

CHAPTER - ONE

INTRODUCTION

1.1 Background of the Study

The word 'Budget' is said to have its origin from the French word 'Bougett' which refers 'a small bag'. Today bag itself is not vital but people are anxious to see what the bag contains. Therefore the bag contains economic bill presented by the Finance Minister in the parliament House annually. Every democratic government makes vigorous effort for this end, maximizing the welfare of the community in the modern times. In order to achieve, the government takes in hand various socioeconomic activities. A budget, therefore, is not only a financial statement of actual and anticipated revenues and outlays of the government but is also a document of detailed programmes and policies of action which they desire to pursue in the coming years for raising the level of economic activity.

Government budget now is the nerve center of public economy since it is a major instrument of social and economic development. But there was a time when it was considered merely a report for the information of the legislature. It was even made an object of ridicule. A budget maps out the process of acquiring scope resources for government use or for use under government direction. It should be noted that it is not a balance sheet of the whole economy because it does not present a complete picture of the financial condition of the country. From government budget we can not get a picture of the total assets and liabilities of the country but only that of receipts and expenditures of a government for the year under reference.

A government budget is a financial plan covering outlays and receipts of the government. "Usually it is embodied in a document that may be called the budget, but the budget is much more than that. It is the outcome of a process that includes preparation of the financial plan, review of the plan by the legislature where there is one, execution of the plan, and (ideally) evolution and public reporting of the results." (Singh 1982)

Budgetary system of Nepal is not so longer. In the form of systematic presentation of budget was introduced in 1951 after democracy presented by the finance minister Subarna Shamsher with the anticipated revenue estimation was of amount Rs. 3.05 crore. According Government Act. 1951, it was mandatory to prepare income and expenditure estimate for coming year and obtain consent from the president, after obtaining from president the budget was made public.

In every under developed country, national government play leading roles in planning and implementing programs for economic development would require and provide the incentive for a rapid improvement in the system and technique o government budgeting. It is thus found essential and important to pursue a study that would highlight and assess the policy framework of the budgets of the democratic government in Nepal.

The budget being a financial statement of the government is a decision making process to incur expenditure and generate revenue. Budgeting is carried out to fulfill certain state responsibilities and objects of social and economic development. Public budgeting involves the selection of ends and the selection of means to reach those ends. Public budgeting systems are systems for making choices about ends and means. Complex channel information exchange and assessments about what is or isn't being achieved. Series of intricate processes that link both political and economic values are integral to budgeting system. Government is entrusted with number of social and economic obligations. Some of the objectives are social while others are political. It can become a good source of public information of past activities, current decision and future prospects.

A government budget is a financial plan outlays and receipts. Usually it embodies in a document that may be called the budget, but the budget is much more than that. It is the outcome of a process that includes preparation of the financial plan, review of the plan by the legislature where there is one, execution of the plan and (ideally) evaluation and public reporting of the results. A good budget document includes text and tables designated to serve the multiple purpose of the budget. The text explains and justifies the decisions reflected in the budget. Budgeting serves several purposes that: a) it sets a framework for policy formulation, b) it is a means of policy implementation, c) it is a means of legal control and d) the budget document may be a

source of public information on past activities, current decisions and the future prospects.

There was a time when the budget was considered merely a report of information of legislation. But today the budget is the nerve center of public economy. It has developed into a major instrument of social and economic development. Before Keynesian theory in the period of classical economists and their followers, the budget has the passive role in the economic development, since the classical economist advocated the balanced budget as the golden rule and advocated the use of public expenditure only for maintenance of law and order, defense and certain social overheads. But the economic depression of the 1930`s reveals the fact that the correct disorder situation of the capitalist economy. The government intervention has become a principal instrument which has emerged from the words of Keynes.

In today`s world the budget is known as the device for influencing the allocation of resources throughout the economy directly through expenditure decision and indirectly through policy decision built in to the budget. It is important tool in learning the relationship of government programs to economic and financial conditions and trends in fashioning suitable economic and financial policies and measures.

The role of budget in a developing country is much different from that of developed country. In developed countries (economic), budgetary measures can minimize the cyclical influence through the maintenance of aggregate demand. Conversely, unemployment is not cyclical in nature in developing countries but chronic, reflecting structural bottlenecks of the economy. Therefore, injection of additional purchasing power, instead of increasing the level of production and employment causes larger import and raises the price level. This is why budget is used in developing countries as an integral part of development plans.

Deficit budgeting is common characteristics of almost all budget in today`s world. As state has right to use all the available resources in the economy and not limited to its possession only, government can have excess to its revenue. Deficit financing may be added productivity and additional value in the economy but it may also create burden to the economy. Deficit financing is productive when expenditure is made on capital

goods and productive channels. Deficit financing for the current expenditure and consumption may cause the burden to society.

1.2 Statement of the Problem

In developing countries like Nepal, unemployment is not cyclical in nature but chronic, reflecting structural bottlenecks of the economy. Therefore, injection of additional purchasing power, instead of increasing the level of production and employment, causes larger imports and raises the price level. This is why budget is used in developing countries as an integral part of development plans.

Nepal is a country facing a major macro economic crisis, indeed, in many respects its macro economy is reasonably sound, with an improving balance of payments, adequate foreign exchange, reserve, relatively modest inflation, fiscal deficits financed largely by external aid and relatively low levels of domestic borrowing. However, it is stuck in a low level equilibrium, with declining investment, modest economic growth, high population growth and widespread particularly weak and fiscal stability is being maintained largely at the expense of development activity, Although public spending averages at round 18 percent of 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 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 resource mobilization and reduced dependence on foreign financing, current account and balance of payment improvements, poverty reduction, fiscal welfare improvements, better law and security environments, etc. but non of these indicators are found to be satisfactory in our national development exercise despite the implementation of ten periodical plans. In Nepal, budgets seem to have been characterized uncertainties allocation of resources usually more with optimal expectations. Due to such phenomenon several programs have to leave out. It may be noted here greater preparation of the total development budget is financed by foreign government and loan.

It has been widely realized that the developing countries are suffering from the resource gap and it is financed through internal and external sources. Realizing this factor, importance of government role in economic development has been greatly accepted over the time. The government expenditure has been increasing every year due to expanding activities of the government of Nepal. And increase in government revenue is not sufficient to finance increased government expenditure. Domestic resources have been ever insufficient and there is different between outlay and revenue. Therefore, increasing resource gap is the characteristic phenomena of Nepalese budget each year. The way out for the fulfillment of such gap of Nepal budget is to resort either to the grant or loan.

Deficit financing has been adapted to Nepal right from the introduction of budgetary system. Deficit in a country indicates a situation in government's budgetary operations when expenditure in government sector exceeds the resources at its disposal in a particular year. The government may cover the deficit either by running down its accumulated cash balances and internal borrowing or by foreign loan and new tax proposals. In the budget structure of Nepal, although all the means are employed to cover the deficit, virtually it is customary that the foreign aid disbursement has been increasing every year.

As accordingly the situation of a budget deficit is increasing. There are many challenges to finance it. Most of the countries are financing it with the help of foreign loan and domestic borrowing. As deficit is increasing, there is no doubt to increase foreign loan or domestic borrowing. Nepal is also facing the same problem where budget deficit is increasing. But can economy endure the financing process easily is the main question. In such context of increasing budget deficit, it is important to study the sources of financing it and also to analyze the trend of financing instrument as well as their relationship with budget deficit.

1.3 Objectives of the Study

This study is to find out the role of budget in economic development of Nepal. The specific objectives are as follows:

- i. To examine the trend and pattern of public expenditure and public revenue.
- ii. To examine the budget deficit.

1.4 Significance of the study

Budget plays the important role for the economic development of the every country in the world. It has number of social and economic objectives. For the rapid development of the economy, budget should fulfill the objective of increasing employment opportunities, reducing poverty and inequality, increasing the standard of living of its people and the most important the stability in the economy.

This study intends to seek the degree of relationship between budgetary deficits and it's impact. This study entitled "Trend and Pattern of Budget Deficit (A case study of Nepal)" has attempted to fulfill the research gap and to suggest some policy recommendations for the future budgetary practice. Being a developing country, the budgets in Nepal have been implementing to solve the problem encountered by the economy by targeting for higher goals whereas the capability and resource of the government could not match. Although nearly sixty budgets have been already implemented since 1951, improvements in the quality of life of the people have been at marginal and the rate of economic growth has remained insignificant. In this context, it would be interesting and useful to see and analyze the type of objectives, politics and priorities set in the budgets and the level of their actual outcomes so that the differences between the two could be identified and some useful measures could be find out to improve the system of formulating budgetary objectives, policies and priorities.

Foreign aid and loan has been increasing steadily to meet the resource gap showing economic dependency. Such gap between demand and supply of resources can not be fulfilled only from internal sources of developing countries. Hence, there is need of

external capital and therefore foreign aids are one of the most important sources of deficit financing. Foreign aid has two forms: grants and loans. Grant is resource transfer without any requirement of repayment. On the other hand loan must be repaid after the end of maturity period interest charges as well.

