

# Report for Congress

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## **Nepal: Background and U.S. Relations**

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K. Alan Kronstadt  
Analyst in Asian Affairs  
Foreign Affairs, Defense, and Trade Division

# Nepal: Background and U.S. Relations

## Summary

A landlocked Himalayan kingdom between India and China, Nepal ranks among the world's poorest countries. In 1990, following a democratization movement, the country became a parliamentary democracy under a constitutional monarch. Although this led to a process of economic restructuring and market liberalization, more than a decade of political instability and nearly seven years of increasingly dire internal security challenges have seriously hampered Nepal's economic growth and reform efforts. After several years of relatively robust growth, the economy is reported to have contracted in the fiscal year ending July 2002. Compounding the country's difficulties was the June 2001 tragedy in which 10 members of the royal family, including King Birendra, were killed in an assassination-suicide, reportedly carried out by Crown Prince Dipendra.

At present, the Kathmandu government faces increasing pressure to end a 7-year-old Maoist insurgency that has caused widespread violence and crippled the Nepali economy. Nearly 8,000 people reportedly have been killed in the insurgency, with some two-thirds of the deaths occurring since the Maoists broke a cease-fire agreement in November 2001. In May 2002, then-Prime Minister Deuba met with President Bush to discuss U.S. financial help in suppressing the insurgency. Actual U.S. security assistance to Nepal was \$14 million included in the FY2002 Supplemental Appropriations Act (P.L. 107-206) of August 2002. An additional \$3.5 million was allocated for FY2003 and the Bush Administration is requesting \$10.6 million for FY2004. Pending legislation in the 108<sup>th</sup> Congress includes S. 662, introduced in March 2003, that seeks to extend to Nepal certain preferential treatment with respect to apparel articles.

Since the final months of 2002, the Nepali government has faced constitutional crises that, many argue, are interfering with its ability to combat the Maoist uprising. On October 4, 2002, amid dissatisfaction with the worsening security situation and the inability of the prime minister to hold parliamentary elections as scheduled, King Gyanendra dismissed the prime minister and the cabinet and assumed "temporary executive authority." One week later, the king chose royalist Lokendra Bahadur Chand to serve as prime minister and oversee a caretaker cabinet until new elections are held sometime in late 2003. Leading Nepali political parties and figures have denounced the appointment as undemocratic and unconstitutional, and pro-democracy demonstrations involving tens of thousands of Nepalis were held in late 2002 and early 2003.

Also in the final months of 2002, Nepal's Maoist rebels stepped up their violent campaign to overthrow the Kathmandu government. Large-scale battles caused mass casualties and heightened concerns about the government's ability to effectively counter the insurgency. There exists fear that further deterioration of Nepal's security circumstances could destabilize neighboring regions, spur new tensions between India and China, and potentially create a new terrorist haven in South Asia. Hopes for a permanent resolution were bolstered by a January 2003 cease-fire agreement and plans for peace talks in April. This report will be updated periodically.

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# Nepal: Background and U.S. Relations

## Recent Developments

On January 29, 2003, the Nepali government and Communist Party (Maoist) rebels announced an agreement to cease armed hostilities in their 7-year-old conflict. The United States welcomed the announcement as “concrete evidence that the Maoists are serious about holding peace talks with the Nepali government” and it supports “a meaningful dialogue leading to a peaceful resolution of the conflict.” The U.S. State Department, while describing the security situation in Nepal as “fluid,” subsequently eased its travel advisory for U.S. citizens to reflect the apparently improved circumstances there.<sup>1</sup> As of late-March, no date has been set for proposed peace talks, but the two sides have signed a 22-point code of conduct for such talks, Maoist leaders have emerged from hiding, and the cease-fire is holding. Despite widespread optimism that the country can be returned to normality, some analysts identify the country’s ongoing political instability and doubts about the Maoists’ sincerity as reasons to be pessimistic about chances for an enduring cease-fire and eventual negotiated settlement.<sup>2</sup>

### NEPAL IN BRIEF

**Population:** 25.9 million (July 2002 est.); *growth rate* 2.3% (2002 est.)

**Area:** 147,181 sq. km. (about the size of Tennessee)

**Capital:** Kathmandu (pop. approx. 700,000)

**Ethnic Groups:** Brahman, Chetri, Newar, Gurung, Magar, Tamang, Rai, Limbu, Sherpa, Tharu, et. al.

**Language:** Nepali (official); about 12 others

**Religion:** Hindu 86%; Buddhist 8%; Muslim 4%

**Life Expectancy at Birth:** female 58.2 years; male 59.0 years (2002 est.)

**Literacy:** total 42%; female 25%; male 60% (2001)

**Gross Domestic Product:** \$5.5 billion (2001); *per capita* \$240; *growth rate* -0.6% (2001/02), 0.9% (2002/03 est.)

**Inflation:** 3.1% (2002 est.)

**U.S. Trade:** exports to U.S. \$152 million; imports from U.S. \$20 million (2002)

**Sources:** CIA World Factbook; Reuters News; U.S. Departments of Commerce and State; World Bank; Asian Development Bank; Global Insight.

The increasingly bloody internal rebellion waged by Maoist fighters contributed to a political crisis in Nepal during the final months of 2002. Though the insurgency

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<sup>1</sup> American Embassy, Kathmandu, Press Release, January 30, 2003; U.S. Department of State, Office of the Spokesman, “Public Announcement : Nepal,” March 5, 2003.

