

ASIAN DEVELOPMENT BANK

PPA:NEP 22268

PROGRAM PERFORMANCE AUDIT REPORT

ON THE

**FORESTRY SECTOR PROGRAM
(Loan No. 1040-NEP[SF])**

IN

NEPAL

February 2001

CURRENCY EQUIVALENTS

Currency Unit — Nepalese Rupee/s (NRe/NRs)

		At Appraisal	At Program Completion	At Operations Evaluation
Nre 1.00	=	\$0.0341	\$0.017	\$0.02
\$1.00	=	NRs29.30	NRs58.77	NRs68.00

ABBREVIATIONS

ADB	-	Asian Development Bank
ADBN	-	Agricultural Development Bank of Nepal
BAEDP	-	Biogas and Agricultural Equipment Development Pty., Ltd.
DNPWC	-	Department of National Parks and Wildlife Conservation
DOF	-	Department of Forests
EA	-	Executing Agency
FINNIDA	-	Finnish Department for International Development Cooperation (formerly Finnish International Development Agency)
FPDB	-	Forest Products Development Board
FSCC	-	Forestry Sector Coordinating Committee
FSPL	-	Forestry Sector Program Loan
HPPCL	-	Herbs Production and Processing Co. Ltd.
M&E	-	monitoring and evaluation
MED	-	Monitoring and Evaluation Division
MFSC	-	Ministry of Forests and Soil Conservation
MOF	-	Ministry of Finance
MPFS	-	Master Plan for the Forestry Sector
NPC	-	National Planning Commission
OEM	-	Operations Evaluation Mission
PCR	-	program completion report
PPAR	-	program performance audit report
TA	-	technical assistance

NOTES

- (i) The fiscal year (FY) of the Government ends on 15 July.
- (ii) In this Report, "\$" refers to US dollars.

Operations Evaluation Office, PE-557

CONTENTS

	Page
BASIC DATA	ii
EXECUTIVE SUMMARY	iii
I. BACKGROUND	1
A. Rationale	1
B. Formulation	1
C. Objectives and Scope at Appraisal	2
D. Financing Arrangements	2
E. Aid Agency Coordination	3
F. Program Completion Report	3
G. Operations Evaluation	4
II. IMPLEMENTATION PERFORMANCE	4
A. Policy Reform Measures	4
B. Investment Component	6
C. Procurement and Distribution	7
D. Organization and Management	8
E. Effectiveness of Technical Assistance	8
F. Compliance with Loan Covenants	9
G. Monitoring	10
H. Use of Counterpart Funds	11
III. PROGRAM RESULTS	11
A. Performance Indicators	11
B. Institutional Development	13
C. Socioeconomic Impact	13
D. Gender Development	14
E. Environmental Impact and Control	14
F. Gestation and Sustainability	14
IV. KEY ISSUES FOR THE FUTURE	15
V. CONCLUSIONS	16
A. Overall Assessment	16
B. Lessons Learned	18
C. Follow-Up Actions	19
APPENDIXES	19

BASIC DATA
FORESTRY SECTOR PROGRAM (Loan No. 1040-NEP [SF])

Program Preparation/Institution Building

TA No.	TA Name	Type	Person-months	Amount (\$)	Approval Date
1393-NEP	Monitoring and Evaluation of Program Activities	AOTA	7	208,000	23 Oct 1990
1394-NEP	Equitable and Efficient Energy Pricing Policies	AOTA	17	490,000	23 Oct 1990

As Per ADB

Key Project Data (\$ million)	Loan Documents	Actual
Total Program Cost	40.0	20.97
Foreign Exchange Cost	40.0	20.97
ADB Loan Amount/Utilization	40.0	20.97
ADB Loan Amount/Cancellation		
Amount of Cofinancing	00.0	0.00

Key Dates

	Expected	Actual
Fact-Finding (period with 4 missions)		Feb–Sept 1989
Appraisal		19-27 Oct 1989
Loan Negotiations		23-24 Aug 1990
Board Approval		23 Oct 1990
Loan Agreement		2 Dec 1990
Loan Effectiveness	21 Jan 1991	24 Dec 1990
First Disbursement		27 Dec 1990
Program Completion	31 Dec 1995	15 Jul 1996
Loan Closing	31 Dec 1993	15 Jan 1994
Months (effectiveness to completion)	52.47	66.24

Borrower Government of the Kingdom of Nepal

Executing Agency Ministry of Forests and Soil Conservation

Mission Data

Type of Mission	No. of Missions	No. of Person-Days
Fact-Finding	4	48
Appraisal	1	54
Program Administration		
Inception	1	30
Review	4	41
Special Loan Administration	2	19

Program Completion	1	32
Operations Evaluation	1	15

EXECUTIVE SUMMARY

The Forestry Sector Program Loan was in response to the Government of Nepal's request for assistance following its Master Plan for the Forestry Sector. The Program was to be the first phase of the Government's systematic efforts to restore the forest cover. The rationale for the Program was appropriate given the continuing forest degradation and destruction caused by encroachment from poor people, an inappropriate legal framework for exploiting forestry resources, weak enforcement of regulations, and the lack of a well-defined, long-term forestry development plan. Formulation of the Program was carried out without the benefit of a program preparatory technical assistance. Sector analysis was inadequate with overoptimistic or unrealistic targets both in regard to the policy reform measures and the investment component.

The Program's objectives were to (i) encourage forestry sector policy reforms, and (ii) support the necessary institutional restructuring. The Program comprised two main components: (i) policy and institutional reforms aimed at restructuring the Ministry of Forests and Soil Conservation (MFSC) and increasing the role of the community and private sector in forest management; and (ii) investment aimed at reforesting degraded forests, improving management of natural forests, restoring major watersheds, protecting the habitat, establishing biogas plants, and supporting medicinal and aromatic plant cultivation. Two technical assistance (TA) grants accompanied the Program to enable the Government to carry out (i) monitoring and evaluation (M&E), and (ii) equitable and efficient energy pricing policies. The Asian Development Bank (ADB) provided a loan of \$40 million equivalent and TA grants of \$698,000. The loan was to be released in two equal tranches once the specific conditions for each tranche were met.

The overall implementation of policy reform measures was partly effective. Failure to comply with some policy conditions, particularly the passage of the Forestry Act and its enabling bylaws, led to the cancellation of the second tranche. A few of the important policy conditions have remained unfulfilled to date (such as the establishment of a reforestation fund and the promotion of private forestry) because they are no longer relevant or circumstances have changed. Many of the second tranche conditions were fulfilled after the program period.

The most effective element was the policy reform on community forestry where the targets for the formation of user groups and the area of natural forests handed over to user groups were exceeded. But implementation of leasehold forestry was not effective due to practical difficulties involved and the Government's preference for community forestry. Institutional reform measures aimed at strengthening the various departments within MFSC were implemented with varying degrees of success.

The performance of the investment component, affected by the delay in the passage of the Forestry Act, was generally poor. While targets for setting aside land for habitat protection,

for the establishment of biogas plants, and for support to farmers growing medicinal and aromatic plants were met, only partial achievement was realized in the more critical subcomponents of reforestation (less than 40 percent), natural forest management (about 20 percent), and forest plantation and other area-based soil conservation treatments (48 percent).

Program implementation was hampered by the lack of capacity in the field to organize the human resources, equipment, and material necessary to carry out the investment component of the Program. Administrative and coordination weaknesses in MFSC were compounded by the lack of an acceptable M&E system in addition to the frequent changes of staff. The close monitoring of ADB through various review missions apparently did not impact significantly on the effective implementation of the Program.

Non-compliance with loan covenants on major policy reforms relate to the failure to pass the Forestry Act, select leaseholders for award of leasehold forestry, create a reforestation fund, and specify forest products to be prohibited for export. This led to the cancellation of the second loan tranche. Compliance with administrative covenants was generally better. Compliance with covenants relating to the use of funds under the investment component was not fully fulfilled, particularly that on the use of counterpart funds to establish large-scale plantations and natural forest management.

The two TAs were not effective. An effective M&E system was not put in place. Support for the M&E division was not apparent within MFSC and the division was not in a position to exert any influence on the compliance of some of the major reform measures. The lack of a full-time program director further constrained monitoring of the Program. The Government did not follow through with the recommendations on equitable and efficient energy pricing policies.

As for program results, reforestation of forests was only partly achieved, mainly with encouraging response to community forestry. The original target of forestland to be handed over for community forestry was exceeded by more than 100 percent. The priority given to community forestry and the Government's readiness to hand over forest management to local community user groups marked a very significant change in policy implementation.

Reforestation through leasehold forestry was only partly effective as leaseholders were mainly confined to poor farmers' groups (with a very insignificant area allocated for industrial leasehold forestry). The issue is whether such an approach could be sustainable as no fees were levied, or whether it would be adequate as such leases were given in small parcels.

Institutional development performance under the Program was partly effective. Satisfactory strengthening was achieved with the organizational structure of the Department of Forests to reflect changing priorities brought about by the emphasis on community forestry. In contrast, the M&E capability of MFSC was not significantly improved. The success in the formation of the forest user groups is the most significant change in institutional development brought about by the Program.

Income improvement resulted from the harvesting of forest products (fuelwood, herbal plants, etc.) and employment opportunities from reforestation and conservation activities. The Program did not have a specific component targeted at gender development. However, the primary products of several of the investment projects were fuel and fodder, and the Program substantially reduced the burden of gathering these products, a major task allocated to female members of the household. The Program included training courses for women in agriculture and

forest management. It contributed positively to the environment, particularly through its subcomponents on community forestry and soil conservation.

A key issue is the role of private sector in forest management. Leasehold forestry, the apparently least effective of the measures, was intended to provide the opportunity for private sector involvement in forest management. But private sector investment was not encouraged by the various stiff conditions required for its participation. Another issue is the need to address the basic cause of forest degradation, i.e., poverty and vested interest, before reforestation and other forest activities are pursued. A third issue concerns the absorptive capacity of the Government requiring rationalization of various offers of external assistance to effectively use the existing staff capacity. This is linked to the fourth issue of streamlining the mechanism for coordination of aid agencies.

The performance of the Forestry Sector Program Loan is rated less than successful.¹ The design of the Program could have focused more directly on addressing the needs of the poor. The program components taken as a whole were partly effective in terms of the policies to be pursued and the investment targets undertaken. Many of the policy reforms have since been fulfilled. A positive result of the Program was the policy thrust favoring community forestry through forest user groups. Overall impact on institutional development is partly effective.

Lessons learned include the need for components of a forest management program to address poverty and the vested interests (including illegal loggers and encroachers); program design and target setting should be based on a credible forest management plan; an M&E system should be established early during program implementation; and government ownership of TA should be obtained.