No doubt, foreign aid plays an important role for deficit financing in economic development of underdeveloped countries like Nepal. This accounts the fact that domestic resources are inadequate to meet the financial requirement. The present level of capital level of capital formation is too low and any substantial increase in saving is not possible due to the extreme low level of income and wide spread poverty. The tax base is very low and most of the taxes are indirect in nature. This limits the possibility of mobilizing the tax revenue. On the other hand, there is very little scope of public borrowing due to very low per-capita income, underdeveloped money and capital markets. At this critical situation the only alternative to pull the economy out of the vicious circle of poverty is the foreign aid. Thus, foreign aid is gainful for the acceleration of the growth mechanism in underdeveloped countries like Nepal.

Therefore, this study on budgetary deficit and its sources of financing in Nepal will make additional contribution to some extent for pointing out some important facts regarding the policy instruments along with the assessment of revenue and expenditure pattern and internal and external sources of financing budget deficit.

1.5 Research Methodology

Government Budget is the sole tool for the successful implementation of Fiscal Policy. It is the focal point of Government Finance. In its simplest form a budget is collection of documents that refer to the financial condition of the government including information on revenues, expenditure, debt, activities and purpose. Budgeting is one of the universal human experiences. Budget means the estimate of revenue and expenditure during a specific period ordinarily.

Most government policies involve outlays should be reflected in the budget. Budgeting is technically and politically difficult for all countries, but particularly so for less developed countries. Above all, their governments tend to embrace objectives that are ambitious in relation to the means available for their attainment. The scarcity of means is indicated by low per capita national income and by conditions that result

in low productivity and inefficient markets. Other forms of scarcity that complicate budgeting in the majority of less developed countries are a shortage of civil servants who are well trained and experienced in financial and economic matters and a lack of systems to provided needed information. The cyclical instability to which primary-producing countries are subject is a hazard to revenue forecasting; if the government attempts to use fiscal policy to mitigate such instability, heavy demands are placed on the budget process. Economic planning, which is widely considered essential to accelerate development, gives rise to problems of co-ordination between planning in the broad sense and budgeting.

1.5.1 Research Design

This study is primarily based on secondary data descriptive, analytical as well as quantitative approaches are 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 governments in Nepal after the restoration of multi-party democratic in 1990. Therefore, the study is mainly related with the various budget speeches. The data information and policies extracted from the budget documents have been tabulated and presented in meaningful order. Different statistical and other models have been tabulated and presented in meaningful order. Different statistical and other models have been applied to interpret the data and to come into conclusion. Among them trend analysis has been made extensively. Besides these quantitative data presentation, this study also possesses qualitative aspects of the budgetary policies; their implementation and actual outcomes.

1.5.2 Sources of data and information

The main sources of information for this study are based on published secondary data mainly the budget speeches and economic surveys. List of others sources of data are given below.

- i. Government of Nepal, Ministry of Finance:
-Various issues of Budget Speeches, Economic Surveys,
- ii. Government of Nepal, National Planning Commission:

-Various issues of plans.

iii. Nepal Rastra Bank:

-Various issues of Quarterly Economic Bulletin, Economic Report, Current Economic situation of the nation, Government Finance Statistics and other publications

iv. Central Bureau of Statistics:

-Various issues of Statistical Yearbook, Statistical pocket book and other publications.

v. Centre for Economic Development and Administration (CEDA):

-Various published research report of CEDA specially the reports pertaining the fiscal affairs.

1.5.3 Analysis and interpretation of Data

This study is based on the secondary data collection as stated above in ‘Sources of data and information.’ Processing of data has been done in computer using application programs like MS WORD, MS EXCEL etc. Some relevant statistical, accounting, mathematical and financial tools have been applied in analysis and interpretation. Presentation has been made in the form of tables, graphs, charts and figures etc.

1.5.4 Limitations of the Study

This study concentrates on fact finding and mainly covers major aspects of the budget such as revenue, expenditure and different sources of deficit financing.

- a. This study is based on secondary data hence the reliability of the study is based on accuracy of secondary data.
- b. This study does not analyze the overall impact of budget of the economy.
- c. This study considers the time frame of only 12 years (1996/097-2007/08).

1.6 Organization of the Study

The study has been segregated in to the six chapters, each defining to some aspect of the budget deficit and its sources to finance. The titles of each of this chapter are as follows:-

Chapter one describes the general background of the study, statement of the problem, objectives of the study, significance of the study, research methodology is presented the major components of this methology are its design, sources of data, tools and techniques used in this study. Limitation of the study as well as its organization.

Chapter two deals with review of related studies. In this chapter related books, articles and dissertation is reviewed.

Chapter three includes the major part of this thesis that is presentation and analysis of data. Revenue and expenditure as well as deficit financing and its sources to fulfill are presented in this chapter.

Chapter four includes the Share of Debt servicing, Regular Expenditure and GDP

Chapter five consists of Summary, Finding and Recommendation of the study.

CHAPTER-TWO

REVIEW OF LITERATURE

2.1 Concept

The concept of budget is normally associated with national governments 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. Along with the proposed revenues and expenditure relating to these activities, a budget presents the financial accounts of the previous year, the budget and revised estimates of the current year and the budget estimate of the coming financial year. In the context of budget, several publications are published in the form of booklet, book, journal; articles etc. Like wise, there are several books, booklets, journals and articles written by Nepalese as well as foreign writers.. Various studies have been done in the past on 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 Perspective

2.2.1 The World Bank

World Bank had reviewed public expenditure pattern of Nepal in 1999. In this study, WB has pointed out that fiscal management is weak reinforcing in widespread perceptions of misuse and waste of scarce public resources. The review further found that budget preparation is divided into 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 drive away too little resources. There is even weak link between plans and the annual budget without having rolling public expenditure programmes.

Moreover the study found that institutional mechanisms for project screening and expenditure management are weak and the fund release process favor quick spenders rather than priority projects/programs. The study has identified that the government budget preparation process is as a top-down process, which is unresponsive to local needs and initiatives. Most of the projects are centrally administered and managed through line ministries with little involvement of local beneficiary/community groups.

As the study pointed out, institutional weakness was the result of over-staffing, low-salaries, political interference 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 economic and political development.

The study conducted by the WB has suggested some solutions to improve public resource 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, (f) strengthens the institutional capacity for caring development activities.

The WB had carried out another study on “Public Finance in Development” in 1988 and had drawn the conclusions 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 play a greater role as an investor than in industrial countries.

2.2.2 International Monetary Fund (IMF)

Barrow (1991) found a weak relationship between public investment and growth, especially if the ratio of private investment to GDP is held constant. He argues, his cross-sectional findings indicate the public investment is not an important determinant of growth.

In recent years, an increasing number of countries around the world have implemented fiscal decentralization programs consisting primarily of devolving revenue sources and expenditure functions from the central government to local

government. A strong argument drives this phenomena is that local government. A strong argument drives this phenomena is that local governments are closer to the people and hence better equipped to collect information on local preferences and necessities at lower costs. Moreover, decentralization is expected to boost public sector efficiency to deliver service and eventually scarce public resources that can channel into more productive sectors. On this ground, a research work entitled Fiscal Decentralization strengthen social capital focusing on three indicators such as confidence in government, civic cooperation and associational activity with the help of cross-country estimation by regression of industrialized and developing countries between fiscal decentralization and social capital. It is found that social capital can be boosted by fiscal decentralization that brings the government closer to the people and be integrated into second generation reforms. The findings reinforce the subsidiary principle of public finance on the ground that social capital can be boosted when local differences in necessities and preferences are taken into account in the policy making and expenditure management processes.

It is argued that the protection and enforcement of rights and civil liberties entail public costs. Therefore, government spending has a bearing on civil rights. However, the budgetary expenditures needed to protect and enforce one type of right may displace resources that could be used to protect and enforce other rights because of the resources constraints with the government. Viewing this, Luiz de Mello and Randa Sabi carried a study on the little Government Spending Rights and Civil Liberties. They used sample data taken from some developed and developing countries as an empirical evidence and found the results that the government expenditure on defense, law and order, social security, education and health care are associated with three rights indicators –property rights, equality of citizen before the law and economic freedom. An increase in spending on law and order seems to improve the indicators of rights and civil liberties, and lower budget deficits seem to improve property rights and equality before the law. Furthermore, they found that corruption is associated with worse rights indicators.

2.3 Others

Government Expenditure and inflation are related. It is generally believed that higher government spending leads to higher inflation as the government seeks additional sources of revenue. In this reference had performed a comparative study of the 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 the level of government expenditure, the larger the increase in nominal interest rate that result from a given increase in government spending.
-) The more inefficient the tax collection system is, the higher is the optional interest rate for a given level of government spending.
-) The share or revenue 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 a inflation tax. Because the ultimate reason for the existence of a high inflation tax lies in the fact that government need for revenue co-exists with increasing marginal costs of collecting alternatives taxes.”

