

PUBLIC FINANCE BUDGET BRIEF

EXPENDITURE REVIEW

Draft. For discussion only

The urgency to develop credible and inclusive budgets for
a happy and prosperous Nepal for all

SPGE, UNICEF NPL CO

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ABBREVIATIONS AND ACRONYMS

a.e	Actual (realized) expenditures
b.e	Budget(target) estimate/allocation
Bill.	Billion
CG	Central Government (federal)
COFOG	Classification of functions of government
FY	Fiscal Year
IMF	International Monetary Fund
LG	Local Government (Palikas)
MoEST	Ministry of Education, Science and Technology
MoHP	Ministry of Health and Population
MoF	Ministry of Finance
NPC	Nepal Planning Commission
NPR	Nepalese Rupee
NRB	Nepal Rashtra Bank
NSO	National Statistical Office
PG	Provincial Government
SDGs	Sustainable Development Goals
UNICEF	United Nations Children's Fund
USD	United States Dollar
%	Percent

1 PREFACE

The manner in which the government of Nepal raises revenues and spends resources not only have a significant impact on the but also profoundly affects the lives of children in Nepal. This brief examines the overall FY 2023/24 expenditure allocations in the budget based on data primarily from Redbooks and budget speeches (Ministry of Finance, various years) and the most recent Economic Survey (Nepal Rashtra Bank, 2022). This is one of a series of briefs produced each year. The objective is to provide a concise summary of the latest budget data while highlighting trends.

The organization of this budget brief is as follows. It begins with a brief synopsis of the current economic scenario and presents the objectives of the budget. This is followed by a summary of key findings. Then it examines trends in allocations and expenditures for the last six fiscal years. It then draws out the expenditure allocations to the top ministries. This is followed by a discussion of the functional classification of the budget (COFOG) for several years where trends in allocations to different sectors are analyzed. It then focuses on allocations to the three social sectors comprising education, health and social protection. Details of the functional classifications for the social sectors are also provided. This is followed by a discussion on budget allocations and federalism. Finally, the focus shifts on allocations towards the Sustainable Development Goals (SDGs). This is apt, given that the midpoint for reaching the SDGs have arrived and it would be useful to examine allocations towards the SDGs. The conclusion summarizes the key challenges and contains some suggestions for future action to meet the multiple challenges that remain.

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2 ECONOMIC BACKGROUND IN FY 2022/23

A brief synopsis of the economic scenario in fiscal year (FY) 2022/23 leading up to the budget for FY 2023/24 is provided below (MoF, Budget Speech 2023/24).

- Elections for the federal, provincial, and local levels, and the President and Vice-President, had been successfully conducted for the second time following the promulgation of the Constitution of Nepal. This has generated new optimism among the people.
- In the last fiscal year real economic growth at base prices was estimated to be 2.16%. Economic growth has remained low due to a slackening of economic activities, which resulted from structural and some policy-related reasons. The Nepali economy was on a path to recovery from the COVID-19 pandemic, but the war in Ukraine had adversely affected global supply chains and spiked the prices of cereals and oil. Reduced investment due to high interest rates, low levels of capital expenditure, and a decline in aggregate demand have caused further slackness in economic activities. Policies aimed at containing inflation and improving foreign exchange reserves have added to this effect.
- As of mid-April of 2023 (FY 2022/23), inflation stood at 7.76%. Although inflation is gradually moderating, it remains above the desired limit (7%). Price increases in food, dairy products, household consumer goods, imported goods, and the depreciation of the Nepali currency against the US dollar have put pressure on consumer prices.
- As of mid-April of April 2023 (FY 2022/23), the balance of payments registered a surplus of Nepalese Rupee (NPR) 180.17 billion. Foreign exchange reserves seem adequate to cover 11 months of imports of goods for and 9.4 months import of goods and services (NRB, 2023).
- Remittance inflows have increased by 24.2% to NPR 903 billion (NRB, *opcit.*). However private sector investment has not increased as expected nor has been the inflow of foreign investment.
- The revised total government expenditure for FY 2022/23 was estimated to be NPR 1,504.99 billion, accounting for 83.90% of the original allocation. Of this total government expenditure, the revised current expenditure, capital expenditure, and financing are estimated to be NPR 1,043.39 billion (88.18%), NPR. 258.34 billion (67.91%), and NPR 203.26 billion (88.29%), respectively. The revised target for revenue collection in FY 2022/23 was estimated to be NPR 1,179.84 billion, which is 84% of the initial target and 5.95% lower compared to the actual collection of

FY 2021/22. The performance of revenue collection remained weak, primarily due to import restriction policy and the economic slowdown.

- General government expenditures are increasing. Around NPR 1,280.25 billion was allocated in FY 2022/23 to manage committed expenditures, such as salary, allowances, social security, fiscal transfers, administrative expenses, and increasing debt repayment liabilities. This amount is calculated to be 73.10% of the total budget. Therefore, resource management for development programs is under pressure as a significant share of the total budget must be allocated for essential expenditure.
- The revised estimate for foreign grant and loan amounts to NPR 38.46 billion and NPR 170.54 billion, respectively. The level of foreign aid mobilization was lower than expected, primarily due to weak project implementation performance. The revised estimate for internal loan mobilization in the last FY was Rs. 256 billion.
- The total public debt stock as of mid-April 2023 stood at NPR 2,134.32 billion, consisting of internal debt (NPR 1,063.67 billion) and foreign debt (NPR 1070.65 billion).

As stated in the Budget Speech for FY 2023/24, **the objectives of this year's budget are centered around 17 goals:**

- To attain broad, sustainable, and inclusive growth by invigorating the economy.
- To ensure qualitative social development, along with security and justice.
- To boost the morale of the private sector by creating an investment friendly environment, and to alleviate poverty by generating income and employment opportunities.
- To maintain macroeconomic stability.
- To fortify federalism and uphold good governance.
- To augment the effectiveness of public expenditure through budgetary reforms.
- Development of agriculture, energy, and tourism.
- Promotion of investment, industrial development, and trade balance.
- Advancement of the social sector and enhancement of social security.
- Construction of high-quality physical infrastructure.
- Promotion of digital and green economy.
- Protection of the environment, climate change mitigation, and disaster management.
- Development of human resources and job creation.
- Reform of the financial sector.

- Strengthening of fiscal federalism and enhancement of service delivery.
- Reform in the public finance management system

3 SUMMARY OF FINDINGS

- Fiscal Year (FY) 2023/24 saw a 16% increase in the consolidated budget (budget estimate, b.e) over the previous fiscal years revised expenditures (r.e). The budget allocation for FY 2023/24 has been estimated at Nepalese Rupees (NPR) 1,751.31 billion. The growth rate consolidated budget allocations and expenditures has been higher over the last two fiscal years after reaching negative values in FY 2019/20 and registering near zero growth in FY 2020/21. When comparing allocations over the last two fiscal years, the budget allocation for FY 2023/24 is lower than the initial consolidated budget allotment for FY 2022/23 (NPR 1751.31 billion in FY 2023/24 compared to NPR 1793.84 billion in FY 2022/23).
- There are valid concerns regarding implementation given the historic context of under-spending. Due to constraints imposed by COVID-19, there was a large divergence between planned and actual expenditures in FY 2019/20 as the second half of that fiscal year felt the socio-economic shocks emanating from the COVID-19 pandemic and containment. The situation has improved considerably over the last two fiscal years although in FY 2021/22 actual expenditures (a.e) were 80% of the budget allocation and in FY 2022/23 actual expenditures were 84% of the budget allocation. This is a vast improvement compared to 70% utilization during FY 2019/20.
- Recurrent budget allocations for FY 2023/24 comprise 65% of allocations, a decrease from 69% observed in the last fiscal year. However, in nominal terms it rose from NPR 1,043.34 billion to 1,141.78. It is interesting to note that 'non-votable' or 'committed' expenditures are comprising a larger share of recurrent expenditures over time and have been squeezing out resources for development and other purposes. Capital expenditures are estimated at 17% of the total - unchanged from last year. Financial management (investment, loans and principal repayment) comprises 18%. Aside from grants to Provincial Governments (PGs) and Local Governments (LGs) that absorb about 23% of the budget, the largest share of recurrent expenditures are for civil service pensions and facilities as well as remuneration and benefits. Given the "ageing" of the civil service this situation creates the potential to crowd out other expenditures.

- In terms of functional allocations (COFOG¹ classifications) **general public service and economic services continue to be allocated more than 55% the budget.**
- Social sector allocations have remained within the range of 29 – 30% of the total budget. **Most notably there has been a decline in the per cent of the budget allocated for health which fell to 7% of the total in FY 2022/23 from 9% in FY 2021/22. In FY 2023/24 it dropped further to 6%.** Social protection expenditures increased from 12% to 13% of the total budget. **Although the Ministry of Education, Science & Technology has the highest allocation among all ministries, government allocations are well below its own commitment of 15%.** There has been a trend to "return to normal" as social sector allocations in terms of GDP and the total budget have declined over the last two fiscal years.
- **In terms of fiscal federalism, 76% of the budget is allocated to central government (CG), 7% to Provinces (PG) and 17% to Local Governments (LG).** Compared to the previous fiscal year, central government shares have decreased by 1% and exactly offset by an increase in the provincial share (by 1%). The share of the local governments (LGs) have remained unchanged. Given that most fiscal flows to LGs are in the form of conditional grants, it is not clear if the LGs have any autonomy in the design and implementation of their own local specific plans and programmes.
- Public expenditures have a direct bearing on the ability to achieve the Sustainable Development Goals (SDGs) and influence the lives of children. **In FY 2022/23, 73% of the budget is allocated for SDGs while 27% remains to be allocated for any SDG.** There is a notable decrease in the proportion allocated for SDGs from 79% in the last fiscal year. This translates to a notable increase in the amount not allocated for any SDGs. Compared to the priorities in FY 2021/22, SDG1 (End Poverty in all its forms), SDG2 (Zero Hunger), and, SDG16 (Peaceful, Just and Active Society) had increased allocations. On the other hand, there was a decline in SDG3 (Health Lives), SDG7 (Access to modern energy), SDG9 (Resilient infrastructure) and SDG11 (Sustainable cities and settlements). For all other SDGs allocations remained the same. Six SDGs are allocated less than 5% of the budget. There is scope to allocate more expenditures towards gender equality, sustainable clean water/sanitation, Cli-

¹ These are based on international norms defined in the Classifications of Functions of Government (COFOG) produced by IMF and World Bank to enable comparisons across countries.

mate change adaptation, Inclusive growth, and, Sustainable utilization of ecosystems. There also does not appear to be any allocation towards SDG 12: Sustainable consumption and production.