For follow-up actions, the Government should streamline the Forestry Sector Coordinating Committee and ensure that the Committee meets every quarter. The Government should have the M&E system in place by the end of 2001.

¹ This is on a four-point scale of highly successful, successful, less than successful, and unsuccessful.

I. BACKGROUND

A. Rationale

1. Forests and forest resources play a vital role in Nepal's economy and ecology. Forest degradation and destruction of the decades prior to 1989 was the result of indiscriminate and excessive exploitation. A high incidence of rural poverty, an inappropriate legal framework for exploiting forestry resources, weak enforcement of regulations, and the lack of a well-defined, long-term forestry development plan are all reasons for an alarming degree of forest losses in Nepal and damage to the fragile Himalayan ecosystem. The Government developed a Master Plan for the Forestry Sector (MPFS) with joint technical assistance (TA) from the Asian Development Bank (ADB) and the Finnish Department for International Development Cooperation (FINNIDA).¹ The Plan, together with the new Forestry Sector Policy approved in 1989, called for, among others, accelerated reforestation of degraded forestland, particularly through community and private sector involvement.² At the time, various aid agencies were assisting in several individual forestry projects, most of which were investment projects focusing either on specific geographic areas or specific aspects of forestry development.³ None of them really addressed policy reform issues.⁴ A sector approach was needed to address the sector-wide problems (particularly those relating to the inappropriate policy and legal framework) and to fund a comprehensive program of activities. The Forestry Sector Program Loan (FSPL) of ADB was intended to be the first phase of the Government's systematic efforts to restore the forest cover and reduce rural poverty. The rationale for the FSPL was relevant as the natural forests continued to be degraded (about 1.3 million hectares [ha] have been deforested in the last 16 years).

B. Formulation

2. No program or project preparatory TA (PPTA) was implemented, even though the FSPL included investment projects. In response to the request for assistance, ADB sent four fact-finding missions to the country from February to September 1989. The missions were part of a continuing policy dialogue initiated during the preparation of the MPFS and, concomitantly, with

¹ TA 670-NEP: *Forestry Development*, for \$1.35 million, approved on 20 February 1985, with \$1.10 million from Finnish Department for International Development Cooperation (FINNIDA) and \$250,000 from Asian Development Bank (ADB).

² The Ministry of Forests and Soil Conservation (MPFS) proposed 12 development programs with major emphasis on community and private forestry (46.6 percent of the budget) and national and leasehold forestry (with 20.2 percent). Other objectives included meeting people's basic needs for fuelwood, timber, fodder, and other forest products, protection against degradation, and promoting participation in forestry resource development.

³ For example, *Forestry Sector Institutional Strengthening Program* (grant assistance of \$1.156 million from FINNIDA), *Forestry Development Project* (\$8.0 million grant assistance from the United States Agency for International Development), and *Hill Community Forestry* (Phase III - \$30.5 million from the International Development Association, World Bank). ADB was implementing Loan 749-NEP: *Third Forestry Development Project*, for \$10 million, approved on 31 October 1985 and closed on 15 July 1991.

⁴ The MPFS indicated that major reforms were needed in government forestry policy and regulations.

another TA to assist in the implementation of the MPFS.⁵ These missions apparently served in lieu of a PPTA. An appraisal mission subsequently visited Nepal in October 1989 and policy reform measures were mapped out and reflected in the Government's Development Policy Letter to ADB. While there was close consultation with the Ministry of Forests and Soil Conservation (MFSC) (the Executing Agency [EA]), and other implementing agencies in the course of the missions, there was no evidence of any intensive consultation with target beneficiaries. Neither was there much consultation with local communities or the private sector during the preparation of the MPFS upon which the investment projects and activities of the FSPL were based.⁶ Loan negotiations were held in August 1990 and the loan was approved in October 1990. The FSPL was the 65th loan to Nepal, the fourth in the forestry sector, and the second program loan to the country. However, many of the FSPL subprogram targets were not met; some of these targets were too optimistic or unrealistic, suggesting that any sector analysis undertaken during the preparation of the program was inadequate. No proper forest inventory or detailed forest management plans were available at the start of FSPL implementation.⁷

C. Objectives and Scope

3. The FSPL had the twin objectives of encouraging forestry sector policy reforms, and supporting the necessary institutional restructuring, which would ensure that the Government's efforts resulted in an efficient and sustainable program for development of forest resources. The FSPL consisted of two main components: policy and institutional reforms and investment. The policy and institutional reforms were aimed at restructuring and reorganizing the MFSC and increasing the role of the community and private sector in reforestation, management, and utilization activities. The investment component was aimed at reforesting degraded forests, improving management of natural forests, restoring major watersheds, protecting and maintaining the habitat, establishing biogas plants, and supporting medicinal and aromatic plant cultivation. Improvements were to be achieved in (i) the quality of decisions on investment and management of reforestation programs, (ii) efficient and equitable forest-product pricing strategies on a competitive market basis, (iii) more effective forest regulations, and (iv) a policy regime that would encourage environmentally sustainable development of forest resources. No logical framework for the FSPL was prepared.⁸ The major investment targets were set out in the policy reform matrix (Appendix 1).

4. Two TAs relating to the forestry sector were provided along with the loan to enable the Government to carry out monitoring and evaluation (M&E), and equitable and efficient energy pricing policies. Special assistance for M&E of the program was required to ensure that a comprehensive, nationwide M&E system was established. The study on energy pricing policies was to help develop policies for rationalizing fuelwood and commercial energy demand. MFSC was the EA for the TA on M&E while the Water and Energy Commission Secretariat was the EA for the TA on energy pricing policy.

D. Financing Arrangements

⁵ TA 1120-NEP: *Implementation of the Master Plan for the Forestry Sector Project*, for \$724,000, approved on 6 February 1989 and cofinanced with FINNIDA.

⁶ Report of the Government of Finland, *Forestry Sector Cooperation between Nepal and Finland: Review of Past and Current Developments and Preparation of Possible Future Cooperation*, December 1995, p.41.

⁷ A point confirmed by the Government's program completion report dated October 1996.

⁸ The use of a logical framework was not a requirement at the time of program preparation.

5. ADB provided a loan of SDR29.193 million (\$40.0 million equivalent) and TA grants of \$698,000. The Loan Agreement became effective in December 1990. The loan proceeds were used to finance the foreign exchange component of eligible imports. The Government was expected to draw down the foreign exchange proceeds of the loan by 31 December 1993. The loan was to be released in two tranches, with the first tranche, amounting to \$20 million, drawn down on the date of loan effectiveness. The second tranche of \$20 million was to be released when the Government met its program commitments. The program period was intended to be from fiscal year (FY) 1990/91 to FY1994/95. Total external assistance committed to the country during the period was \$1.60 billion while total disbursements amounted to \$2.07 billion (Appendix 2).⁹ The Program loan of \$40 million would have represented about 12 percent of the total amount disbursed to the agriculture, forestry, and fisheries sector during the program period, if the full amount of the FSPL had been released.

E. Aid Agency Coordination

6. Coordination with other aid agencies was undertaken during loan processing through the usual consultations during fact-finding and appraisal missions. It was necessary to institutionalize coordination both among aid agencies and between aid agencies and the Government. This led to the Government's establishing a Forestry Sector Coordinating Committee (FSCC) prior to loan effectiveness. The FSCC was scheduled to meet quarterly, but did not convene this frequently. The FSCC still existed at the time of the Operations Evaluation Mission (OEM) but had grown rather unwieldy with the inclusion of various government agencies and nongovernment organizations. Meaningful discussions of issues of concern to aid agencies were difficult in the presence of such a big group of participants with varied interests. A smaller group or subgroup of representatives from aid agencies and the relevant central agencies of the Government meeting quarterly would have been more effective. Despite such efforts at coordination, duplication of effort by the Program and projects of other aid agencies became apparent during FSPL implementation. An example is the case of the biogas component. Under the FSPL, Biogas and Agricultural Equipment Development Pty., Ltd. was to establish 5,000 biogas plants to be funded through the Agricultural Development Bank of Nepal (ADBN). However, the ongoing Biogas Support Program supported by the Dutch Government already had an agreement with the company to establish biogas plants and so the company was too busy to be able to implement the FSPL's biogas component. Other private biogas companies were used instead. The FSPL was also seen by other aid agencies as contributing to the oversupply of development funds that could not be effectively absorbed by the country at the time of implementation.

F. Program Completion Report

7. The program completion report (PCR) was circulated in May 1998, and was, in general, adequately prepared. It provided comprehensive information on the status of implementation of program components, a balanced discussion of the status of compliance of covenants, and a

⁹ Data on commitment from the Ministry of Finance appeared to be underestimated though the difference in reporting period (fiscal year and calendar year) could be a reason (see Appendix 3). Data on disbursements for the corresponding period from the Ministry of Finance were not available.

fair assessment of the impact of the FSPL. Because of delays in the implementation of policy reforms and unrealized investment targets of some components, the PCR considered the Program partly successful.¹⁰ Based on information available at the time, this rating was appropriate. The PCR indicated that the FSPL was instrumental in triggering sector policy reforms and in achieving a major shift in emphasis to community-based forest development and management of natural resources.

G. Operations Evaluation

8. This program performance audit report (PPAR) focuses on pertinent aspects of the FSPL and presents the findings of the OEM, which visited Nepal from 27 March to 10 April 2000. The PPAR also assesses the FSPL's effectiveness in achieving its objectives, and its sustainability.

9. The PPAR is also based on a review of the PCR, the Report and Recommendation of the President (RRP), material in ADB files, and discussions with staff members of ADB, MFSC, implementing agencies, other government agencies, and with representatives of the funding institutions and the private sector. Copies of the draft PPAR were provided to the Government, MFSC, and ADB staff concerned for review and comment. Comments received were taken into consideration in finalizing the report.

II. IMPLEMENTATION PERFORMANCE

A. Policy Reform Measures

10. The overall implementation performance of policy reform measures was only partly effective due to numerous factors, including political and institutional changes. These include the democratization process in 1990-1991, a trade and transit dispute with India in 1989-1990, civil service reform in 1993 leading to staff reduction, and political instability in 1994-1995 resulting in changes in government. Most of the policy reform measures were time-bound. Some were to be accomplished prior to the loan negotiations or loan effectiveness.¹¹ Three others were specifically dated¹² while the majority were to be completed prior to the release of the second loan tranche. The fact that many of the latter were not accomplished led to the cancellation of the second tranche.

