

CHAPTER-I

INTRODUCTION

1.1 Background of the Study

In the mid-1940s, a new word “Aid” came into common use especially in the literature of economic development to describe the flows of resources from one country to another country. The name given to the developed countries was donors and the name given to the developing countries was recipients.

In the development process of Nepal foreign aid has been playing a key role. Development expenditure is almost dependent upon foreign aid. From the current days study it can be said that Nepal might be in need of foreign aid more than its development expenditure, foreign grant took an important place at the beginning of the development process. Firstly, there was a negligible tendency of utilizing foreign loans than foreign grants and secondly, budget size was so small and small sum of foreign grant made a significant presence in the total budget.

In the whole of foreign aid, presence of foreign grant has significantly big. However, after the decade of 80s situation has become reversed. The proportion of foreign loans has been becoming big and big in foreign aid. Foreign loan has become key source of financing development budget. The proportion of foreign grant has been increasing marginally though government is applying various strategy and policies, which is largely insufficient to meet the public expenditures. Scenario of the need of foreign aid is being created day by day. Therefore, the country is heavily dependent and relied upon foreign aid. Nepal is in letting foreign aid in the form of loan grant from the both bilateral and multilateral sources. Nepal is receiving and taking the foreign aid.

In the developing countries like Nepal, domestic resources are inadequate to meet the financial requirements development. The present level of capital formation of these countries is too low and any substantial increase in saving is not possible due to extremely low level of income and wide spread poverty. Taxation and public borrowing have got their own limitations. Deficit financing is also discarded because of its inflationary impact on the economy. At this juncture; the only alternative to pull the economy out of vicious circle of poverty remains the foreign aid. Thus, foreign aid is advantageous for the acceleration of growth mechanism in these underdeveloped countries. In fact, it is a supplement to poor domestic savings of less and backward economics. From the economic history of various countries, it may be seen that almost every advanced country of the modern world had to rely on foreign aid for speeding up the pace of economic development. Prof. W. A. Lewis has pointed out; “Nearly every developed state has had these assistance of foreign finance to supplement its own meager savings during the early stage if its development”. England borrowed from Holland in the 17th and 18th centuries and in turn came to lend to almost every other country in the world in the 19th and 20th centuries. The United States of America, now the richest country in the world, borrowed heavily in the 19th century and is in turn called upon to become the major lender of the twentieth century (Lewis, 1973).

In Nepal, the formal assistance program commenced with the “point four program” of the United States, signed on 23rd January 1951. After US, India took an interest in providing assistance; through there were only two major countries during 1950’s and early 1960’s. In later years, Nepal received considerable amount of aid from USSR, China, France, Canada and Germany etc. for various projects. After late 1970’s Nepal had been receiving foreign aid mostly from Nepal aid group (Australia, Belgium, Canada, Denmark, Finland, France, Germany, Japan, Saudi Arab, Sweden, Switzerland, UK, USA and eight multilateral donors ADB, IFAD, OECD, SFD, UNDP, IDA, FEC and UNCIAD). Besides, Nepal has been receiving foreign aid from other bilateral

donors as well as multilateral agencies like-WB, IMF, WHO, OPEC fund, UNICEF, DAC, IBRD etc.

On the other hand, Japan is one of the developed countries in the world. Therefore Japan is placing almost importance on the support to self-help efforts of developing countries. It provides official development assistance to help ensure the efficient and fair distribution of resources and 'good governance' in developing countries through developing a wide range of human resources and socio economic infrastructure, and through meeting the basic human needs, there by promoting the sound economic development of the recipient Japanese assistance in the financial as well as technical terms. Japan aid comes for the construction of many projects for the development purposes and to enhance the relationship between Nepal and Japan.

1.2 Importance of the Study

In the light of economic development foreign aid depends on many factors such as ability of resources, domestic and foreign resources. The focus in development, namely this study will be solely on one of these factors contributing to the economic the availability of resources, it has been proved beyond doubt that the higher the availability of resources, the higher will be the rate of economic development. The evidence can be obtained from ASEAN countries where economic development became possible through availability of resources. In most under developed countries home resources (internal) are not augments the capital formation and naturally and reasonable economic growth is possible only if domestic saving is supplemental by foreign aid and investment.

Nepal likes other developing countries in the world and rich in natural resources but they are poor in skill, capital and good managements. Least developing countries like Nepal do not process a strong and stable economy. They are unable it have economic growth because of low saving ratio, stagnant

export earnings and lack of technical knowledge. So the main aim of providing assistance to these countries is using resources properly and to take speed of economic growth for the economic development.

The Japanese aid has started since 1956 and regularly coming to Nepal in large and increasing amount only since 1970. Japan is one of the most donor countries in the world to provide assistance for developing countries like Nepal for uplift of economic status. So Nepal is receiving huge amount of Japanese assistance to develop various fields of economy for economic development. With the help of present study, it aims to analyse the trend and volume of aid being provided by Japan for economic development of Nepal in various sectors.

1.3 Statement of the Problem

The gap between the rich and poor has become inevitably the most tragic and urgent problem of modern world. Domestic source of capital is not enough to break the vicious circle of poverty in the current days situation, foreign aid has inspired the nation left source to gap. So foreign aid has been taken as a means of reducing the gap.

Less developed countries like Nepal have many problems. These groups of countries have low level of living standard, low level of productivity, high rates of population growth, high and rising level of unemployment, dependency on agriculture, low ability to pay tax, considerable revenue and Expenditure gap of the public sector, and so on. It is argued that these countries need foreign assistance to overcome these problems. Furthermore, in order to improve the human development status and create basic economic infrastructures, there is the need of large amount of public spending, which cannot be financed by the current level of domestic saving. This in turn demands foreign assistance for the economic development of developing countries like Nepal.

Nepal has been receiving large amount of foreign aid in south Asian region and has been striving to accelerate economic growth through planned development process since 1956. But even after the completion of nine periodic development plans, government efforts to attain high economic growth rate with higher level of public spending have not brought desirable results. Economic growth is not associated only with an increase in capital per head but also associated with values and initiations that give incentives to effort, economic efficiency and the technical know how. Thus, in the absence of all those institutions, an underdeveloped country has low general absorptive capacity with regard to aid. At the same time, formulation and evaluation of projects and programs are directly related to the majority of the people, the success of such programs will depend upon the co-operation of the people. But, if the project is of highly sophisticated type in implementation, requires considerable expertise and absence of which minimizes the success. Problem arising while employing foreign aid is uncertainty of magnitude and character of foreign aid over the period of time. Elements of uncertainty have adverse effects. Another fact is that foreign aid is motivated by some political motives which will lead to deep suspicions and prejudices against nationalism and sovereignty of developing nation which is more sensitive.

The extra money injected in the monetary system of country by foreign assistance builds up social and economic overheads, which may bring inflation. Though mild inflation is a normal feature of developing countries but beyond the limit, it has adverse effect. It is said that if foreign aid does not involve any substantial sacrifice for the people, it is utilized in an unproductive way. Everybody should have a sense of responsibility to allocate funds in productive channels. In case of aid repayment, if it is a debt, which is wasted, it would increase extra burden for the people while repayment is made on it. So, aid receiving countries should in advance work out detail planning and designing of individual project so that it may be easier for donor governments to judge the worthiness of the projects in order to channel the aid resources. It should be

linked with development process rather than with individual project. Aid receiving countries should try to get longer period commitments from donor countries to avoid uncertainty in advance. Underdeveloped country should try abstaining from assistance from foreign government and international agencies and also create conditions that could attract foreign private investments.

Foreign aid has not been discussed and analyzed seriously so far Very few studies and research works have been conducted with respect to foreign aid. Japan is one of the major aid giving countries to Nepal but there is lack of studies on Japanese aid to Nepal. So a study on Japanese aid to Nepal would throw valuable lights.

1.4 Objectives of the Study

The general objective of this study is to analyze the impact of Japanese aid in the economic development of Nepal. However, the specified objectives are as follows:

1. To review the history and examine the trend and structure of foreign aid to Nepal.
2. To examine the trend and structure of Japanese aid to Nepal.
3. To analyze the impact of Japanese aid in the economic development of Nepal.
4. To suggest measures for further flow and effective use of Japanese to Nepal.

1.5 Limitations of the Study

This study covers the period from FY 1991/92 to FY 2005/06 and it is based on secondary data. Although the impact of foreign aid on the economic development of developing countries covers a wide range, this study is limited to the trend and structure of the foreign aid provided by Japan. This study excludes the political and social effects, which are difficult to measure

quantitatively. This study also excludes the military and private assistance. Only official development assistance is considered.

1.6 Organization of the Study

The study is divided into seven chapters.

The first chapter introduction has contained background of the study, importance of the study, statement of the problems, objectives of the study, and limitations of the study.

The second chapter of the study is about literature review.

The third chapter research methodology has contained introduction, source of data, research design, data processing and analysis, statistical tools for analysis, hypothesis, statistical test of significance and descriptions of variables.

The fourth chapter has foreign aid in Nepal has contained historical background, magnitude and trend of foreign aid, sources of foreign aid, foreign aid disbursement by sectors, foreign aid commitment and disbursement, resource gap and need of foreign aid and burden of foreign aid.

The fifth chapter of the study is about Japanese aid to Nepal. It includes historical background of Nepal-Japan relation, review of Nepal-Japan relation, Japanese aid, Loan assistance, grant assistance, organization and agencies for cooperation, Japanese aid distribution by sector, scholarship program and general introduction to Japan's ODA to Nepal.

The sixth chapter of the study is about impact of Japanese and in Nepal. It includes empirical analysis, micro-performance and macro performance.

The seventh chapter is last chapter of the study. This chapter includes the findings, conclusion and recommendations.

CHAPTER-II

REVIEW OF LITERATURE

The concept of foreign aid is certainly not a recent phenomenon. It has been coming from primitive period of classical economists. But it is generally agreed that foreign aid is originated from the disruption of the world economy that followed World War II.

Foreign aid in the present context refers to the flow of capital and technical resources either direct from the government of a donor country or through international channels in the form of loan or grant on occasional scale. In recent time, foreign aid is taken as a major instrument of development for developing countries. Because, in the process of economic development a country may be faced with the situation where its domestic savings are short of investment requirements and where its imports needs are larger than its export capacity for the purpose of attaining a targeted rate of economic development. By the help of foreign aid it can fulfill its desire of development filling the gap between saving and investment. So, foreign aid plays supplementary role to solve the foreign exchange, saving gap and technology gap problem, which are hindrances for such countries at the initial stage of economic development.

In the context of foreign aid in Nepal, several books, booklets, journals and articles has written by Nepalese as well as foreign writers. Similarly, the students of economics have submitted dissertations referring to foreign aid for the fulfillment of their master's degree and several articles in the local newspapers are published referring to this field.

United Nations (1960), an "The least development countries report defined foreign assistance as" all transaction (for a country or an international organization), which result in a permanent net addition to total resources available for economic development of another country." According to the United Nations, aid consists only of outright grants and net loan term by

leading international organization. Now a days giving foreign aid either in the term of grant or loans has been considered as the responsibility of the international community.

Outlying the objectives of foreign aid in international aid for underdeveloped countries, “Rosenstein Rodan (1961), one of the development economists as well as a very famous writer of economics, speaks about the external supply of capital. He states the purpose of an international programmed of aid is to accelerate economic development of countries up to a point where a satisfactory rate of growth can be achieved on self-sustaining basis. He also includes technical assistance as part of aid, although it is not a normal capital inflow, because it is a form of transfer of skills, which can result in economic growth. According to him, foreign aid assumes much importance as means to break the vicious circle of poverty and to accelerate the growth rate.’”

He argued that foreign capital inflows and foreign aid are not synonymous concepts. “Aid properly speaking refers only to those parts of capital inflows which normal market forces do not provide.” in the contest of aid impact, Rosenstein Rodan opined that, aid has a positive role for development in the recipient countries.

Rosenstein Rodan also asserted that a reasonable amount of aid is determined by the absorptive capacity of the developing countries economy. He pointed out that aid should be for generating capacity or efforts aid ideally aid was therefore to be allocated where it would have the maximum catalytic effect in mobilizing additional national resources. He listed out the major achievements of aid, which are; increase in life expectancy, the fall infant mortality; the rate of growth, development of socio-economic overheads etc.

Hollis Chenery has defined foreign aid as an instrument of bringing various gaps and relieving various bottlenecks existing in an underdevelopment economy. Chenery, with Bruno (1962), MacEwan (1966) and Strout (1966) has formalized this argument in a “two gap” model. Foreign aid is expected to fill the two gaps, i.e. saving-investment gap and the foreign exchange gap. Centralized planning and a fixed exchange rate regime seem to be the implicit assumptions behind this concept. For this model, the authors presumes on omnipotent inter-temporal decision-maker and assumes away any complications that fluctuations in export and import prices (which might affects saving and investment in a country) could bring about as a result of floating exchange rate for the domestic currency.

The “Two gap” model is actually quite simplistic and very intuitive. The model starts with the familiar equation for national accounts. Using the national income accounting identities, uses of national income is equal to disposable of national income. Using the symbols, this can be expressed as

$$C + I + G + X - M = C + S + T \quad \text{----- (1)}$$

Where,

C = Household consumption

S = Private saving

I = Business investment

T = Taxation

G = Government expenditures

X = Export of goods and net factor services

M = Imports of goods and services and net factor income.

Canceling the ‘C’ term from both sides and rearranging the other terms of equation (1), we obtained the relation as

$$(I+ G) - (S+T) = (M-X) \text{ ----- (2)}$$

Equation (2) is fundamental relationship reflecting a development economy's domestic resource gap and its foreign exchange gap. As long as a developing country like Nepal is spending more on I and G than it's earning from domestic resources released through private S and T, there will be a domestic resource gap that will translate into the balance of payments with M greater than X. The inflow of foreign aid is assumed to help on filling the domestic resource gap ($I + G > S + T$) and foreign exchange gap ($M > X$). By providing additional domestic resources, foreign aid is also supposed to facilitate and help to accelerate the development process, thereby eliminating the long-term need to further aid transfers.

He showed the impacts of the minor aid programmes provided by different donor countries. According to him, in minor aid programmes, few of them are successful to fulfill their indicated aim, but in aggregate, they created serious problem of Nepal. In addition, he has shown the impact of two types of foreign aid in Nepal, short term and long-term impacts. In short term impact aid project did not improve political consciousness as hoped by donors. In long-term impact aid not only failed to give a significant boost of Nepal's economy but also, it may even have made growth more difficult to achieve.

Benjamin Higgins (1969), emphasize the importance of foreign aid by saying that "it is highly unlikely that measures to increase voluntary domestic savings alone or even measure for voluntary and compulsory savings together can provide all the financial sources needed for developing or underdeveloped countries." Foreign aid is primarily used in the construction of social overhead capital requirements of LDCs are concerned, it is not so work in LDCs is equated with public utilities and more often with basic necessities. Foreign aid has been a must for them without which development process it will be obstructed.

E.K. Hawkins (1970), states that, "Foreign aid is only a recent phenomenon originating in the international scene after scene word war. Foreign aid will remain a permanent part of international economy and it will continue to be further development and thinking which will themselves and influence the amount and character of foreign aid".

He states that "it is foreign because it originates outside the national boundaries of the recipient country, it is aid because such aid flow are not determined by the same principal that governs normal flow of trade and capital."

G.M. Meier (1970), in his book "leading issues on economic development." writes that capital accumulation is regarded as core process by which all other aspect of growth are possible. Capital increases investment. Investment need s more saving or foreign assistance. In his view, foreign aid might have some limited use; aid should be given to those who help themselves. In short run calculation on aid, requirements through the industrial assumptions needs to be looked at very carefully over the long run, it is not of much use indeed it may be positively harmful.

Meier also writes, "Public financial aid i.e. confessional finance, or the grant equivalent in the capital flow has two fold functions. It supplements the LDCs low domestic savings and hence helps till the resources gap or saving gap is filled, and also provides additional foreign exchange and thereby helps fill the foreign exchange gap."

Another early explication of foreign aid is provided by Hollis chancery, who defines foreign aid as an instrument of bringing various gaps and relieving various bottlenecks existing in an underdeveloped country.

In the report of United Nations (1972), it is said, “In the case of the poor developing countries a successful attack on mass poverty and unemployment can hardly be launched and maintained on an adequate scales without more financial aid form abroad. This applies especially to the poorest countries where very low income and hence in many cases, the inadequacy of their financial resources, will otherwise result in budgetary deficit, which will in turn improve on the balance of payment.” Another UN Report said, “In underdeveloped countries where income per capita is lowest, current domestic savings, even if effectively mobilized and directed to productive investment, is not enough to produce a satisfactory rate of economic development. The addition of outside financial resource may be a necessary and, in some instances a substantial feature of such development, particularly, in order to accelerate development; the additional of foreign capital can be most benefit when the combined utilization of domestic and external financial resources result in a high rte of investment.”

In the words of Friedman, “If other conditions for economic development are ripe, capital will be readily available, if they are not capital made available is likely to be wasted. “Foreign aid may serve to delay the inevitable, and to provide the government with the false façade with which it can postpone taking necessary measure like securing properly rights, and maintaining a good environment for the private sector.

Y.P. pant (1974), in his book, “problems of development of smaller countries; a case study in problem and prospects of development process” writes that the external assistance available to the least development and smaller countries can be discussed under the headings of foreign of foreign aid in the form of grants, loan and technical assistance. According to him, capital shortage will be supported by foreign aid at least in the initial stage of development plans. He adds rapid capital formation for accelerating the growth of development plans. He adds rapid capital formation for accelerating the

growth of LDSs cannot be possible without foreign aid, even if domestic resources are mobilizes efficiency.

Mr. Pant claims where stage of development, greater the percentage of foreign loans and grants should be necessary the efforts of advanced countries and international agencies to knowledge and skills to developing countries through technical assistance have been increasing in recent years.

B. Dhungana (1981), puts forward the view that there is not even on sector, which is free form foreign assistance. In the impact of foreign assistance, he says that, because of small resource flow, foreign aid has only marginal effect in recipient countries. He further adds that net foreign investment out of the gross foreign assistance come only about 25 percent.

Many writers have realized the significance of external assistance to Nepal. Highlighting its role, S.R. Paudyal (1982), has said that foreign aid appears to have played a laudable role in as much as it inspired successive government in Nepal to demonstrate their living standard has a product of dangerous stimuli, everything else from the objective of the development to the strategy policies and projects were destined to be influenced by foreign aid. He claimed that foreign aid besets the country. The increase dependency on aid without the expansion in the production base, the country must be destroyed. To avert such harmful situation of Nepal, attention should be centered on the following three issues.

Firstly, he suggest, we should try to reduce dependence on foreign aid strengthen the internal capacity of generating resource. Secondly, the country should try to shift the concentration of foreign aid form transportation infrastructure to industrial and agriculture sector. Thirdly, the utilization of foreign aid should be strengthened. He says the corrupt and inefficient administration retards the growth process of economic development.

He further writes in his another book, “Trend of foreign aid in Nepal”, (1991), had the assistance been productively used, they would have generated the funds of repayment. But if they have not been productivity used, the debt servicing is become increasingly burdensome to the country. Thus the way in which foreign aid has been used and makes it look as if it is going to become a self-perpetuation process.

In the paper “Economic implication of foreign aid,” Harka Gurung (1986) writes, foreign assistance to developing countries is related less with economic consideration but more with strategic and political implication. Economic development continues to be externally oriented and most of foreign agencies have had to rely on its own infrastructure before planning into aid programmers. The poor domestic saving rate and resources to finance the development expenditure required the external assistance. Thus is excess reliance in meeting government expenditure.

Mr. Dharmdasani in his book, Dynamics of foreign aid in South Asia (1990), Nepal has been taken as a main component in his study regarding to foreign aid. In which, at attempt has been made to analyze the nature, dimensions and implications of Nepal’s dependence on foreign aid to sustain her development process. The central theme of study is that with in the study is that with in the prevailing structure constraints of Nepal society, the process of development has itself contributed to the growth of external assistance.