4 TRENDS

There has been a 16 percent increase in the consolidated budget allocation for FY 2023/24 when compared to the revised estimates for FY 2022/23. (Table 1).

Total consolidated fiscal expenditures (actual estimates, a.e) rose from NPR 1,015 billion in FY 2017/18 to NPR 1,111 billion in FY 2018/19. In FY 2019/20, as revenues collapsed, expenditures shrank to NPR 1,091 billion. In FY 2020/21 as the government unleashed programmes to contain the impact of COVID-19 expenditures rose by 10% to NPR 1,196 billion. As the economic recovery began in FY 2021/22, revenues increased, and actual expenditures rose to NPR 1,310 billion. In FY 2022/23, allocations were initially projected at NPR 1,794 billion. However the estimates for FY 2022/23 were revised (r.e) to NPR 1,505 due to revenue shortfalls. This marks the sixth year in a row that budget estimates were revised downwards.². The consolidated budget allocation for FY 2023/24 is estimated to be NPR 1,751 billion. This is 16% higher than the revised estimate for FY 2022/23, but slightly less when compared to the original consolidated budget allocation for FY 2022/23 (NPR 1,793.84 billion).

Table 1: Trends in expenditures

Fiscal Year	Expenditure	% Growth rate
2017/18 (a.e)	1,015.17	
2018/19 (a.e)	1,110.46	9
2019/20 (a.e)	1,091.13	-2
2020/21 (a.e)	1,196.68	10
2021/22 (a.e)	1,310.00	9
2022/23 (r.e)	1,505.00	15
2023/24 (b.e)	1,751.31	16

Expenditure data are in NPR Billion

The ratio of budgeted expenditures to Gross Domestic Product (GDP) has been between 30 – 25% of GDP since FY 2017/18. It fell from about 31% of GDP in FY 2018/19 to 28% of GDP in FY 2019/20 - a year when GDP also contracted sharply in Nepal along with expenditures. It fell further to 25% of GDP the year after in FY 2020/21 as GDP had started recovering but expenditures had not. Since then the expenditure to GDP ratio has risen and currently is estimated to be 28% of GDP for the current fiscal year. These GDP ratio's are lower than what was observed in the years leading up to the COVID-19 pandemic.

² But the revised figures were still 15% higher than the actual estimate for the previous fiscal year



Figure 1: Credibility of the budget: Allocations and expenditures (top, NPR Bill.), utilization rates (%), bottom)

4.1 Credibility of the budget

There has been a persistent deviation between actual expenditures and budget allocations since FY 2017/18 (Figure 1). Expenditure utilization became problematic during the COVID-19 pandemic and lock-downs and paid put the government's counter cyclical budget allocations. In the years after the pandemic, utilization rates have increased but still points to a large gap between allocations and utilizations.

- Budget utilization has remained below 85% since FY 2017/18. Given that international financial flows (aid and otherwise) hinge on budget credibility, there needs to be an improvement in budget utilization, especially for capital expenditures. Furthermore, as noted by the World Bank (2021), a large chunk of development project expenditures tend to occur in the last quarter of the fiscal year signalling a rush to deplete allocations.

- Critically, there are no reasons given by the government justifying the deviation between budgeted allocations and actual expenditures other than revenue shortfalls and lack of capacity at local levels. However, local levels are allocated under 20% of the budget and though lack of capacity could be critical, it is unable, on its own, to explain the significant deviations being observed. Hence there is some urgency to initiate expenditure tracking and monitoring to ascertain the sources and causes of deviations that have been observed. In tandem, the situation also points to the lack of credible costed programmes and targets that can realistically be achieved given that revenue shortfalls and capacity gaps will likely endure in the immediate future.
- During the pandemic, as the economies and revenues collapsed, a divergence of 30% between budgeted expenditures of NPR 1,533 billion in FY 2019/20 and actual expenditures of 1,091 billion that fiscal year. Budget utilization was over 80% prior to the pandemic, but dropped to 70% in FY 2019/20 before rising to 84% for the last fiscal year (based on revised estimates of FY 2022/23). There is a risk that given past trends (Figure 1), the proposed budget allocation for FY 2023/24 like previous years, would remain under-spent and require a mid-year revision of target expenditures.
- A recent survey of more than 50% of Palika Mayors in October 2022 (UNICEF, CFT 10 Palika Mayors) brought out some challenges and difficulties at local levels. These related to untimely release of funds, inadequate capacity to fulfil constitutionally mandated responsibilities, gaps in coordination and communication, and the lack of participation by communities and households in needs based planning and monitoring.

4.2 Allocation among major headings

The breakdown among major headings in the budget allocations for FY 2023/24 indicate (Table 2):-

- **65% (NPR Bill. 1141.8) would be for recurrent expenditures** of which about 15% are for salaries and benefits, another 10% for employee social benefits of the government. The highest recurrent expenditures are for conditional, equalization, matching and special grants to PGLGs that amount to 35% of total recurrent expenditures and 23% of total expenditures. Expenditures on social security comprise about 13% of recurrent expenditures. Interest on loans (domestic and external) absorb 9% of recurrent expenditures and 6% of the total budget allocation.
- **17% for capital expenditures (NPR Bill. 380.4)** a major portion of which is allocated for 'fixed assets receiving expenditures'

(93%) such as road and bridge construction, and, repairs, as well as non-residential building construction and purchase.

- **18% (NPR Bill. 307.5) for financial management** which includes investments (in domestic debentures and, domestic and international shares) as well as debt servicing (principal repayments). Debt servicing is a non-votable expenditure item (must be paid) and consists of approximately 13% of total budgetary allocations – higher in magnitude compared to the education or social protection budgets. Further, domestic debt has begun to replace external debt and to the extent that domestic interest rates are higher than external interest rates, this will exert a fiscal burden in the future.
- It is critical to note that recurrent expenditures for human development is being crowded out by an increasing share of committed expenditures such as salaries and benefits, interest and principal repayments for loans and employee social security benefits. These expenditures need to be constrained in order to allow resources to be freed for other development purposes.

Table 2: Heading-wise classification of Expenditures

Heading	% of heading	% of Total
Recurrent	1141.78	65%
Grants to PGLG	35%	23%
Salary & Benefits	15%	10%
Social Grants to agencies	10%	7%
Employee social benefits	10%	6%
Interest on loans	9%	6%
Social security	13%	8%
Capital	302.1	17%
Expenditure on fixed assets	93%	16%
Expenditure on natural assets	4%	1%
Contingency expenditures	3%	.4%
Financial Mgmt	307.5	18%
Investment in public enterprises	27%	5%
Principal repayment (Dom.)	59%	10%
Principal repayment (Int.)	14%	3%
Total	1,751.3	

Expenditure data are in NPR Bill. unless stated otherwise

4.3 Ministries with the top allocations

- Ministries with the top 5 budget allocations in FY 2023/24 budget allocations are: The Ministry of Finance-including debt repayment, miscellaneous expenditures, and civil service pensions, (32.41%), Ministry of Education, Science & Technology (11.27%),

Ministry of Home Affairs (11.09%) Ministry of Physical Infrastructure & Transport (7.67%), and the Ministry of Energy, water resources and irrigation (5%) as well as the Ministry of Health and Population (4.80%)

- The ministry of health and population saw a decline in the allocation in FY 2022/23 (5.75%).
- The allocation to MoF for repayment of loans and principal is almost 20% of the budget which is much larger than the health and education budget allocations combined for FY 2023/24. Similarly, the budget allocation for civil service pensions and facilities is also larger than the health budget allocation. Given the imminent "ageing" of the civil service work force in the near future, this category of expenditure will rise and has the potential to crowd out expenditures for other ministries.

These five/six ministries account for over 66% of budget allocations. The remaining 34% is allocated among 14 commissions, the offices of the President, Vice President, Province Chiefs, Federal Parliament, courts, Office of the Prime Minister and council of Ministers and eighteen remaining Ministries.

