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## Policy pointers

**Nepal needs to develop** an enabling policy, institutional and legislative environment to increase private sector involvement and investment in forestry business.

**Establishing and** strengthening a forest product value chain would help promote fair, transparent and competitive processes, and increase private sector investment in forest-related business.

**Stripping back excessive** bureaucracy along the value chain would provide the legal and policy framework Nepal needs to encourage growth and sustainability in small-scale forestry enterprises.

**Increased transparency** would reduce transaction costs and increase market competition to minimise the gap between forest gate and market prices, ensuring that producers reap the benefits of Nepal's large, lucrative markets for forest products.

## Increasing private sector involvement and investment in forestry in Nepal

Although forest covers 40 per cent of Nepal, the forestry sector's potential to generate huge employment opportunities is largely untapped. Private sector involvement and investment could create 1.38 million work days a year. But certain policies and administrative hurdles hinder both community and private investment in the sector. The lack of business ethics, access to finance and other business services, primitive technology and poor market integration all limit the growth of viable forestry enterprises. The Forest and Farm Facility's cross-sectoral platform initiatives at local and national levels offer entrepreneurs a forum to discuss their business problems and policy and legislative hurdles with policymakers and other stakeholders, ensuring and improving business and policy engagement among smallholders, women and socially excluded groups.

### Potential contribution to the green economy

Nepal's forestry sector has the potential to play an important role in enhancing livelihoods, well-being and social equity, while significantly reducing environmental risks and ecological scarcities, which directly contribute to the green economy.<sup>1</sup> Small and medium forest-based enterprises could generate more than US\$8.7 billion and 1.38 million work days through 400,000 sustainable full-time equivalent green jobs.<sup>2</sup> The sector offers informal workers the opportunity to enter formal employment, through enterprise-oriented forest management and other functions in the value chain. Potential areas for private-public sector partnerships in the sector include reforestation activities, carbon sequestration and trading, and eco-tourism. But despite the sector's great potential, several challenges exist:

- Protection-oriented forest management: by limiting the number of live trees that can be harvested and focusing instead on dead, dying and fallen trees, this approach also limits the commercialisation of forest resources
- Strong bureaucracy throughout the forest product value chain: causes increased costs and delays that hinder growth and sustainability of small-scale forest enterprises
- A lack of transparency: increases transaction costs and reduces market competition, allowing local traders and middle men to cartel and control the value chain.

### The policy and legal framework

Nepal's Forest Policy (2015) gives high priority to sustainable and productive forest resource use, promoting forest-based enterprises and creating green jobs through private sector involvement.<sup>3</sup>

## *In spite of Nepal's large, lucrative markets for forest products, producers are not reaping the benefits*

The policy envisions a forest development fund to increase private sector investment in forestry. It aims to simplify the harvest and transportation of forest products from private forests and promotes private, public and community partnerships to develop forestry-based enterprise.

The Forestry Sector Strategy (2015) focuses on enhancing forest productivity and the sustainable supply of forest products and services. It also promotes

community-based and private forest enterprises to improve livelihoods and the forestry sector's contribution to national economic development.

But the older Forest Act (1993)<sup>4</sup> and Forest Regulations (1995)<sup>5</sup> have not been harmonised with the Forest Policy and Forest Sector Strategy. Implementing the policy will therefore prove challenging in the absence of a timely amendment of these laws.

There are also contradictory dual taxations, where both the central and local government are charging taxes on forest products, especially on high value timber. For example, the 2015 Finance Act requires the District Forest Office to charge 15 per cent of revenue on sale of high value timber from national forests, especially on community forests.<sup>6</sup> Likewise, local government is imposing taxes on the forest produce, especially on harvesting through the 1999 Local Self Governance Act.<sup>7</sup> This has not only increased the bureaucratic hurdles but also market price of the commodities.

Rather than support small-scale forest enterprises, this legal and policy framework obstructs local producers from harvesting and selling forests products, especially timber and non-timber forests products (NTFPs). Although the forest policy encourages the private sector to get involved in the forestry business on paper, in practice there are many hurdles to be overcome and very few incentives for private sector investment and partnerships to happen on the ground.

### **Barriers to business development**

In spite of Nepal's large, lucrative markets for forest products, producers are not reaping the benefits. Nepal's small-scale forestry businesses are characterised by their limited production capacity and cannot compete in the market. Here we examine some of the main barriers to business development in Nepal's forestry sector.

