CHAPTER-I

INTRODUCTION

1.1. Background of the Study:

International trade is concerned with the exchange of goods and services with foreign countries. It consists of exports and imports between nations across international borders. The emergence of market-driven economies in many countries of the world has increased the importance of international trade. It has appeared as the engine of globalization. It is an important mode of international business.

No country can be self-sufficient in all the goods and services. Nor can all the products be produced efficiently in all the countries. Specialization in production is needed to gain the benefits of comparative advantage.

The basis of international trade is the comparative advantage in price ratios between countries. Price ratios are based on cost structures. Factor endowments can also be a source of comparative advantage.

International trade is important to achieve macroeconomic objectives of economic growth, price stability, employment generation, and balance of payments. It promotes efficient utilization of resources through economies of scale. Trade deficits create imbalances in the economy. All countries aim for a favorable trade balance.

International trade is exchange of capital, goods, and services across international borders or territories. In most countries, it represents a significant share of gross domestic product (GDP). While international trade has been present throughout much of history (see Silk Road, Amber Road), it's economic, social, and political importance has been on the rise in recent centuries. *(http://en.wikipedia.org/wiki/International_trade)*

International trade is in principle not different from domestic trade as the motivation and the behavior of parties involved in a trade do not change fundamentally regardless of whether trade is across a border or not. The main difference is that international trade is typically more costly than domestic trade. The reason is that a border typically imposes additional costs such as tariffs, time costs due to border delays and costs associated with country differences such as language, the legal system or culture. *(http://en.wikipedia.org/wiki/International_trade)*

Nepal is one of the least developed countries of the world. The country is surrounded by the world's biggest economy countries China & India. The international trade of the country is highly dependent with the neighboring country, India. The country has the negative balance of payment as well as the trade deficit every year. The country is fully dependent from the household commodities to the industrial products with the neighboring countries.

Nepal is a landlocked nation, surrounded by India on three sides and by Tibet (now a province of China) in the north. Historically, international trade before the 1950s was with these countries. Exports have consisted of primary agricultural produce, while everything not produced locally has been imported. Throughout the years of development, these imports have included industrial inputs, fertilizers, and petroleum. Since the 1970s, the balance of trade has been increasingly negative. During the same period, however, exports of garments and carpets have grown; reaching sales close to US$300 million, and trade with other countries has increased to the detriment of the trade with India.

Until the 1950s, 90 percent of Nepal's trade was with its giant neighbor, India. The essentially open border facilitates trade, but also makes unquantifiable smuggling hard to control. Exports to India are generally supplied by agricultural surplus from the fertile Tarai region— mostly rice, but also tobacco, jute, and vegetable oils. Raw materials such as hides, skins, herbs, textile fibers, metal ores, and some manufactured goods, such as bamboo products, wooden furniture, and textiles, are also exported. Imports consist of daily necessities such as salt, sugar, tea, medicines, petroleum products, and items such as chemicals, machines, cement, coal, and spare parts that are needed for development work. The trading relationship with India was first codified in 1950 with the Treaty of Trade and Transit, which lowered tariffs and tax duties on goods passing between Nepal and India. In successive modifications and renewals of the treaty (notably in 1960), transit facilities for trade between Nepal and other countries were established in India at the port of Calcutta. The decline in India's percentage of trade with Nepal to just above 30 percent in 1998 demonstrates the success of these arrangements. In March 1989, delayed negotiations led to the expiration of the treaty, and all but two trading points were closed for a year. This crippled the Nepalese economy, as internal trade (much of which had to pass through Indian Territory) and external trade with India was subjected to virtual closure. Shortages of basic goods such as salt and petroleum caused considerable strife, leading to both anti-India and anti-government demonstrations in Nepal, and were partly responsible for the downfall of the Panchayat system. An interim government successfully reinstated the treaty in June 1990. *(http://www.nationsencyclopedia.com/economies/Asia-and-the-Pacific/Nepal-INTERNATIONAL-TRADE.html)*

Till 1951, Nepal was kept in a state of virtual isolation from the outside world. It was only in 1956 that the country launched its First Five Year Plan and got into the process of development.

The dependency of the foreign trade of Nepal with neighboring country, India is seen increasing every year. At the same time, the amount of the trade deficit of Nepal is also seen increasing every year. Still, the there is a lack of trade diversification of Nepal.

1.2. Statement of the Problem:

Till 1970, no attempt was made to diversify the country's overall trade. Till 1970, the country's overall trade was confine to India alone. After the establishment of Trade Promotion Center in 1971, the share of India's trade gradually declined and the share of overseas improved.

After being the member of WTO also, the country has not been able to diversify the foreign trade the further countries. The previous partners are being also not maintained by the business-men as well as the government. The trade to the leading European countries has been declining. The past concentration of foreign trade with the respective countries has been remaining same & the trade deficit with India is increasing every year.

Still, the total exports, India alone occupies more than 60% of the total trade and more than 40% of the total imports to Nepal till now.

Mainly the problem arises in the Indo-Nepal Trade is:

- Has the trade-balance between the India and Nepal has turned lesser negative?
- Is the portion of the trade of Nepal has been diversified from India in the recent year?

1.3. Objectives of the Study:

The main objectives of the study are:

i. To find out the foreign trade composition of Nepal.

ii. To find out the export-import position of Nepal with the neighboring country mainly India.

iii. To find out the trade balance of Nepal with India.

1.4. Significances of the Study:

The significances of the study are:

i. It helps to put the actual picture of the foreign trade of Nepal.

ii. The study helps to show the macro level of trade of Nepal with the neighboring country India.

iii. The study will be helpful for the student & researcher who are eager to know the actual situation of foreign trade of Nepal with India.

1.5. Limitations of the Study:

The study has tried to show certain aspects of the foreign trade of Nepal. So, it cannot escape from these limitations:

i. The study is based on the historical data.

ii. The study is concentrated on the foreign trade with the one of the neighboring country of Nepal, India.

iii. Product wise analysis of the import-export has not been analyzed in the study.

iv. The study is done based on the secondary data mainly. Very few sample of question regarding the Indo-Nepal trade has been collected for the research purpose.

CHAPTER-II

REVIEW OF LITERATURE

2.1. International Trade:

The exchange of goods between citizens of different countries is called International trade. This kind of trade across national frontiers has grown in size with improved means of transport. Steamships, railways and aero planes have been largely responsible for this increase in the volume of trade.

With the introduction of mechanical transport, the world has become a small place. Goods are constantly transported from country to country. Freights are cheap. It does not take much time and money to send them from one end of the world to another. The development of banking and credit has also provided facilities for trade across the frontiers. As a result, one can say that no country in the world, however huge and populous it may be, in self-sufficient-not even the U.S.A. or China, blessed as they are with vast natural resources. None of them can stand alone without imports from other countries. Of India, too, the same is true. She, too, is not self-sufficient. *(Dewett & Verma, 1999:432)*

2.2. Advantages of International Trade:

The advantages of international trade rest on international division of labor. There is world-wide specialization in industries which results in increased total production and other advantages which are as follows:

i. The productive resources of the world are utilized to the best advantage. Every country concentrates on the production of goods for which it is best fitted. There is economy of effort and a consequent fail in prices. Thus, every country receives the highest return from its resources.

ii. A country is able to consume goods which it cannot produce at all, or only at an impossibly high cost. Thus consumers can enjoy a large variety of products. Commodities produced in the tropics find their way to the temperate zone, and vice versa. This provides greater economic welfare and a higher standard of living.

iii. Violent price fluctuations are togged down. As the area of market is enlarged by trade, the effects of the disturbing factors are spread over this large area and prices become more stable. If, at any time, the price of a commodity goes up abnormally, it can be imported from aboard and its price brought down.

iv. Shortage in times of famine and scarcity can be met from imports. Surplus produce can be sent out to needy countries. The world thus tends to be united into one economic unit. Food scarcities in India and Europe have often been relieved by imports of surplus food grains from the U.S.A., Canada and Australia.

v. Countries economically backward but rich in unused resources are able to develop their industries. Japan provides a good example. India is also adopting the same methods. In the early stage, the industries of a backward country have to be protected but once they develop, free trade stimulates them still further.

vi. Trade develops racial sympathies and creates common interests. Man gains culturally and cause of world peace is promoted. Exchange of goods is accompanied by exchange of ideas. This promotes international understanding, since a war is bound to interrupt international trade and put the people to loss; every effort is made to avoid it.

The existence of international trade promotes peace. No country, however big, can be self-sufficient. To achieve self-sufficiency, it will have to undertake expensive wars, conquer free areas and convert them into colonies. This is horrible. Free international trade supplies the essential needs of nations, and thus checks their greed and desire to conquer. *(Dewett & Verma, 1999:437)*

2.3. Disadvantages of International Trade:

In theory, no one can dispute the advantages of international trade. But, in practice, the other side of the picture cannot be ignored. Some countries, especially those which are at a lower stage of industrial development, have had a bitter experience of international trade. The disadvantages are:

i. The worst effect of foreign trade on backward countries is the destruction of their handicrafts and cottage industries. In India such industries had reached a high stage of perfection. But the flood of cheap British manufactures swept them before it. In recent times, Japan tried to crush our cotton industry by flooding Indian markets with cheap goods and protection had to be granted to save it. Industrially weak countries have to suffer like this.

ii. The empire-builder follows the trader. The foothold gained by traders is used to complete a country’s political slavery. For example, the British came to India for trade and stayed to rule.

A powerful country can easily find some excuse for attacking a weak country.

iii. Dependence on foreign goods creates difficulties in time of war when the country is cut off by enemy action. India had to face great trouble in getting ordinary articles like needles, tools and medicines during the war.

iv. Extreme specialization which makes a country depend on one or two industries only is bad. This is like putting all one's egg in one bucket. If a substitute is discovered or the industry otherwise suffers, the economic life of the people would be endangered.

v. Countries which sell primary commodities and buy manufactured goods in return are losers. The standard of living of the people in such countries remains low. And the pity is that this state of affairs tends no persist. Foreign trade under such conditions leads more to discontent and unrest than to peace and goodwill. It is well known that the feelings of the Indian people for the British before they left India were very bitter.

vi. Foreign trade may completely exhaust a country's natural resources like coal and oil which are irreplaceable. These goods are exported for the sake of profit. But the country suffers in the long run when their source is dried up completely.

vii. Imports of harmful drugs and luxuries, as opium in China, ruin the health of nation. For the use of such harmful articles, the blame must be put on international trade which brings them into the country.

viii. Through foreign trade, the economic troubles of one country are transmitted to others. The economic disturbances in one country are transmitted to others and their economy is upset. For example, the collapse of American markets in 1929 resulted in a world-wide depression.

ix. Trade rivalry leads to war and friction. Germany's desire to secure markets for her goods was the most important cause of the last two World Wars. Commercial competition often strains relations. Nearer home, India and Pakistan find it difficult to come to an understanding due, to some extent, to a clash of trade interest.

Thus, international trade is not an unmixed blessing. But, on the whole, the advantages far outweigh the disadvantages. At any rate, it has come to stay, and it is no longer possible to call a halt. *(Dewett & Verma, 1999:438)*

2.4. Doctrine of Free Trade:

A policy of no restriction on the movement of goods between countries is known as the policy of Free Trade. Restrictions placed with a view to safeguarding home industries constitute the policy of protection. In the words of Adam Smith, this term 'free trade' has been used to denote "that system of commercial policy which draws no distinction between domestic and foreign commodities and, therefore, neither imposes additional burdens on the latter, nor grants any special favors to the former."

