

# **Deepening India-Nepal Economic Ties: From Trade to Development Cooperation**





**EXPORT-IMPORT BANK OF INDIA**

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## **Deepening India Nepal Economic Ties: From Trade to Development Cooperation**

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## Executive Summary

Nepal, a landlocked country in South Asia, is bordered by China to the north and India to the south, east, and west. About one-third of its land area is covered by forests, most of which are state-owned. The country's economy has historically been reliant on agriculture, foreign aid, and trade with India. For many years, political uncertainty shaped economic policies, but the adoption of a permanent constitution in 2015 established Nepal as a secular federal republic with seven administrative regions and a bicameral legislature.

Nepal's nominal GDP has steadily grown, rising from US\$ 34.2 billion in 2019 to an estimated US\$ 43.7 billion in 2024. Economic growth is expected to stabilize at 4.9% in 2025 and 2026, driven by structural reforms and economic normalization. The industrial sector, particularly electricity and construction, is expected to expand in the medium term, contributing to continued growth. Inflation, which peaked at 7.8% in 2023 due to rising food and fuel prices, is projected to stabilize at 5.6% in 2024 and further moderate to 5.2% and 5.4% in 2025 and 2026 respectively, reflecting effective monetary policies.

Nepal's external sector has faced fluctuations, especially in its current account balance. After a sharp deficit of 12.6% of GDP in 2022, indicating trade imbalances and remittance fluctuations, a temporary current account surplus of 3.2% of GDP is expected in 2024. This improvement is likely due to a recovery in tourism, increased remittances, and reduced imports, signaling a positive shift in Nepal's economic landscape.

### International Trade Landscape of Nepal

Nepal's economy, heavily reliant on agriculture, remittances, and a growing service sector, faces challenges due to its landlocked geography and limited resources. As a Least Developed Country (LDC), Nepal benefits from tariff concessions under the Generalized System of Preferences (GSP) and has signed multiple trade agreements.

In 2021, UN's Committee for Development Policy (CDP) recommended graduation of Nepal from LDC status in 2026. Nepal's impending graduation from LDC status presents a complex scenario, particularly concerning its trade dynamics.

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## Merchandise Trade

Nepal's total merchandise trade rose from US\$ 8.5 billion in 2014 to US\$ 11.6 billion in 2023, reflecting increases in both exports and imports. Exports grew gradually from US\$ 900.9 million in 2014 to US\$ 1.7 billion in 2021, driven by demand for agriculture, textiles, and handicrafts. However, exports declined to US\$ 1.2 billion in 2023 due to global economic slowdown and supply chain disruptions. Imports surged from US\$ 7.6 billion in 2014 to US\$ 15.8 billion in 2021, fueled by rising consumer demand and industrial growth, before moderating to US\$ 10.4 billion in 2023. Compared to a trade deficit of US\$ 14.1 billion in 2021, it shrank to US\$ 9.2 billion in 2023, with moderation in imports due to government restrictions on non-essential goods and weaker economic activity.

Nepal's major exports in 2023 included carpets (9%), coffee, tea, maté, and spices (8.9%), and iron and steel (8.4%). India remains the largest export destination, accounting for 65.7% of Nepal's total exports, followed by the USA and Germany. On the other hand, Nepal's merchandise imports included mineral fuels and oils accounting for 22.4% of total imports, followed by iron and steel (9%) and electrical machinery and equipment (7.2%). Nepal's import basket is dominated by India, which accounts for 69.8% of Nepal's total imports due to geographical proximity and healthy trade relations. China was the second largest source of commodities to Nepal, followed by UAE.

## Services Trade

Nepal's service exports have shown a fluctuating trend over the years, with total exports reaching US\$ 1,640 million in 2023 from US\$ 1389 million in 2014. A major share of these come from commercial services while government goods and services contribute 7.6%. Within commercial services, travel services account for 36.7%, reflecting the importance of tourism to Nepal's economy. A significant portion (57.9%) of Nepal's commercial service exports falls under other commercial services, with other business services making up 85.8% of this category.

Nepal's service imports have grown significantly from US\$ 1,197 million in 2014 to US\$ 2,275 million in 2023, reflecting a 91% increase. The majority of these imports are concentrated in commercial services (99.2%), with transport and travel services being the dominant sectors. In addition to transport and travel, other commercial services, including business services (66.8% of this category), play an increasing role in Nepal's service imports.

## India Nepal Bilateral Trade Relations

The bilateral framework for trade is anchored on the India-Nepal Treaty of Trade and Agreement of Co-operation to Control Unauthorized Trade – 2009 (renewed in October 2023). The Trade Treaty allows Nepal unilateral duty-free access to the Indian market. India and Nepal also have a Treaty of Transit, which confers transit rights through each other's territory through mutually agreed routes and modalities.

India accounts for approximately two-thirds of Nepal's merchandise trade, a third of its service trade, and a third of foreign direct investment. India also supplies nearly all of Nepal's petroleum and plays a crucial role in inward remittances from workers, pensioners, and professionals in India.

Bilateral trade between India and Nepal has grown from US\$ 4.8 billion in 2014 to US\$ 8.1 billion in 2023, reflecting an average annual growth rate of 9.3%. India's total exports to Nepal amounted to US\$ 7.3 billion

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while imports were recorded at US\$ 811.5 million in 2023. The trade balance has been in India's favour with trade surplus increasing from US\$ 3.6 billion in 2014 to US\$ 6.4 billion in 2024.

In 2023, Nepal ranked as the 17<sup>th</sup> largest export destination for India, accounting for 1.7% of India's total exports. India's export basket to Nepal remains fairly diversified, with mineral fuels and oils making up 32% of total exports in 2023. Other significant export categories include iron and steel and machinery and mechanical appliances, among others.

Coffee, tea and spices and iron and steel accounted for major imported commodities each accounting for 12.7% of India's total imports from Nepal. Other major commodity included animal and vegetable oil (10.3%), man-made staple fibres (9.8%) and aircraft, and its parts (7.9%) among others.

## **Bilateral Services Trade between India and Nepal**

India's trade with Nepal has primarily focused on merchandise, but the trade in services has seen steady growth over the past decade. From 2014 to 2023, services trade between the two countries grew from US\$ 630.6 million to US\$ 1.4 billion, reflecting an average annual growth rate (AAGR) of 10.4%. Services exports from India to Nepal increased at an AAGR of 10.8%, rising from US\$ 286.8 million in 2014 to US\$ 663.6 million in 2023. At the same time, imports grew at a slightly slower pace of 10.3% annually. Overall, India's bilateral trade in services with Nepal constituted less than 1% of India's trade in services with the rest of the world.

In 2023, of India's total services exports to Nepal, travel services accounted for the largest share at 81.7%. Other commercial services ranked second, amounting US\$ 65.1 million while contributing 9.8% of the total export value followed by transport services making up 8.5%, of the total services exports during the year.

Service imports have grown significantly from US\$ 343.8 million in 2014 to US\$ 760.8 million in 2023, more than doubling over the period. Commercial services dominate India's imports, consistently accounting for over 99% of the total value. Transport and Travel together contribute 84.5% of the total commercial services imports reflecting increasing tourism and travel between India and Nepal. Other commercial services accounted for more than 14% of the total imports, followed by other business services, particularly professional and management consulting services.

## **Trends in Nepal's Foreign Direct Investments**

Nepal has been striving to attract Foreign Direct Investment (FDI) since 1980-81 fiscal year, with significant reforms in its legal and institutional frameworks designed to facilitate foreign investment. Over the years, the government has made efforts to create an environment conducive to attracting investment by introducing investment-friendly laws and regulations. These reforms have aimed at improving the ease of doing business, offering tax incentives, and promoting key sectors such as hydropower, manufacturing, and tourism.

Nepal's strategic location between two major economies—China and India—presents opportunities for foreign investors to tap into regional markets. Additionally, the country's young workforce, natural resources, and untapped potential in sectors like infrastructure and energy make it an appealing destination for investment. There are however, also a few challenges such as cumbersome policies for foreign investors, limited infrastructure and the legal and regulatory framework which are relatively less aligned with respect to international standards.

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As per United Nations Conference on Trade and Development (UNCTAD Stat), Nepal's FDI inflows have had a tumultuous trend in the past decade. The total inflows rose from US\$ 30 million in 2014 to US\$ 74 million in 2023. FDI peaked in 2017 at US\$ 198 million, driven by Chinese investments in infrastructure, cement, and mining, aided by improved policies following the 2015 earthquake. However, FDI dropped in 2018 due to political uncertainty, infrastructure challenges, and weak policy implementation. It rebounded in 2019 to US\$ 185 million, primarily due to Indian investments in hydropower projects. In 2020, FDI fell sharply by 32% to US\$ 126 million, largely due to the decline in tourism, a key industry for Nepal. While there was a slight recovery in 2021, FDI again decreased in 2022 due to restrictive regulations on profit repatriation and foreign transactions, highlighting Nepal's limited integration into the global financial system.

According to Financial Times' fDi Markets, during the period January 2014 to December 2023, Nepal received a total envisaged capital expenditure of US\$ 4.8 billion across 64 projects, in the country. Maximum envisaged FDI inflows were from China, accounting for 39.8% of total capital expenditure, followed by the US and Singapore. In terms of the total number of projects and number of companies invested, India ranked first with a total of 16 projects and companies respectively.

Renewable energy sector has been the major recipient of envisaged capital expenditure in Nepal, accounting for 46.4% of the total envisaged capital expenditure followed by investments in communications and building materials, among others.

The Act Restricting Investment Abroad, 1964 imposes stringent controls on Nepali individuals and entities seeking to invest overseas. The Act prohibits Nepali individuals or entities from making any form of investment in a foreign country except in case an exemption is provided by the Nepal Government.

## **Nepal's Investment Relations with India**

India is one of Nepal's largest trading partners and a significant source of FDI. The two countries collaborate in key sectors such as energy, infrastructure, manufacturing, and agriculture, with India investing in various development projects across Nepal. According to fDi Markets database, from January 2014 to December 2023, the total envisaged capital investment of India in Nepal stood at a cumulative amount of US\$ 381 million. In terms of capital investments during 2014-2023, the largest share has been in communications (23.6% of Indian investment in Nepal), pharmaceuticals (17.2%), and financial services (17.1%) among others.

## **Potential for Enhancing India's Exports to Nepal**

The study has identified potential items of exports which could be targeted by Indian exporters. To identify the products based on their export competitiveness in Nepal, a four-quadrant analysis has been undertaken based on the HS Code classifications at 6-digit level by calculating their Normalised Revealed Comparative Advantage (NRCA) and mapping them against Annual Average Growth Rate (AAGR) of global imports of Nepal for all products. The quadrants are drawn by comparing the overall AAGR of global imports of Nepal for all products during 2020-2023 (which was 0.9%), to the NRCA of India's exports to Nepal during the same period. This exercise aims to identify products whose imports in the Nepal over the period 2020-2023 have performed better than the overall average of Nepal for all products during this period, implying that the share of such products in Nepal's import basket has witnessed an increase, a reflection of their rising demand and map them with products where India has a comparative advantage. At 6-digit HS Code level, with minimum exports of US\$ 0.1 million from India to Nepal, 2337 products have been identified with the total exports from India to Nepal amounting to US\$ 7.2 billion (99.7% of India's exports to Nepal in 2023),

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while the total world imports by Nepal for the same products stood at US\$ 9.5 billion in 2023 (91.8% of Nepal's global imports in 2023).

Out of the 2337 items at the HS 6-digit level, 1109 items belonged to the category of the product champions. The combined exports of these items from India to Nepal were US\$ 5.1 billion in 2023, representing approximately 69.8% of India's exports to Nepal in 2023. The study has identified potential items of exports which could be targeted by Indian exporters. According to the analysis, in the short term, it is suggested to strengthen the existing products in the category of Product Champions to harness the full potential for the products which are already showing a robust growth in Nepal, where India's exports also hold a comparative advantage. These are mainly petroleum oil (refined) and gaseous hydrocarbons, iron and steel, pharmaceutical products, rice, oilcakes of soyabean oil, electrical energy, parts and accessories of motorcycles, wheat, electrical equipment, among others.

The product category of Underachievers comprised 627 items, with India's exports of these products amounting to US\$ 591 million to Nepal. These products constitute a share of 8.2% in India's total exports to Nepal. These are the product items in which import demand in Nepal's market are rising, but exports from India are currently not competitive. Nepal's imports of these products stood at US\$ 2.4 billion in 2023, presenting significant opportunities for exporters. In the medium to long run, efforts and investments could be enhanced in the Underachievers category products to develop capacities in these products, which will help in meeting the demands of Nepal in a more competitive manner. These include smart phones, motor vehicles with electric motors, urea, wire of refined copper, board and cabinets for electric control, liquid dielectric transformer, parts of hydraulic turbine, ceramic sanitary fixtures, among others. The export gap in case of Underachievers is around US\$ 1777.3 million (difference between Nepal's Global Imports and India's Export to Nepal for the respective products) which could be targeted to increase India's exports to Nepal. India needs to expand its production and exports of the products in which it has comparative advantage with Nepal with a cumulative export potential gap of US\$ 2 billion.

## **Potential Areas of Cooperation and Recommendations**

### ***Enhancing Bilateral Services Trade***

During the last decade, except in 2017 and 2018, India has maintained a services trade deficit with Nepal, with travel and transport services being the dominant sectors. India is Nepal's largest source of imports of travel services and a key destination for medical tourism. India also supplied 64.1% of Nepal's global computer services imports, offering opportunities in software development, data analytics, and IT support. Additionally, India contributed 21.9% of Nepal's global business services imports, with growth potential in professional, technical, and consulting services. Strengthening these sectors, which present promising opportunities, could further enhance India-Nepal economic ties.

### ***Cooperation in Energy Infrastructure***

Nepal's electricity sector plays a crucial role in its economy, leveraging its vast hydropower potential for exports to South Asia. The country aims to achieve 11,700 MW of installed capacity by 2029, driving industrial growth, with over 9,500 MW of projects licensed for construction. Nepal currently exports 650 MW of electricity to India, with Indian enterprises actively involved in major hydropower projects, and both countries having agreed on a framework to import up to 10,000 MW over the next decade. India is also facilitating

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Nepal's electricity exports to Bangladesh, with a tripartite power sales agreement signed in October 2024 with the first transaction inaugurated in November 2024. Additionally, India is financing key transmission lines projects under Government of India's Lines of Credit routed through Exim Bank and supporting petroleum pipeline projects to enhance regional energy security. These initiatives highlight deepening energy cooperation between Nepal and India, fostering trade and infrastructure development in the region.

### ***Cooperation in Transport and Connectivity***

Nepal's tourism sector, contributing over 8% to GDP, relies on strong connectivity infrastructure, with key priorities in road, aviation, and urban transport development. India and Nepal are enhancing cross-border connectivity through rail links, roads, and Integrated Check Posts (ICPs) with India's grant assistance. Notwithstanding the significant progress made through improved rail and road connectivity between the two countries, cross-border trade remains constrained by high transaction costs due to inadequate infrastructure at border points, with some Land Custom Stations (LCSs) lacking modern facilities. India is supporting improvements in trade infrastructure, including new ICPs, enhancing infrastructure facilities including storage and testing infrastructure, which could further reduce trade costs and strengthen bilateral economic integration.

### ***Banking and Financial Cooperation***

India and Nepal are strengthening financial collaboration to facilitate investment flows and improve banking services. As on December 31, 2024, 3 Indian Banks have established presence in Nepal through joint venture or representative office. These are Nepal SBI Bank Ltd (subsidiary of SBI with 55.1% stake), Everest Bank Ltd (Joint Venture / Associate of Punjab National Bank with 20% share), and ICICI Bank Ltd (Representative Office in Kathmandu). Expanding Indian banks' presence could enhance financial services for businesses. Both countries have also advanced cross-border digital payments, with NPCI International Payments Limited (NIPL) partnering with Nepal's Fonepay to enable Unified Payment Interface (UPI) transactions. Additionally, Nepali visitors can now use UPI One World in India, improving seamless digital payments and strengthening economic and cultural ties.

### ***Healthcare***

India is a key player in Nepal's healthcare sector, being the largest supplier of pharmaceuticals (71.2% share) and the second-largest source of medical devices. Nepal's hospital and medical technology markets are projected to grow, offering significant investment opportunities for India. Key areas include establishing multi-specialty hospitals, tertiary care centers, and diagnostic facilities, as well as setting up pharmaceutical manufacturing units to ensure affordable medicine supply. India can also support Nepal's healthcare through investments in telemedicine, AI-driven diagnostics, and medical education programmes. Expanding collaborations in healthcare infrastructure and skill development would enhance Nepal's medical resilience while strengthening bilateral ties.