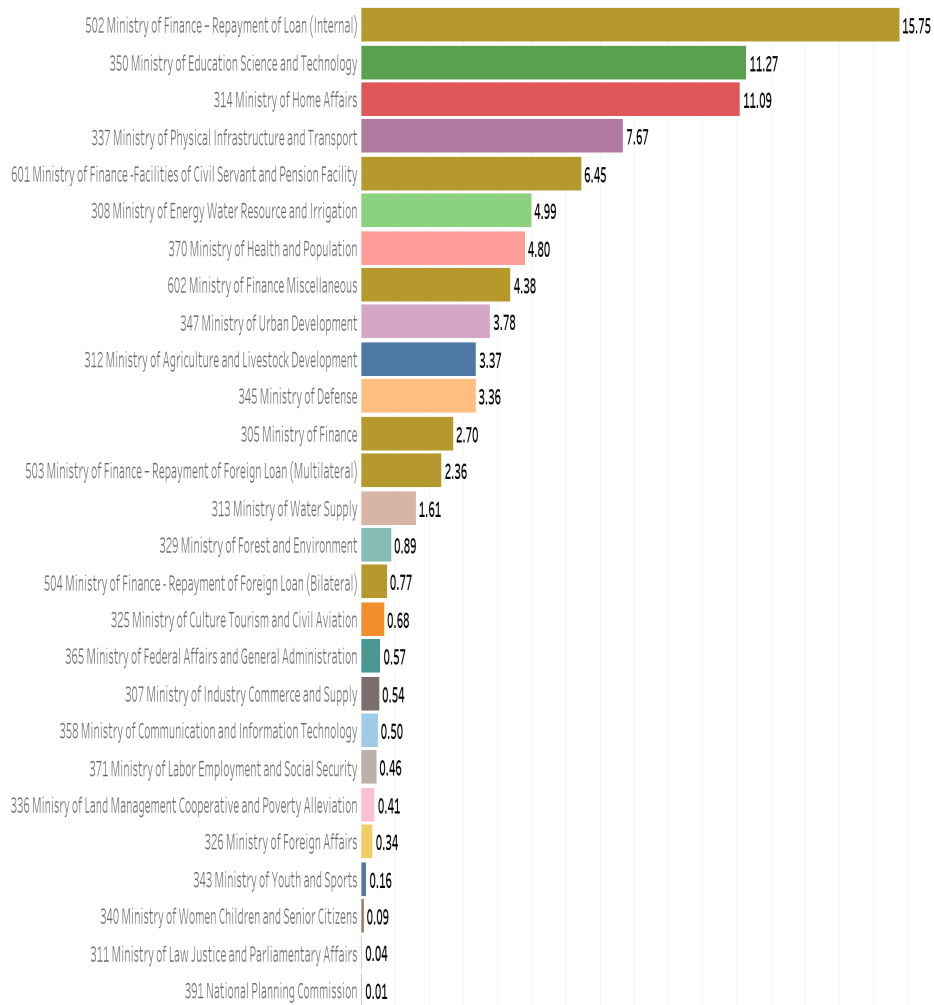


Figure 2: Ministry-wise allocation of FY 2023/24 budget (% of total)

5 FUNCTIONAL CLASSIFICATION

The breakdown of expenditures (FY 2022/23 budget estimates) according to the 'Classifications of the Functions of Government' (CO-FOG) along with the breakdown for the last several years is shown in Figure 3.

- From a functional perspective the largest share of expenditures is for general public services (which includes transfers and funding for the executive and legislative branches of the government) and the share allotted for this category has been increasing. The next largest share is for economic affairs (which consists of sectors such as transport, communication, agriculture, etc.) but its share has been declining. These two sectors have absorbed over 56% per cent of all expenditures in the last several fiscal years and this has tended to put a squeeze on allocations for other sectors such as health.

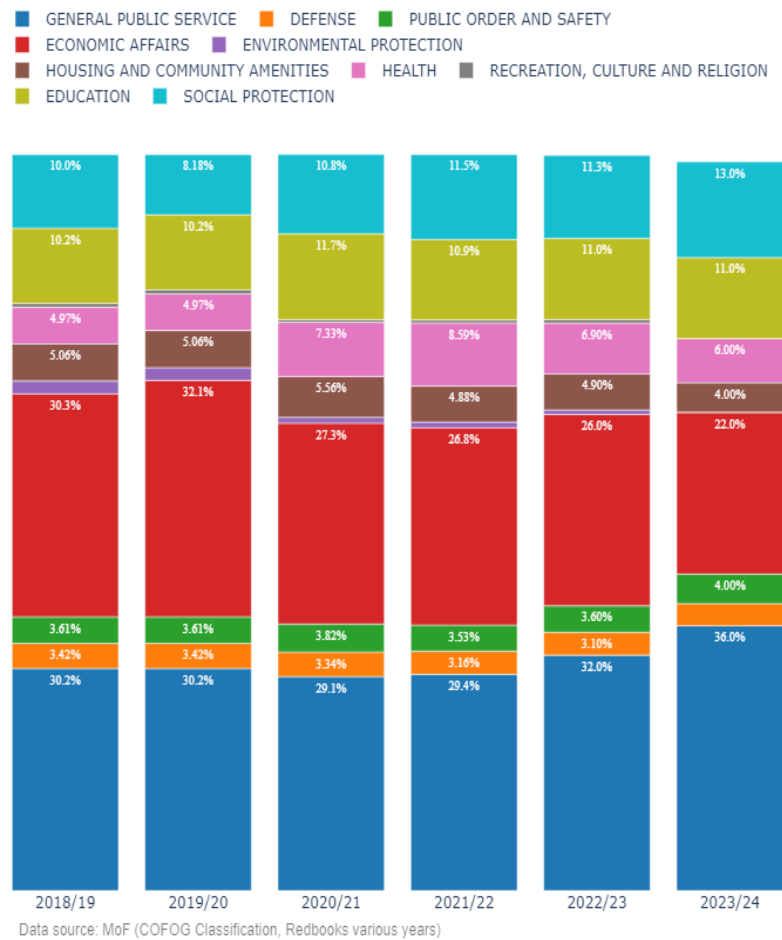


Figure 3: Functional Composition of the budget (%): FY 2018/19-2023/24

- Defense, and, peace and security, comprise another 6 – 7% of allocations. As a share of the total, allocations to the former have been decreasing while allocations for the latter have increased.
- The budget for environment protection which includes waste and sewage management among other things has been less than 1% of allocations for the last two fiscal years and on a declining trend.
- Housing and amenities (which includes drinking water supply among other things) has been allotted about 4% of the budget, significantly down from 5% observed the last fiscal year.
- Functional allocations for health, education and social protection amount to 29 – 30% of the total. There was an increase in social protection expenditures in FY 2023/24 which offset the decline observed for health while the education share remained constant.

5.1 Social Sector allocations

Isolating the social sectors (Health, Education and Social Protection) the data shows a strong increase in social sector allocations between FY 2017/18 and FY 2021/22. In particular, allocations towards the social sector increase sharply during FY 2019/20 and FY 2020/21 as a countercyclical COVID-19 response. Since then, the total social sector allocations have remained static, and for the first time in recent years declined slightly in FY 2023/24 (Figure 4).

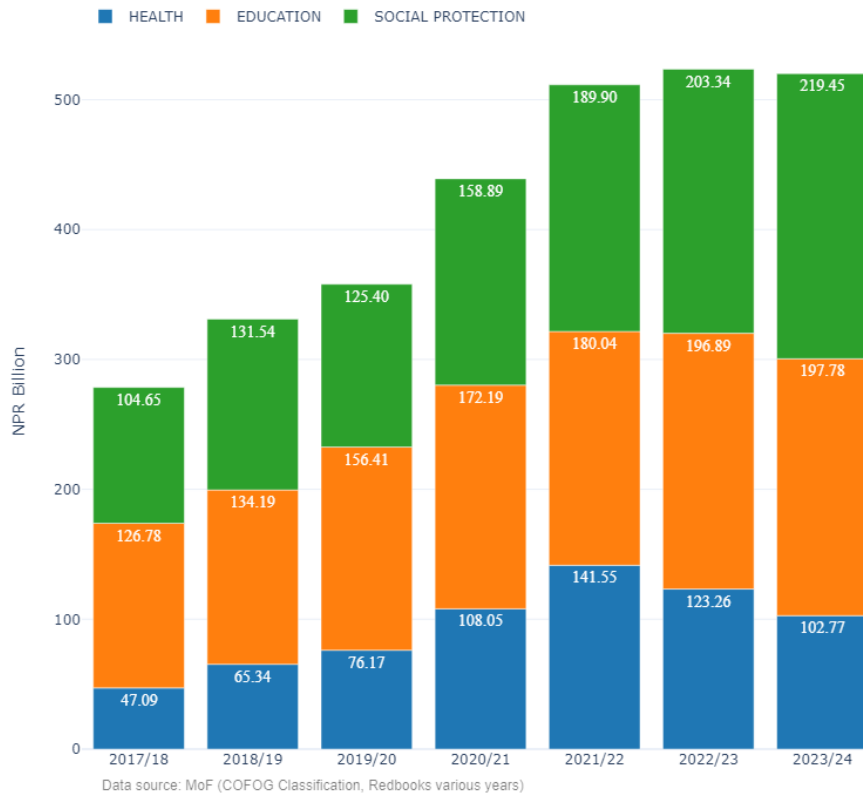


Figure 4: Social Sector allocations (NPR Bill.)

- The total social sector budget increased from NPR 279 billion in FY 2017/18 to a targeted NPR 520 billion in FY 2023/24: an increase of 87%. However, in FY 2023/24, budget allocations towards the social sector dropped marginally from NPR 523 billion in FY 2022/23 to NPR 500 billion in FY 2023/24 marking for the first time in the last seven years that the allocations for social sectors have decreased. This has occurred despite a growth in expenditures this fiscal year. It may be worth noting that this reflects a global trend of a "return to normal" although socio-economic risks are still considerably high in Nepal.

- It is noteworthy that as the COVID-19 pandemic unleashed across Nepal, even as revenues plunged, the government was able to increase overall social sector expenditures. However, in the last two fiscal years, the expansion has slowed down and reduced in FY 2023/24.
- The increases or changes have not been even across the social sectors. Since FY 2021/22 the health sector budget allocations have been declining in nominal and real terms. Allocations to the education sector also grew, but in the last fiscal year, increases were marginal. Allocations for social protection fell marginally in FY 2019/20 but since then have been rising - being driven by demographic changes as well as increases in the benefit amounts for the different social security assistance transfers, the majority of which are geared towards the elderly. Social Protection is the only sector for which nominal budget allocations have been rising since FY 2019/20.

The COFOG classification provides details on each sector including the social sectors. The data for the last four fiscal years for each sector is shown in Figure 5.