Free trade, however, does not require the removal of all duties on commodities. It only insists that they shall be imposed only for revenue and not at all for protection.

As a practical policy, free trade is based on the theory of international trade already examined in the present chapter. In the words of Cairnes, "If nations only engage in trade when an advantage arises from doing so, any interference with their free action in trading can only have the effect of debarring them from an advantage."

Long before that wrote Adam Smith: "If a foreign country can supply us with a commodity cheaper than we ourselves can produce, better buy it from them with some part of the produce of pour own industry, employed in a way in which we have some advantage." He continued further: "Whether the advantage which one country has over another be natural or acquired is in this respect of no consequence. As long as one country has those advantages and the other wants them, it will always be more advantageous for the latter rather to buy of the former than to make."

The only expectation that Adam Smith would make was industries necessary for defense. These might be protected since "defense is more important than opulence."

The doctrine of free trade is the extension of the doctrine of division of labor to the international field. In the words of Adam Smith again, "Individuals find it to their interest to employ their industry in a way in which they have some advantage over their neighbors." And he adds. "What is prudence in the conduct of every private family can scare be folly in that of a great kingdom."

In short, the free trade theory is that such policy enables every country to devote itself to those forms of production for which it is best suited on the basis of comparative advantage. *(Dewett & Verma, 1999:439)*

2.4.1. Arguments in Favor of Protection:

Protection aims at helping some industries against foreign competition. This is done either through duties on imported goods, or bounties to domestic producers. An import duty makes the foreign articles sell at higher prices and so helps the home manufactures. This method is used with the following objectives:

i. To infant industries. An infant has to be protected till it grows to manhood. 'Nurse the baby, feed the infant and free the adult' is a well-known maxim. Protective duties are 'crutches' to reach new manufactures to walk. The advantage thus gained is often greater than the cost paid by consumers in the shape of higher prices. India extended protection to some important industries on the basis of this argument.

ii. To keep 'money at home'. When we purchase 'swadeshi' goods, we are keeping purchasing power in our own country. It is possible that we are paying more for these goods than we may have to pay for foreign goods of the same quality, if allowed come in freely. But we do not mind paying more and feel a glow of pride, when making a little sacrifice.

iii. To get an inflow of gold. When you send goods to others and close your doors to others' goods, you may have to be paid in gold. This will be possible, however, only when your goods have an inelastic demand and the others either cannot or do not retaliate.

iv. To develop 'key industries'. Key industries are keys to further industrial expansion. They provide machines and materials for other industries. They have a strong case for protection if they need help. Chemical and metallurgical industries are of this type. They serve as a base for the national economy. They are essential for the defense of the country in war and its prosperity in peace. This was a very strong argument for the Government of India to protest India's heavy chemical industry.

v. To attain self-sufficiency. When the government wants to make the country independent of foreign supplies, protection is necessary. Complete self-sufficiency, however, is impossible and even a partial one is costly. Therefore, self-sufficiency should be sought for only in essential industries.

vi. To secure diversification of occupations. The greater the number of openings for the people of a country, the better it is for their material progress. Too much reliance on any single industry is risky. To keep all one's eggs in one basket is not a wise policy. Therefore, it may be necessary to encourage some industries with the artificial aid of protection.

vii. To prevent dumping of foreign goods. When a foreign country plans to crush our industry by selling goods at a price even below the cost of production, it is a case of dumping. Such a supply of cheap goods might be welcome if it were permanent; but it is usually temporary. It is done to kill competition and then to make up all loses by charging higher prices. Anti-dumping duties are, therefore, justified to save the home industry.

viii. To create employment. Protection helps to develop industries, and it creates more employment. There is no doubt that the development of sugar and other Indian industries under protection provided a large volume of employment.

ix. To correct adverse balance of payments. Sometimes, protection is given with a view to correcting an adverse balance of payments situation can thus be improved, although temporarily.

x. For the country's defense. Adam Smith asserted that 'defense is better than opulence' and ever since then the exigencies of preparedness for defense have been an important justification for protection. Certain industries which produce defense materials and equipment such as arms, ammunition, tanks must be protected.

xi. To safeguard the interest of high-wage labor. Sometimes it is argued that in the absence of protection, the highly-paid labor of the industrially advanced countries would be exposed to the competition of cheap foreign labor, and that the products of their high-wage labor can be undersold by those of "pauper labour" from abroad. *(Dewett & Verma, 1999:439-440)*

2.4.2. Arguments against Protection:

Protection is not an unmixed blessing. It has some positive disadvantages or dangers too. Some of these dangers are given below:

i. When foreign competition is removed, the home manufacturers become lethargic. Protection acts like an opiate. It sends the home producer to sleep. All improvements are neglected. There is no incentive to cut down the costs or to improve the quality. Technical progress thus comes to a standstill.

ii. Another disadvantage is that there is a loss in public revenues. If high protective duties are imposed, imports will shrink and revenue from customs will fall.

iii. Burden on consumers. The most important objection to protection comes from the consumers. The burden of protective duties does not fall on the foreign manufacturers as it is sometimes supposed. The burden is on the home consumer because he has to pay a higher price than before on account of the imposition of import duties. It is said that it does not look fair that a poor consumer should be penalized to enrich the already rich manufacturer. Thus inequalities of wealth distribution are further aggravated.

iv. Tariff is said to be the mother of trusts. As soon as protection has removed foreign competition, the home manufacturers are induced to form combinations of their own in order to remove the internal competition also. In India, the sugar factory owners formed the Indian Sugar Syndicate to eliminate competition among themselves, and to charge a monopoly price from the consumers.

v. There is also the danger of corruption. It is very well known that in America the legislators used to be offered bribes by industrialists. The object was that no legislative measure may be adopted which might adversely affect them, and legislation which suits them may be passed.

vi. Inefficient concerns perpetuated. The removal of foreign competition perpetuates weak and inefficient concerns. If competition were free, only sound and healthy concerns will remain in the field. Although it may inflict some injury on some individual manufacturers, yet weeding out of unhealthy concerns is considered to be good for the society as a whole.

vii. Misdirection of resources. Protection diverts labor and capital and other factors of production into set channels. They are prevented from seeking their most remunerative employment. This is bound to decrease the national dividend. Misallocation of the available resources into unsuitable channels cannot be economically justified.

viii. Vested interests are created which refuse to give up protection. The 'infants' refuse to admit that they are grown up. They start kicking at the slightest indication of withdrawal of protection.

ix. There is a danger of retaliation from aboard. As a result, some home industries might suffer.

x. Choice limited. Protection limits the choice of consumer goods. Through tariffs, quotas and exchange control, the availability of foreign goods is severely limited. The various protective policies drastically cut down the availability of foreign movies, books, magazines, pictures, clothing, food, etc. Goods imported from other countries also bring with them ideas and styles and other ways of living. Indeed, they enrich life. *(Dewett & Verma, 1999:441)*

2.5. Theories of International Trade:

Various theories of international trade have been propounded. The important theories are: *(Agrwal, 2062, 59-62)*

1. Mercantilist Theory
2. Absolute Cost Theory
3. Comparative Cost Advantage Theory
4. Opportunity Cost Theory
5. Factor Proportions Theory
6. Modern Trade Theories

2.5.1. Mercantilist Theory:

This theory was popular in the 18th century. It advocated that a government should encourage exports and restrict imports. The positive balance of trade leads to flow of wealth for the well-being of the country. Its fundamental principles are nationalism, bullionism and favorable balance of payments.

- This theory is simple. However, it ignored production efficiency through specialization.

2.5.2. Absolute Cost Theory *(Adam Smith, 1776) (Classical Theory):*

This theory states that countries should specialize in products of absolute cost advantage. Countries can benefit from trade by concentrating on products in which they have absolute cost advantage.

For example:

Country	Labour Unit	Cotton Production	Jute Production
Nepal	1 man day	10 units	5 units
Bangladesh	1 man day	5 units	10 units

Nepal should specialize in cotton production and Bangladesh should specialize in jute production because of absolute cost advantage. Nepal should export cotton in exchange for jute from Bangladesh.

- This theory ignores absolute cost advantage in both products by a country.

2.5.3. Comparative Cost Advantage Theory *(David Ricardo):*

This theory states that countries should specialize in products of absolute comparative cost advantage. Example

	Labour hours required to products	
Country	**1 gallon wine**	**1 yard cloth**
Portugal	80	90
England	120	100

For Portugal, comparative cost of 1 gallon of wine is 80:120 and for 1 yard of cotton is 90:100. Portugal should specialize in production of wine because of comparative cost advantage.

Assumption of Ricardian Theory are:

- Labour is the only factor of production
- All labor is uniform in quality
- Labor is perfectly mobile within country
- Free competition exists among labour
- There is full utilization of labour
- No transport and other costs are involved in production

2.5.4. Opportunity Cost Theory *(Gottfried Haberler, 1993):*

This theory states that cost of producing a particular good is the goods which have to be foregone to obtain this good. Countries should specialize in production of goods in which they have opportunity cost advantage for international trade.

- Production possibilities curves of various countries are indicators of opportunity costs.

2.5.5. Factor Proportion Theory *(Heckscher-Ohiln/H-O Theory):*

This theory states that international trade is based on differences in comparative costs determined by:

- Relative differences in factor endowments in different countries.
- Differences in costs of factors of production.

According to this theory, countries with relatively large labour forces will concentrate on producing labour-intensive goods, whereas countries with relatively more capital will concentrate on producing capital-intensive goods.

Assumption of Factor Proportion Theory are:

- There should be two countries, two commodities and two factors of production.
- Quantitative heterogeneity but qualitative homogeneity of factor endowments.
- Perfect competition in commodity and factor markets.
- Fully utilized resources.

- Production functions are same for two commodities but differ in factor intensities.
- Free Trade between two countries.
- Factor of production are immobile between two countries.

Leontief Paradox: The empirical testing of Factor proportion Theory found that USA had abundance of capital compared to labour. But it was exporting less capital-intensive goods. It was a paradox.

2.5.6. Modern Trade Theory:

These theories advocate that the only necessary condition for the gains from trade is that price ratios should differ between countries.

2.5.7. Standard Trade Model:

This model is based on welfare effects of growth, income transfer and trade policy, which are important determinant of terms of trade. As a result, changed in commodity prices due to trade liberalization magnify the resulting changes in factor prices. This means that there would be rise in relative returns to the abundant factor i.e. unskilled labor in the context of developing countries. On the grounds of expansion in labor intensive economic activities including employment, international trade considered to be contributing to reduce poverty in developing countries.