Other areas of cooperation include capacity building and supply of aerospace and defense equipment, among others.

In conclusion, India and Nepal share strong economic ties, reinforced by historical and cultural linkages, and people-to-people connections. Under its "Neighbourhood First Policy", India has prioritized enhancing economic, infrastructure, energy, and digital connectivity cooperation with Nepal, alongside capacity-building

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initiatives. Both economies offer immense opportunities for closer collaboration with each other as well as in the region for economic development.

India Exim Bank's commitment towards India's Neighbourhood First Policy" is reflected through its various activities and programmes, which support Government of India's initiatives in promoting strategic partnerships with Nepal.



# Macroeconomic Overview of Nepal

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Nepal, a landlocked country nestled in the Himalayas, is home to eight of the world's fourteen highest peaks, including the Mount Everest, boasts of a breathtaking Himalayan landscape that attracts adventurers, researchers, and nature enthusiasts from around the globe. Despite being a landlocked country with limited natural resources and an evolving transportation network, Nepal possesses significant potential for economic growth.

Approximately one-third of Nepal's land area is covered by forests, the majority of which are state-owned. Timber remains one of the country's most valuable natural resources, holding significant economic potential. The export of forest products plays a crucial role in generating Indian rupees, with a large fraction of timber being sent to India. Additionally, the government-run Timber Corporation of Nepal operates sawmills that supply construction and furniture wood to the Kathmandu Valley.

Nepal's economic and political evolution has been deeply intertwined, with governance changes significantly shaping the country's development trajectory. Economic modernization efforts began in the 1950s, alongside political reforms that aimed to transition the Kingdom towards democracy. The parliament was dissolved in 1960. As a result this period saw slow economic progress, as state-controlled policies stifled private enterprises, restricting large-scale investment and leading to trade diversification.

During the 1980s, economic and ideological groups evolved stemming from eased regulatory norms. The shift to multiparty system and the promulgation of a new constitution in 1990, marked a shift towards a more liberalized economy. A more open political and economic framework emerged fostering a gradual move concerning market-oriented policies and increased foreign trade.

Despite these changes, Nepal's economy remained heavily dependent on agriculture, foreign aid, and trade with India. The political instability of the late 1990s and early 2000s has impacted the country's economic growth. Amid shifting governance structures, an interim constitution was introduced in January 2007, paving the way for the establishment of a republic in May 2008.

For several years, Nepal operated under an interim framework, with economic policies largely shaped by political uncertainty. The long-awaited permanent constitution, adopted in 2015, formally established Nepal as a secular federal republic with seven administrative regions and a bicameral legislature. This constitutional shift

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aimed to provide greater stability for economic planning, encouraging regional development, infrastructure investment, and larger participation of private enterprises in Nepal's economic landscape.

Nepal's macroeconomic indicators reflect a mix of resilience and challenges, shaped by global trends, domestic policies, and external shocks. Nepal's GDP at current prices has shown steady growth, rising from US\$ 34.2 billion in 2019 to an estimated US\$ 43.7 billion in 2024 (**Table 1.1**). However, economic growth was severely impacted by the COVID-19 pandemic, with the economy experiencing a contraction of (-) 2.4% in 2020. A gradual recovery followed, reaching 5.6% in 2022, but the economy slowed to 2.0% in 2023, stemming from global inflationary pressures, reduced remittances, and trade disruptions, before picking up to 3.1% in 2024. Growth is estimated to stabilize at 4.9% in 2025 and 2026, indicating a positive outlook driven by structural reforms and economic normalization. The industrial sector of Nepal is expected to flourish in medium term stemming from significant expansion in electricity and construction. According to World Bank, over the past decade, more than 9,500 MW of hydropower projects have been licensed for construction, with many already underway and others expected to become operational during the projection period, given their long gestation times. The government's ambitious goal of exceeding 11,700 MW of installed electricity capacity by FY29 is anticipated to fuel industrial growth. Additionally, a series of monetary policy measures aimed at supporting the construction sector—such as extensions for loan repayments, moratoriums on blacklisting, and relaxed credit rating requirements—are likely to stimulate activity in this crucial industry

Despite short-term volatility, GDP per capita is expected to improve, reaching US\$ 1607.5 by 2026, from its current estimated level of US\$ 1381.1 in 2024, signalling long-term economic progress. Inflation has remained a concern, peaking at 7.8% in 2023, due to rising food and fuel prices, before stabilizing to an estimated 5.6% in 2024, and further moderating 5.2% and 5.4% in 2025 and 2026 respectively, reflecting anticipated monetary policy effectiveness. Nepal's external sector has seen fluctuations in its current account balance, with a sharp deficit of 12.6% of GDP in 2022, indicating high trade imbalances and remittance fluctuations. However, a temporary surplus of an estimated 3.2% of GDP in 2024 suggests improvements, possibly due to a recovery in tourism, increased remittances, or reduced imports<sup>1</sup>.

The exchange rate has shown depreciation over time, with the Nepalese rupee (NPR) weakening from NPR 112.6 per US\$ in 2019 to an estimated NPR 133.7 per US\$ in 2024, due to inflation differentials, trade deficits, and external economic pressures. The NPR is expected to further depreciate to NPR 137.7 per US\$ in 2026. Overall, Nepal's economy is on a recovery path but faces challenges including financial vulnerabilities, such as rising non-performing loans, which could limit private sector credit. Frequent administrative changes could deter investment, while delays in capital expenditure could slow infrastructure growth. External risks include regional instability, trade disruptions affecting tourism and demand, and natural disasters threatening welfare gains. A slowdown in migrant-receiving economies could impact remittances, which are vital for household income and poverty reduction. However, migration also presents challenges like high costs and poor working conditions. To maximize migration benefits and sustain growth, Nepal must strengthen migration management and foster domestic job creation.

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<sup>1</sup> Nepal Development Update (October 2024), World Bank

**Table 1.1: Macroeconomic Indicators of Nepal**

Indicator	2019	2020	2021	2022	2023	2024 <sup>e</sup>	2025 <sup>e</sup>	2026 <sup>e</sup>
GDP, current prices (US\$ bn)	34.2	33.4	36.9	41.2	40.9	43.7	47.8	52.6
Real GDP Growth (% change)	6.7	-2.4	4.8	5.6	2.0	3.1	4.9	4.9
GDP per capita, current prices (US\$)	1,185.7	1,139.2	1,229.5	1,348.2	1,316.1	1,381.1	1,486.5	1,607.5
Inflation (avg, % change)	4.6	6.2	3.6	6.3	7.8	5.6	5.2	5.4
General government gross debt (% of GDP)	34.0	43.3	43.3	42.7	47.1	49.7	50.4	50.4
Population (mn)	28.8	29.3	30.0	30.5	31.1	31.6	32.2	32.7
Current account balance (US\$ bn)	-2.4	-0.3	-2.8	-5.2	-0.6	1.4	-0.8	-2.1
Current account balance (% of GDP)	-6.9	-1.0	-7.7	-12.6	-1.4	3.2	-1.6	-4.0
National currency per US\$ (average)	112.6	118.3	118.1	125.2	132.1	133.7	136.1	137.7

Note: <sup>e</sup> Estimates

Source: World Economic Outlook (WEO), IMF, October 2024 and Exim Bank Research

## Nepal's Least Developed Country (LDC) Graduation

The category of least developed country (LDC) was established in 1971 by the United Nations General Assembly (UNGA). It was created to attract special international support for the most vulnerable and disadvantaged members of the United Nations. At the beginning, 25 countries, including Nepal, were identified as LDCs.

The UN LDC category is assessed using three criteria: Gross National Income (GNI) per capita, Human Assets Index (HAI) and Economic and Environmental Vulnerability Index (EVI). Countries must meet two of the three criteria at two consecutive triennial reviews of the Committee for Development Policy (CDP) to be eligible for graduation. Nepal exceeded the thresholds for graduation on two of the three LDC criteria, namely the HAI and the EVI, for more than two consecutive triennial reviews of the CDP, in 2015, 2018 and 2021. In 2021, CDP recommended graduation of Nepal from LDC status in 2026<sup>2</sup>.

Nepal's impending graduation from LDC status presents a complex scenario, particularly concerning its trade dynamics. The most significant implication is the loss of preferential market access granted through LDC-specific schemes, which could lead to increased tariffs on its exports. While Nepal benefits from a strong bilateral trade relationship with India, where preferential access is secured through a treaty, its exports to other key markets could face potential setbacks.

The European Union (EU), United Kingdom, and Turkey provide a crucial three-year transition period for graduating countries, but other preference-granting nations would implement new, potentially higher, tariff regimes immediately post-graduation. This disparity in tariff changes poses a challenge, as some product would transition smoothly to "next-best" tariffs, while others will experience significant increases, impacting their competitiveness.

<sup>2</sup> National Planning Commission, Government of Nepal, February

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According to the report titled “Nepal’s graduation from the LDC category” published by South Asia Watch on Trade, Economics and Environment (SAWTEE)<sup>3</sup>, Nepal’s merchandise exports could fall by 2.5% to 4% as a result of increased tariffs upon graduation. Exports to the European Union (EU) are expected to see the largest losses, assuming that Nepal’s exports will face ordinary Generalized System of Preferences (GSP) instead of GSP+. The impact would be the largest for the clothing and textiles sector. Therefore, to mitigate the negative impacts, Nepal must prioritize enhancing its export competitiveness, diversifying its markets, and actively engaging in trade negotiations to secure favourable access.

<sup>3</sup> [https://sawtee.org/publications/LDC\\_graduation\\_study\\_Sep\\_2022.pdf](https://sawtee.org/publications/LDC_graduation_study_Sep_2022.pdf)



## International Trade Landscape of Nepal

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Nepal's economy, characterized by a mix of agriculture, remittances, and a growing service sector, faces inherent challenges due to its landlocked geography and resource constraints. As a small economy with limited resources, it relies heavily on trade to meet the needs of its population. In the 1980s, Nepal's exports primarily consisted of raw materials, agro-based products, handicrafts, and blankets—items traded in large volumes but with low profitability. However, since the 1990s, there has been a shift towards exporting manufactured components to some extent. The rising inflow of remittances has boosted people's purchasing power, leading to increased imports of vehicles, electronics, jewellery, and other luxury goods.

According to the World Bank, in 1991, Nepal's merchandise trade accounted for approximately 25.4% of its GDP, with overall trade, including services, reaching around 34.7%. By 2005, Nepal witnessed a significant increase in its merchandise trade share to nearly 38.7% and overall trade to 44.1%, indicating a growing integration into the global economy. This upward trend in trade continued into the following years, with a peak in merchandise trade reaching 47.6% of GDP in 2021. However, a slight decline in the years following 2021 saw a drop in both merchandise trade and overall trade as percentages of GDP. Notably, the share of trade in services has been relatively steady over time, contributing around 10-11% to GDP, with some fluctuations—reaching a low of 6.4% in 2021 before recovering to 9.6% in 2023. Through these shifts, it is evident that Nepal's economic landscape has been increasingly influenced by its external trade activities, with merchandise trade being a significant driver.

As LDC, Nepal currently benefits from tariff concessions under the Generalized System of Preferences (GSP) offered by several countries. Additionally, Nepal has signed multiple regional and bilateral trade agreements to facilitate trade. Nepal has signed bilateral trade agreements and treaties with seventeen countries, including the United States, United Kingdom, Serbia, India, Russia, Republic of Korea, Egypt, Bangladesh, Sri Lanka, Bulgaria, China, Czech Republic, Pakistan, Romania, Mongolia, and Poland. The Treaty that Nepal signed with India in 1996 and amended in 2009 is its most important in terms of trade volume. Except for some items under quantitative restrictions, the trade treaty puts Nepal in a unilateral duty-free trade regime with India, which accounted for more than 60% of Nepal's total trade in FY 2019-20<sup>4</sup>.

The South Asian Free Trade Area (SAFTA) under the South Asian Association for Regional Cooperation (SAARC), which Nepal ratified, and which came into effect in 2006 is a key regional agreement for Nepal. Under SAFTA, the eight SAARC member nations—Nepal, Bhutan, India, Bangladesh, Pakistan, Sri Lanka, Maldives,

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<sup>4</sup> International Trade Administration (ITA), Department of Commerce, USA

and Afghanistan—have committed to providing advantages to LDCs, including reduced sensitive lists in certain SAFTA member states. This ensures Duty-Free Quota-Free (DFQF) access for a broader range of products. Additionally, LDCs benefit from more lenient rules of origin, requiring a change in tariff heading and value addition that is 10% lower than the standard requirement for non-LDCs. While the general rule mandates 60% value addition, certain products are subject to specific regulations.

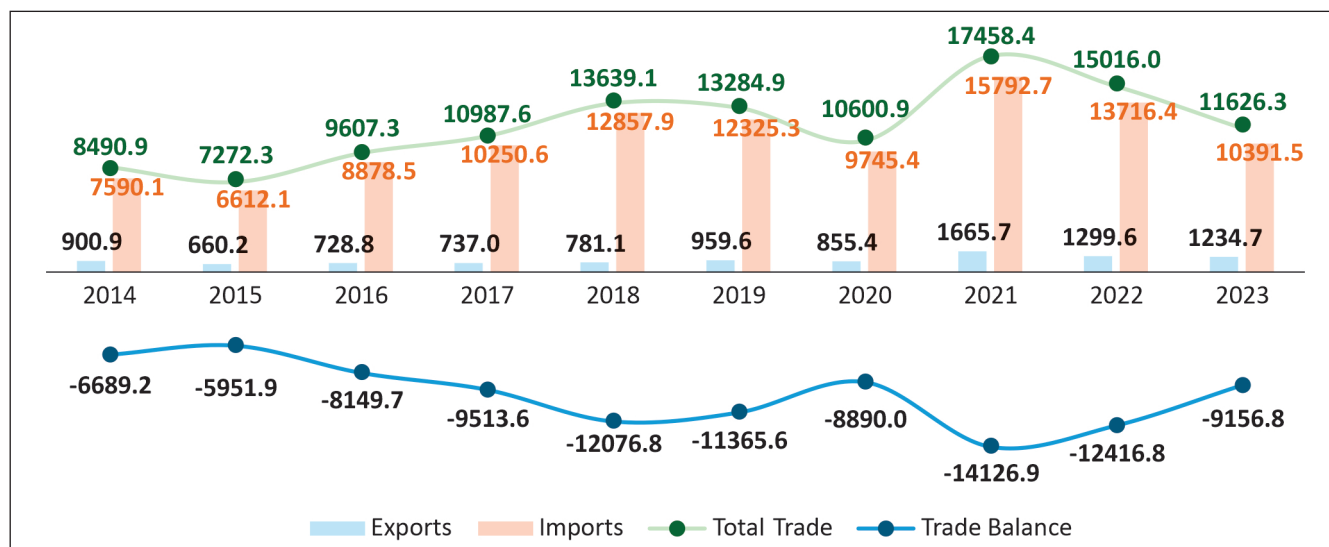
Nepal's trade relations have historically been dominated by India due to geographic proximity, historical ties, and economic interdependence. India remains Nepal's primary trading partner, accounting for the majority of its imports and exports. However, in recent years, Nepal has also engaged in trade with other significant partners, including China and the USA.

## Nepal's Merchandise Trade

Total merchandise trade of the Nepal has risen from US\$ 8,490.9 million in 2014 to US\$ 11,626.3 million in 2023, reflecting the rise in both exports and imports (**Chart 2.1**). Nepal's merchandise trade has experienced a persistent trade deficit from 2014 to 2023. Exports showed gradual growth from US\$ 900.9 million in 2014 to US\$ 1,665.7 million in 2021, driven by increased demand for agriculture, textiles, and handicrafts, along with government incentives and improved trade connectivity. However, exports declined to US\$ 1,299.6 million in 2022 and further to US\$ 1,234.7 million in 2023, likely due to global economic slowdown, reduced foreign demand, and supply chain disruptions. On the other hand, imports surged from US\$ 7,590.1 million in 2014 to a peak of US\$ 15,792.7 million in 2021, fuelled by rising consumer demand, industrial expansion, and reliance on imported raw materials. This rapid import growth significantly widened the trade deficit, reaching its highest level in 2021 at US\$ 14,126.9 million.

However, in 2023, Nepal saw some improvement, as the trade deficit shrank to US\$ 9,156.8 million, mainly due to a sharp decline in imports to US\$ 10,391.5 million. The drop in imports was influenced by government restrictions on non-essential goods, foreign exchange reserve concerns, and weaker economic activity. Total trade, which peaked at US\$ 17,458.4 million in 2021, also declined to US\$ 11,626.3 million in 2023, reflecting Nepal's efforts to reduce import dependence and manage trade balance.

