# Directors Report

# Your Directors Are Pleased To Submit Their Report And The Audited Accounts Of Your Company For The Year Ended ३१ St Asadh २०७४ (१Sth July २०१7). Socio Economic Environment

The economy of Nepal, in the year under review was a melange of positive and negative indicators. Good monsoons and substantial improvement in the power supply situation aided a turnaround in agriculture and industry and resulted in GDP growth of 6.९% (O.०१% in the previous year). Against a degrowth of 6.३% witnessed in the previous year the industry sector grew by १०.१% during the year under review. The average consumer inflation during the year eased to ४.५% (9 ९% in the previous year) on the back of a positive impact on the supply side coupled with base vear effect.

The merchandise trade deficit however increased to 35.3% of GDP as against ३१.३% during the previous year. Moreover the share of inward remittances from expatriate Nepalese the primary source of foreign exchange for the country continued to slow down and hit २६.8% of share of GDP as against २९ ६% in the previous year Consequently the Current Account recorded a deficit of O.४% versus a surplus of 6.२% in the previous fiscal. These factors, coupled with the recent floods and substantial land inundation in the Terai continue to challenge the macroeconomic stability of the country over the short to medium term.

New legislations like the Industrial Enterprises Act Labour Act and Social Security Act incorporate features that will, no doubt, enhance the ease of doing business. Further measures like contemporisation of legislation in areas like Foreign Investment and alignment of laws on Intellectual Property with the provisions of the WTO Framework and the Paris Convention of the World Intellectual Property Organization will further boost investor confidence and strenathen the lona term health of the economvy.

Similarly, interpretation and implementation of laws which, at times, are at odds with legislative intent need to be addressed. For example, while the Income Tax Act permits set-off of losses of one business with the profits of another business carried out by the same assessment authorities do not permit such set-off, interpreting the law differently Such denial of set-off acts as a disincentive for companies such as yours that are investing in new lines of business which invariably make losses in the initial vears. entity

Your Company continues to engage with the policy makers on such matters to induct clarity and contemporaneity in the regulatory framework that can contribute in revitalizing investment and industrial activity in Nepal.

Despite the fact that the legal cigarette industry occupies an important place in the countrys economy, having substantial share in the manufacturing GDP the discriminatory taxation and restrictive regulatory framework governing the industry continue to pose extraordinary challenges and complexities for the industry The industry provides livelihood, directly and indirectly to more than 4 lakh farmers, farm workers and others engaged in the cultivation of tobacco and the tobacco trade and contributes approximately १०% of the total excise revenue collected by the Government. Moreover in the backdrop of diminishing share of manufacturing in the GDP the legal cigarette industry is one of the handful of industries that has adequate domestic manufacturina capacity.

Notwithstanding these factors, the Government unfortunately elected to once again increase the excise duty on domestic manufacture Of cigarettes in the last Budget while leaving the tax rates on imported cigarettes unaltered. Unlike the global trend of more than 9०% of tobacco consumption in cigarette form, in Nepal the consumption of tobacco in the form of dutypaid cigarettes is around २०%. Notably the share of duty cigarettes has dropped significantly over the years. Despite the low share of tobacco consumption, dutypaid cigarettes contribute more than 8४% of the total tobacco revenue collected by the Government Notwithstanding this, the cigarette centric taxation policy of the Government has resulted in punitive and discriminatory taxation of this product. According to the affordability index of cigarettes published by WHO , duty paid cigarettes in Nepal are the least affordable in entire South East Asia The affordability index (% of per capita GDP required to purchase २००० cigarettes of most popular brand) which stands at २3. १०% is one of the highest in the world. paid region.

In contrast the balance 8०% of tobacco consumption in the country in the form of Bidis, Smokeless Tobacco (SLT) products like khaini, gutka, snuff and betel quid with tobacco ( "Paan" ) and illicit cigarettes are lightly taxed or evade tax. Also, by virtue of fragmented manufacture over thousands of units operating in the unorganized sector these products manage to evade taxes substantially and outside the purview of regulatory oversight, thus avoiding compliance with the statutory provisions of the Tobacco Products Control Act (TOPCAJ including those relating to Graphic Health Warnings (GHW). Moreover, the quality credentials Of most of these products are highly suspect due to the unhygienic conditions under which are manufactured and the mostly inferior inputs used in their manufacture. The high tax cost of dutypaid cigarettes has been driving consumption to revenue inefficient products like bidi, SLT and illicit stay they

cigarettes which, due to reasons of low tax incidence as well as tax evasion are offered to consumers at verv attractive and affordable prices.