Increasing internal and/or external economies of scale are important causes of trade which are not included in classical trade theory. Classical trade theories do not offer complex explanations on international trade that may not driven by a factor proportion interpretation, trade regularities that is two way trade in similar products, extension of the HO model; intra industry trade, increasing returns to scale, economies of scale and production, monopolistic competition and differential products, transaction cost, joint production, government induced distortions-taxation & differential products; consumer substitutability, quality differential, differentiation by style and technology gaps. *(Khatri, 2011:298)*

2.5.8. New Trade Theory:

New trade theory that emerged in 1980's assumes scale economies, imperfect competition and product differentiation lead to gains from trade. Imperfect competition leads to intra-industry trade that is dumping and monopolistic competition. External scale economies and trade allows increasing across borders which creates lower unit average cost and gains from trade through opening the trade. It incorporates the following four innovations.

a) Market Imperfections

It includes informational asymmetries and adjustment costs. The models based on market imperfections give good reason for free intervention policy.

b) Strategic Behavior and New Industrial Economics

Strategic behaviors and new industrial economics assumed about competition, growth and government policy instruments. Dynamic effects of trade liberalization and openness on total factor productivity and efficiency at the industry level which justify trade intervention policy.

c) **New Growth Theory**

It is also based on market imperfections as well as government intervention leading to higher saving and externalities especially with respect to innovation that is technology and knowledge, research and development.

d) **Political Economy Arguments**

This argument is based on rent seeking; distribution between labor and capital; the presence of oligopoly and donation by interest group which is leading to inefficiency in policy making. *(Khatri, 2011:298-299)*

2.6. Barriers to Trade:

Free trade enables countries to specialize in the activities they perform best. It leads to production efficiency, wider choice of products, market expansion, more jobs and higher standards of living. It liberalizes international trade.

Many countries use restrictive measures in trade. They prevent foreign competition. They serve as barriers to international trade. The reasons for trade barriers are:

a) Raise revenue through tariff for the government.

b) Improve balance of payments by restricting imports.

c) Encourage local production to promote exports and replace imports.

d) Diversify the economy.

e) Protect domestic industries and defend strategic industries.

f) Protect local jobs by preventing foreign competition.

g) Encourage foreign direct investment.

h) Preserve national heritage and culture.

i) Retaliate against unfair trade practices by foreign suppliers. Prevent dumping (selling of goods below cost to capture market share).

j) Promote political and other objectives.

- Trade barriers generally provoke retaliation by foreign countries. They also result in reduction of the volume of world trade. Inefficiencies in production may lead to higher prices and poor product choice. Unemployment can increase.

- The world Trade Organization (WTO) regime advocates trade without discrimination. It deals with multilateral trading system. *(Agrawal,2062, 62-63)*

2.7. Types of Trade Barriers (Techniques of Protection):

Trade barriers can be of three types. They are:

1. Tariff Barriers

Tariff is a tax on goods that are traded internationally. It is added to the price of goods. It directly provides price protection. Tariff barriers can be:

a) Export Tariff: It is a tax on goods sent out of country. It is generally ad valorem imposed as a percentage of value of goods exported.

b) **Imported Tariff:** It is a tax on goods brought into the country. It is known as customs duty. It is generally ad valorem imposed as a percentage of the value of goods imported.

- Countervailing duty may be imposed on imports to offset export subsidy provided to exporters.

c) **Specific Duty:** It is a tax based on number of items exported or imported. The value of the goods is disregarded.

d) **Compound Duty:** It is a tax consisting of both ad valorem and specific duty. It is based on both the value and number of items imported or exported.

e) **Transit Tariff:** It is a tax levied on goods passing through a country.

- Tariff barriers raise revenue, discourage imports and make local products more attractive.

2. Para Tariff Barriers

They consist of border charges, fees, and local taxes other than tariffs on imports and exports. They can be:

- Custom valuation systems
- Tariff classifications systems
- Fees, special charges, local taxes

3. Non-Tariff Barriers

They are rules, regulations and bureaucratic red tapes. They delay or prevent purchase of foreign goods. They limit imports. They indirectly provide non-price protection.

Non-tariff barriers can be:

a) **Quotas:** It is quantity limit on the volume of imports or exports. They restrict the number of units or share of market. Licensing can be used. A quota set at zero is called Embargo. It prevents imports from particular countries.

- Some countries resort to voluntary trade restraint for exports. Other tie-up imports with exports.

b) **Subsidies:** They involve use of public funds by the government to lower costs. They can be direct or indirect. They help domestic companies to compete with imported products.

c) **Local Content Requirement:** It specifies that a specified percent of value added must be sourced locally to avoid import duties. Exports are subjected to this restriction.

d) **Technical and bureaucratic Barriers:** They are restrictive specifications of technical standards. They relate to:

- Quality standards for products
- Consumer safety, health and sanitary regulations
- Packaging and labeling
- Quarantine requirements for imported goods

- Documentary requirements and Bureaucratic delays in processing documentation.
- Antidumping restrictions

e) **Procurement policies:** They favor domestic producers. A "buy local" policy is an example.

f) **Exchange Controls:** They restrict the availability of foreign currencies to pay for imports. Foreign exchange licensing and variable exchange rates can be used. Foreign exchange earnings may need to be deposited in central bank for export earnings. *(Agrawal,2062, 63-65)*

2.8. Problems of International Trade:

The problems of international trade are:

1. Protection

Countries resort to protection through tariff and non-tariff barriers.

2. Laws and Institutions

Every country has its laws, regulations and institutions. They regulate the conduct of international trade. They impact trade as follows:

a) **Bilateral:** They regulate trade between two countries on a bilateral basis. For example, the Treaty of Trade regulates trade between Nepal and India. Such agreements are enforced by individual countries. They constrain flexibility and freedom of international trade.

b) **Regional:** They regulate trade at regional level. They are enforced by a group of countries by establishing preferential trading arrangements, free trade areas or customs union. SAARC, ASEAN, NAFTA and EU are examples.

c) **Multilateral**: They regulate international trade worldwide. They are enforced by international institutions, such as WTO.

- Laws and institutions provide both constraints and opportunities to international trade.

3. Foreign Exchange Problems

Every country has its own currency and financial system. International trade involves use of different currencies. Not all currencies are freely convertible. Currency values keep on changing, especially for countries subject to floating exchange rates. The risks of changes in currency value need hedging. This adds to costs of international trade.

- Many developing countries have foreign exchange control regulations. They adversely affect international trade.

- Countries also face balance of trade and balance of payment problems which constrain international trade. Countries with trade deficits resort to import restrictions or import substitution practices.

4. Transit Problems

Land-locked countries face transit problems. They restrict accessibility to markets for international trade. Such problems also add to the cost of products. Export documentation, customs clearance, demurrage charges, damages and pilferages related to transit adversely affect the competitive position of land-locked countries in international trade. Transit delays constrain meeting of deadlines for exports. The use of many intermediaries also adds to costs of exports.

5. Unfair Competition

International trade is subject to intense competition. However, unfair competition is one of its major problems. In order to capture markets, some countries resort to dumping. They sell their products at less than fair value. China provides example of dumping practices.

- Corrupt and unethical practices have also appeared as serious problems for international trade. Under-the-table deals are increasing.
- Domestic industries in developing countries suffer adversely from unfair competition.

6. Government Policies

Government policies relating to foreign trade differ from country to country. They change with the changes in the political and dynamic environments. Changing government policies create problems for international trade. Bureaucratic hurdles constrain implementation of foreign trade policies.

7. Information Gap

Many developing countries lack up-to-date information for international trade. They lack institutional mechanism to monitor movements and changes in international markets. Market development is constrained by lack of market research. The information gap has led to overdependence on few countries for international trade.

8. Poor Quality Control

Developing countries have not been able to control the quality of exportable products. Unscrupulous exporters tarnish the image of their products by exporting low quality products. An interesting example is hand-knotted woolen carpets and Pashmina shawls of Nepal. The high image of these products in the European market has been adversely affected by the export of products made from waste wool.

- The system of labeling and quality certification are also lacking in many developing countries. ISO certification is lacking.
- Poor quality control of exportable products is a big problem of international trade. *(Agrawal,2062, 65-67)*

2.9. Risk in International Trade:

Companies doing business across international borders face many of the same risks as would normally be evident in strictly domestic transactions. For example,

- Buyer insolvency (purchaser cannot pay);

- Non-acceptance (buyer rejects goods as different from the agreed upon specifications);
- Credit risk (allowing the buyer to take possession of goods prior to payment);
- Regulatory risk (e.g., a change in rules that prevents the transaction);
- Intervention (governmental action to prevent a transaction being completed);
- Political risk (change in leadership interfering with transactions or prices); and
- War and other uncontrollable events.

In addition, international trade also faces the risk of unfavorable exchange rate movements (and, the potential benefit of favorable movements). *(http://en.wikipedia.org/wiki/International_trade. June 15, 2011)*

2.10. Structure of Nepal's Foreign Trade:

Till 19511, Nepal was kept in a state of virtual isolation from the outside world. It was only in 1956 that the country launched its First Five Year plan and got into the process of development. But till 1960, no attempt was made to diversify the country's overall trade. Till 1970, the country's overall trade was confined to India alone. After the establishment of Trade Promotion Centre in 1971, the share of India's trade generally declined and the share of overseas improved. *(Shrestha, 2008:242)*

2.10.1. Nepal's Efforts on Trade Diversification:

With a view to achieve economic independence and diversify Nepal's foreign trade, especially in oversea countries, the government of Nepal introduced the 'Bonus System' with the incentives to the Nepali exporters to compensate them for the high transit cost due to the landlocked character of Nepal. But this system could not fulfill its objectives because the country had two fundamental weaknesses:

- Nepal's export products were not being subject to the discipline of the international market forces; and
- The economy was kept in ignorance concerning its real comparative advantages and hence was not receiving adequate signals for resource allocation.

Till 1970, Nepal's 99 percent of total trade was confined to India alone. It was only after the establishment of the Trade Promotion Centre (TPC) that Nepal could successfully diversify its foreign trade. As such, since 1971 the share of Nepal's trade with India gradually declined while the share with overseas countries increased.

Although Nepal was able to diversify its foreign trade, the volume and value of trade did not rise substantially because, instead of promoting the country's export trade, the old bonus system brought a great distortions and dislocation in foreign trade by creating the practice of 'over-invoicing' among the traders. Therefore, in order to assure stable incentives to the exporters, the government of Nepal introduced a new system the 'dual-rate system' in 1977.

The dual-rate system provided 33 percent incentive minus 19 to 20 percent transit cost, and thus, 13 percent effective profit to the exporters. But this system also could not serve the basic objective of the country, because the exporters did not pay attention to the question of creating a basic and favorable infrastructure for expansion of the country's export trade. They confined their attention merely to the profit margin to be earned through the system. Therefore the government of Nepal abolished the dual-rate system and introduced a multiple exchange system, which was able to adjust the foreign exchange rates according to the demand for supply of foreign exchange and essential commodities in the country.