2.4 National Perspective

2.4.1 A brief review of previous research works

Very few research 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 have been made are also not in depth and details. A few dissertations have been submitted to Tribhuvan University Thesis which are somehow related on this area. An attempt has been made to review some of these dissertations.

Sharma (1988) has made a research about the Nepalese budgetary structure. In this study it has attempted to point out some features, prevailing practices and problems of the Nepalese budgetary structure inherent in the Panchayat

System. This study covers the time span of twenty-two years from 1964/65 through 1985/86. He has used only secondary data, which are mostly published by the Ministry of Finance and has made an effort to analyze them in a meaningful manner by using some common statistical measures. Mr. Sharma conducted this research to fulfill and to accomplish the following mentioned objectives;

1. To analyze the overall budgetary structure of Nepal specifically for the period of 1964/65 through 1985/86.
2. To examine the trends in public expenditure, revenue, internal and external borrowings.
3. To assess the policies and problems of budget in Nepal.

His work clarifies that the pattern of government expenditure has followed more or less the uniform course throughout the reference period. The regular expenditure on the heading 'loan repayment and interest' has been enhancing its relative position due to growing reliance of Nepalese budgets on foreign as well as domestic loan. Similarly, in the development budget on the heading 'social services' is scanty through out the reference period except in FY 1964/65. It has been mainly due to the policy of privatization of most consuming sector under social services such as education and health.

Major finding regarding the trend of government expenditure is that it has been increasing both in absolute and relative terms. The increasing pace of government expenditure is higher than that of government revenue. It is not enough to cope with the development objectives and targets as preceded by periodic development plans. The study comes out vividly from the fact that the called outlay as projected by periodic plans never been met by the summation of development expenditure of corresponding period. Thus, he points out a serious problem of widening resources gap existing since the inception of the budget history in Nepal. It has supported this finding with measuring low expenditure ratio and expenditure elasticity. This finds poor tax efforts and negligible contribution from non-tax revenue primarily responsible for the resources gap.

Sharma has measured the elasticity of co-efficient for all taxes heading i.e. direct tax, indirect tax and land tax during the period 1975/76 to 1985/86 is less than unity. The

actual performance for collecting the tax revenue shows a downward trend. This fact is supported by the comparative study of elasticity coefficient of these tax heading during the period 1972/73 – 1980/81 and 1975/76 – 1985/86. Though the elasticity of land tax has been seen negative but plays a crucial role for lowering the overall tax revenue in the revenue structure of Nepal.

He concludes that the Nepalese budget has been working in a perpetual financial crisis resulting in excess on external assistance. At the same time Nepal has been experiencing the problem of inefficient and under utilization of available funds. Actually and external capital inflow can not have strengthened the national economy, and Nepal has been restoring to the subsistence economy. It further concludes that that the basis at which Government of Nepal has been building its budgetary evolution is very weak and cannot have shouldered these evolutions in the budget of Nepal.

The study has recommended the following recommendations.

1. To cope with the existing financial problem Government of Nepal should aim to mobilize the domestic resources adequately. For this, the revenue share of non-tax sources should be increased by reforming administration and management.
2. The upward revision of tax rate for mobilizing the additional resources will give the negative result, such as tax evasion and tax dodging. Therefore, attention should be paid to increase the tax elasticity by broadening the tax base, and strengthening the revenue administration.
3. Maximum efforts should be paid on collection of direct taxes.
4. Government of Nepal should be serious to utilize foreign capital into more productive sector and infrastructures development in such a way that can create the necessary basis for the self reliance of the national economy in the future.
5. The basis on which programmed and performance budgeting system is formed, should be strengthened. This fact should be taken seriously by Government of Nepal.
6. Government should find the effective ways to check corruption.

Ranjitkar (1987) has made a research entitled 'Budget innovation in Nepal' in 1987. She has attempted to identify the budgetary problems and has suggested some remedial measures to them. It has included some theoretical aspects of budget innovation in developed countries. It has also 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. It has pointed out the following objectives of his study.

1. To examine the revenue and expenditure pattern of Government of Nepal,
2. To analyze the share of external and internal borrowing in the budget of Nepal, and
3. To make a critical assessment of the budgetary policy of Government of Nepal.

It has recommended that the government should first create an environment in which the innovation could be adopted. In her opinion, the guidelines for innovation as suggested by John C. Bayer might be of great relevance in this connection. Some of the important guidelines enlisted by Ranjitkar are as follows.

1. Integration with decision making: The innovation should be incorporated within the normal decision-making process of budget from the very beginning rather than being initiated as a parallel process to be integrated at a latter stage.
2. Selective introduction: The change has to be introduced gradually with careful phasing over a period of time as the constraints are relaxed.
3. Mitigation of new demands: It is suggested to minimise those changes that involved operating ministries and departments. There is a built-in reluctance to change which can turn to unwillingness to participate if changes are extensive and frequent, are not fully understood, or place new demands on the departments.
4. Institutionalize the innovations: Institutionalize the budgetary innovations so as to make them accepted as a part of the administrative and planning of Government of Nepal.

5. Planning for staff development: It is considered essential to incorporate planning for staff development as an integral component of the entire exercise. It further recommends that the manpower development in Ministry of Finance as well as the line agencies is a precondition for the institutionalization.

Upreti (2002) had conducted a research on the topic “Some Aspects of Public Expenditure in Nepal (1981-2002)”. The time span of the study was 18 years from 1981 to 1998 which covers two distinct political regimes viz.the panchayat system and the multiparty democratic system. In this study it has attempted to analyze the trend and structure of government expenditure to find out the major priority sectors identified by the government. He has also tried to study its impact on employment and production using some economic models.Some of the major findings is as follows:

1. The growth of public expenditure in Nepal has taken place more rapidly than the growth of GDP of the country in both pre liberalization and post liberalization periods. The higher relative growth of regular expenditure than development expenditure in post liberalization period explains the increasing consumption expenditure. Although the rate of investment has been growing faster in post liberalization reflecting the private sector’s participation. The private sector is attracted mainly towards the selected areas.
2. Neither structural adjustment nor the liberalization process has been fully successful in achieving some of the economic goals such as reducing deficit and the resources gap. Furthermore, the government lacks the strong commitment, clear vision and sufficient assessment necessary to apply liberalization and privation in Nepal.
3. The inconsistency between planning and budgeting of public expenditure is due to the setting of unrealistic planned, government’s inability to collect sufficient resources and to utilize them properly in time. On the basis of this study, It concludes that the present expenditure pattern of government in the Nepalese economy is unable to create more resources and to achieve faster economic growth.

Upreti has developed some policy measures that could be considered by the relevant authorities reforming the budgetary policy in Nepal.

1. The government should increase the proportion of productive investment and allocate efficiency unlike its past lit-and miss policy. Therefore, a major reform in planning and budgeting required.
2. The pattern of public expenditure should be re-arranged. The budgetary classification should be done according to the nature of productivity of different sectors. Budget should be properly classified and planning of expenditure should be realistic.
3. The government should be involved in those areas where private sector is still unlikely to go. People's participation should be increased in development activities that help to achieve sustainability and to utilize resources
4. For proper accountability, internal and external auditing and budgetary control should be tightened up.
5. Foreign aid policy should be reviewed. The government should not be keen to obtain foreign aid haphazardly. Foreign aid should be invested in the sectors that generate further income rather than present consumption. The government should be aware of "conditions" attached to aid.

2.5 Others

Khanal's(1988) research work on the topic "Public Expenditure Pattern in Nepal: Growth Pattern and Impact." for the period of 1965 through 1981 was conducted in 1988 for Ph.D. with the following objectives:

1. To examine the growth and pattern of public expenditures;
2. To explain the public expenditure growth in terms of both demand and supply factors:
3. To examine the impact of public expenditure on the economy in general and private investment, foreign trade, money supply and prices in particular; and

To draw some policy implications to short term economic stabilization and long term development.

It came to the conclusion that public expenditure in Nepal had increased for more than the increase in GDP of the country. During his study period, total government

expenditure increased by only 2.04 percent; regular expenditure by 8.66 percent and development expenditure by 9.08 percent. It is found that the consumption type of expenditure also expanded at a faster rate. As per the growth rate analysis, Khanal pointed out the social services sectors: Education and health increased in a faster growth than that of other services like general administration and defense.

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 FY 1954/55 – 1974/75 and concluded that the expenditure/GDP ratio had increased substantially. This ratio 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 centre in Nepal, had carried out a study on financing of the public sector expenditure in Nepal in 1987. The study covered a period of a decade from FY 1974/75 to 1984/85. IDS reported 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.