Chart 2.1: Nepal's Merchandise Trade (in US\$ million)



Source: ITC Trade map and India Exim Bank Research

## Nepal's Merchandise Exports

Nepal's major export commodities in 2023 reflect a diverse mix of traditional and emerging sectors, with carpets and other textile floor coverings leading at US\$ 111.1 million (accounting for 9% of Nepal's total global exports), followed by coffee, tea, maté, and spices with a share of 8.9% (**Table 2.1**). The export of iron and steel witnessed significant growth, reaching US\$ 104 million (8.4% share), a remarkable rise from US\$ 33 million in 2019, possibly due to increased demand in neighbouring markets. Man-made staple fibres remained a key export at US\$ 94.2 million (7.6% share), though slightly lower than in 2022 (US\$ 102.6 million). A notable decline was observed in animal, vegetable, or microbial fats and oils, which peaked at US\$ 391.9 million in 2022 but dropped sharply to US\$ 83.6 million in 2023, likely due to price fluctuations.

At more disintegrated level, major export commodities included carpets and other textile floor coverings made of wool or fine animal hair, palm oil and its fractions whether or not refined (excluding chemically modified and crude), cardamoms, neither crushed nor ground and non-alcoholic beverages (excluding water, fruit or vegetable juices, milk and beer), among others. These trends highlight Nepal's growing strength in textiles, processed food, and industrial goods, but also the need for diversification and sustainable market strategies to maintain export growth.

**Table 2.1: Major Merchandise Exports of Nepal (in US\$ million)**

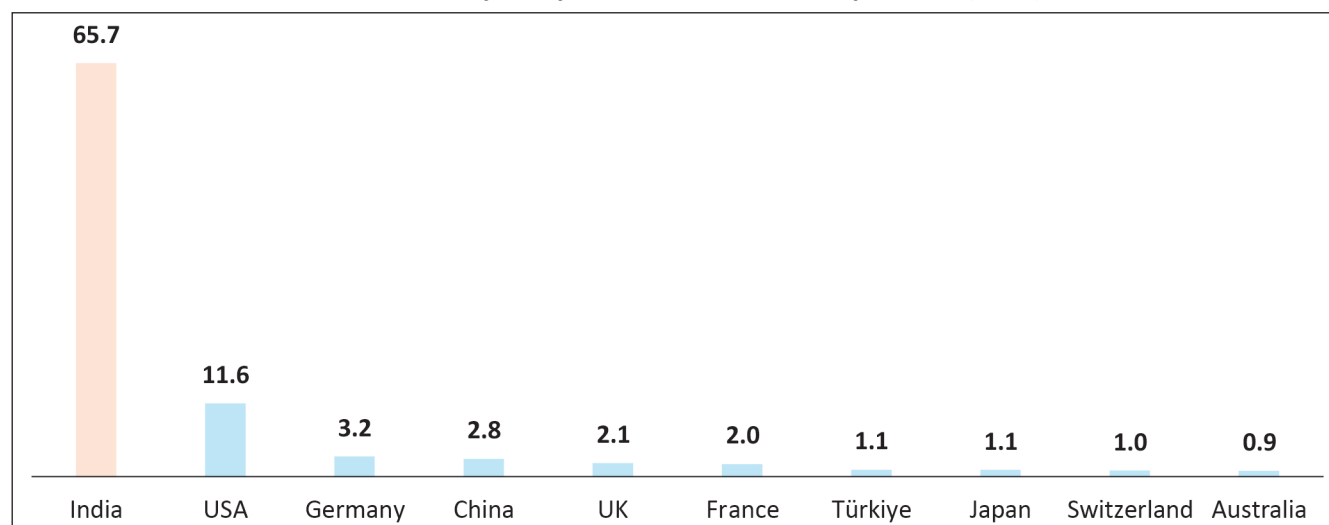
HS Code	Product label	2014	2019	2022	2023	% Share in 2023
<b>Total</b>	<b>All products</b>	<b>900.9</b>	<b>959.6</b>	<b>1299.6</b>	<b>1234.7</b>	<b>100.0</b>
57	Carpets and other textile floor coverings	74.3	67.7	89.0	111.1	9.0
09	Coffee, tea, maté and spices	59.5	75.1	90.4	110.1	8.9
72	Iron and steel	78.9	33.0	54.3	104.0	8.4
55	Man-made staple fibres	68.4	83.5	102.6	94.2	7.6
15	Animal, vegetable or microbial fats and oils	1.4	245.2	391.9	83.6	6.8
88	Aircraft, spacecraft, and parts thereof	1.9	2.6	0.3	66.8	5.4
22	Beverages, spirits and vinegar	3.0	0.9	4.7	64.7	5.2
44	Wood and articles of wood; wood charcoal	2.1	0.5	16.8	53.8	4.4
63	Other made-up textile articles	37.2	34.6	22.2	53.0	4.3
23	Residues and waste from the food industries	15.3	29.0	51.2	52.9	4.3

Source: ITC Trade map and India Exim Bank Research

## Nepal's Export Destinations

India remains Nepal's largest export destination, accounting for 65.7% of Nepal's total exports in 2023 (amounting US\$ 811.5 million) (**Chart 2.2**). Other major markets include the USA (11.6%), Germany (3.2%), China (2.8%), the UK (2.1%) and France (2%). It's worth noting that India is the top destination for nine of the top ten export commodities of Nepal aforementioned in **Table 2.1**.

Chart 2.2: Major Export Destinations of Nepal in % (2023)



Source: ITC Trade map and India Exim Bank Research

The dominance of India in Nepal's top export destinations is evident across key commodities such as iron and steel (99.4% share in Nepal's exports of the commodity), animal and vegetable fats and oils (99.7%), beverages and spirits (97.9%), and wood products (94.2%), indicating Nepal's high trade dependence on India (Table 2.2).

Notably, coffee, tea, and spices are majorly exported to India (93.9%), with minimal shares going to Germany and Pakistan. While India remains Nepal's primary trade partner, there is a growing export presence in markets like Türkiye (for man-made staple fibres), the USA (for food residues), and France (for textile articles).

Table 2.2: Major Export Destinations for Commodities Exported by Nepal, 2023

HS Code	Product (Export Value)	Major Export Destinations of Nepal	Exports (US\$ million)	% Share in Nepal's Exports of Product
	All products (US\$ 1,234.7 million)	India (largest)	811.5	65.7
		USA	143.6	11.6
		Germany	39.5	3.2
		China	34.8	2.8
		UK	26.5	2.1
57	Carpets and other textile floor coverings (US\$ 111.1 million)	USA	57.8	52.0
		UK	8.4	7.6
		Germany	8.1	7.3
		India (4 <sup>th</sup> largest)	5.2	4.7
		Italy	4.4	4.0

HS Code	Product (Export Value)	Major Export Destinations of Nepal	Exports (US\$ million)	% Share in Nepal's Exports of Product
09	Coffee, tea, maté and spices (US\$ 110.1 million)	<b>India (largest)</b>	<b>103.4</b>	<b>93.9</b>
		Germany	2.6	2.3
		Pakistan	0.7	0.6
		USA	0.6	0.5
		Japan	0.5	0.5
72	Iron and steel (US\$ 104.0 million)	<b>India (largest)</b>	<b>103.3</b>	<b>99.4</b>
		Romania	0.63	0.61
		Belgium	0.03	0.03
		Czech Republic	0.01	0.01
55	Man-made staple fibres (US\$ 94.2 million)	<b>India (largest)</b>	<b>79.72</b>	<b>84.65</b>
		Türkiye	13.30	14.12
		China	1.06	1.12
		United Kingdom	0.07	0.07
		Belgium	0.02	0.02
15	Animal, vegetable or microbial fats and oils (US\$ 83.6 million)	<b>India (largest)</b>	<b>83.31</b>	<b>99.68</b>
		Poland	0.13	0.15
		Australia	0.11	0.13
		Taiwan	0.02	0.02
		Japan	0.01	0.01
88	Aircraft, spacecraft, and parts thereof (US\$ 66.8 million)	<b>India (largest)</b>	<b>63.9</b>	<b>95.6</b>
		France	1.7	2.5
		Australia	0.4	0.6
		Canada	0.4	0.5
		Malaysia	0.3	0.5
22	Beverages, spirits and vinegar (US\$ 64.7 million)	<b>India (largest)</b>	<b>63.3</b>	<b>97.9</b>
		Japan	0.5	0.8
		Australia	0.3	0.4
		Italy	0.1	0.2
		Hong Kong	0.1	0.2
44	Wood and articles of wood; wood charcoal (US\$ 53.8 million)	<b>India (largest)</b>	<b>50.7</b>	<b>94.2</b>
		China	1.1	2.1
		USA	1.1	2.1
		Germany	0.2	0.4
		UK	0.1	0.2
63	Other made-up textile articles (US\$ 53 million)	<b>India (largest)</b>	<b>17.3</b>	<b>32.8</b>
		USA	14.4	27.2
		France	4.7	8.9
		China	3.4	6.4
		Germany	3.2	6.0

HS Code	Product (Export Value)	Major Export Destinations of Nepal	Exports (US\$ million)	% Share in Nepal's Exports of Product
23	Residues and waste from the food industries (US\$ 52.9 million)	India (largest)	25.7	48.6
		USA	24.5	46.3
		Canada	2.0	3.8
		Pakistan	0.1	0.2
		Singapore	0.1	0.2

Source: ITC Trade map and India Exim Bank Research

## Nepal's Merchandise Imports

Nepal's merchandise imports have experienced significant fluctuations over the years, peaking at US\$ 15.8 billion in 2021 before dropping to US\$ 13.7 billion in 2022 and US\$ 10.4 billion in 2023 (**Table 2.3**). Among the major imported commodities, mineral fuels and oils held the largest share in 2023, accounting for 22.4% of total imports (amounting US\$ 2.3 billion). Iron and steel followed at 9% (amounting US\$ 933.4 million), while electrical machinery and mechanical appliances together constituted 14% of the total import value. Vehicles, cereals, plastics, and pharmaceuticals also represented notable shares, though their import values saw some decline in 2023 compared to previous years.

The decrease in overall imports in 2023 largely stems from economic adjustments, possibly influenced by policy measures, trade restrictions, or global market trends. The significant share of mineral fuels underscores Nepal's reliance on petroleum oil imports, making it vulnerable to international price fluctuations.

**Table 2.3: Major Merchandise Imports of Nepal (in US\$ million)**

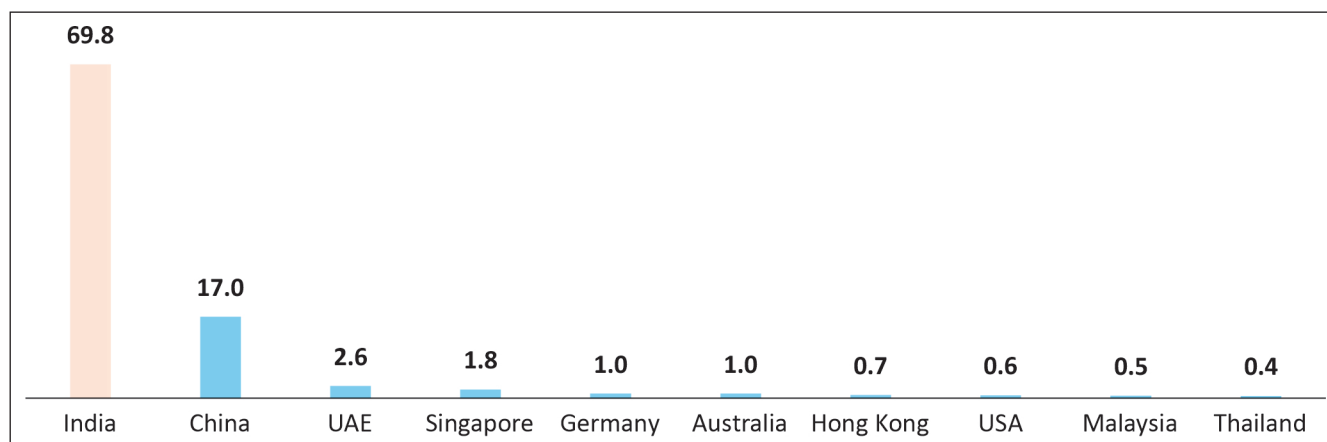
HS Code	Product label	2014	2019	2022	2023	% Share in 2023
<b>Total</b>	<b>All products</b>	<b>7,590.1</b>	<b>12,325.3</b>	<b>13,716.4</b>	<b>10,391.5</b>	<b>100.0</b>
27	Mineral fuels and oils	1,497.0	2,145.6	3,149.6	2,330.6	22.4
72	Iron and steel	614.2	1,078.5	1,113.9	933.4	9.0
85	Electrical machinery and equipment	506.8	907.9	856.2	749.4	7.2
84	Machinery and mechanical appliances	488.0	1,049.3	949.5	711.8	6.8
87	Vehicles other than railway or tramway	445.1	780.7	525.8	487.4	4.7
10	Cereals	335.6	451.9	476.9	366.7	3.5
39	Plastics and articles thereof	277.7	455.0	532.6	331.7	3.2
30	Pharmaceutical products	183.9	261.1	435.7	312.2	3.0
71	Natural or cultured pearls, precious or semi-precious stones and metals	390.4	376.2	443.8	254.5	2.4
07	Edible vegetables and certain roots and tubers	136.0	266.3	247.7	196.9	1.9

Source: ITC Trade map and India Exim Bank Research

## Nepal's Import Sources

Nepal's import basket is dominated by India, which accounts for 69.8% of Nepal's total imports (**Chart 2.3**). The heavy reliance is largely due to geographical proximity, simplified foreign exchange mechanism, long-standing trade agreements, and ease of transportation. India supplies essential goods, including petroleum, food, medicines, and industrial products, making it Nepal's most crucial trade partner. The second-largest source, China, contributes 17% followed by UAE (2.6%), Singapore (1.8%), Germany (1%) and Australia (1%).

**Chart 2.3: Major Import Sources of Nepal in % (2023)**



Source: ITC Trade map and India Exim Bank Research

Nepal's dependence on India is particularly evident in essential commodities such as mineral fuels (99.6% share in Nepal's total imports of the commodity), cereals (98.6%), and iron and steel (91.4%), indicating Nepal's economic and logistical ties with its southern neighbour (**Table 2.4**). Behind India, China contributed significantly to imports of electrical machinery (42.6% share in Nepal's total imports of the commodity) and vehicles (26.1%). Other countries such as the UAE, Singapore, and Germany play minor roles in Nepal's imports, particularly in pharmaceuticals, plastics, and precious stones and metals, among other products. The UAE dominates Nepal's import of precious metals, while Australia has emerged as a key supplier of edible vegetables (36.1% share in Nepal's total imports of the commodity).