The Sixth and the Seventh Five Year Plans had also emphasized greater diversification of trade, especially the export trade, both commodity- and country-wise. However, these plans also could not create a favorable environment for the country's trade (especially export trade) diversification. *(Shrestha, 2008:242-243)*

2.11. Nepal's Trade Arrangements with India:

A Treaty of Trade recently signed between Nepal and India has mentioned several trade arrangements as follows:

i. Strengthen cooperation and trade by exploring and undertaking all necessary measures.

ii. Provide maximum facilities and undertake all necessary measures for the free and unhampered flow of goods between the two countries. For this purpose, both the countries have agreed to use 22 routes for mutual trade.

iii. Accord unconditionally to each other treatment no less favorable than that accorded to any third country with respect to (a) customs duties and charges of any kind imposed on or in connection with importation and exportation, and (b) import regulations including qualitative restrictions.

iv. Provide preferential treatment on 14 primary products including agricultural products, forest products, horticultural products, rice, pulses, timber, animals, birds, fish, bees, honey, raw wool, milk, herbal medicines, yak tails, etc., on reciprocal basis.

v. Help promote the industrial development of Nepal by granting free of customs duty and quantitative restrictions for some industrial products manufactured in Nepal on non-reciprocity basis.

vi. Facilitate greater exchange of goods between the two countries by waiving additional customs duties on all Indian exports by Nepal Government to the maximum extent compatible with their development needs and protection of their industries.

vii. Payments for transactions between the two countries can be made in accordance with their respective foreign laws, rule and regulations on the basis of mutual consultations.

viii. Presentation against infringement and circumvention of the laws, rules and regulations of either country in regard to foreign exchange and foreign trade.

ix. Maintain or introduce restrictions for protecting public morals, human, animal and plant life, safeguarding national treasures, implementation of laws relating to export and import of gold and silver bullions and such other interests as may be mutually agreed upon.

x. Take measures for the protection of essential security interests of the either country relating to transit, export and import of certain articles such as narcotics and psychotropic substances, literary or artistic property or relating to false marks, false indication of origin or other methods of unfair competition.

xi. Implement harmoniously the recently signed treaty through mutual consultations.

xii. Automatic renewal of the Treaty for the next five years upon the expiry of the Treaty unless either of the parties intends to terminate it. *(Shrestha, 2008:260-261)*

2.12. Nepal's Transit Arrangements with India:

Transit refers to movement of persons and goods through the territory of transit countries (transit facility providing country). Transit state is a state with or without a seacoast, situated between land-locked state and the sea through whose territory traffic-in-transit should take place. For Nepal, India is a major transit state and Nepal is a land-locked state. The land-locked state like Nepal needs Freedom of Transit, which means the right of crossing the territory of transit state to or from the territory of the other party.

The Freedom of Transit represents:

- Through land;
- Through water routes (including rivers and sea);
- Through air space, etc.

There are altogether countries in the world including 14 in Africa, 5 in Asia, 2 in South America and 9 in Europe (including 4 Autonomous States-Vatican, San Marino, Andorra, and Liechtenstein).

All the European landlocked countries (Austria, Switzerland, Hungary, Luxembourg, and Czechoslovakia) have been turned in the row of developed nations while the remaining 21 countries remained underdeveloped or least developed; Nepal is one among them. The main reason for economic backwardness of these countries is their land-locked character.

Nepal is China-locked in the North. However, Chinese ports are about 5,000 km away from Nepalese border. The snowy range of Himalaya stands as a transit barrier between these two countries. Tibet, which is one of the nearest neighbours, is just in the earliest stage of its economic development. Nepal has transit agreement with Bangladesh also; it is about 16 kms away compared to Calcutta port. Therefore, Nepal has no alternative transit route for its cargo except India's Calcutta port, which provides very poor physical facilities to Nepal traders. *(Shrestha, 2008:261-262)*

2.12.1. Agreed Routes for Mutual Trade between India & Nepal:

Following are the agreed routes or transits for mutual trade between India & Nepal:

1. Pashupatinagar/Sukhia Pokhari
2. Kakarbhitta/Naxalbari

3. Bhadrapur/Galgalia
4. Biratnagar/Jogbani
5. Setobandha/Bhimnagar
6. Rajbiraj/Kunauli
7. Siraha, Janakpur/Jayanagar
8. Jaleswar/Bhitamore (Sursand)
9. Malangawa/Sonabarsa
10. Gaur/Airgania
11. Birgunj/Raxaul
12. Bhairahawa/Nautanwa
13. Taulihawa/Khunwa
14. Krishnanagar/Barhni
15. Koilabas/Jarwa
16. Nepalgunj/Nepalgunj Road
17. Rajapur/Katerniyaghat
18. Prithvipur/Sati (Kailali)/Tikonia
19. Dhangadhi/Gauriphanta
20. Mahendranagar/Banbasa
21. Mahakali/Jhulaghat (Pithoragarh)
22. Darchula/Dharchula

Source: Indo-Nepal Treaty of Trade Agreement

There are all together main customs posts along Nepal India and Nepal China borders with the additional of 143 Choti Bhabsar (sub-customs posts). Nepal has transit treaty with India only. .Nepal has established 3 dry ports on the Nepalese side for the transport of goods directly to and from Calcutta Port. They are in Biratnagar, Sirshiya east of Birgung and Bhairahawa, and the dry port of Sirshiya Hs provision of railway connection via Raxaul to Calcutta port.

2.12.2. Agreed Transit Points between India & Nepal:

The development of market towns took place along the Nepal India border, mostly near the Indian railway heads since the early twentieth century. These towns along the Tarai emerged as trade routes between Nepal and India with some trade points located in the hills along border in the east and the west. The development of numerous transit points emerged during different period after 1951. The following are the mutually agreed main trade routes for trade between Nepal and India and transit points for access to sea from Calcutta Port:

1. Sukhia Pokhari
2. Naxalbari (Panitanki)
3. Galgalia
4. Jogbani
5. Bhimnagar
6. Jayanagar
7. Bhitamore
8. Raxaul
9. Nautanwa (Sonuali)
10. Barhni

11. Jarwa
12. Nepalgunj Road
13. Tikonia
14. Gauriphanta
15. Banbasa

Source: Department of Custom, GON

2.13. International Transit Agreement relating to Sea Route for Landlocked Countries:

Some of the major international transit agreements relating to sea route for landlocked countries are as follows:

- Westphalia Treaty, 1648
- Vienna Congress, 1817
- President Udro Wilson's 14 points Agenda
- Barcelona Convention, 1921
- GATT, 1947-Some Sections
- Sea-related Conference, Geneva 1958
- New York Convention, 1965
- Law of Sea, 1982- Prepared under the afford of UN

2.14. Review of the Past Studies:

EDERI (Economic Development and Engineering Research Institute) *(1994)* in their paper ***Trade Imbalance with India*** discussed on the India's cost advantage which made India Nepal's principal trade partner. Similarly, the study states Nepal and India, while possessing low tariffs themselves, did not have a common tariff with respect to the rest of the world, it created incentives for smuggling. It states it the past, given India's high tariff structure and Nepal's need to keep a lower tariff structure in order to meet import demand at a lower cost, there was an incentive to smuggle third country goods from Nepal to India. The paper also discussed on the Trade and Transit Treaty of 1991 which was signed on December 6, 1991. Similarly, the report focused on the weakness and the strength side of the treaty from the Nepal's point view. The paper also discussed on the agreement of October 20, 1992 and the changes made in the Trade and Transit Treaty of December, 1991. The paper has stated that India is the major market of Nepal's export of agricultural and primary products and discussed on the potential export products & their performance.

Khadka *(2052)* in his article ***Diversification of Exports in Commodity: An Issue of Concern*** has discussed on the Nepal purchasing power of Nepalese which is needed to boost up the demand for production one of the means to expand and specialize its products is export trade, diversified in terms of commodity and country. He has stated that the ever widening foreign trade deficit for Nepal has become the bitter pill to swallow for the economy. He suggested that one of the measures to correct the situation would be to discourage imports but as understood theoretically, export is also a function of imports. Therefore, import restriction will not be the acute solution to the problem; rather it will ultimately affect the base of exports too. He concluded that the ever broadening volume of trade imbalance on the one hand and squeezing base of exports on the other are the major issues of concern in external sector of the economy.

Jha *(2053)* in his article ***Nepalko Baideshik Byapar Esthiti*** has pointed out that the increase in the import of Nepal were due to the high dependency in goods imported and stable situation in the domestic production. The import of goods in Nepal has not been for the development purpose but for the profit-oriented business. Similarly, Nepal has not been able to produce the international level of goods as well. He suggested for the increase in the hydro-power trade with India to reduce the high amount of trade deficit between the two countries. He also added to diversify in the trade with respect to the commodities and the countries to reduce the high level of deficit trade balance of the country. He also suggested for the improvement of the agro-based industries of Nepal to cope with the food scarcity in the country.

Chettri *(2054)* in his article ***Nepalko Baideshik Byapar Ra Samjaoyta*** has discussed the historical trade relations with the neighboring countries India & an autonomous region of China, Tibet. He has also stated that due to the high level of influence from the Indian side on the political and economic situation of Nepal, the trade of Nepal with India is also seen increased. He has also discussed the settlement process of trade with China, India, Bhutan & other countries. The settlement of trade with China is done through letter of credit opened in Nepal Bank Limited & Peoples' Bank of China. In context to Bhutan, the Indian currency, letter of currency is opened. The payment for India is done through three modes of payment namely; cash, Indian currency draft, telegraphic transfer, hundi or letter of credit & for certain industrial raw materials payment is done through foreign currencies letter of credit. He had also discussed on the Indo-Nepal Trade Treaty 2053. He has stated that being a land-locked country, Nepal competing with a huge economy country, India is really a shameful situation.

Busy *(1998)* in his article ***Nepalko Nerayat Byapar: Esthithi, Samasyaya Tatha Chunauti*** has stated the major challenges of Nepal in the sector of trade is to reduce the deficit trade balance, bring the balance of payment in the normal condition & finally bring the high level of economic growth rate of the nation. He pointed that the major reasons for the downfall in the foreign trade is due to the looseness in the import business, coping the trend of others unknowingly, high dependency in import & generating resource within the country. He has argued for the development of the agro-based & software industries in Nepal to improve the deficit trade position. He has also argued for the production of the quality herbal products which are highly demanded in the European region which helps to diversify the trade of Nepal from India.

Luitel *(2056)* in his article ***Nepalko Baideshik Byaparko Bartamaan Sanrachana Ra Siknuparnay Paath*** has stated that there is an existence of exchange of foreign currencies in the process of international trade which will directly affect the country economy. Import-export will also effect on the industrialization of the country. He stated that Nepal has been facing a huge trade deficit since long time. The foreign trade of Nepal is highly influenced by the two huge neighboring countries India & China. He added that among these two countries also existing the long open border especially with India has highly affected in the foreign trade of Nepal.

He has found that the major trade partner in context to import or export among the SAARC nations, India leads in total.

Rijal *(2000)* in his article ***Nepal's Foreign Trade*** has pointed out the policy reform after 1986 when Nepal adopted structural adjustment program (SAP) that intended to remove some of the structural imbalance in the economy to achieve macroeconomic stability. He also pointed out the services export of Nepal especially travel and tourism. He also found that Nepal's merchandize trade is characterized by primary products dominated exports (excluding carpet and garment) and manufactured products dominated imports. Persistently large amount of trade deficit has been the hallmark of Nepal's foreign trade. He found Nepal's merchandize trade is very highly concentrated in two products: overwhelmingly Germany-bound woolen carpets and the US bound ready-made garments. Barring the trade in these two products, Nepal's merchandize trade has been stagnant in the 25 years period until 1995/96. However, because of the favorable trade and treaty of 1995 between two countries, Nepal's export trade with India has grown almost three folds in three years since then India then provides market to 37% of Nepal's export. He found a substantial amount of intra-firm trade between Indian joint venture companies in Nepal and their parent companies in India has contributed to this.