<sup>2</sup> “Nepal: Regional Talks,” *Jane’s Intelligence Digest*, February 7, 2003.

began in 1996, as many as two-thirds of the nearly 8,000 deaths caused have come in the past year alone.<sup>3</sup> Political instability and insurgency-related violence in 2001 and 2002 combined to shrink the country's economy – and devastate the vital tourism sector – for the first time in nearly two decades. According to a close advisor of the Nepali king and chairman of the country's largest private company, “Nepal is on the verge of becoming a failed state.”<sup>4</sup> There exists fear that further deterioration of Nepal's circumstances could destabilize neighboring regions, spur new tensions between India and China, and potentially create a new terrorist haven in South Asia.<sup>5</sup>

## Politics

On October 4, 2002, amid dissatisfaction with the worsening security situation and the inability of then-Prime Minister Deuba's government to hold parliamentary elections as scheduled, King Gyanendra dismissed the prime minister, disbanded his cabinet, and assumed executive powers, while pledging to relinquish his authority once a new government was formed. This event marked the first time since absolute monarchy was ended in 1990 that a Nepali king dismissed an elected government and assumed direct power; the move thus stunned the main political parties in Nepal and has led to a constitutional debate. While the king claimed that his decision was in accordance with his constitutional power to dismiss the government during a political crisis, the ousted prime minister and key political parties denounced the action as unconstitutional. In the days following Deuba's dismissal, thousands of Nepalis took to the streets of Kathmandu to demonstrate their opposition to the king's decision and demand the speedy restoration of democracy. Smaller demonstrations were held in support of the king.<sup>6</sup>

One week after his assumption of executive power, King Gyanendra met with senior political leaders to discuss formation of a new government, and he subsequently chose Lokendra Bahadur Chand, a member of the royalist, right-wing National Democratic Party and former premier, to oversee a caretaker cabinet until new elections are held sometime in late-2003. The United States extended its best wishes to the new government and pledged its continued support in Nepal's anti-terrorism efforts.<sup>7</sup> Leading Nepali political figures, including Deuba, denounced the

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<sup>3</sup> John Lancaster, “Nepal's War turns Brutal For Rural Civilians,” *Washington Post*, January 2, 2003; Philip Shenon, “Rebels in Nepal Drive Down Tourism,” *New York Times*, February 9, 2003.

<sup>4</sup> Binod Bhattarai and Edward Luce, “Nepal's New Premier Unmoved by Clamor at Parliament's Gates,” *Financial Times* (London), November 21, 2002.

<sup>5</sup> Bertil Litner, “Nepal's Maoists Prepare For Final Offensive,” *Jane's Intelligence Review*, October 2002.

<sup>6</sup> Binaj Gurubacharya, “Nepal King Fires Prime Minister,” Associated Press Newswire, October 4, 2002; Y.P. Rajesh and Gopal Sharma, “Ousted Nepal PM Brands Dismissal Unconstitutional,” *Washington Post*, October 5, 2002; Y.P. Rajesh, “Nepal Protesters Demand King Restore Democracy,” Reuters News, October 8, 2002; Sushil Sharma, “Anti-King Protests in Nepal,” BBC News, November 26, 2002.

<sup>7</sup> “Senior US Official Meets New Nepal Premier, Extends Support,” BBC Monitoring South (continued...)

appointment as an “undemocratic exercise,” and more pro-democracy demonstrations involving tens of thousands of Nepalis were held in December and January.<sup>8</sup>

Nepal’s main political parties remain split on how to proceed: some, including the Nepali Congress, seek reinstatement of the dissolved parliament, while the left-wing United Marxist-Leninist party is among those seeking establishment of an interim government comprising members of mainstream parties.<sup>9</sup> On February 3, 2003, in his first address to the nation as prime minister, Chand announced that he would hand over power to an elected government, but set no deadline for holding elections. His call for a first-ever all-party meeting subsequently was turned down by Nepal’s major political parties, who complain that the sitting government is “illegitimate, unconstitutional, and has failed to make the dialogue with the Maoists transparent.”<sup>10</sup>

## Security

The November 9, 2002 murder of a Nepali guard of the U.S. embassy in Kathmandu contributed to spurring a U.S. Department of State advisory that American citizens faced a “heightened security risk” in Nepal and should defer plans to travel to that country (the travel advisory has since been eased). Maoist rebels claimed responsibility for the attack (along with a similar murder in December 2001) and issued threats against the “American Diplomatic Mission” in Nepal.<sup>11</sup> The United States reiterated that “the Maoist insurgents need to lay down their arms immediately, stop their brutal and senseless attacks, and engage in a peaceful pursuit of their aims and concerns within the framework of Nepal’s constitution.”<sup>12</sup>

Assistant Secretary of State for South Asia Rocca traveled to Nepal in mid-December 2002 and stated that peaceful dialogue between Maoists and the Nepal government is “imperative” for the country’s political and economic well-being.<sup>13</sup> Prime Minister Chand called resolution through dialogue the only option and pledged

<sup>7</sup> (...continued)

Asia, October 22, 2002.

<sup>8</sup> “Nepal Parties React Strongly to New Government,” *Asia Pulse* (Sydney), October 11, 2002; Sushil Sharma, “Thousands Protest Against Nepal King,” BBC News, December 15, 2002; “Thousands Urge Nepal King to Revive Parliament,” Reuters News, January 13, 2003.

<sup>9</sup> Sushil Sharma, “Nepali Party Starts Protest Rallies,” BBC News, January 13, 2003.

<sup>10</sup> “Chand Govt to Continue Until Elections Are Held,” *Kathmandu Post*, February 4, 2003; Yuvraj Acharya, “Political Parties Turn Down PM’s Invitation to Discuss Peace Talks,” *Kathmandu Post*, February 15, 2003.

<sup>11</sup> U.S. Department of State, Office of the Spokesperson, “Public Announcement: Nepal,” November 22, 2002, available at [[http://travel.state.gov/nepal\\_announce.html](http://travel.state.gov/nepal_announce.html)]; “U.S. Says Think Twice About Visiting Nepal,” Reuters News, November 22, 2002.

<sup>12</sup> Philip Reeker, U.S. Department of State Daily Briefing, November 19, 2002.