The study has analyzed the data relating to foreign aid. In this context the Study examined the role of foreign aid in the process of plan development up to six Plans. Dharmadasani has also examined the inflow of aid form aids in Nepal. On his study about donors of Nepal he says only a few countries among the bilateral donors in Nepal have contributed in a manner that can lead to self sustain growth.

In his conclusion, he pointed out that Nepal will have to be self - reliant and it has to find its own development ideas not to remain at the perpetual mercy of the political and economic compulsion of the aid donors. He emphasized that instead of visualizing the future without aid. Nepal should cease to be dependent on aid as the prime mover of the economy.

B.R. Shrestha's book (1990), "Managing External Assistance in Nepal" he has made attempt to portray an insider's view regarding foreign aid in Nepal. It is worth wide exercise done with objectively free form bureaucratic institution. He starts with a brief overview on the genesis of aid transaction and perceptions of donors 'agencies. He than traced the trends of acid flow in Nepal that evidenced sizeable increase in quantum and sources as well as a major shiftment form the grant to the loan component. Besides that he has attempted to review the performance of foreign aid in Nepal based on various sources along with the problems, constraints and future perspectives in the changing context of the world economy.

He highlighted the following facts in his books, although there has been a continuous rise in total foreign aid since 1956, the grants assistance as a percentage of development expenditure has fallen but bilateral loan is steadily increase, secondly due to increasing loans component, debt servicing ratio has also increased gradually, finally Nepal has a low absorptive capacity of foreign aid due to several causes such as staffing problem, centralized decision making problem, financial management problem, problem of local contractors and other miscellaneous problem. So far that HMG will first have to demonstrate a huge level of absorptive capital. For this period project managers should be made accountable for every thing regarding projects.

Finally in his book writer put some recommendation regarding foreign aid, first government should request to the donors to finance agro based industries that could reduce cost of production, secondly, emphasized on the road project could help to generate income and employment thirdly, HMG

should request such donors to accommodate the local people in training and learning process so as to maintain and operate the projects satisfactorily after handover.

Narayan Khadka (1991), in his book, "Foreign aid poverty and stagnation of Nepal" has written that Nepal is a country, heavily dependent on aid whose dependence on aid increased from 45 percent development expenditure up 1975 to about 56 percent in 1986 and whose aid import dependence increased from 21 percent aid GDP ratio increased from 2.6 to 6.9 during the same period. It is obvious that aid become all pervasive in the economy. Added to this dependency, is the time factoring i.e. the condition in dependence, this means that development projects and programs implemented in the country. Hence, measuring the impact of aid on development in both complex and difficult.

Aid has been effective in alleviating poverty in Nepal. On the country, aid has created socio-economic dualism by favoring urban biased and growth maximization development priorities; it caused dualisms between urban and rural areas in terms of consumption. But neither aid contributed to attain a goal of maximization of the GNP nor helped establish institutional political machineries through which the distribution of benefits would trickle down, hence aid failed to alleviate poverty and over development of the country because it failed to grasp the majority population who live in the rural areas.

S. R. Poudyal (1992), has made an effective study on different aspects of foreign aid in this article "Trends in foreign aid in Nepal". He has analyzed the trend, composition, sources, sectoral distribution, aid utilization, tying of aid that received by Nepal as assistance during 15 years. The main issues that he raised in his articles firstly, Nepal's dependence on foreign aid is increasing the influence of foreign aid is pervasive in Nepal's development, secondly, composition of aid indicates a shift from debt servicing liabilities, a crisis of foreign debt has been emerging, thirdly. The sources of aid have changed

clearly from bilateral to multilateral. Bilateral assistance is also gradually shifted towards loans, fourthly, there is a large gap between commitment and disbursement of aid, finally, tying of aid with projects gradually push up cost.

Along with these issues, he pronounced distorted condition of aid on the Nepalese economic. According to him, aid has substituted domestic saving, aid resource have not utilized effectively, aid is very much urban biased; aid it is serving the politicians, bureaucrats, commission agents and contractor.

Kishor K. Gurugharana's article "Development co- operation: an appraisal of the activities of agencies in Nepal" in NEFAS's book foreign aid...(1992), has highlighted an overview of foreign assistance in Nepal with plan wise, foreign aid as percentage of development expenditure and international comparison of per capita aid, besides these, he has briefly gone through review of major bilateral donor's assistance, multilateral assistance and its overall positive and negative impacts in Nepalese economic.

According to him, Nepal is receiving substantial amount of aid since the collapse of Rana regime in 1951, many bilateral and multilateral donors are keenly taken interest for investing in Nepal. There are some factors such as geopolitical, socio- economic as well as non – aligned and friendly relation with all countries caused substantial aid inflow of Nepal. Some donors are provided aid purely on humanitarian basis, while others assisting us just to fulfill their vested motives while taken into consideration of the multilateral aid, they are provided loans aid in concessional term for the infrastructures development of Nepal in various fields.

He has also stated some of the positive and negative impact on aid in Nepalese economy it will be factually wrong to claim that external assistance has not brought any significant improvement, whatever improvement have occurred in the economy are mainly due to the cordial support of external donors. Some notable gains have been made in the development of socio-economic

infrastructures such as education, health, human resources development, transport, communication and irrigation and power. Its negative impact in Nepalese economy also cannot seriously paralyze us; we are now ultimately in the aid trapped. Instead of these, Nepal has not yet received the quantum of aid comparable to those of Korea, Taiwan and Europe; it is like giving a medicine for below the prescribed dose. The effect not only prolongs diseases, but also eventually increases its severity.

Mohan Man Sainju (1996), in his book, foreign aid shifting statistical evidence, says “While thinking about ways to increase the utilization rate of foreign aid in Nepal, policy makers should realize that merely making arrangements to bring more money to the country may not be sufficient. Rather than encouraging self-sustaining growth through an initial infusion of foreign aid, the growth through an initial infusion of foreign aid, the growth of debts may force a country to suppress consumption and investment in the long run and to run trade surpluses to fulfill all debt obligations ways in which such actions may reduce the welfare of the citizen in the long run.”

He further stated, in the case of Nepalese government, the multitude of agencies handling foreign aid negotiations might be yet another reason the ratio of utilization has been slow. There is no central agency that prioritizes the projects according to their merits and strengthens the position of the country in the negotiation process. The lack of coordination may be that the ratio of utilization is being lowered.

Bam Dev Sigdel (1997), in his book ‘Japanese economy and economic diplomacy’ has highlighted that Japanese assistance to Nepal has been mainly directed to agriculture power generation and distribution, health, transportation, education, communication, development of human resources, environment preservation and so forth.

Japan's assistance program has been highly concentrated in agriculture i.e. nearly 40% of the total aid. However its improvement is considerably very low in comparison to national output. The potential for the expansion of further cooperation between Nepal and Japan is very great. Nepal is very facing serious backwardness in each and every sector of the economic and society. To alleviate poverty, to meet basic needs and to upgrade standard of living is not an easy task for Nepal. To meet such goals, there is urgent need to invest heavily in social service sector, agriculture sector, industrial sector as well as infrastructure of Nepal in coming days; in such a situation one cannot ignore the role of Japanese aid to Nepal in coming days.

Keshav P. Acharya (1998), in his report, "A review of foreign aid in Nepal" says that although foreign aid did not substantially contribute to the economic development of Nepal, the importance of foreign aid cannot be denied, because the domestic resources mobilization of Nepal is still very low to fulfill investment requirement. In this respect new ways of aid utilization have to be through from both donors and recipients have to use these aids in the related or concerned sectors optimally not considering aid as a free gift.

He further stressed on the effective utilization of foreign aid artery making list of priority of the urgent needs; of the recipient countries and most urgent projects will bar to be selected with full of enthusiasm for implementing effectively so that it can generate s sufficient resources to back the aid. Corruption is burning problem, which is gradually destroying our economy. So level by introducing anti-virus programs transparency and dedication should be maintained in the economic to deal with these viruses.

He study while discussing various factors affecting the utilization rate of foreign aid in Nepal, also discuss composition of aid (in the form of loan or grants), source of aid lateral and bilateral, pro portion of aid tying , government inefficiencies using time series data, the study, then proceeds to examine contribution made by foreign aid indifferent facets of economic development in

the country looking at its association with national output and aid are positively associated as well it present how foreign aid may affect national savings relatively by using views some radical economists.

Finally, this book presents how the committed aid can be disbursed by means of effective absorptive capability. Absorptive capacity determined by its institution and its capital, human or otherwise aid disbursement beyond this limit is bound to have an effective impact.

Minendra P. Rijal (2001), in his article "Foreign aid in Nepal" writes that Nepal's economy is characterized by various structural constraints leading to low per capita income. Its revenue growth is sluggish and has low rate of public and private savings. Investment GDP ratio has been declining for last few years and the large industrial enterprises has been stagnant. Mobilizing adequate domestic resources to carry out infrastructure and social development programs thus remains a major challenge for Nepal while national efforts to mobilize savings and to create a favorable climate attracting investment are important, the role of ODA will remain vital in the near future.

Gopal Sibakoti (2002), in the paper "Impact of Japanese aid in Nepalese economy", analyze that when citizens and groups make requests or judicial complaints for the accessibility of documents of research and study, they are either simply ignored claiming that these do not exist or give the narrow arguing about who should give the permission first. The game of denial goes on and on for months without any result.

It is equally impossible to meet the responsible Japanese ODA officials in their offices in Katmandu or the meetings end just in brief conversations, which are very formal, hierarchical and diplomatic. All these exercise end up in a nice afternoon or tea, some glossy brochures or a few pages of reports highlighting the history of great cooperative or achievements.

There is also a general experience and reaction to Japanese ODA in sense that the Japanese officials have been clever in promoting their business. There is a saying that no equipment or machine could be repaired or fixed without calling a Japanese consultant or export all the way from Japan or in Katmandu if there is any, implying that even fixing some nuts and bolts to replace some simple machinery arts require the services of Japanese consultants. The Kulekhani hydropower project and the Udaypur cement factory have some very interesting stories like this. One example of such conditionally can be cited form the project for the expansion and reinforcement of power transmission and distribution system in Kathamandu valley.

The booklet entitle, Nepal Japan economic and technical co- operation exhibition published by Nepal Japan students and trains club, embassy of Japans, JICA and JOCV offices in Katmandu give the picture of Japanese aid in Nepal form initial till now, which is provided by Japan.

Overall, having found out that foreign aid positively affects GDP, its importance to lift every sector of the economy in Nepal viz., infrastructure development, minimizing resource gap etc. but on the other side, the inefficiencies, misuses, cost of dependence syndrome aid has generated makes every concerned citizen about it existence in Nepal. There are the guiding factors that have prompted me to undertake this research.

CHAPTER-III

RESEARCH METHODOLOGY

3.1 Introduction

This study entitled “Japanese Aid to Nepal: Trend and Structure” is based on secondary data. This section discusses about the sources of data, data collection procedure data presentation, research design, and data analysis, mathematical as well as statistical tools used to analyses the data in accordance with the objectives of the study.

3.2 Sources of Data

This study based on secondary data obtained from various publications of National Planning Commission (NPC), Nepal Rasta Bank (NRB), Embassy of Japan, etc. To achieve the goals of the study, official and unofficial books magazines, newspapers, and journals have been studied. The required data are collected from various issues of economic survey budget speech, and various plans of Nepal.

3.3 Research Design

The research design of the study is descriptive. It is designed to describe the relation between the increasing volume of Japanese aid inflow and GDP growth in Nepal. It focuses on trend, magnitude; structure impact and role of Japanese aid in Nepal. The descriptive, quantitative and analytical research tools are used for the study.

3.4 Data Processing and Analysis

In the process of data analysis, the available required data from various sources are collected, classified and tabulated to fulfill the requirements of the study. Data are presented in percentage when required. Tables, diagrams, pie

charts etc. are used according to situation and requirement of the study. The aid has been calculated in different forms such as loans, grants and technical assistance, which have been compared with total aid inflow in Nepal.

To find out the correlation between Japanese aid inflow and GDP growth, some statistical calculations have been used mainly regression analysis, marginal productivity of aid and elasticity of Japanese aid has been determined.

3.5 Statistical Tools for Analysis

The study attempts to show the correlation between Japanese aid inflow and GDP growth in Nepal. To measure the aid results, two techniques are applied in the study, one is marginal productivity of aid and the other is elasticity.

a) Regression Analysis

Regression technique is used to establish the nature of relationship between a dependent variable and or more independent variables. It also provides a basis for prediction or forecasting. The regression of Y on F is used to estimate the relation between GDP and Japanese aid.

$$Y_t = a + b F_t$$

Where,

Y_t = gross domestic product (GDP) in time period t

F_t = Japanese aid in time period t

a and b = regression parameters

b) Distribution Lag Model

This model describes a casual relation in which a change in dependent variable can be explained by lagged values of the explanatory variables. The

general form of distributed lag model of Japanese aid and GDP can be expressed as:

$$Y_t = \alpha_0 + \alpha_1 F_t + \alpha_2 F_{t-1} + \alpha_3 F_{t-2}$$

Where,

Y_t = GDP at time period t

F_t, F_{t-1}, F_{t-2} = Japanese aid at different time periods

$\alpha_0, \alpha_1, \alpha_2, \alpha_3$ = regression parameters

The rationale behind these models in this study is to examine the impact of past values of the Japanese aid on the GDP at time period t in Nepalese economy.

c) **Double Log Linear Model**

Double log linear model depicts the relationship between dependent and independent variables in the logarithmic form.

$$\text{Log } Y_t = r_0 + r_1 \log F_t$$

Where,

Log = natural logarithm

Y_t = GDP at time period t

F_t = Japanese aid at time period t

r_1 = regression parameter shows elasticity of GDP with respect to Japanese aid.

3.6 Hypothesis

Null Hypothesis: H_0 : There is no significant relationship between Japanese aid to Nepal and GDP growth in Nepal.

Alternative Hypothesis: H_1 : There is significant relationship between Japanese aid to Nepal and GDP growth in Nepal.

3.7 Statistical Test of Significance

a) **Coefficient of Determination (R^2):**

After estimating the regression parameter, R^2 is used for judging the explanatory power, which measures the dispersion of observations around the regression line. It is essential because the closer the observation to the line, better the goodness of fit that is better explanation of the variation of Y by the change in the explanatory variables. R^2 shows the percentage of the total variation of dependent variable that can be explained by the independent variables of the multiple determinations and is the square of the correlation coefficient. The formula to derive R^2 is mentioned below.

$$R^2 = \frac{\hat{a}_1 \sum yx + \hat{a}_2 \sum yx_2 + \dots + \hat{a}_n \sum yx_n}{\sum y^2}$$

Where, $y = Y - \bar{Y}$, $x = X - \bar{X}$

b) **Test of Significance of the Parameter Estimates:**

It is applied for judging the statistical reliability of the estimates of the regression coefficients. The following tests will be performed to test the hypothesis in the study:

T-test: This test will be performed in order to identify the statistical significance of an observed sample regression coefficient and the formula for calculating the value is:

$$t = \frac{\hat{a}_i}{SE(\hat{a}_i)}$$

Where,

\hat{a}_i = estimate value of a_i

SE (a_i) = standard error of $a_i = \sqrt{Var(\hat{a}_i)}$

The calculated t-values will be compared with tabulated t-values at a certain level of significance, for a given degree of freedom. If the calculated t exceeds is significantly different from zero.

F-test: F-test is used to examine overall significance of the model. The formula for calculation is:

$$\frac{R^2}{K-1} \div \frac{1-R^2}{N-K}$$

Where,

R^2 = coefficient of determination

K = number of explanatory variables

N = number of observations in the sample

The calculation F-variance ratio is compared with the tabulated value at a specific level of significance with (K-1) degrees of freedom. If F_{cal} is less than F_{tab} , we accept null hypothesis and otherwise we reject null hypothesis.

3.8 Descriptions of Variables

The key terms have been defined in order to avoid misunderstanding regarding the macro-variables.

Foreign Aid: Refers to international transfer made at concessional term rather than at market rates for promoting economic development. The transfers include both grants and loans.

Foreign Loan: The provision of resources, excluding good or other bulk commodities, for relief or development purposes, including important procurement programs, which must be repaid according to conditions established at the time of the loan agreement or as subsequently agreed.

Foreign Grant: A grant is the same as the provision of funds by a donor that does not require reimbursement from the recipient government or organization.

Recipient: Country that receives aid.

Donor: It is the origin of fund for development assistance.

Disbursement: Disbursement represents the actual international transfer of financial resources. They may be recorded at one of the several stages provision of goods and services, placing of funds at the disposable recipient in the embarked fund or account, payment by the donor of invoices on behalf of the recipient, etc.

ODA (Official Development Assistance): ODA is defined as those flows to developing countries and multilateral institutions provision official agencies.

GDP (Gross Domestic Product): It refers to the market price of the total flow of goods and services produced by an economy over a specified period normally a year.

CHAPTER-IV

FOREIGN AID IN NEPAL

4.1 Historical Background

Foreign aid has been playing a crucial role toward fulfilling Nepal's development aspiration. Transfer of capital and technologies from developed 'Third world' countries either in the form of loans or grant from time to time is generally known as the 'foreign aid'. Foreign aid is generally considered as one of the important factors for development after Second World War. With growing independence of many developing countries and with the workout of the Marshall plan, the scope of foreign aid has become more significant. The term 'aid' has any different interpretations. At one extreme, it is narrowly interpreted to mean grants and long-term loans for the purpose of economic development of a country but on the other, it is defined as an inclusion of private investments and trade together with grants and loans.

On January 23, 1951, the United States became the first country to confer foreign assistance to Nepal valued at Rs.22, 000 through a point four agreement. India was the only country to follow suit almost immediately in October 1951. The socialist donors, namely china and the Soviet Union, joined the group in October 1965 and April 1959 respectively. The strategic location of Nepal between India and China and its non-aligned friendly relation with all countries, including the two super powers, helped increase the volume of aid from "torrent" after 1956. The role of strategic location evidence from fact that up to 1979/80, the US, India and China together provided more than three-fourth of the total bilateral grants.

When Nepal embarked on a development course in 1951 her economy possessed a drastic dearth of domestic savings, foreign exchange and trained manpower. Naturally the foreign aid was expected to fill the hiatus by

providing additional resources in the form of cash, equipment and trained personal.

Even the first year plan was introduced in Nepal mainly as a response to the requirement of the Colombo plan consultative group meeting which Nepal attended as a full fledged member of the first time in 1955. The increasing demand of the country and the growing ambition of the countrymen required increased assistance for economic development. The volume of aid flow in to the country played a meaning full role in the progress of various sector of Nepal. Nepal remained underdevelopment because it was poor because of lack of resources and technical know-how; foreign aid transmits not only money but also ideas, valued and technologies.

After 1956, the sources and volume of aid to Nepal rapidly increased because of its strategic location between India and China, non-aligned policy and friendly relation with all countries including the two super powers, the importance of strategic location is evidenced by the fact up to 1979/80, the US, India and China together provided more than three fourth of the total bilateral grants. Before 1951, the flow of aid to Nepal was negligible; almost were for the military purpose as we mentioned above became of the fact that the Rana Regime following a policy of isolation of conservation. After the democratic government in 1951, many bilateral along with multilateral agencies came into aid field. Besides these donors countries (India, USA, UK) and agencies ford foundation and SATA (Swiss Association for Technical Assistance) many countries like India, UK, Japan, Austria etc. begun to co-ordinate aid programs through the Colombo plan.

In order to canalized foreign aid in a co-ordinate and internationally agreeable manner Nepal aid group was formed in 1996 under the aegis of the World Bank to provide a forum for coordinating the increasing level and complexity of assistance. Since then, an over whelming portion of aid from aid

group members flowing toward our country. The need for forming Nepal aid group has arisen because of two main reasons:

- a) Growing aid requirement for Nepal, and
- b) Need for better co-ordination of aid – financed project / programmed.