11. The more effective measures that contributed to the better performance of the FSPL were those aimed at encouraging local participation in forest management and protection through forest user groups. To support this approach, the Government strengthened the Community and Private Forestry Division of the Department of Forests (DOF). Formation of

¹⁰ This is on a three-point scale adopted at the time of project completion report preparation of successful, partly successful, and unsuccessful.

¹¹ For example, selection of leaseholders for implementing the leasehold forestry program and appointment of a high-level officer to oversee implementation of the Program.

¹² Approval of national forestry conservation guidelines by January 1991, establishment of 600 user groups by June 1992, and the handing over of 65,000 hectare (ha) of national forests as community forests by June 1992.

forest user groups was at first tardy with only 105 groups formed during the program period against a target of 600 user groups. Delayed enactment of the Forestry Act and promulgation of the enabling bylaws meant an inadequate legal basis for user groups in community forestry.¹³ Nevertheless, user group formation continued and by FY1995/1996, 1,026 groups had been established, far exceeding the original target. Against a target of 65,000 ha of national forests to be handed over to user groups as community forests, about 157,500 ha were handed over by the time of the OEM, a substantial improvement over the 280 ha handed over during the program period.¹⁴

12. The enactment of the Forestry Act, the promulgation of associated bylaws, and the strengthening of the Community and Private Forestry Division of DOF were consistent with the forestry sector strategy and Government policy. In keeping with the MPFS's important strategy of reducing the Government's role in reforestation by force account (that is, through the relevant government departments' own efforts or management), the FSPL included policy measures aimed at encouraging leasehold forestry. However, the reform measures involving the award of 2,500 ha of leasehold forestry and 1,200 ha of contract reforestation prior to the release of the second tranche of the program loan could not be fulfilled during the FSPL period and provided one of the major reasons for the cancellation of the second tranche.

13. The non-compliance of reform measures affecting the award of leasehold forestry and contract reforestation was largely due to the delayed enactment of the Forestry Act and the associated bylaws. Procedures for awarding reforestation contracts to private contractors were already finalized prior to loan negotiations (a policy reform condition under the FSPL) but could not be implemented. Fundamentally, preference has been given to community forestry that involves forest user groups as a way to protect the forests. The Government saw the formation of user groups as a sound and effective approach to forest management. These group members, living on site, have an interest in protecting, maintaining, and managing forest resources to maximize a sustainable yield of both timber and nontimber forest products. As these groups comprise private stakeholders, their participation is in line with the privatization strategy enunciated in the MPFS, notwithstanding that in reality the land area that can be managed by a user group is relatively small (average 50 ha). Less emphasis was given to leasehold forestry due to practical difficulties that will be discussed under the investment component of the FSPL (para.15), even though national and leasehold forestry was considered the second most important development program in the MPFS.

14. Many of the policy or administrative measures that were to be taken prior to the second tranche release were either fully or partly implemented after the close of the FSPL. They include specification of the class and type of products prohibited for export, contract reforestation, and leasehold reforestation (to poverty groups). However, some of the substantive policies remain unimplemented, namely, the creation of a reforestation fund, industrial leasehold reforestation, large-scale forest plantation, and the appointment of task force to analyze the extent of subsidies in the price of fuelwood. The reforestation fund needed Ministry of Finance (MOF) agreement, but it was reluctant to support the creation of dedicated off-budget funds over which it had no control. Given the emphasis on community forestry, the establishment of a reforestation fund was no longer pursued. Nevertheless, MFSC, in an effort to secure dedicated funds, requested the establishment of a forestry sector development fund with a broader mandate. Institutional reform measures designed to strengthen the Community and Private Forestry Division, and Forest Management and Utilization Division, of DOF, and the Parks and

¹³ The Forestry Act was passed in 1993 and the enabling bylaws were promulgated in 1995.

¹⁴ MFSC supplied these data to the Operations Evaluation M. There was no other source to verify their accuracy.

Reserves Division of the Department of National Parks and Wildlife Conservation (DNPWC) were implemented with varying degrees of success. On the positive side, staff members of the Community and Private Forestry Division have been increased so that forest user group applications can now be processed in an orderly fashion, potential forests can be delineated and inventoried, forest management plans can be drawn up, and forests can be handed over to applicants.

B. Investment Component from Counterpart Funds¹⁵

15. The investment component of the FSPL was to be funded from counterpart proceeds generated from the foreign exchange funds of the FSPL and channeled through adequate budgetary appropriations during 1990 and each year thereafter. The appropriations were to meet (i) the cost of developing a minimum of 104,000 ha of forest (reforestation of 29,000 ha and improved natural forest management of 75,000 ha) under the national and leasehold forestry program, (ii) the cost of developing 1,000 ha for the cultivation of medicinal plants involving small farmers under the production of medicinal and aromatic plants and other minor forest products program, (iii) the cost of preventive and rehabilitative soil conservation measures under the soil conservation and watershed management program, (iv) the cost of habitat protection of 7,000 ha under the conservation of ecosystems and genetic resources program, and (v) the cost of setting up about 5,000 biogas plants under the establishment of biogas plants program. Efficiency of the FSPL with respect to the investment component could not be assessed. As this was a program loan, there was no economic analysis undertaken during appraisal. Neither did the PCR undertake an economic analysis as there was no benchmark economic data for meaningful analysis and comparison.

16. Under the national and leasehold forestry program, the reforestation target of 29,000 ha was to be achieved with 16,500 ha to be reforested by DOF on force account, 5,000 ha through forestry by private contractors, and 7,500 ha through leasehold forestry (5,500 ha family and 2,000 ha industrial). DOF in fact planned to reforest only 11,500 ha by force account as it thought this target was more realistic in contrast to the FSPL's target. It actually reforested about 9,040 ha during the program period (about 79 percent of its own plan). The Government allocated only 3,000 ha to private contractors for reforestation (about 60 percent of the target). As in the case of direct reforestation, DOF has its own target for leasehold forestry. It selected 248 leasehold farmer groups, and awarded 1,565 ha of leasehold forest out of its own target of 2,500 ha (63 percent) instead of 5,500 ha. The Government did not allocate any industrial leasehold forestland during the program period. At the time of the OEM, only about 110 ha had been leased for industrial purposes.

17. Many practical problems confronted the leasehold forestry program. Leasehold forestry was intended to provide an opportunity for the private sector to be involved in forest management. But intending participants had to face various rigorous conditions required of leaseholders, the lack of specific guidelines for considering applications, and inadequate information provided to interested parties. There was also the political dimension of who should be allocated the land and at how much, when wealthy politically connected urban individuals or tribal chiefs were also interested parties. The result was that participation in leasehold forestry

¹⁵ The usual sector development program loans include investment lending and policy-based assistance. The investment component of the Forestry Sector Project Loan is funded from the counterpart funds generated from its foreign exchange proceeds.

was confined to those families falling below the poverty line; no fees or rent were collected. Leasehold forestry for industrial purposes (e.g., timber supply for construction) was also not favored. Fundamentally, private sector reforestation (whether through leasehold or contract planting) was not favored at the time of the OEM. The consensus in DOF was that it would be resolved through natural forest management and community forestry programs. But this runs counter to the strategy of the MPFS which, apart from its stress on community forestry, also places strong emphasis on private sector participation (by entrepreneurs) in forest management through leasehold and contract reforestation.

18. The target for improved natural forest management of 75,000 ha comprised 60,000 ha for timber stand improvement, pruning, and thinning and 15,000 ha for scrubland management. During the program period, management activities were carried out on only 5,082 ha (7 percent). Timber stand improvement activities were carried out on only 2,838 ha (5 percent) while scrubland management was carried out on only 2,244 ha (15 percent). The target for natural forest management was too ambitious, particularly when proper forest management plans did not exist and strategies for natural forest management were not clearly spelled out at the time of program implementation. Scrubland management activities were focused on the Terai, lowland areas where very little scrubland exists. An appropriate inventory of the problem area was not carried out. Efforts to implement the Program did identify the lack of management plans as a constraint and eight management plans were prepared and four were updated during the program period. The Government plans to intensify its natural forest management activities with 368,164 ha as the target for the next five years.

19. The FSPL support to the medicinal and aromatic plants program was partly effective. Against a target of 600 farmers, support was provided to 1,815 small farmers in the cultivation of medicinal and aromatic plants. The purchase of crude herbs was only 204 tons, which is about 19 percent of the target of 1,096 tons. In contrast, the target for the production of extracts was 1,231 tons while actual production was 2,178 tons (177 percent). Production of essential oil at 74.6 tons from all the farms organized by the Herbs Production and Processing Co., Ltd. (HPPCL) was below the target of 106 tons.

20. Targets in the soil conservation and watershed management program were partly achieved. The target for forest plantation and other area-based soil conservation treatments was 5,200 ha. Only 2,500 ha were treated (48 percent). Against a target of 800 kilometers for shelterbelt, road-bank and other linear conservation treatments, only about 495 kilometers were completed (62 percent). The target for improving gully plugs, waterway protection, and other structures was 900 units, but only 566 (63 percent) were completed. The Government considered the targets as too ambitious given that it was difficult to select subproject areas: watersheds had to be selected and watershed management plans prepared. These activities took time and since there was no accepted consensus of what constituted successful treatment of a specific area, it was sometimes difficult to tell if a target was met.

21. The target set under the FSPL for setting aside 7,000 ha for habitat protection and maintenance was exceeded with 8,394 ha set aside. DNPWC conducted about 17 conservation education seminars, far exceeding the target of seven.

22. The FSPL target under the biogas program was to help 5,000 biogas plants. In total, the Program supported the establishment of 5,295 biogas plants (106 percent).

C. Procurement and Distribution

23. Procurement contracts under the Program were made in accordance with Government procedures acceptable to ADB. A negative list was used for financing eligible imports from the foreign exchange proceeds of the loan. The loan was to be disbursed in two equal tranches. The first tranche of \$20.968 million was given in December 1990. It was fully liquidated in January 1994. The release of the second tranche was cancelled at the request of the Government. The loan account was closed on 31 January 1994.

D. Organization and Management

24. The EA for the FSPL was MFSC with the ADBN and HPPCL as participating agencies for the investment subcomponents of biogas plants, and medicinal and aromatic plant production, respectively. Implementing agencies included the various departments under MFSC with the Monitoring and Evaluation Division (MED) of MFSC as the monitoring and coordination body. The failure to establish an M&E system during the Program was a serious shortcoming in monitoring implementation in an integrated manner and in providing information for corrective or adjustment measures.