<sup>13</sup> Gopal Sharma, “U.S. to Nepal Rebels – End Violence, Begin Talks,” Reuters News, December 14, 2002.

government reciprocation if the Maoists were to formally propose a peace initiative.<sup>14</sup> Although Maoist leaders expressed a willingness to engage in talks, their statements were not formally submitted to the Chand government, which they consider to be unconstitutional.<sup>15</sup> General strikes called for by the rebels were highly effective in curtailing Nepali commerce and education in the final months of 2002, especially in the Kathmandu Valley.<sup>16</sup> Evidence of the rebellion's severe effects came with a December 2002 decision by the World Bank to scrap nine irrigation projects in midwestern Nepal due to security concerns. Tens of thousands of farmers will be affected.<sup>17</sup>

On January 26, 2003, the chief of Nepal's armed police force, his wife, and his bodyguard were shot and killed by suspected Maoist rebels. Initial speculation held that the daring attack in the Nepali capital marked a new, high-profile, low-risk rebel strategy.<sup>18</sup> Yet, only three days after the assassination, the Kathmandu government and Maoist rebels declared a cease-fire. The surprise development apparently was enabled by the efforts of Minister for Physical Planning and former army colonel Narayan Singh Pun, who coordinated directly between the palace and the insurgents. The breakthrough reportedly came after 24 hours of secret negotiations in which the government agreed to remove the bounties it was offering for rebel leaders, withdraw Interpol alerts on them, and cancel its declaration of the Maoists as a terrorist organization.<sup>19</sup>

On March 11, several Maoist leaders emerged from hiding to attend a meeting of mainstream political parties in the Nepali capital. Working with government negotiators, and with the approval of all major Nepali political parties, they were able to unveil a 22-point code of conduct for proposed peace talks.<sup>20</sup> In what may signal a major shift in the rebel position, a top member of the Maoists' negotiating team

<sup>14</sup> "Dialogue Only Way Out of Crisis: PM," *Kathmandu Post*, December 30, 2002; Yabaraj Ghimire, "Govt Willing to Reciprocate If Maoists Formally Propose Peace Initiative: PM," *Kathmandu Post*, December 23, 2002.

<sup>15</sup> "Nepal Rebels Renew Talks Offer," BBC News, December 4, 2002; Mandavi Mehta and Nisala Rodrigo, "Nepal Update," *South Asia Monitor* 53, Center for Strategic and International Studies, December 1, 2002.

<sup>16</sup> "Nepal Shuts Down as Maoists Call General Strike," Reuters News, November 10, 2002; Sushil Sharma, "Maoists Close Nepal Schools," BBC News, December 12, 2002.

<sup>17</sup> Motilal Poudel, "Decision Leaves Thousands of Farmers Shattered," *Kathmandu Post*, December 3, 2002.

<sup>18</sup> Gopal Sharma, "Nepal Killing Seems to Signal Twist in Rebel Strategy," Reuters News, January 28, 2003.

<sup>19</sup> "Govt, Maoists Announce Cease-Fire," *Kathmandu Post*, January 30, 2003; Gopal Sharma, "Nepal Government, Rebels Declare Cease-Fire," *Washington Post*, January 29, 2003; "Hopes Rise for Nepal Peace," BBC News, January 30, 2003.

<sup>20</sup> The code stipulates that both sides are committed to finding a peaceful solution through dialogue, will stop violent activities including strikes and kidnappings, gradually release prisoners, not obstruct the transport of food and medicine, and help displaced people return home ("Nepal's political parties welcome code of conduct for Maoist peace talks," Agence France-Presse, March 14, 2003).

indicated that the monarchy could remain “if the people accept” it.<sup>21</sup> As of late March a date for talks has not been set, but the Kathmandu government has expressed that it is “sincerely committed and engaged in making [peace] talks successful,” and the rebel’s chief negotiator, appearing in public for the first time in 7 years, said, “We have come with a commitment that the peace talks must succeed.”<sup>22</sup>

## Key Country Issues

### Governance

**Political Background.** Nepal, the world’s only officially Hindu country, has been an independent kingdom since 1768. Never colonized, the country was almost totally isolated from outside influence until the early 1950s. A transition from strict king’s rule to constitutional monarchy began in 1959, when then-King Mahendra issued a new constitution and held the country’s first democratic elections. In 1960, however, the king declared the parliamentary system a failure, dismissed the fledgling government, suspended the constitution, and established a partyless system of rule under the monarchy. Although officially banned, political parties continued to exist and to agitate for a return to constitutional democracy.

In February 1990, student groups and the major political parties launched the Movement for the Restoration of Democracy. The centrist Nepali Congress (NC) party joined with the leftist parties to hold peaceful demonstrations in Nepal’s few urban centers. In April 1990, after more than 50 people were killed when police fired on a crowd of demonstrators, then-King Birendra turned power over to an interim government. This government drafted a constitution in November 1990 establishing Nepal as a parliamentary democracy with a constitutional monarch as head of state. The king retains limited powers, including the right to declare a state of emergency with the approval of a two-thirds majority of parliament. However, he is largely disassociated from day-to-day government affairs.

Nepal’s first decade of democracy was marked by political turbulence in which three parliamentary elections were held and 9 governments came to power.<sup>23</sup> In the third parliamentary elections in May 1999, NC president and former Prime Minister Girija Prasad Koirala agreed to support Krishna Prasad Bhattarai as prime minister.

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<sup>21</sup> “Nepal Maoists Open to Talks on Monarchy’s Future,” Reuters News, March 13, 2003.

<sup>22</sup> “Nepal Says to Hold ‘Goodwill Talks’ With Rebels,” Reuters News, March 28, 2003; Gopal Sharma, “Nepal Rebels Say Committed to Peace Talks,” Reuters News, March 29, 2003.

<sup>23</sup> The bicameral parliament consists of a 205-seat House of Representatives (Lower House), whose members are elected by popular vote to serve five-year terms; and a 60-seat National Assembly (Upper House), whose members are appointed (10 by the king, 15 by an electoral college, and 35 by the House of Representatives). For the purpose of this report, “parliament” refers to the House of Representatives, which is the main focus of legislative reporting.



However, in mid-March 2000, rivalry between the two leaders and party dissatisfaction led to Bhattarai stepping down. On March 20, King Birendra appointed Koirala prime minister for a fourth time.