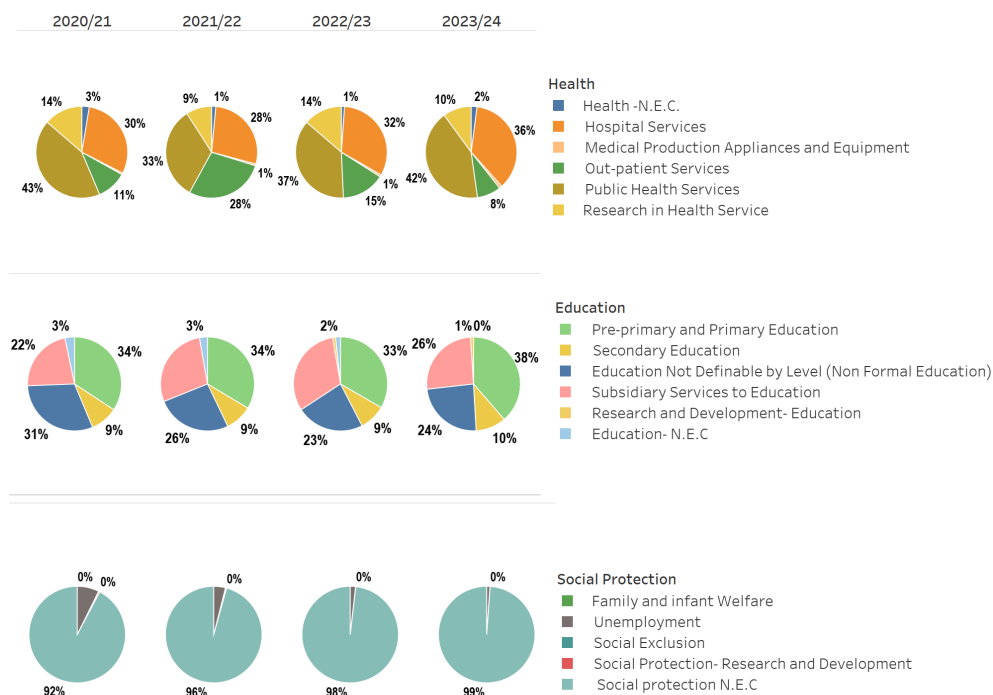


Figure 5: COFOG classification of social sectors (% of total)

- Health sector allocations are used primarily for public health services and hospital services: these two account for nearly 80% of health allocations in FY 2023/24. The allocations across the

various categories have varied. For instance, allocations for out-patient services have reduced while public health services has increased.

- Education sector allocations are typically for pre-primary and primary, education not defined by any level (including non-formal education) and the provision of subsidiary services for education. As in the case of health, there are slight variations in the allocations across the sub-categories for education.
- It becomes clear that the social protection categories are problematic as an overwhelming majority of social protection expenditures are showing up under the "not elsewhere classified" category which includes both social assistance and social insurance clumped together. There is therefore an urgency to unpack the social protection allocations in a manner that indicates how much is being allocated to social assistance (non-contributory) and how much to social insurance (contributory).

It is also useful to examine social sector allocations as a percent of Gross Domestic Product (GDP).³ After rising for the last five fiscal years, social sector expenditures as a per cent of GDP have been falling in the last two fiscal years making the "return to normal" scenario more evident (Figure 6).

- As a share of GDP, allocations for health had more than doubled between FY 2017/18 and FY 2021/22 rising from 1.48% of GDP to 3%. Since then they have dropped significantly to 1.88%.
- As a share of GDP, allocation for education rose from 4% in FY 2017/18 to 4.12% during FY 2021/22. However, since then as a share of GDP education allocations have been falling and in FY 2023/24, allocations as a percent of GDP declined to levels below FY 2017/18.
- Social Protection allocations as a percent of GDP had been increasing since FY 2019/20 from 3.31% of GDP to 4.02% of GDP in FY 2021/22. Since then, allocations have been falling.

In relation to the share of the total consolidated budget, the social sector allocations had risen from 21% of the total consolidated budget to 31% in FY 2021/22. Since then it had decreased to 29.18% in FY 2022/23 and risen slightly to 29.69% in FY 2023/24. Hence in terms of the total consolidated budget, there has been a marginal decline when compared to FY 2021/22. It is remarkable to note that during the COVID-19 pandemic and after there was a significant increase in the share of the total budget allotted for social sectors. Since then, there has been a slight decrease (Figure 7).

³ Being a ratio of two nominal amounts, the effect of inflation is cancelled.

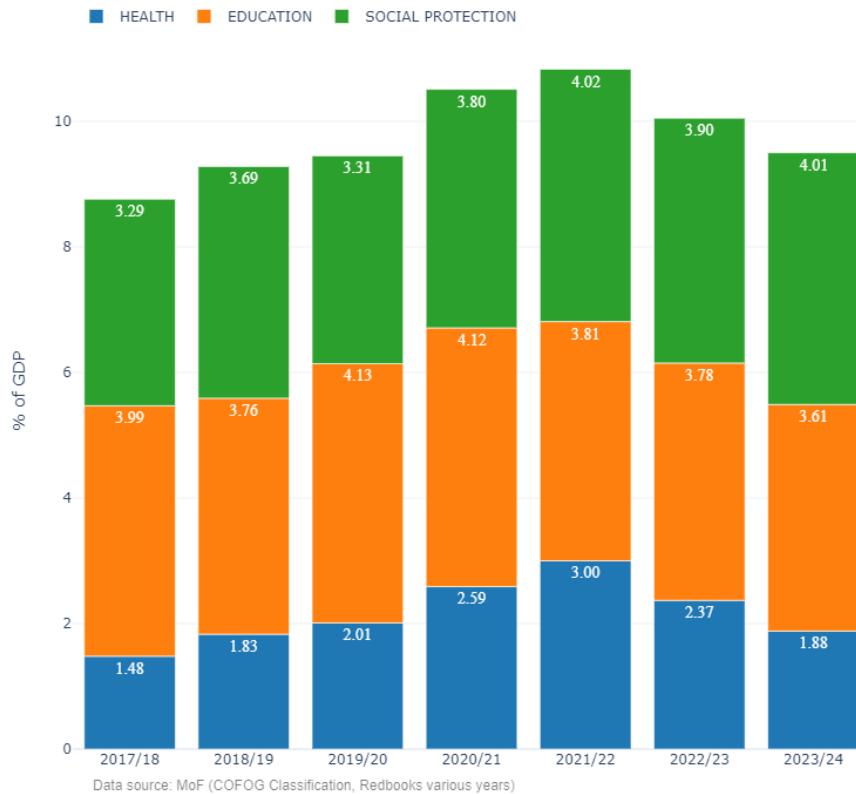


Figure 6: Social Sector allocations as % GDP

- The share of the health sector budget rose from 3.68% to nearly 9% by FY 2021/22. Since then there has been a decline in the health sector allocation to 5.87% in FY 2023/24.
- The education sector budget also rose from 9.91% of total expenditures to nearly 12% in FY 2020/21. Since then the allocation has fallen to 11.29% in FY 2023/24. These allocations are well below the government's own target of 15% for the education sector.
- It is interesting to note that in FY 2023/24, social protection allocations were at the highest observed values since FY 2017/18 absorbing 12.53% of the total consolidated budget. By FY 2023/24, social protection allocations were the highest in the social sector budget.

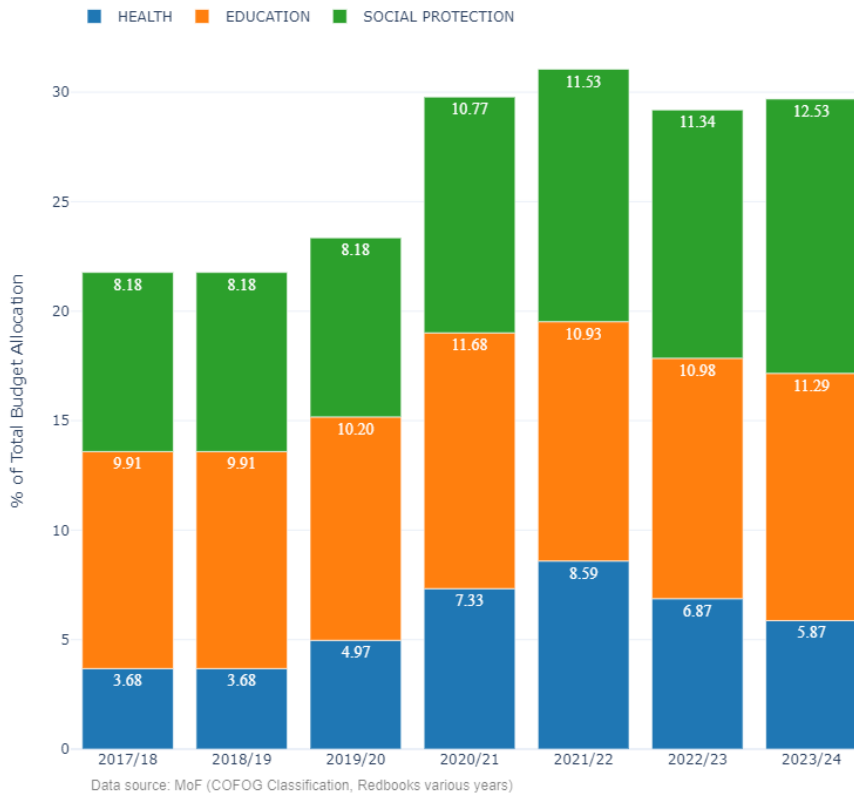


Figure 7: Social Sector allocations as % budget

6 FEDERALISM AND THE BUDGET

The classification of COFOG expenditures can be split into the three different layers of government. Over the last four fiscal years, the shares allocated among the three different layers of government have remained steady: the federal government is allocated 77% of the total consolidated budget. The rest is shared between the provincial governments (7%) and local governments (17%).

Education has the highest allocation to local governments, followed by General Public Services and Health (in per cent terms). Only two sectors are completely centralized: Defense and Public peace, security. (Figure 8). Except for education, the federal government has the highest allocation among the different layers of the government in all functional expenditure classifications. Just under 70% of the education allocation is to the local governments (Palikas) and 28% of the budget for health is allocated to the local governments. These patterns are due to the increasing devolution to the local levels for education and health services as per the constitutionally mandated functional responsibilities of different government layers. It is not clear as to extent to which allocations to provinces and local governments are aligned to local needs and their constitutional functional responsibil-

ities. Given that a large portion of the allocation still flows in the form of conditional grants, it is questionable if these arrangements empower local governments to have a higher degree of autonomy in decision making.