25. Program implementation was hampered by the lack of capacity in the field to organize the human resources, equipment, and material necessary to carry out the investment component of the FSPL. The weaknesses in MFSC headquarters with regard to FSPL administration and coordination were compounded by the lack of an acceptable M&E system and adequate staff capacity to handle the various projects in the same sector assisted by different aid agencies. MFSC failed to appoint a full-time coordinator of the FSPL and frequent changes of staff dealing with the FSPL inhibited continuity. Administrative weaknesses in MOF regarding timeliness of release of budget funds and of approval of district budgets to accomplish agreed targets, added to implementation difficulties. From the onset, ADB closely monitored the performance of the FSPL with four reviews and two special administration missions, as there were implementation problems from the start. Frequent changes to ADB staff were made (five officers administering the FSPL), but it is difficult to assess whether such frequent changes affected implementation significantly.

E. Effectiveness of Technical Assistance

26. Implementation of the TA on M&E (para. 4), originally intended to monitor and evaluate FSPL activities, was delayed to await the establishment of an M&E system under a separate TA from FINNIDA. When it became apparent that this new M&E system would not be established, the ADB TA was then implemented in 1995 to design an M&E system and obtain data to measure the results of the FSPL. By then, however, it was too late for the ADB TA to be fully effective as initial benchmark data for comparison purposes could not be compiled. The Loan Agreement had become effective in December 1990. The TA report was presented to the Government in June 1996, after the Program had been officially completed. Nevertheless, the training received by the counterpart staff in MED and the data gathered under the TA apparently helped the Government prepare its own PCR. Yet the TA has not significantly strengthened the M&E capability of MED. The current M&E system is still limited to monitoring physical progress of projects and programs, not benefits and impacts on the beneficiaries. The number of MED professional staff has been recently increased from 2 to 10 and this should boost the capacity of

MED to provide more accurate data. However, any M&E system is subordinate to the current M&E system that the National Planning Commission (NPC) is setting up.¹⁶ The TA has not been effective in achieving its main purpose of monitoring and evaluating the FSPL, nor has it led to the establishment of an effective M&E system. This TA is therefore rated unsuccessful.

27. The TA on equitable and efficient energy pricing policies (para. 4) was implemented. The report of the study was submitted to the Government in 1994. No government follow-up on the recommendations of the report seems to have been made in regard to (i) encouraging industrial enterprises to increase efficiency of energy use, (ii) eliminating all subsidies, and (iii) commercializing the operations of enterprises in the energy sector. The EA for the TA was not part of MFSC and any recommendation on energy pricing policies was to be considered within the EA's own priorities and policies in regard to the management of energy and water resources. This TA is therefore rated unsuccessful.

F. Compliance with Loan Covenants

28. The covenants of the FSPL (Appendix 3) can roughly be divided into four categories: (i) policy reforms, (ii) administrative measures, (iii) investment component, and (iv) other covenants. Some policy covenants that were not fulfilled (as they were second tranche release conditions) included the passage of the Forestry Act and enabling bylaws, selection of leaseholders and award of leasehold forest, and specification of forest products to be prohibited for export. While nonfulfillment of these conditions led to the cancellation of the second tranche, many were subsequently fulfilled by the end of the FSPL period. But some remained unfulfilled even at the time of the OEM. These include the establishment of a reforestation fund and the implementation of the recommendations of the study on equitable and efficient pricing of fuelwood and commercial fuels. The establishment of the reforestation fund was no longer pursued by the Government as there was a change in emphasis to natural reforestation (that is, through natural growth of indigenous species) through community forest management and conservation measures. The administrative measures complied with include depositing counterpart funds in a special account, using the counterpart funds to finance five specific programs, and giving highest priority to the national and leasehold forestry program. Measures partly complied with include seeking adequate appropriations to meet identified targets of the investment programs to be supported by the loan, implementing the necessary policies for awarding timber harvesting rights on a competitive bidding system, and rationalizing and modernizing wood-based industries. Many of the administrative covenants were framed in an unmonitorable manner in which compliance could easily have been deemed fulfilled. An example is the requirement to give the highest priority to the national and leasehold forestry program. Such a priority was already part of the MPFS of 1989.

29. Covenants relating to the investment component were associated with some of the more serious shortcomings. The Government, for instance, technically complied with the covenant stating that counterpart funds may be utilized to finance timber stand improvement activities, and scrubland management as part of the natural forest management program by using the funds in 18 districts of the Terai areas. But only about 5 percent of the target for timber stand improvement and 15 percent for scrubland management was achieved (para. 16). The same

¹⁶ The National Planning Commission is the Executing Agency for ongoing TA 2954-NEP: *Strengthening the Project Performance Management System*, for \$500,000, approved on 19 December 1997. Monitoring and evaluation (M&E) components would be subsumed under the PPMS.

can be said for the counterpart funds to be used for the national and leasehold forestry program as well as the soil conservation and watershed management program. The covenant to use the counterpart funds to support the development of the medicinal and aromatic plants program was well complied with as the targets were fully met. The Government also adequately complied with the covenant to utilize funds to finance expenditures for the conservation of ecosystems and genetic resources as well as to establish biogas plants. Nevertheless, it could not comply with a significant covenant stating that it should use counterpart funds to establish large-scale plantations either using DOF itself, or helping lessees or user groups develop large-scale plantations with DOF working with ADBN. Government efforts to attract leaseholders from the private sector (other than poor farmers) to participate in forest plantation were unsuccessful. The covenant requiring large-scale plantation by DOF itself might not have been appropriate given that there was limited government experience in large-scale plantation and in working the terrain of the country.

30. As for the other covenants, a covenant on the use of funds to establish the Nepal Conservation Training and Research Institute was not fulfilled as the funds for the Institute came from the King Mahendra Trust for Nature Conservation. Those relating to reporting requirements, independent M&E of FSPL accomplishments and impacts, carrying out a benchmark survey of farmers, and undertaking feasibility studies of biogas plants, were not complied with. There were partial attempts using the counterpart funds to carry out site surveys and appraisals for plantation development programs but nothing came of them. Generally, much of the non-compliance of the reporting covenants was due to MFSC's unfamiliarity with ADB's procedures, or the need to set up a different system for monitoring progress from the one which MFSC already used, particularly in regard to supplying detailed data, or MFSC's lack of capacity and commitment as seen in its failure to carry out benchmark surveys and feasibility studies. Benchmark surveys would have provided the basis for a proper evaluation of the impact of FSPL, while Feasibility studies would have determined the economic and financial value of the subprojects.

G. Monitoring

31. An M&E system was not in place at the beginning of the Program. Monitoring of compliance of the FSPL's policy reform measures and the covenants should have been the task of MED. However, MED was inadequately staffed at the time of program implementation, while its supervisory staff lacked timely and accurate data on the FSPL's performance. MED's importance has not really been recognized within MFSC and it was often left out of major programming work within MFSC. MED was not in a position to exert any influence on the compliance of some of the major reform measures, such as the passage of the Forestry Act, the delay of which was beyond the control of MFSC given the political environment at the time. The failure to assign a full-time staff as program director exacerbated the difficulties in supervising progress of the FSPL. This was to a degree unavoidable given the political uncertainties and the consequent changes in the civil service during 1990-1993. Establishing an M&E system early in the program period could have improved the FSPL's performance. In fact, concerns were raised at the ADB Board on MFSC's capacity to monitor implementation and effectiveness of the FSPL. Had there been an early warning system, remedial actions could have been taken to ensure that the targets were achieved.

H. Use of Counterpart Funds

32. The use of counterpart funds was prioritized in the covenants as essential to support the investment component of the Program. They were deposited in a special account at the central bank that could be drawn down by MOF and channeled through the budgetary process. They were used to meet the investment costs of the Program. A total of NRs631 million (\$12.7 million based on the average exchange rates from 1992 to 1996) were released between FY1991/92 and FY1995/96. The actual budget allocations to the districts were not enough to complete the investment targets. In the aftermath of the democratization process, there was in fact no budgetary allocation for development projects in 1991, the first year of the FSPL period. This was in contrast to the stated position at the time of cancellation of the second tranche. When the Government requested the cancellation of the second tranche, it indicated that the counterpart funds from the release of the first tranche would be sufficient to implement the FSPL's investment component. It is difficult to assess whether the counterpart funds were especially earmarked as additional to the normal budget allocation of MFSC. The fact that the Soil Conservation and Watershed Department as well as district offices experienced difficulties in obtaining adequate budgetary provisions for their activities indicates that problems occasionally arose in using the counterpart funds for their stated purposes.

III. PROGRAM RESULTS

A. Performance Indicators

33. The FSPL was to help restore forests to meet the country's need for fuelwood, timber, and fodder and to preserve the vital Himalayan ecosystems within an improved policy environment. It was expected that these efforts would reduce rural poverty, which was a major cause of forest destruction. No mechanism, such as a logical framework, was prepared during appraisal that identified the relationship between the proposed activities and the social and/or economic objectives, nor were the key performance indicators identified. The extent to which the objectives of the Program have been achieved and sustained would have been a key performance indicator. Economic benefits from the investment component would also have been important indicators. However, no rigorous economic analyses were undertaken at appraisal or at the PCR stage. Data on physical achievements, such as area reforested, conservation education seminars presented, etc., were available but the link between these figures and a major goal of the FSPL, reducing rural poverty, was very tenuous. Other possible indicators would have shown whether the environmental improvement that was to be pursued through the reform measures had been realized and, if so, to what extent.

34. Restoration of forests was achieved to some degree with the encouraging response to community forestry. Even though only 280 ha of forests had been handed over for community forestry at the close of the program period, at present, more than 157,000 ha have been handed over for community forestry, which far exceeds the original target of 65,000 ha. However, the mere handing over of forests to user groups does not ensure sustained forest management. The user groups have to be strongly supported by the Government at all levels against encroachment by vested interests (especially illegal loggers and encroachers) particularly in the Terai areas. Much of the community forestry program was confined to the middle highlands

where encroachment by powerful parties is less frequent but still real. The progress made in community forestry during and after the program period was also due to assistance from other aid agencies.¹⁷ The priority given to community forestry and the apparent readiness of the Government to hand over forest management to local community user groups mark a significant change in policy application. The Government felt that community forestry would provide the means of reforesting degraded forestland, and so provide fuelwood and fodder to the rural communities in a sustainable manner and stem deforestation in the region. However, as the land given for community forestry was often in small separate parcels there would be some environmental implications in terms of the forest surrounding the community-managed land. When a community forest was allocated to a community, the forest was protected from grazing, fire, and trespassing, resulting in substantial natural forest growth. People who were excluded from their previous sources of fuel and fodder had to find their sources elsewhere, and these were often on the land adjacent to the community forest. An “edge effect” was often created where the community forest was protected and growing strongly, but the land around the perimeter was stressed through unsustainable harvesting. The answer is to have a contiguous area of community forest where local communities will protect all the area.