The Kathmandu government faced additional turmoil in June 2001, when Crown Prince Dipendra reportedly shot and killed his parents, King Birendra and Queen Aishwarya, seven other members of the royal family, and himself, after a disagreement over whom he should marry. King Gyanendra, the former king's brother, was crowned on June 4 and he appointed a commission to investigate the assassination. By mid-June, the country began returning to normal following rioting and widespread refusal to believe official accounts of the massacre. In July 2001, Prime Minister Koirala stepped down amid fears of continuing instability and his government's failure to deal with the growing Maoist insurgency. He was replaced by NC leader Sher Bahadur Deuba, who then became the head of Nepal's 11<sup>th</sup> government in as many years.

**Constitutional Crisis.** During the summer of 2002, the government of Nepal was thrown into a constitutional crisis that, many argue, has interfered with its ability to effectively combat the Maoist insurgency. The crisis began in late May, when King Gyanendra, at the request of the prime minister, dissolved parliament and unilaterally declared a three-month extension of emergency rule, which had expired on May 24. The prime minister, who also scheduled early elections for November 2002, reportedly took such action after his centrist Nepali Congress party refused to support his plan to extend emergency rule. Following the prime minister's actions, 56 former members of parliament filed a lawsuit against the prime minister, claiming that there was no constitutional precedent for the dissolution of parliament during emergency rule. In August, the Supreme Court rejected this lawsuit. Although opponents of the prime minister agreed to accept the verdict, they emphasized the difficulty of holding free and fair elections two years ahead of schedule when much of the country was under either rebel or army control.<sup>24</sup>

Meanwhile, these events effectively split the Nepali Congress into two factions. First, the Nepali Congress, led by former Prime Minister Koirala, expelled Deuba from the party for three years for his unilateral actions. Then, in mid-June, Prime Minister Deuba called an NC convention that overturned his expulsion and elected him, rather than Koirala, as NC president. Supporters of Koirala, however, argued that the NC convention led by Deuba, who was an expelled party member at the time, was invalid. In September, Nepal's Election Commission ruled that Koirala was the president of the NC, and, therefore, his faction was authorized to use the party's name and emblems in the November elections. In accordance with the Election Commission's ruling that allowed it one week to apply under a new party name, the Deuba-led faction registered as the Nepali Congress (Democratic) party on

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<sup>24</sup> "Parties React to Court Ruling Backing PM's Right to Dissolve Parliament," BBC Monitoring South Asia, August 7, 2002; Shusham Shrestha, "Nepal PM's Foes Begrudgingly Accept Court Approval of Early Elections," Agence France-Presse, August 7, 2002.

September 23.<sup>25</sup> Given that almost 60% of the population is illiterate, use of the NC emblems could be a significant advantage for the Koirala faction in future elections. On the other hand, some observers speculate that the ruling party split may benefit the Nepal Communist Party-United Marxist and Leninist (NCP-UML) party, the country's second largest.<sup>26</sup>

Although the prime minister pledged that there would be no emergency rule during the scheduled November 2002 elections, Maoist attacks and threatened strikes prompted the government to consider various measures to prevent a Maoist disruption of the polls. The government discussed imposing a partial state of emergency in areas badly affected by the insurgency. However, opposition parties, which urged the government to open a dialogue with the Maoists, argued that by curbing civil liberties, emergency rule would inhibit free and fair elections. As an alternative, the government announced in September that it would hold the elections in six stages over two months, starting in mid-November, so that government troops could be transferred around the country to protect voters and candidates.<sup>27</sup> After further deliberation, however, Nepal's cabinet concluded that the security situation was too risky to hold elections. On October 3, the cabinet asked King Gyanendra to postpone the national elections for one year.<sup>28</sup> The next day, he dismissed the prime minister, disbanded his cabinet, and assumed executive powers.

## Maoist Insurgency

In February 1996, the leaders of the underground Communist Party of Nepal (Maoist) and the United People's Front (UPF) launched a "People's War" in the midwestern regions of Nepal, with the aim of replacing the constitutional monarchy with a one-party Communist regime. Nearly 8,000 people, including civilians, guerrillas, and security personnel, reportedly have been killed in the ensuing insurgency.<sup>29</sup> The uprising appears to have been fueled by widespread perceptions of government corruption and failure to improve the quality of life of citizens, including providing access to cultivable land. The Maoist movement is estimated to include between 5,000 and 10,000 armed fighters and to control one-quarter to one-half of the territory of Nepal.<sup>30</sup> In the Rolpa district of western Nepal, the Maoists

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<sup>25</sup> "Nepal's Embattled PM Forms New Political Party," Reuters News, September 23, 2002.

<sup>26</sup> Kedar Man Singh, "Nepal Says PM is not Head of Ruling Party, Hands Title to Foe," Agence France-Presse, September 17, 2002; "Nepal Poll Panel Rejects PM as Head of Ruling Party," Reuters News, September 17, 2002.

<sup>27</sup> Binaj Gurubacharya, "Nepal to Hold Elections in Stages," Associated Press Newswire, September 28, 2002.

<sup>28</sup> Gopal Sharma, "Nepal Cabinet Seeks to Put Off Elections by a Year," Reuters News, October 3, 2002.

<sup>29</sup> Philip Shenon, "Rebels in Nepal Drive Down Tourism," *New York Times*, February 9, 2003.

<sup>30</sup> Philip Pan, "China Backs Nepal Over Maoist Rebels," *Washington Post*, July 14, 2002; Bertil Litner, "Nepal's Maoists Prepare For Final Offensive," *Jane's Intelligence Review*, October 2002; Binod Bhattarai and Edward Luce, "Nepal's New Premier Unmoved by

(continued...)

reportedly run a parallel government, setting up their own tax system, burning land records, and redistributing seized property and food to the poor. The insurgency has been waged, in part, through torture, killings, and bombings targeting police and public officials. Some analysts have equated the insurgency with the Shining Path movement in Peru. A string of bank robberies, combined with “revolutionary tax” revenue, has made the Nepali Maoists among the wealthiest rebel groups in Asia, with up to \$128 million in net receipts.<sup>31</sup>