The Nepal aid group has enlarged the number of its members to about two-dozen including half a dozen multilateral donors namely: IDA, WB, IMF, EEC, UNCTAD, ADB, and UNDP. At present the share of the aid group members in total aid commitment exceeds 90 percent if total Nepal's participation in Colombo plan in 1952 was another factor for increase in the bilateral aid from UK, INDIA, CANADA, AUSTRIA and JAPAN for several years.

After the restoration of multiparty democracy many international donors as well as Multilateral agencies are taken interest of providing aid in different sectors of the Nepalese country. So, the substantial amount of aid that has been provided up to now, the last meeting of Nepal aid group was held in Katmandu, that was concluded with pledge of aid utilization and performance results under poverty reduction program (PRP).

4.2 Magnitude and Trend of Foreign Aid

Nepal began to receive foreign aid since 1951, and the volume of aid inflow began to expand steadily after 1956. The main factors responsible for the remarkable increase in the aid receipt of Nepal seem to be mainly three causes: Firstly, Nepal expanding international relations increased and diversified the source of aid. Secondly, the introduction of development plan helped it to rationalize the demand for aid. Thirdly, the bonus effect of the cold war and feeling of the competition among some donors pushed up the level of aid. The increasing trend of foreign aid in Nepal is evident from the data presented in the table.

Table 4.1
Composition of Aid Inflow in Nepal 1991/92~2005/06

(Rs in million)

Fiscal Year	Grant aid	% in Total	Loan aid	% in Total	Total aid inflow
1991/92	1531.0	19.62	6269.4	80.38	7800.6
1992/93	3273.9	35.44	5961.7	64.56	9235.6
1993/94	2393.6	20.71	9163.6	79.29	11557.2
1994/95	3937.1	3.53	7312.3	96.47	11249.4
1995/96	4825.1	33.76	9463.9	66.24	14289.0
1996/97	5988.3	39.83	9043.6	60.17	15031.9
1997/98	5408.0	32.86	11054.5	67.14	16457.1
1998/99	433.6	26.78	11852.4	73.2	16189.0
1999/00	5711.7	32.59	11812.2	67.41	17523.9
2000/01	6753.4	35.92	12044.0	64.08	18797.4
2001/02	6686.2	46.48	7698.6	53.52	14384.8
2002/03	1139.1	71.38	4546.4	28.62	15885.5
2003/04	11283.4	59.66	7629.0	40.34	18912.4
2004/05	14391.2	60.83	9266.1	39.17	23657.3
2005/06	13827.5	62.73	8214.3	37.27	22041.8
Total	91486.1	74.49	31332	25.51	122818.1

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

Table 4.1 displays the declining share of grants loan and increasing proportion of loan assistance. In the FY1991/92, the foreign grant recorded the lowest, i.e.19.62 percent of foreign aid was increasing. In the FY 2002/03, Nepal received Rs 158855 million, 71.38 percent of foreign aid in the form of 2003/04, 59.66 percent of foreign aid in the form of grants and 40.34 percent in the form of loans. But in the FY 2005/06, 62.73 percent of foreign aid in the form of grants and 37.27 percent in form of loans. Nepal received total foreign

aid since 1991/92 to 2005/06 is Rs 122818.1 composed of 74.49 percent grant in total aid and 25.51 percent of loan among the total aid.

Though Nepal has been receiving foreign assistance from different sources, she has not been able to produce good performance in utilizing them. Monitoring and evaluation of foreign aid has also not been systematic so the trend of inflow of foreign aid is quite erratic.

4.3 Sources of Foreign Aid

Nepal adopted the policy of non-alignment after the collapse of Rana Regime. This concept was very relevance as this tiny nation is sandwiched between two-grant neighbors china and India who are following democratic and communist system. This is the major cause why Nepal is obtaining aid from heterogeneous sources. Nepal receives aid exactly from two sources: (1) bilateral sources (2) multilateral sources. Receiving aid from bilateral channels refers to aid received from foreign government and their aid administering bodies in Nepal such as united stated agency for international administering bodies in Nepal such as United States agency for international development (US AID), Japan international Co-operation Agency (JICA), German Technical co-operation (GTZ), Swiss Development co-operation (SDC) and the like.

Multilateral aid includes assistance form international agencies such as World Bank (WB), international monetary fund (IMF), Asian Development Bank (ADB), UN agencies and so on. The volume of aid inflow to Nepal through bilateral and multilateral sources is studied with the help of following table.

Table 4.2
Bilateral and Multilateral Aid Inflow in Nepal

(Rs in million)

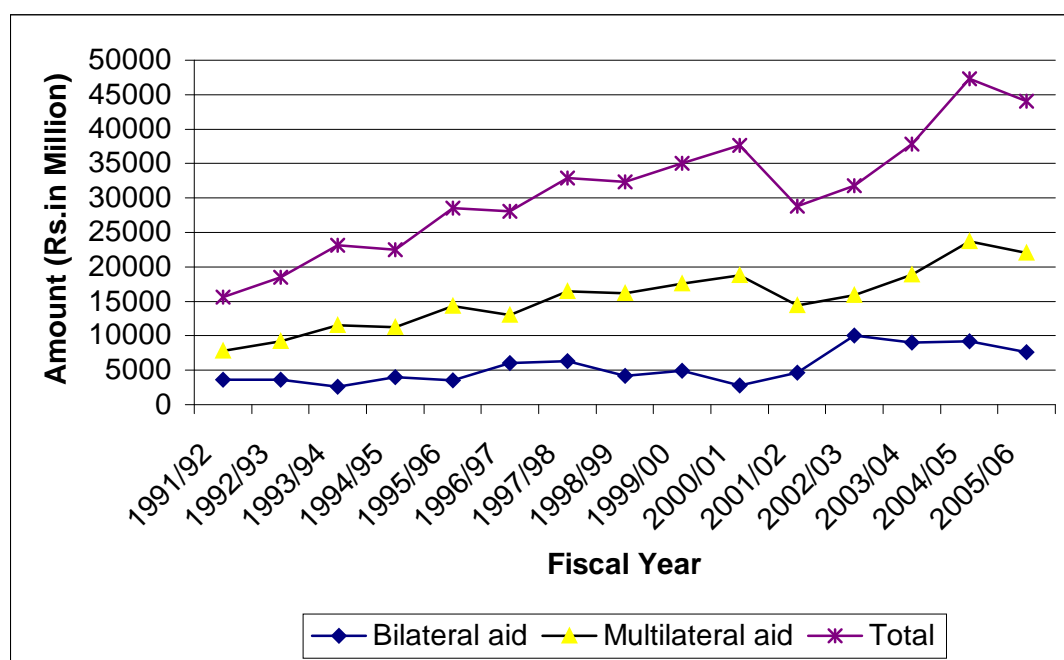
Fiscal Year	Bilateral aid	% of total	Multilateral aid	% of total	Total
1991/92	3597.3	46.1	4203.1	53.9	7800.4
1992/93	3638.5	39.4	5597.1	60.6	9235.6
1993/94	2627.1	22.7	8930.1	77.3	11557.2
1994/95	3988.7	35.4	7260.7	64.5	11249.4
1995/96	3533.3	24.7	10755.7	75.3	14289.0
1996/97	6012.7	40.0	7019.2	60.0	15031.9
1997/98	6297.7	38.3	10159.4	61.7	16457.1
1998/99	4167.6	25.7	12021.4	74.3	16189.0
1999/00	4929.1	28.1	12594.8	71.1	17523.9
2000/01	2771.2	14.7	16026.2	85.3	18797.4
2001/02	4675.3	32.5	9709.5	67.5	14384.8
2002/03	10044.4	63.2	5841.1	86.8	15885.5
2003/04	9013.2	47.7	9899.2	52.3	18912.4
2004/05	9230.8	39.0	14426.5	60.1	23657.3
2005/06	7658.4	34.7	14383.4	65.3	22041.8
Total	82185.3	35.3	150827.4	64.7	233012.7

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

Bilateral aid depends up on the co-operation between two countries. However, the aid given with some unfamiliar interest of the donor countries generates great set back to the recipient nation. Recent trend from table-4.2 indicates that bilateral aid has been declining from 46.1 percent of total aid in FY 1991/92 to 14.7 percent in FY 2000/01. Japan was the lager bilateral donor country providing 30.29 percent of total bilateral assistance in FY 1999/2000; other major bilateral donors are USA, UK, Denmark, Switzerland, Germany, Canada, Netherlands, Norway and Finland. Japan was the largest bilateral donor in terms of grant as it disburses 23.04 percent grant in the same fiscal year. Multilateral assistance begins with the establishment of international labor organization and then IMF and IBRD. The number of regional multilateral donors increased after the sixties. Nepal gets a strong support and feedback

from various multilateral agencies and donors. The trend of aid has shown that the share of multilateral aid in Nepal has been increasing tremendously during these years. Figure increased from 53.9 percent in the FY1991/92 to 85.3 percent in FY2000/01. The significance if the multilateral assistance is more effective in the terms of program delivery and less political motive of the total foreign aid in FY 2005/06, 34.7 percent is bilateral and 65.3 percent is multilateral aid. The proportion of bilateral and multilateral aid in total aid up to FY 2005/06 is 35.3 percent and 64.7 percent respectively.

Figure 4.1
Bilateral and Multilateral aid Inflow in Nepal



4.4 Foreign Aid Disbursement by Sectors

In case of Nepal, foreign aid is needed in order to mobilize resources available for implementing national plans and programs. Nepal is rich in natural resources, which are mostly unexploited due to scarcity of capital, lack of skilled manpower, appropriate technology, lack of commitment and many others reasons. Therefore, foreign aid is one of the strong weapons for better utilization of international resources of Nepal for the economic development.

Here we can see how the foreign aid has been allocated in different sector and which sector and which sector has given priorities. In 1956 when Nepal embarked on planned development, it did not have required infrastructure transformation and communication in the country. There was an indispensable need to link the country through a modern transport system, realizing its importance road construction emerged as the priority investment at the initial periods. Table 4.3 gives the general information on sectoral aid priority during the last fifteen-year (FY 1991/92 to 2005/06).

Table 4.3
Sectoral Allocation of Foreign Aid in Nepal (1975/76~2005/06)

(Rs in million)

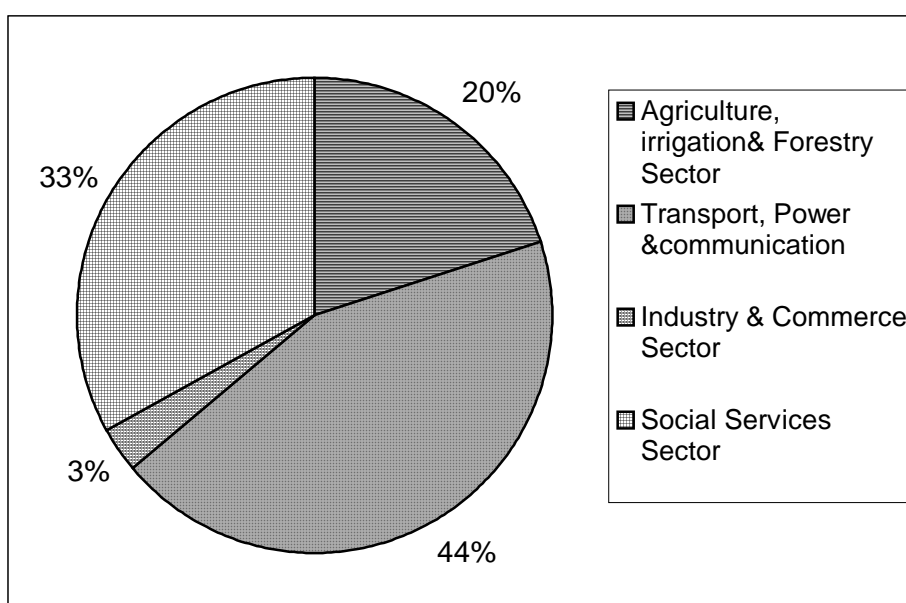
Fiscal Year	Agriculture, irrigation & Forestry Sector	Transport, Power & communication	Industry & Commerce Sector	Social Services Sector	Other sector
1991/92	24.9	31.8	27.9	15.2	0.1
1992/93	20.8	42.7	07.5	28.8	0.1
1993/94	47.7	36.1	03.4	12.7	0.1
1994/95	30.0	40.7	04.3	23.2	0.4
1995/96	23.8	56.4	0.1	18.4	1.2
1996/97	18.8	56.6	0.2	24.3	0.1
1997/98	17.3	54.6	1.2	26.8	-
1998/99	20.9	48.7	02.5	27.4	0.3
1999/00	18.3	46.6	01.7	33.0	0.3
2000/01	20.1	49.1	00.1	30.6	0.1
2001/02	22.8	41.1	02.6	32.5	1.5
2002/03	13.7	48.9	02.5	33.5	1.3
2003/04	12.8	40.0	0.7	46.2	0.2
2004/05	11.0	41.7	0.5	45.4	1.3
2005/06	13.4	32.3	0.5	50.5	5.8

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

As shown in table 4.3, Foreign aid involved all the major sectors of the Nepalese economy i.e. Agriculture, irrigation, forestry, transport, power and communication, industry and commerce, social sectors etc. In the FY 1991/92, the total disbursed aid was distributed to agricultural, irrigation forestry at 24.9 percent of total, transport, power and communication 31.8 percent and others 0.1 percent. In the FY 2005/06 these sectors received respectively 13.4 percent, 32.3 percent, 0.5 percent, 50.5 percent and 5.8 percent.

During the last fifteen years, it can be seen that transport, power and communication' sector has absorbed the largest share 44 percent of the total aid. 'Social services' sector 33 percent, agriculture, irrigation and forestry sector 20 percent, the industrial sector has received about 3 percent of total aid. Thus it can be seen that transport, power and communication and social sector has got the high-test priority compared to ' agriculture, 'industry ' and 'commerce ' sector during the last fifteen years (see figure 4.2). It clearly shows that donors are more interested in helping to build infrastructure than in directly productive sector development.

Figure 4.2
Sect oral Allocation of Aid (FY1991/92-FY 2005/06)



4.5 Foreign Aid Commitment and Disbursement

Most of the developing countries who received foreign aid have been unable to utilize the total committed aid or they have very low absorptive capacity. The existing state of government finance clearly reflects its gradual weakening over the years. Due to insufficient mobilization of internal resources; there occurred a rapid growth in debt servicing obligations of the payments of foreign debts and interest exceeded the rate of gross government revenue earnings. Although there were substantial increases in foreign aid commitments, due to a low disbursement ratio, there was a big increase in non-disbursed amounts. Due to delay in timely implementation of the projects, there has been inefficiency on the disbursement of committed amounts of foreign aid.

The main cause of the short falls in disbursement is the time lag because aid for the many projects is committed in one year and committed aid is being disbursed in subsequent years. As the returns from the investment in the economy were not obtained in time, the foreign assistance too could not be fully utilized owing to the inability to sustain the counterpart expenditure. Table-4.4 shows the status of foreign aid commitment and disbursement.

Table 4.4
Foreign Aid Commitment and Disbursement

(Rs in Million)

Fiscal Year	Total aid Commitment	Total aid Disbursement	Disbursement as % of Commitment
1991/92	21084.1	7800.4	37.0
1992/93	20526.7	9235.6	45.0
1993/94	13172.2	11557.2	87.7
1994/95	12876.9	11249.0	87.4
1994/96	16537.3	14289.0	86.4
1996/97	36643.0	15031.9	37.1
1997/98	32022.1	16457.1	51.4
1998/99	18352.5	16189.0	88.2
1999/00	20448.0	17523.9	85.7
2000/01	31287.0	18797.4	60.1
2001/02	3322.7	14384.8	43.3
2002/03	43202.7	15885.5	36.7
2003/04	23738.0	18912.4	79.67
2004/05	28152.3	23657.3	62.0
2005/06	20924.2	22041.8	105.3

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

In the fiscal year 1991/92, only 37 percent of the total committed aid was disbursed. The percent of disbursement if foreign aid is against low position with only 36.7 percent in the fiscal year 2002/03. Then, the percentage is fluctuating. The optimum percentage of the committed foreign aid is disbursed in the fluctuating rate. The optimum percentage if the committed foreign aid is disbursed in the fiscal year 2005/06, 105.3 in the fiscal year 1998/99, Rs16189 million was disbursed including bilateral as well as multilateral grant and loan, which is 88.2 percent of the total aid committed. In

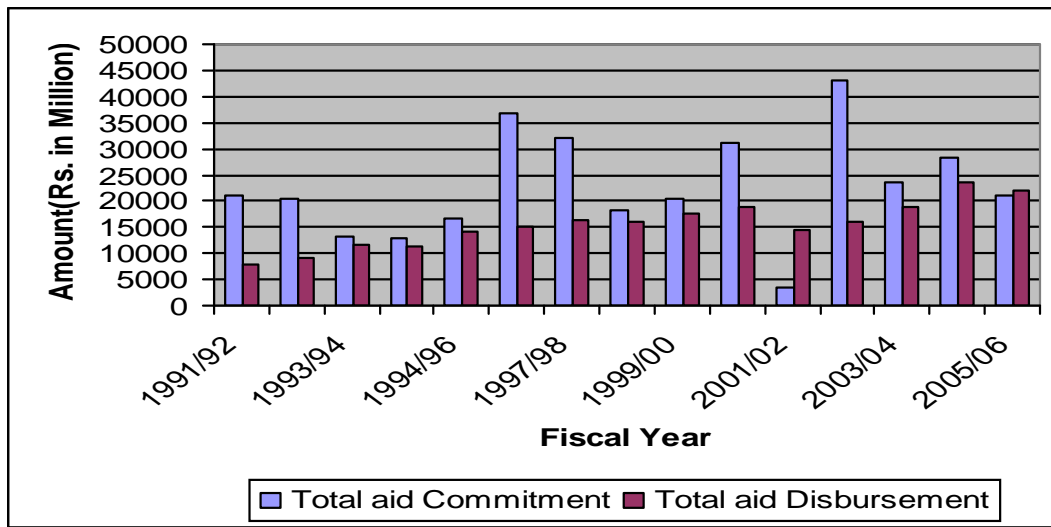
fiscal year 2002/03, Rs15885.5 million was disbursed including bilateral and multilateral grant and loan, which is 36.7percent of the total foreign aid committed. However, it is relevant to state that bilateral assistance and multilateral constitute a low percentage. It shows that disbursement ratio has been high in fiscal year 2005/06.

The rising difference between foreign aid commitment and disbursement is mainly due to poor absorptive as well as non-performance on the side if the Nepalese economy. Donors seek to provide the assistance on their own priority on installment basis and they observe the first performance on implementing the projects in difference sectors. If they do not find good performance of foreign aid utilization, they will not disburse the wholly committed aid, some Projects often show the negative impact in the society and they even stop to provide the aid in such cases. Unless there is a substantial improvement in our absorptive capacity, it will be very difficult to utilize foreign aid as such; concrete steps should be taken towards the section of present obstacles (like delay in approval of tender, weakness in administrative Management and coordination, and impractical rules and regulation etc) to enhance the absorptive capacity.

In order to enhance the foreign aid utilization and to boost up production with out loss of time, a substantive portion of foreign aid should be available in each year contributing to the increase in production. This approach will greatly help in the speedy utilization of foreign aid and in attaining the objective if increasing production and of meeting the minimum basic needs of people. (See Figure: 4.3)

Figure 4.3

Foreign Aid Commitment and Disbursement



4.6 Resource Gap and Need of Foreign Aid

Nepal has been experiencing a serious and growing resource gap on her finance. Resource gap is the difference between expenditure and revenue. Like other less developed countries Nepal also in circled by the “Vicious circle of poverty ”. Expenditure is more than revenue on one hand and population grow higher rate of population growth on the other hand, which make difficult even to maintain the same speed of economic growth. Table- 4.5 shows the serious position and growing financial resources crisis in Nepal.