35. Reforestation through leasehold forestry was only partly effective, particularly in regard to industrial leasehold forestry (only 110 ha at present). The allocation of leasehold forest to private individuals, an important strategy in the MPFS, was scarcely achieved. Its success was confined primarily to individual families below the poverty line, and these allocations were given free. About 1,560 ha (compared to a target of 2,500 ha under the FSPL) have been awarded. The OEM sees this as an attempt to address the fundamental cause of forest degradation, namely poverty, though the intent was apparently different from that at appraisal. While this development may be consistent with the objectives of the FSPL, such an approach is not sustainable as no fees are levied, and is inadequate as the leases are given in small parcels.

36. Leasehold forestry, together with contract plantation, aimed at reducing the role of the Government in large-scale reforestation. The Government had limited success in promoting sustainable reforestation by private groups through leasehold and contract forestry, which means that the reform measures have been ineffective in getting the right groups in the private sector to undertake reforestation on a large-scale as intended in the MPFS. The habitat protection and maintenance, and the soil conservation and watershed management targets, were met but the implementation of intensive natural forest management activities such as timber stand improvement, thinning, weeding, and in-planting achieved only limited success.

37. The annual value of the estimated increase in the production of fuelwood on the 6,105 ha completed at the end of the FSPL period and designated as community forest was estimated to be approximately NRs43.7 million or about \$643,000 (at the exchange rate during the OEM) all of which will be realized by farm families in rural communities. The total national forest area handed over between 1991 and 1996 was estimated to be 157,000 ha. Using the same estimates for increases in firewood production and values for firewood used in the previous estimate, the annual increase in benefits realized by rural farmers would be more than NRs1 million (about \$15,000) per year. The number of biogas plants built under the FSPL was 5,295. The annual saving in firewood, a value directly realized by farm families in rural communities, was approximately NRs33 million (\$485,000). Employment in the medical and aromatic plant

¹⁷ For example, *Community Forestry Development Program* (Phase III - \$15.5 million loan from World Bank/United Nations Development Programme for the period 1990-1996), *Nepal Australia Community Forestry Project* (Phase IV - \$7.12 million grant from Australian Government, 1991-1996), *Dolakha Ramechlab Community Forestry Development Project* (\$3.70 million grant from the Swiss Development Cooperation, 1991-1996), and *Community Forestry Training Project* (\$6.04 million grant from the Danish International Development Agency, 1989-1996).

production program was approximately 2,800, which included 147 permanent staff, 2,000 part-time employees who collected plants, 300 who cultivated plants, and 380 who collected resin.

B. Institutional Development

38. Institutional development measures were directed at strengthening MFSC, particularly MED (through the TA on M&E), the Community and Private Forestry Division and the Forest Management and Utilization Division of DOF, and the Parks and Reserves Division of DNPWC. Efforts at strengthening MED were hampered by lack of staff (only 2 professional staff were employed until recently when the number was increased to 10) and the weak effectiveness of the TAs on M&E from both ADB and FINNIDA. Following the emphasis on allocation of national forests to user groups as community forests, DOF revised and strengthened its organizational structure to reflect changing priorities and prepared new job descriptions for all senior staff to reflect the new forestry policy. The strengthening of the Community and Private Forestry Division was important given the relative success in the number of forest user groups being formed. In 1995 (that is, at the close of the FSPL period), the primary factor inhibiting forest user group formation and community forest management was the lack of technicians and funds to support the community forestry program. Since then, enough technicians and support for the community forestry program have been mobilized not only to process user group requests but also to provide TA to the user groups on a continuous basis after the forests were handed over. Nevertheless, there is still a need to increase the number of technicians working at the regional level to support the community forestry program as forestry operations were decentralized by national, district, and local level. A significant change is that district foresters can now make most forest management decisions in the field within a broad policy set by DOF headquarters. Nevertheless, staff are still being moved too frequently both to and from the field, to and from regions, and within headquarters. Further, given the low salaries and the differences in daily allowances, DOF staff compete to be assigned to projects sponsored by aid agencies with negative implications for motivation and morale.¹⁸

39. The most significant impact of the FSPL in terms of institutional development is the increasing number of forest user groups being established and the priority that the Government gives to these groups as a matter of policy. Nevertheless, poachers and illegal loggers (especially in the Terai areas) often threaten the sustainability of user groups.

C. Socioeconomic Impact

40. While the basic cause for the degradation of forests has been poverty and strong vested interests, the FSPL's focus on reforestation, forest management, and conservation (as originally designed) particularly when involving the private sector, appeared to address the issue of poverty only indirectly. Community forestry through the use of user groups has good potential for poverty reduction only in so far as the user groups are deliberately selected from among the poor. Only in the case of the leasehold forestry program and poor farmer groups was the link to poverty reduction direct, but that was the result of deliberate Government policy rather than the design of the FSPL.

¹⁸ An individual working on a government-sponsored project receives a per diem of NRs100. If he or she works on a donor-sponsored project, it is NRs1000.

41. Income improvement resulted from the sustainable harvesting of forest products, particularly fuelwood; the sale of herbal and aromatic plants; and employment opportunities arising from reforestation and conservation activities. Based on a conservative figure of about 6,000 ha of land transferred to community forestry by the end of 1994 for instance, the value of the increase in fuelwood production accruing to farm families is estimated at about NRs18 million (\$265,000) in that year. The national and leasehold forestry, and soil conservation and watershed development component, have between them created about 510,000 person-days of employment annually with a total wage bill of about NRs24 million (\$353,000). The number of biogas plants established is 5,295. Based on the average benefit produced by each plant of NRs6,240 (\$92) per year, the estimated value of biogas production is NRs39.3 million (\$578,000) per year.

D. Gender Development

42. The Program did not have a component dealing directly with gender issues. Nevertheless, while the FSPL will benefit most of the people participating in the investment projects and their communities as a whole, some of the major beneficiaries will be women. The primary products of several of the projects were fuel and fodder, and the program substantially reduced the burden of gathering these products, a major task allocated to the female members of the family. Households using biogas reduced the use of firewood and lightened the burden (primarily on women) of gathering fuelwood. Women's training courses have also been conducted with the support of the district soil conservation and watershed management programs to strengthen women's knowledge and decision-making power with respect to such topics as forestry, agriculture, and conservation.

E. Environmental Impact and Control

43. The Program was intended to rehabilitate forests and prevent further forest degradation with the underlying purpose of improving and restoring the ecological balance of the environment. Its subcomponents relating to reforestation and natural forest management would have contributed substantially to forest rehabilitation had all the investment targets relating to forest plantations, leasehold forestry, timber stand improvement, and scrubland management been fully met. That the targets fell short (except for community forestry) certainly detracts from the full impact of the FSPL on the environment, but the impact is still positive. The greater success in achieving the targets in the components of biogas development, medicinal and aromatic plants, and soil conservation will help prevent further degradation of the forests. It is difficult to quantify the positive impact on the environment but the establishment of a forest plantation (as part of reforestation activity) alone will reduce erosion from 32 to 6 tons per ha per year based on the report prepared under the TA on M&E. Biogas plants produce approximately 14.2 million cubic meters of biogas each year. This is equivalent to the annual growth of 9,800 ha of fully stocked hardwood forest or 15,500 ha of fully stocked plantation saved for fuelwood purposes.

F. Gestation and Sustainability

44. Continuing efforts to promote community forestry can be expected, given the Government's priority and commitment to allocate forests to local forest user groups. However, community forestry is currently most successful in the middle mountain area while forest management in the Terai (or lowland) areas is left mostly to government programs. But it is in the Terai areas that forest encroachment is most rampant, not only by the poor but also illegal loggers. Industrial demand (for construction, furniture, etc.) adds to the pressure on forests. Community forestry programs run against strong interests in the Terai areas. The pursuit of community forestry renders the issue of establishing a reforestation fund less critical than previously thought because the Government expects forest user groups to sustain management of the forests. Such expectations may not be reached without corresponding efforts to implement (i) leasehold forestry on a large-scale, (ii) private reforestation, and (iii) better control of encroachment to accelerate reforestation of degraded land and to satisfy the demand for forest products. This is especially so when a longer gestation period is expected in the case of intensifying forest management on 75,000 ha of natural forest given the weak capacity of DOF. DOF has acknowledged that the quality of its staff needs improvement through further training in forest management. Industrial leasehold forestry is not vigorously pursued at present given the practical difficulties involved in the selection of potential lessees and other constraints.

45. The major reform measures centering on the passage of the Forestry Act and the enabling bylaws have been substantially implemented. But reforms relating to private forestry remain essentially unaccomplished. Risks to continuing the benefits (however limited) that have resulted from the FSPL relate to the sustainability of the reform measures and the investments made. Changes in policy could jeopardize these benefits. An example is a recent decree that banned the harvest of green timber for commercial purposes and that therefore provided a disincentive for any leaseholders because forest products from thinning, for instance, could not be sold. Although this decree was subsequently withdrawn, it created a cloud of uncertainty as to the Government's commitment to honor the terms of a lease. Such uncertainty could affect the forest management programs of current forest user groups and other lessees as well as the formation of future groups. The OEM believes that this is a genuine concern. Several aid agencies with programs in Nepal expressed their concern over the decree and the possible impact on their programs,

IV. KEY ISSUES FOR THE FUTURE

46. **Private Sector Participation.** The MPFS recognized the important role that can be played by the private sector in forest management. Leasehold forestry was intended to provide an opportunity for the private sector to be involved in forest management. However, the various stiff conditions required for leaseholders, the lack of specific guidelines for considering applications, and the inadequate information provided for interested parties, acted as a constraint for successful implementation of this program. Leasehold forestry was also intended to provide a wider opportunity for larger-scale forests plantation to be undertaken by investors (within the constraints imposed by the fragile ecosystems) and would provide a viable option to rejuvenate and maintain the forests faster and on a sustainable basis while providing the needed supplies for construction and other uses. The role of the Government in sustainable forest management needs to be reduced as envisaged under the MPFS.

47. **Preventing Forest Encroachment by the Poor.** A basic cause of forest degradation was the encroachment of forests by very poor rural farmers living nearby. Participation by the

rural poor in community and leasehold forestry activities will not be sufficient for reducing degradation when the farmers still need land for other economic activities (such as raising livestock and producing crops). Alternatives have to be provided to meet the immediate needs of rural farmers, or forests will continue to be under the constant threat of degradation. Forest management activities will have to be oriented toward the people living around the forests rather than be predominantly concerned with the number of trees or area to be replanted or rehabilitated. Only when such activities can be held in a proper perspective will reforestation, whether by the Government or the private sector, be sustainable. Agro-forestry would be one alternative that should be seriously considered.