Shortly after Prime Minister Deuba took office in July 2001, the Nepali government and the Maoists announced a truce and began peace talks the following month. After three rounds of promising discussions, talks broke down over the Maoists’ demand that the monarchy be eliminated. On November 23, 2001, the Maoists broke the cease-fire with coordinated attacks on army and police posts. Three days later, King Gyanendra declared a state of emergency, which allowed the 53,000-man Royal Nepal Army (RNA) to join the police in fighting the insurgents. The poorly trained, largely ceremonial RNA, however, was unable to stem the increasing Maoist violence. The state of emergency was extended for three months in February and again in May 2002. The government also passed the Terrorist and Disruptive Activities (Control and Punishment) Bill in April, which replaced an anti-terrorism ordinance issued at the time of the first declaration of emergency. The new law makes terrorism a crime punishable by life in prison and allows government forces to detain terrorist suspects for an extendable 90-day period.<sup>32</sup>

After breaking the cease-fire, the Maoists staged numerous deadly attacks on police and army posts, government facilities, and civilian areas, and forced the country’s economy to a standstill in successive general strikes protesting the state of emergency. Of the more than 7,200 deaths attributed to the 7-year-old insurgency, some 60% have occurred since November 2001. Two of the deadliest battles came in May 2002, when, according to Nepali officials, up to 650 rebels and at least 100 soldiers and police officers were killed. Following those clashes, the rebel commander, Pushpa Kamal Dahal – also known as “Prachanda” or “the fierce one” – issued a statement declaring a one-month cease-fire beginning May 15, 2002. Claiming that the rebels have used cease-fires to regroup, the government of Nepal promptly rejected the cease-fire offer and insisted that the rebels first lay down their arms.<sup>33</sup> Critics of the Deuba government’s hard-line approach toward the Maoists argued that it failed to address the rural poverty that underlies the Maoist campaign.<sup>34</sup>

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<sup>30</sup> (...continued)

Clamor at Parliament’s Gates, *Financial Times* (London), November 21, 2002.

<sup>31</sup> Bertil Litner, “Nepal’s Maoists Prepare For Final Offensive,” *Jane’s Intelligence Review*, October 2002.

<sup>32</sup> Binaj Gurubacharya, “Nepal Parliament Approves Anti-Terrorism Bill,” Associated Press Newswire, April 4, 2002.

<sup>33</sup> Neelesh Misra, “Government Rejects Maoists Cease-Fire Offer; Army Says Rebels Withdraw From Western Stronghold,” Associated Press Newswire, May 9, 2002.

<sup>34</sup> David Rohde, “Ousted by King, Nepal Premier Asks for Support,” *New York Times*, October 6, 2002.

After the state of emergency expired on August 28, 2002, the Maoists again stepped up their attacks. During the first week of September, Maoist bombings and battles with police officers and soldiers left more than 300 people dead. On September 16, a general strike called by the Maoists shut down much of the country. November clashes in areas to the west of Kathmandu involved rebel attacks on police stations and administrative headquarters and caused at least 200 deaths, including some 60 security personnel.<sup>35</sup> Along with this accelerated pace of violence, there were reports that sizeable Nepali army units had undergone anti-terrorist training in India, while Maoists may have established a presence in nearby Indian states such as Bihar. Intelligence reports also indicated that, in return for arms and training, Maoist forces provide bases to rebel groups fighting New Delhi's rule in India's northeastern Assam state.<sup>36</sup>

There may be a growing consensus among the governments of the United States, India, and Britain for an increased military effort to contain the rebels, an approach that contrasts sharply with the European donor community's preference for a mediated settlement.<sup>37</sup> Classical Maoism conceives three phases of protracted war: strategic defensive, strategic stalemate, and strategic offensive. With this view, the rebels appear to have reached the stalemate phase and may be preparing to take an offensive posture. Although the insurgents' tactical-level efforts have had great successes thus far and represent a significant threat to the Kathmandu government's ability to govern, one recent assessment indicates that the rebels' tactics may be ill-suited to urban combat, that the Maoists may be outstripping their supply resources, and that the king's assumption of power may provide Kathmandu with the firm leadership necessary to mount an effective counterinsurgency campaign.<sup>38</sup>

## Economy

Nepal is ranked as the 12<sup>th</sup> poorest country in the world, with a per capita annual income of about \$230. Some 42% of the country's 24 million people live in poverty and at least 80% earn a living through agriculture, which accounts for roughly 40% of the country's gross domestic product. Only 20% of the land is arable. Major crops include rice, wheat, maize, jute, sugarcane, and potatoes. Continued reliance on subsistence farming likely will keep Nepal poor for many years to come. Though the industrial base is small, carpet, garment, and textile production has increased in recent years and now accounts for about 70% of merchandise exports. Other major

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<sup>35</sup> Kedar Man Singh, "Nepal Considers New Emergency After 300 Dead in Maoist Unrest," Agence France-Presse, September 11, 2002; Binaj Gurubacharya, "General Strike Shuts Most of Nepal," *Washington Post*, September 16, 2002; "Upsurge in Nepal Violence," BBC News, November 15, 2002; Sushil Sharma, "Nepal Rebels 'Suffer Heavy Casualties,'" BBC News, November 23, 2002.

<sup>36</sup> R. Bedi, "Maoist Battle to Control Nepal," *Jane's Terrorism and Security Monitor*, November 2002.

<sup>37</sup> Rita Manchanda, "'War For Peace' Approach Promises More Bloodshed," Inter Press Service, December 26, 2002.

<sup>38</sup> John Mackinlay, "A Military Assessment of the Nepalese Maoist Movement," *Jane's Intelligence Review*, December 2002.

revenue sources are tourism and remittances from Nepal's famed Gurkha soldiers serving in the British and Indian armies.