Thapa (1996) has described in ‘Deficit Financing in Nepal’ that the deficit financing has important role for economic development. It is more significant and useful in the context of dealing with problem of stabilization. The fundamental virtue of deficit financing is that it helps to reduce the level of unemployment. From the point of economic view, Deficit financing is desirable and will remain a continuous feature in the budget of developing countries and so in Nepal. However, deficit financing is inflationary and therefore, it must be within the desirable limit. After analyzed the deficit financing in Nepal, It found the budget and fiscal deficit is widening over the study. So, it is suggested that the fiscal deficit should be at level of 7 percent of GDP where as the level of budget deficit should be at around 5 percent of GDP.

Nepalese budget estimation is mainly based on foreign aid and grants because of the limitation of Nepal’s internal financial source. In this regard **Poudel** (1986) writes; there is hardly any sector which has not received some form of assistance and in which several donor had been involved. The larger proportion of external assistance

still comprises of grants even though, the share of loans especially from international agencies has been increasing the recent years.

Singh carried out a study under the title of “The fiscal system of Nepal”. Which was analyzed the trend of revenue and expenditure during the period from FY 1954/55-1974/75 and concluded that the expenditure/GDP ratio had increased substantially. This ratio was only 2.44 percent in 1955 and increased to 10.57 percent in 1975. Another notable finding of Mr. Singh was the rise in the development expenditure/GDP ratio, which increased from 4.07 percent in 1966 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.

2.6 Research Gap

Resources gap is the difference between total expenditure and total revenue of the government of country. When a country is spending more than its internal resources, there will be a resources gap in the economy. To find out the resource gap in the economy the annual budget documents of the government analyzed. All the research works mentioned are basically related to the budgetary situations. Those studies have found different conclusions in global as well as Nepalese context. Some of these researches concentrated on the area of expenditure management and some, in contrast, on public resource management.

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

None of the available works analyses the budgetary situation in Nepal especially after the liberalization of Nepalese economy, which in fact, is a challenging issue among the Nepalese planners, policymakers and social scientists. Hence, a clear gap is seen among the research works available in the area of Nepalese budgetary system. This study has attempted to fulfill this research gap and to suggest some policy recommendations for the future budgetary practice.

CHAPTER- THREE

ANALYSIS OF EXPENDITURE, REVENUE AND BUDGET DEFICIT

In this chapter an attempt has been made to analyze the trend and pattern of expenditure, revenue budget deficit of government during the period of 1996/97 to 2007/08.

3.1 Government Expenditure

Government expenditure means the actual expenditure of government during the specific fiscal year. It can be divided into the following headings:

1. Recurrent Expenditure
2. Capital Expenditure
3. Expenditure on debt servicing

It is noted here that the terminologies used for recurrent and capital expenditure were regular and development expenditure representing until 2003/04. Current expenditure, capital expenditure and principal repayment are used to describe governmental expenditure from 2004/05.

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. Its main components are expenditure on general administration, social service, defense, economic services, loan, principal payment 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. Expenditure on debt servicing:

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 regular 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 largert as that of the previous year. (Adhikari, 2004)

3.1.1 Trend of Government Expenditure

Table 3.1 reflects the amount of regular, development, principal repayment and total expenditure during the review period. In 1996/97 the total expenditure was only Rs. 56723.7 million that mounted up to Rs. 168995.6 million in 2007/08. This clearly depicts the steady and increasing trend of expenditure in Nepal.

Table 3.1 also shows the amount and percent share of regular and development expenditure in total expenditure during the period of 1996/97 to 2007/08.

The percent share of regular expenditure in total expenditure has moved up from 47.67 in 7996/97 to 66.80 in 2007/08. Its total amount and percentage share in total expenditure is in increasing trend during review period. When expenditure is analyzed, regular expenditure could not be controlled by government as compulsion of increment in employee's salary, among others together with the expansion of government machinery leads regular expenditure to increase every year.

Similarly, total amount and percentage share of development expenditure in total expenditure has been decreasing from 52.33 in 1996/97 to 34.70 in 2007/08. The total amount of development expenditure has also been increasing, however, relatively less

than that of regular expenditure because of the compulsion of expanding infrastructural facilities, social services, economic services etc. The percentage share of developing expenditure in total expenditure is in decreasing trend during the review period except fiscal year 2004/05 and 2005/06.

The fiscal year 2003/04 in which the percentage share of regular expenditure in total expenditure is the greatest than that of development expenditure in the study period which shows the consumption nature of government.

In the same fashion, regular expenditure heavily increased during the review period. In absolute term it has risen from Rs. 24181.1 to Rs. 98172.50 million in 2007/08. The percentage share gives clear idea of the very trend of regular expenditure. However, small fluctuation is seen in the share of regular expenditure to total expenditure. The development expenditure of government has increased slowly as compared to regular expenditure. In absolute term, it has moved up from Rs. 26542.6 million to Rs. 55261.70 million from fiscal year 1996/97 to 2007/08. The percentage share of development expenditure to total expenditure shows a continuous decreasing trend up to 2003/04. Then it has also a fluctuating in nature. The annual percent change of total expenditure, development expenditure and regular expenditure is also shown in table 5.1. All these expenditure heads have fluctuating trend. But in development expenditure there is also have negative annual percentage change in the fiscal year 1998/99, 2001/02 and 2002/03. Such types of allocation of budget in development slow down the development activities. Such scenarios of expenditure took place in the Nepalese budgetary history because of insurgency and political instability in the country. But such negative growth rate of development expenditure has not been taken place since fiscal year 2002/03. In the final fiscal year of review period the annual growth rate of budget in development is 34.7 percent.

Table 3.1

Government Expenditure (Rs. in million)

Fiscal Year	Regular Expenditure	Annual % Change	Development Expenditure	Annual % Change	Total Expenditure	Annual % Change	% share of Total Expenditure		
							R.E.	D.E.	T.E.
1996/97	24181.1	10.8	26542.6	6.3	56723.7	9.0	47.67	52.33	100
1997/98	27174.4	12.1	28943.9	9.0	56118.3	10.6	48.42	51.58	100
1998/99	31047.7	37.4	28531.3	-20.6	59579.0	6.2	52.11	47.89	100
1999/00	34523.3	11.4	31749.2	10.8	66272.5	11.2	52.09	47.91	100
2000/01	42769.2	28.8	37065.9	11.1	79835.1	20.5	53.57	46.43	100
2001/02	48590.0	6.6	31482.2	-12.5	80072.2	0.3	60.68	39.32	100
2002/03	54973.1	6.6	29033.0	-9.8	84006.1	4.9	65.44	34.56	100
2003/04	55552.1	6.6	23095.6	3.3	89442.6	6.5	74.18	25.82	100
2004/05	61686.4	11.0	27340.7	18.4	102560.7	14.7	73.34	26.66	100
2005/06	67017.8	8.6	29606.6	8.3	110889.2	8.1	73.51	26.49	100
2006/07	80331.1	15.1	36379.9	34.2	131851.0	20.7	70.30	29.70	100
2007/08	98172.5	18.6	55261.7	34.7	168995.6	20.8	66.8	33.2	100

Source: Various issues of Economic Survey, MOF N/G

Note: R.E. = Regular Expenditure

D.E. = Development Expenditure

T.E. = Total Expenditure

Regular Expenditure

According to the budgetary classification of public expenditure, expenditure can be divided in two heads i.e. regular expenditure and development expenditure. Hence, regular 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 regular expenditure they are loan repayment and interest, social service sector, general administration, defense, miscellaneous and economic service sector the larger share of regular expenditure is made the share of these sectors are given respectively.

In Table 3.2 the expenditure on economic service reached to Rs.9037 million in FY 2007/08 from Rs.1738.2 million in FY 1996/97. The expenditure on social service sector reached to Rs.32498.2 million in FY 2007/08 from Rs.5909.1 million in FY 1996/97. Interest payment was to Rs.82254 million in FY 2007/08 from Rs.7527.2 million in FY 1996/97. The expenditure on general administration was Rs.10254 million in FY 2007/08 from Rs.2842.3 in FY 1996/97. The expenditure on miscellaneous was Rs.6322.4 million in FY 2007/08 from Rs.2277.5 million in FY 1996/97. The expenditure on defense reached to Rs.1389.0 million in FY 2007/08 from Rs.2357.6 in FY 1996/97. Similarly the expenditure on others was to Rs.6423.8 million in FY 2007/08 from Rs.1529.2. In this way from the given table 3.2 we can see that the regular expenditure on different heads has been increasing.