Taneja & Pohit *(2000)* in their paper ***India's Informal Trade with Nepal: An Exploratory Assessment*** stated that the large and vibrant informal trade between India and Nepal continues to thrive despite unilateral/bilateral/regional/multilateral trade liberalization in the two countries. This calls for an in-depth analysis of India's informal trade with Nepal. The analysis, carried out on the basis of an extensive survey conducted in India and Nepal reveals that informal traders in India and Nepal have developed efficient mechanisms for contract enforcement, information flows, risk sharing and risk mitigation. Further, informal traders prefer to trade through the informal channel because the transaction costs of trading in the informal channel are significantly lower than the formal channel implying that informal trade takes place due to the inefficient institutional set up in the formal channel. Moreover, lower education levels of informal traders could be an important dete\\rrent for using the formal channel. Finally, the analysis of discriminating characteristics of formal and informal traders in India and Nepal indicates that transaction cost and education level are the two common discriminating factors.

Poudel *(2058)* in his article ***Nepalko Baideshik Byapar: Bigat Ra Bartamaan*** has stated that before 1934, Nepal has a bilateral trade with only two neighboring countries India & Tibet (an autonomous region of China). After 1934 only, Nepal made a diplomatic relation with United Kingdom then with other nations of the world. In the early days of the trade with the India & Tibet, the made concentration was only on the agro-based commodities. Then Nepal started to import locomotive equipments, steel, electrical equipment, polyester fiber, cement, caustic soda, vehicles, gold, machineries and parts, aero-plane parts, computer, petroleum products, medicine, raw wool, etc. He found that the import amount has been extremely increased than the export which had affected in the balance of payment of the nation. The link with the other nations through various means of transports, the trade of Nepal is increasing day-by-day.

Kafle *(2058)* in his article ***Export Promotion through Exchange Arrangements*** discussed on the Exporter's Exchange Entitlement Scheme. He has stated that the scheme used to be popularly known as the Bonus System. This system existed for about 15 years (1963-1978). Under this system, exporters who were capable of exporting the countries other than India and earning convertible currencies used to be provided bonus certificate which was to be used for the purpose of importing goods from those countries. Thus in order to import from third countries one must had to export first and get bonus certificate. This system contributed significantly in the process of diversification of Nepal's exports to third countries. However, some problems like uncertainty in bonus premium value, price instability could not persuade exporters to envisage vigorous endeavor to undertake sound and persistent export efforts. He concluded that the policies till adopted were not sufficient and efficient. There is a very need of development of the physical infrastructure. The local level utilization of local resources should be increased to get the market in international level.

Shrestha *(2003)* in his paper ***Nepal-India Bilateral Trade Relations Problems and Prospects*** studied on the direction of trade of Nepal historically towards the India and other nations. He also briefly discussed on the commodities traded with the India. The balance of trade with India has also been studied. Major India-Nepal Trade Treaties that have been signed and implemented have been reviewed in the paper. The trade points between India and Nepal has been deeply analyzed according to their functions, institutionalization and operationalization. Similarly, the major problems and prospects regarding the trade and transits between India and Nepal have been pointed out in the paper.

Chettri *(2003)* in his article ***Byaparko Seroferoma Nepal-Bharat Sambandha*** has presented a scenario of result from the deadlock between India & Nepal trade and transit in 1989. Due to change in the political situation in Nepal, the treaty was not taken for a year & a new interim government renewed a trade and transit treaty. Due to the deadlock in the transit points constraining in Biratnagar & Birgunj Customs, Nepal face a load of 40% in its economy. The agreement on value added between India & Nepal on December3, 1996 also affected the trade. Similarly, he also added that the provision of 'One time lock' also facilitated on bilateral trade.

The Editorial *(2003)* in the article ***Mist over Birganj ICD*** has stated that Nepal's business sector should have gone for a celebration spree on hearing the signing of the railway agreement between Nepal & India. The editorial states that it paves the way for the operationalisation of Inland Container Depot (ICD) at Birganj. And this is expected to reduce by about 40% the cost of transportation for the imports and exports of Nepal that move through Calcutta port. It has also stated that as the consumers have repeatedly heard of the expected reduction in transport cost once the ICD is operational, they expect the price of the imported goods to come down. And the private sector should be prepared to fulfill this expectation. It has stated the private sector should also start preparing further suggestions to the government to maximize benefits from the ICD.

Special Studies Division *(2004)* in their paper ***Trends of Nepal's Import Duties: Implication with Future Trade Liberalization*** states that Nepal is accelerating the process of trade liberalization that had commenced in the mid-eighties; this is reflected in membership of WTO, agreement of a framework for a free trade area (FTA) in south Asia and entering an FTA with BIMST-EC. Since import duties are presently an important source of government revenue, the likely impact of trade liberalization on this important revenue source has to be evaluated. The study addresses this felt need through an elasticity and buoyancy analysis of import duties over the span of fiscal year 1980/81 to 2001/2002 as well as analyzing the responsiveness of Nepal's import duties through empirical regression and five year ahead projection. The paper finds low measure of elasticity and buoyancy as well as low elasticity of import duties, although five-year projections do not suggest a decline in contribution to government revenue. The prior indicate low productivity and responsiveness of the domestic tax base suggesting a need to accelerate reforms of the tax administrative system while the latter indicates that diversification of the import basket would be appropriate.

Maharjan *(2006)* in his thesis ***Trade Policy of Nepal with India and Its Impact on National Economy*** has analyzed foreign trade direction of Nepal. He also analyzed impact of Indo-Nepal Trade Treaty of 1996, in particular, in improving trade relation between two countries; identify the scope and areas of improvement in Indo-Nepal trade relations. In brief he discussed on the economic relationship between Nepal and India accompanied by an overview of economic reforms & macro-economic performance of the both countries. It has also been made an effort to analyze the impact of the bilateral treaties with the focus on treaties of 1990s onward realizing the significant role to be played by the trade-points in the future towards the development of bilateral and multilateral trade.

Regmi *(2008)* in his paper ***Indo-Nepal Trade: A Quantitative Analysis*** has been made to empirically analyze the Indo-Nepal trade position, using market share analysis, dependency ratio, trade intensity, complimentarity and country bias indices, degree of horizontal trade, comparative advantage, similarity index and intra-industry trade. India is losing Nepal as the target market whereas Nepal has barely maintained its share in India. Owing to the existence of poor complementarity, Nepal's export composition could not match to that of import composition of India. Among the commodities that Nepal has comparative advantage, India has tended to remain the potential market only for a few commodities. Despite a shift in export composition, there is no possibility of horizontal trade between Nepal and India. The existing intra-industry trade linkages between these two countries are also very poor. In addition, the partial complementarity in export-import structures and the competitive export structure suggests that the prosperous expansion of trade between these countries can be achieved through vertical trade, harmonization of production structures, and change in trade and industrial policies.

Pant & Pant *(2009)* in their paper ***Export Diversification and Competitiveness: Nepal's Experience*** has stated Nepal's policy regime has not been very instrumental in improving trade competitiveness. Although policy measures have been announced from time to time to identify new exportable products and encourage diversification of export markets, these have hardly been executed.

The challenge for Nepal is complicated by the legacy of the past. Against this perspective, the paper a) examines the export scenario of Nepal and reviews the past studies on the country's export potential; b) illustrates Nepal's competitiveness of the export sector; and c) suggests measure for promoting export diversification and competeveness. Based on the estimation of the real effective exchange rate (REER), this paper shows that the country is gradually losing in competitiveness. Although various studies have demonstrated that Nepal possesses competitive advantage in herbal products, woolen carpets, tea, garments and pashmina, among others, a comprehensive case-by-case analysis of home and host countries trading environment, supply and demand conditions, cost of production, capacity to innovate, as well as its forward and backward linkages should be conducted to translate the export potential to the actual trading opportunities.

The Times of India *(2009)* in the article ***New Indo-Nepal trade treaty comes to life*** states that the ministers of India and Nepal signed a new bilateral trade treaty in Kathmandu, which comes into effect immediately offering an upgraded seven-year pact with proviso for automatic renewal every seven years, cutting down red tape and opening a new port as well as land and air routes to Nepal. The news stated the new treaty will have seven-year validity instead of the earlier five years and will be extended automatically every seven years, creating a "stable framework for bilateral trade and investment".

Bashyal *(2066)* in his article ***Nepal's Trade Expansion among SAARC Countries and Regional Trading Arrangements*** has concluded that through beginning of 1990s witnessed the liberalization process of economics in most of the developing nations, the trade expansions under the rule-based system is focused after the establishment of WTO in the mid 1990s. An underdeveloped country like Nepal should undertake a two-track strategy, i.e. multilateral trade negotiations under the WTO and the meaningful regional trading arrangements like SAFTA. A march from SAPTA to SAFTA is an important step for trade expansion among SAARC countries. Nepal's trade with other countries in the region depends on transit facilities provided by India. Restrictive trade policies also cause a low level of intra-regional trade mainly on export trade. However, it would be beneficial if the member states aim at further deepening and widening of the existing arrangements as well as exploring some other possible initiatives like cross-border infrastructural linkages for the expansion of regional markets beyond the SAARC region.

Karkee *(2010)* in his thesis ***Nepal-India Bilateral Trade Relations-Problems And prospects*** has found that the rate of export to India is not same trend. And import from India is also slowly decreasing trend. He found that in the overall foreign trade of Nepal, India occupied very large space in both import & export sector. He found the geographical situation of Nepal is the main barrier for the foreign trade. He argues for the development of hydro-electricity, mines & minerals production, tourism industry development & expansion of information & technology based industries to reduce the trade deficit.

Jha *(2011)* in his paper ***India's Economic Miracle and its Impact on Nepal*** has stated that in such moments of economic breakdown, there has been a growing Indian concern not only about the health of the Indian investment in Nepal but also about the investment climate in the country. The Indian investors in general feel quite insecure to make an investment in Nepal as the business environment in the country has been badly shattered mostly due to the frequent *bandhs*, prevailing culture of strikes, labour disputes, forced donations, poor law and order situation and above all the continuing political instability in the country. He added that Nepal could not benefit that much from India's fast economic growth with market of 1.21 billion populations, despite the significant level of privileges made available by India to Nepal. Therefore, more and more engagement is required at business to business (B&B) level to dig out potential opportunities, promote information dissemination, and organize trade fairs, exhibitions and different other business activities. Nepal could, of course, concentrate on investment in areas in which it has comparative advantage over India.

Shashi *(2011)* in his article ***Jatahiaai Mul Bhansar Maanayta Dinaa Maag*** has discussed on one and only custom between Janakpur (Nepal) & Jayanagar (India). Due to the regular obstacle in Janakpur-Jayanagar Railway, the local businessmen have asked the government to validate the Jatahi Custom of Dhanusha. He has stated that there are 8 sub-customs operating in Janakpur. The article states that the Indian side has constructed the custom points and office at the Jatahi Custom on their side. The main reason to ask for the Jatahi Custom is the irregularities in the operation of the Janakpur-Jayanagar Railway.

CHAPTER-III

RESEARCH METHODOLOGY

This chapter presents the short outline of the methods applied in the process of analyzing the Foreign Trade Nepal with India is a systematic method of finding out solution to a problem whereas research methodology refers to the various sequential steps to adopt by a researcher in studying a problem with certain objective in view.