**Table 2.4: Major Import Sources for Commodities Imported by Nepal, 2023**

HS Code	Product (Import Value)	Major Import Suppliers of Nepal	Imports (US\$ million)	% Share in Nepal's Imports of Product
	All products (US\$ 10,391.5 million)	India (largest)	7,250.3	69.8
		China	1,768.9	17.0
		UAE	265.8	2.6
		Singapore	185.4	1.8
		Germany	99.7	1.0

HS Code	Product (Import Value)	Major Import Suppliers of Nepal	Imports (US\$ million)	% Share in Nepal's Imports of Product
27	Mineral fuels, mineral oils and products of distillation (US\$ 2,330.6 million)	<b>India (largest)</b>	<b>2,320.2</b>	<b>99.6</b>
		UAE	4.7	0.2
		Singapore	2.3	0.1
		Malaysia	1.4	0.1
		Bahrain	0.3	0.01
72	Iron and steel (US\$ 933.4 million)	<b>India (largest)</b>	<b>852.7</b>	<b>91.4</b>
		China	26.1	2.8
		Taiwan	20.9	2.2
		Belgium	11.7	1.3
		South Korea	6.5	0.7
85	Electrical machinery and equipment and parts (US\$ 749.4 million)	<b>India (largest)</b>	<b>323.2</b>	<b>43.1</b>
		China	319.0	42.6
		Singapore	43.0	5.7
		Hong Kong	35.5	4.7
		Japan	3.9	0.5
84	Machinery and mechanical appliances (US\$ 711.8 million)	<b>India (largest)</b>	<b>379.3</b>	<b>53.3</b>
		China	165.7	23.3
		Singapore	55.0	7.7
		UAE	35.0	4.9
		USA	7.8	1.1
87	Vehicles other than railway or tramway rolling stock, and parts (US\$ 487.4 million)	<b>India (largest)</b>	<b>336.1</b>	<b>69.0</b>
		China	127.4	26.1
		Singapore	5.2	1.1
		Japan	4.6	1.0
		South Korea	3.9	0.8
10	Cereals (US\$ 366.7 million)	<b>India (largest)</b>	<b>361.7</b>	<b>98.6</b>
		Türkiye	2.4	0.6
		Argentina	1.0	0.3
		Brazil	0.6	0.2
		China	0.4	0.1
39	Plastics and its articles (US\$ 331.7 million)	<b>India (largest)</b>	<b>249.9</b>	<b>75.3</b>
		China	49.4	14.9
		Saudi Arabia	9.9	3.0
		UAE	5.2	1.6
		Thailand	3.8	1.2

HS Code	Product (Import Value)	Major Import Suppliers of Nepal	Imports (US\$ million)	% Share in Nepal's Imports of Product
30	Pharmaceutical products (US\$ 312.2 million)	<b>India (largest)</b>	<b>222.2</b>	<b>71.2</b>
		Germany	54.8	17.6
		Belgium	17.1	5.5
		Netherlands	3.5	1.1
		China	2.5	0.8
71	Natural or cultured pearls, precious or semi-precious stones and metals (US\$ 254.5 million)	UAE	177.7	69.8
		<b>India (2<sup>nd</sup> largest)</b>	<b>25.6</b>	<b>10.1</b>
		Hong Kong	22.5	8.9
		Türkiye	22.4	8.8
		China	4.0	1.6
07	Edible vegetables and certain roots and tubers (US\$ 196.9 million)	<b>India (largest)</b>	<b>102.6</b>	<b>52.1</b>
		Australia	71.1	36.1
		China	11.4	5.8
		Myanmar	4.9	2.5
		Türkiye	1.7	0.9

Source: ITC Trade map and India Exim Bank Research

## Service Exports of Nepal

Nepal's service exports have shown a fluctuating trend over the years, with total exports reaching US\$ 1,640 million in 2023, marking a recovery from US\$ 1,235 million in 2022 (**Table 2.5**). The bulk of these exports (92.4%) comes from commercial services, while government goods and services contribute 7.6%. Within commercial services, travel services account for 36.7%, reflecting the importance of tourism to Nepal's economy. Although travel exports rebounded to US\$ 557 million in 2023 from US\$ 373 million in 2022, they remain lower than the pre-pandemic level of US\$ 705 million in 2019. Transport services, particularly air transport, contribute 5.3%, with passenger air services forming the majority. A significant portion (57.9%) of Nepal's commercial service exports falls under other commercial services, with other business services making up 85.8% of this category.

**Table 2.5: Service Exports of Nepal (in US\$ million)**

Product/Sector	2014	2019	2022	2023	% Share in 2023
<b>Services Exports of Nepal</b>	<b>1,389</b>	<b>1,615</b>	<b>1,235</b>	<b>1,640</b>	<b>100</b>
Government goods and services	289	109	87	124	7.6
Commercial services	1,099	1,506	1,148	1,516	92.4
Transport	30	100	66	81	5.3
Air Transport	-	97	59	71	87.7
Passenger (Air)	-	96	55	69	97.2
Freight (Air)	-	1	4	3	4.2

Product/Sector	2014	2019	2022	2023	% Share in 2023
Other	-	3	7	10	12.3
Travel	487	705	373	557	36.7
Other commercial services	582	701	710	878	57.9
Insurance and pension services	4	16	10	7	0.8
Telecommunications, computer, and information services	359	185	118	118	13.4
Other business services	219	501	581	753	85.8

Source: WTO Stat and India Exim Bank Research

## Service Imports of Nepal

Nepal's service imports have grown significantly from US\$ 1,197 million in 2014 to US\$ 2,275 million in 2023, reflecting a 91% increase. The majority of these imports are concentrated in commercial services (99.2%), with transport and travel services being the dominant sectors. Transport services, particularly sea transport (61% of transport imports), are vital for Nepal's trade, while air transport and other transport services also contribute substantially. The growth in travel services, rising from US\$ 504 million in 2014 to US\$ 1,359 million in 2023, suggests a booming tourism sector, which is an essential part of Nepal's economy.

In addition to transport and travel, other commercial services, including business services (66.8% of this category), play an increasing role in Nepal's service imports. The slight decline in telecommunications and information services could reflect improvements in Nepal's domestic infrastructure.

**Table 2.6: Service Imports of Nepal (in US\$ million)**

Product/Sector	2014	2019	2022	2023	% Share in 2023
<b>Services Imports of Nepal</b>	<b>1,197</b>	<b>1,718</b>	<b>2,027</b>	<b>2,275</b>	<b>100.0</b>
Government goods and services	24	30	12	18	0.8
Commercial services	1,173	1,687	2,016	2,257	99.2
Transport	435	628	691	579	25.7
Sea Transport	-	408	431	353	61.0
Air Transport	-	11	29	26	4.5
Other	-	209	231	200	34.5
Travel	504	702	983	1,359	60.2
Other commercial services	235	358	342	319	14.1
Insurance and pension services	42	69	104	90	28.2
Telecommunications, computer, and information services	32	40	10	16	5.0
Other business services	161	249	229	213	66.8

Source: WTO Stat and India Exim Bank Research



# India-Nepal Bilateral Trade Relations

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Nepal, a landlocked country in South Asia, is bordered by China to the north and India to the south, east, and west. It shares borders with five Indian states: Sikkim, West Bengal, Bihar, Uttar Pradesh, and Uttarakhand. India-Nepal relations are rooted in strong people-to-people ties, with shared religious, linguistic, and cultural connections. India's cooperation with Nepal dates back to the 1950s. It has been Nepal's largest developmental partner, focusing on major infrastructure projects and providing grants in priority sectors like health, education, and connectivity to support Nepal's rapid development.

The bilateral framework for trade is anchored on the India-Nepal Treaty of Trade and Agreement of Co-operation to Control Unauthorized Trade - 2009. The Trade Treaty allows Nepal unilateral duty-free access to the Indian market. Both Treaties were automatically renewed in October 2023. India and Nepal also have a Treaty of Transit, which confers transit rights through each other's territory through mutually agreed routes and modalities. Its revised version was signed on 1<sup>st</sup> June 2023 for a period of 7 years and then will be auto-renewed for further period of 7 years. The Treaty allows Nepal's merchandise to move seamlessly through India's road, railway, inland waterways and ports network.

India and Nepal are also signatories to South Asian Free Trade Agreement (SAFTA) along with the other SAARC<sup>5</sup> nations namely, Afghanistan, Bangladesh, Bhutan, Maldives, Pakistan and Sri Lanka. The Objectives of this Agreement are to promote and enhance mutual trade and economic cooperation among member countries, by eliminating barriers to trade, promoting conditions of fair competition in the free trade area, and ensuring equitable benefits for its members and recognizing the need for special and differential treatment for least-developed country (LDC) like Nepal, such as zero or very low tariff rates on many of Nepal's exports.

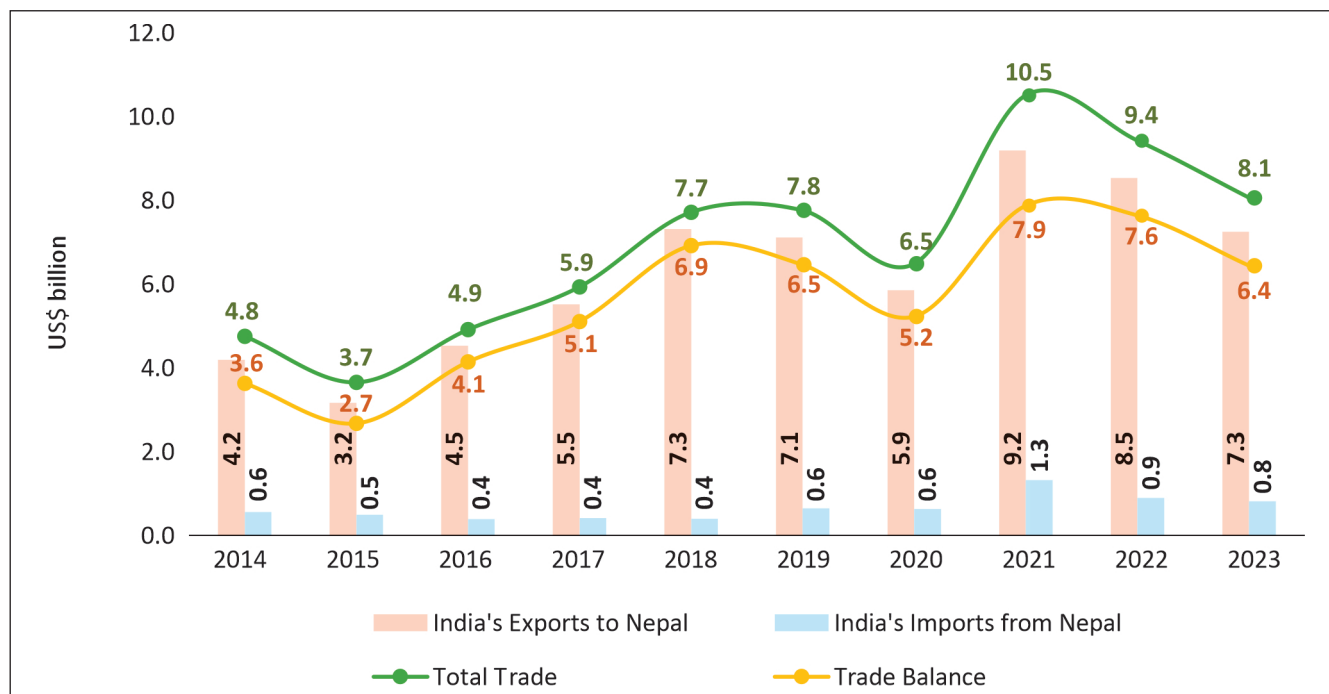
Since the China-Nepal borders pass through rugged terrain with limited road access, Nepal heavily relies on India for all the imports of goods. As Nepal's largest trade partner and primary source of foreign investments, India also facilitates nearly all of Nepal's third-country trade. India accounts for approximately two-thirds of Nepal's merchandise trade, a third of its service trade, and a third of foreign direct investment. It also supplies nearly all of Nepal's petroleum and plays a crucial role in inward remittances from workers, pensioners, and professionals in India.

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<sup>5</sup> SAARC stands for South Asian Association for Regional Cooperation and is an intergovernmental organization for the development of economic and regional integration.

Bilateral trade between India and Nepal has grown from US\$ 4.8 billion in 2014 to US\$ 8.1 billion in 2023, reflecting an average annual growth rate of 9.3%. While imports have generally shown an upward trend, exports have experienced contractions in certain years, particularly in 2015 and 2020. The trade balance has been in India's favour with trade surplus increasing from US\$ 3.6 billion in 2014 to US\$ 6.4 billion in 2023.

**Chart 3.1: Bilateral Trade between India and Nepal, 2014-2023**



Source: ITC Trade Map and India Exim Bank Research

## India's Merchandise Exports to Nepal

In 2023, Nepal ranked as the 17<sup>th</sup> largest export destination for India, accounting for 1.7% of India's total exports. Nepal was the 2<sup>nd</sup> largest export destination for India among the SAARC countries accounting for 29.6% of India's exports to the region in 2023.

India's export basket to Nepal remains fairly diversified, with mineral fuels and oils making up 32% of total exports in 2023. Other significant export categories include iron and steel (accounting for 11.8% of total exports), machinery and mechanical appliances (5.2%), and cereals (5%). India continues to be Nepal's largest trading partner, supplying 69.8% of Nepal's total global imports (**Table 3.1**).

**Table 3.1: India's Major Export Commodities to Nepal (US\$ million)**

HS Code	Products	2014	2019	2022	2023	Share in 2023 (%)	Share of India in Nepal's Global Imports in 2023 (%)
	<b>All products</b>	<b>4193.4</b>	<b>7108.9</b>	<b>8531.4</b>	<b>7250.3</b>	<b>100.0</b>	<b>69.8</b>
27	Mineral fuels and oils	1237.4	1854.8	2992.3	2320.2	32.0	22.3
72	Iron and steel	498.0	941.0	981.4	852.7	11.8	8.2
84	Machinery and mechanical appliances	216.3	558.1	480.8	379.3	5.2	3.7
10	Cereals	259.8	377.5	483.0	361.7	5.0	3.5
87	Vehicles other than railway	383.9	663.8	463.6	336.1	4.6	3.2
85	Electrical machinery and equipment	112.0	294.5	317.2	323.2	4.5	3.1
39	Plastics and articles	154.4	229.9	292.4	249.9	3.4	2.4
30	Pharmaceutical products	142.6	212.0	228.5	222.2	3.1	2.1
23	Residues and waste from the food industries	68.8	94.5	98.7	148.6	2.0	1.4
73	Articles of iron or steel	59.9	128.1	149.2	113.2	1.6	1.1

Source: ITC Trade Map and India Exim Bank Research

### India's Merchandise Imports from Nepal

Nepal was India's 66<sup>th</sup> largest import source accounting for a share of 0.1% in India's global imports and 6.5% share in India's imports from the SAARC countries. Nepal was the 3<sup>rd</sup> largest import source for India among the SAARC countries in 2023. India on the other hand, was Nepal's largest export destination with 65.7% of Nepal's total commodities exported to India in 2023. Coffee, tea and spices and iron and steel accounted for major imported commodities each accounting for 12.7% of India's total imports from Nepal. Other major commodity included animal and vegetable oil (10.3%), man-made staple fibres (9.8%) and aircraft, and its parts (7.9%) among others (Table 3.2).

**Table 3.2: India's Major Import Commodities from Nepal (US\$ million)**

HS Code	Products	2014	2019	2022	2023	Share in 2023 (%)	Share of India in Nepal's Global Exports in 2023 (%)
	<b>All products</b>	<b>560.7</b>	<b>649.4</b>	<b>894.0</b>	<b>811.5</b>	<b>100.0</b>	<b>65.7</b>
09	Coffee, tea and spices	42.1	47.7	85.2	103.4	12.7	8.4
72	Iron and steel	60.7	30.3	53.2	103.3	12.7	8.4
15	Animal, vegetable fats and oils	1.2	251.9	345.6	83.3	10.3	6.7
55	Man-made staple fibres	49.2	60.4	76.6	79.7	9.8	6.5
88	Aircraft, spacecraft, and parts	0.0	0.0	0.1	63.9	7.9	5.2
22	Beverages, spirits and vinegar	92.7	40.9	52.0	63.3	7.8	5.1
44	Wood and articles of wood	1.1	0.2	15.3	50.7	6.2	4.1
53	Other vegetable textile fibre	12.4	33.9	44.3	38.3	4.7	3.1
39	Plastics and articles thereof	69.5	42.4	33.7	34.2	4.2	2.8
23	Residues and waste from the food industries	12.4	19.1	25.1	25.7	3.2	2.1

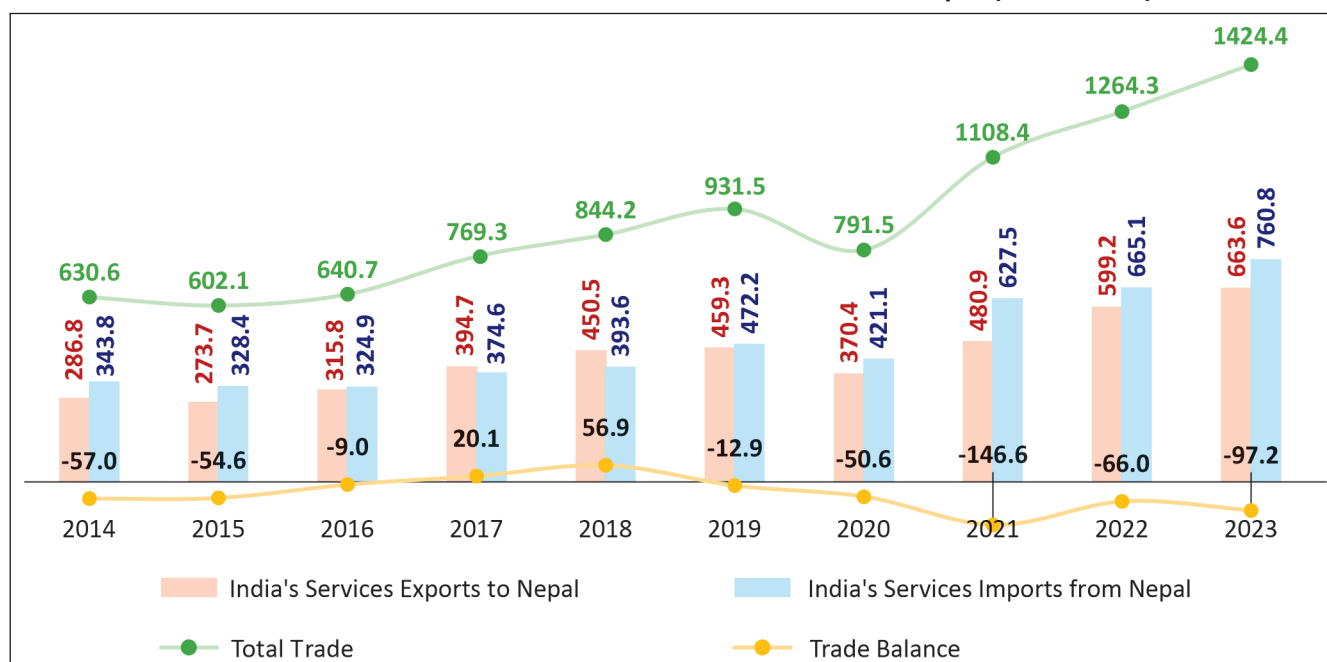
Source: ITC Trade Map and India Exim Bank Research

## Bilateral Services Trade between India and Nepal

Bilateral services trade between India and Nepal has been obtained from the OECD-WTO Balanced Trade in Services (BaTIS) dataset<sup>6</sup>.