Table 3.2

Structure of Regular Expenditure in Different Heads (Rs in million)

FY	Economic service	Social service sector	Interest payment	General administration	Defense	miscellaneous	others
1996/97	1738.2	5909.1	7527.2	2842.3	2357.6	2277.5	1529.2
1997/98	1889.9	6993.3	7682.8	3158.8	2582.8	3357.3	1509.5
1998/99	4480.4	10794.6	8723	3435	18290	4767.9	1689.5
1999/00	4683.2	12814.1	10032.8	3864.2	3482.2	4512.9	1905.5
2000/01	4899.9	15366.3	10388.4	5419.8	3813.4	9912.6	2164.9
2001/02	5795.1	16953.1	12205.2	7140.8	5859.4	5494.8	2521.5
2002/03	5078.5	18886.9	161813.3	7335.9	7381.5	5326.4	2726.3
2003/04	5512.8	20808.5	173388.8	8226.5	8520	6069.4	2807.7
2004/05	7167.8	23208.8	14751.3	9269.5	10993	5303	3193.7
2005/06	4529.8	25382.6	20423.5	9735	113112.2	5639.6	5073.2
2006/07	8384	29497.6	6164.0	9735	127112.1	5825.1	5712.1
2007/08	9037	32498.2	82254	10254	1389.0	6322.4	6423.8

Source: Various issues of Economic Survey, MOF N/G

Development expenditure:

The development expenditure has also various components. i.e general administration, economic administration and planning, social services, economic services and miscellaneous and others as the table 3.3 shows that expenditure on economic services was Rs.17054.7 million in fiscal year 1996/97 it is declined to Rs.14349.6 in FY 1998/99 the rate of expenditure is not stable in different Fiscal Year. The expenditure on economic administration and planning reached Rs.30 in FY 2007/08 from Rs.17.3 million in FY 1996/97.The expenditure on Social service was Rs.19254.8 in FY 2007/08from Rs 9281.3.The expenditure on General administration reached to Rs.1635 million in FY 2007/08 from Rs.34.5 million in FY 1996/97.The expenditure on miscellaneous was Rs.16.4 in FY 2007/08 and Rs.650.9 million in FY 1996/97.

Table 3.3

Structure of Development Expenditure in different Heads (Rs in million)

FY	Economic Service	Economic Administration and planning	Social service sector	General Administration	Constitutional organization	Miscellaneous
1996/97	17054.7	17.3	9281.3	34.5	-	650.9
1997/98	17900.2	19.3	10323.5	46.4	3.6	813.3
1998/99	14349.6	2.1	7495.5	259.9	76.5	510.2
1999/00	15466.7	4.8	8638.5	314.3	34.2	519.2
2000/01	17745.1	17.4	8489	965.8	19.8	642.4
2001/02	13562.1	7.6	7927.5	838	11.9	1755.5
2002/03	12561.0	3.4	7075.9	581.3	16.8	875.6
2003/04	13129.0	8.9	7135.2	578.1	36.9	172
2004/05	15394.0	24.2	7940.7	883.6	38	435
2005/06	14797.1	20.3	10151.8	1181.7	100	8.8
2006/07	17938.9	26.8	15529.3	1482.1	115	13.8
2007/08	20840	30.0	19254.8	1635	125	16.4

Source: Various issues of Economic Survey, MOF N/G

Figure 3.1

Trend of expenditure growth rate

3.2 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 there by 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.

3.2.1 Composition and Trend of Government Revenue.

Table 3.4 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. 30373.5 million in 1996/97 to Rs. 103667.3 million in 2007/08. From the trend diagram, it can be seen that it is increasing all the way in the nominal term.

Similarly, table 3.2 shows the trend of tax revenue, which in absolute term has increased from Rs. 24424.3 million in 1996/97 to Rs. 80962.0 in 2007/08. Non tax revenue, in absolute term has increased from Rs. 5949.2 million in 1996/97 to Rs.22705.0 in 2007/08. It is, as a whole is fluctuating in nature. Table 3.2 shows that the absolute amounts of both sources are increasing annually.

In the initial study period the tax revenue was 80.41 of total revenue where as non tax revenue was only 19.59 percent of the total revenue. The percentage distribution of tax and non tax revenue in total revenue are 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 3.4

Composition of Government Revenue (Rs. in million)

Fiscal Year	Total Revenue	Tax Revenue		Non tax Revenue	
		Amount	% of TR	Amount	% of TR
1996/97	30373.5	24424.3	80.41	5949.2	19.59
1997/98	32937.9	25938.8	78.75	6998.1	21.25
1998/99	37251.0	28752.9	77.19	8498.4	22.81
1999/00	42893.8	33152.1	77.29	9741.6	22.71
2000/01	48893.6	38565.1	79.49	10028.8	20.51
2001/02	50445.5	39330.6	77.97	11115.0	22.03
2002/03	56229.8	42587.0	75.73	13642.7	24.27
2003/04	62331.0	48173.0	77.28	14158.0	25.34
2004/05	70191.0	54104.7	77.08	16018.0	25.75
2005/06	72282.1	57430.4	79.45	14851.7	26.64
2006/07	86135.5	70046.0	81.1	16089.3	18.9
2007/08	103667.3	80962.0	79.1	22705.0	20.9

Note: TR= Total Revenue

Source: Various Issues of Economic Survey, MOF N/G

Figure 3.2

Trend of Government Revenue

3.3 Deficit financing

Today, deficit financing has emerged as an important tool of financing the government expenditure. Today's government spends more than its revenue to show itself as welfare state. Government sources of revenue are limited but it has to spend more than its revenue in many social, economic and political fronts. So to maintain its imbalance it has to taken resort of deficit financing. In simple words, deficit financing means filling the gap caused by the excess of government expenditure over its receipts through various sources. Thus deficit financing regarded as when government spends more than it gets through taxes and other sources of revenues.

Developing countries are characterized by low level of income. It is not possible to adopt force saving for resource mobilization. So deficit financing is being used as a reliable instrument. In the period of Second World War when economy was destroyed, it induced that a useful financial policy should be adopted to recover the economy and deficit financing policy was that.

Hence, deficit financing refers to the way in which the budgetary gap is financed. The government resorts to this method of financing when it is unable to cover its total

expenditure through the normal sources of revenue such as taxation, income from the government properties and undertakings, proceeds of loans, small savings, capital receipts and funds as its disposal. Government, in this case, can undertake deficit financing by drawing accumulated cash balance or drawing from central bank or by taking loan from internal and external sources.

Generally, when current expenditure of the government excess the current revenue it is called deficit budgeting. When we take into consideration not only current receipts but also receipts on capital accounts and we still find a gap between receipts and expenditure, the method of financing used to cover this gap is called deficit financing.

So there are two kinds of deficits viz. fiscal and budget deficit.

3.3.1 Fiscal Deficit 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 then budget deficit. Fiscal deficit is covered by grant portion to some extent.

In table 3.5 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. 60875.8 million in 2007/08 from Rs. 20350.2 million in 1996/97. Similarly budget deficit reached to Rs. 33406.7 million in 2007/08 from Rs. 14361.9 million in FY 1996/97. 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.5988.3 million in 1996/97 to Rs.27469.1 million in 2007/08. 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 table 3.5 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 3.5

Fiscal Deficit and Budget Deficit (Rs. in Million)

Fiscal Year	Total Expenditure	Total Revenue	Fiscal Deficit	Foreign Grants	Budget Deficit
1996/97	50723.8	30373.5	20350.21	5988.3	14361.9
1997/98	56118.3	32937.9	23180.40	5402.6	17777.8
1998/99	59579.0	37251.0	22328.02	4336.6	17991.4
1999/00	66272.5	42893.8	23378.70	5711.7	17667.0
2000/01	79835.1	48893.6	30941.50	6753.4	24188.1
2001/02	80072.2	50445.5	29626.70	6686.1	22940.6
2002/03	84006.1	56229.8	27776.30	11339.1	16437.1
2003/04	89442.6	62331.0	27111.60	11283.4	15828.2
2004/05	102560.5	70191.0	32437.70	14391.2	18046.5
2005/06	110889.2	72282.1	39861.10	13827.5	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

Source: Various issues of Economic Survey, MOF N/G

3.4 Sources of Deficit Financing

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 3.6 explains 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 external sources. External loan is carried 66.68 percent of budget in 1999/00 as high point of review period. However, it has seemed 31.15 percent of budget deficit as low point of the same study period in 2005/06. In the fiscal year 1996/97 the external source of financing budget deficit was 62.97 percent of the total budget deficit but the percentage share of external loan in budget is only 31.15 percent in the final year of the study period. The average share of foreign loan in budget deficit is 49.94 percent in the study period.

The table 3.6 further shows that the contribution of internal borrowing plus cash balance was 73.10 percent, highest in the FY 2007/08 of the study period and lowest 33.14 percent of the budget deficit in 1999/00. The average share of internal source of financing in total budgetary deficit is 50.06 percent.