Table 4.5
Resources Gaps in Nepalese Finance

(Rs in million)

Fiscal Year	Regular	Development	Total	Internal Rev.	Gap
1991/92	9905.4	16512.8	26418.2	13512.7	12905.5
1992/93	11484.1	19413.6	30897.7	15148.4	15749.3
1993/94	12409.2	21188.2	35597.4	19580.8	16166.6
1994/95	19265.1	19794.9	39060.0	24575.2	14484.8
1995/96	21561.9	24980.5	46542.4	27893.1	18649.3
1996/97	24181.1	26542.6	50723.7	30373.5	20350.2
1997/98	27174.4	28943.9	56118.3	32937.9	23180.4
1998/99	31047.5	28531.3	59579.0	37251.0	22328.0
1999/00	34523.3	31749.2	66272.5	42893.8	23378.7
2000/01	42769.2	37065.9	79835.1	48893.6	30941.5
2001/02	48590.0	31482.2	50072.2	50445.5	29626.7
2002/03	54973.0	29033.0	84006.1	56229.8	17776.3
2003/04	66347.0	23095.6	89442.6	62331.0	27111.6
2004/05	75219.7	27340.7	102560.4	70122.7	32437.7
2005/06	81282.6	29606.6	110889.2	72282.1	38607.1

Source: Various Issues of Economy Survey, MOF, HMG/N

The table shows that each year we are facing the problem of resource gap tremendously. The magnitude of this gap is augmenting year coming year. In FY1991/92, initial resource gap was Rs 12905.5 million. In FY 1992/93 resource gap was 15749.3 million. It increased to Rs 30941.5 million in FY2000/01, which are more than two folds of gap on FY1992/93. It increased to Rs38607.1 million in FY2005/06. The trend of increasing resource gap shows that foreign aid is considered as an important instrument in financing the

public expenditure. Comparing from FY1991/92 to FY2005/06, the resource gap has increased about three times in Nepal.

Regular increment of resource gap and management of this gap by means of foreign aid signifies that foreign aid plays very crucial and pivotal role in Nepalese economy. In order to operate the development plan smoothly we have to manage large amount of resource by mean of generating foreign resources. The contribution of foreign aid in different plan periods is shown in table.

Table 4.6
Foreign Aid in Development Expenses in Different Plans in Nepal.

(Rs in million)

Plan Period	Development Expenditure	Foreign aid	% of Foreign aid
1 st plan (1956-61)	382.9	382.9	100.0
2 nd Plan (1961-62)	614.7	478.3	77.8
3 rd plan (1965-70)	1639.1	919.8	56.1
4 th plan (1970-75)	3356.9	1509.1	45.0
5 th plan (1975-80)	8870.6	4264.1	48.1
6 th plan (1980-85)	21750.6	13260.0	61.0
7 th plan (1985-90)	48345.4	23978.5	71.6
8 th plan (1992-97)	113519.1	74355.0	65.5
9 th plan (1997-02)	215154.4	114290.0	53.1
10 th plan (2002-07)	234030.0	134620.0	57.5

Note: Estimate value for 10th plan is at 6.2 percent growth rate

Source: Various issues of economic survey, MOF, HMG/N

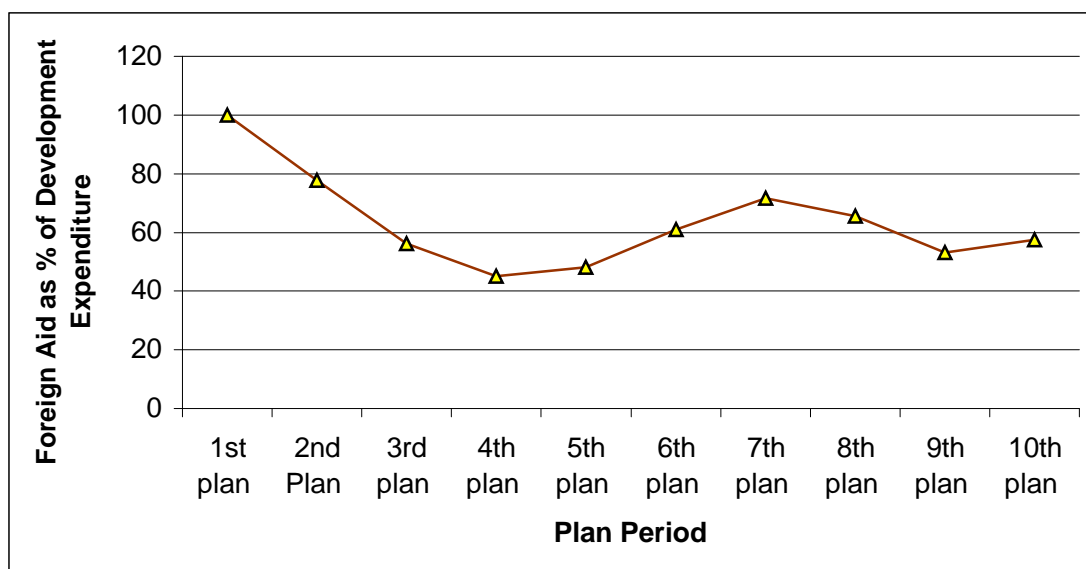
Foreign aid as percentage of development expenditure, which was 100 percent for the first plan, declined over a period of next fifteen years, but still remained high. The percentage for the no plan year (1961/62) was 81.9 percent.

Foreign aid constituted 77.8 percent (478.3 million) of the total development expenditure (614.7 million) incurred during the second plan period (1962/65). This proportion however, fell to 56.1 percent in the third plan (1965/70) with development expenditure of Rs 1639.1 million and foreign aid of Rs 919.8 million. The share of foreign aid in the total development expenditure fell further to 45 percent in the fourth plan (1970/75) for which only Rs 1509.1 million of foreign aid was available against a development expenditure of Rs 3356.9 million. Foreign aid constituted 48.1 percent of the development expenditure of the fifth plan, which had a development expenditure of Rs 8870.6 million and foreign aid Rs 4264.1 million. This increasing trend continued over the next two plan periods. The share of foreign aid in the total development expenditure in the sixth plan (1980/85) registered a sharp increase from 48.1 percent in fifth plan to 61 percent in the sixth plan which had at its disposal foreign aid of Rs 12360 million against its total development expenditure of Rs 21750 million. The share of foreign aid in the development expenditure in the seventh plan (1985/95) but it is still high at 65.5 percent. The share of foreign aid in the ninth plan (1997/02) was 53.1 percent (Rs 114290 million) to the total development expenditure of Rs 215154.4. In the tenth plan, the foreign aid is estimated to finance 57.5 percent (Rs 134620 million) of the total development expenditure of Rs 234030 million for 6.2 percent growth rate for 4.3 percent growth rate, foreign aid is estimated to finance 67.1 percent (Rs 119690 million) of the total development expenditure of Rs 178350 million.

The priority sector of different plans seems to be different. The first and second plans had the priority to build the foundation for economic planning and the third plan concentrated with development of agriculture sector. The fourth, fifth, sixth, seventh and eight plans have the priority in sustainable development. The ninth and tenth plans totally concern on eradication of poverty from Nepal with the various priorities in different plan period, foreign aid has played significant role.

Figure 4.4

Foreign Aid as Percentage of Development Expenditure in Different Plan Periods of Nepal



4.7 Burden of Foreign Aid

If foreign aid is not used judiciously, future generation of recipient countries will be forced to bear heavy burdens. Foreign loan pose a burden to the country mainly due to their debt servicing requirements. Debt servicing not only impinges on already scarce revenues, it also claims foreign exchange the most precious resource of a country, since repayment is made in foreign exchange. Global experiences show that debt servicing drains the public budget and reduce the availability of counterpart funds and additional domestic resources required of for operating and maintaining aid investment facilities. When returns from loans exceed the debt servicing burden, there is no cause for concern. Otherwise, foreign debt becomes a long-term burden to the recipient country. The greater amount of foreign aid required, the greater the burden to be faced. Moreover if foreign assistance isn't used properly, foreign grants also became burdensome to the recipient economy. One of the main reasons for the failure of the past 14 years of parliamentary Nepal is the complete domination

by international aid agencies and bilateral donors through their conditional loans and aid. The 'sovereign' parliament and the elected government remained largely as the agent of the foreign interest lobby. Thus, we are never allowed to express our own needs and priorities. There are even cases of the government refusing to release secret dealings and agreements with the international financial institutions to parliaments and even the Supreme Court. The spirit of democratic governance was taken over by donor-driven corporate governance, and human rights and the rule of law were subject to corporate rules. As a result, Nepal's adoption of a democratic constitution and laws, as well as the ratification of dozens of major international human rights and environmental instruments, remained totally ineffective, as the governments have always been compelled to comply with the donor's Pre-conditions and corporate obligations.

Though, Nepal has been borrowing external capital only since the early 1960s, debt servicing began only in the late 1960s. A few governments guaranteed loans were carrying comparatively higher rate of interest and a few other direct loans were not mature until the mid 1970s. Nepal's debt servicing burden has been reduced to some extent by the conversion of some loans into grants. Although, Nepal has been receiving foreign loans with very low rate of interest and the time of maturity period is very long ranging from 25 to 40 years, the debt burden has been growing consequently. Table -4.7 shows foreign loan and Debt-Servicing situation.

Table 4.7
Foreign Loans and Debt Servicing

(Rs. in million)

Fiscal Year	Net Outstanding Debt	Repayment	Interest Payment	Total Debt Services
1991/92	70923.9	942.2	722.7	1664.9
1992/93	87420.8	125.9	879.0	1231.9
1993/94	101966.8	1468.2	1020.0	2488.7
1994/95	18000.9	1828.2	1156.5	2984.7
1995/96	128044.4	1987.7	1316.6	3304.3
1996/97	132086.4	2102.4	1247.0	3349.4
1997/98	161208.0	2780.2	1421.0	4201.2
1998/99	169465.9	3196.5	1549.0	4745.5
1999/00	190691.2	3681.1	1640.3	5321.4
2000/01	200404.4	4500.6	1700.8	6201.4
2001/02	220125.6	4751.4	1816.1	6567.5
2002/03	223433.2	5497.5	2021.7	7519.2
2003/04	232779.3	5767.1	2141.8	7908.9
2004/05	219641.9	5954.5	2146.8	8101.3
2005/06	234805.6	4321.3	1172.6	5493.9

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

Table 4.7 shows that the net outstanding debt was only 70923.9 million in the FY1991/92. Repayment was Rs 942.2 million; the component of interest payment was introduced. The total debt servicing was Rs 1664.9 million but the component of interest payment was 722.7. In the FY2003/04 the net outstanding debt was Rs 232779.3 million. This increased by 3.3 times compared to the FY 1991/92. The total debt service was Rs 7908.9 million in the FY2003/04 which increased by 4.8 times over the period FY 1991/92. In every subsequent year, the debt dynamics is increasing. In the FY 2005/06, the

amount of net outstanding debt was Rs 234805.6 million; Repayment was Rs 4321.3 million and interest payment was Rs 1172.6 million. This shows that the net outstanding debt increased by 31 times, repayment increased by 22 times and total debt services increased by 30 times compared to the FY1991/92. This shows the real debt situation of Nepal. If we divide the total net outstanding debt of the FY2005/06 by our total population 23.2 million, we get the per capita external debt of Rs 10121, which shows the share of every Nepalese external loan.

When the domestic currency in aid recipient country depreciates, the debt burden increases even without any new borrowing taking place. For example, in different years during 1985 to 2001, Nepal acquired foreign loans totaling Rs 115 billion or US\$ 2,345 million. If all loans were to be repaid by 2001, the country would have to repay Rs 175 billion (multiplying outstanding loans by the current exchange rate), excluding interest. This means that the amount equivalent to more than 50 percent of foreign aid would have to be repaid without actually borrowing any more money. Thus, the interest rate in multilateral loans, seemingly very low (1-2 percent), in actuality turns out to be very expensive in the long run.

It is generally believed that foreign grants are free since they do not require repayment by recipient country. This is not always true. If either foreign grants or technical assistance is not used properly, both can prove to be burdensome in a number of ways. First in the name of technical assistance, thousands of foreign experts weakens the potential for the human resources capacity building in recipient countries, and perpetuates dependence upon donors. Further, however qualified foreign experts may be, most of them cannot understand the cultural, social, economic and political contexts of Nepal as well as local experts can. Hence, their hiring implies some degree on resources misutilization. Second, technical assistance tied with some conditionality can be harmful to the receiving economy. Aid tying compels recipient countries to buy goods and services from donor countries. Donors

expand their markets in developing countries by this important means. For example, donor food support (in large quantities) depresses demand for local products and helps the donor guarantee itself a market. Similarly, introducing new technology that cannot be produced domestically increases dependence on imports in the long-run.

Regarding aid tied with goods and services, it is worthwhile to reflect briefly on Japanese assistance to Nepal. Japan, the largest bilateral donor, supports its business interests through consultants and procurements rather than by exerting policy influence. Their working style is justified in the name of quality control. For example, in the contract for the Japanese grant project. Extension and reinforcement of the power transmission and distribution system in Kathmandu, one of the conditions imposed was: 'the grant will be used by His Majesty's Government of Nepal properly and exclusively for the purchase of the product of Japan or the Kingdom of Nepal and the services of Japanese or Nepalese nationals.' Deepak Gyawali, a forthright social scientist and a former minister for water resources and electricity, observes "While Japan's generosity with grants has endeared Japan to Nepali politicians, and most bureaucrats, this generosity will have the technocrats worried. The primary reasons cited are the items to be bought with Japanese grants are almost three times costlier than items financed by credit with international competitive bidding in other projects in Nepal. Also the items supplied are difficult to maintain with locally available spare parts, necessitating subsequent import of spares from Japan at high prices."

Foreign assistance can perpetuate social inequalities provoking adversely affected groups of people to resort to destructive behavior. For example, the salaries and benefits of Nepali staff working in donor funded agencies, generally, are very high in comparison to those of government officials, teachers and university lecturers. This has dampened the morale of those employed in the latter categories. Similarly, foreign aid is considered to be one of the major causes of the ongoing Maoist insurgency, as aid funded

development efforts have contributed to widened inequalities between different groups and geographical regions of Nepal.

Last but not the least inappropriate policy changes due to donor pressure are sometimes painful to bear. On this it is worthwhile to cite the specific case of the subsidy withdrawal policy of the government succumbing to the ADB's pressure, HMGN started to cut down on subsidies in the agriculture sector in the 1990s, without properly studying the possible consequences. However, the country competes with Indian farmers for agricultural markets. India has already successfully achieved a green revolution. Indian farms enjoy access to much better infrastructure than Nepali farms, resulting in higher agricultural productivity. Further, the government of India continues to provide subsidize power, fertilizer and other inputs used in the agricultural sector.

CHAPTER-V

JAPANESE AID TO NEPAL

5.1 Historical Background of Nepal-Japan Relation

Nepal is a landlocked country whereas Japan is a sea locked country. In modern times, Nepal and Japan has bilateral relations for more than one hundred years. The relationship of Nepal with Japan cannot be viewed only with the aid it gives to Nepal. Nepal has a long religious and friendly attachment with Japan. This is main reason why Japan is giving a colossal amount of aid to this poorest nation. It is obligation of Japan to provide resources to the poorest nation of the world. The philosophy of Lord Buddha has very significant and remarkable interference in the Japanese society. A great influence of Buddhist religion. In April 1902, three years after Kawaguchi's visit, Prime Minister Chandra Shamsheer sent eight Nepali students to Japan. They were also the first Nepali to go overseas for study under government scholarship upon their return to Nepal in 1905, all eight student were employed in their respective fields. They minted copper coins, improved the arsenal and manufactured light weapons. In 1905, during his second visit to Nepal, Kawaguchi wrote 75 pages long letter to Prime Minister Chandra Shamsheer Rana. The letter was full of patriotic feelings recommending the prime minister of Nepal for the promotion of education, vocational schools, and exploration of mines, production of electricity, construction of roads, trade, banks and modernization of administration. This was the beginnings of personal exchanges between the two countries. Based upon these direct encounters a century ago, the two countries now enjoy wide ranging bilateral relations conducted in a lasting spirit of friendship and cooperation.

The year 2002 marked the completion of a hundred year of Nepalese students in Japan in which was one of the most recent memorable events in Japan-Nepal relation. The Embassy of Japan in collaboration with the Japan

University Student Association in Nepal (JUSAN) and the Japan Nepal Association in Japan Organized Celebrations in Nepal and Japan. Kawaguchi was printed on a postal stamp in 2002. This gesture highlights the deep respect that exists between the people of Japan and Nepal. Although Japan and Nepal are geographically miles apart, having a similar cultural heritage, a strong spiritual line exists between the people. This common spiritual, religious and traditional value is the foundation of friendly and cordial relations between the people of Japan and Nepal. Exchanges at people to people level are also one of the driving forces to further strengthening friendly relation between Japan and Nepal. Taking this into account, the governments of Japan and the Japan Foundation have provided an opportunity to a wide range of Nepalese nationals such as social studies teacher of secondary school, young students school studies etc. to visit Japan. Through such visits, they can exchange views with their Japanese counterparts and acquainted themselves with contemporary Japanese society, economy, culture, politics etc. allowing them to broader mutual understanding between the people both nations. The year 1956 is Important in the history of Japan – Nepal ties when diplomatic relations were established between the two countries on the September 1956. In the same month Ambassador, the Royal Nepalese embassy was established in Tokyo in 1965. In July of the same year, Ambassador B. R. Rajbhandari went to Tokyo to take up the office. Three years later, in February 1967; the Embassy of Japan in Nepal was officially opened in Katmandu. The first residential Ambassador Japan, Heimlich biro arrived in Katmandu in the same month. After the established of diplomatic relationship in September 1956, cultural exchange and economic co-operation between these nation got momentum. Following the establishment of diplomatic relationship, their Majesties King Mahendra and Queen Ratna paid a state visit to Japan. The visit was very crucial to Nepal as Japan was entering in to the stage of high mass consumptions. The government of Japan at that time was adopting the income doubling policy. They visit Japan at a time when strong economic growth was about to take off through the government's income doubling policy.

In 1970, their imperial highness prince and princes Hitachi visited Nepal to attend the marriage ceremony between his Royal Highness Crown Princess Aishwarya. In 1975, coronation of his Majesty King Birendra was held and the occasion was graced by the presence of crown prince and crown princes of Japan. The royal couple also presided over a commemorative planting of several varieties of Japanese cherry sampling at the royal Botanical Gardens in Godawari. The lasting beauty of the Himalayan Cherries of Godawari symbolizes strong and intimate ties between the two royal families and the people of Japan and Nepal.

In 1979, their Majesty king Birendra and Queen Aishawarya paid a state visit to Japan. During the visit the king renewed old friendship with member of the imperial family, university professors and many other friends. In 1983 their Majesties the king and Queen revisited Japan on their way back from the United States and met with the Japanese emperor. In 1985, their Majesties visited Japan once again to grace Nepal's national day in Japan, king Birendra met with the Japanese emperor and talked with then Prime Minister Yasuhiro Nakasone. In 1987, his highness crown prince of Japan paid on official visit to Nepal and went trekking to Sarangkot on the outskirts of Pokhara.

In 1990, His Royal Highness Crown Prince Dipendra went to Japan to attend the enthronement ceremony of Japanese emperor and express facilitations on behalf of the Nepali people. Similarly frequent exchange of visits at high official level has taken place between Japan and Nepal. In 1998 Prime Minister Girija Prasad Koirala paid on official visit to Japan. This was the first official visit to Japan by a prime minister of Nepal. In 25th August 2000, the Prime minister of Japan, Mr. Hoshiro Mori paid a daylong official visit to the kingdom of Nepal at the incitation of Prime Minister Girija Prasad Koirala. That was the first visit of Japanese Prime Minister to the kingdom of Nepal.

On 4th June, the relation between them is becoming more and more warm and cordial during the period of king Gynendra. The Girija Prasad Koirala government and the present Nepali Congress government led by Sher B. Deuba (July 22, 2001 on wards) have also done much for the save of improving further relations between the two Countries. Besides, Nepali parliamentary delegations have visited Japan from time to time.