India's trade with Nepal has primarily focused on merchandise, but the trade in services has seen steady growth over the past decade. From 2014 to 2023, services trade between the two countries grew from US\$ 630.6 million to US\$ 1.4 billion, reflecting an average annual growth rate (AAGR) of 10.4% (**Chart 3.2**). Exports from India to Nepal increased at an AAGR of 10.8%, rising from US\$ 286.8 million in 2014 to US\$ 663.6 million in 2023. At the same time, imports grew at a slightly slower pace of 10.3% annually. India's services trade balance with Nepal has largely remained negative, with India witnessing a surplus in services trade only during 2017 and 2018. Overall, India's bilateral trade in services with Nepal constituted less than 1% of India's trade in services with the rest of the world.

**Chart 3.2: Bilateral Trade in Services between India and Nepal (US\$ million)**



Source: WTO - OECD Balanced International Trade in Services (BaTIS) and India Exim Bank Research

## India's Services Exports to Nepal

**Table 3.3** below provides the overall trend in India-Nepal services exports. In 2023, India exported services worth US\$ 663.6 million to Nepal, with travel accounting for the largest share at 81.7% of total services exports. Within the travel sector, personal travel consistently made up a larger proportion compared to

<sup>6</sup> BaTIS contains annual bilateral data covering 202 reporters and partners, broken down by the 12 main EBOPS2010 (BPM6) categories. BaTIS has been developed by the OECD and WTO.

BaTIS is considered to be a relatively complete and consistent database for bilateral services trade data. At present, only about 63% of world trade in services is bilaterally specified, and the percentage is even lower for the individual service categories. The OECD-WTO methodology leverages all available official statistics and combines them with estimations and adjustments to provide users with a complete matrix covering virtually all economies in the world. BaTIS is balanced. To resolve the asymmetries between reported and mirror flows, exports and imports are reconciled by calculating a symmetry-index weighted average between the two, following a similar approach to that developed for international merchandise trade statistics.

business travel over the years. Other commercial services ranked second, contributing US\$ 65.1 million, or 9.8% of the total export value. Transport services followed, making up 8.5%, while other business services accounted for 7% of the total services exports in the same year.

**Table 3.3: India's Major Services Export to Nepal (US\$ million)**

Product/ Sector	2014	2019	2022	2023	% Share in 2023
<b>Total Services Exports to Nepal</b>	<b>286.8</b>	<b>459.3</b>	<b>599.2</b>	<b>663.6</b>	<b>100.0</b>
Government goods and services	0.2	0.3	0.3	0.3	0.0
Commercial services	286.6	459.1	598.8	663.3	100.0
Transport	28.9	43.2	80.5	56.2	8.5
Travel	220.0	355.3	445.1	541.8	81.7
Other Commercial Services	37.7	60.4	73.0	65.1	9.8
Construction	1.6	2.9	5.1	4.6	0.7
Insurance and pension services	1.5	2.4	4.2	3.0	0.5
Financial services	0.1	0.1	0.3	0.3	0.0
Charges for the use of intellectual property	0.0	0.0	0.0	0.0	0.0
Telecommunications, computer, and information services	11.5	16.3	8.7	10.3	1.5
Telecommunications services	1.4	1.3	0.2	0.4	0.1
Computer services	10.1	14.9	8.5	9.8	1.5
Other business services	22.9	38.6	54.4	46.7	7.0
Research and development services	0.9	4.8	10.6	8.8	1.3
Professional and management consulting services	3.1	5.5	15.2	14.0	2.1
Technical, trade-related, and other business services	18.8	28.3	28.5	23.8	3.6
Personal, cultural, and recreational services	0.1	0.1	0.3	0.3	0.0

Source: OECD Balanced International Trade in Services (BaTIS) and India Exim Bank Research

## India's Services Imports from Nepal

An analysis of India's service imports from Nepal is provided in **Table 3.4**. Service imports have grown significantly from US\$ 343.8 million in 2014 to US\$ 760.8 million in 2023, more than doubling over the period. This indicates increasing economic ties between India and Nepal in the service sector. Commercial services dominate India's imports, consistently accounting for over 99% of the total value. Transport and travel services together contribute 84.5% of the total services imports reflecting increasing tourism and travel between India and Nepal. Other commercial services accounted for more than 14% of the total imports, followed by other business services, particularly professional and management consulting services which indicates a rising demand for specialized expertise from Nepal in India.

**Table 3.4: India's Major Services Import from Nepal (US\$ million)**

Product/ Sector	2014	2019	2022	2023	% Share in 2023
<b>Total Services Imports from Nepal</b>	<b>343.8</b>	<b>472.2</b>	<b>665.1</b>	<b>760.8</b>	<b>100.0</b>
Government goods and services	13.5	4.5	5.9	7.1	0.9
Commercial services	330.3	467.7	659.2	753.8	99.1
Transport	95.4	92.0	194.7	168.1	22.1
Travel	199.2	328.7	354.9	474.4	62.4
Other Commercial Services	35.7	47.1	109.5	111.2	14.6
Construction	0.0	0.0	0.0	0.0	0.0
Insurance and pension services	15.0	11.1	23.7	25.8	3.4
Financial services	0.1	0.1	0.2	0.2	0.0
Charges for the use of intellectual property	0.0	0.1	0.1	0.2	0.0
Telecommunications, computer, and information services	9.2	11.3	24.7	22.3	2.9
Telecommunications services	0.7	0.2	0.4	0.4	0.1
Computer services	7.4	10.3	22.6	20.2	2.7
Other business services	11.0	23.6	59.3	60.8	8.0
Research and development services	0.2	0.4	1.2	1.2	0.2
Professional and management consulting services	9.7	21.6	51.7	53.0	7.0
Technical, trade-related, and other business services	1.1	1.6	6.4	6.6	0.9
Personal, cultural, and recreational services	0.4	0.8	1.5	1.9	0.2

Source: OECD Balanced International Trade in Services (BaTIS) and India Exim Bank Research



# Trends in Nepal's Foreign Direct Investments and Investment Relations with India

Foreign Direct Investment (FDI) has the potential to be a key driver of economic growth and development for recipient countries. By facilitating the infusion of capital, FDI can create new job opportunities, enhance human capital, and foster the growth of industries. The inflow of FDI is crucial for expanding exports and contributing to economic diversification, which ultimately spurs overall economic growth.

## *Inward FDI into Nepal*

Since 1980-81, Nepal has progressively emphasized foreign investment, with the government recognizing its crucial role in driving economic development. This is evident in the country's formulation of various policies and reforms aimed at attracting foreign direct investment (FDI). The Sixth Plan, introduced in 1980, marked the beginning of this push, followed by the promulgation of the Foreign Investment and Technology Transfer Act (1981), which has been revised over time to improve the investment climate.

More recently, Nepal introduced a series of legal and institutional frameworks to further stimulate FDI. These include the Foreign Investment Policy (2015), the Foreign Investment and Technology Transfer Act (2019), and the Public-Private Partnership and Investment Act (2019), which facilitate private-sector participation in development projects. Additionally, the Industrial Enterprises Act (2020) and the Nepal Rastra Bank Foreign Investment and Foreign Loan Management Bylaw (2021) (Third Amendment) have improved the regulatory environment for foreign investments<sup>7</sup>. Institutional reforms, such as the establishment of the One Stop Service Center, aim to simplify the process for foreign investors. Notably, the Automatic route for foreign investment in seven industrial sectors for investments up to NPR 500 million (US\$ 37.6 million)<sup>8</sup> and the waiver of the minimum threshold of NPR 20 million for foreign investments in the IT sector have been significant incentives. These developments are aimed at attracting capital and expertise to foster industrial growth, innovation, and job creation.

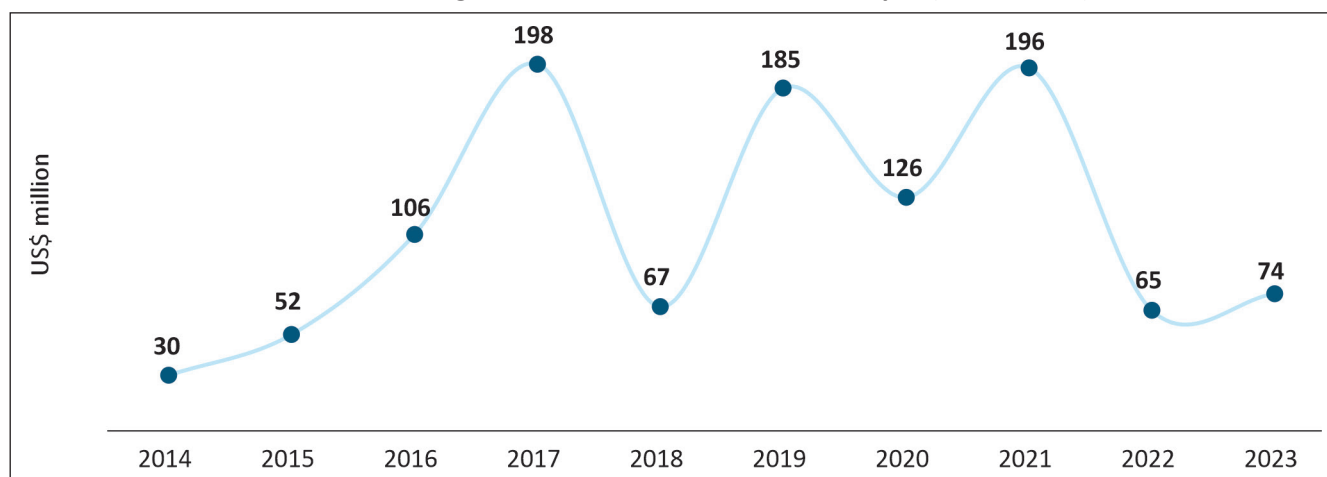
As per United Nations Conference on Trade and Development (UNCTAD Stat), Nepal's FDI inflows have had a tumultuous trend in the past decade. The total inflows rose from US\$ 30 million in 2014 to US\$ 74 million in 2023 (**Chart 4.1**). FDI in Nepal rapidly increased from US\$ 30 million in 2014 to a record high of US\$ 198 million in 2017, driven by Chinese investments in infrastructure, cement products and mining. The introduction of new policies contributed to improving the country's investment climate since the devastating 2015 earthquake. FDI

<sup>7</sup> Nepal Rastra Bank, Survey Report on Foreign Direct Investment in Nepal (2022/23) (August 2024)

<sup>8</sup> UNCTAD Investment Policy Hub

dipped in 2018 as a result of increased political uncertainty, infrastructural limitations like chronic shortages of electricity and weak policy implementation capabilities by the government. However, FDI in Nepal rose, recovering from a low of US\$ 67 million in 2018 to US\$ 185 million in 2019, driven by hydropower projects by Indian investors. In 2020, this amount plummeted down by 32% to US\$ 126 million, mostly because of the stall in tourism, one of the country's key industries. The decline in tourism had a significant effect on the economy through the industry's multiple linkages with other economic activities, including FDI inflows<sup>9</sup>. Despite a slight recovery in 2021, investments again dove in 2022 owing to burdensome procedures on profit repatriation and other regulations on external transactions reflecting Nepal's minimal amount of foreign direct investment and limited integration into the global financial system<sup>10</sup>.

**Chart 4.1: Foreign Direct Investment Inflow in Nepal (US\$ million)**



Source: UNCTADStat and India Exim Bank Research

To get a meaningful understanding on the trends in Nepal's overseas investments, this study has also analysed the data collated by the Financial Times through its online database tracking cross-border greenfield investment, viz. fDi Markets<sup>11</sup>. According to Financial Times' fDi Markets, during the period January 2014 to December 2023, Nepal received a total envisaged capital expenditure of US\$ 4.8 billion across 64 projects, with a total of 58 companies invested in the country (**Table 4.1**).

**Table 4.1: Envisaged FDI Inflows in Nepal, 2014-2023**

Year	Capital Expenditure (US\$ million)	Number of Projects	Number of Companies Invested
2014	538.2	4	4
2015	823.9	6	6
2016	105.8	3	3
2017	168.4	6	6
2018	332.4	9	9

<sup>9</sup> World Investment Report 2018 to 2024

<sup>10</sup> Fitch Country Ratings Report of Nepal, November 2024

<sup>11</sup> fDi Markets tracks cross-border investment in a new physical project or expansion of an existing investment which creates new jobs and capital investment. This data differs from official data on FDI flows as company can raise capital locally, phase their investment over a period and can channel their investment through different countries for tax efficiency.

Year	Capital Expenditure (US\$ million)	Number of Projects	Number of Companies Invested
2019	427.2	11	10
2020	303.1	5	5
2021	1231.6	5	3
2022	34.6	6	5
2023	798.2	9	9
<b>Total</b>	<b>4763.4</b>	<b>64</b>	<b>58</b>

Source: fDi Markets online database and India Exim Bank Research

As shown in **Table 4.2**, maximum envisaged FDI inflows were from China, accounting for 39.8% of total capital expenditure during the period January 2014 to December 2023. The US was the second largest investor with a share of 18.3%, followed by Singapore (13.1%), South Korea (11.4%) and India (8%). In terms of the total number of projects and number of companies invested, India ranked first with a total of 16 projects and companies respectively.

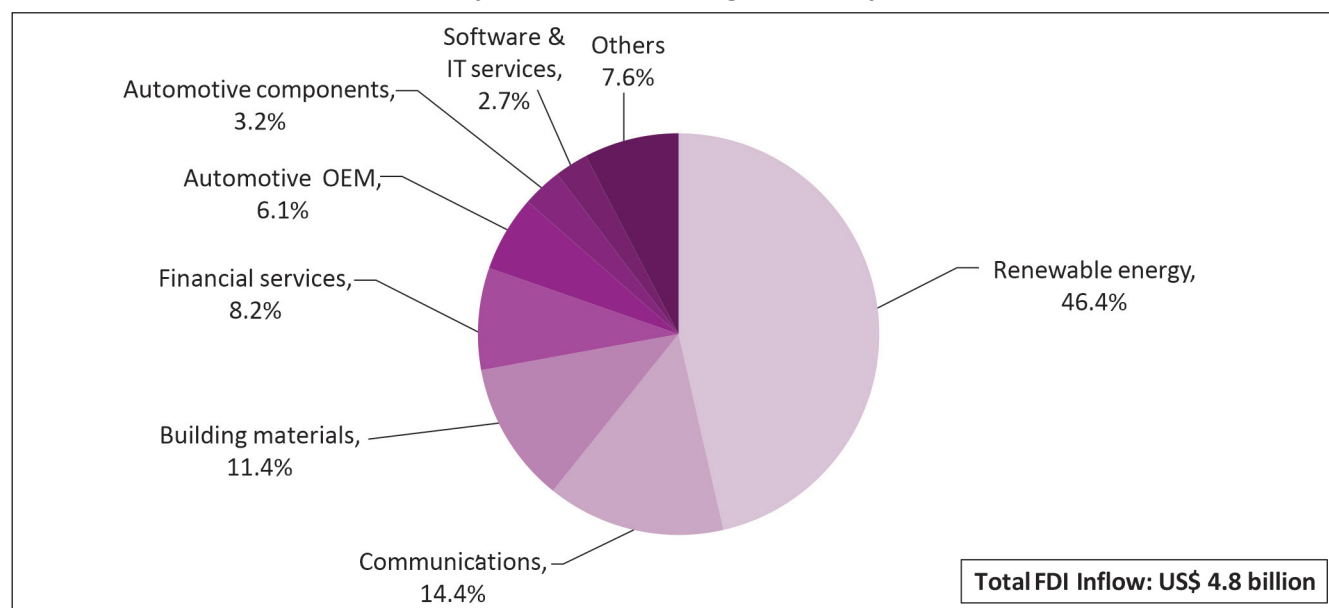
**Table 4.2: Major Investors in Nepal, 2014-2023**

Source Country	Capital Expenditure (US\$ million)	Number of Projects	Number of Companies Invested
China	1898.7	9	7
US	872.4	9	7
Singapore	624	2	2
South Korea	545.2	3	3
<b>India</b>	<b>381.0</b>	<b>16</b>	<b>16</b>
Australia	140.6	6	6
UK	93.6	3	3
UAE	68.7	3	3
Qatar	32.6	1	1
Denmark	29.3	2	2
<b>Total</b>	<b>4763.4</b>	<b>64</b>	<b>58</b>

Source: fDi Markets online database and India Exim Bank Research

Renewable energy sector has been the major recipient of envisaged capital expenditure in Nepal, with a value of US\$ 2.2 billion, accounting for 46.4% of the total envisaged capital expenditure received during the period January 2014 to December 2023 (**Chart 4.2**). This is followed by investments in communications (US\$ 684 million), building material (US\$ 541.1 million) and financial services (US\$ 391.3 million), among others.