Table 3.6

Budget deficit and source of Financing (Rs. in Million)

Fiscal Year	Total Budget Deficit	External Source (Foreign Loan)		Internal Source (Borrowing + Cash Balance)	
		Amount	% of BD	Amount	% of BD
1996/97	14361.9	9043.6	62.97	5318.36	37.07
1997/98	17777.8	11054.5	62.18	6723.30	37.82
1998/99	17991.4	11852.4	65.88	6139.00	34.12
1999/00	17667.0	11812.2	66.86	5854.80	33.14
2000/01	24188.1	12044.0	49.79	12144.10	50.21
2001/02	22940.6	7698.7	33.56	15241.90	66.44
2002/03	16437.1	4546.4	27.66	11890.76	72.34
2003/04	15828.2	7629.0	48.00	8199.20	52.00
2004/05	18046.5	9266.1	51.34	8780.40	48.66
2005/06	24779.6	8214.3	31.15	16565.30	68.85
2006/07	30091.7	10331.0	33.40	19438.53	66.60
2007/08	33406.7	17367.4	26.9	24430.40	73.10

Note: BD= Budget Deficit.

Source: Various issues of Economic Survey, MOF N/G

Figure 3.3

Budget deficit and source of Financing

It is indeed the economy of Nepal is heavily depending upon the foreign assistance, particularly with loan and grants. Therefore, we can conclude that the foreign assistance plays a significant role in Nepalese economy.

CHAPTER-FOUR

DEBT BURDEN IN NEPAL

4.1 Introduction

Burden of public debts refers to the sacrifices and effect on the community through a rise in taxation at the time of repayment and for paying the annual interests on the government loans. In the other words, every government is bound to repay the public borrowing whether internally or externally with interest (Lekhi, 2002). This burden of public debt is classified as primary burden (financially burden) and secondary burden (real burden). When the debt is increased by the government, the level of taxation has to be raised in order to meet the interest charges, and the income of the people are transferred to the government and such a loss in income of the people is called as the primary burden, secondary burden refers to the high level of taxation imposed upon the community so that their willingness to save and capacity to work is affected.

The total burden of public debt can be divided into two parts; (1) internal burden of public debt (2) External burden of public debt. The internal burden of public debt means that the total part of the debt is held internally. Dalton (1949) takes internal public debt burden as not much significant as the payment of principal amount and its interest involves taxation. It is an early transfer of purchasing power from one person to another or money market. Similarly, (Learner 1995) points out the internal debt may not have any direct monetary burden on a community as a whole, since the payment of interest and increased taxation to meet the burden of debt involved simply transfer the purchasing power from one group of people to another to extent the creditors and tax payers are the same, there may not be any net burden to all the community. But to the extent of creditors and tax payers belong to different income groups, the changes in the distribution of income among different section of the community may take place.

In case of external debt burden is however completely different. External debt imposes real burden on the economy because it reduces national welfare. External debt is paid not in monetary terms but in real terms, in terms of goods and services. Which are exported to the creditor country for the settlement of the debt? The process will have to continue during the whole period of loan because the borrower country

has to pay interest charges, but if external loans are used for increasing the productivity capacity of country, the debt repayment may not be a serious burden. The debtor country may pay off the debt and interest without any difficulty because of increased capacity of export oriented industries. If debtor country does not sufficiently increase the productive capacity, they will have to face the balance of payment problem.

Therefore, any borrower country has to spend the borrowed fund on creation of productive capacity, which further generate income and increase the rate of capital information then it is quite possible than the debt would not be burden to the society. If the borrowed fund spent otherwise and the government would have to borrow again to meet the requirements of development funds and for meeting the charge of debt servicing as well then it is quite possible that this process lead to bankruptcy of the government or debt crisis in the future.

In case of shifting the burden of public debt to the future generation, there is always debate among the economists. Some of the economists have viewed if then present generation reduces its saving in order to meet the debt finance and leaves a smaller amount of capital resources for the further. This will reduces the productive capacity of the coming generation and they will accordingly lose. In this way, burden of public dept may pass on to the future generation. but on the other hands, some economists have challenged the above version and expressed opposite opinion on the subject of burden to the future generation because of state posterity, which pays the additional taxes, will be benefited from the repayment of dept of the dept.

In case of Nepal, outstanding public dept is increasing rapidly each year. Large scale of public depts. have been incurred in the past for financing development programs, but dept servicing capacity has not increasing in the same pace, so that there may be undue strain in the balance of payment owing to out flow of found through dept services. Nepal has been borrowing new fresh loans to repay old loans. This also has alarmed situation of “dept trap“ in the future. Hence, in the context of Nepal, proper utilization of public dept is necessary to reduce the burden of public dept.

4.2 National Outstanding Debt and its Share in GDP

The ratio of public debt to GDP is an important indicator of the manageability of public debt in an economy. The relative magnitudes of public debt to GDP should be taken into consideration for assessing the burden of growing public indebtedness in an economy. Nepal has to borrow huge amount of loans from external as well as internal sources for meeting deficit budget. Burden of outstanding debt is increasing because of the tax revenue and non-tax revenue is not increasing as its expectation and utilization of public debt and corruption. Here, table 4.1 shows the burden of debt through the method of measure of burden of debt as the ratio of public debt to GDP.

Table 4.1

Outstanding Debts and Its Share in GDP (Rs. in Million)

Fiscal Year	External outs. Debt	Internal outs. Debt	Total public Debt	GDP at producer's price	Share in percentage of GDP		
					External Debt	Internal Debt	Total
1996/97	132086.8	35890.9	167977.7	280513	47.1	12.8	59.9
1997/98	161208.0	38406.7	199614.7	300845	53.6	12.8	66.4
1998/99	169465.9	49669.6	219135.5	342036	49.5	14.5	64.0
1999/00	190691.2	34357.0	245048.2	379488	50.2	14.3	64.5
2000/01	200404.4	60043.7	260448.1	441519	45.3	13.5	58.8
2001/02	220125.6	73620.7	293746.3	459443	47.9	16.0	63.9
2002/03	223433.2	84645.3	308078.5	492231	45.3	17.1	62.4
2003/04	232779.3	86133.7	318913.0	536749	43.3	16.0	59.3
2004/05	219641.0	87560.0	307201.0	589412	37.2	14.8	52.0
2005/06	233968.6	116039.5	328679.4	644055	36.3	14.2	43.9
2006/07	216628.9	103776.04	320404.9	727089	29.7	14.2	43.9
2007/08	249965.4	116039.5	366004.9	818402	30.5	14.1	44.6

Source: Various issues of Economic Survey, MOF N/G

Table 4.1 shows the magnitude of outstanding debt, GDP and their ratio, which also assesses the burden of public debt. Above table shows the ratio of internal and external debt to GDP in the year between 1996/97 to 2007/08. The share of external debt in GDP was 47.1 percent in the year 1996/97 which has increased at the higher level 50.2 percent in the year 1999/00. Then it started to decrease, which has decreased to 30.5 percent in the year 2007/08. Similarly, this table also shows the share of internal debt in GDP. It has also decreased from 12.8 percent in 1996/97 which has increased at the higher level 17.1 percent in the year 2002/03. Then it started to decrease which has decreased to 14.1 percent in the year 2007/08. It means burden of public debt is increasing where total outstanding of public debt has increased from Rs.167977.7 million in 1996/97 to Rs.366004.9 million in 2007/08 and share of total outstanding of public debt to GDP has increased from 59.9 percent in 1996/97 to 63.9 percent in 2003/03. Then, it started to decrease to 44.6 percent in the year 2007/08.

This table shows the horrible situation of burden of public debt in Nepal. Above table also shows that the burden of external outstanding debt is greater than internal which may be danger for future generation. This magnitude of the burden of public debt may increase to alarming proportion of productive capacity is not created in the economy for increasing production.

4.3 Issues of Debt servicing in Nepal

Debt servicing obligation of government is very high and has been growing rapidly. The country faces great challenges in front of domestic debt servicing due to stock of debt is of a short term in nature. Even the debt of larger maturity period has now come to the stage of redemption. The internal rate on such debt is high and most of the loans come from banking sector creating imbalances in the monetary sector with its impact on inflationary situation.

The ratio of internal and external debt servicing to total debt servicing and their average annual growth rate and percentage of internal and external to total debt servicing are shown in table 4.2.

Table 4.2

Share of External and Internal Debt servicing in Total Debt servicing (Rs. in Million)

Fiscal Year	Total Debt servicing(I)	External Debt servicing(II)	Internal Debt servicing(III)	'II' as a percent of (I)	'III' as a percent of (I)
1996/97	7527.2	3349.4	4177.8	44.5	55.5
1997/98	7682.8	4201.2	3481.6	54.7	45.3
1998/99	8723.0	4745.5	3977.5	54.4	45.6
1999/00	10032.8	5321.4	4711.4	53.0	47.0
2000/01	10388.4	6201.4	4187.0	59.7	40.3
2001/02	12205.2	6567.5	5637.7	53.8	46.2
2002/03	16181.3	7519.2	8662.1	46.5	53.5
2003/04	17338.8	7908.9	9429.9	45.6	54.4
2004/05	18366.8	10786.7	7580.1	58.7	41.2
2005/06	20423.5	9151.4	11272.1	44.8	55.1
2006/07	22916.3	9594.5	13321.8	41.8	58.1
2007/08	22760.5	10014.7	12745.8	44.8	55.9
Average Annual Growth Rate	9.43	8.26	8.46	–	–

Source: Various issues of Economic Survey, MOF N/G

External Debt Servicing=Repayment+ Interest payment

Internal Debt Servicing=Total Debt Servicing-External Debt Servicing

Total Debt Servicing=Interest payment + Principal payment.