3.1. Research Design:

The study is designed in order to evaluate the foreign trade with the neighboring country, India.

The study especially deals with the depth analysis will be descriptive and analytical in order to answer the problem identified. Similarly, it will be guideline for future researcher.

3.2. Sources of Data:

The data used in the research are secondary in nature gathered from the published reports by government agencies.

Required data and information is collected by using the government published data as per the research objective-oriented. Similarly, the questionnaires have been used to collect the primary data needed for the research purpose.

3.3. Data Collection Methods:

The data published by the Government of Nepal in the past years has been made basis for the research purpose. Only the foreign trade related data with the neighboring country, India has been picked up for the research purpose. The sample of 50 respondents have been taken for the research purposes.

3.4. Data Processing Techniques:

The collected data have been processed and tabulated in the forms of table. Graphs and diagrams are presented after data are processed. Similarly, further statistical analysis has been done to interpret the data in the research.

3.5. Tools Used:

Various statistical tools have been used to interpret the raw data for the research purpose. The statistical tool used to analyze the data in the report is:

3.5.1. T-test:

To test the validity of our assumption, if the sample size is less than 30, t-test is used. For applying t-test in context of small sample the t-value is calculated first and compared with the t-value on table at certain level of significance for given degree of freedom. If calculated value of “t” exceeds the table value (say 0.05) we can say that the difference is significant at 5% level, but if calculated value is less than the concerning values the difference is not treated as significant. The value is calculated by using following formula:

$$\therefore t = \frac{r}{\sqrt{1-r^2}} \times \sqrt{n-2}$$

Where, r= Correlation Coefficient

3.5.2. Diagrammatic Presentation:

Graphic presentation is a power full and effective way for highlighting variable. A very common way of presenting data for two variables which have a relationship is in a figure or chart. For the presentation of the data, the multiple bar diagram, percentage bar diagram and line graph has been in the report.

CHAPTER-IV

PRESENTATION & ANALYSIS OF DATA

4.1. Total Trade Volume of Nepal:

The total volume of Nepal foreign trade with the neighboring country, India & other countries is tabulated below:

Table No.4.1.

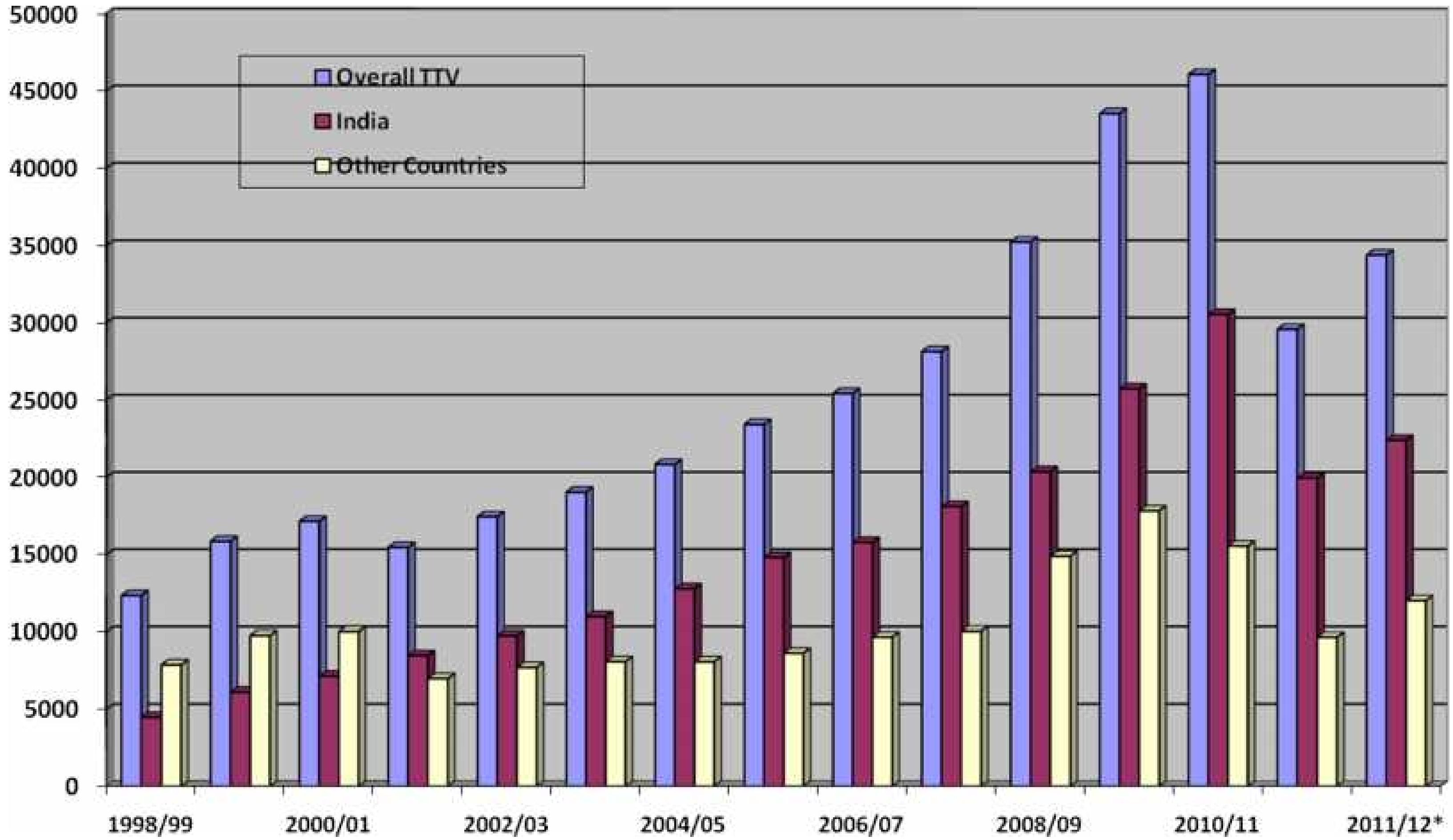
Total Trade Volume of Nepal

F/Y	Overall TTV	India	Other Countries
1998/99	12320.16	4465.04	7855.12
1999/2000	15832.76	6088.08	9744.68
2000/01	17134.13	7124.12	10010.01
2001/02	15433.38	8457.83	6975.55
2002/03	17428.27	9735.42	7692.85
2003/04	19018.78	10951.66	8067.12
2004/05	20817.93	12759.24	8058.69
2005/06	23401.44	14785.78	8615.66
2006/07	25407.77	15760.11	9647.66
2007/08	28120.42	18093.22	10027.20
2008/09	35216.71	20344.35	14872.36
2009/10	43515.92	25710.80	17805.12
2010/11	46051.40	30528.56	15522.84
2010/11*	29567.56	19925.86	9641.70
2011/12*	34380.46	22386.75	11993.71

Source: Economic Survey 2011/12*, MOF/GON

Figure No.4.1.

Total Trade Volume of Nepal



Source: Economic Survey 2011/12*, MOF/GON

The volume of the overall trade of Nepal with India as well as with other countries is seen increased heavily in the past decade. Especially, the volume of trade with India is seen heavily increased in the past decade.

Lack of industrialization, poor economic development, Nepal is fully being dependent towards the huge neighboring countries India & China. Traditionally also, Nepal's foreign trade was deviated towards these two countries. At present also, the large bulk of trade of Nepal is with these two countries. Being a landlocked country, Nepal is fully dependent on India to get the access to trade with the third county. Geographically, also the limited access to China in the northern border also made Nepal to highly depend on India.

From the F/Y 2002/03, the total volume of the trade of Nepal is seen consistently increasing every year. In the F/Y 1995, the volume of trade with India & other countries were at Rs. 2808.12 thousands & Rs. 6625.44 thousands but from F/Y 2001/02 the situation was just opposite & the volume was at Rs.8457.83 thousands for India & Rs.6975.55 thousands for other countries.

The volume of trade with India during the first eight months of the F/Y 2010/11* was Rs.19925.86 thousands and it was at Rs. 22386.75 during the first eight months of the F/Y 2011/12*.

4.2. Proportion of Total Trade Volume of Nepal:

The total trade of Nepal is segregated into the trade with India & the trade with the remaining other counties of the world. The proportion of trade volume of Nepal with India & other countries are as follow:

Table No.4.2.

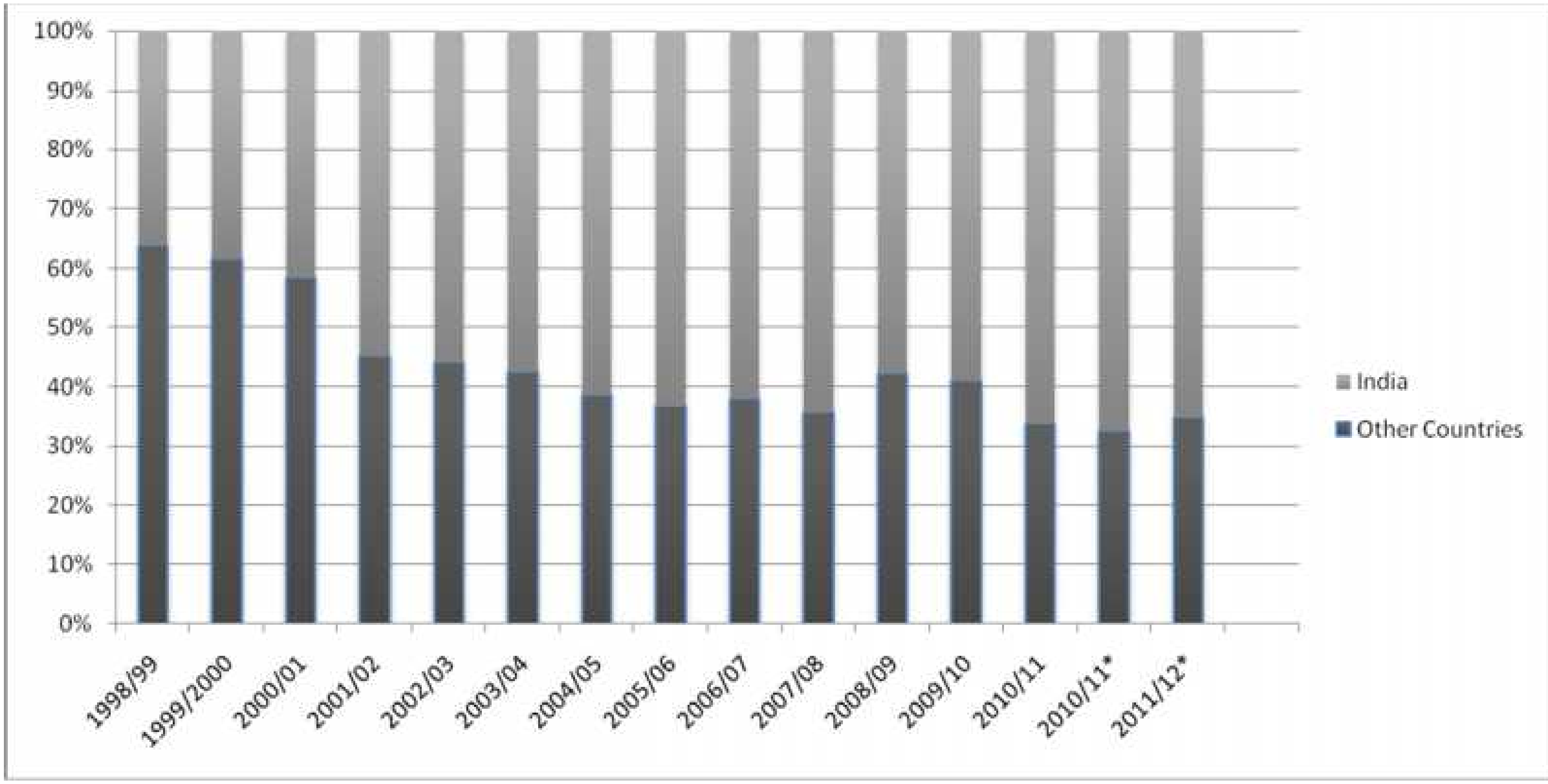
Proportion of Total Trade Volume of Nepal

F/Y	Overall TTV	India	Other Countries
1998/99	100%	36.20%	63.80%
1999/2000	100%	38.5%	61.5%
2000/01	100%	41.6%	58.4%
2001/02	100%	54.80%	45.20%
2002/03	100%	55.86%	44.14%
2003/04	100%	57.58%	42.42%
2004/05	100%	61.29%	38.71%
2005/06	100%	63.18%	36.82%
2006/07	100%	62.03%	37.97%
2007/08	100%	64.34%	35.66%
2008/09	100%	57.77%	42.23%
2009/10	100%	59.08%	40.92%
2010/11	100%	66.29%	33.71%
2010/11*	100%	67.39%	32.61%
2011/12*	100%	65.11%	34.89%

Source: Economic Survey 2011/12*, MOF/GON

Figure No.4.2.