**Chart 4.2: Major Sectors Attracting FDI in Nepal, 2014-2023**



Source: fDi Markets online database and India Exim Bank Research

Despite the significant strides Nepal has made in attracting foreign investment, several challenges remain that hinder the country's ability to fully capitalize on FDI opportunities. Addressing challenges such as political instability, restrictions on foreign banks, challenges in repatriating profits, lack of clarity in the currency exchange policies, minimum foreign investment threshold, prohibition of FDI in certain sectors, and limited infrastructure facilities, could help Nepal realize its full potential as a favourable destination for foreign investment. Further, simplifying Nepal's legal and regulatory framework, which is often misaligned with international standards, especially in terms of taxation and compliance and creating a favourable business environment, could also auger well for the country in attracting global investments into the country.

## India's Investments in Nepal

India is one of Nepal's largest trading partners and a significant source of foreign direct investment (FDI). The two countries collaborate in key sectors such as energy, infrastructure, manufacturing, and agriculture, with India investing in various development projects across Nepal. This economic cooperation is supported by bilateral agreements and initiatives aimed at enhancing trade, connectivity, and economic growth, fostering a mutually beneficial partnership. Indian companies and investments have played a key role in boosting Nepal's economy by contributing to industrialization, employment generation, government revenue and export earnings.

According to Financial Times' fDi Markets database, from January 2014 to December 2023, the total envisaged capital investment of India in Nepal stood at a cumulative amount of US\$ 381 million (**Table 4.3**). Indian investments in Nepal have significantly increased from US\$ 6.3 million in 2014 to US\$ 26.9 million in 2023. The peak of this investment trend occurred in 2019, when it reached an impressive US\$ 127.1 million.

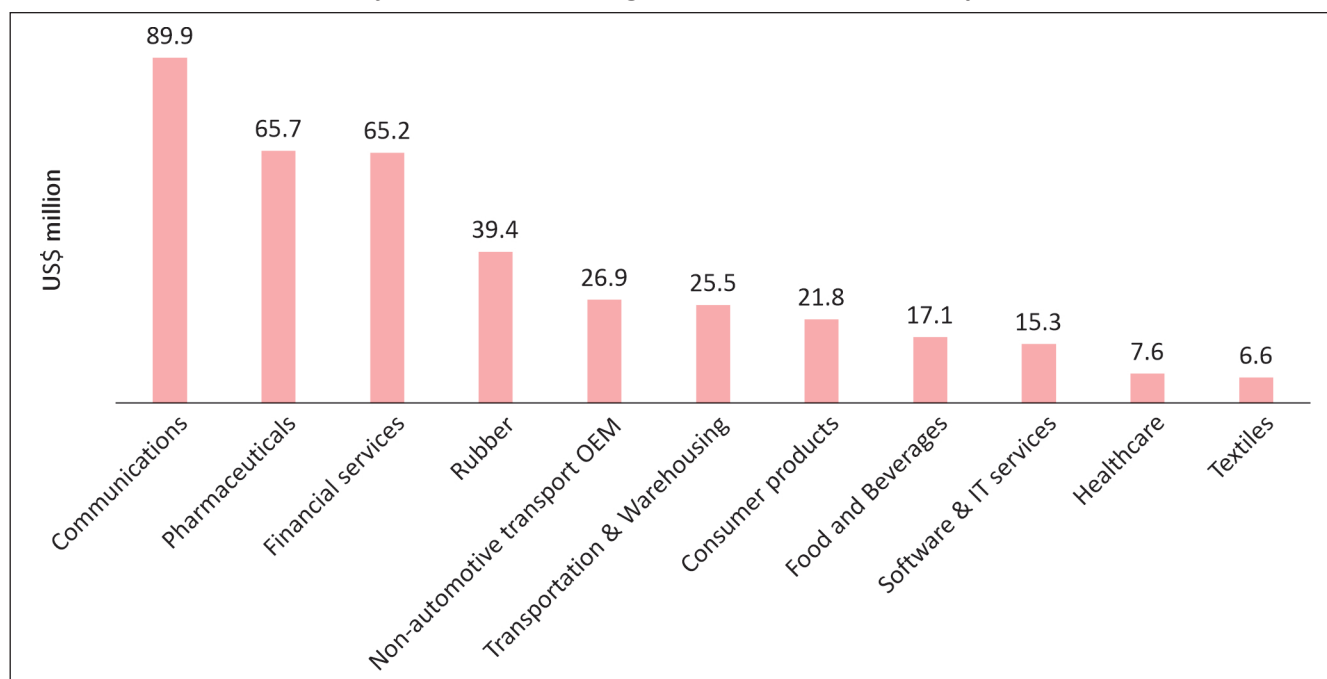
**Table 4.3: Indian Foreign Direct Investments in Nepal, 2014-2023**

Year	Capital Expenditure (US\$ million)	Number of Projects	Number of Companies Invested
2014	6.3	1	1
2015	6.4	1	1
2016	103.8	2	2
2017	49.6	2	2
2018	7.9	1	1
2019	127.1	4	4
2020	36.3	2	2
2022	16.6	2	2
2023	26.9	1	1
<b>Total</b>	<b>381</b>	<b>16</b>	<b>16</b>

Source: fDi Markets online database and India Exim Bank Research

As shown in **Chart 4.3**, in terms of capital investments during 2014-2023, the largest share has been in communications (23.6% of Indian investment in Nepal), pharmaceuticals (17.2%), and financial services (17.1%) among others.

**Chart 4.3: Major Sectors Attracting Indian Investments in Nepal, 2014-2023**



Source: fDi Markets online database and India Exim Bank Research

### ***Outward FDI from Nepal***

The Act Restricting Investment Abroad, 1964 imposes stringent controls on Nepali individuals and entities seeking to invest overseas. The Act prohibits Nepali individuals or entities from making any form of investment in a foreign country except in case an exemption is provided by the Nepal Government.

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According to UNCTAD<sup>12</sup>, the global landscape of outward foreign direct investment (OFDI) promotion, facilitation and regulation has undergone substantial changes since the early 2000s. Although there is a growing recognition that OFDI policies can provide global competitiveness to the domestic companies of a country and contribute to sustainable development in the host countries, however, it also presents potential risks, which has led several countries to adopt policies to regulate and restrict outward FDI. Historically, restrictions on OFDI were mainly observed in developing countries and related to balance-of-payments risks. Over time, the imposition of restrictions on OFDI has been increasingly driven by efforts to combat money laundering practices, such as the Financial Action Task Force (FATF) anti-money laundering policy framework.

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<sup>12</sup> Investment Policy Monitor, Outward FDI Policies (February 2024)



## Potential for Enhancing India's Exports to Nepal

Bilateral merchandise trade between India and Nepal exceeded US\$ 8 billion in 2023, making India Nepal's largest trading partner. The revised Transit Treaty, signed in June 2024, allows Nepal to use India's inland waterways for transit trade, improving trade logistics. India exports petroleum, iron and steel, machinery, cereals, and vehicles to Nepal, while Nepal exports edible oils, tea, coffee, spices, and synthetic yarn, among others to India. Cross-border connectivity projects, including rail links, roads, and Integrated Check Posts (ICPs), are being developed with Indian assistance to facilitate smoother trade and movement.

### Assessing Revealed Comparative Advantage of India's Exports

Analysing the key products where India has comparative advantage and mapping it with Nepal's import demand for these products are necessary to increase India's exports to Nepal. Quantification of comparative advantage helps in identification of products where exports from India have been performing well, as also those where success has been limited, although opportunities are significant.

Revealed Comparative Advantage (RCA) is a measure which has been used extensively to help assess a country's export potential/competitiveness. It helps in identifying categories of exports in which an economy has a comparative advantage by way of comparison of the country's trade scenario with the world trade scenario. It provides useful information about potential trade prospects with new partners. The basic assumption underlying the concept of revealed comparative advantage is that the trade profile reflects the inter-country differences in terms of relative costs as well as non-price aspects.

As per Balassa's (1965) measure, RCA index for country  $i$  for commodity  $j$  is:

$$RCA_{ij} = (x_{ji}/X_i) / (x_{jw}/X_w)$$

where,

$x_{ji}$ : Exports of Commodity 'j' from Country 'i'

$X_i$ : Total Exports from Country 'i'

$x_{jw}$ : Total Exports of Commodity 'j' from World

$X_w$ : Total Exports from World

The RCA index ranges from 0 to infinity, with 1 as the break-even point. An RCA value of less than 1 means that the product does not have a comparative advantage, while a value above 1 indicates that the product has a comparative advantage.

Since the RCA analysis is used in regard to one country's exports profile with reference to the world, the above formula of revealed comparative advantage has been modified to assess India's competitiveness in bilateral trade relations with Nepal.

$$RCA_{ijn} = (x_{ijn}/X_{in}) / (x_{wjn}/X_{wn})$$

where,

$x_{ijn}$ : India's Exports of Commodity 'j' to Nepal

$X_{in}$ : India's Total Exports to Nepal

$x_{wjn}$ : World's Exports of Commodity 'j' to Nepal

$X_{wn}$ : World Total Exports to Nepal

The Normalized Revealed Comparative Advantage (NRCA) index demonstrates the capability of revealing the extent of comparative advantage that a country has in a commodity with more precision and consistency. NRCA can be defined in the following manner.

$$NRCA_{ijn} = (RCA_{ijn} - 1) / (RCA_{ijn} + 1)$$

NRCA ranges from -1 to 1, with 0 as the breakeven point. That is, an NRCA value of less than 0 and greater than -1, means that the product has no export comparative advantage, while a value above 0 and less than 1, indicates that the product has a comparative advantage. The extent of comparative advantage/disadvantage can be gauged from the proximity of the NRCA values to the extreme data points, viz. +1 and -1.

The export competitiveness of India has been mapped with respect to Nepal's demand. This has been undertaken with a view to outline a market specific approach for exporters. An overarching analysis has been attempted to identify products from the industries for which India has existing export capabilities to Nepal. These products are the potential export growth drivers from India to Nepal and could suitably be targeted. The section also attempts to identify the products where India could focus on, to realize potentially higher values of exports to Nepal, especially when considering that India already possesses manufacturing capabilities for these products. The objective of the exercise is to construct a product market matrix for products in demand in Nepal, so that necessary actions and policies can be formulated in the direction to enhance exports of these potential products from India to Nepal.

Following are the considerations in the analysis:

- **Time Period:** The time period considered for the analysis is 2020-2023.
- **Product Limit:** Only those products at 6-digit HS code level with a minimum export value of US\$ 0.1 million from India to Nepal is considered in the analysis.

- **Parameters in Consideration:** The analysis in this section considers two major determinants of India's performance in Nepal, namely, the **NRCA for products**, and **Average Annual Growth Rate (AAGR)** of world exports to Nepal.

On the basis of these three considerations, a four-quadrant matrix is prepared for product identification. The four quadrants imply the following:

**Product Champions (Product Import AAGR of Nepal > World Import AAGR of Nepal; Positive NRCA):** These products have the maximum potential, as Nepal's import demand for these products has shown robust AAGR over the period 2020-23, while India's exports of these products to Nepal are also competitive, reflected in positive NRCA values for such products. These are the products with maximum export potential to Nepal and India needs to further expand its exports of these products in order to take advantage of its competitive position and achieve a greater market share in Nepal.

**Underachievers (Product Import AAGR of Nepal > World Import AAGR of Nepal; Negative NRCA):** India does not have competitiveness in these products although their import demand has grown in Nepal significantly over the period under consideration. India can strive towards building capacities and capabilities in these identified products. These are the products in which India can diversify in the medium to long term to continue being a strategic trade partner to Nepal and further expand its bilateral ties with the country.

**Winners in Declining Sectors (Product Import AAGR of Nepal < World Import AAGR of Nepal; Positive NRCA):** India has competitiveness in these products, even though Nepal's import AAGR for these products has been declining. These products may not have much demand in the future, and hence, scarce resources from these sectors could be diverted to other sectors where demand expectations are positive.

**Lagging in Declining Sectors (Product Import AAGR of Nepal < World Import AAGR of Nepal; Negative NRCA):** India does not have competitiveness in these products, and these sectors have also registered weak import demand in Nepal during the period under consideration.

## Product Identification Based on Competitiveness

To identify the products based on their export competitiveness in Nepal, a four-quadrant analysis has been undertaken based on the HS Code classifications at 6-digit level, whilst calculating their NRCA and mapping them against the AAGR of global imports of Nepal for all products. The quadrants are drawn by comparing the overall AAGR of global imports of Nepal for all products during 2020-2023 (which was 0.9%), to the NRCA of India's exports to Nepal during the same period. This exercise aims to identify products whose imports in Nepal over the period 2020-2023 have performed better than the overall average of Nepal for all products during this period, implying that the share of such products in Nepal's import basket has witnessed an increase, a reflection of their rising demand and dynamism. At 6-digit HS Code, with minimum exports of US\$ 0.1 million from India to Nepal, 2337 products have been identified with the total exports from India to Nepal, amounting to US\$ 7.2 billion (99.7% of India's total exports to Nepal in 2023) while global imports by Nepal for the corresponding products stood at US\$ 9.5 billion in 2023 (91.8% of Nepal's global imports in 2023) (**Chart 5.1**).

**Chart 5.1: Product Identification for Exports from India to Nepal (2023)**



Source: India Exim Bank's Estimates based on ITC Trade Map

Out of the 2337 items at the HS 6-digit level, 1109 items belonged to the category of the product champions. The combined exports of these items from India to Nepal were US\$ 5.1 billion in 2023, representing approximately 69.8% of India's exports to Nepal in 2023. Major product champions are provided in **Table 5.1**. These products are low hanging fruits for India and can be targeted in the short to medium term. Nepal's global imports of these product champions amounted to US\$ 5.2 billion in 2023, implying that there remains scope for continuing to tap Nepal's market for these products.