Table 4.2 shows that the amount of total debt servicing in FY 1996/97 was Rs.7527.2 million and has increased to Rs.22760.5 million in FY 2007/08 with 9.43 percent of average annual growth rate. This indicates an increasing trend of total debt servicing.

Similarly, the volume of external debt servicing was Rs.3349.4 million in FY 1996/97 to Rs.10014.7 million in FY 2007/08 with an average annual growth rate of 8.26 percent and the volume of internal debt servicing was Rs.4177.8 million in FY 1996/97 to Rs.12745.8 million in FY 2007/08 with an average annual growth rate of 8.46 Percent .The average annual growth of total and internal debt servicing is higher than external debt servicing. Till FY 2000/01, the average annual growth rate of external debt servicing is higher than internal, since the internal debt servicing is increasing in higher rate than external. At the end of the year, Government is doing well because it has increased its internal sources of debt servicing. It shows us a good condition of Nepal's debt servicing situation.

Table 4.3

Principal Payments in Total Debt servicing (Rs. in Million)

Fiscal Year	Total Debt servicing(I)	Principal Payments(II)	Interest Payments (III)	'II' as a percent of (I)	'III' as a percent of (I)
1996/97	7527.2	3453.3	4073.9	45.9	54.1
1997/98	7682.8	3931.2	3751.6	51.2	48.8
1998/99	8723.0	4642.7	4080.3	53.2	46.8
1999/00	10032.8	5212.7	4820.1	52.0	48.0
2000/01	10388.4	5690.6	4697.8	54.8	45.2
2001/02	12205.2	6435.0	5770.3	52.7	47.3
2002/03	16181.3	9559.5	6621.8	59.1	40.9
2003/04	17338.8	10794.9	6543.9	62.3	37.7
2004/05	18366.8	13533.3	6218.0	73.6	26.3
2005/06	20423.5	14264.8	6158.7	69.8	30.1
2006/07	22916.3	16752.3	6164.0	73.1	26.8
2007/08	22760.5	16386.9	6373.6	71.9	28.0
Average Annual Growth Rate	10.25	13.16	3.72	–	–

Source: Various issues of Economic Survey, MOF N/G

Similarly Table 4.3 shows the servicing amount of interest payments and principal payments in total debt servicing amount. While observing Table 4.3, we can see 10.25 percent of average annual growth rate of increasing trend of total debt servicing. Where the share of interest amount was Rs.4073.9 million in FY 1996/97 and Rs.6373.6 in FY 2007/08 and share of principal payment was Rs.3453.3 million in FY

1996/97 and has gone up to Rs.16386.9 million in FY 2007/08. The average annual growth rate of principal payments and interest payments are 13.16 and 3.72 percent. This shows the increasing trend of principal payments is higher than interest payments.

The share of interest payments to total debt servicing is greater than principal payments in FY 1996/97. Then after; the share of principal payments to total debt servicing is greater than interest payments till under the review period.

The servicing amount of interest and principal payments indicate that large proportion of regular expenditure has gone to creditor countries, which has hampered regular expenditure as well as development expenditure.

4.4 Analysis of Total Debt Servicing Situation

The burden of public debt is measured by the ratio between the debt servicing and aggregate tax revenues and non-tax revenue or total revenue and the ratio between servicing cost and national income (GDP). To analyze the Debt servicing situation to regular expenditure and GDP. This has been shown by table 4.4

Table 4.4

Share of Debt servicing in Regular Expenditure and GDP (Rs. in Million)

Fiscal Year	TD Servicing	Growth rate of TD servicing	RE	Growth rate of RE	GDP	Growth rate of GDP
1996/97	7527.2	10.78	24181.1	10.82	280513	11.26
1997/98	7682.8	2.02	27174.4	11.01	300845	6.75
1998/99	8723.0	11.92	31047.7	12.47	342036	12
1999/00	10032.8	13.05	34523.3	10.06	379488	9.86
2000/01	10388.4	3.42	42769.2	19.28	441519	14.04
2001/02	12205.2	14.88	48863.2	12.47	459443	3.9
2002/03	16181.3	24.57	52090.5	6.19	492231	6.6
2003/04	17338.8	6.67	55552.1	6.23	536749	8.29
2004/05	18366.8	5.6	61686.4	10	589412	8.9
2005/06	20423.5	10.07	67017.8	8	644055	6.48
2006/07	22916.3	10.87	77122.4	13.1	727089	11.42
2007/08	22760.5	-6.8	91446.9	15.6	818402	11.15
AAGR	8.92		11.26		9.22	

Source: Various issues of Economic Survey, MOF N/G

Note: TD=Total Debt,RE=Regular Expenditure,AAGR=Average Annual Growth Rate

From the above table period form FY 1996/97 to 2007/08 The magnitude of Debt Servicing, Regular Expenditure and GDP was Rs.7527.2, Rs.21563.8 and Rs.280513 million in the FY1996/97 and which has increased to Rs.22760.5, Rs.91446.9 and Rs.818402 million in FY 2007/08 respectively.

From the table the nature of Total Debt Servicing, Regular Expenditure and GDP has been decreasing and fluctuating. The growth rate of Debt Servicing, Regular Expenditure and GDP was 10.78, 10.82 and 11.26 percent respectively in FY 1996/97 which was reached to -6.8, 15.6 and 11.15 percent in FY 2007/08. The Average Annual Growth Rate of Total Debt Servicing, Regular Expenditure and GDP are 8.92, 11.26 and 9.22 percent respectively.

CHAPTER-FIVE

SUMMARY, FINDINGS AND RECOMMENDATIONS

5.1 Summary

Budget is a guideline of annual programme and policy of a government. The main aspects of budget are expenditure, sources of revenue and financing of deficit. Expenditure is divided into two parts; regular and development expenditure. Tax non-tax revenue plays a vital role in collection of revenue for meeting the requirement of expenditure. Foreign grants are also included in sources of financing. Sources of deficit financing are clearly mentioned in the budget.

In Nepal, it has been found that the government expenditure is increasing fast compared to revenue. Among the expenditure, regular expenditure, probably has been increasing readily due to growing burden of dept services 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 development expenditure. It is because of numerous in projects implementation resulted from resulted from frequent change in government. During the recent years, because of political instability, the development expenditure stood even below the regular expenditure stood even below the regular expenditure. Obviously, such decaling sanitation of development expenditure would erode the productive capacities of economy through lack of basic socio economic infrastructure.

Due to inefficient government revenue system, the government's revenue collection has not become responsive to the need of the expenditure. That is why, only about one fifty of development expenditure has been fulfilled from revenue surplus. Revenue growth even lags behind the growth of regular expenditure.

After the restoration of the multi-party system, the democratic government also seems unable to introduce new, bold and brilliant measures to mobilize domestic resources. Recently, a major feature of budgetary development has been growing dependence on

foreign loans for deficit financing. Around 66 percent of the development expenditure has been proposed to be financed through the development expenditure has been proposed to be financed through the foreign sources. This is not a happy situation for the country like Nepal which has already borne foreign debt around Rs. 220.0 billion (NRB Report). Its development expenditure upon foreign assistance (grant plus loan) could not be broken even by the democratically elected government. So much remains to be done in the area of budgetary policy if it has to be consistent with the overall macroeconomic policy.

In nutshell, budgetary policies of the government during the 1990s were found to be directed towards economic liberalization, privatization, poverty reduction and decentralization government gave focuses on revenue mobilization with speed.

Up the development expenditure. Agriculture and infrastructure were prime focus of the government with giving due attention to expansion of social services. It can be said that the policy and programs of the budget during the 1990s with poverty alleviation, agriculture modernization, employment promotion, women employment, financial sector reform, good governance, social service and the development of basic and physical infrastructure.

The budgetary policy measures taken by the democratic government through its two budgets deserves appreciation at least in terms of direction towards liberalization, But they are quite inadequate in terms of the desired results. On expenditure side, effort to control expenditure has been made only through the wage and salary which constitute only 30 percent of regular expenditure. But other headings, where the possibility of leakage of resources is equally high, have been left untouched. On revenue side, mainly customs duty and income tax have been reformed. But the reform in the customs duty has been far from rectifying the anomalies contained in the foreign trade regime. These reforms could neither boost the import revenue from the third countries nor enhance the revenue collection in a remarkable manner. Reform in income taxation in line with what is prevailing around the world today, is by far a welcome step. However, it has been at the revenue loss caused by the tax reforms.