Proportion of Total Trade Volume of Nepal



Source: Economic Survey 2011/12*, MOF/GON

The proportion of trade volume of Nepal has completely changed its picture in the last decade. The rate of trade with the other countries was more than 70% during the F/Y 1995/96. But the rate has been reversed and it was 64.34% for India & 35.66% for other countries in the F/Y 2007/08.

The ratio of trade with India & other countries of Nepal was reversed form the F/Y 2001/02. The proportion of trade with India went to 54.80% & with other countries at 45.20%. Just a year earlier the ratio was 41.6% for India & 58.4% for other countries.

The ratio of trade with India of Nepal during the first eight months of the F/Y 2011/12* covered more than 65% of the trade volume of the country.

Due to the high dependency of trade with India, the Nepal trade has been increasing every year. The long open borders the new trade policy and treaty with India has also facilitate to increase the proportion of trade with India.

4.3. Export F.O.B from Nepal to India:

The trade relation with the neighboring country, India is very old. The major trade partner of Nepal in the past was also either India or an autonomous region of China, Tibet. The following table shows the export from Nepal to India:

Table No.4.3.

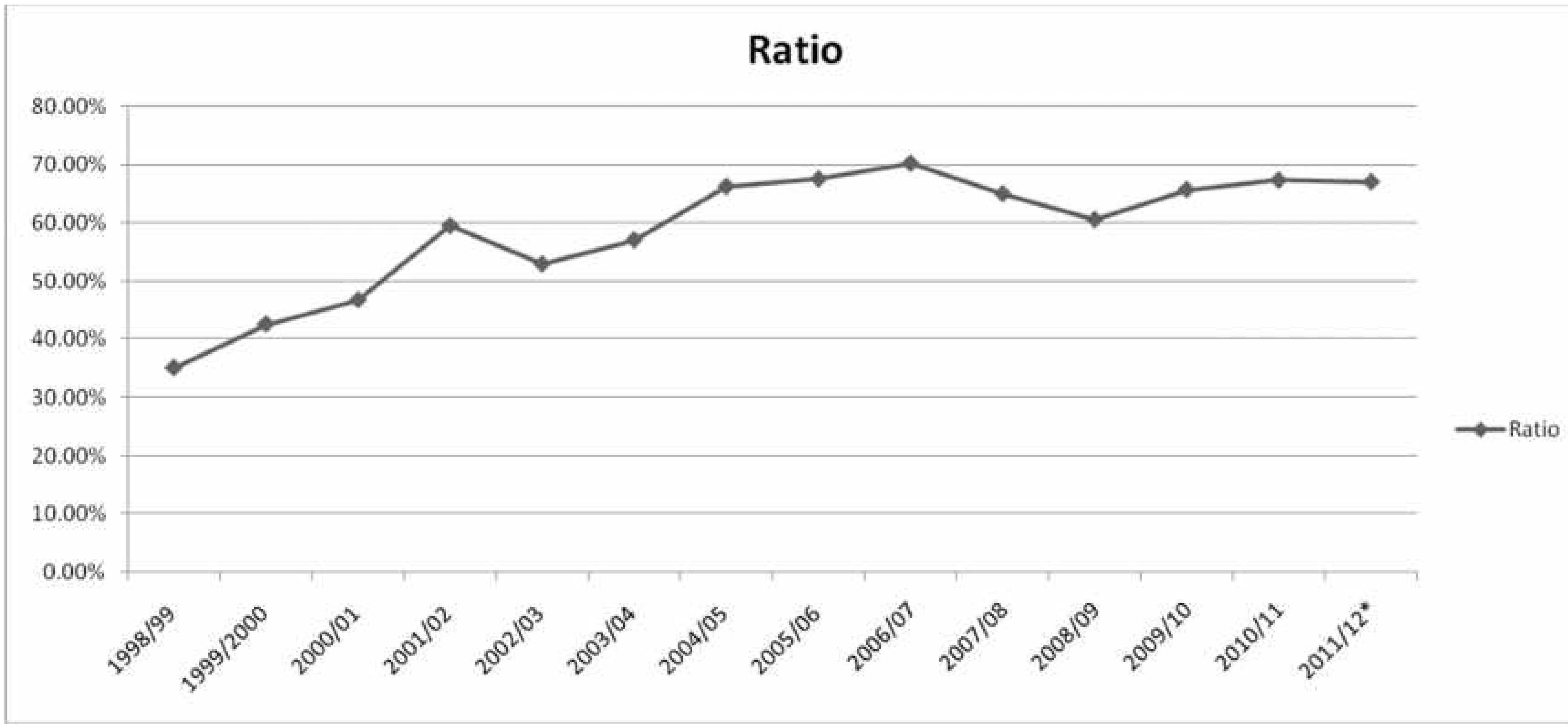
Export F.O.B from Nepal to India

F/Y	Total	India	Ratio
1998/99	3567.63	1253.07	35.12%
1999/2000	4982.27	2122.07	42.59%
2000/01	5565.41	2603.02	46.77%
2001/02	4694.48	2795.62	59.55%
2002/03	4993.06	2643.00	52.93%
2003/04	5391.07	3077.71	57.08%
2004/05	5870.57	3891.69	66.29%
2005/06	6023.41	4071.47	67.59%
2006/07	5938.31	4172.88	70.27%
2007/08	5926.65	3855.57	65.05%
2008/09	6769.75	4100.59	60.57%
2009/10	6082.40	3999.37	65.75%
2010/11	6433.85	4336.04	67.39%
2011/12*	4856.26	3259.27	67.11%

Source: Economic Survey 2011/12*, MOF/GON

Figure No.4.3.

Ratio of Export F.O.B from Nepal to India



Source: Economic Survey 2011/12*, MOF/GON

India has been the major trade partner from the ancient time. And at present also, it is a major trade partner of Nepal. Nepal is fully dependent on India in the foreign trade. The country is importing goods of day-to-day needs to heavy machineries from India.

Due to no access to the marine transit to Nepal & geographical difficulties to access the market of China, Nepal has also made a major market to India for trading its certain domestic products.

Similarly, some of the multinational companies of India have established the industry in Nepal & the products produced from these industries are exported to the India.

The ratio of export F.O.B. from Nepal to India is also seen in increasing trends. The ratio was at only 18.52% in the F/Y 1995/96 & it start to increase tremendously and reached up to 70.27% in the F/Y 2006/07. This might be a good sign for Nepal to increase in the export to India, which might slightly help to reduce the huge amount if trade deficit facing by the country.

The volume of export ot India from Nepal has improved slightly during the first eight month of the F/Y 2011/12*. The ratio has remained at the 67.11%.

4.4. Import C.I.F. from India to Nepal:

The major trade partner of Nepal has been the neighboring country, India. The country is dependent on India for the basic needs goods to heavy equipment. The amount of import from India has been tabulated below:

Table No.4.4.