**Table 5.1: List of Major Product Champions from India to Nepal**

HS Code	Product	India's Exports to Nepal (US\$ mn)	Share in India's Total Exports to Nepal (%)	Global Imports of Nepal (US\$ mn)	Share in Global Imports of Nepal (%)
271019	Medium oils and preparations, of petroleum or bituminous minerals	1194.5	16.5	1203.4	11.5
271012	Light oils and preparations, of petroleum or bituminous minerals which >= 90% by volume	459.8	6.3	460.0	4.4
271119	Gaseous hydrocarbons, liquefied	383.4	5.3	383.4	3.7
720310	Ferrous products obtained by direct reduction of iron ore, in lumps, pellets or similar forms	308.9	4.3	308.9	3.0
720839	Flat-rolled products of iron or non-alloy steel, of a width of >= 600 mm, in coils, simply hot-rolled, not clad, plated or coated, of a thickness of < 3 mm, not pickled, without patterns in relief	177.6	2.5	202.9	1.7
300490	Medicaments consisting of mixed or unmixed products for therapeutic or prophylactic purposes, put up in measured doses "incl. those for transdermal administration" or in forms or packings for retail sale	142.1	2.0	147.0	1.4

HS Code	Product	India's Exports to Nepal (US\$ mn)	Share in India's Total Exports to Nepal (%)	Global Imports of Nepal (US\$ mn)	Share in Global Imports of Nepal (%)
100610	Rice in the husk, "paddy" or rough	120.7	1.7	121.1	1.2
230400	Oilcake and other solid residues, whether or not ground or in the form of pellets, resulting from the extraction of soya-bean oil	104.6	1.4	111.4	1.0
271600	Electrical energy	64.4	0.9	64.4	0.6
871410	Parts and accessories of motorcycles, incl. mopeds, n.e.s.	54.3	0.7	55.7	0.5
100199	Wheat and meslin	47.6	0.7	47.6	0.5
854460	Electric conductors, for a voltage > 1.000 V, insulated, n.e.s.	38.9	0.5	39.6	0.4
760511	Wire of non-alloy aluminium, with a maximum cross-sectional dimension of > 7 mm	36.5	0.5	36.5	0.4
550320	Staple fibres of polyesters, not carded, combed or otherwise processed for spinning	36.1	0.5	38.3	0.3
401120	New pneumatic tyres, of rubber, of a kind used for buses and lorries	35.0	0.5	37.2	0.3

Source: ITC Trade Map and India Exim Bank Research

The total number of products in growing in declining markets category is 409, with India's exports amounting to US\$ 1.4 billion and constitute a share of 19.8% of India's exports to Nepal in 2023. These are the product items in which India has competitive advantage and has attained a significant share in Nepal's import basket, however, Nepal's import demand for these products has been falling in the last four years (**Table 5.2**). India needs to diversify away from this segment of products and move towards the Product Champions and the Underachievers segment.

**Table 5.2: List of Major Products Under Growing in Declining Markets Category from India to Nepal**

HS Code	Product	India's Exports to Nepal (US\$ mn)	Share in India's Total Exports to Nepal (%)	Global Imports of Nepal (US\$ mn)	Share in Global Imports of Nepal (%)
720719	Semi-finished products of iron or non-alloy steel containing, by weight, < 0.25% of carbon	133.5	1.8	133.5	1.3
270119	Coal, whether or not pulverised, non-agglomerated	105.1	1.4	105.1	1.0
100590	Maize	96.6	1.3	100.7	0.9
721391	Bars and rods, hot-rolled, in irregularly wound coils, of iron or non-alloy steel, of circular cross-section measuring < 14 mm in diameter	93.5	1.3	93.5	0.9
100630	Semi-milled or wholly milled rice, whether or not polished or glazed	85.8	1.2	86.0	0.8
871120	Motorcycles, incl. mopeds, with reciprocating internal combustion piston engine of a cylinder capacity > 50 cm <sup>3</sup> but <= 250 cm <sup>3</sup>	68.4	0.9	68.6	0.7

HS Code	Product	India's Exports to Nepal (US\$ mn)	Share in India's Total Exports to Nepal (%)	Global Imports of Nepal (US\$ mn)	Share in Global Imports of Nepal (%)
271320	Petroleum bitumen	60.2	0.8	60.5	0.6
790111	Unwrought zinc, not alloyed, containing by weight >= 99,99% of zinc	34.8	0.5	36.5	0.3
390210	Polypropylene, in primary forms	34.5	0.5	36.1	0.3
070190	Fresh or chilled potatoes	34.0	0.5	34.0	0.3
390120	Polyethylene with a specific gravity of >= 0,94, in primary forms	30.4	0.4	35.8	0.3
870899	Parts and accessories, for tractors, motor vehicles for the transport of ten or more persons, motor cars and other motor vehicles principally designed for the transport of persons, motor vehicles for the transport of goods and special purpose motor vehicles	29.6	0.4	33.7	0.3
230990	Preparations of a kind used in animal feeding	23.2	0.3	30.8	0.2
240120	Tobacco, partly or wholly stemmed or stripped, otherwise unmanufactured	22.4	0.3	22.4	0.2
841821	Household refrigerators, compression-type	19.4	0.3	20.5	0.2

Source: ITC Trade Map and India Exim Bank Research

The product category of underachievers comprised 627 items, with India's exports of these products amounting to US\$ 591 million to Nepal. These products constitute a share of 8.2% in India's total exports to Nepal. These are the product items in which import demand in Nepal's market are rising, but exports from India are currently not competitive (**Table 5.3**). Nepal's imports of these products stood at US\$ 2.4 billion in 2023, presenting significant opportunities for exporters. There is a need for capacity creation in these product categories, through an appropriate incentive framework for attracting investments into the country.

**Table 5.3: List of Major Underachievers from India to Nepal**

HS Code	Product	India's Exports to Nepal (US\$ mn)	Share in India's Total Exports to Nepal (%)	Global Imports of Nepal (US\$ mn)	Share in Global Imports of Nepal (%)
851713	Smartphones for wireless networks	63.0	0.9	192.4	0.6
870380	Motor cars and other motor vehicles principally designed for the transport of <10 persons, incl. station wagons and racing cars, with only electric motor for propulsion	53.3	0.7	151.5	0.5
310210	Urea, whether or not in aqueous solution	37.7	0.5	56.9	0.4
740811	Wire of refined copper, with a maximum cross-sectional dimension of > 6 mm	18.2	0.3	28.5	0.2
853720	Boards, cabinets and similar combinations of apparatus for electric control or the distribution of electricity, for a voltage > 1.000 V	15.6	0.2	29.4	0.1

HS Code	Product	India's Exports to Nepal (US\$ mn)	Share in India's Total Exports to Nepal (%)	Global Imports of Nepal (US\$ mn)	Share in Global Imports of Nepal (%)
853710	Boards, cabinets and similar combinations of apparatus for electric control or the distribution of electricity, for a voltage <= 1.000 V	12.9	0.2	35.1	0.1
850423	Liquid dielectric transformers, having a power handling capacity > 10.000 kVA	11.9	0.2	19.5	0.1
841090	Parts of hydraulic turbines and water wheels incl. regulators	9.9	0.1	20.8	0.1
691010	Ceramic sinks, washbasins, washbasin pedestals, and similar sanitary fixtures of porcelain or china	9.3	0.1	14.9	0.1
480257	Uncoated paper and paperboard, of a kind used for writing, printing or other graphic purposes, and non-perforated punchcards and punch-tape paper, in square or rectangular sheets with one side > 435 mm or with one side <= 435 mm and the other side > 297 mm in the unfolded state	9.1	0.1	14.7	0.1
300241	Vaccines for human medicine	8.8	0.1	79.1	0.1
480256	Uncoated paper and paperboard, of a kind used for writing, printing or other graphic purposes, and non-perforated punchcards and punch-tape paper, in square or rectangular sheets with one side <= 435 mm and the other side <= 297 mm in the unfolded state	7.5	0.1	13.0	0.1
330290	Mixtures of odoriferous substances and mixtures, incl. alcoholic solutions	6.3	0.1	9.1	0.1
071340	Dried, shelled lentils	6.3	0.1	55.3	0.1
540752	Woven fabrics of yarn containing >= 85% by weight of textured polyester filaments	6.0	0.1	28.6	0.1

Source: ITC Trade Map and India Exim Bank Research

Exports from India to Nepal under lagging in declining market category stood at US\$ 144.6 million comprising 192 products and 2% of India's total exports to Nepal in 2023. The corresponding global imports of Nepal stood at US\$ 395.2 million. The considerable range of exports under the category of declining sectors, which include among others, food preparations not elsewhere specified (HS 210690), instruments and appliances used in medical or surgical procedure not elsewhere specified (HS 901890), polyethylene with a specific gravity of < 0.94, in primary forms (HS 390110), Air conditioning machines designed to be fixed to a window, wall, ceiling or floor, self-contained or "split-system" (HS 841510), among others, highlight the need for diversification to other sectors as well as industries which have greater scope for exports in the future. If the scarce resources are not diverted, then excess of supply to these sectors facing limited demand in Nepal, would result in further fall in their prices in the future. Thus, a shift needs to be made from the declining sectors to the product champions in the short run and underachievers in the medium to the long run, to make efficient utilization of resources and further enhance exports from India to Nepal.



# Activities of Export-Import Bank of India in Nepal

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The Export-Import Bank of India (India Exim Bank) was set up under an Act of Parliament in 1981 and commenced operations in 1982. The Bank was set up for providing financial assistance to exporters and importers, and for functioning as the principal financial institution for coordinating the working of institutions engaged in financing export and import of goods and services with a view to promoting the country's international trade. In its endeavour to promote India's international trade, India Exim Bank's vision has evolved from financing, facilitating, and promoting trade and investments, to a conscious and systematic effort at creating export capabilities. India Exim Bank seeks to develop commercially viable business relationships with externally oriented companies. In line with the Government of India's "Neighbourhood First Policy", India Exim Bank has supported various projects and activities in the neighbouring countries in the South Asia region. India Exim Bank's commitment towards building relationships with the countries in the neighbourhood is reflected in the various activities and programmes, which India Exim Bank has set in place. India Exim Bank plays a critical role and is committed towards supporting GOI's initiatives in promoting strategic partnerships with countries in different regions and especially those in Asia. This is achieved through continuous engagement with partner countries at bilateral, regional and multilateral levels, and financing and supporting of projects of national importance, thereby strengthening India's role as a development partner in the region. With the proposed opening up of a representative office by Export-Import Bank of India in Nepal, bilateral economic engagement is also envisaged to get a boost in the coming years.

## Financial Products and Programmes of India Exim Bank in Nepal

### *Lines of Credit*

To promote India's trade and economic relations with developing countries, the Government of India launched the Indian Development and Economic Assistance Scheme (IDEAS) – with the objective of sharing India's development experience through capacity building and skill transfer, trade, and infrastructure development, by extending concessional Lines of Credit (LOCs) routed through India Exim Bank, to developing partner countries, towards creating socio-economic benefits in the partner country. As a part of its financing programmes, and to enhance bilateral trade and investment relations with partner countries, India Exim Bank extends several Lines of Credit (LOCs) to overseas sovereign governments or their nominated agencies, national or regional development banks, overseas financial institutions, commercial banks abroad, and other select overseas entities, to enable buyers in those countries to import developmental and infrastructure projects, equipment, goods and services from India, on medium and long term credit basis. These LOCs offer a risk-free financing option to the Indian exporting companies, while helping them penetrate new markets, enhance

their export volumes in the overseas market, and demonstrate project execution capabilities. The LOCs are aimed at financing and catalysing Indian exports by way of financing key projects of national importance to the borrower countries, such as agriculture and irrigation development, development of various small and medium enterprises, upgradation of factories, development of railways and related infrastructure, projects for transmission lines and substations, rehabilitation and improvement of water supply system, among others.

The LOC programme has gained considerable recognition abroad, as it enables the LOC recipient countries access to much needed large scale developmental and infrastructure projects, on concessional and deferred credit terms.

Government of India supported Lines of Credit (LOC) extended by the Export Import Bank of India to Government of Nepal focuses on execution of infrastructure development projects and post-earthquake reconstruction projects as prioritized by Government of Nepal as shown in **Table 6.1**.

**Table 6.1: India Exim Bank's Operational Lines of Credit in Nepal**

Sr. No	Key Sectors / Projects Covered	LOC Amount (US\$ mn)
1	Financing infrastructure projects such as highways, airports, bridges and irrigation projects	250.0
2	Road projects, rural electrification projects, power transmission projects and hydro power projects	100.0
3	Hydropower, Irrigation and Infrastructural development projects.	350.0
4	For post-earthquake reconstruction and other infrastructure projects	50.0

### ***Project Exports***

Under its Project Exports assistance, India Exim Bank extends both funded and non-funded facilities for overseas turnkey projects, civil construction, supplies as well as technical and consultancy service contracts across various sectors of the economy. India Exim Bank also supports existing or new projects, plants or processes that require additional assistance in processes such as international competitive bidding, including multilaterally funded projects in India. Such projects executed by assistance received from India Exim Bank, have contributed to the host country's developmental endeavours and have assisted in narrowing developmental gaps in such countries.

### ***Buyer's Credit under National Export Insurance Account (NEIA)***

In order to provide further impetus to project exports from India on medium or long-term basis, especially in the infrastructure sector, in April 2011, a financing product called Buyer's Credit under National Export Insurance Account (BC-NEIA) was introduced. Under this programme, India Exim Bank facilitates project exports from India by way of extending credit facility to overseas sovereign governments and government owned entities for import of goods and services from India on deferred credit terms. Indian exporters can obtain payment of eligible value from India Exim Bank, without recourse to them, against negotiation of shipping documents. NEIA is a Trust, set up by Ministry of Commerce and Industry, Government of India, and administered by ECGC. As of December 31, 2024, the positive list of 53 countries identified by ECGC Ltd. for which Indian exporters could avail Buyer's Credit under NEIA, includes Nepal as one of the eligible countries.

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### ***Overseas Investment Finance***

India Exim Bank supports Indian companies in their endeavour to globalise their operations, through overseas joint ventures (JVs) and wholly owned subsidiaries (WOS). Such support includes loans and guarantees, equity finance and in select cases direct participation in equity along with Indian promoters to set up such ventures overseas. These ventures serve to promote value addition, as also contribute to capacity building and capacity creation in host countries. As of December 31, 2024, India Exim Bank has supported 5 Indian companies for setting up JVs in Nepal, with a sanctioned amount of ₹ 994.9 crores across sectors including in power, capital goods, engineering goods, textiles and garments sectors.

### ***Trade Assistance Programme***

India Exim Bank introduced a new trade finance product - Trade Assistance Programme (TAP) in 2022 to address the widening trade finance gap. Under the aegis of TAP, Exim Bank provides support through credit enhancement to trade instrument(s), thereby enhancing the capacity of commercial banks / financial institutions to support cross-border trade transactions involving untapped markets, where trade lines are constrained or where the potential has not been harnessed, and transactions may not materialise in the absence of such support. As on February 28, 2025, India Exim Bank has supported 107 transactions of Risk Participation (RP), Standby Letter of Credit (SBLC) and Letter of Credit (LC) negotiation aggregating to more than US\$ 29 million in Nepal under the Trade Assistance Programme. The transactions executed are for supporting exports in the iron and steel sector, food and beverage industry, chemical industry, supply of electromechanical equipment for hydropower projects, supply of medical equipment and other materials for constructions, plant and machinery. Further, India Exim Bank under TAP has also supported longer tenor LCs in relation to hydropower projects in Nepal.

### ***Consultancy Assignments***

Over the past four decades, India Exim Bank has continuously evolved its programmes and services to meet the needs of its stakeholders. This experience of evolving as a principal financial institution in a developing country context has been found to be of particular relevance in other developing countries that seek to set up institutions and strengthen institutional structure for supporting international trade and investment. The Bank has leveraged its vast experience in export financing to render assistance to several institutions in the developing world through its well-knitted advisory and consultancy services backed by a strong in-house research team.



## Potential Areas of Cooperation and Recommendations

India and Nepal share strong economic ties, reinforced by historical and cultural linkages, open borders, and people-to-people connections. Under its “Neighbourhood First Policy”, India has prioritized enhancing economic, infrastructure, energy, and digital connectivity with Nepal, alongside capacity-building initiatives. India plays a key role in Nepal’s development through financial and technical assistance for large-scale infrastructure and connectivity projects, as well as community-focused social initiatives in education, healthcare, irrigation, and rural development.

Indian investments account for nearly 33% of Nepal’s FDI, with over 150 Indian companies operating in key sectors such as power, banking, insurance, education, pharmaceuticals, agricultural products and manufacturing. India and Nepal extend visa-free entry in their respective territories to each other’s nationals. The open-border arrangement enables movement of people, with 8 million Nepalese living and working in India and around 600,000 Indians residing in Nepal. Tourism is another key contributor, with Indians making up 30% of foreign tourists in Nepal. India’s development partnership has also been instrumental in Nepal’s human resource development, with India awarding 1,242 scholarships to Nepalese students and providing 484 training slots under the ITEC programme in 2023<sup>13</sup>.

Nepal has duty free access to the Indian market. However, India continues to face high tariff rates in Nepal and has duty free access (based on effectively applied tariff) to only 1.5% of Nepal’s total imports from India and more than 80% of imports face tariffs above 10% to tariffs going up to as high as 80%<sup>14</sup>.

### Enhancing Merchandise Trade Potential

India needs to expand its production and trade in products in which it has comparative advantage with Nepal with a cumulative export potential gap of US\$ 2 billion. The study has identified potential items of exports which could be targeted by Indian exporters with export potential gap under current trade regime for Product Champions around US\$ 190.6 million (difference between Nepal’s Global Imports and India’s Export to Nepal for the respective products). According to the analysis, in the short term, it is suggested to strengthen the existing products in the category of Product Champions to harness the full potential for the products which are already showing a robust growth in Nepal, where India’s exports also hold a comparative advantage. These are mainly petroleum oil (refined) and gaseous hydrocarbons, iron and steel, pharmaceutical products, rice,

<sup>13</sup> India Nepal Bilateral Relations, Ministry of External Affairs, Government of India, June 2024.