For the first time in nearly 20 years, Nepal's economy reportedly contracted by 0.6% in the fiscal year ending July 2002, an apparent result of the internal rebellion's impact on trade (including tourism) and manufacturing.<sup>39</sup> Although expansion in agriculture and manufacturing contributed to a 6.4% economic growth rate for fiscal year 1999/2000 (ending in July), Nepal's economic growth slowed to 5.8% in 2000/2001. The export sector, particularly garment exports (85% of which go to the United States), was hard hit by the global economic downturn. The economy is expected to improve in 2002/2003, yet reports from the troubled tourism sector have brought revised estimates of below 1%. Analysts estimate more positive growth over coming years, but Nepal's long-term outlook is clouded by limited resources – both human and natural – and an unfavorable geographic setting.<sup>40</sup> Government efforts to increase foreign trade and investment have been impeded by political instability, the resistance of vested interests, the small size of the economy and its remoteness, the lack of infrastructure and technological development, and frequent natural disasters, including floods and landslides. The Nepali government budget for 2002/2003 included a 31% increase in spending allocated to fighting the Maoists.<sup>41</sup>

**Hydroelectric Power.** Hydroelectric potential may be Nepal's most attractive asset in the eyes of investors. Nepal and India have completed several joint irrigation-hydroelectric projects and, in 2001, the Kathmandu government implemented a Hydropower Policy that opened the entire sector to private investment. U.S. and EU companies have shown interest, and a reported October 2002 construction deal may make an Australian company the country's largest foreign investor.<sup>42</sup> However, a number of factors, including lack of capital, high transportation costs, environmental and social impact concerns, and political impediments, continue to hamper Nepal's hydropower potential, leaving only 15% of the country's population with access to electricity.

**Tourism.** Nepal's tourist industry – which typically earns Nepal some \$170 million per year, making it the country's third largest foreign exchange source after foreign aid and exports – received a boost in 1997, when an air transport agreement with India increased the number of seats on flights between the two countries by 50%. However, due to the burgeoning Maoist conflict, the royal family killings, and the September 2001 terrorist attacks on the United States, tourist arrivals fell by 20% in 2001, and again by 28% in 2002, to roughly 220,000. Recent government efforts to revive the industry include opening up more mountain peaks to expeditions, reducing visa fees and easing visa procedures, and launching the “Destination Nepal Campaign 2002-2003.”

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<sup>39</sup> “Nepal Economy Hits 20-Year Low,” BBC News, December 11, 2002.

<sup>40</sup> “Nepal: Executive Summary,” Global Insight, October 10, 2002.

<sup>41</sup> “Nepal Allocates More Money to Fight Maoist Rebels,” Associated Press Newswire, July 8, 2002.

<sup>42</sup> “Nepal: Executive Summary,” Global Insight, October 10, 2002.

## Environment

Deforestation is one of the major environmental problems in Nepal. Between 1979 and 1994, Nepal's forest cover declined from 38% to 29%. A 2001 report prepared by the United Nations and the Nepali government cites several key causes of deforestation: population growth, increased consumption of fuel wood, expansion of grazing and agricultural land, internal migration, smuggling of logs into India, and government forest policy. Rapid depletion of forest resources has contributed to landslides, floods, erosion of agricultural lands, silting of waterways, and loss of settlements and human life.<sup>43</sup>

## Refugees

Little progress has been made towards the resolution of a decade-old refugee issue that has soured relations between Bhutan and Nepal, and that has left an estimated 100,000 Bhutanese refugees sheltered in 7 U.N. camps in Nepal. Thousands of ethnic Nepalis, including Bhutanese of Nepali descent, left Bhutan or were forcibly expelled in 1991-1992 after Bhutan began cracking down on illegal immigration as part of an effort to preserve the cultural dominance of the Ngalong ethnic group. The Bhutanese government has maintained that some of the refugees were never Bhutanese citizens and therefore have no right to return. After years of negotiation, a Bhutan-Nepal team has begun verifying the status of the refugees, and Nepal's foreign minister made a March 2003 trip to Bhutan for two-day talks on the dispute.<sup>44</sup>

## India-China Balancing Act

Nepal's geopolitical status as a small, landlocked country sandwiched between two Asian giants – India and China – has severely constrained its foreign policy and trade options. Although Nepal has sought to maintain friendly relations with both neighbors, cultural, linguistic, religious, and economic ties with India historically have been much closer than those with China. Nepal is heavily dependent on India as the primary source of imports, the main market for exports, and for access to the sea through the major port of Calcutta. Moreover, the Himalayan mountain range along Nepal's northern border limits access to China, whereas the 500-mile southern border with India is almost entirely open plains. India, which has always considered Nepal a strategic link in its northern border defenses, has supported Kathmandu's efforts against the Maoist guerrillas by providing helicopters, transport vehicles, and arms and offering to train Nepali soldiers.<sup>45</sup> Some believe that India has the most to

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<sup>43</sup> "Rampant Tree-Felling Shrinks Nepal's Forest Cover," Reuters News, March 27, 2001; United Nations Environment Program, "Nepal: State of the Environment 2001," available at [<http://www.ricap.unep.org>].

<sup>44</sup> U.S. Department of State, *Country Reports on Human Rights Practices: Bhutan 2001*, March 4, 2002; Bhagirath Yogi, "Nepal and Bhutan in Refugee Talks," BBC News, March 24, 2003.

<sup>45</sup> "India Pledged to Support Nepal in Rebel Fight," Reuters News, August 23, 2002.

lose from Maoist advances in Nepal, as New Delhi views Nepali instability as a potential catalyst for the destabilization of India's own troubled northeastern states.<sup>46</sup>

At the same time, the Nepali leadership has long resented Indian economic influence and has sought to establish a more independent foreign policy. Kathmandu has at times "played the China card" in seeking to counterbalance what it considers undue pressure from India. In recent years, Beijing has contributed significant economic aid to Nepal – roughly \$10 million per year – and has pledged "political and moral" support for Nepal's fight against the Maoist insurgency, which it denounces as misusing the ideas of Chairman Mao Zedong. In November 2001, Beijing agreed to provide communications equipment to assist the Nepal Army in operating in mountainous terrain. Some observers have noted that Nepal's stability is important to China, given that it serves as a buffer between China and India, and that a destabilized Nepal could serve as a potential base for Tibetan exiles seeking to challenge Beijing's rule in Lhasa.<sup>47</sup>

## U.S.-Nepal Relations

Relations between the United States and Nepal have always been friendly. U.S. policy objectives toward Nepal include supporting democratic institutions and economic liberalization, promoting peace and stability in South Asia, supporting Nepalese independence and territorial integrity, and alleviating poverty. The United States became Nepal's first bilateral aid donor in January 1951 and has since contributed more than \$1.4 billion bilaterally and multilaterally to that country.<sup>48</sup>

Pending legislation in the 108<sup>th</sup> Congress includes S. 662, introduced in March 2003, that seeks to extend to Nepal certain preferential treatment with respect to apparel articles. Many Tibetan exiles currently reside in Nepal. Members of the 107<sup>th</sup> Congress showed concern for the Tibetan people, their treatment, and their national aspirations. H.R. 1779, with 105 cosponsors in the House, and S. 852, with 20 cosponsors in the Senate, were introduced in May 2001 to address these concerns, but neither was voted upon.