People's level contracts between the citizens of two countries have increased gradually since Royal Nepal Airlines inaugurated direct flight between Katmandu and Osaka in 1994 which create and solid foundation for Nepal-Japan relations. The cordial-Culture and diplomatic relationship between Nepal and Japan proves to be a sufficient reason for Japan being a top donor country in the development effort of Nepal.

5.2 Review of Nepal-Japan Relation

Japan recognizes the fact that cultural that cultural exchange provide a vital means that lead to a greater understanding and trust of Japan with in the international community Japan is actively promoting cultural exchanges and place great Important on international exchanges in various field including people to people, cultural and academic field. These exchange programs have been progressing both at the bilateral and at the people's level. In Japan there are several friendship societies related with Nepal that are very active and also in Nepal there are very a dozen associates related with Japan. These friendship associations contribute to promoting cultural ties between both countries. In the field of cultural and art exchange, Many contemporary as well as traditional aspects of culture have been widely introduced to the Nepalese people including ikebana (flower management), kimono, Japanese traditional music, tea ceremony, graphics arts, architecture etc. The study and teaching of both the Nepali and the Japanese languages in both countries is one of the major driving forces for helping to promote mutual understanding. At this movement, there are a growing number of Nepalese people who are learning

Japanese and the number of Japanese language schools in Nepal has now reached 20. The Japan foundation has been engaged in assisting Japanese language teacher in Japan, donating Japanese language educational materials and by administering the Japanese language proficiency test.

In recent years, the exchanges of visits among promising students, youths and intellectuals have been increasing. The government of Japan has invited Nepalese from different backgrounds such as governmental officials, academics and Journalists etc to help them gain a deeper understanding of Japanese society and culture, as well as for strengthening ties with their counterparts in Japan. Soon after the establishment of diplomatic relations between Japan and Nepal in 1956, Japan offered scholarships to Nepal and since then hundreds of students have been benefiting from these exchanges.

This year marks the 50th Anniversary of diplomatic relations between Japan and Nepal. The embassy of Japan and other Japan related organizations in Nepal are planning to organize various commemorative events such as a samisen concert, an exhibition of Japanese contemporary clay work, Judo and kendo competition, opera evening, Japan week, to name just a few. This anniversary is expected to mark the beginning of another chapter for the continuing friendly relations between our two countries.

5.3 Japanese Aid to Nepal

The flow of total foreign aid to Nepal has been growing over the years. Nepal receives foreign aid in the form of loan and grant from both bilateral and multilateral sources. Japan has a significant share in the total aid flow to Nepal. Table 5.1 shows the total amount of Japanese aid from the fiscal year 1991/92 to the fiscal year 2005/06.

Table 5.1
Inflow of Total and Japanese Aid in Nepal

(Rs in million)

Fiscal year	Total Foreign Aid	Total Japanese aid (grant+ loan)	% of Japanese Aid to Total
1991/92	7800.4	1757.4	22.5
1992/93	9235.6	3501.4	37.9
1993/94	11557.2	1571.9	13.6
1994/95	11249.4	6928.3	61.6
1995/96	14289.0	5295.5	37.1
1996/97	15031.9	4994.4	33.2
1997/98	16457.1	1746.6	10.6
1998/99	16189.0	2894.5	17.9
1999/00	17523.9	8394.1	47.9
2000/01	18797.4	7090.3	37.7
2001/02	14384.8	5326.2	37.0
2002/03	15885.5	2802.2	17.7
2003/04	18912.4	1494.6	7.9
2004/05	23657.3	2726.3	11.5
2005/06	22101.9	1727.8	7.8
Total	277966.6	65864	23.69

Source: I) Economic survey issues MOF/HMG/N

II) Foreign aid division MOF/ HMG/N

III) Various Issues of Japan's ODA annual report MOFA Japan

Table 5.1 shows that the increasing trend of Japanese aid inflow in Nepal leaving apart some fluctuation. In the initial period up to 1991/92, the amount of Japanese aid inflow was 22.5 percent (Rs1757.4 million) in the total inflow of Rs 7800.4 million foreign aid. After the 1992/93, the amount of Japanese aid inflow was 37.9 percent (Rs3501.4 million) in the total inflow of Rs 9235.6 million foreign aid. In 1999/00, the total foreign aid to Nepal was Rs 17523.9 million out of which Japanese aid occupied Rs 8394.1 million(47.9

percent of the total aid) which is nearly one half of the total foreign assistance. In 2000/01, Japanese assistance to total foreign assistance occupied a share of 37.7 percent on total aid (Rs 7090.3 million out of Rs 18797.4 million) which is greater than one third of the total assistance. In 1994/95 share of Japanese assistance was the highest with 61.6 percent in total foreign aid (Rs 6228.3 million out of Rs 11249.4 million) and from 1999/2000, the share in Japanese aid is decreasing trend but still large.

Figure 5.1
Share of Japanese aid and Other Bilateral and Multilateral Aid to
Total Aid in Nepal.

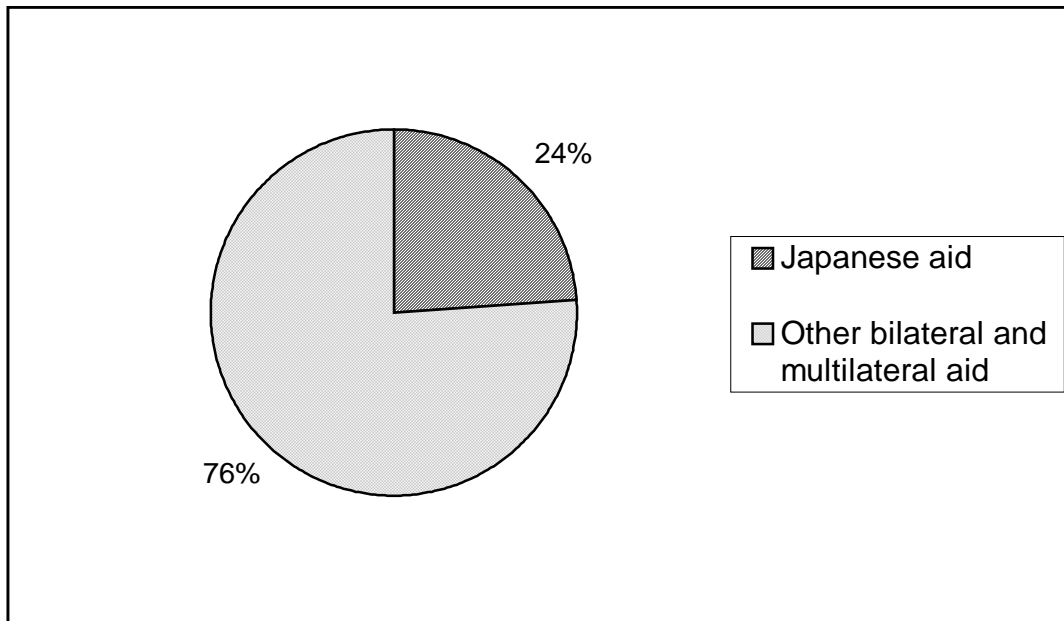


Figure 5.1 depicts that Japanese aid has occupied an important place in the total inflow of foreign aid to Nepal. From 1991/92 to 2005/06, Nepal received a sum of total Rs 58251.5 65864 million assistance from Japan and these constitute 24% of total aid on an average for the period 1991/92-2005/06.

Some of the major projects successfully completed under Japan's aid are Kulekhani Hydropower project I and II, Udaypur cement plant, TU teaching hospital, national tuberculosis centre, modernization of Tribhuvan international airport and Gongobu Bus Park. Ongoing projects that are yet to be completed

include Kaligandaki Hydropower, Banepa Sindhuli Bardibas road, Bagmati irrigation project and so on. Japan has also provided loan assistance to Melamchi water supply project, which will help to reduce the problems of water supply in Kathmandu valley.

With in the period of three decades, the volume of Japanese aid to Nepal has been increasing and it covers all the major sectors of the economy. Some major donors as India, China, USA and Soviet Union may have been motivated by political and other subjective consideration in granting aid to Nepal. However, Japan has no such political or strategic consideration, and its aim is nothing other than to help for our economic development.

5.4 Japanese Loan Assistance to Nepal

Although the history of Japanese aid is not that much long, the amount of loan provided to Nepal is very remarkable. This sort of loan is bilateral direct loan and is usually provided by the government of Japan and is referred as Japan's ODA. Japan has provided loan assistance to Nepal for the first time in March 1970 through Export Import Bank of Japan to NIDC for industrial development of Nepal. The second and third loan assistance was provided to Kulekhani Hydro Power Project I and II respectively from Japan overseas economic cooperation fund (OECF) for power generation in Nepal. The share of Japanese loan to the total loan assistance to Nepal is presented in Table 5.2.

Table 5.2
Share of Japanese Loan to Total Loan

(Rs in million)

Fiscal Year	Total Foreign loan	Total Japanese loan	% of Japanese loan to Nepal
1991/92	6269.4	3746.7	59.8
1992/93	5961.7	3422.8	57.4
1993/94	9163.6	1401.3	15.3
1994/95	7312.3	6372.5	87.1
1995/96	9463.9	5150.0	54.4
1996/97	9043.6	4462.5	49.3
1997/98	11054.5	0.0	0.0
1998/99	11852.4	0.0	0.0
1999/00	11812.2	7364.3	62.3
2000/01	12044.0	3296.4	27.4
2001/02	7698.6	*	
2002/03	4546.4	*	
2003/04	7629.0	*	
2004/05	9266.1	*	
2005/06	8214.3	*	
Total	119519.8	35216.5	

Note: *means not available

Source: I) Economic survey of various year

II) Foreign aid division

III) Various issues of Japan's ODA annual report MOFA, Japan.

Table 5.2 shows that there was no loan in the FY 1997/98 to 1998/99. But with the passage of time Japanese loan assistance has started to increase some fluctuation. In 1993/94 Japan provided Rs 1401.3 million-loan assistance that was 15.3 percent of the total foreign loan of Rs 9163.6 million. In 1994/95, Japan provided Rs 6372.5 million loan assistance, which was 87.1 percent of the total foreign loan of Rs 7323 million. From 1975/76 to 2005/06 total loan assistance during the last 15 years it is thus clear the Japanese loan assistance has occupied an important place in the total loan assistance to Nepal.

5.5 Japanese Grant Assistance to Nepal

Nepal being a poor country also receives foreign aid in the form of grant. Since 1951, Nepal started to receive foreign grant. United States of America was the first donor country to Nepal. After that, India also started to provide grant assistance to Nepal. Japan has been providing grant assistance since the diplomatic relation between the two countries was established in 1956. Currently, more than twenty countries and some agencies are providing bilateral as well as multilateral grant to Nepal. Japan is providing bilateral as well as multilateral grant to Nepal. Japan is providing grant assistance to Nepal in a considerable amount. Japanese grant assistance and its share in the total grant inflow to Nepal are shown in table 5.3.

Table 5.3
Share of Japanese Grant to Total Grant

(Rs. in million)

Fiscal Year	Total Foreign grant aid	Total Japanese grant aid	% of Japanese grant total grant aid
1991/92	1531.0	11.0	0.7
1992/93	3273.9	78.6	2.4
1993/94	2393.6	170.6	7.1
1994/95	3937.1	555.8	14.1
1995/96	4825.1	145.5	3.0
1996/97	5988.3	531.9	8.9
1997/98	5402.6	1746.6	32.3
1998/99	4336.6	2894.5	66.7
1999/00	5711.7	1029.8	18.0
2000/01	6753.4	3793.8	56.2
2001/02	6686.2	5326.3	79.6
2002/03	11339.1	2802.2	24.8
2003/04	11283.4	1494.6	32.2
2004/05	14391.2	272.3	18.9
2005/06	13827.5	1727.8	12.5
Total	101680.7	22581.3	22.2

Note: NA means non- availability of data

Source: I) Economic survey

II) Various Issues of Japan's ODA annual report.

The above table shows that in 1991/92, the total grants assistance received was 1531.0 million in which Japan shared Rs 11.0 million, which is 0.7 percent of the total grant assistance. Since 1997/98, the Japanese grant assistance is increasing with fluctuation. In the FY 1995/96, share of Japanese grant assistance was 3.0 percent to the total grant assistance (Rs 145.5 million out of total grant assistance of Rs 4825.1 million), where as in 2001/02 the share was 79.6 percent to the total (Rs 5326.3 million out of total grant assistance of Rs 6686.2 million). During the last 15 years (i.e. from 1991/92 to 2005/06), Nepal received Japanese grant assistance of Rs 22581.3 million. This is 22.2 percent of the total grant assistance received by the country during the same period.

However, the Japanese assistance has been playing an important role in the process of development of Nepal, it has created some serious problems in last years. Most of the Japanese grant aid projects are based on capital intensive technologies, which give less benefit to local people from employment generation viewpoint. Large parts of the funds returns Japan through the salaries of experts and heavy capital equipment.

Since the establishment of Nepal-Japan diplomatic relationship in 1956, Japan begun to provide technical assistance to Nepal through the Overseas Technical Cooperation Agency (OTAC). From 1970, Japan's assistance to Nepal has not concentrated only in the form of technical assistance but also in the form of grant and loan assistance. In 1974, OTCA was merged into a newly created statutory organization, the Japanese international cooperation Agency (JICA). Since then the technical assistance from Japan gradually coming through JICA and its branch agency Japan overseas cooperation volunteers (JOCV) in Nepal. From 1970s, Japanese official development assistance (ODA) to Nepal increased rapidly. Japan is providing assistance in different forms under three headings viz. grant assistance loan assistance and technical assistance through ODA, JICA, JOCV and OECF.

Japan assists Nepal taking in consideration of the following factors:

- Nepal has amicable relation with Japan.
- Nepal has the lowest income in terms of percapita in south Asia. The fact that Nepal is a land locked nation makes its situation all the more serve. Consequently, Nepal has a strong demand for foreign aid.
- Since democratization in 1990, Nepal has pursued economic development in an environment in which democracy has taken root and the economy has been liberalized (Japan's ODA report 1999).

Japan, the biggest donor nation for Nepal has been providing assistance for all development sectors efforts of cooperation (assistance) cover public healthcare, education poverty relief environment awareness and human resource development. Between 1975/76 and 2005/06, the assistance which Nepal received, stood , at around Rs 61409.9 million which included outright grant, aid loan, as well as technical assistance.

5.6 Japanese Technical Assistance to Nepal

Donor countries have assisted Nepal not only in terms of financial aid but also in the form of ideas knowledge, skills and technology. Technical assistance is very important to the development of countries like Nepal. The term "technical assistance" is related to the human resource development. It is the fundamental force drives the country along path of peace and prosperity technical assistance is aimed at bringing up personnel that are technically required in taking a positive part in the task of nation's economic and social development in developing countries.

Japanese technical assistance covers wide area of activities, from accepting the students forms Nepal as well as the supply of technique and modern equipment in different field like health, education, agriculture, hydropower, transportation and communication. The foreign development partners of Nepal are not only helping through the government agencies but

also through the INGOs. It has an important role in the economic and social development of Nepal.

The donor countries and agencies have shown a tendency of providing assistance in the field of social service through the NGOs and INGOs. In the case of Japan, official Bilateral Technical Cooperation is executed through the Japan international cooperation Agency (JICA). Scheme of technical cooperation includes acceptance of trainees, dispatch of experts, provision of equipment, project type technical cooperation and dispatch of Japan overseas cooperation Volunteers (JOCV).

Japan has been providing technical assistance to Nepal since 1954 prior to other kinds of assistance through different sources. But after the establishment of JICA in 1970, Japan is providing technical assistance to Nepal through JICA and Japanese volunteers are as the eleventh host country in accordance with exchange of notes between the government of Japan and Nepal. Table 5.4 shows the flow of Japanese technical assistance to Nepal.

Table 5.4
Japanese Technical Assistance to Nepal

(Rs in million)

Fiscal Year	Total technical assistance	Japanese technical assistance	Percentage
1991/92	4370.8	1228.2	36.4
1992/93	3356.6	1728.7	28.1
1993/94	3808.9	1531.2	51.1
1994/95	3365.5	1484.2	40.2
1995/96	5983.5	1699.3	44.1
1996/97	3953.3	1387.6	28.4
1997/98	3344.5	1173.9	35.1
1998/99	5107.7	2216.7	43.4
1999/00	5314.2	1865.3	35.1
2000/01	5475.3	2190.1	40.0
2001/02	753.6	354.9	47.1
Total	44833.9	16860.1	37.6

Source: Various Issues of Japanese's ODA annual report, MOFA, Japan

From the table 5.4, it is clear that Japanese technical assistance is increasing smoothly except in few years. During the period between 1991/92 and 2001/02, Japanese technical assistance was equivalent to Rs 16860.1 million. The Japanese technical assistance includes training program, experts dispatch program, survey mission, equipment supply and JOCVs.

Under the Japanese technical assistance, the major agency JICA is running several types of technical program in Nepal. Since the establishment of its office at Kathmandu, JICA is providing following technical assistance programs:

- Training program
- Expert dispatch program
- Equipment supply program

Project type cooperation

- Western region basis health development project
- Janakpur agriculture development program
- TU Medical education project
- Cottage industries development project
- Development survey program.
- Japanese Overseas Co-operation Volunteers

5.7 Organization and Agencies for Cooperation

There are many organizations and agencies through which Japan has been assisting to Nepal. Some of them are as described below:

I) Japan International Cooperation Agency (JICA):

The agency for the implementation of government based technical assistance was established in August 1974 through a special act of the government of Japan. In Nepal, JICA was established in 1978. Japans quest for

international economic cooperation and her endeavor towards providing technical cooperation to the outside world dates back to 1957, when it became a member of Colombo plan. The agency for technical cooperation, Japan Overseas Cooperation Technical Agency (JOCTA), which was instituted in 1962, was transformed into JICA. JICA extends technical cooperation and facilities grant aid with the objective of supporting self reliant and sustainable development in developing countries in line with the ODA chapter. JICA is focusing on human development and the establishment of economy and social infrastructure. Through this, it aims to contribute to the economic and social development of developing countries.

Keeping economic cooperation as the mainstay of international cooperation, JICA has pursued economic and social infrastructure development as its policy of activities. To encourage developing countries to reduce aid dependency and promote self help efforts. JICA has always been supporting them by providing guidance and advice to the counterparts from the behind. In the recent years, JICA has tried to address the development issues of the developing countries through various four approaches.

- a) Regional and country specific approach,
- b) Project cycle management approach,
- c) Integrative approach and
- d) Cooperation approach

JICA's main activities at present can be summarized as follows:

- Human Resource Development: It includes training for Nepalese professionals and counterparts in Japan and other types of technology transfer as well.
- Dispatch of experts for technological back stopping.
- Provision of equipment for skill handover.
- Project type technical co-operation: It integrates the technology transfer program covering dispatch of experts, provision of equipment and training in abroad.

- Grant aid program: It constitutes a major portion of Japan's bilateral ODA with out repayment obligation out of many forms of grant aid categories recognized by Japan; JICA has been commissioned to execute three types. They are: General Grant Aid, Fishery Grant Aid and Grant Aid for increased Food production. The philosophy of providing grant aid is in the field of basic human need requirement.
- Dispatch of JOCV (Japan Overseas Cooperation Volunteers): Under it, Volunteers ' are dispatched to work in various development field hand-in-hands with the recipient countries counterparts.
- Disaster Relief Cooperation: This includes emergency relief upon request as well as short and long-term cooperation, as warranted.
- Development study it covers from master plan studies on technical subject to other types of feasibility studies.
- Immigration.