<sup>14</sup> Calculations based on data from World Integrated Trade Solution (WITS)

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oilcakes of soyabean oil, electrical energy, parts and accessories of motorcycles, wheat, electrical equipment, among others.

In the medium to long run, efforts and investments could be enhanced in the Underachievers category products to develop capacities in these products, which will help in meeting the demands of Nepal in a more competitive manner. These include smart phones, motor vehicles with electric motors, urea, wire of refined copper, board and cabinets for electric control, liquid dielectric transformer, parts of hydraulic turbine, ceramic sanitary fixtures, among others. The export gap in case of Underachievers is around US\$ 1777.3 million (difference between Nepal's Global Imports and India's Export to Nepal for the respective products) which could be targeted to increase India's exports to Nepal.

## Enhancing Bilateral Services Trade

According to the WTO, during the last decade, except in 2017 and 2018, India has maintained a services trade deficit with Nepal, with travel and transport services being dominant sectors. India's major services exports to Nepal comprised travel services contributing 81.7% of services exports followed by transport (8.5%), other business services (which include research and development services; professional and management consulting services and technical, trade-related, and other business services) at 7% and computer services (1.5%). Comparing India's share in Nepal's global services imports in 2023 shows that India accounts for 9.7% of Nepal's global transport services imports. India could gain further market share by expanding its sea transport services exports to Nepal. India is a major source for travel, mainly personal, accounting for 39.9% of Nepal's global travel services imports. Nepal accounted for 2.1% of total foreign tourist arrivals in India in 2023. Medical tourism has emerged as key contributors, to India's foreign tourist arrivals from developing economies with India being a global hub for affordable healthcare, drawing 6.9% of foreign visitors for medical purposes in 2023<sup>15</sup>. India's computer services accounted for 64.1% of Nepal's global computer services imports in 2023. India's strong IT services expertise can be utilised for software development, data analytics and IT support services for Nepalese businesses. In case of other business services, India accounted for 21.9% of Nepal's global business services imports in 2023. This remains another potential area for expansion by India to increase professional and management consulting services like legal and accounting as well as technical services like architectural and engineering services exports to Nepal.

## Cooperation in Energy Infrastructure

Nepal's electricity sector holds strategic importance for its economy. The country's vast hydropower potential presents a significant opportunity to generate revenue through electricity exports to the South Asian region. Nepal's industrial sector is poised for growth over the medium term, driven by significant expansion in electricity. Over the past decade, more than 9,500 MW of hydropower projects have been licensed for construction, with many already in progress, given their long gestation periods. The government's ambitious target of surpassing 11,700 MW of installed electricity capacity by 2029 is expected to be a key driver of industrial expansion<sup>16</sup>.

Nepal currently exports over 650 MW of electricity to India, with Indian enterprises actively involved in the development of major hydroelectric projects in Nepal, including Arun III (900 MW), Lower Arun (679

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<sup>15</sup> India Tourism Data Compendium 2024, Ministry of Tourism, Government of India.

<sup>16</sup> Nepal Development Update, World Bank, October 2024.

MW), Arun-4 (490 MW), West Seti and SR-6 (1200 MW), and Upper Karnali (900 MW)<sup>17</sup>. India and Nepal have also signed an agreement to facilitate the import of up to 10,000 MW of electricity from Nepal over the next decade. Additionally, India has agreed to support the export of electricity generated by Nepal to Bangladesh via Indian transmission infrastructure, further enhancing regional energy cooperation. To deepen collaboration in the energy sector, a Project Development Agreement was signed for the 669 MW Lower Arun Hydroelectric Project, to be developed by NHPC Ltd. The Prime Ministers of both countries jointly carried out the groundbreaking ceremony of 400 KV Gorakhpur-Butwal transmission line, during visit of the Prime Minister of Nepal to India in June 2023. The visit witnessed the signing of an MoU for the development of 480 MW Phukot-Karnali project by National Hydroelectric Power Corporation (NHPC) and Vidhyut Utpadan Company Limited (VUCL Ltd), Nepal and the Project Development Agreement for the development of 669 MW Lower Arun between Satluj Jal Vidyut Nigam (SJVN) and the Investment Board of Nepal (IBN). In addition, India announced its decision to facilitate the first trilateral power transaction from Nepal to Bangladesh through the Indian grid, with an export of up to 40 MW of electricity. This mechanism will enable Nepal to capitalise on its access to the real-time market, day ahead market and medium-term power agreements, and export up to 631 MW of electricity to India. Accordingly in October 2024, a tripartite power sales agreement between NTPC Vidyut Vyapar Nigam, Nepal Electricity Authority and Bangladesh Power Development Board was signed, and inauguration of the power transaction was carried out in November 2024<sup>18</sup>. Additionally, India agreed to provide financing for the Bheri Corridor, NijgadhInaruwa, Gandak-Nepalgunj transmission lines and associated substations under the Government of India's Lines of Credit. Furthering bilateral cooperation in energy infrastructure, India is supporting the second phase of the Motihari-Amlekhgunj Petroleum Pipeline Project, while an agreement has been reached for the construction of a new petroleum pipeline from Siliguri to Jhapa in eastern Nepal. These initiatives underscore the commitment of both nations to fostering regional energy security, trade facilitation, and infrastructure development.

## Cooperation in Transport and Connectivity

The tourism sector, which accounts for over 8% of Nepal's GDP and serves as one of the country's largest employment generators, is highly dependent on robust connectivity infrastructure. To support sustainable and affordable transport development - in the road sector, key priorities include ensuring all-weather connectivity roads, expanding lane capacity on high-density highways, and enhancing road safety. For aviation, Nepal aims to develop world-class airports to promote regional air travel, enhance disaster preparedness, and align with International Civil Aviation Organization (ICAO) safety and operational standards. In urban transportation, critical goals include increasing road density, establishing efficient mass transit systems, improving road safety, and integrating disaster management into transport planning<sup>19</sup>. India and Nepal have intensified their engagement in connectivity infrastructure and economic integration to strengthen bilateral ties. A series of cross-border connectivity projects like rail links, roads, Integrated Check Posts (ICPs) are under development with India's grant assistance.

There is steady progress in developing cross-border rail networks between India and Nepal, including the operationalisation of the Jayanagar-Bardibas cross-border section and Jogbani-Nepal Customs Yard rail section. Indian assistance has helped to construct 807 kms of the 1024 km-long East West Highway. Apart from this,

<sup>17</sup> Annual Report 2023-24, Ministry of External Affairs, Government of India.

<sup>18</sup> Inauguration of first trilateral power transaction – from Nepal to Bangladesh through the Indian Grid, PIB Press Release, November 2024.

<sup>19</sup> Nepal Infrastructure Sector Assessment, World Bank, 2019.

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the assistance offered by India has also helped construct the 6-lane major bridge across the Mechi River, connecting Kakarbhitta in Nepal to Panitanki in West Bengal. This bridge is a part of the Asian Highway-02 and provide critical connectivity to Nepal. The countries signed MOU to develop a cross border motorable bridge over the Mahakali River at Dharchula in Uttarakhand in September 2022<sup>20</sup>. In terms of cross-border connectivity, in June 2023, India and Nepal jointly inaugurated an Integrated Check Post (ICP) at the Nepalganj-Rupaidiha border, and another ICP at the Bhairahawa-Sunauli border. India and Nepal also signed an MoU for the construction of an ICP and dry port at Dodhara-Chadani with Indian assistance<sup>21</sup>.

High trade transaction costs remain a major constraint for India-Nepal trade due to limited connectivity and lack of quality infrastructure at border crossing points. Land Custom Stations (LCS) facilitates the cross-border movement of goods and passengers. Infrastructure facilities like cargo handling facilities and facilities required for digitization of trade processes are required for optimising the transaction time and cost for cross border trade. There are 27 trading points along the Indo-Nepal border. Most LCSs on India Nepal border, except few recently developed Integrated Check Posts (ICPs), are challenged by infrastructure deficit. Absence of storage facilities along with poor testing infrastructure has been hindering trade integration, especially the trade in perishable agricultural goods. Therefore, improving availability and quality of infrastructure at ICPs could help in further facilitating bilateral trade between the two neighbours<sup>22</sup>. India and Nepal could explore mutual areas of collaboration through technical and financial assistance for Nepal for implementation of trade facilitation measures.

## Banking and Financial Cooperation

Strengthening collaboration between Indian and Nepali financial institutions is important to facilitate bilateral trade and investment. As on December 31, 2024, 3 Indian Banks have established their presence in Nepal through joint venture or representative office. These are Nepal SBI Bank Ltd (subsidiary of SBI with 55.1% stake), Everest Bank Ltd (Joint Venture / Associate of Punjab National Bank with 20% share), and ICICI Bank Ltd (Representative Office in Kathmandu)<sup>23</sup>. Expanding the presence of Indian banks in Nepal could provide better financial services for businesses. India and Nepal have also successfully developed mechanisms for cross-border digital payments and fintech solutions. NPCI International Payments Limited (NIPL), the global arm of the National Payments Corporation of India (NPCI), has achieved a significant milestone by surpassing 100,000 cross-border Unified Payments Interface (UPI) Person-to-Merchant (P2M) transactions in Nepal. This achievement follows NIPL's collaboration with Fonepay, Nepal's largest payment network, to introduce cross-border UPI acceptance in March 2024<sup>24</sup>. UPI, India's widely used real-time mobile payment system, has streamlined transactions for Indian travellers in Nepal. Additionally, Nepali visitors to India can now make UPI payments through UPI One World, enabling seamless transactions at merchant locations by simply scanning QR codes. This advancement enhances digital payment connectivity between the two nations, making cross-border travel more convenient while fostering economic and cultural exchanges.

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<sup>20</sup> Annual Report 2023-24, Ministry of External Affairs, Government of India.

<sup>21</sup> Rejuvenating Nepal-India bilateral relations through digital connectivity, Arpan Gelal, Observer Research Foundation, April 26, 2024.

<sup>22</sup> Analysing India-Nepal Economic Integration: Status, Challenges and Way Forward, Pankaj Vashisht, RIS Discussion Paper Series, February 2024.

<sup>23</sup> RBI List of Presence of Indian Banks Abroad, December 31, 2024.

<sup>24</sup> NPCI Press Release (<https://www.npci.org.in/PDF/npci/press-releases/2024/NIPL-Press-Release-UPI-merchant-transactions-in-Nepal-surpass-100000-mark.pdf>)

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## Aerospace and Defence Cooperation

India's aerospace and defence cooperation endeavours with Nepal span across a wide range of areas. India has been assisting the Nepal in capacity building and supplying of equipment in the aerospace and defense sector. India has also exported advanced light helicopters to Nepal<sup>25</sup>.

## Healthcare

Nepal accounted for US\$ 16.1 million of India's medical devices and instruments exports (HS 9018) in 2023 accounting for 22.6% share in Nepal's global import of medical devices and emerged as the 2<sup>nd</sup> largest import source after Germany. India is the largest source of pharmaceutical products for Nepal accounting for 71.2% of Nepal's global imports. According to Statista, the hospitals market in Nepal is expected to reach a revenue of US\$ 933.8 million whereas the revenue in the medical technology<sup>26</sup> market in Nepal is expected to reach US\$ 214.5 million in 2025. Nepal is a tourist destination with immense natural resources creating a conducive environment for wellness tourism.

India has significant opportunities to invest in Nepal's healthcare infrastructure, fostering both economic and developmental benefits. Key areas include the establishment of multi-specialty hospitals, tertiary care centres, and diagnostic facilities. Indian pharmaceutical companies can set up manufacturing units to ensure a steady supply of affordable medicines and vaccines, enhancing Nepal's healthcare resilience. Opportunity also exists to tap the domestic requirement in syringes, needles, instruments and appliances. Investments in telemedicine and digital health services can improve access to medical care in remote areas, leveraging India's expertise in health tech and AI-driven diagnostics. Additionally, collaborations in medical education, training programs, and skill development can strengthen Nepal's healthcare workforce. Through strategic investments and policy collaboration, India can play a crucial role in strengthening Nepal's healthcare system while deepening bilateral ties.

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<sup>25</sup> Ministry of Defence, Indian Defence Goes Global,2020. (<https://www.ddpmod.gov.in/coffee-table-book>)

<sup>26</sup> The medical technology market covers devices and products used for prevention, diagnosis, and treatment of diseases. Some examples of medical technology products are, among others, pacemakers, imaging instruments, dialysis machines, and implants.

## **About India Exim Bank's Working Paper Series**

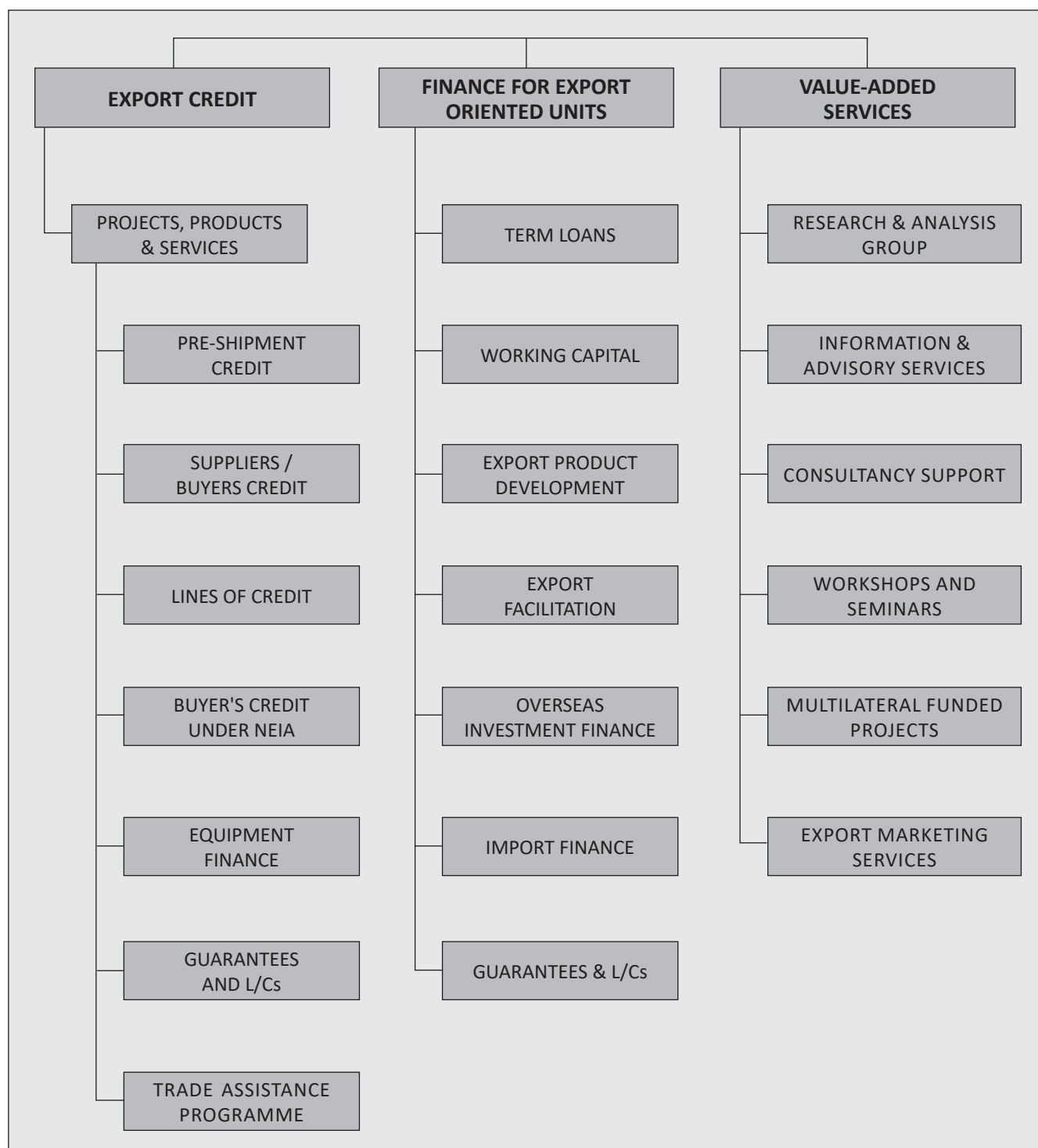
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