#### **1. Poor private sector engagement:**

public-private partnership is used globally in a number of sectors to facilitate investment and development of sectors. And although Nepal's forest policy highlights the need for private sector involvement in the sector, investment is limited.

#### **2. Geographical barriers:**

the geographical spread of Nepal's small enterprises means their transaction costs are high. Low production rates, expensive transportation and the large number of actors in the value chain mean there is a huge difference between forest gate and market prices. This is particularly so for timber products and NTFPs. Forest-based enterprises often encountered problems in both purchase of raw materials and selling of produce, as they are geographically scattered and operating business at a very small scale.

#### **3. Gaps in capacity:**

sustaining forest-based enterprises in the long run is a major challenge. In Nepal, limited awareness of the market and the business scenarios that directly affect product demand means that entrepreneurs often operate without adequate knowledge of market requirements. As well as being affected by the seasonality and scattered availability of raw material, smallholder producers use primitive technology and are poorly integrated in the market. With their limited business capacity, they often struggle to compete with others.

While external agencies provide direct cash incentives or financial grants to establish enterprises, they do not build capacity on sustainable business practices. There are few government interventions to strengthen business skills or production capacity. It is not common practice for local businesses to develop plans for sustainable management. As a result, there is no proper market analysis to set prices. Buyers usually determine the price of products, at times far below the cost of production.

This lack of local-level awareness and skills has resulted in low-quality and less competitive products. Business linkages are poorly developed and access to business services is very limited. Because they use primitive technology, small businesses need to invest more time and labour to produce their goods, which ultimately limits economic growth. Smallholders also struggle to keep up with market trends and changing consumer preferences.

**4. Poor access to business services:** in remote rural areas access to technical extension-, business support- and financial-services is limited. Entrepreneurs often have to depend on local technicians, with varying levels of capacity, and high interest informal loans because they have little or no access to financial institutions. A large number of middle agents are also involved in the value chain of forest products, and their profit margins are much higher than those of local producers and processors. As a result, only a small portion of the profit reaches the entrepreneurs.

**5. Administrative hurdles and bureaucracy:** trading farm and forestry products, particularly timber products and NTFPs — even from private land — involves a number of often costly bureaucratic hurdles. Getting permission to establish an enterprise in the first place is a lengthy process. Forestry regulations state that forest-based enterprises — such as saw mills, processing plants and furniture industries — have to be at least 0.5km from national forest boundaries in the mid-hills and 1km away in the Terai. So many small and medium forest-based enterprises cannot be legally established in a village, as these tend to be very near national forests. This makes it extremely difficult to find an appropriate setting for a new business.

Unreasonable environmental regulations — many of which are based on the 1995 Environment Protection Act and the 1997 Environment Rule — are major obstacles to private sector and community involvement in the forestry business. By law, community forestry groups and entrepreneurs need to carry out environmental impact assessments (EIAs) for commercial cultivation of medicinal and aromatic plants or if they establish saw mills and other forest-related processing plants within 1km from the boundary of a national forest. But EIA procedures are too technical and costly for small scale businesses, making compliance difficult, if not impossible.

Once a business is established, administrative processes continue to be time-consuming and often require frequent travel to district headquarters. Enterprises need permission from the District Forest Office to harvest, transport and sell timber or NTFPs, even within the district. The actual sale value of many of the forest products does not always cover the cost of getting the permit and paying royalty fees at the multiple check-points.

There are also often delays in receiving permits and in particular for transport, as these need to be obtained from various government line agencies. Product quality can deteriorate while sales and collection are delayed. The lack of regulation around the types of business allowed to trade leads to unhealthy competition. There are also unofficial costs, such as incentives and allowances for those who are directly or indirectly involved in the chain.

### **Tackling barriers to business development**

The Forest and Farm Facility (FFF) works with the Federation of Community Forestry Users of Nepal (FECOFUN), the Federation of Nepal Cottage and Small Industries (FNCSI) and the International Union for Conservation of Nature (IUCN) in Nepal. These three partners facilitate change at the producer and government level to improve livelihoods of forest and farm producers and more sustainable landscape management. IUCN plays an overall coordinating role and the forest and farm producer organisations (FFPOs) FECOFUN and FNCSI lobby for producers' rights and needs, and provide support services at district and national levels. The FFF works with these organisations to strengthen smallholders', women's and socially excluded groups' capacity for business and policy engagement.