The importance of increasing taxes on non cigarette tobacco products has been recognized in the Technical Manual on Tobacco Administration published by the World Health Organisation. However, a skewed focus on cigarettes has resulted in a taxation policy that not only sub-optimises the revenue potential of tobacco but also spurs growth of contraband cigarette trade and encourages consumption of inferior quality tobacco products, thereby defeating the health objectives of tobacco control as well. The distortions in the Governments tax policy on tobacco products have also been highlighted in the Report on Tobacco Control in Nepal published by the Ministry of Health. Your Company continues to engage with the policy makers on the importance of a balanced and equitable approach to tobacco taxation.

The regulatory framework for cigarettes also continues to stifle the legal cigarette industry. As per provisions of the Tobacco Products Control and Regulation Act (TOPCA), cigarette packages have to carry Graphic Health Warnings (GHW ) covering at least 7५% of the area of the cigarette packet. Whilst the legal cigarette industry adheres to statutory compliances in this regard scrupulously the smuggled international brands of cigarettes do not bear the GHW required under Nepalese laws. Consequently these cigarettes are perceived to be " safer" alternative by many consumers, resulting in almost unfettered growth of contraband cigarettes. Thus, even the regulatory framework on cigarettes unwittingly, in encouraging the growth of illicit trade in cigarettes. In this context it would be pertinent to note that as per a WHO Reporti published earlier this year out of the १९५ countries jurisdictions, ५२ do not require warning or have small warnings and ६५ others have medium size health warnings (covering less than ४९% of the front and back of the packaae . helps,

USA, China and Japan the top three countries that account for more than half the global cigarette consumption do not mandate any GHW on cigarette packages and have, instead, adopted textual warnings only

|  |  |  |  |
| --- | --- | --- | --- |
| 0 | 1 | 2 | 3 |
| Country | Annual Consumption (Billions) | Per Capita Cigarette Consumption | Health Warning Requirement |
| USA | 282 | 1028 | Text only on side panel) |
| China | 2512 | 1711 | Text30%front& back) |
| Japan | 193 | 1841 | Text-30%front& back) |
| Nepal | 12 | 420 | Pictorial-75% of the entirepack area |

Significantly GHW proposed by the US Food and Drug Administration (FDAJ in the past were held to be unconstitutional by the United States Court of Appeals, for the District of Columbia Circuit. In reaching this conclusion the Court noted that "FDA failed to present any data much less the substantial evidence required under the APA ~showing that enacting their proposed graphic warnings will accomplish the agency s stated objective of reducing smoking rates. FDA has not provided a shred of evidence much less the substantial evidence" required by the APA showing that the graphic warnings will "directly advance its interest in reducing the number of Americans who smoke. FDA. offers no evidence showing that such warnings have directly caused a material decrease in smoking rates in any of the countries that now require them. The Court further observed that one of the principal researchers relied upon by the FDA had also conceded, on the basis of survey of relevant literature on the subject that there is no way to attribute declines in smoking to the new health warninas.

In line with the global lack of correlation between GHW and decline in smoking no correlation has been established in Nepal either between implementation of GHW and reduction in consumption increase in cessation of tobacco. Despite this, the Ministry of Health issued twO new Directives in Kartik71 and Poush७1 (November २०१4 and January २०१5) which, inter requires manufacturers to multiple pictorial warninas and warnina messaqes on at least 9०% of the pack area. alia, print

Like the ७५% GHW the proposed 9०% GHW are also excessively large. are even more gruesome and unreasonable in comparison with the existing ७५% GHW. There is no evidence that smoking causes the diseases depicted in the dreadful pictures neither there is any that such warnings lead to decreased consumption of tobacco. These warnings will only have unintended consequences including: Also, they proof

further fillip to contraband trade of non GHW bearing international

brands of ciaarettes that by virtue of beina dutyevaded are available