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BOOK REVIEW

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Nepal's Investment Climate: Leveraging the Private Sector for Job Creation and Growth

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World Bank Publications (2012), 272pp, USD 29.95.

Nepal is urgently in need of private sector investment to promote jobs and growth: 25 per cent of the population live beneath the poverty line and youth unemployment is a chronic problem. Despite the efforts of the government to boost the private sector and attract foreign investors, many barriers to investment exist and the overall business climate is poor. A lack of access to finance, political instability and weak infrastructure are all major obstacles to the development of a thriving private sector.

The World Bank report "Nepal's investment climate: Leveraging the private sector for job creation and growth" provides a comprehensive evaluation of the investment climate in Nepal. It covers critical aspects of the business environment including product and factor markets, the availability of infrastructure, and the related political, legal, institutional and macroeconomic institutions. By providing a detailed and data-driven assessment of needs, the report aims to help public officials and policy makers better understand the challenges facing the private sector, and alert them to potential remedies.

The original research in the report is largely derived from three major national surveys. The surveys examined the operation of both formal and informal businesses. Of most importance was the enterprise survey which covered a wide range of registered firms, operating within the manufacturing and services sectors. In addition, to better understand the informal sector, separate surveys were done with employees and unregistered entities. To put Nepal in context, several cross-country comparative methods were also used, so as to be able to single out the peculiarities of the investment climate in Nepal. Conclusions were validated by stakeholders through peer reviews.

The report makes clear that despite some sectors of the Nepalese economy performing well, such as tourism, overall macroeconomic prospects are limited by a wide range of factors. Most importantly, political instability undermines the predictability of investment laws and regulations as well as damaging overall perceptions of the country as an investment location. This uncertainty deters long-term commitments from the private sector. Although the Nepalese government has announced a new investment strategy and set up an Investment Board to operate as focal point for foreign investors, the investment community remain sceptical. As the report notes, in recent years, potential investments from Russia, Saudi Arabia, the UK and the USA have all been cancelled.

Another worrying trend is the persistent weakness of infrastructure, including in the power, transport and communications sectors. 99 per cent of registered Nepalese companies report frequent power outages, leading to an estimated loss of 22 per cent of their annual sales. Moreover, the poor transportation infrastructure hinders local companies wishing to export, or link with global supply chains. 97 per cent of firms reported substantial losses due to transportation problems. This helps explain why only 3.8 per cent of Nepalese enterprises currently export. Despite the fact that the level of government investments into infrastructure is comparable with that of other governments in South Asia, because of Nepal's difficult geography the country faces greater challenges in improving connectivity.

The third critical concern is the dominance of the informal economy, which itself is a consequence of the absence of political and economic stability. The informal sector comprises a significant proportion of production, employment and consumption in Nepal. Despite the fact that informal enterprises are frequently represented by micro-firms, up to 70 per cent of total non-agricultural employment in Nepal is informal. The development of a ''ghost economy'' costs the government in lost taxation revenues, thereby making it harder to finance and launch initiatives aimed at building sustainable economy and creating a favorable climate investment climate. Hence, the government's inability to address the weak business environment and the dominance of the informal sector are connected in a vicious circle.

Additional challenges highlighted in the report are poor access to land, an undeveloped financial sector, employers' reluctance to hire employees under formal contracts, and low levels of human capital.

Following their evaluation, the authors of the report provide a number of recommendations, aimed at both promoting the investment climate and conditions for the private sector. These are: strengthening linkages between the formal and informal sectors; addressing constraints related to access to financial products and services; promoting the development of human capital; simplifying the registration process of legal entities; reforming labor laws, regulations and practices; reducing non-wage costs of employers; increasing electrification rates; investing in the strategic expansion of roads networks, and engaging the private sector more in improving infrastructure.

Overall, the report makes a useful contribution to the policy debate in Nepal, in particular by highlighting that without efforts to tackle the country's political instability, it will be hard to address economic failures including a lack in foreign investment and a weak private sector. Nevertheless, the book misses an important opportunity to draw lessons from the success of Nepal's fast growing tourism sector that could be applied more widely.

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