The Japan overseas Cooperation Volunteer (JOVC) was established in 1995 as an agency under the ministry of Foreign Affairs for providing official technical assistance programs to developing countries. Japan Overseas Cooperation Volunteers was introduced in Nepal as the eleventh host country, in accordance with the exchange of notes between the governments of Japan and His Majesty's Government of Nepal on February 2, 1970. Since then about 838 young Japanese volunteers have shared their technology in the development activities of the kingdom of Nepal at the request of different Ministers and departments of his Majesty's government of Nepal. The office of JICA and JOCV in Nepal were amalgamated into one roof in 1983. Since then resident representative of JICA Nepal office has been made responsible for carrying out both the activities together.

II) **Overseas Economic Cooperation Fund (OECF):**

It was established in 1961 and is responsible for providing loans to public cooperation. The objective of OECF is to contribute to industrial development and economic stability of the developing countries. The fund is provided as bilateral loan on the government level. This fund has provided loan

assistance to Kulekhani Hydropower project. OECF namely cost of loan to underdeveloped countries when the countries income surpasses a per capita GNP to US&100(Sigdel, Bamdav 1997, Japanese Economy and economic Diplomacy).

III) Export Import Bank of Japan (EIBJ):

Export Import Bank of Japan was established in 1951 in Japan, which is a public Cooperation oriented bank. The bank extends loans with a grant element to less than one percent to foreign government. The object of the bank is to promote economic exchange between Japan and other countries. It provides assistance to both developed and developing countries for the economic cooperation only part of business undertaken by the bank.

IV) Other organization:

Besides JICA, OECF, EIBJ there are also other organizations that provide economic as well as technical cooperation from Japan to the developing nations. These are namely:

- The Overseas Fisheries Cooperation Foundation (OFCF),
- Japan Overseas Development Cooperation (JODC),
- Metal Mining Agency of Japan (MMAJ)

There are also some private organizations also which are helping developing countries with the economic cooperation. These are:

- The association for promotion of industrial cooperation (APIC)
- International Development Centre of Japan (IDCJ)
- Association for overseas technical Scholarship (AOTS)
- The internal Management Association of Japan (INAI)
- The OISCA industrial Development Body etc.

5.8 Japanese Aid Distribution by Sector

Over the period of last three decades, the volume of Japanese aid to Nepal has increased and it covers all the major sectors of our economy. An analysis of the Japanese assistance of the last one and half decades confines that the volume has steadily gone up and the areas of cooperation are in the line with the priority as set by successive development plans.

Japan has made available generous assistance to almost all the sectors of our economy. Major beneficiaries of the Japanese ODA are agriculture, industry, water supply, power and communication sectors. From the fiscal year 1970 to 2006 sector wise Japanese assistance to Nepal are shown in the table below.

Table 5.5
Sector wise Japanese grant Assistance to Nepal (1970-2005)

Sector	Amount in 000'J¥	Percent
Agriculture	34336900	20
Irrigation	1202000	1
Food Aid	6918440	4
Other-Agriculture Sector	1456000	1
Health	4708000	3
Education	15370000	9
Drinking Water	13173000	8
Other-Social Sector	2253000	1
Civil Aviation	4831000	3
Communication	12946000	8
Energy	1339800	8
Road/bridge	20322000	12
Other-infrastructure Sector	8108000	5
Disaster Mitigation	7072000	4
DRF	19528678	11
NPGA	3300000	2
Other	1296680	1
Total Commitment	170,219,696	100

Source: Japanese Embassy in Nepal; MOFA

Figure 5.2

Sector wise Japanese Grant Assistance to Nepal

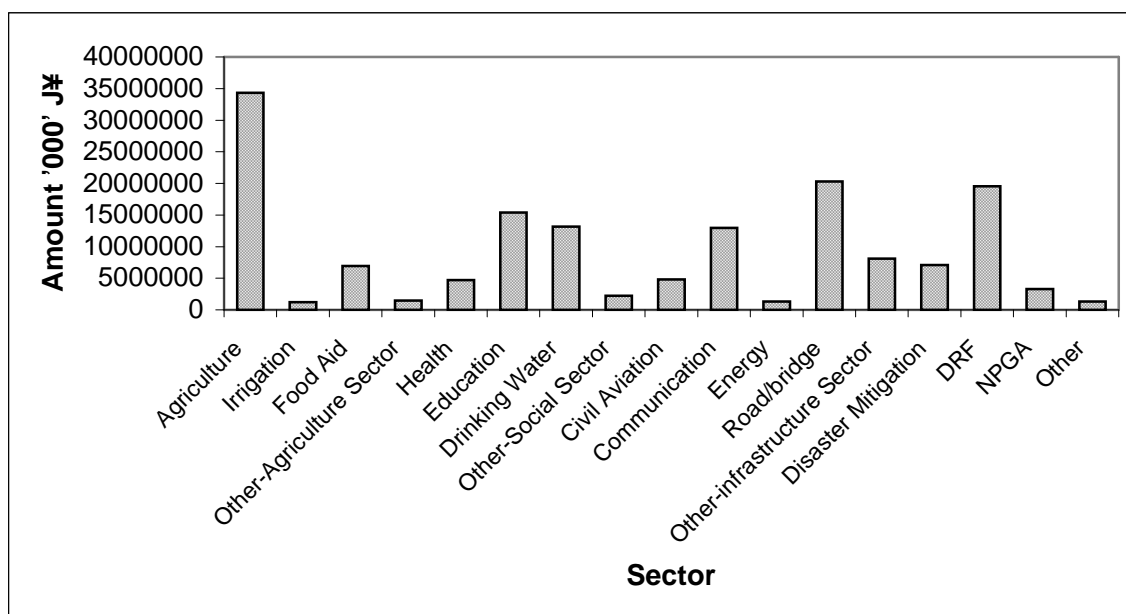


Table 5.5 shows that the Japanese grant assistance has gone powered in agriculture, energy and water supply, education and transport etc. program in Nepal. Japanese aid was concentrated on the agriculture sector, which is 20 percent of total Japanese Aid. Second priority has gone onto Road/bridge, which is 12 percent of total Japanese Aid. Third priority has gone upon DRF sectors, which is 11 percent of total Japanese Aid. Likewise the priority has gone upon education communication energy, Drinking water, other infrasture-sector, Disaster mitigation, health, food Aid, etc. respectively. In the recent years, the Japanese Aid has concentrated on Agriculture and Road/bridge. Besides this, the Japanese Aid also concentrated on education and health.

5.9 Scholarship Program

The government of Japan has provided scholarship to Nepali students for education in Japan. The government of Japan provides Monkukagasho scholarship to students from across the world every year. More than 100 Nepalese students have already received this kind of scholarship and pursued their higher studies in Japan and they are now contribution to the task of nation

building in Nepal. The government of Japan started providing technical training to Nepalese since Japan joined the Colombo plan in 1952.

Scholarship has been provided for university students by the government of Japan since the early 1960s, few years after the establishment of diplomatic relations. As a result, many Nepalese got the scholarship and returned home after completing their study/ research and technical training in Japan. Nepalese who have become acquainted with Japanese society and cultural have organized the Japan university students Association of Nepal (JUSAN) and JICA Alumni Association of Nepal (JAAN) respectively and between the people of two countries. JUSAN has been conducting a wide range of cultural and academic exchange activities. As a part of active people to people exchange between the two countries, sister city and sister village relations were established between Katmandu with Matsumoto of Toyama prefecture in 1989.

In addition, Pokhara and Kamagane of Nagano prefecture signed an agreement of international cooperation and friendship between the two cities in April 2001. After the affiliation, both cities have been jointly improving the pane in Pokhara as Pokhara Kamagane Friendship pane as a symbol of friendship by providing a design for pane as well as support project to beautify the area.

Grant Assistance for Grassroots' Projects (GGP)

The Japanese government offers financial assistance for development project designed to meet the diverse needs of developing countries under this scheme previously known as Small Scale Grant Assistance (SSGA), GGP scheme supports projects proposed by various bodies such as non-governmental organizations (NGOs) and local government authorities. The scheme has acquired an excellent reputation because it provides flexible and timely support to development projects at the grassroots level.

The GGP scheme provides non-refundable financial assistance to NGOs, hospitals, primary school and other non-profit associations to help for implementing their development projects. As of March 28, 2003 government of Japan has extended GGP grant assistance to 89 different grassroots project. The Japanese government has provided Rs 313492567 from JFY 1992 to JFY 2005. The detail about grant assistance to GGP is shown in Table- 5.6.

Table 5.6
Grant Assistance for Grassroots Projects (GGP) to Nepal During
JFY 1992-2005

JFY	No. of projects	Total in US\$	Total in ¥	Total NRs
1992	3	93,451	12,055,179	4,311,785
1993	6	107,820	1,3154,040	5,281,379
1994	3	189,360	20,072,160	9,494,511
1995	9	472,138	46,269,587	29,298,921
1996	17	462,285	48,056,613	28,115,664
1997	5	145,016	15,516,782	9,149,059
1998	5	185,494	21888,292	11,166,153
1999	8	299,600	35,952,000	20,507,768
2000	8	461,360	48,442,800	33,760,752
2001	16	129,873	138,990,111	98,691,717
2002	9	429,495	52,832,305	33,442,337
2003	7	281,727	33,658,918	20,963,333
2004	2	129,408	14,234,880	9,309,188
2005	6	384,941	4,1271,110	27,177,199
Total	104	4,974,213	541,944,707	337,669,766

Source: Embassy of Japan, Kathmandu, Nepal.

A number of Japanese NGOs are actively engaged in diverse areas of development activities. These NGOs have been rendering services to the community people at the grass root level even in the hilly areas far from the

city. The above-mentioned activities have brought the people of both countries closer and have further strengthened friendship and understanding.

As a part of Japan's ODA to Nepal, the government of Japan provides grant assistance for grass root project mainly to be implemented by the local government and NGOs, for socio economic development as grass root level. The following are the outlines of the projects, which were completed and handed over to Nepal in recent days.

A) Construction of new building of Shree Krishna School, Palpa.

Shree Krishna Secondary School located in a remote part of Western Nepal has been providing education to the students of popaldanda and pholsigkot VDCs of Palpa district for over three decades. However, as the school building was in a dilapidated condition with insufficient classroom and space it had not been able to provide accommodation to all the students. The new two-storied building equipped with 12 classrooms is expected to create a more conducive study environment. It is hoped that the school will be able to fully utilize classroom for further enhancement of education for the children of the region. Furthermore it is also anticipated that the school will contribute to the socioeconomic development of the local communities. This project required NRs 2305964 approximately was executed by Jhekan development committee and was handed over in February 2003.

B) Construction of health post in Gongolia, Rupendehi.

The basic healthcare and medical facilities in the rural areas of Nepal are not sufficient. It is quite apparent that the minimum level health services need to be strengthened in view of the existing inadequacies, which are prevalent in the health facilities in remote areas. In order to partially address these inadequacies in the rural health services, the government of Japan was extended financial support for the construction of a new health post building at Gongolia VDC in Rupendehi district. The new health post building equipped with operation room

and other facilities is expected to provide adequate environment and space for providing primary health care services to the people of this region. The newly health post will be able to address the communities demands of health care more efficiently .this project required approximately of NRs 2512815 and handed over in February 11,2003 and it was executed by B.P. rural services centre.

C) Japan's Assistance for construction of Disabled children education and Training centre in Pokhara Municipality: August 17, 2007

The government of Japan has decided to extend financial assistance of eighty- thousand, three hundred and forty six us Dollars (US \$ 83,346); equivalent to approximately five million four hundred and ninety thousand Nepali Rupees (NRs 5,490,000) to the Shishu Bikes Kendra of Nepal Jesuit society for the Implementation of the project for construction of Disabled children education and Training Centre in Pokhara Municipality in Japan's FY 2007. This financial assistance is extended under the Grant Assistance for Grassroots Human Security project (CUP) scheme of the Government of Japan.

A Grant contract to this effect was sign and exchanged today between his Excellency Mr. Tsutomu Hiraoka, Ambassador of Japan to Nepal Jesuit society Pokhara.

Speaking at the ceremony, H.E. Hiraoka mentioned Japan's assistance to Nepal in achieving sustainable development through poverty alleviation and ensuring human security. He explained the difficult circumstance of disabled people in Nepal and lauded the remarkable contribution of the Shishu Bikas Kendra for the betterment of welfare of disabled children. Furthermore, he expressed his hope that disabled children will live in dignity and that the grant will play a symbolic role in further strengthening the relationship between Japan and Nepal.

D) Japan's Assistance for improvement of Phedi-Kotyang-Ghumaunec Rural road in Kavrepalanchok District August 31, 2007.

The government of Japan has decided to extend financial assistance of eighty thousand, nine hundred and twenty three US Dollars (US \$ 80,923), equivalent to approximately five million, three hundred sixteen thousand Nepali Rupees (NPR 5,316,000) to the committee for Restriction and maintenance of Phedi-Kotyang-Ghumaunechaur Rural Road for the implementation of the project for improvement of Phedi-Kotyang-Ghumaunechaur Rural Road Kavrepalanchok District in Japan's FY 2007. This assistance has been extended to the committee under the grant Assistance for grassroots Human Security Projects (GGP) scheme of the government of Japan.

A grant contract to this effect was signed and exchanged today between his Excellency Mr. Tsutomu HIRAOKA, Ambassador of Japan to Nepal, and Krishna Bahadur Tamang chairman of the committee for Restriction and maintenance of Phedi-Kotyang-Ghumaunechaur Rural Road, Kavrepalanchok.

The grant will be utilized for the improvement of a 10 KM road linking the above three VDCs construction work will be carried out with the participation of local people, and will benefit approximately 18000 people residing along the road. Originally, the farmers in the area were engaged growing Japanese seeds provided through the cooperation of a Japan NGO. The improvement of the road will enable easy transportation of the produce to markets and will contribute to the enhancement of living standard of the area.

E) Japanese Grant for the Detailed Design Study for the Improvement of Kathmandu-Bhaktapur Road: (September 5, 2007):

The government of Japan has decided to extend a grant up to forty-eight million Japanese Yen (¥ 48,000,000) approximately twenty-seven million two hundred and sixth thousand Nepalese Rupee (NRS 27,216,000) or equivalent to

four hundred and fourteen thousand US Dollars (US \$414,000) to the government of Nepal for the project for the improvement of Kathmandu-Bhaktapur road in Japan's FY 2007.

His Excellency, Mr. Tsutomu HIRAOKA, Ambassador of Japan to Nepal, and Mr. Vidyadhar Millik, secretary of the minister of finance, the Government of Nepal, signed and exchanged notes today on behalf of their respective governments. The grant extent to the government of Nepal is intended to be used to procure the services necessary for the detailed design study of the project.

The Details design study will be carried out to upgrade about 9.1 KM of the Kathmandu-Bhaktapur road section of the Araniko Highway expanding the existing two-lane road of four lanes. The Kathmandu-Bhaktapur road will be designed in such a way that it will serve not only as a road to ensure consistent transportation of goods and people between Kathmandu and Bhaktapur, but also to play an important road role linking Kathmandu valley with the eastern Terai via the Sindhuli road, which connects Banepa-sindhuli-Bardibas. The Sindhuli road is now under construction with grant assistance of the government of Japan. It is already benefiting several million people residing along the completed section of the road.

It is expected that the Kathmandu–Bhaktapur road, for which the detailed design study is conducted, will help save time and reduce fuel expenses considerably for road users, who are currently facing very congested traffic situation especially during rush hours. The study will take into consideration advanced traffic engineering so as to help protect ordinary citizens from accidents and health hazards. It is expected the road to be proposed by the detailed design study will bring a positive impact to the Nepalese economy thus contributing to the poverty alleviation efforts of the government of Nepal. It will also improve access to health and education institutions for the residents along the road.

On the occasion, H.E.Hiraoka expressed his hope that this assistant will prove to be yet another milestone in further strengthening the friendly relations between Japan and Nepal. Similarly, the amount provided by Japan in various projects in JFY 2006 is shown in table 5.7.

Table 5.7
Grant Assistance for Grassroots' Human Security Projects for the
Period JFY 2006

S.N.	Project Name	Recipient Institution/NGOs	Amount US\$
1	Construction of AMDA Mechi Hospital	Association of Medical Doctors of Asia (AMDA), Nepal	83,137
2	Construction of Bhimshengola Secondary School	AIUEO Circle Association (ACA) Japan	102,250
3	Extension of Academic Building of Nursing Campus, Maharajung Institute of Medicine, TU	Nursing Campus, Maharajung Institute of Medicine, TU	84,895
4	Construction of Sub-Health Post Buildings in Kavrepalanchok District	Adventist Development and relief Agency (ADRA) Japan	76,866
5	Establishment of intensive Care Home for HIV/AIDS Patients	Nava Kiran Plus	83,035
6	Construction of Sindhuli Cold Storage House for Junar	Sindhuli Junar Development Association	86,230
7	Construction of Students' Hostel for Dhulikhel Medical Institute	Dhulikhel Medical Institute	182,660
8	Project for Forest Conservation in remote Village in Myagdi and Parbat Districts	Institute for Himalayan Conservation (IHC)	51,890
		Total	750,963

Source: Embassy of Japan, Kathmandu, Nepal

5.10 General Introduction to Japan's ODA to Nepal

There have been close and friendly relationship between Japan and Nepal for many years. This land locked country, Nepal having no direct access to the sea, is one of the least developed countries in south Asia. In this severe condition the needs of her socio-economic development remain. Since the restoration of democracy in 1990, Nepal has been striving towards economic development through the process of liberalization; it has been a privilege to Japan to participate in the economic development programs of Nepal since 1954. Grant and loan aid started soon after the opening of the embassy in Katmandu in 1968. At present Japan is one of the top donors to Nepal and involved in every important sector of the country. In Japan's fiscal year 2005, the government of Japan had provided a total assistance of ¥286.8 billion that constitutes grants ¥169.9 billion loan ¥88.9 billion and technical assistance ¥29.9 billion mainly in the following sectors.

Human Resources Development: Realizing the fact that human resources development is indispensable for the self-supporting development of Nepal, and efficient management and utilization of natural resources, the government of Japan has been providing technical assistance to Nepal in implementing and managing technical cooperation projects. Japan has dispatched 1,424 technical experts and 873 Japan overseas cooperation volunteers (JOCV), dispatching of senior volunteers to Nepal started in 1995 and so far 57 of them have served in different areas in Nepal. Similarly, the number of Nepalese trainees accepted in Japan was 3,491 (as of JFY 2005).

Social sector (Health and Education): considering the fact that Nepal has a high incidence of diarrhea. Caused by unclean water which is also one of the causes of the country's high infant mortality rate, Japan has extended cooperation for safe drinking water supply, maternity health care, providing polio vaccine and other medicinal care programs for the last few years. The construction of T.U. Teaching hospital, National Tuberculosis centre and assistance to Kanti

children's hospital are the main projects that have been implemented successfully under Japan's ODA. Recognizing the vital Importance of providing educational opportunity for children as the prerequisite and back bone to socio- economic development of the country, the Government of Japan has provided grant assistance for the construction of approximately 5,500 classrooms in primary schools under BPEP I (94-98) and BPEP II (99-02).

Agriculture Development: Agriculture is the main sector in Nepal consisting of nearly 40% of GDP and 80% of the population live on agriculture. However, the traditional farming method is still prevalent which isn't cost effective and is not conducive to substantially improving the living standard. Under such circumstances, the agriculture sector has not been able to contribute greatly to the economic growth of the country since 1977. Japan has been providing assistance.

In such areas as improving agriculture infrastructure, in improving high value agriculture products as well as in the development and diffusion of agricultural production technologies in order to increase employment opportunities and to raise the income level of farmers. Starting with the cooperation in Janakpur agriculture development project (JADP), Japanese assistance has been valuable in the field of fisheries, sericulture, horticulture and irrigation.

Economic infrastructure: Japan attaches importance to the improvement of basic infrastructure such as in areas of power generation, roads, airport, bridges, water supply facilities, telecommuting captions etc. the construction of Sindhuli road is expected to greatly increase the economic activity of the common people. Japan has also provided extensive loan assistance to Nepal such as for the Kulekhani (I and II) hydro-power station, cement industry and Melamchi water supply project. Recently the project for the improvement of the intersections in Katmandu under the grant aid was completed for further facilitating smooth vehicular movement in the city.