48. **Absorptive Capacity of the Government.** The continuing interest of many aid agencies in the forestry sector assures that development assistance to the sector will be sustained. Nevertheless, the limited absorptive capacity of the Government must be recognized. It is not only a question of having enough staff but also of the quality and capability of staff, to manage the forests. The various offers of assistance need to be rationalized through a coordinating mechanism among aid agencies so as to effectively use and improve the capacity of existing staff and to prevent high turnover of better qualified staff (because of varying aid agency incentives). A basic concern is the commitment of forestry staff to better forest management.

49. **Aid Coordination.** Coordination of assistance by various aid agencies remains a key issue to prevent duplication of efforts and to take advantage of synergistic development efforts for the benefit of the country. While the FSCC provided the mechanism for such coordination, it met infrequently and apparently had not met in 18 months at the time of the OEM. Only the Government calls the meetings. Part of the reason for such infrequent meetings could be the Government's reluctance to discuss matters that are politically sensitive. The number of participants (more than 100 including nongovernment organizations) has become unwieldy and made the meetings unproductive. Even though subcommittees have now been formed, the meetings are still too large and are not informative enough. Under such circumstances, continuing dialog on policy reforms and other developments in the sector risks incoherent and possibly conflicting activities by individual aid agencies. This shortcoming in the FSCC may lead not only to suboptimal use of resources but also to government inability to provide a coherent response to the proposals of the aid agencies.

V. CONCLUSIONS

A. Overall Assessment

50. **Program Relevance.** The FSPL was framed at a time when there was a need for accelerated reforestation of degraded forestland and the appropriate policy and legal framework was not in place. While the objectives of the FSPL were highly relevant, its design should have focused more directly on removing a basic cause of forest degradation, namely, poverty. The focus during implementation on community and leasehold forestry to poor farmer groups had the potential to address a basic cause of poverty, provided that this approach could also provide the community and farmers with opportunities to carry out other economic activities (that would raise their income) rather than just forest management. The FSPL did not provide for such other activities to be undertaken.

51. **Program Efficacy.** FSPL components were at best partly effective in rehabilitating the forests, mainly because many of the targets for the investment component were not fully met. The primary goal of accelerated reforestation of degraded land under this component could not be fully accomplished. Some of the shortcomings had their roots in the delays in policy reforms, particularly in the late enactment of the Forestry Act. But a greater part could be attributed to overoptimistic or unrealistic targets when proper management plans did not exist for much of the targeted area or when strategies for implementation were not clearly spelled out in the FSPL. Scrubland rehabilitation was scheduled in the Terai areas, for instance, where the supply of degraded scrubland was inadequate. Yet the FSPL called for intensive forest management activities to take place on 75,000 ha within the program period. While a number of second tranche policy conditions were fulfilled though delayed, the FSPL has not been effective in pursuing important policy reforms relating to privatization of forest management through leasehold and industrial reforestation. The only major positive result of the FSPL relates to the policy thrust favoring community forestry through forest user groups. The efforts by the Government to indirectly address a basic cause of forest degradation through leasing forests to families below the poverty line is worth noting but this is not sustainable on a large-scale as the families are heavily subsidized.

52. **Program Sustainability.** Given the current Government preference for community forestry, the reform measures in regard to establishing a reforestation fund and private reforestation through industrial leasehold forestry and contract reforestation are not likely to be vigorously pursued. Much hope is placed on community forestry and the favorable response from user groups which contribute to greater sustainability. However, the parcels of land given for community forestry are small and do not compensate adequately for the ongoing degradation brought about by encroachment and illegal logging. While community forestry is succeeding well in the middle mountain area, it has yet to be fully tested in the Terai areas where strong vested interests in logging and encroachment exist. Continuing reforestation attempts by DOF alone are inadequate to reverse the ongoing degradation, which arises particularly from demand for forest products. Program sustainability as originally envisaged is doubtful. More needs to be done, including reforestation on a large-scale either through leasehold or contract planning and prevention of further degradation through conservation and protection measures.

53. **Institutional Development.** Impact on institutional development was positive as seen in the emergence of user groups to manage and protect the forests and in the decentralization of forest management. However, the overall impact on institutional development was only partly effective as the M&E system at MED needs further strengthening to adequately assess the longer-term impact of the FSPL and other forestry programs. The inadequate capacity of DOF to undertake large-scale forest plantation also needs further strengthening. The TAs provided under the FSPL were ineffective as, while they were successfully concluded and contributed to limited upgrading of capacity of counterpart staff, they did not result in a satisfactory M&E system (in the case of the TA on M&E) or in adoption of the recommendations made (by the TA on equitable and efficient energy pricing policies).

54. **Program Rating.** Performance of the FSPL suffered mainly from the ineffective implementation of its components both in terms of the policy reforms and more so, of the investment targets achieved with negative implications for the overall goal of accelerated reforestation. While the FSPL was consistent with Government strategies and priorities for the forestry sector, its relevance could have been improved by more direct targeting of poverty reduction to ensure a more sustainable solution to forest degradation. The Program's most significant achievement is the promotion of community forestry managed by user groups, which

offers a strong potential for contributing to sustained forest management. The impact of user groups over the long run remains to be seen, particularly when their effectiveness is strongly tested by the vested interests in the Terai areas (where forest degradation is most prevalent). The OEM's view is that community forestry by itself is inadequate. The unfinished reforms of bringing the private sector into forest management as well as promoting plantation forestry to supply forest products needed for industrial development should be pursued. Unless this is done, program sustainability is at risk. The FSPL's contribution to institutional development has only been partly effective. Its only notable success has been in the formation of user groups for community forest management. Much more is needed to strengthen government institutions to manage and monitor forestry development on a larger scale. The FSPL is rated as less than successful.¹⁹

55. Performance by MFSC and ADB. Performance by MFSC and its implementing agencies were mixed, with both the HPPCL and the ADBN fulfilling their targets but not DOF, which is a key agency in forest management. Political and administrative difficulties partly account for the lack of commitment to policy reforms. The failure to have a full-time program director reflected staff constraints as well as the lack of commitment in effective implementation of the FSPL. ADB's close supervision did not apparently help to implement the FSPL effectively. Reports of an apparent lack of staff commitment and of persistent difficulties in policy compliance and meeting the investment targets were filed, but no subsequent change in the situation was detected. There was no evidence that continuity in program monitoring was significantly affected by the frequent changes in ADB staff administering the FSPL.

B. Lessons Learned

56. Addressing the Basic Cause of Forest Degradation. Components of a forest management and conservation program should directly address the basic cause of forest degradation, namely, poverty, and the vested interests in forest degradation. Greater emphasis should be placed on the people rather than the natural resources if the benefits of the program are to be sustained.

57. Incorporation of Realistic Considerations in Design. Forestry program design and target setting (by ADB and the national government) should be based on a credible forest management plan and inventory of resources, taking into consideration physical constraints, linkage to reform measures, and capacity of agencies in both executing and implementing the program.

58. Necessity of an M&E System. An M&E system should be a fundamental component of any program. It should be established early in the program period both to enable benchmark data to be compiled and, with continuous data collection, to provide a planning system for effective monitoring, coordination, and real-time evaluation of program performance according to operational targets. It would also allow for mid-term adjustments in targets that are deemed unrealistic.

¹⁹ This is on a four-point scale of highly successful, successful, less than successful, and unsuccessful.

59. **Importance of Government Ownership of TAs.** Government ownership of TAs and their output should be obtained to prevent outputs and recommendations from being ignored or given low priority due to constraints of human and financial resources. Follow-up dialogue should be undertaken to assess why outputs and recommendations were not adopted.

60. **Continuity of Assigned Staff.** Institutional strengthening and capacity development of government agencies are less likely to be effective when staff turnover is high, staff are poorly paid, and when competing aid agencies provide various levels of incentives.

C. Follow-Up Actions

61. The Government should streamline the FSCC (by cutting down the number of participants, for instance) and have the FSCC meet once every quarter as originally intended to coordinate the progress (and possibly further external assistance) of its forest management activities. This should be done by the first quarter of 2001 and should be monitored by the Forestry and Natural Resources Division of the Agricultural and Social Sectors Department (West) in ADB.

62. To ensure sustainability of FSPL benefits, a well-equipped (in terms of human and financial resources) M&E system needs to be put in place by MFSC that will not only monitor and evaluate past but also ongoing development projects, whether financed externally or internally. Among others, the M&E system should provide feedback on what efforts should be made to ensure that the benefits of the Program continue to flow in an optimal manner. In this connection, the M&E system should dovetail into the project performance management system being implemented by NPC. MFSC should set up the M&E system by the end of 2001; NPC should monitor the system.

APPENDIXES

Number	Title	Page	Cited on (page, para.)
1	Policy Reform Matrix	20	2, 3
2	Summary of Disbursements of Counterpart Funds	23	3, 5
3	Compliance with Loan Covenants	24	8, 28

POLICY REFORM MATRIX

Policy Reforms	Target Date for Accomplishment	Actual Accomplishment Status as of November 1997	Current Status
A. Community Forestry Program			
1. Enactment of the Forestry Act based on the approved forestry sector policy and issuance of related administrative orders.	Prior to release of second loan tranche.	Improved legal basis for community and leasehold forestry. Practical results developing only slowly.	Complied with Forestry Act enacted in 1993. Enabling legislation enacted in 1995 to provide legal basis for user groups.
2. Involvement of local communities. Declaration of accessible national forests as community forests for the purpose of handling them over to user groups.	Prior to release of second loan tranche.	Complied with.	Complied with. An area of 156,711 hectares (ha) has been delineated in 14 Operational Forest Management Plans.
3. Establishment of 600 user groups clearly defining their roles and functions.	June 1992	Complied with. User groups numbered 2,237 at end 1994.	Currently, 1,026 user groups formed in 24 Terai and inner Terai districts in contrast to only 105 formed during program period.
4. Handing over of 65,000 ha of national forests as community forests to user groups.	June 1992	Total area of forests handed over was 6,105 ha at end 1994.	In 24 Terai districts, 157,554 ha were handed over as community forests versus 280 ha during program period.
5. Strengthening of the Community Forestry Division under Department of Forests (DOF).	Prior to release of second loan tranche.	Complied with. Assistance of other agencies in community forestry.	Complied with.
B. Leasehold Forestry Program			
1. Completion of classification of forests into national forests.	Prior to release of second loan tranche.	Complied with.	Complied with.
2. Selection of leaseholders for implementing the leasehold forestry program.	Prior to loan negotiations.	Not complied with.	Only 248 leasehold farmer groups selected under poverty group category in nine districts. One group under industrial leasehold category (110 ha) selected.
3. Finalization of procedures for awarding reforestation contracts to private contractors.	Prior to loan negotiations.	Complied with.	Complied with. Reforestation contracts procedures finalized.
4. Award of leasehold forestry (2,500 ha). Award of reforestation contract (1,200 ha).	Prior to release of second loan tranche.	No leasehold forestry awarded. Contract reforestation awarded totaled 3,108 ha by 1996.	Leasehold forests: 1,565 ha awarded to poverty group. Contract reforestation of 3,041 ha and plantation by DOF of 6,332 ha completed.
5. Strengthening of Forest Management and Utilization Division under DOF.	Prior to release of second loan tranche.	Forest management remains a weakness of DOF.	Ongoing process. Total area of 2,407 ha brought under forest management.