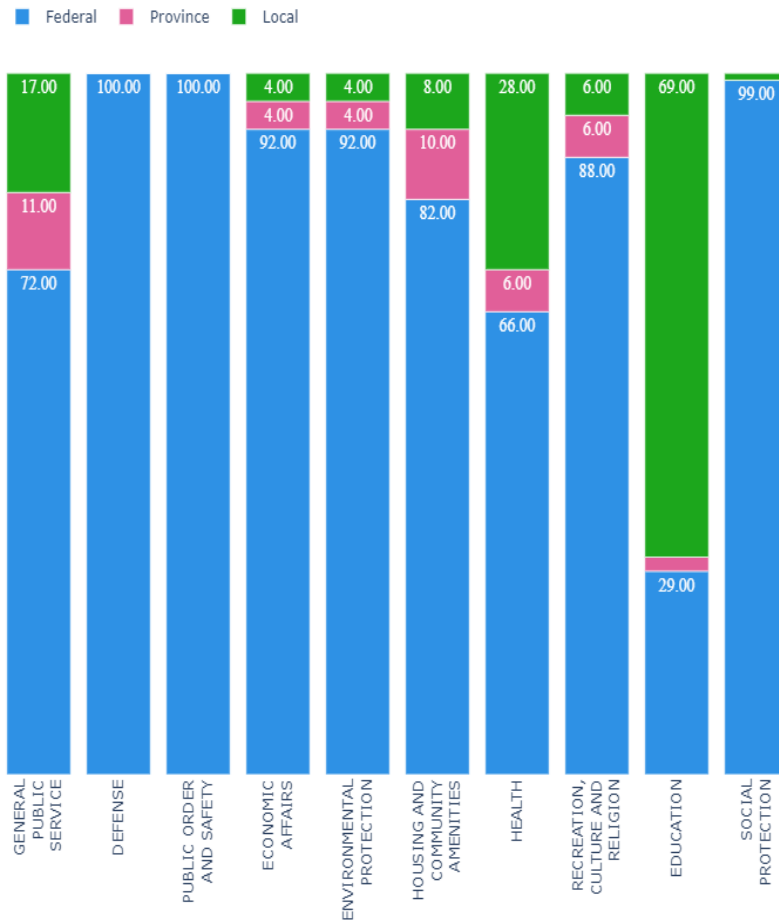


Figure 8: COFOG allocations among government types (% , FY 2023/24)

Education has the highest devolution to local governments. Within education, the budget allocations for pre-primary and primary education, secondary education, and education not definable by level (including non-formal education) are largely for local governments. Provincial governments play a limited role, their allocations being solely for education not definable by any level. Over the last two fiscal years, local governments have been getting higher allocations that offset decreases in federal and provincial allocations.

In the social sectors, health has the next highest devolution to the local governments and over the last two years, the allocation for local governments increased from 23% of the total health budget to 28% of the total health budget allocation.

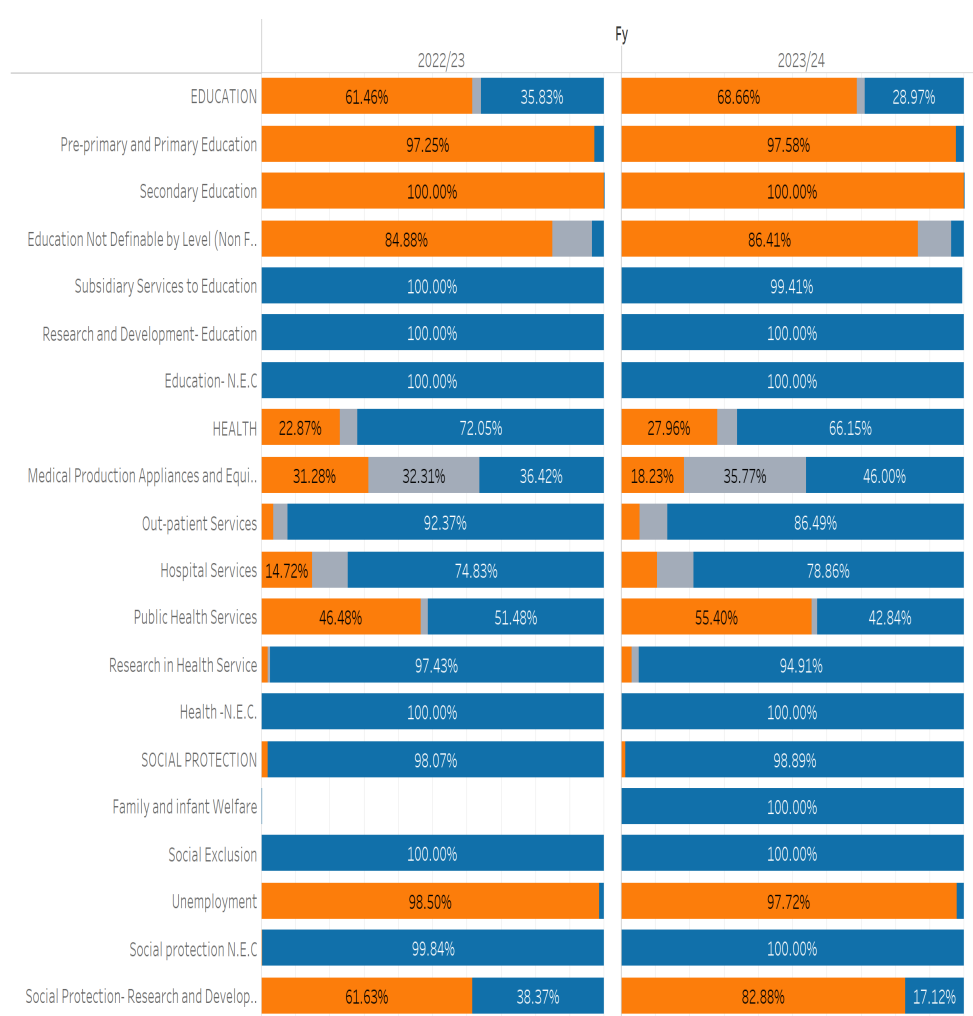


Figure 9: Allocations to social sectors and federalism (% allocation among governments)

7 SDGS AND THE BUDGET

The time is propitious to examine budget allocations as the mid-point towards achieving the SDGs has arrived. Budget expenditures directly affects SDG goals prescribed by the government. Failing to meet one directly impacts progress on SDG actions. Despite this, government has been reporting on SDG allocations only sporadically. It did so in FY 2017/18 but did not produce any SDG allocations from FY 2018/19 to 2020/21. In FY 2021/22 and FY 2022/23 the government once again produced SDG allocations but has not produced any SDG allocation data for FY 2023/24. The last two years for which data exist are used to compare changes (FY 2021/22 and FY 2022/23).

- The most significant change was the increase in the category "Not allocated for any SDG" which went up from 21% in FY 2021/22 to 27% in FY 2022/23. This means that in FY 2022/23, only 73% of the total budget allocations were for SDGs.

Table 3: Percent allocated for SDGs

SDG	Goal	FY 2021/22	FY 2022/23
1	End Poverty in all forms	7	10
2	Zero Hunger	4	5
3	Healthy Lives	8	6
4	Inclusive & Quality Education	11	11
5	Gender Equality	< 1	< 1
6	Sustainable clean water/sanitation	2	2
7	Access to modern energy	5	4
8	Inclusive Economic Growth	3	2
9	Resilient infrastructure	14	12
10	Inequality Reduction	6	6
11	Sustainable cities and settlements	9	7
13	Climate change adaptation	1	1
15	Sustainable Utilization of ecosystem	< 1	1
16	Peaceful, Just and Active Society	7	8
0	Not allocated for any SDG	21	27

Source. MoF Budget Speech (2022/23); MoF 2021/22 Redbook

- In FY 2021/22 the top 5 SDG priorities in terms of budget allocations were for SDG9: resilient infrastructure (14%),SDG4: Inclusive and Quality Education (11%), SDG11: Sustainable cities and settlements (9%), SDG3: Healthy Lives (8%), and, SDG10: Inequality reduction (45%).
- In FY 2022/23, the top 5 SDG priorities as per allocations saw some changes. The top 5 SDGs receiving allocation were SDG9 (Resilient infrastructure,12%), SDG4 (Inclusive and Quality Education, 11%), SDG1 (End Poverty in all its forms, 10%), SDG16 (Peaceful, Just and Active Society, 8%) and SDG11 (sustainable cities and settlements, 7%).
- Compared to the priorities in FY 2021/22, SDG1 (End Poverty in all its forms), SDG2 (Zero Hunger), and, SDG16(Peaceful, Just and Active Society) had increased allocations. On the other hand, there was a decline in SDG3 (Health Lives), SDG7 (Access to modern energy), SDG9 (Resilient infrastructure) and SDG11 (Sustainable cities and settlements). For all other SDGs, allocations remained the same.
- Six SDGs are allocated less than 5% of the budget. There is scope to allocate more expenditures towards gender equality, sustainable clean water/sanitation, Climate change adaptation, Inclusive growth, and, Sustainable utilization of ecosystems. There also does not appear to be any allocation towards SDG 12: Sustainable consumption and production.

Recent data regarding SDG progress (NPC, 2020) suggests that there are numerous indicators off-target and in need of acceleration. For

progress, maximum available resources need to be directed towards the SDGS. The financing gap is likely to be large⁴ and would involve participation from numerous stakeholders. Hence it is critical that SDG allocations are monitored closely going forward to demarcate government contributions and elicit support from other national and international stakeholders as Nepal develops its vision to accelerate and attain SDGs by 2030.

⁴ Estimated at a staggering NPR 2,025 billion per year to achieve the SDGs,NPC, 2017

8 CONCLUSION

Historical data suggests that the current fiscal years budget proposal is ambitious and optimistic. Credibility of the budget, or lack thereof has been a persistent issue for the last six fiscal years (for which data are available). There is an urgency to therefore ensure implementation capacity exists - especially at local levels while strengthening PFM systems such as expenditure tracking and monitoring. The dependence on loans (increasingly private) had implications on the overall debt structure, foreign exchange reserves and liquidity. Although the current gross debt to GDP ratio in Nepal is lower than some of her neighbours, debt servicing consumes a significant share of the budget and are considered non-votable expenditures: they must be paid. Adding in other non-votable expenditures like salaries and benefits for civil service employees means there is a squeeze on development expenditures.