Environmental conservation: In view of Nepal 's population growth and poverty, the country has a considerable problem of environmental degradation, particularly deforestation in this regard; Japan gives priority to assisting the proper utilization of natural resources for environmental improvement and disaster mitigation. Japan has extended assistance for projects in the areas of disaster mitigation, forest /watershed conservation, studies of few lakes in Pokhara as well as community development.

Cultural Grant Aid: As one of the international exchanges in the field of cultural, since 1977 Japan has been providing cultural grant aid to Nepal with the aim of promoting cultural, educational and research activities including the preservation of cultural assets and relics and the holding of cultural performances and exhibitions. The recent aid in this scheme are micrographic equipment to Nepal National library, dubbing equipment and educational programs to Nepal Television, display equipment to Buddhist Art Gallery at National Museum, Sport equipment to National sports council and printing equipment to Royal Nepal Academy.

CHAPTER-VI

IMPACT OF JAPANESE AID IN NEPAL

6.1 Empirical Analysis

Foreign aid is said to have effects on economic growth and overall welfare of country. Larger amount of foreign aid becomes necessary for further growth of the economy. In recent years, Japan has been the largest bilateral development partner of Nepal and the economic supremacy of Japan has been reflected in its high level of assistance.

This chapter makes an attempt to analyze the effect of Japanese aid to the gross domestic product (GDP) of Nepal. Thus, the basic starting point is the examination of a direct relationship between the GDP and the amount of Japanese aid. Different lagged and un-lagged models have been used in order to analyze the impact. Models have been estimated in simple and log linear forms. In all statistical analysis, numbers in parenthesis below the coefficient of dependent variables indicate their respective t-value. All regressions in this chapter are conducted by using SPSS program.

$$(1) \quad Y_t = 347207.6 + 4.68 F_t$$

(5.06) (3.05)

$$R^2 = 0.715, \text{ Adj. } R^2 = 0.692, F = 23.432, D-W = 0.152$$

(t and F parameters at 95% significance level)

Equation (1) shows a positive relationship between real GDP and Japanese Aid inflow. The beta coefficient is 4.68 implying that one million changes in Japanese Aid has product 4.68 million changes in the GDP. Though it seems impossible but logically it has give the approximate figure. As change in GDP is not simply explained by the change in Japanese Aid, it is also explained by other variables. The value of R^2 and adj. R^2 show the tolerable

good fit of the model. Adj. R^2 (=0.692) implies that 69.2% change in GDP is explained by the change in Japanese aid and rest 30.8% change is due to the other variables. F and t parameters show the best theoretical fit of the model at 95% significance level. However, D-W statistics shows the positive autocorrelation among the error terms.

Impact of Japanese Aid with one year lag:

$$(2) \quad Y_t = 296162.6 + 8.44F_{t-1}$$

(4.347) (5.546)

$$R^2 = 0.512, \text{ Adj. } R^2 = 0.50, F = 30.75$$

(t and F parameters at 95% significance level)

In equation (2) GDP is regressed with the foreign aid in the lagged one year. The beta coefficient is 8.44 implying the one million changes in Japanese aid has produced 8.44 million changes in the GDP. The value of R^2 and adj. R^2 show the tolerable good fit of the model. Adj. R^2 (=0.50) implies that 50% change in GDP is explained by the change in Japanese aid and rest 50% change is due to the variables other than Japanese aid. F statistics shows the best fit of the model at 100% significance level. t statistics also supports the best fit of theoretical distribution of the parameters at 95% confidence level.

It can be seen that equation (2) has high R^2 and adjusted R^2 explaining that Japanese aid has greater impact upon GDP with one year lag.

Impact of Japanese aid with two year lag:

$$(3) \quad Y_t = 271576.3 + 15.20 F_{t-2}$$

(4.332) (7.334)

$$R^2 = 0.726, \text{ Adj. } R^2 = 0.707, F = 11.52$$

(t and F parameters at 95% level of significance)

In equation (3) GDP is regressed with the Japanese Aid two year lag. The beta coefficient is 15.20 implying that one million changes in Japanese Aid has produced 15.20 million changes in the GDP. The value of R^2 and adjusted R^2 show the tolerable good fit of the model. Adjusted R^2 (0.707) implies that 70.7% change in GDP is explained by the change in Japanese Aid and rest 29.3% change is due to the variables other than Japanese Aid. F-statistics shows goodness of fit the model at 100% significance level t-statistics also supports the best fit of theoretical distribution of the parameters at 95% confidence level.

Keeping the R^2 and Adjusted R^2 in mind, the one year lag model is not as strong as the two year lag model. It can be inferred that Japanese Aid has been primarily made with short gestation period of two year.

Following relation has tried incorporating one year lag and two year lag data of independent variable that is Japanese aid.

$$(4) \quad Y_t = 264455.7 + 2.835 F_{t-1} + 14.17 F_{t-2}$$

(3.41) (5.17) (3.89)

$$R^2 = 0.793, \text{ Adj. } R^2 = 0.781, F = 54.8$$

(t and F parameters at 95% significance level)

Log linear model

$$(5) \quad \log Y_t = 8.316 + 0.437 \log F_t$$

(21.633) (4.298)

$$R^2 = 0.795, \text{ Adj. } R^2 = 0.767, F = 100.18, D-W = 1.4$$

Equation (5) is double log linear mode. The beta coefficient explains the elasticity of Nepal's GDP with respect to the Japanese aid. The elasticity coefficient is 0.473 implies that 1% change in Japanese aid results into the

0.473% change in GDP of Nepal. The adjusted R^2 value is 0.767 implying that 76.7% change in GDP is explained by the change in Japanese Aid while rest 23.3% change is explained due to other factors. F-test is as high as 100.18 giving the best fit of the model at 0% significance level. t-statistics show the best theoretical fit of the parameters at 5% significance level.

6.2 Micro-performance

The flow of Japanese assistance in Nepal is quite high in comparison with the total aid flow, i.e., Japanese aid is increasing gradually year by year and the amount of Japanese assistance in the development expenditure of Nepal is quite discernible. It is also true that Japanese aid has been more effective for the economic development of Nepal. Japanese assistance to Nepal has been directed to agriculture, power generation and distribution, health, transportation, education, communication, development of human resources, environmental preservation and so forth. Japanese assistance covers almost 40 percent of development field of Nepal (Sidgel, 1997). Hence, Japanese assistance has occupied large field of Nepal's development.

A. Impact on agricultural development

It is known fact that Nepal is agriculture-based country. Therefore, without developing this sector, it is not possible to develop the Nepalese economy. Almost 80 percent people are engaged in agriculture. Table shows that 20 percent of the Japanese grant assistance from the fiscal year 1970 to 2006 has been disbursed to the agricultural sector. This shows that Japan is also taking interest in agricultural development of Nepal.

In Nepal, agriculture farming depends upon monsoon and irrigation facilities have not been adequate. About one thousand pumps sets with ring machine, casting pipes, casting pipes, shallow tube wells program had fuelled the shortages in the districts of Teri through Japanese grant aid in 1970. Japanese technical assistance in the agricultural sector has encouraged the

farmers to use modern improved farming techniques. Nepalese farmers are benefited by the teaching and volunteer's services of Japanese agriculturists in different districts of Nepal. Japanese assistances has brought demonstrates effect and extension of agricultural techniques of Nepalese farmers through the Japanese agricultural program in Janakpur agriculture development project. It has provided new ideas of farming, storing and selling. The status of farmers of those regions is changing. Japan also provided agricultural experimental farming in Rapti Zone by way of providing equipments and experts under the Colombo plan.

B. Impact on economic and social infrastructure

Improvement of technology, good network of transport system and setting of basic and key industries are necessary in the process of development. This means that infrastructure development is the foundation of economic development. . There should be a direct effect to infrastructure development in order to attain the faster rate of economic growth. Japan is also playing a vital role in building infrastructure for the creation of economic and social development of Nepal. For the development of socio- economic infrastructure, Japan has been providing machinery and equipments for the construction of Sindhuli road. Kulekhani hydroelectric project is also a vital project undertaking of Japanese assistance in the infrastructure development of Nepal, which has been constructed under Japanese assistance on power transmission and distribution system in Kathmandu has brought regulatory in electricity.

In transportation improvement project, Japan has been providing buses, trucks and repair shops, which have been very useful for the social life of Nepalese people in Kathmandu valley. Japanese contribution to medium wave radio broadcasting network improvement project has played a significant role for the communicative development of Nepal. Radio Nepal was able to broadcast in medium wave only after completing this project. For the educational development, Japan has been providing materials and equipments

for construction of primary schools in remote regions of Nepal. Japan has also provided assistance to Janak educational material centre and Tribhuvan University. Japanese assistance to Tribhuvan university teaching hospital is a landmark in social development of Nepal. Japan has also been providing higher-level education in medical science. Due to this assistance, basic status of Nepalese people is changing gradually.

C. Impact on industrial development

Industrialization is a prerequisite for economic development as the history of advanced country shows. Industrialization is also necessary in order to provide employment to the underemployed and unemployed in the agricultural sector. Thus, industrial development is essential for the Nepalese economy in order to attain the rapid growth rate. It is necessary to reduce the increasing pressure of population in agriculture sector by diverting it from agriculture to industrial sector. Most of the big industries have been established with the help of foreign assistance in Nepal.

Japan also cooperated in the field of industrial development. Nepal industrial development cooperation (NIDC) and Udaypur cement factory are the major industries, which have been benefited by Japanese assistance. Japan is also contributing in the development of different small scale industries in Nepal. Japan is conducting cottage industries development projects for the hand made paper and ready made garments. They are also providing ideas for the development of grass root projects in Nepal.

D. Impact on capital formation

Capital formation or accumulation is regarded as one of the important and principal factors in economic development. Capital is an essential tool for financing the development budget in developing countries. Japan has been providing both financial and human capital to Nepal. Japanese training facilities have been used in different fields of development. Similarly, Japanese

financial assistance has been used in different field of development. Japanese training facilities have contributed to building human capital formation. In the field of capital formation, Japan has been providing different types of assistance in the form of grant, loan, commodity and technical assistance as well as equipment and machinery in order increase the capital. The nature of Japanese aid has multidimensional effects.

Japan has emerged as the most important bilateral aid donor for the development of Nepal. Role of Japanese aid has become very important after 1975. Japan has provided different types of cooperation through JICA, OECF, EIBJ and other institutions to Nepal. Japanese assistance has been increasing, which consists of grant assistance, loan assistance and technical assistance to Nepal. Among them grant is very important for Nepal. Japanese assistance to Nepal covers mot of the sectors, such as agriculture, power generation, health, transportation, education, communication, human resource development environment preservation.

The impact of Japanese aid in Nepalese economy and society has been found very significant. but foreign aid should utilized only for those sectors and project which are more vital for the socio- economic enlistment of the society form which the majority of the population, the poor section in particular, may be benefited.

6.3 Macro Performance

The macro perspective of analyzing the role of Japanese aid is considered as an instrument to fill up the resource gaps of the recipient economies. This resource gap can be defined in terms of gaps in savings, foreign exchange and technological skills.

Saving gap

Growth of a country depends upon investment and the less developed countries face a serious problem in providing the requisite savings. The gap between level of investment and saving is so wide that it is generally not possible to achieve sustainable growth rate, if Nepal is entirely dependent on own domestic savings. It is in the contest that foreign aid seems to be almost on indispensable condition of development. The function of aid, as viewed by the recipient countries is to raise the investment rates by supplementing domestic savings with foreign resources to an extent the additional saving generated is large enough to provide the basis for a significant increase in the marginal saving rate.

In the Nepalese economy, savings and investment gap has been increasing subsequent year foreign aid is considered as an instrument of saving gap.

Foreign exchange gap

Domestic savings are not perfect substitute of financial outlays beyond a point on account of what is described as the structural balance of payments problem of the less development countries. As most of the less developed countries conspicuously lack the requisite equipment, know how and skills, a given rate of development will imply a certain volume of imported goods. It is in this contest that foreign aid helps in meeting out the exchange gap. The role of external assistance in Nepal on the overall foreign exchange situations has been extremely favorable. In this situation, foreign aid has played the important role in Nepal. However, the remittance obtained from the foreign employment has held this situation to some extent recently.

Technology gap

The analyses of the savings gap and the foreign exchange gap imply the needs for capital aid. The less developed countries like Nepal are not only poor in capital resources but also deficient in technical know how and skills. It is mainly due to poor technology and underdeveloped infrastructure that the absorptive capacity in the less developed countries is low.

By technology we generally mean combination of technical knowledge and skills. Given that higher level of technology implies more efficient utilization of resources and there fore, a higher out put. The problem of raising the level of technology is one of the pressing needs of the less developed countries. Foreign aid fulfils the deficiency of technical know how and skill in the form of technical assistance.

CHAPTER-VII

FINDINGS, CONCLUSION AND RECOMMENDATIONS

7.1 Findings

Nepal is one of the least developed countries of the world with a very poor economic and social infrastructure for development. It suffers from a serious resource gap with low saving and low investment. Foreign aid plays an important role in the economic and social development of an underdeveloped country. Capital is considered a crucial factor in economic development. This is brought out by various growth models, which have been put forward by economists since Adam Smith as well as the actual experiences of economic development. But precisely this capital is scarce in underdeveloped countries. Foreign aid helps development by meeting this requirement. It also helps the underdeveloped countries in their endeavor for development by providing the necessary modern technology.

In the context of the Nepalese economy, which is characterized by structural bottlenecks, large fiscal and external deficits and significant imbalances between savings and investment ratios, the role of foreign aid is particularly significant. The major findings arrived at from the analysis of the available data are listed below;

1. Sectoral disbursement of assistance from 1991/92 to 2005/06

a) Transport, power and communication	44 percent
b) Agriculture, irrigation and forestry	20 percent
c) Social services	33 percent
d) Industry and commerce	3 percent

2. Trends indicate that bilateral aid has declined from 46.1 percent of total aid in 1991/92 to 25.7 percent in 1998/99 to 14.7 percent in 2000/01. However, it has been small increased to 34.7 percent in 2005/2006.
3. Multilateral aid increased from 53.9 percent of total aid 1991/92 to 74.3 percent in 1998/99; it has reached its peak in 2002/03 (86.8 percent) average share of multilateral aid is 57.6 in total aid between 1991/92 to 2005/06.
4. Trend analysis clearly shows that proportion of loan has been increasing consistently with commensurate decline in grants, which imply an increasing debt burden.
5. Aid disbursements have been much lower than the commitments by huge proportion except for 2005/06 when disbursement is higher than commitment.
6. Japanese aid to Nepal is in the form of grant loan, and technical assistance. Technical assistance is being provided in the form of equipment supply, training to Nepalese personnel and dispatch of Japanese experts to Nepal.
7. The total amount of Japanese aid given to Nepal is increasing with the passage of time. The growth is found in both loan and grant assistance. However, the proportion of Japanese loan assistance to Nepal is more than that of the grant assistance.
8. In Nepal, Japan has extended its assistance to grass root projects in various sectors.
9. Japanese aid has covered various sectors of Nepalese economy and health, education, agriculture, hydropower, and industry appear as the major sectors of Nepalese economy consuming Japanese aid.

During the course of this study, the Foreign Aid Division of Ministry of Finance's data management system was found to be extremely weak. Under such an environment, it is almost impossible to know how foreign aid is being utilized or how much duplication is taking place. There is, thus, example scope for miss-utilization of foreign aid resources. With such a large share of development expenditure being financed through foreign assistance, a complete lack of consistent data and information systems and a virtual absence of consistent data and information systems and a virtual absence of monitoring and evaluating systems are bound to have serious negative consequence on the development over the last five decades. This has had direct impact on the low rate of saving and investments, low rate of internal revenue mobilization and high inflationary pressure in the economic. The government's inability to bring deficit financing under control has also affected economic performance. This has in turn resulted in low productive capacity, high level of unemployment and underemployment, low labour productivity, a weakened competitive edge, and rosin in personal income, which are strongly reflected in high level of poverty and low level social development.

A possible reason for the low disbursement of grant assistance can be attributed to the government inability to come up with matching funds, which has in turn, resulted in the low absorptive capacity of foreign assistance. However, even more important is the weak institutional capability of the government machinery, which is not even enabled during five decade of developing. If government is seriously committed to the efficient utilization of foreign assistance, concerted efforts committed to the efficient utilization of foreign assistance, concerted efforts should be directed towards maximum use of grant assistance by strengthening its institutional capabilities and fulfilling its matching fund commitments. Donors should be pressurized to match their commitments of grant aid with actual disbursements. This will contribute, to a large extent in reducing the debt burden, especially for future generations.

Development activities will be considerably diluted with out strong macro and micro linkages. Without such linkages, the utilization of foreign assistance will continue to be fraught with inefficiencies and mismanagement. However, it is extremely important to have adequate information to monitor and evaluate the use of foreign aid to ensure that macro and micro linkages are properly in place. There are glaring lacunae in this regard and this has greatly affected the management of the country development activities.

Both the government and the donors should be accountable to their respective constituents regarding the proper use of foreign assistance. It is evident that under the existing environment, such accountability on the part of both government and the donors are sorely missing. It is very important to generate public awareness so that pressure groups in both the donor countries and the recipient government can effectively police the efficient use of foreign aid and ensure accountability. With out this, a very large part of foreign assistance will continue to be wasted a dependency syndrome will be entrenched in the country, and the people will continue to be deprived of the benefits supposed to be derived by the foreign aided development as they are pushed further down the poverty line with large new entrants joining every year.

With out complete transparency, unrestricted access to information and consistent and correct statistics, it will be impossible to ensure efficient utilization of aid resources into those sectors where aid funds can benefit both the country's development and the people for whom development is initiated in the first place. This calls for an urgent need to develop a transparent information management system. Only then, macro/micro linkages in the use of aid resource can be clearly established and accountability of the governments and the donors alike is ensured, to attain these objectives, it is also imperative to have an effective autonomous monitoring and impact evaluation system.

However, because of the political instability and absence of the government controlling mechanism (i.e. parliament), the loan might likely to be misutilized and because of the weakened security position most of the development projects have already been centered in the district headquarters and the urban areas of the country. In such a situation, the government and its machinery are unable to absorb development expenditure. Hence, it is questionable that whether the government should seek more loans or nor.

7.2 Conclusion

For last fifty-five years, foreign aid has remained an integral part of the Nepalese economy. There has been many fold increase in the quantum of aid flows to Nepal. During this period, there has been some improvement in the physical and socio-economic indicators of Nepalese economy. Numbers of hospitals and health posts have increased. Numbers of schools, teachers and students have also added up. Same hold true in the case of the government supply of drinking water, irrigation, electricity and road access. Nevertheless, all these facilities remain beyond the reach of a large mass of the people. One can definitely say, except for irrigation, most of the foreign aided projects concentrated on urban sector, where barely one tenth of the populations live.

In 1997, 235 out of 360 projects are found to be directly or indirectly related with the urban areas. As foreign aided projects bring in advanced technology and sophisticated products catering to the needs of urban population, the economic dualism is found to increase further. Moreover, the foreign aid, directly or indirectly has been increasing the gap between the rich-poor people, rural-urban and hill-terai. High salary paid to people working in foreign aided projects and leakages in the project implementation are some of the reasons for the expansion of haphazard urbanization. The difference in salary payment between project and government employees has been inspiring the latter towards corruption.

From the research study it has been found that Nepalese economy can be compared with a sinking boat, If we look at different aspects of Nepalese economy, it shows the gloomy pictures of it, the country is already in debt trap; debt per head is more than Rs. 12000, Loan's amount is increasing overwhelmingly in comparison to the grant component. Saving-Investment gap has been increasing over the years, still a larger number (about 31 percent) of people live below the poverty line. On the other side foreign aid component is declining.