In December 2002, the United States and Nepal signed an accord calling for the non-surrender of nationals to any international criminal court without prior consent.<sup>49</sup> A similar pact, known as an Article 98 agreement, was signed by the governments of the United States and India earlier in the year.

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<sup>46</sup> Mandavi Mehta and Nisala Rodrigo, "Nepal Update," *South Asia Monitor* 53, Center for Strategic and International Studies, December 1, 2002.

<sup>47</sup> Philip Pan, "China Backs Nepal Over Maoist Rebels; Move Reflects Beijing's Growing Interest in Fostering Stability, Not Revolution," *Washington Post*, July 14, 2002.

<sup>48</sup> U.S. Department of State, Bureau of South Asian Affairs, "Background Notes: Nepal," October 2001; "Deputy Assistant Secretary of State Donald Camp's Statement," American Embassy, Kathmandu, Press Release, March 3, 2003.

<sup>49</sup> "Nepal-U.S. Non-Surrender Accord," American Embassy, Kathmandu, Press Release, December 31, 2002.

## Security Assistance

During the final months of 2002 and early months of 2003, U.S. attention to Nepal focused on issues related to the Maoist insurgency. In May 2002, then-Nepali Prime Minister Deuba met with President Bush at the White House and requested military aid to more effectively battle the rebels. The Bush Administration asked Congress for \$20 million in Foreign Military Financing (FMF) to support the Kathmandu government's crackdown on the Maoist rebels, including \$15 million for helicopters for Army Transport Support and \$5 million for Night Vision Goggles and Protective and Communications Gear. The bulk of this funding was included in the FY2002 Supplemental Appropriations Act (P.L. 107-206) of August 2002.

During a December 2002 visit to Nepal, Assistant Secretary of State for South Asia Rocca met with Prime Minister Chand and assured him of continued U.S. aid in combating the insurgency.<sup>50</sup> In January 2003, a spokeswoman for the American embassy in Kathmandu indicated that total U.S. military and security assistance to Nepal will be worth \$17 million, with the smaller amount reflecting an overall reduction in such global aid by the U.S. Congress.<sup>51</sup> This amount combines \$14 million in actual FMF for FY2002 and \$3 million allocated for FY2003 (P.L. 108-7). The Bush Administration has requested another \$10 million in FMF for FY2004 to "continue funding training and equipment programs" that focus on "the acquisition of body armor, communications gear, night vision goggles, perimeter protection, and small arms" for the Royal Nepal Army.<sup>52</sup>

While U.S. officials have pledged to support Nepal's efforts to combat the Maoist insurgency and to strengthen democracy there, they also have dismissed any speculation that the United States seeks to establish military bases in Nepal. Given an expressed U.S. interest in maintaining and improving relations with India, some have argued that the United States should limit any military presence in Nepal that might rile New Delhi.<sup>53</sup> Continuing a military exchange program that was established in the mid-1990s, a platoon-sized team of U.S. Pacific Command forces reportedly will engage in month-long joint military exercises in Nepal beginning

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<sup>50</sup> Gopal Sharma, "U.S. to Nepal Rebels – End Violence, Begin Talks," Reuters News, December 14, 2002.

<sup>51</sup> "U.S. to Give \$17 million in Military Aid to Nepal," Reuters News, January 6, 2003.

<sup>52</sup> U.S. Department of State, "FY2004 Congressional Budget Justification for Foreign Operations," February 13, 2003, available at [<http://www.state.gov/m/rm/rls/cbj/2004>]. The Administration also seeks \$500-600,000 per year for International Military Training and Education programs in Nepal. Much of the Development Assistance, Economic Support Funds, and Child Survival and Health funding for Nepal is aimed at addressing "the root causes of the insurrection."

<sup>53</sup> "US Official Reiterates His Country's Support," BBC Monitoring South Asia, September 6, 2002; "USA Establishes Military Funding to Help Nepal Combat Maoist Insurgency," BBC Monitoring South Asia, September 11, 2002.



January 2003. The exercise is meant to improve force interoperability and to boost Nepal's tactical efficiency.<sup>54</sup>

In a bilateral purchase deal unrelated to promised U.S. security assistance, a consignment of 5,000 U.S.-made M-16 rifles was delivered to Nepal in January and February 2003. These weapons were expected to be combined with a scheduled shipment from Belgium of 5,500 advanced automatic rifles to enhance significantly Kathmandu's anti-insurgency capabilities.<sup>55</sup>

## Other U.S. Assistance

In January 2002, Secretary of State Powell met with Nepali leaders in Kathmandu, where he praised Nepal's strong tradition of tolerance and pledged continued U.S. support for "helping the people of Nepal on the continuing path of development."<sup>56</sup> Actual U.S. assistance to Nepal under Child Survival and Health, Development Assistance, and Economic Support Fund programs in FY2002 totaled \$30.6 million (plus an additional \$2.4 million in food aid). Requested funding for these programs stands at \$37.7 million for FY2003 and another \$38.8 million for FY2004. Peace Corps operations are also funded at more than \$2 million per year.<sup>57</sup>

International assistance to Nepal totals about \$550 million annually. Japan, the World Bank, and the Asian Development Bank are the largest donors, with the United States traditionally providing about 5% of total donor assistance. U.S. foreign assistance to Nepal for FY2002 focused on health and family planning, hydropower development, strengthening democratic processes and civil society, combating trafficking in women and children, providing educational opportunities for women, and supporting Nepali involvement in international peacekeeping. FY2003 and FY2004 assistance will continue these efforts while renewing a focus on economic and infrastructure improvements that can "address the root causes of the insurrection."