Another risk for the sustainability of current expenditures relates to civil service pensions - which consumes a significant share of recurrent expenditures. Given that the civil service workforce will age imminently, this may pose a problem as pension related expenditures would surge even higher. The reliance on loans, especially for capital expenditures, makes it important to synchronize project capital requirements with donor and internal flows of loans.

Capital expenditures are below 20% of the budget and there are concerns that current levels of capital expenditures may not be sufficient to develop the infrastructure in Nepal at an optimal pace.

In terms of COFOG classifications, general administrative services and economic affairs absorb a lion's share of the allocations squeezing out allocations for other sectors. Allocations towards the social sectors are showing a trend of constrained growth over the last two fiscal years suggesting a "return to normalcy". However, socioeconomic risks still remain high in Nepal. Moreover, the COFOG classifications for SP as presented in the budget are inadequate as 99% is classified as "not elsewhere classified" which clumps together several different programme categories.

The per cent not allocated to any SDG has increased in the recent budget. Many SDGs remain underfunded and this situation could undermine Nepal's achievements thus far and in the future.

Finally, the absence of child budget codes in the budget makes it difficult to identify public expenditures focused on children. The Government has already begun contemplating this issue and needs support to amplify results in this area.

In conclusion, it would be fair to summarize by saying that although Nepal's performance during the peak of the pandemic, especially in relation to social sector allocations was commendable, and

prevented many lives from catastrophe, recent allocations show a trend towards "normalcy". This is a matter of great concern on multiple fronts as the risks emanating from COVID-19 and other poly-crises have the potential to undermine years of hard fought progress in Nepal.

DATA NOTES

This brief is based on publicly available secondary data. This document was written and typeset in \LaTeX while the data analyses and graphs were produced using Excel, R and Python. The data sources for this brief are:

- FY 2023/24* budget speech (translated english version)
- Budget Red books published by the MOF for previous fiscal years. These were translated and converted to Excel, R and Python for further analyses and graphics.
- The most recent socio-economic survey by the Nepal Rashtra Bank (NRB, April, 2022)
- The most recent World Economic Outlook (IMF, April 2023)
- The most recent census estimates to derive per capita estimates

To the extent possible, the data have been checked and cross-validated from multiple sources. Each years Red books lists data for the current budget/target estimate, the previous years revised estimate and the actual estimate for the year previous to that. Hence analyzing the Red books from FY 2017/18 through to FY 2022/23 and using data from the FY 2023/24 budget speech, it is possible to construct the time series data used in this brief for actual estimates, budget/target estimates and the revised estimates for the last few fiscal years. Other macro data used in the brief were from the latest publications by the Nepal Rashtra Bank (NRB, *ibid.*) as well as from the International Monetary Fund (IMF 2023.)

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10. World Bank (WB), Public Expenditure Review, 2021

11. World Bank (WB), Nepal Development Update, April 2022.

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ANNEX: DATA & FIGURES

This data annex presents a copy of the raw data as well as scaled versions of the figures in this brief. These graphs are also available in interactive html format for dashboards, infographics and presentations upon request.

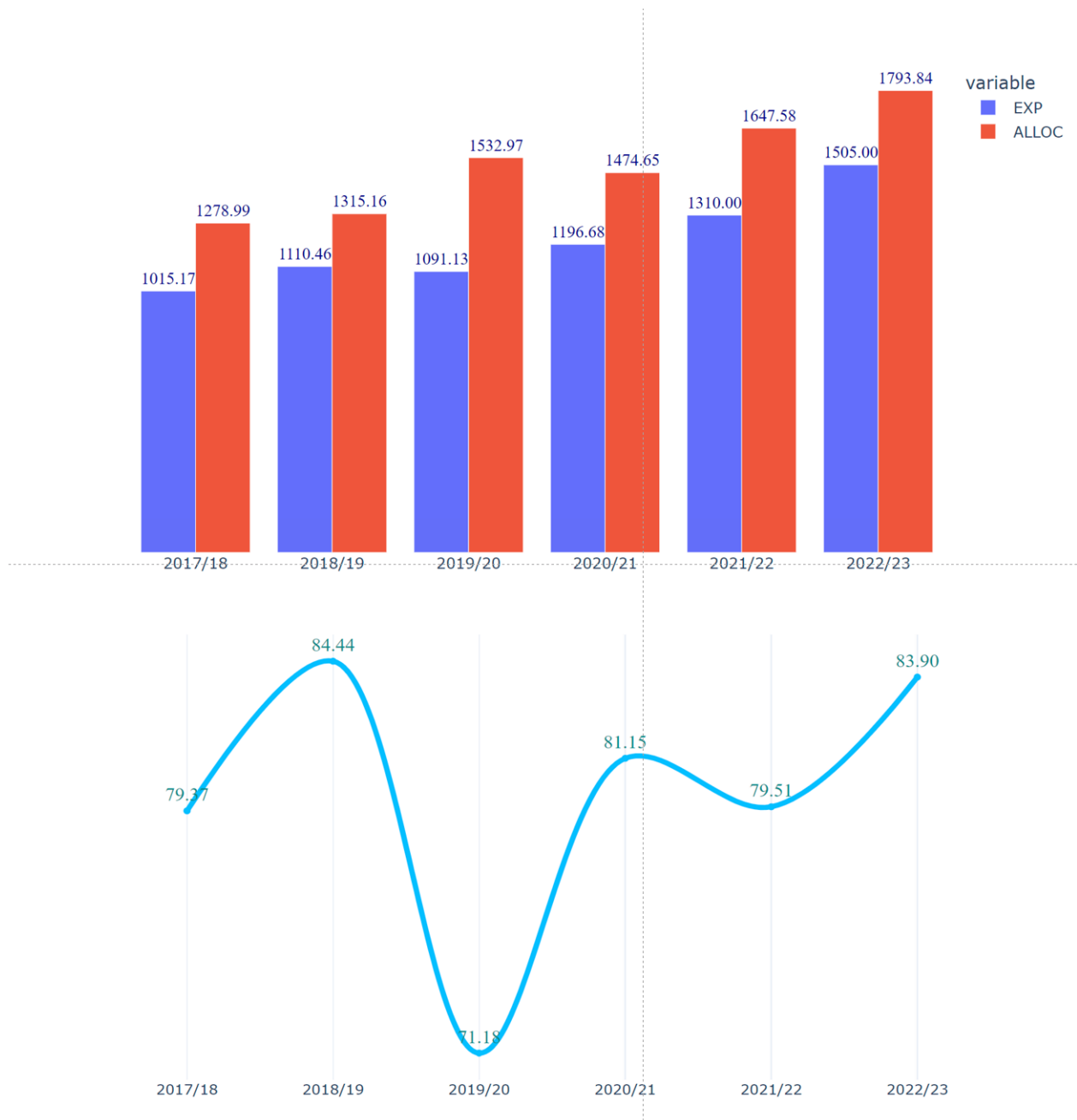


Figure 1: Budget allocations, expenditures (in NPR bill., top) and utilization rates (bottom)

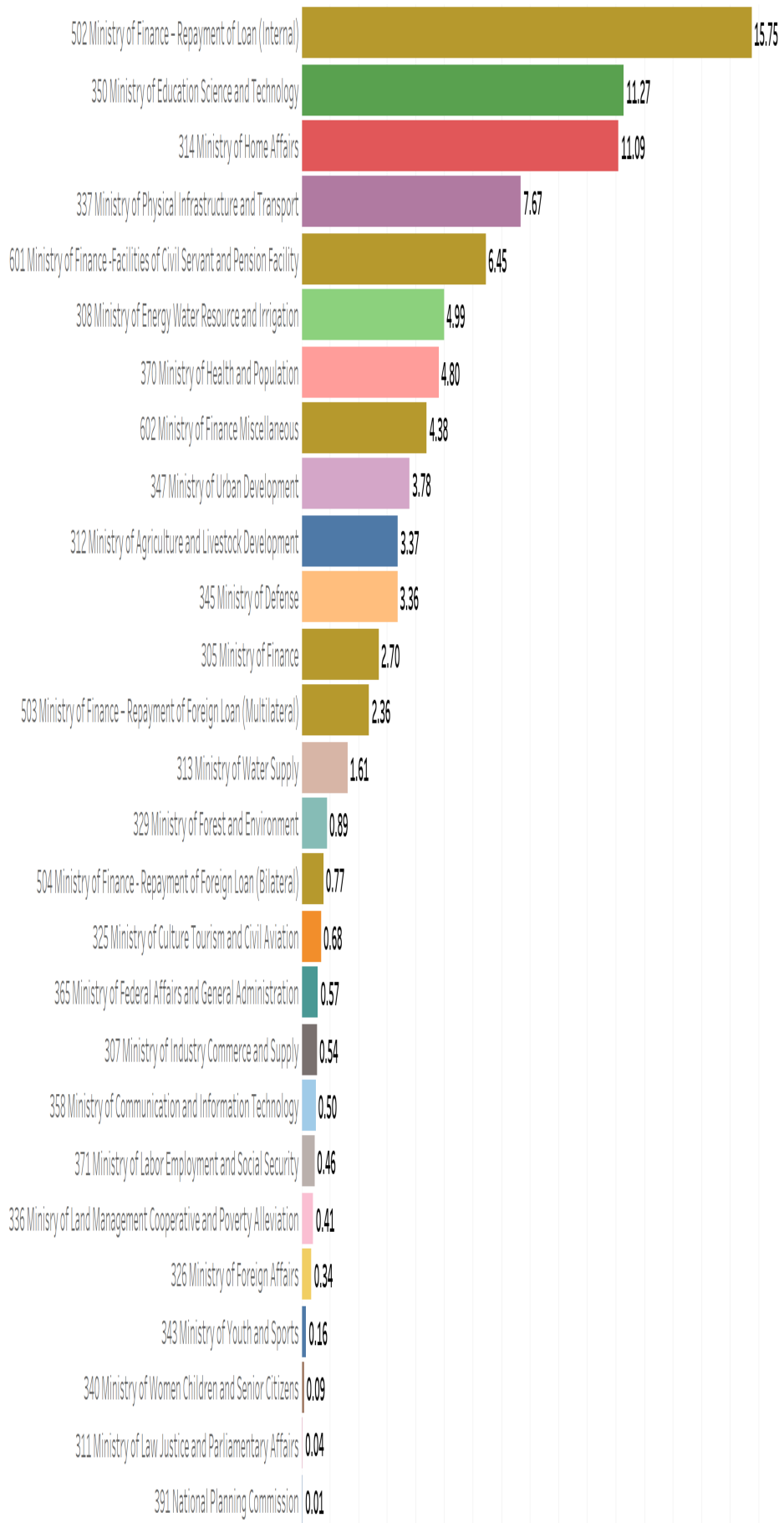


Figure 2: Ministry-wise allocation of FY 2023/24 budget (% of total)