POLICY REFORM MATRIX

Policy Reforms	Target Date for Accomplishment	Actual Accomplishment Status as of November 1997	Current Status
C. Creation of a Reforestation Fund			
Creation of a reforestation fund, promptly after enactment of Forestry Act, from grants, appropriations, rents, and reforestation levies.	Prior to release of second loan tranche.	Not complied with.	Not complied with. Ministry of Forest and Soil Conservation (MFSC) decided to modify Fund as National Forest Development Fund for Cabinet approval.
D. Conservation of Biodiversity and Threatened Ecosystems			
1. Approval of the national forestry guidelines including preparation of conservation management plans.	January 1991	Complied with.	Complied with.
2. Strengthening Parks and Reserves Division, Department of National Parks and Wildlife Conservation (DNPWC), MFSC.	Prior to release of second loan tranche.	DNPWC reported inadequate working policy to achieve consistent management of protected areas. Cooperation problems with Royal Nepal Army over control of protected areas.	Preparation of management plans in progress (based on ZOPP workshop proceedings); buffer zone program launched (buffer zones in five national parks have been declared); community development program initiated in buffer zone areas. Cooperation has improved with the Army through regular meetings.
E. Monitoring and Evaluation			
Installation of a system to monitor and evaluate the ADB-financed program loan.	Prior to release of second loan tranche.	M&E capacity depends on staff continuity and adequate budgets.	M&E system set up but could monitor physical progress only.
F. Wood-based Industry and Nonwood Forest-based Processing			
1. Specification of the class and type of forest products to be prohibited for export.	Prior to release of second loan tranche.	Not complied with.	Three tree species (Sal, Khayar, and Champ) and 10 species of medicinal plants prohibited for export.
2. Commissioning of a study on rationalization and modernization of wood-based industry.	Prior to release of second loan tranche.	Policy regarding the private wood industry still being considered.	Not complied with.

POLICY REFORM MATRIX

Policy Reforms	Target Date for Accomplishment	Actual Accomplishment Status as of November 1997	Current Status
G. Fuelwood Demand Management and Policies			
1. Appointment of a task force to analyze the extent of subsidies in the price of fuelwood.		Not complied with.	Not complied with. Subsidies applied to fuelwood supplied to disaster-affected people and for cremation purposes. Also applied to reconstituted District Forest Product Supply Board supplying fuelwood for household consumption and industrial uses at the Board's own rate.
2. Implementation of the recommendations of the study on equitable and efficient pricing of fuelwood and commercial fuels.	Prior to release of second loan tranche.	Role of Timber Corporation of Nepal (TCN) reduced but still problematic. Forest Products Development Board (FPDB) sells by auction to highest bidder.	Not complied with.
H. Institutional Improvement Measures			
1. Appointment of a high-level officer to oversee implementation of the Program.	Prior to loan effectiveness.	Complied with. Effective since enhancement of monitoring and evaluation.	Complied with but not on a full-time basis.
2. Job description of senior staff in line with new forest policy.		Complied with.	Complied with.
3. Regionalization and decentralization of MFSC operational functions.	Ongoing.	Partly effective. Frequent staff transfers limit effectiveness.	Complied with.

SUMMARY OF DISBURSEMENTS OF COUNTERPART FUNDS
(NRs)

Program Component	1991/92	1992/93	1993/94	1994/95	1995/96	Total
A. Investment Program						
1. National and Leasehold Forestry	20,631,178	69,031,852	80,906,765	65,747,308	55,946,857	292,263,960
2. Conservation of Ecosystems and Genetic Resources	13,347,514	11,011,353	12,183,787	14,133,920	8,416,794	59,093,368
3. Medicinal and Aromatic Plants	10,000,000	20,000,000	10,000,000	3,000,000	6,349,000	49,349,000
4. Soil Conservation and Watershed Management	13,921,959	30,062,277	37,813,150	27,352,643	20,798,219	129,948,248
5. Establishment of Biogas Plants	18,957,000	7,617,000	18,846,000	0	0	45,420,000
Subtotal A	76,857,651	137,722,482	159,749,702	110,233,871	91,510,870	576,074,576
B. Administrative Cost						
1. Operating Cost	1,956,016	11,081,146	5,100,267	2,422,963	6,216,503	26,776,895
2. Vehicles and Equipment	6,235,141	10,271,479	6,009,359	5,536,064	443,413	28,495,456
Subtotal B	8,191,157	21,352,625	11,109,626	7,959,027	6,659,916	55,272,351
Total	85,048,808	159,075,107	170,859,328	118,192,898	98,170,786	631,346,927
Exchange Rate (NRs/\$)	42.68	46.08	47.77	48.78	50.19	

COMPLIANCE WITH LOAN COVENANTS

Reference	Covenant	Compliance at PCR Stage	Current Status of Compliance
Schedule 5, para. 2, Loan Agreement	The Borrower will promptly cause Nepal Rastra Bank to deposit into the special account the corresponding amounts of the counterpart funds equivalent to the amounts of proceeds of the loan so withdrawn.	Complied with, but delayed. The Government put up counterpart funds equivalent to the first tranche of \$20.968 million.	Complied with.
Schedule 5, para. 3, Loan Agreement	The Ministry of Forest and Soil Conservation (MFSC) will utilize the counterpart funds to finance the local currency cost of the following program components: (i) national and leasehold forestry program; (ii) medicinal and aromatic plants and other minor forest products; (iii) soil conservation and watershed management; (iv) conservation of ecosystem and genetic resources; (v) establishment of biogas plants; and (vi) other programs of activities eligible for financing as specified in paras. 4 to 10, Sched. 5, Loan Agreement.	Complied with, but delayed. MFSC has been utilizing the counterpart funds as specified to finance the local currency costs. The physical accomplishments so far achieved are low.	Complied with. Physical accomplishments varied according to components. Only counterpart funds from first tranche involved as second tranche was cancelled.
Schedule 5, para. 4, Loan Agreement	<p>The Borrower's 1990/91-1994/95 program on national and leasehold forestry will receive the highest priority for the use of counterpart funds. The use of counterpart funds for this purpose will, however, be subject to the following terms and conditions:</p> <p>(i) New Plantation Development Projects</p> <p>(a) The counterpart funds will be utilized to finance new plantation development projects by force account and by contract. All new plantation development projects which MFSC intends to finance with the use of counterpart funds will be subject to clearance by the Planning Division and the Monitoring and Evaluation Division (MED) of MFSC. For this purpose, Department of Finance (DOF) will</p>	<p>Complied with, but delayed. Most of the allocated budget was utilized for the program on national and leasehold forestry. However, progress on this component was hampered by the long delay in approval of the bylaws.</p> <p>Partly complied with. All plantation programs were endorsed by the Planning Division and MED of MFSC.</p>	<p>Complied with but performance of leasehold forestry was not encouraging. Leasehold forestry confined to applicants from poor families.</p> <p>Draft annual plans are first cleared at the district level by District Development Committee before being sent to central planning units. The DOF and the Ministry's planning units submit the final annual program to National Planning Commission who will approve. Only then can district offices implement the programs.</p>

Reference	Covenant	Compliance at PCR Stage	Current Status of Compliance
	<p>furnish ADB with a copy of the report of the proposed schemes/programs as prepared by the district forest offices which will show the area, its land use, species proposed, and its utilization. These small scattered schemes will be carried out by contractors.</p>		
	<p>(b) For large-scale plantation areas, DOF will furnish ADB with a copy of the report approved by the Planning Division and MED of MFSC. This report will include the economic and/or environmental consideration that justify the project, program, scope, and cost estimates and implementation arrangements proposed.</p>	<p>Partly complied with. Large-scale plantations had not been carried out. The area planted by force account was 2,028 ha.</p>	<p>DOF has no experience in large-scale plantations. Large-scale plantation was carried out by the Forest Products Development Board by force account.</p>
	<p>These types of activities will preferably be done by force account.</p>	<p>Complied with. Forest Products Development Board plantations done by force account.</p>	
	<p>(c) For plantation development by lessees/user groups, DOF will help implement the program with Agricultural Development Bank of Nepal.</p>	<p>Not complied with.</p>	<p>Not complied with. DOF efforts are geared toward community forestry rather than plantation development as a matter of policy.</p>
<p>(ii) Program for Timber Stand Improvement (TSI) and Management of Natural and Degraded Forests</p>			
	<p>(a) The counterpart funds may be utilized to finance the cost of implementing the programs for TSI and enrichment planting in natural forest, provided that the program is translated into projects specifying the location, quantity of work, costs, annual rate of</p>	<p>Complied with. The funds for TSI and management of natural and degraded forest were utilized in 18 districts of the Terai region.</p>	<p>Complied with.</p>

Reference	Covenant	Compliance at PCR Stage	Current Status of Compliance
Schedule 5, para. 5, Loan Agreement	<p style="text-align: center;">accomplishment, period of completion, and implementation arrangements.</p> <p>Medicinal and Aromatic Plants and Other Minor Forest Products:</p>	Complied with. HPPCL prepared annual working plans broken down into activities, production, marketing strategies, and financial details.	Complied with.
Schedule 5, para. 6, Loan Agreement	<p>Soil Conservation and Watershed Management:</p> <p>In addition to the rehabilitation of watershed areas to be carried out in conjunction with plantation development, MFSC may also fund from counterpart funds the cost of other exclusive soil conservation and watershed management projects which are agreed upon between the Borrower and ADB. Such funding shall be subject to:</p> <ul style="list-style-type: none"> (i) each proposal being cleared by the Planning Division and MED of MFSC in a manner specified in para. 4(i)(a), Schedule 5 of the Loan Agreement; (ii) measures of a civil works nature and establishment of forest or other forms of vegetative cover shall be executed by 	Complied with. The program focused on (i) landslide treatment; (ii) irrigation and waterways improvement; (iii) waterways protection; and (iv) shelterbelts.	<p>Complied with except for monitoring evaluation.</p> <ul style="list-style-type: none"> (i) Complied with. (ii) Complied with.