**Cross-sectoral platforms.** The FFF collaborates with its local partner organisations to help them engage in policymaking to overcome the legislative and administrative barriers that prevent businesses from developing locally. FECOFUN and FNCSI help build horizontal and vertical linkages to mainstream local needs into regional and national policies, while IUCN and FECOFUN focus on national cross sectoral linkages to strengthen producer and government institutions.

For this to happen effectively, FFF has stimulated cross-sectoral policy platforms at national and sub-national levels and works to strengthen them further. With representatives from government, private sector and rights holder FFPOs, these platforms explore, discuss and solve grassroots issues and increase information sharing and coordination between sectors. FFF mobilises the platforms to effectively address the problems and challenges of forest and farm enterprises.

**Working with the public sector.** Nepal needs to build partnerships to transfer technical knowledge and enhance business capacity. The FFF collaborates with public sector institutions

to implement activities related to green economic development. The institutions provide technical support and services, including technology transfer to producer organisations, and FFF provides material support and business skill training for collaborative activities. FFF also works with the public sector to develop a policy environment that is conducive to increasing private sector investment and involvement in forestry businesses.

**Improving business development.** FFF helps producer organisations in pilot districts to revise their resource management plans, particularly around forest operation guidelines, to ensure they integrate business planning approaches through enterprise development plans. It also supports the producer organisations to mobilise funds for business development, so they can access credit, technology and markets. FFF further strengthens the value chains through embedded exchange visits, market fairs and by building partnerships with all stakeholders.

FFF has been training public sector staff — from frontline extension workers to policymakers — in business development. It also organises workshops and interactions with producer organisations and business communities to discuss the problems and constraints producers face. This includes exposure visits within and outside the country to build business development competence.

## Conclusion

Nepal needs to develop an enabling policy, institutional and legislative environment to increase private sector involvement and investment in forestry businesses. We believe that the following policy and programme recommendations will help promote this.

There must be more flexibility around the siting of forestry businesses. Regulations should take into account an enterprise's production capacity and its likely impact on the forest. Small and medium enterprises, with forest management plans to sustainably manage the resource, would have less of an impact on their surroundings compared to large scale forest concessions, and should be able to operate in settlements or villages even if they are within 0.5km from a national forest boundary.

Obtaining harvesting, collection and transportation permits needs to be made more straightforward. Allowing forest products, especially NTFPs, to be sold as agriculture products would help remove some of the hurdles producers face.

Community forestry plans should include provisions for enterprise development, to help producers add value to and process forest products with high commercial value and to build their capacity to operate a sustainable business.

Strengthening forest enterprises and cooperative networks and establishing business linkages between them would help increase production capacity through economies of scale and marketing. An environmental certification programme would increase market access for smallholder producers.

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## Knowledge Products

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Forest and Farm Facility (FFF) is a partnership between FAO, International Union for Conservation of Nature (IUCN) and IIED. IUCN Nepal in partnership with the Federation of Community Forestry User Group of Nepal (FECOFUN) and Federation of Cottage and Small Scale Industry (FNCSI), is implementing FFF initiatives in Nepal to build the capacity of small holders' producer groups to improve access to business services.

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## Notes

<sup>1</sup> UNEP, U (2011) *Towards a green economy: Pathways to sustainable development and poverty eradication*. A synthesis for policymakers.  
<sup>2</sup> Subedi, B P *et al.* (2014) *Private sector involvement and investment in Nepal's forestry: status, prospects and ways forward*. Study report. Multi Stakeholder Forestry Programme, Services Support Unit, Babarmahal, Kathmandu, Nepal. / <sup>3</sup> Government of Nepal (2015) *Forest Policy, 2071*. Ministry of Forests and Soil Conservation, Kathmandu, Nepal. / <sup>4</sup> Government of Nepal (1993) *Forest Act, 2049*. Ministry of Forest and Soil Conservation, Kathmandu, Nepal. / <sup>5</sup> Government of Nepal (1995) *Forest Regulation, 2051*. Ministry of Forest and Soil Conservation, Kathmandu, Nepal. / <sup>6</sup> Government of Nepal (2015) *Finance Act*. Ministry of Finance, Kathmandu, Nepal. / <sup>7</sup> Government of Nepal (1999) *Local Self Governance Act, 2055*. Ministry of Law and Justice, Kathmandu, Nepal.