It is being seen that, the political parties in the government evaluate themselves and think themselves successful if they beg more from the donors without rethinking its effect and impact on the whole economy, it has paralyzed the very core of the administrative machinery and institutionalized corruption in the political administrative system. Similarly, the absorptive capacity is not satisfactory; only about 60 percent of the total committed amount of foreign aid has been disbursed.

Foreign aid in Nepal appears to be less effective on focusing on the needs of majority of the people and also maintain accountability; it has been unable to address the specific problems of equity and justice and to ensure propriety in the process of aid utilization. Aid underutilization has been the serious problem than the availability of the foreign aid. After the change of each government the key staffs of aid-funded projects are also changed immediately. The motive behind this may be for the corruption.

Thus, Nepal is facing a difficult situation, the country can neither promote the economy without aid, nor it has been able to avoid the risk of becoming the victim of aid intoxication, Meanwhile, aid for long periods has created a separate social group, namely, the rental class. So, a clear vision strong will and committed government is required to increase internal capability of generating resources and to mobilize internal resources in activities

which complement the foreign aided projects in expanding the productive base of the economy.

7.3 Recommendations

Although foreign aid did not substantially contribute to the economic development of Nepal, the importance of foreign aid cannot be denied, because the domestic resources mobilization of Nepal is still very low to fulfill the investment requirement. In this respect new vision and ways of aid utilization have to be thought from both donor and recipient countries, Especially recipient countries have to revitalize foreign aid resources by considering aid not as a 'free lunch'.

Questions can be asked as to whether the quite significant aid volumes should not have produced more results, particularly among the most disadvantaged, the rural population that still represents the overwhelming majority of Nepalese people. Why has the nation failed to develop even after receiving so much foreign aid? In the first place, the country has taken foreign assistance as a consumer item rather than a capital investment item. Whatever it receives, it consumes. Secondly, it has taken foreign assistance as something that is available free of cost, like air and water; this attitude has given rise to various inconsistencies, which are obstructing the process of its development. The country must not, therefore, determine the philosophy of development through reliance on external source of finance.

If the country learns from its previous mistakes and weakness, improvement can be brought without any doubt. Following recommendations have been put forward based on above analysis.

- Foreign aid should be used in a transparent manner with proper accounting system of recording the movement of foreign aid. A scientific accounting and audit system, an effective Management information

system, a hierarchy specifying rights, duties and responsibilities the like should be in place.

- In the view of increasing external debt, Foreign aid should be accepted in accordance with the development need and the development priority of the country instead of accepting anything that is available from the external sources.
- More over, in our context most of the aid money is used to procure costly equipment, vehicles and building and to pay consultancy fees to the technicians/consultants brought along by the donors themselves, for that unnecessary expenses must be cut down and local and rational consultants should be appointed in order to minimize their cost.
- Nepali contractors and laborers should be employed as far as possible in construction works of foreign aided projects.
- Selected projects should be implemented with full commitment so that they can generate sufficient resources to pay back the aid.
- People's participation should be increased when a project is launched.
- Trust and co-operation among donors, government and society should be built.
- The priority should be given to grants rather than loans.
- At present most of aid comes with strict conditions. Therefore the conditions should be properly studied and only those projects, which are favorable for the country, should be chosen. So bargaining capacity must be increased to make foreign aid more favorable.
- Waste and ineffective implementation of development programs should be reduced.
- More researches should be carried in future in order to assess the impact of overall foreign aid and country specific foreign aid in Nepal.
- Project management efficiency should be improved and enhanced.
- The country has to concentrate itself on the projects, which can generate backward and forward linkages.

- Heavy dependency on foreign aid should be slowly reduced by better mobilization and efficient utilization of domestic resources.
- Most of Japanese aid is disbursed in infrastructure not giving concern to socio-economic up-liftment of Nepalese people. So there is need to provide assistance to benefit poor people.

APPENDIX-I
THE MEMBER OF NEPAL AID GROUP- NEPAL
DEVELOPMENT FORUM

Asian development bank

Denmark

France

Germane

International fund for agriculture development

Italy

Japan

Netherlands

Norway

Organization for economic co- operation and development

Saudi fund for development

Switzerland

United Kingdom

United nation development program

United States of America

World Bank

*Norway participated as an observer (Paris, April 1996) and expressed its intention to become a permanent member of Nepal aid group in future.

APPENDIX-II

LIST OF BILATERAL, MULTILATERAL DONORS AND INGOS

Bilateral

Australia, Canada Denmark, France, Germany, Italy, Israel, Japan Netherlands, Norway, Switzerland, unites states of America, United Kingdom, Finland and republic of Korea.

Multilateral

ADB, European union , FAO, IDA, IFAD, ILO, LMF, ITU, UNCDF, UNDP, UNESCO, UNFPA, UNICEF, UNIFEM, UNV, UPU,WFP, SFD, UNCHR, AND WHO.

INGOs

Action AID, CARE international, communication cultural promotion foundations, international Nepal fellowship, Lutheran world federation, PLAN international, Save the children / USA, save the children/ UK, save the children / Norway (Redd Baran), the Asia foundation , united mission to Nepal, world neighbor Neumann foundation, Sir Edmund Hillary foundation, Canadian Lutheran word relief, comrose international institute, Jesuits International South Asia partnership, DISVI, Save the children / New Zealand and trans-Himalayan aid society.

APPENDIX-III

GDP AND JAPANESE AID AT NOMINAL PRICE

(Rs in Million)

Fiscal Year	GDP	Japanese Aid
1991/92	144931	1757.4
1992/93	165262	3501.4
1993/94	191540	1571.9
1994/95	209974	6928.3
1995/96	239388	5295.5
1996/97	269570	4994.4
1997/98	289798	1746.6
1998/99	330018	2894.5
1999/00	366251	8394.1
2000/01	394052	7090.3
2001/02	406138	5326.2
2002/03	437546	2802.2
2003/04	474129	1494.6
2004/05	433538	2726.3
2005/06	582948	1727.8

Source: Economic Survey, 2006/07

APPENDIX-IV

TECHNICAL OPERATION EXTENDED TO NEPAL (IN DETAIL)

JFY	Technical cooperation	Acceptance of Trainees	Dispatch of JICA Experts	Dispatch of Mission Members	Dispatch of JOCV Volunteers	Dispatch of Senior Volunteers	Provision of Equipment	Project type Technical cooperation	Implementation of Development Study
	(In million Yen)	(Persons)	(Persons)	(Persons)	(Persons)	(Persons)	(In million Yen)	(Number of Projects)	(number of Studies)
Up to 81	5928	621	211	313	233		1,506.0	5	9
1982	1198	64	25	49	18		323.0	4	3
1983	1297	74	31	85	23		217.0	4	3
1984	1214	69	17	90	45		255.0	2	2
1985	927	73	44	70	40		115.0	4	3
1986	1610	71	46	116	26		271.0	3	3
1987	1889	82	42	143	26		320.1	4	5
1988	1928	93	50	112	31		355.1	4	4
1989	1553	99	38	108	33		184.4	5	5
1990	1677	80	20	109	15		247.9	4	7
1991	2190	106	49	152	28		115.0	5	7
1992	3537	114	61	211	26		556.0	6	10
1993	3336	142	98	209	16		535.0	7	9
1994	2350	149	90	72	28		365.0	8	4
1995	2591	171	84	139	41		312.0	7	4
1996	2792	174	74	107	27		225.7	6	3
1997	2343	166	60	114	30		230.7	6	9
1998	2318	163	63	110	34		215.67	6	2
1999	1934	160	63	104	13	5	169.20	5	7
2000	1989	153	44	178	21	4	110.59	3	2
2001	1840	128	43	131	14	5	129.25	3	3
2002	1777	155	25	106	27	11	106.95	4	3
2003	1512	133	44	51	25	13	80.96	2	0
2004	1770	147	57	86	40	13	52.16	1	1
2005	1418	102	45	74	13	6			
Total	52916	3491	1424	3039	873	57	6998.03	23	53

Source: Japanese Embassy

APPENDIX-V

REGRESSION

Variables Entered/Removed

Model	Variables Entered	Variables Removed	Method
1	JAPANAID	.	Enter

a All requested variables entered.

b Dependent Variable: GDPNEW

Model Summary

	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
Model					R Square Change	F Change	df1	df2	Sig. F Change	
	.845	.715	.692	13157.3882	.714	.093	1	13	.765	.152

a Predictors: (Constant), JAPANAID

b Dependent Variable: GDPNEW

ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	1617575952.917	1	1617575952.917	23.432	.076
	Residual	225067339435.083	13	17312872264.237		
	Total	226684915388.000	14			

a Predictors: (Constant), JAPANAID

b Dependent Variable: GDPNEW

Coefficients

		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
Model		B	Std. Error	Beta		
1	(Constant)	347207.617	68559.931		5.064	.000
	JAPANAID	4.687	15.335	.845	3.057	.076

a Dependent Variable: GDPNEW

Variables Entered/Removed

Model	Variables Entered	Variables Removed	Method
1	JAPT_1	.	Enter

a All requested variables entered.

b Dependent Variable: GDPNEW

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics	R Square Change	F Change	df1	df2	Sig. F Change	Durbin-Watson
1	.722	.512	.500	130515.3399	.423	30.800	1	13	.059	.164	

a Predictors: (Constant), JAPT_1

b Dependent Variable: GDPNEW

ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	5239614013.430	1	5239614013.430	30.759	.059
	Residual	221445301374.570	13	17034253951.890		
	Total	226684915388.000	14			

a Predictors: (Constant), JAPT_1

b Dependent Variable: GDPNEW

Coefficients

Model		Unstandardized Coefficients	Std. Error	Standardized Coefficients	t	Sig.
1	(Constant)	296162.575	68134.292		4.347	.001
	JAPT_1	8.449	15.234	.152	5.546	.059

a Dependent Variable: GDPNEW

Variables Entered/Removed

Model	Variables Entered	Variables Removed	Method
1	JAPT_2	.	Enter

a All requested variables entered.

b Dependent Variable: GDPNEW

Model Summary

	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
Model					R Square Change	F Change	df1	df2	Sig. F Change	
1	.853	.726	.707	126561.4335	.081	11.521	1	13	.303	.283

a Predictors: (Constant), JAPT_2

b Dependent Variable: GDPNEW

ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	18453561543.069	1	18453561543.069	11.521	.030
	Residual	208231353844.931	13	16017796449.610		
	Total	226684915388.000	14			

a Predictors: (Constant), JAPT_2

b Dependent Variable: GDPNEW

Coefficients

		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
Model		B	Std. Error	Beta		
1	(Constant)	271576.276	62694.390		4.332	.001
	JAPT_2	15.207	14.167	.285	7.334	.003

a Dependent Variable: GDPNEW

Variables Entered/Removed

Model	Variables Entered	Variables Removed	Method
1	JAPT_2, JAPT_1	.	Enter

a All requested variables entered.

b Dependent Variable: GDPNEW

Model Summary

	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
Model					R Square Change	F Change	df1	df2	Sig. F Change	
	.892	.793	.781	13156.5143	.836	54.760	2	12	.592	.259

a Predictors: (Constant), JAPT_2, JAPT_1

b Dependent Variable: GDPNEW

ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	18958470342.323	2	9479235171.162	54.760	.006
	Residual	207726445045.677	12	17310537087.140		
	Total	226684915388.000	14			

a Predictors: (Constant), JAPT_2, JAPT_1

b Dependent Variable: GDPNEW

Coefficients

Model		Unstandardized Coefficients	Std. Error	Standardized Coefficients	t	Sig.
		B		Beta		
1	(Constant)	264455.750	77369.881		3.418	.005
	JAPT_1	2.835	16.602	.051	5.171	.087
	JAPT_2	14.174	15.921	.266	3.890	.039

a Dependent Variable: GDPNEW

Variables Entered/Removed

Model	Variables Entered	Variables Removed	Method
1	LOGFT	.	Enter

a All requested variables entered.

b Dependent Variable: LOGYT

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change in R Square	F Change	df1	df2	Sig. F Change	Durbin-Watson
1	.892	.796	.768	.6273	.796	100.185	1	13	.097	1.438

a Predictors: (Constant), LOGFT

b Dependent Variable: LOGYT

ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	7.277E-04	1	7.277E-04	100.185	.010
	Residual	5.121	13	.394		
	Total	5.122	14			

a Predictors: (Constant), LOGFT

b Dependent Variable: LOGYT

Coefficients

Model		Unstandardized	Std. Error	Standardized	t	Sig.
		Coefficients		Coefficients		
		B		Beta		
1	(Constant)	8.316	5.092		21.633	.001
	LOGFT	.473	.403	.401	4.298	.097

a Dependent Variable: LOGYT

APPENDIX-VI

THE MAJOR EVENTS IN CHRONOLOGICAL ORDER

- 1899: Arrival in Nepal by the first recorded Japanese visitor Ekai Kawaguchi, a Buddhist monk stayed in Nepal on his way to Tibet.
- 1902: Departure of group of Eight Nepal students for higher studies in Japan.
- 1912: Bunko Aoki enters Nepal on his way to Tibet.
- 1933: Kousetsu Nouse, an artist who became well known for his Buddhist paintings, is invited to Nepal by General Kesher Shamsheer Rana
- 1936: prof. Syunichi Amanuma visits Nepal to inspect building after the great earth quake.
- 1951: Exchanges between the Japanese Nepal sports delegates at the first Asian games in New Delhi
- 1952: Eizaburo Nishibori received an audience with king Tribhuvan.
- 1956: Sejiro Yuoshizawa, ambassador to India attended the coronation of king Mahendra.
- 1956: Successful conquest of mensal by Japanese expedition's team led by Yuko Maki.
- 1956: Establishment of diplomatic relations between Nepal and Japan (Exchange of notes on September-1).
- 1960: Official visit to Japan by king Mahendra and Queen Ratna.
- 1960: Official visit to Nepal by crown prince Akihito and Princess Michiko.
- 1962: Dr. Iwamura starts medical service at the united mission hospital in Patan.
- 1965: Establishment of royal Nepalese embassy in Tokyo.
- 1967: Crown prince Birendra goes to Japan to study at TOKYO University.
- 1968: Establishment of Japanese embassy in Katmandu.

- 1968: Hidemichi Kira appointed as the first resident ambassador to Nepal.
- 1970: Prince and princess Hitachi attend the wedding ceremony of the crown prince Birendra.
- 1970: King Mahendra and queen Ratna visit Japan to attend expo'70.
- 1974: Janakpur agriculture development project initiated under the Japanese technical cooperation program.
- 1974: Ghanendra Bahadur Karki, Minister for foreign affairs of Nepal, visited Japan.
- 1975: Crown prince Akihito and Princess Michiko attend the coronation of king Birendra.
- 1975: Junko Tabei becomes the first woman to reach the summit of Mt. Everest.
- 1975: Crown Prince Akihito and Princess Michiko attend the coronation of King Birendra.
- 1975: Their Royal Highness Prince Gyanendra and Princess Komal visited Japan.
- 1977: Parliamentary Vice Chairman for Foreign affairs Keiwa Iida paid an official visit to Nepal.
- 1977: Ichiro Hatouama, Minister for Foreign affairs of Japan paid an official visit to Nepal.
- 1978: State visit to Japan by then Majesties King Birendra and Queen Aishwarya.
- 1980: Parliamentary vice Minister for Foreign Affairs Kaoru Aichi visits Nepal.
- 1982: Completion of Kulekhani-I Hydro Power Project (with a Japanese government loan).
- 1984: Completion of construction of Tribhuvan University Teaching Hospital under the Japanese Technical Cooperation Program.

- 1985: Princes Chichibu visits Nepal.
- 1987: Crown Princes Naruhito pays a visit to Nepal.
- 1988: A Japan-China-Nepal expedition successfully scaled Mt. Everest.
- 1989: HRH Prince Gyanendra attends the funeral ceremony of the late Emperor Hirohito.
- 1990: Nepali-style garden exhibited during Osaka Expo'90.
- 1991: Japanese Parliamentary Esection Observation Mission, led by president Keiwa Ikuda, Japan-Nepal parliamentarians Friendship league visited Nepal.
- 1991: Finance Minister Ryutaro Mashimoto visits Nepal.
- 1991: Acting president of Nepali Congress Krishan Prasad Bhattarai visited Japan.
- 1994: Inaugural flight by Royal Nepal airlines between Katmandu and Osaka.
- 1994: Completion of the construction of Udayapur cement factory with a Japanese government loan.
- 1995: Deputy prime Minister and Minister for foreign affairs Madav Kumar Nepal pay an official visit to Japan.
- 1995: Dr. Prakash Cahandra Lohani, Minster for foreign affairs, visits Japan.
- 1995: Completion of the construction of Bagmati Bridge under Japanese grant in aid program.
- 1996: King Birendra inaugurates the international Buddhist research centre in Lumbini, constructed by the Reiyukai international.
- 1996: Completion of Baha- Bahi temple renovation program in paten.
- 1997: There Highness Prince and princes Aishino visit Nepal.
- 1998: former prime minister Sher Bahadur Devba visits Japan.

- 1998: Prime Minister Giraja Prasad Koirala pays an official working visit to Japan.
- 1998: Section I of Sindhuli road construction project completed.
- 1998: Japanese parliamentary delegation led by vice speaker of the house of representations Kozo Watanabe visits Nepal.
- 1999: His Majesty King Birendra confers Suprasiddha Prabala Gorkha Dakshin Bahu to former Prime Minister Ryutaro Hashimoto of Japan.
- 1999: Embassy of Japan commemorates the centennial of Nepal- Japan relations.
- 2000: Nepali parliamentary delegation led by Rt. Hon. Tara Nath Ranabhat, speaker of the House of Representatives visits Japan.
- 2001: JILCI (JAAN Information, languages and culture institute), the autonomous Japanese language institute under JICA was established in Nepal.
- 2001: Members of “volunteer work camp” form Yashima high schools, visited Nepal as a study tour.
- 2001: Katmandu valley, ten-intersection project started with grant aid of Japan.
- 2002: This year is marked the completion of a century of the first Nepal students in Japan in 1902.
- 2002: seven intersections in Katmandu city were completed.
- 2002: Japanese alpinists hit the new record of climbing Mt. Everest.
- 2002: A portrait of reverend Ekai Kawaguchi was printed on a postal stamp.
- 2003: parliamentary secretary for public Management, Home affairs, posts and Telecommunication, Rokuzaemou Yoshida visits Nepal.
- 2003: Chief judge Kedar Narh Upadhaya visits Japan.
- 2003: Vice- speaker of the lower house of representative Chitra Lekha Yadav visits Japan.

- 2003: Minister for information and communication Ramesh pandey visits Japan.
- 2004: Chief of army staff pyarjan Thapa visits Japan.
- 2004: Chief of commission for investigation of abuse of authority Surya Nath Upadhaya visits Japan.
- 2004: Member of House of Representatives and secretary general of the Japan-Nepal parliamentary friendship league Tadahiro Matsushita visits Nepal.
- 2005: Parliamentary secretary for foreign affairs Katsuyki Kawai visits Nepal.
- 2005: Home minister Purna Bahadur Khadka visits Japan.
- 2006: Major events tentatively planned for the 50th Anniversary of the establishment of Japan-Nepal diplomatic relation.
- 2006: Handover of medical clinic van and Medical equipment to Nepalgunj Medical College.
- 2006: Grant Assistance for Grassroots Human Security Projects (GGP) is a scheme to provide financial assistance for the implementation of social and economic development and emergency humanitarian assistance projects being under taken by non-profit making local organizations and institution in developing countries and regions.
- 2007: Japan Assistance for construction of a Hostel for students of Dhulikhel Medical institute.
- 2007: Japan provides cultural Grant Aid to Nepal Television.
- 2007: Japan's Assistance for improvement of Phedi-Kotyang Ghumaunchar Rural Road in Kavrepalanchok District.
- 2007: Meeting between Mr. Masahiko Koumura, Minister for Foreign Affairs, and Mrs. Sahana Pradhan, Minister for foreign affairs of Nepal.
- 2007: Japan Handover semi- transport Ballot Boxes and security seals to Nepal.

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