expenditures. As a result recurrent expenditure began to outstrip development expenditure during the period over study.

On the revenue side, mainly the customs duty, sales taxes have been reformed. But the reform in the customs duty has not been able in rectifying the anomalies contained in the foreign trade regime. These reforms could neither boost the import revenue from the third countries nor enhance the domestic revenue collection in a r4emarkeble manner. Though reform in income taxation in line with what is prevailing around the world today is by for a welcome step, no serious steps have been taken to compensate the revenue loss caused by the tax reforms.

To sum, despite the sincerity of purpose and the urgency to address the rising popular demands, the popularly elected governments could not transform their budget policies priorities and programs into realistic outcomes mainly because of the inadequate political vision and limited capacity of GoN in transforming the plans and programs into outcomes. Therefore, the urgency for the future governments is to enhance the institutional and bureaucratic capacity to implement the promise and plans in an effective and efficient way inauditing to chalking out a sound development strategy most beneficial to the economy of the Nepal and the Nepalese people.

6.3 Recommendations

This study reveals that the budgetary trend of the GoN over the decades presents a gloomy fiscal scenario-low capital expenditure, high recurrentexpenditure, low revenue collection and high fiscal deficit with high foreign loan inflows.The output of the economy has thus achieved average very low economic growth rate overthe decades. Thus, this study presents some crucial recommendations for the furtherimprovement in the preparation and implementation of budget in Nepal.

1. Government of Nepal needs adequate mobilization of domestic resources. As thegovernment has not sufficient fund to meet its growing expenditure on recurrent anddevelopment program, therefore revenue has to be increased. This can be done byimproving effective tax policy and tax administration. This also includessimplification of tax rates, rationalization of tax structures and expansion of tax net.

2. Revenue policies should be formulated with the objective of industrializing the agrobased national economy through adopting a scientific tax system, transforming taxadministration into electronic system to make it effective and attracting domestic andforeign investment through the relation of an investment friendly environment as wellas trade facilitation.

3. A high level permanent central revenue board should be established with theobjectives of determining revenue policy conducting revenue administration based onshort, medium and long term regular study and research on revenue policy, revenueadministration and revenue related rules and regulations.

4. The tendency of revenue leakage in Excise, value Added Tax, Income Tax, andCustom Duty will be controlled by making information mechanism more effective.

5. In order to control revenue leakages a separate revenue police force has to beestablished and mobilized as emergency flying squad and revenue leakages should bestrictly controlled.
6. Development of self-reliant economy by carrying out speedy development activities isthe need of the day. For this purpose a stronger efforts for rapid mobilization ofinternal revenue is extremely important. This will induce the government to rejectdonor driven aid if it does not fit its priorities and program objectives. Moreover,introduction of performance budgeting or zero based budgeting to selective projectsunder key ministries would be an effective move towards this direction.
7. Allocating aspect of expenditure must be taken into consideration on the basis ofnational priorities so that productivity and production may increase within stipulatedtime period.
8. Bringing peace in the economy could save expenditure on defiance. Resource can be diverted to more economical and productive infrastructure development thus, theremust be cut in defiance as well as unnecessary recurrent expenditure activities as well.
9. The size of overall budgetary deficits including grants has remained high mainly dueto low revenue and high expenditure. This has led to heavy borrowing from internaland external sources. So for reducing the volume of borrowing, revenue collection isto be increased substantially in order to attain self-sufficiently in the long run.
10. Nepal is currently facing a serious problem of resource gap and this urgently needs tobe narrowed. Budgetary deficit need to be reduced by mobilizing additional resources.The government should take a number of measures such as strengthening the taxadministration, increase tax base to promote revenue generation and control ofcorruption.
11. Large proportion of internal borrowing comes from banking sector particularly fromthe central bank which is expansionary therefore this internal borrowing is to be keptwithin limitation.
12. The focus should be drawn upon borrowing from non-banking sources and bankingsources other than central bank that has leased or no inflationary

impact. However, it isnot to be forgotten the effect of crud out' while talking internal borrowing.

13. The gradual increase in external debt has been to great extent responsible forincreasing volume of imports of conspicuous consumer goods. This tendency must bediscouraged by adopting suitable import policy. In other words, import policy shouldemphasize imports of capital goods, for productive purpose.

14. Proper coordination between National planning commission and Ministry of financeshould be maintained and budget should be prepared depending upon the commitmentof the campaign of building prosperous, modern and just Nepal in true sense, learningthe lessons from the past that it would be difficult to maintain sustainable peace,economic growth and stability if the peoples aspirations are not appropriatelyaddressed. The purposed budget should be basically focused on the background ofthese major priorities.

15. While formulating budget, state should be identified the obstacles for higher andinclusive growth and judicious distribution of income and concentrated the policiesand programs towards minimizing them.