## Terrorism

In September 2002, President Bush sent a letter to then-Prime Minister Deuba thanking Nepal for its contributions to ending terrorism.<sup>58</sup> Although the United States repeatedly has condemned numerous insurgent attacks in Nepal as acts of terrorism, the U.S. State Department has not designated the Communist Party of

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<sup>54</sup> Surendra Phuyal, "US Forces in Nepal for Joint Military Exercise," *Kathmandu Post*, January 14, 2003.

<sup>55</sup> Surendra Phuyal, "US Arms Arrive, Wait On for Belgian Minimis," *Kathmandu Post*, January 6, 2002; Sushil Sharma, "Nepal Takes Delivery of US Rifles," BBC News, January 6, 2003.

<sup>56</sup> "Powell Pledges Support For Nepal," USIS Washington File, January 18, 2002.

<sup>57</sup> U.S. Department of State, "FY2004 Congressional Budget Justification for Foreign Operations," February 13, 2003, available at [<http://www.state.gov/m/rm/rls/cbj/2004>].

<sup>58</sup> "Bush Thanks Nepal for Efforts Against Terrorism," BBC Monitoring South Asia, September 18, 2002.

Nepal (Maoist) or the United People's Front as Foreign Terrorist Organizations (FTOs) under U.S. law.<sup>59</sup> During her December 2002 visit to Kathmandu, Assistant Secretary of State for South Asia Rocca reportedly stated that FTO designation may be considered "if [Maoist] violence continues unabated," and the legal requirements for such a decision presently are under examination by U.S. officials.<sup>60</sup> At the time of this writing, no links have been found between the Nepali Maoists and international terrorist organizations such as Al Qaeda, and the Maoist fighters have no known state patrons providing arms or supplies.<sup>61</sup>

## Human Rights Concerns

Although the human rights situation in Nepal has improved since political reforms began in 1990, the United States determined that in 2002 Kathmandu's record on human rights remained "poor" and that the government continues to "commit numerous abuses." Torture, extrajudicial killings, arbitrary arrests and detentions, and police impunity are major concerns. Moreover, "Women, persons with disabilities, and lower castes suffered from widespread discrimination. Violence against women, trafficking in women and girls for prostitution, and child labor also remained serious problems." Freedom of assembly, speech, and the press, mandated by the Nepali constitution, have been suppressed by the government under the current state of emergency.<sup>62</sup> Reports by Amnesty International have echoed these criticisms, asserting that, since the November 2001 breakdown of peace talks, "the people of Nepal have experienced unprecedented levels of political violence." One report claims that at least 66 people "disappeared" in 2002, making Nepal the country with the third highest number of disappearances reported worldwide in the past four years.<sup>63</sup>

Along with the U.S. Department of State, Amnesty International, and Human Rights Watch also have criticized the Maoist insurgents for human rights violations in their ongoing conflict. The Maoists allegedly have committed murders, bombings, torture, abductions, and the severing of victims' limbs. Although they continue to target the police and the army, the Maoists have also killed and injured civilians, including political leaders, local elites, and suspected informers. Reports indicate

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<sup>59</sup> "Foreign Terrorist Organizations" are overseas-based groups that are designated by the U.S. Secretary of State as meeting the criteria specified in Section 219 of the Immigration and Nationality Act (U.S. Department of State Fact Sheet, Office of Counterterrorism, August 9, 2002).

<sup>60</sup> Keshav Pradhan, "US May Declare Maoists Terrorists," *Hindustan Times* (Delhi), December 15, 2002; telephonic interview with U.S. State Department official, January 13, 2003.

<sup>61</sup> "US Official Reiterates His Country's Support," BBC Monitoring South Asia, September 6, 2002.

<sup>62</sup> U.S. Department of State, *Country Reports on Human Rights: Nepal 2002*, March 31, 2003.

<sup>63</sup> Amnesty International, "2003 UN Commission on Human Rights: A Time for Deep Reflection," December 1, 2002 "Nepal: Human Rights Abuses Have Reached Unprecedented Levels," Amnesty International Press Release, December 19, 2002.

that the Maoists recruit children as young as 14 years old as soldiers, messengers, and human shields. According to a July 2002 report prepared by a coalition of international and Nepali human rights groups, at least 30% of the Maoist guerrillas are children.<sup>64</sup>

Human trafficking and child labor are serious social problems in Nepal. An estimated 5,000-12,000 Nepali women and girls are lured or abducted to India and forced into prostitution each year. In addition, reports indicate that 2.6 million children in Nepal, mostly girls, are economically active, with 1.7 million of these children working full-time. Most child laborers – about 95% – work in agriculture, and roughly 40% do not attend school. Until 1994, children reportedly constituted nearly one-third of the workforce in Nepal’s carpet industry. However, due to heightened media attention in consumer nations, the establishment of a certification system for carpets made without child labor, and increased efforts by the Ministry of Labor, children reportedly now comprise only 2% of Nepal’s carpet workers.<sup>65</sup> In August 2002, the International Labor Organization and the Finance Ministry of Nepal reached agreement on a \$5 million project funded by the U.S. Department of Labor to combat the worst forms of child labor in Nepal.<sup>66</sup>

**Figure 1. Map of Nepal**



Adapted by CRS from Magellan Geographix.

<sup>64</sup> “30 Percent of Nepalese Maoist Fighters Are Children: Study,” Agence France-Presse, July 6, 2002.

<sup>65</sup> Amnesty International, *Annual Report 2001: Nepal*, and *Annual Report 2002: Nepal*; U.S. Department of State, *Country Reports on Human Rights: Nepal 2001*, March 4, 2002.

<sup>66</sup> “Agreement to Combat Child Labor,” Press Releases, American Embassy, Kathmandu, August 20, 2002.