Reference	Covenant	Compliance at PCR Stage	Current Status of Compliance
	<p>competent contractors selected under MFSC's existing procedures; and</p> <p>(iii) monitoring and evaluation will be undertaken to cover progress and performance.</p>		<p>(iii) District offices supposed to keep record of information required, guided by M&E System Guidelines of MFSC.</p>
Schedule 5, para. 7, Loan Agreement	<p>MFSC will establish the eligibility of each soil conservation and watershed management project on farmers' fields for funding from the Special Account on the basis of a review of the farmers' income, location of the project, and the method of implementation. The reports of such reviews will be made available to ADB.</p>	Complied with.	Complied with.
Schedule 5, para. 8, Loan Agreement	<p>Conservation of Ecosystem and Genetic Resources:</p> <p>In addition to the expenditures involved in developing infrastructure and facility improvement, MFSC will utilize the counterpart funds to finance expenditures connected with conservation education, species conservation (gharial, blackbuck) and additional staffing required for habitat protection, maintenance, and improvement. The documents relating to the award of contracts, the record of progress, payments, and performance in the field including the progress in conservation education shall be made available to ADB. ADB's comments will be reflected in subsequent activities under this component.</p>	Complied with, but delayed. Expenditures until FY1995/96 were sent to ADB.	Complied with.
Schedule 5, para. 9, Loan Agreement	<p>Establishment of Biogas Plants:</p> <p>The counterpart funds will be utilized to finance the biogas program. Biogas and Agricultural Equipment Development Pty., Ltd. (BAEDP) will establish the eligibility and feasibility of each</p>	Complied with.	Not complied with. Netherlands funded Biogas Support Program made an agreement with BAEDP to implement the biogas program jointly, BAEDP was fully

Reference	Covenant	Compliance at PCR Stage	Current Status of Compliance
Schedule 5, para. 10, Loan Agreement	<p>project on the basis of a report of the income and earning prospects and the repayment capacity of potential clients and will send an appropriate proposal to ADBN for clearance prior to accessing the counterpart funds from the Special Account. The release of funds shall be subject to: (i) each such proposal being economically and financially viable; (ii) construction of biogas plants being executed following the norms developed by ADBN and BAEDP; and (iii) continuous monitoring of the progress and performance of the established biogas plants. The release of funds from the Special Account will be carried out by MOF under arrangements to be agreed upon by MOF, MFSC, and ADBN. MFSC will be involved in the districts where biogas plants will be constructed.</p> <p>The counterpart funds will also be utilized to finance the local currency costs incurred in connection with the following programs and activities:</p>	Partly complied with. Counterpart funds were utilized according to the budget allocated by MOF.	occupied with Biogas Support Program. Thus ADBN and MOF decided to use private biogas companies for implementation of ADB's biogas program.
	(i) site surveys and appraisals for plantation development programs;	Partly done.	Complied with.
	(ii) independent monitoring and evaluation of program accomplishments and impacts by nongovernment organizations (NGOs) to be appointed by MFSC for this purpose;	Not complied with.	Not complied with. M&E supported by FINNIDA project.
	(iii) benchmark survey of farmers who will implement soil conservation schemes;	Not complied with.	Not complied with.
	(iv) feasibility studies on biogas plants;	Not complied with.	Not complied with.

Reference	Covenant	Compliance at PCR Stage	Current Status of Compliance
	(v) financial burden of MFSC arising out of its obligations, if any, to support the plantation development and implementation of other forestry programs undertaken by other local agencies of the Borrower;	Not complied with.	No financial burden involved.
	(vi) implementation of foreign-assisted projects or other international arrangements (as debt-for-nature swaps) aimed at building up or restoring forests or protecting or enhancing ecological balance, subject to prior clearance by the Borrower;	Not complied with.	Not complied with.
	(vii) review by a task force of energy demand management measures;	Not complied with.	Not complied with.
	(viii) institutional facilities as required in support of the Program;	Not complied with.	Complied with.
	(ix) establishment of the Nepal Conservation Training and Research Institute; and	Complied with.	Complied with.
	(x) any other forestry activity that would directly contribute to the objectives of the program as agreed upon between the Borrower and ADB.	No data.	Counterpart funds were not adequate for program components.
Schedule 5, para. 11, Loan Agreement	The Minister of MFSC or his authorized representative will withdraw the counterpart funds for financing eligible expenditures.	Complied with.	Complied with.
Schedule 5, para. 12, Loan Agreement	The Auditor General of the Borrower will institute a regular audit on the legitimacy and appropriateness of the withdrawals from, and the commitments made under and in respect of, the Special Account. The audit shall begin with the calendar quarter after the effective	Partly complied with. The Review Mission of September 1992 recommended the submission of trimester (instead of quarterly) financial statements in the transactions/utilization of funds from	Long process involved in getting audit certificate from Auditor General (>1 year). Submission often late as a result. Auditor General auditing of any particular fiscal year expenditures begins only after completion of that fiscal year.

Reference	Covenant	Compliance at PCR Stage	Current Status of Compliance
Schedule 5, para. 13, Loan Agreement	<p>date, and the audit of the transaction of each quarter will be completed and the report thereon furnished to MFSC, MOF, and ADB before the end of the succeeding quarter. The Borrower, shall, in consultation with ADB, introduce such changes in the rules governing the releases from the Special Account and utilization of the counterpart funds as would rectify and prevent a recurrence of irregularities, if any, reported in audit.</p> <p>The entire amount of counterpart funds deposited in the Special Account will be disbursed, or committed by contracts to meet the expenditures on eligible projects and programs within five years from the effective date. Should any uncommitted balance remain in the Special Account as of the end of that period, such balance, will, except as otherwise agreed to by ADB, be used for financing plantation development projects mainly in the private sector under modalities, terms, and conditions as will be agreed upon between the Borrower and ADB.</p>	<p>the Special Account before the end of each succeeding trimester. These statements were to be certified to by the Auditor General following the regular audit. The Mission fielded in May 1994 recommended a half-year reporting cycle.</p> <p>The Borrower complied with the audit of the Imprest Account. However, audit reports pertaining to the counterpart funds have been only partly complied with. Three EAs out of five submitted reports up to 1994, one EA up to 1995, and one EA (ADBN) has not complied with the requirement. ADBN has been requested to submit pending audit reports.</p>	Complied with.
Schedule 5, para. 14, Loan Agreement	<p>In connection with the implementation of the program, the Borrower will undertake or cause to be undertaken the following:</p> <p>(a) The Borrower will seek appropriate approval during 1990 and each year</p>	Partly complied with. For 1990/91, no budget was approved for MFSC for	Partly complied with.

Reference	Covenant	Compliance at PCR Stage	Current Status of Compliance
	<p>thereafter for budgetary appropriations adequate to meet the following expenditures: (i) the cost over the period FY1990/91 to FY1994/95 of developing a minimum of 104,000 ha (29,000 ha under reforestation and 79,000 ha for improved natural forest management); (ii) the cost of developing 1,000 ha for cultivation of medicinal plants by involving small farmers including production of 1,000 tons of essential oils, purchasing and grading of crude herbs; (iii) the cost of preventive and rehabilitative soil conservation measures; (iv) the cost of habitat protection of 7,000 ha; and (v) the cost of establishing about 5,000 biogas plants;</p>	<p>implementation of the Program. Budgets approved were never adequate to implement the investment program.</p>	
	(b) MFSC will consult ADB on the engagement of NGOs and consulting firms for carrying out independent monitoring and evaluation of program impact;	Not complied with.	Not complied with. M&E is performed by M&E Division of MFSC.
	(c) The Borrower will commission a study on equitable and efficient energy pricing policies and will implement the agreed recommendations of the study;	Partly complied with. Study completed under TA 1394-NEP. No implementation took place.	Complied with.
	(d) The Borrower will carry out the recommendations of a study to be prepared under the Forestry Development Project assisted by the United States Agency for International Development in ways to promote the distribution of more fuel-efficient woodstoves;	Not complied with. Less emphasis on fuel-efficient stoves.	Not complied with.
	(e) The Borrower will not issue any new license for new wood-based industries pending rationalization and modernization of wood-based industries in Nepal.	Complied with.	Complied with.

Reference	Covenant	Compliance at PCR Stage	Current Status of Compliance
Schedule 5, para. 15, Loan Agreement	(f) The Borrower will evaluate and implement necessary policies for the award of timber harvesting rights on the basis of a competitive bidding system which will ensure sufficient stumpage price to cover reforestation costs.	Partly complied with. Incorporated in the draft bylaws but no implementation. Timber Corporation of Nepal retains harvesting rights.	Complied with.
	(g) The Borrower will undertake a study on rationalization and modernization of wood-based industries, mobilizing donor assistance for this purpose as necessary.	Partly complied with. FINNIDA-assisted project ended in 1995 without any achievement.	Partly complied with.
	The Borrower and ADB will undertake a continuing dialogue on major policies and policy adjustments relating to the forestry sector. Accordingly, the Borrower will (i) continue to implement forestry sector policies in a manner consistent with the overall objectives of the Program and as identified in the Borrower's Master Plan for the Forestry Sector; (ii) exchange views with ADB on the implementation of major forestry sector policies whenever the situation so warrants, but not less than once a year during the program implementation period and two years thereafter; and (iii) keep ADB informed of the outcome of any other donor consultation that may directly or indirectly affect the objectives of the Program.	Partly complied with. Dialogue with ADB review missions but policies were not implemented.	Partly complied with.
Section 4.04(a), Loan Agreement	The Borrower will maintain, or cause to be maintained, records and accounts adequate to identify the goods and services financed out of the proceeds of the loan, to record the progress of the Program (including the cost thereof), and to reflect, in accordance with consistently maintained sound accounting principles, the	Partly complied with. Detailed accounts were not kept.	Difficulty of getting detailed information by location (village and plot) whereas district-wise progress (financial and physical) was easier.

Reference	Covenant	Compliance at PCR Stage	Current Status of Compliance
Section 4.05(b), Loan Agreement	expenditures financed out of the proceeds of the loan. The Borrower will furnish to ADB quarterly reports on the implementation of the Program and the accomplishments of the targets and implementation of the actions set out in the Policy Letter.	Not complied with.	Not complied with.