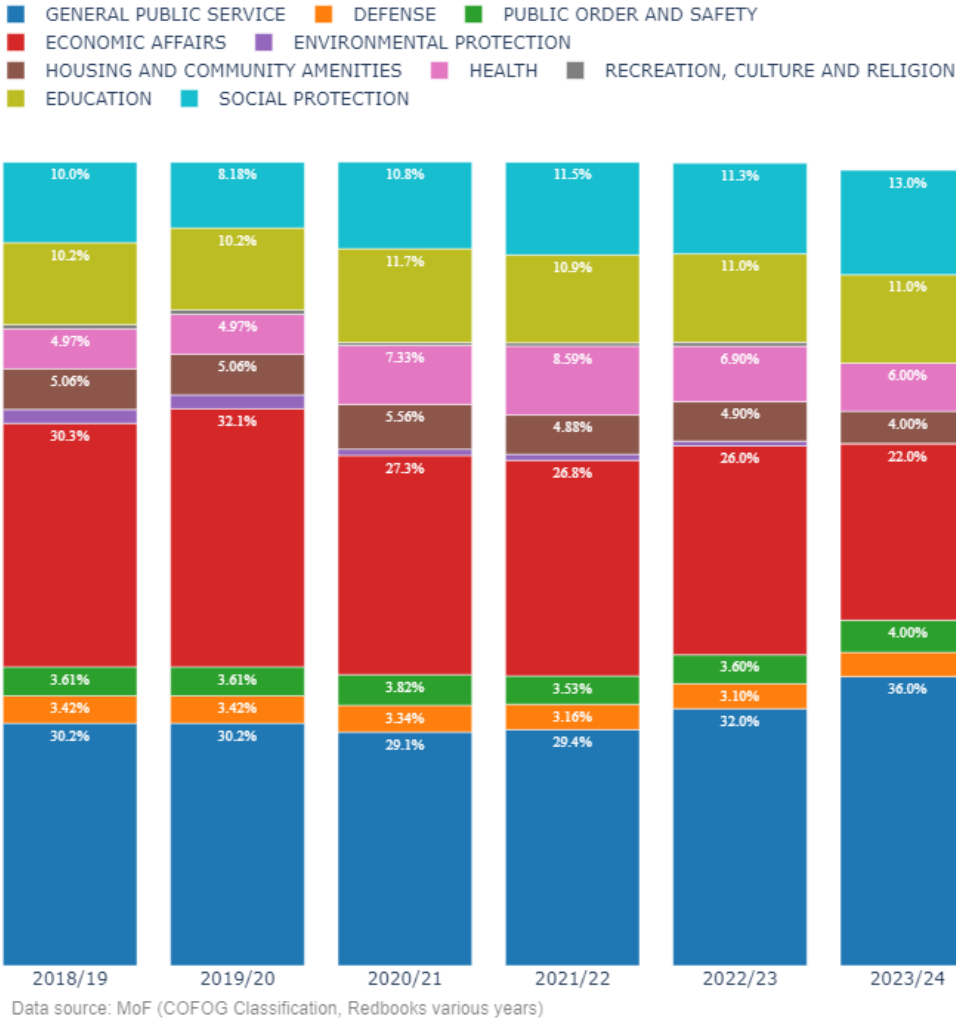


Figure 3: Functional Composition of the Budget

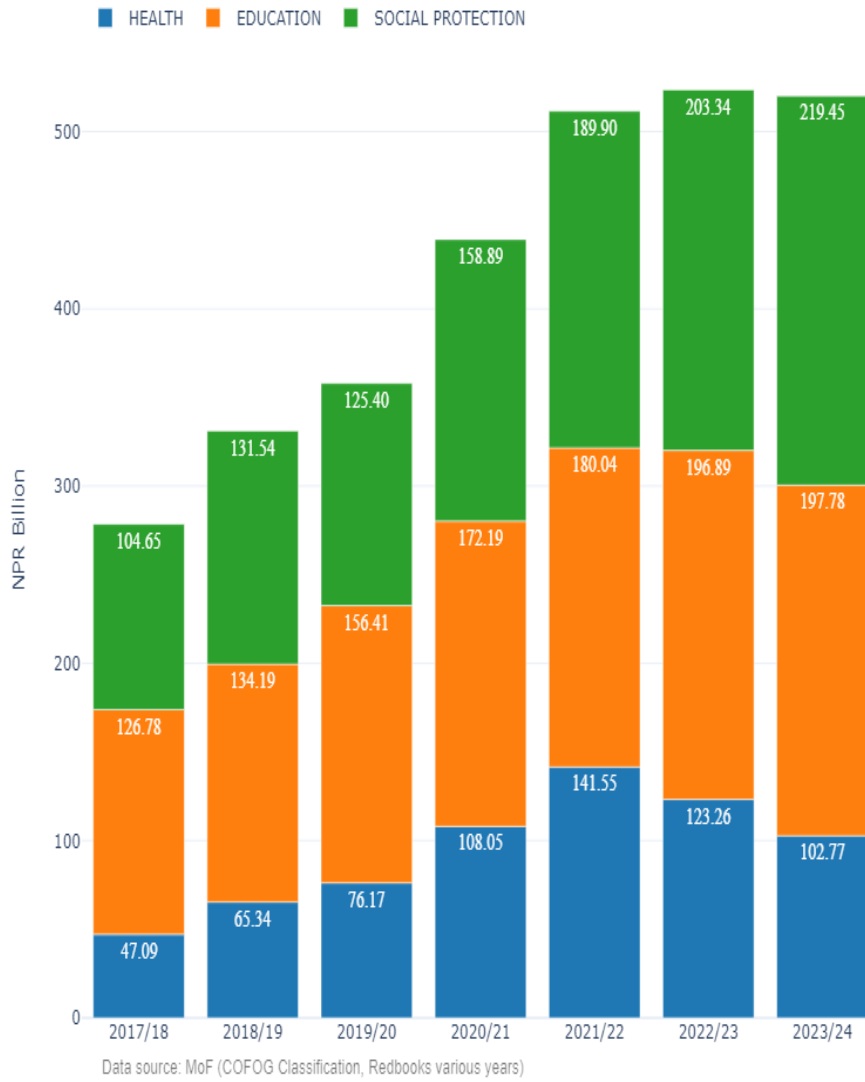


Figure 4: Social Sector allocations (NPR Bill.)



Figure 5: COFOG classification of social sectors (% of total)