Budgetary analysis has revealed that the government has been spending regular expenditure as budgeted but development expenditure and revenue are lacking for behind the budgeted target.

In this way, there is a gloomy fiscal scenario-low development expenditure, high regular expenditure, low revenue collection and high fiscal deficit with high foreign loan inflows. So far, thanks for soft loan provided by donors with low interest rate and high gestation period. But, we can not expect the same situation will remain in coming years in the changing world scenario. There is a drying up of foreign aid flows and donors are reluctant to provide concessional loans. If donors change their attitude, the foreign borrowing will be rather costly. In this way, managing national budget is a challenge for the government, having sole objective of poverty alleviations.

5.2 Findings

1. Unrealistic Budgeting process

Nepal's budgeting process has been highly unrealistic in recent years. In almost all the years in the review period, the budget targets have been set at unduly high levels, particularly for development revenue and foreign aid. This over estimation of resources in turn has led the government to set similar unrealistic targets for the development budget and to accommodate too many new projects. However, the actual budget outcome had fallen significantly short of these optimistic expectations every year. And, since there is little scope for cutting back regular expenditures, the burden of fiscal adjustment has been made through cutbacks in development spending.

2. Development budget is heavily over-programmed

The budget, particularly its development component is heavily over-programmed. The average realization rate during the review period is 89.91 percent. Because of political pressures to accommodate new projects, there are unmanageable projects for development budget. There is a concrete lack of cost-benefit analysis and prioritization of development projects.

3. Declining but still high deficit

Despite a series of fiscal reform, both in revenue and expenditure fronts, the fiscal deficits still remained above the five percent of GDP. This may be partly due to ascendant impact of development expenditure which was dominated by a few but popular and even costly entitlements like social services, rural infrastructure, and power generation, generally tied with demographic and economic factors. In order to finance these entitlements revenue policy has been skewed, making it more difficult to meet resource gap through increased taxes.

4. Increasing burden of debt servicing charges

There has been an increasing trend towards loans rather than grants in the composition of the foreign aid in Nepal. This has imposed the growing burden of debt servicing charges and interest payment. 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 bring instability in the economy but will also slow down the pace of development and will thus produce 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 the regular budget and the development budget are normally prepared different procedures. The MOF prepares regular budget on the basis of past experience and historical accounting whereas NPC prepares the development budget targeting to fulfill the development need of the nation. In such cases, difficulties are frequently encountered in meeting macro objectives where the two budgets 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 in 2002. 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. Over reliance on foreign aid has been creating the situation of loss in self-dignity.

7. Lack of monitoring mechanism

There is a lack of monitoring mechanism during the budget execution. That's why there is a widespread leakage of resources and tardy pace of project implementation. There is also lack of co-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 coordination between necessary budget required and budget allocation for the many development projects. Because of lacking such a planning, many development programs are in under-finished conditions 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 any effective reward and punishment system. Therefore, there is an excessive leakage of the government resources and weak performance. No one takes the responsibility of the project failure. In this way, there is lack of public responsibility and accountability. In other words, there is an absence of good governance that is resulting in the weak fiscal management of the government.

5.3 Recommendations

Nepal is an underdeveloped country and its economic situation is not improving in a satisfactory manner. It is facing economic as well as social problems for its development. Nepal has been experiencing problems of inefficient and under utilization of available resources. Actually the external capital inflow has not strengthened the national economy. In the contest of developing country like Nepal resources gap are generally widening due to limited internal resources mobilization and their potentiality. On the other hand, the government needs to bear the responsibility of creating employment opportunities, need to support the people living below the absolute poverty line and other social obligations along with developmental responsibilities. In Nepal, government has still a greater role to play in development activities even after the adoption of liberalized economic policy especially with respect to developing infrastructures conducive to development and providing facilities to the people under social safety net. So, the following recommendations are made to improve the economy.

Following points should be considered seriously for proper budgetary management of the government in the future.

1. The multi target aspects of the use of customs duties highlight their historical importance which may decline along with the recent developments in regional and international trade organizations like SAPTA, WTO and trade liberalization. Thus, there is an urgent need to reform the domestic taxes even for maintaining the current tax-GDP ratio, while to raise it over time is another issue.
2. For adequate mobilization of domestic resources, the revenue share of non-tax sources should be increased by reforming administration and management of public corporations with the principle of revenue productivity.
3. Proper co-ordination between National Planning Commission and Ministry of Finance should be maintained and budget should be prepared depending upon economic prosperity. Expenditure on unproductive sector should be reduced and transparency in earning and spending should be enhanced. In order to discourage corruption and irregularities, property earned through unfair means should be nationalize.
4. In the context of low domestic resource mobilization in Nepal, the share of foreign loan, though essential for financing development expenditure should be reduced to lower the burden of external debt.
5. Formulation and execution of budget should be guided economically, but not politically. The governance by rule should take place not by ruler.
6. Development projects should be screened based on cost-benefit analysis and enough resources should be allocated to finish such projects on time.
7. To control the development budget and minimize the waste of resources associated with over-programming.
8. To improve the effectiveness of public spending, it is necessary to promote greater local ownership of the public expenditure program. This will require action both from the government and external donors. For example, the government will need to take the lead in designing, financing and implementing the development program. It will need to decide what its own development priorities and programs are, and ask the donors to support such

programs. Where donor aid does not fit its priorities and program objectives, the government will need to reject such 'donor-driven' aid.

9. Government should confine the activities only to social services and infrastructure sector and encourage the development of private sector by providing conducive environment.
10. Government should introduce the multiyear planning approach for the effective execution of the development projects.
11. Rewards and punishment system should be made effective as such public accountability and responsibility will increase, consequently, it will help the effective implementation of development programs as well as the government policies. This will also reduce the rampant misuse of public resources.

BIBLIOGRAPHY

- ADB (2000), *Country Economic Review*.
- Beyer, John (1997), *Resource Mobilization Sponsored by Government of Nepal*, Kathmandu; CEDA.
- Budget Speech of Fiscal Years 1996/97 to 2008/09, *Ministry of Finance*, Government of Nepal.
- CBS (2007), *Statistical Year Book of Nepal*, Kathmandu.
- Dahal, M.K.(2005), *Formulation aspects of Budget: Nepalese Context*, CEDECON, TU, Kritipur, Kathmandu(class note).
- Goode, R. (1986), *Government Finance in Developing Countries*, Tata Mc Graw-Hill Publishing Company Ltd, New Delhi, India.
- Gupta, B.N.(1967), *Government Budgeting: with Special Reference to India*, Asia Publishing House, Bombay, India.
- IMF(1991), *Nepal : Report on Observance of Standards and Codes- Fiscal Transparency Module*, Washington, D.C.
- Kharel, Ram Saran (1996), *Deficit Financing in Nepal*, An Unpublished MA Thesis, TU, Kathmandu.
- Khanal, Dilli Raj (1988), *Public Expenditure in Nepal: Growth pattern and impact*,New Delhi: Sterling Publishers Private Limited.
- Malla, T.B. (1993), *A Study on Planning and Development Budget in Nepal*, An Unpublished MBA Thesis, TU, Kathmandu.
- Nepal Rasra Bank (2008), *A Hand Book of Government Finance Statistics*.
- Neupane, G. (1999), *Budgetary pattern of Nepal*, An Unpublished MA Thesis, TU, Kathmandu.

- Pant, Y.P.(1970), *Problems in Fiscal and Monetary Policy*, A Case Study of Nepal, Sahayogi Prakasan, Kathmandu.
- Pahtak, Rita (1999), *A Study on Deficit Financing in Nepal*, An Unpublished MA Thesis, TU, Kathmandu.
- Paudel, K.N.(2002), *A Study on Budgetary Pattern of Nepal*, An Unpublished MA Thesis, TU, Kathmandu.
- Ranjitkar,Azeliya (1987), *Budget innovation in Nepal*, Submitted to T.U Kathmandu, Nepal.
- Sharma, N.K. (1988), *A Study of the Budgetary Structure of Nepal*, An Unpublished MA Thesis, TU, Kathmandu.
- Singh, S.K, (2008), *Public Finance in Theory and Practice*, Government Budgeting, New Delhi, India
- Singh, S.R. (1977), *The Fiscal System of Nepal*, Ratna Pustak Bhandar, Kathmandu.
- Thapa, N. (1996), *Deficit Financing in Nepal*, An Unpublished MA Thesis in Economics, TU, Kathmandu.
- Upreti,Bhisma Prasad(2000), *some Aspects of public Expenditure in Nepal (1981-1998)*,London: An unpublished dissertation submitted to University of Southampton
- World Bank (2000), *Nepal Public Expenditure Review* (in Five Volumes), Kathmandu.

Selected Websites

<http://www.npc.gov.np>

<http://www.mof.gov.np>