16. MTEF need to be implemented with earnestness and on more comprehensive basisRewards and punishment system should be made effective so that publicaccountability and responsibility will increase, which then will help in the effectiveimplementation of the Government policies and development programs throughamong peoples, the reduction in the rampant misuse of public resources.

17. There are also irregularities and leakages in budgeting. About 10 to 11 percent ofdevelopment budget going irregularities and leakages. The greater dependence onforeign Aid and loans should be minimized to a reasonable extent and taxation systemshould be modernized by expanding the scope of taxation by increasing tax base andby making the tax structure more progressive. Moreover, elasticity of taxation shouldbe increased by mobilizing additional resources through improving efficiency of taxadministration and without increasing the tax rates.

18. In absence of proper forecasting of government revenue, our budget estimations arefar from realistic. Revenue is buoyant but inadequate to supplement developmentactivities. WTO and SAFTA provisions have limited the prospects for additionalrevenue mobilization for developing countries are required to gradually lower downthe tax rates inclusive of both direct and indirect taxes. The long term forecasting isessential to identify the actual size of revenue and determine the magnitude of surplusthat would be available to match counter-part funding to development expenditure.Thus it is essential to ensure great realism in resource forecasting, projection ofrevenue, aid inflows and the size of capital expenditure budget would need to be inline with the recent performance and reasonable expectations.

19. The budget process needs to be made more responsive less "top down" and more"bottom-up" in terms of accommodating programs so long as they are consistent withsectoral strategies and priorities proposed by local level constituents and lineministries to improve the effectiveness of public spending. It is necessary to promotegreater local ownership of the public expenditure program. It is also necessary tostrengthen revenue consultation committee by providing legal status.

20. There should be a budgetary certainty regarding on the scheduled day of presentingthe full-fledged budget for the whole fiscal year.

21. The budgetary decision should be carried out with social and economic objectives inview rather than fulfill political objectives.

22. Earmarking of funds can help better achieving the budgetary goals.

23. Announcing the budget through ordinance (special budget) bringing incomplete andpersistent delay of budget, showing rude behavior and physical attack to the financeminister in the parliament etc. should be discouraged. All political parties and themembers of the parliament must obey the parliamentary norms and values showingserious concerns about the fate of national economy and economic prosperity ofNepalese citizen with strong support and backup for the early budget presentation.

24. There should have strong unity among all political parties on national economicagenda and have consensus for the early and complete budget in

such a manner thatproperly addresses the current issues of the national economy and maintaining theeconomic dynamism.

25. To establish the ownership of the people and enhance the public partnership informulating budgetary policies and programs and policies in democratic system,Government should take valuable suggestions and advices from the leaders of thevarious political parties, member of the legislative-parliament, Economists,academicians professionals, commercial organizations, representatives of variousprofessional, representatives of professional organizations and representatives of civilsociety as well.

26. Sectoral policies and programs of budget should be need based and priorities orientedsuch that they can contribute to trade facilitation, increase in investment, control insmuggling, increase feeling of security in public, increase in billing system of valueAdded Tax through the improvement in custom valuation and impact positively onoverall revenue collection.

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APPENDIX-A

FY	Tex	TR	FD	BD	FG	GDP
2005/06	110889	72282.1	39861.1	24779.6	13827.1	654084
2006/07	133605	87712.1	45037.7	30091.7	15946	727827
2007/08	161350	107623	60875.8	33031.2	27469.1	815658
2008/09	219662	143475	76187.5	49804.7	26382.8	988272
2009/10	259689	179946	79743.3	41197.4	38545.9	1192774
2010/11	295363	199819	95544.4	49622.2	45922.2	1366954
2011/12	339168	244561	94793.4	5379.61	40812.2	1527344
2012/13	358638	289698	49033.1	6383.55	35229.9	1695011
2013/14	435052	369228	78430	3895.66	33969	1964540
2014/15	531340	413930	19520	3315.2	73388	2120470

Source: Economic Survey, FY 2013/14 to 2014/15 MoF, GoN.

APPENDIX-B

Equation	**1**	**2**	**3**	**4**
Dependend variable	BD	TE	TR	FD
Independent variable	GDP	GDP	GDP	GDP
Constant	56157.96	-53941.82	-83372.08	64568.69
Coefficient	0.024062	0.259265	0.225389	-0.000510
R^2	0.4340	0.9830	0.9866	0.000110
AdjR^2	0.363	0.980	0.985	0.124
T-value	4.144	-3.217	-6.459	2.694
D-W	1.299	1.513	0.635	1.263

Note: BD = Budget Deficit,TE = Total Expenditure, TR = Total Revenue and FD = Fiscal Deficit.