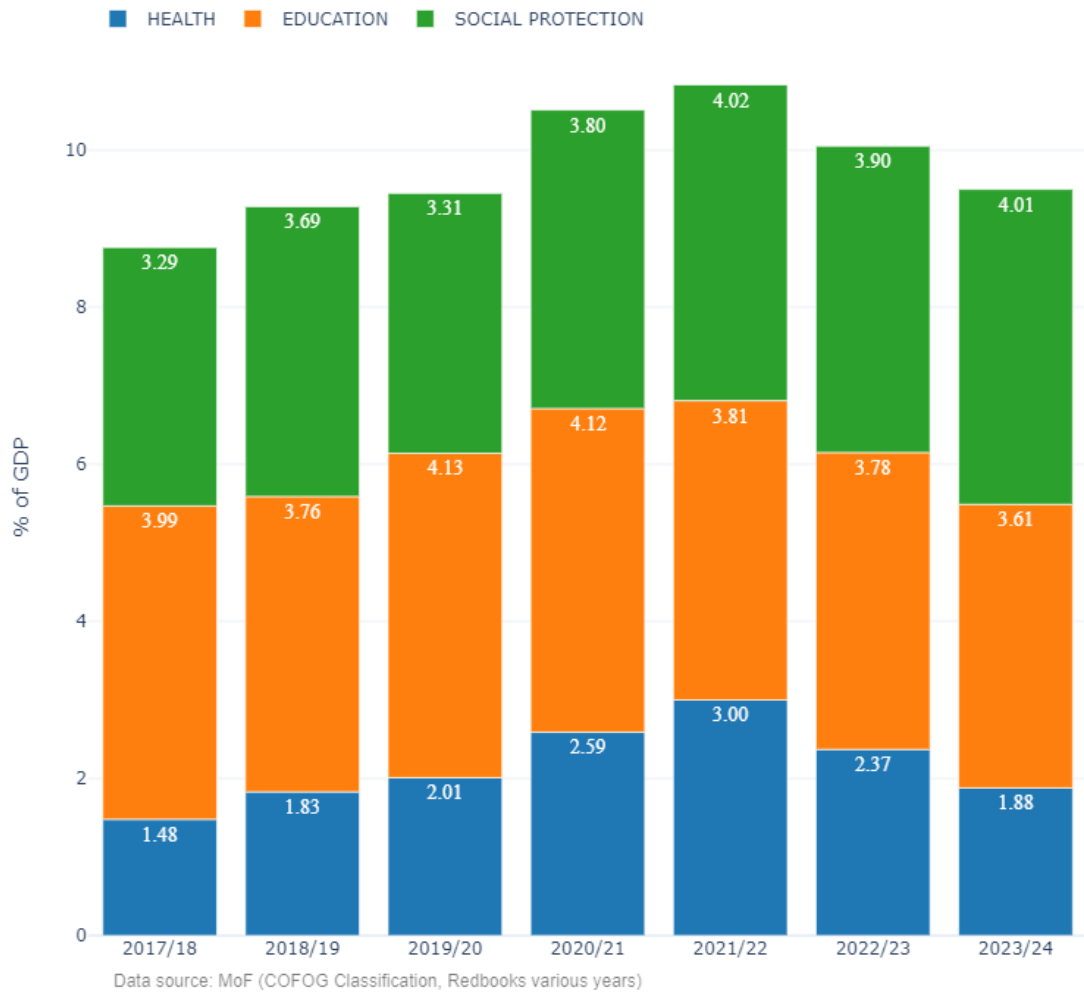


Figure 6: Social Sector allocations as % GDP

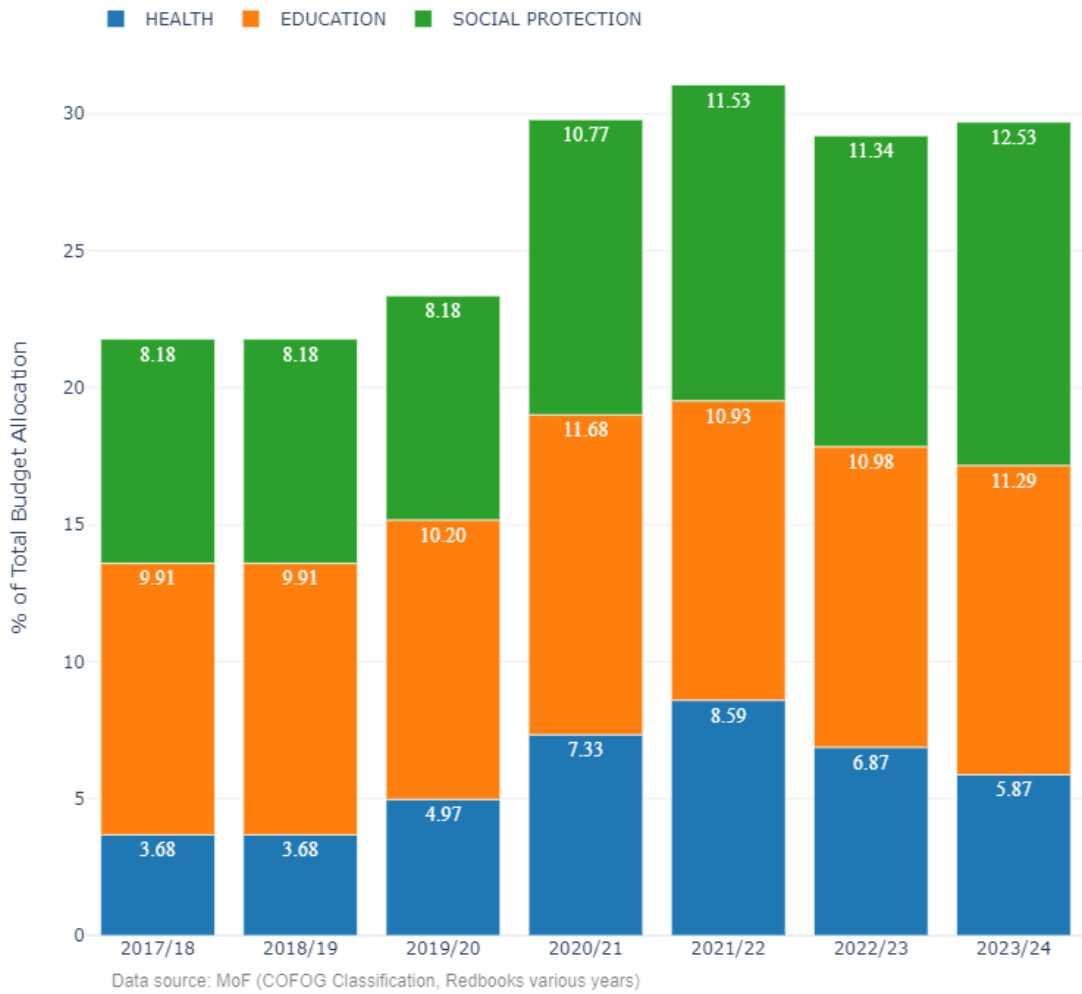


Figure 7: Social Sector allocations as % budget

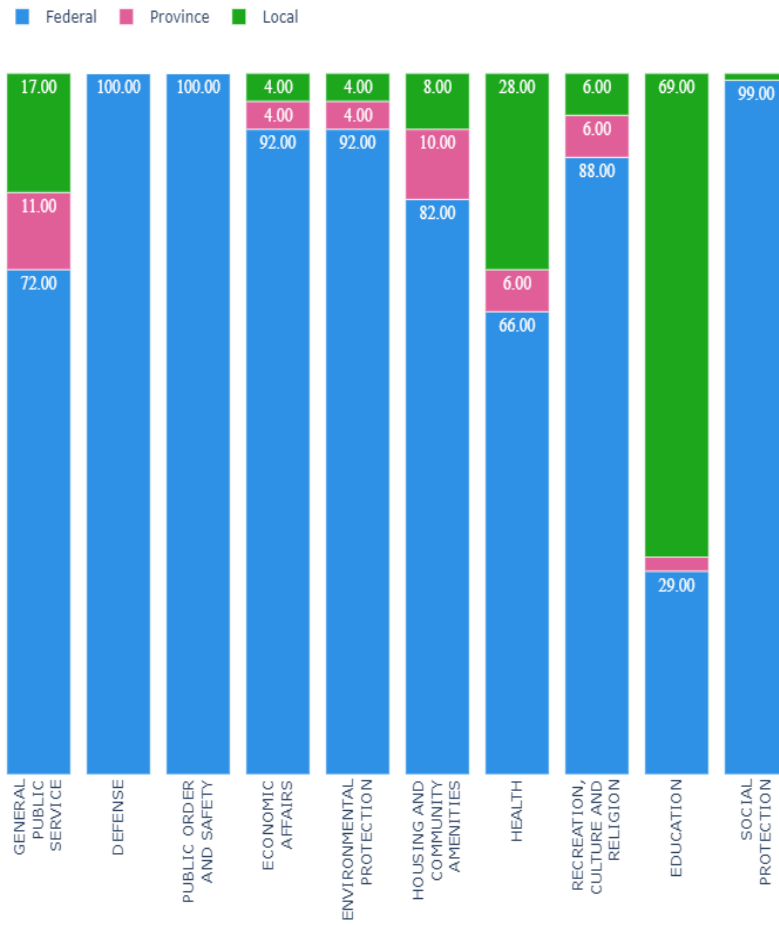


Figure 8: COFOG allocations among government types (% , FY 2023/24)

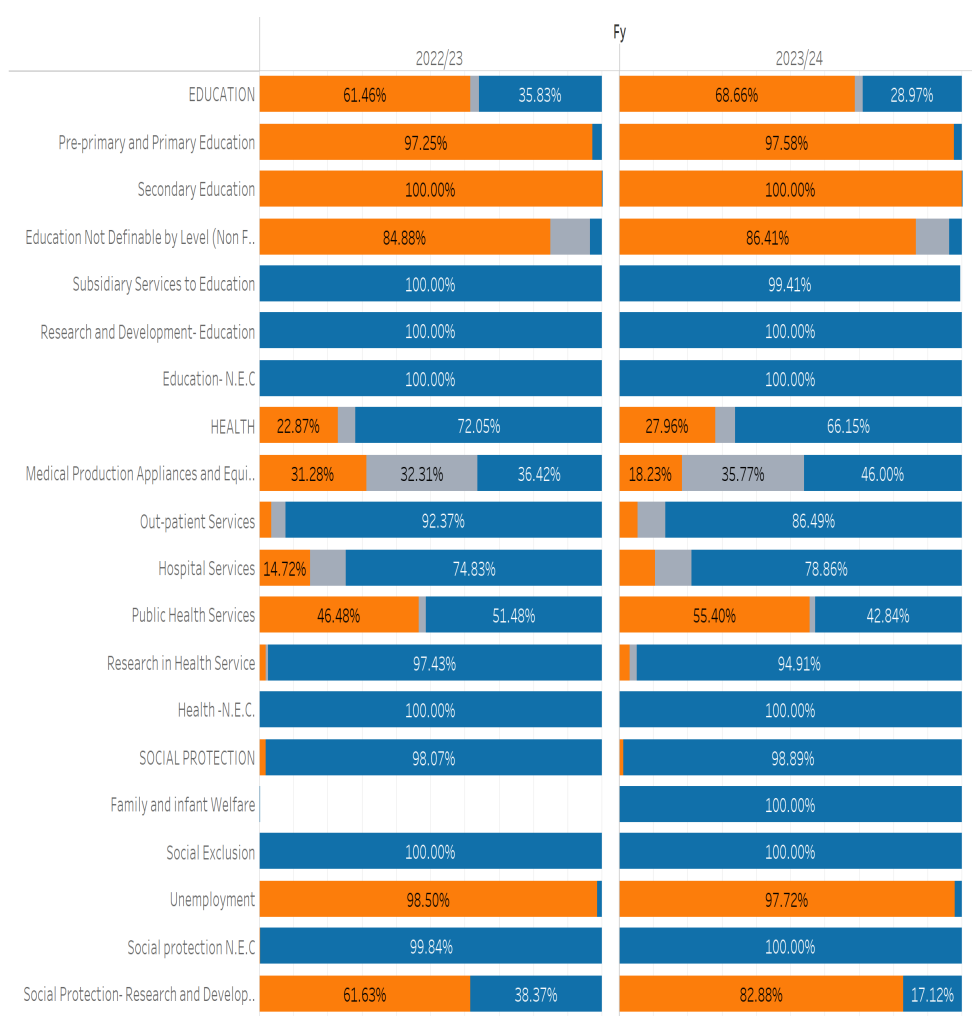


Figure 9: COFOG classification and federalism (% allocation among governments)