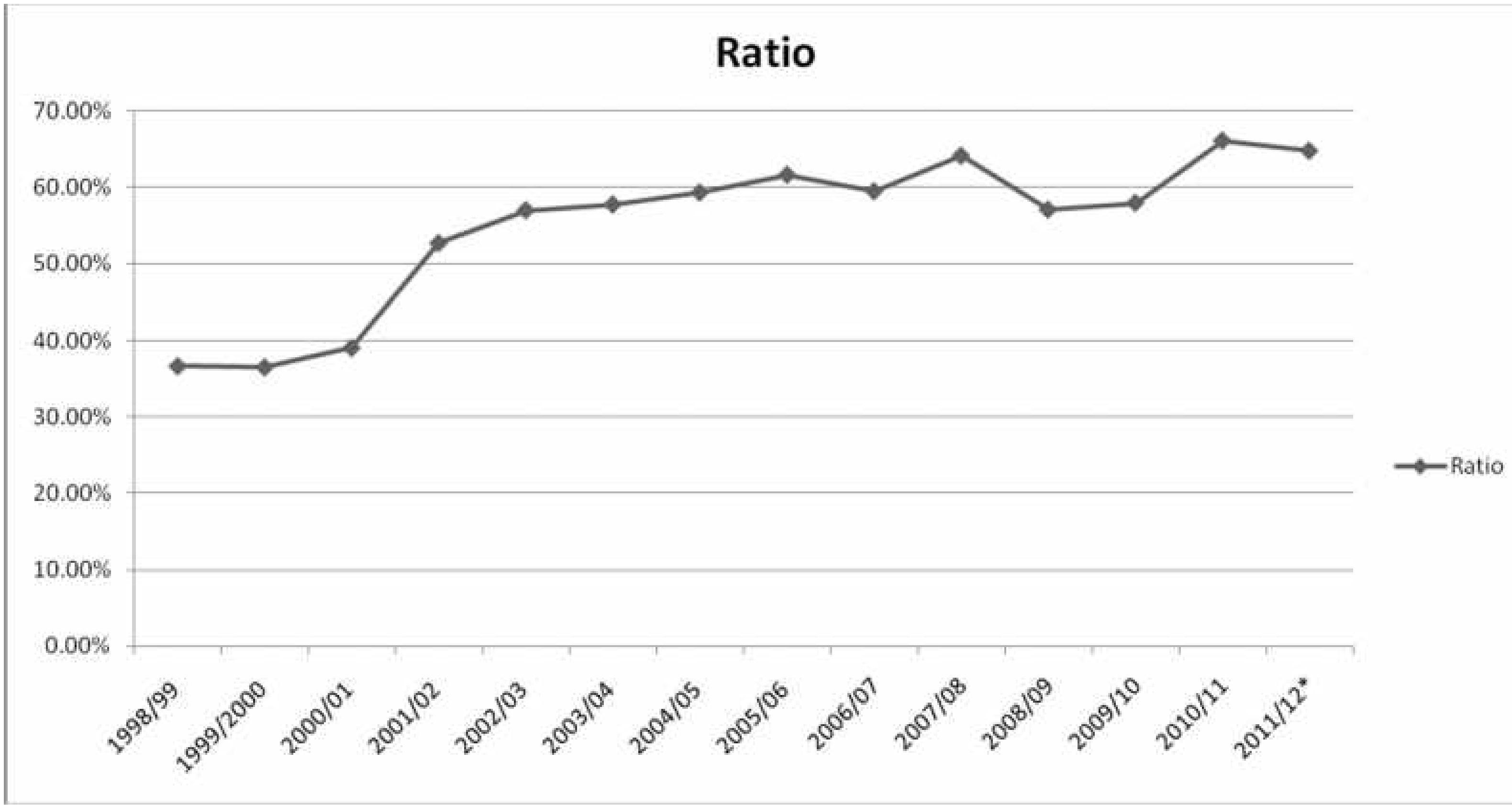
Import C.I.F. from India to Nepal

F/Y	Total	India	Ratio
1998/99	8752.53	3211.97	36.70%
1999/2000	10850.49	3966.01	36.55%
2000/01	11568.72	4521.10	39.08%
2001/02	10738.90	5662.21	52.73%
2002/03	12435.21	7092.42	57.03%
2003/04	13627.71	7873.95	57.78%
2004/05	14947.36	8867.55	59.33%
2005/06	17378.03	10714.31	61.65%
2006/07	19469.46	11587.23	59.51%
2007/08	22193.77	14237.65	64.15%
2008/09	28446.96	16243.76	57.10%
2009/10	37433.52	21711.43	57.99%
2010/11	39617.55	26192.52	66.11%
2011/12*	29524.20	19127.48	64.79%

Source: Economic Survey 2011/12*, MOF/GON

Figure No.4.4.

Ratio of Import C.I.F. from India to Nepal



Source: Economic Survey 2011/12*, MOF/GON

Due to the low level of industrialization of the country, Nepal is fully dependent on the import of majority of the commodities. There is limited level of production of necessary goods in Nepal. Only certain agro-based commodities are produced within the country but that are also not sufficient for the population.

In the last decade Nepal could improve in the level of industrialization due to political instability & low economic growth rate. Thus, the gross domestic products from the industrial sector remain very poor. The country became more and more dependent on import of commodities.

The major reason to increase in the import amount from the neighboring country, India for Nepal is the fully dependency of petroleum products import. A liter of petroleum is also should be imported from India by Nepal. This has also caused the large amount of the import amount in context between India & Nepal.

The import C.I.F. from India to Nepal has been increasing tremendously in a last decade but slight improvement was seen from the F/Y 2008/09. The import was seen declined in this F/Y to 57.10%.

In F/Y 1996/97, the import C.I.F. from India to Nepal was only 26.57% in the F/Y 1996/97. But it reached three-fold in the recent years.

4.5. Trade Balance of Nepal with India:

The trade balance is the difference between the amount of export & import of goods & services. The following table shows the trade balance of Nepal with India:

Table No.4.5.

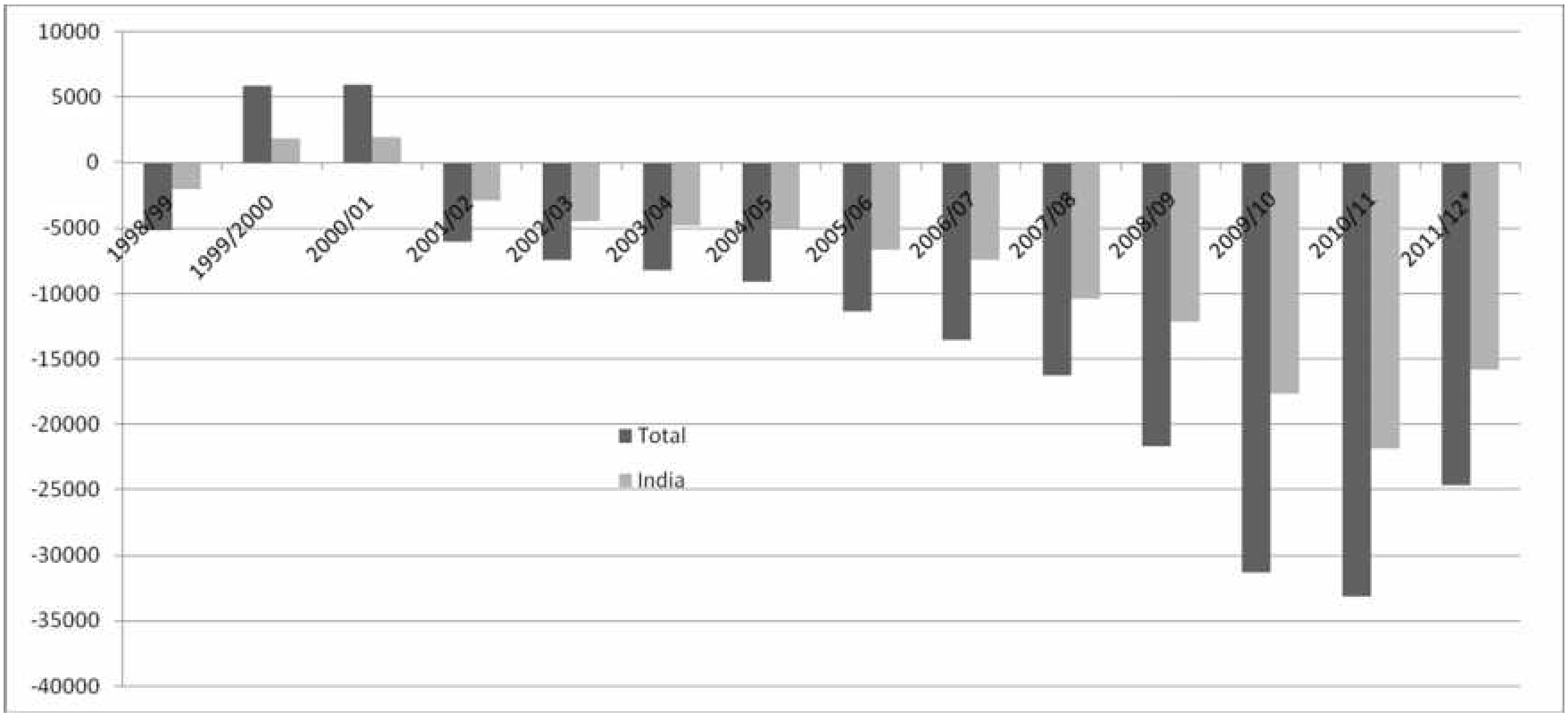
Trade Balance of Nepal with India

F/Y	Total	India	Ratio
1998/99	-5184.90	-1958.90	37.78%
1999/2000	5868.22	1843.94	31.42%
2000/01	6003.31	1918.08	31.95%
2001/02	-6044.42	-2866.59	47.43%
2002/03	-7442.15	-4449.42	59.79%
2003/04	-8236.64	-4796.24	58.23%
2004/05	-9076.79	-4975.86	54.82%
2005/06	-11354.62	-6642.84	58.50%
2006/07	-13531.15	-7414.35	54.79%
2007/08	-16267.12	-10382.08	63.82%
2008/09	-21677.21	-12143.17	56.02%
2009/10	-31351.12	-17712.06	56.50%
2010/11	-33183.70	-21856.48	65.87%
2011/12*	-24667.94	-15868.21	64.33%

Source: Economic Survey 2011/12*, MOF/GON

Figure No.4.5.

Trade Balance of Nepal with India



Source: Economic Survey 2011/12*, MOF/GON

Trade balance is the difference between the total exported amount and the total imported amount. Normally, it is expected to be the positive trade balance of any country, i.e. the amount of total exported amount should be higher than the total imported amount. This situation is said to be the surplus trade balance & the reciprocal is said as the deficit trade balance.

In the majority of the years, Nepal is facing the trade deficit with India except the F/Y 1999/2000 & F/Y 2000/01. In these two F/Y, the trade balance with India is seen surplus.

The amount of import from India to Nepal is always high than the export from Nepal to India. As being a neighboring country of Nepal with a long open border, the trade is at a large scale every year. The imported goods contain from the basic day-to-day commodities to heavy plant and machineries.

As the production within the country is not sufficient for the population, so, the agro-based products are also imported from India.

The importance of trade of Nepal with India can be stated in such way that when a trade surplus with India was seen the overall balance of trade of Nepal was seen surplus & vice-versa.

4.6. Opinion on Dependency of Trade of Nepal with India:

Table No.4.6.

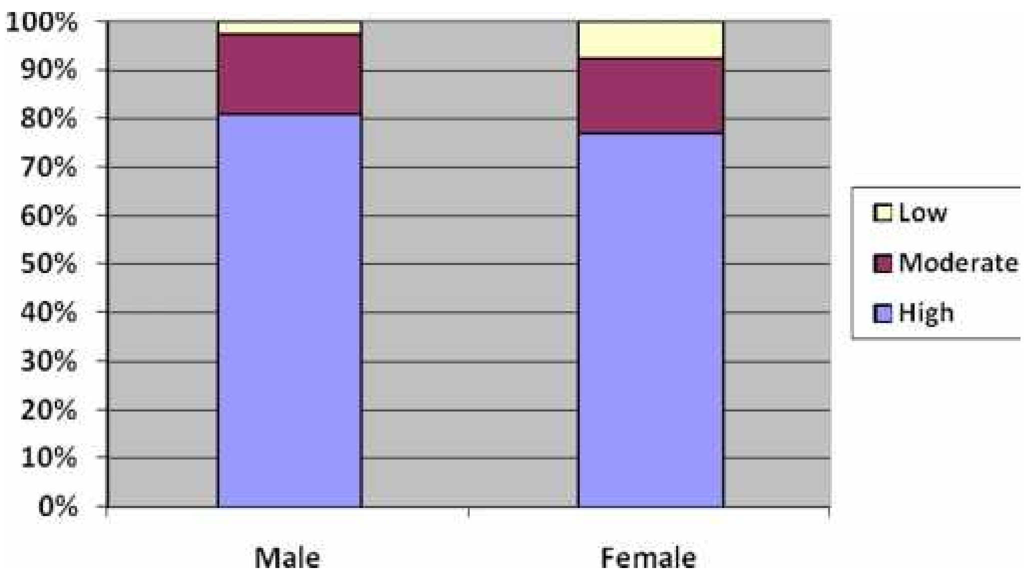
Opinion on Dependency of Trade of Nepal with India

Opinion	**Male**	**Ratio**	**Female**	**Ratio**
High	30	81.08%	10	76.92%
Moderate	6	16.22%	2	15.38%
Low	1	2.76%	1	7.70%
Total	**37**	**100%**	**13**	**100%**

Source: Field Survey

Figure No.4.6.

Opinion on Dependency of Trade of Nepal with India



Majority of the both the male and female respondents stated that the trade dependency of Nepal is high with India. More than 80% & 76% of the total male and female respondents respectively stated that the dependency of the Nepal's trade with India is high.

4.7. Opinion on Impact on Trade with India in Nepalese Economy:

Table No.4.7.

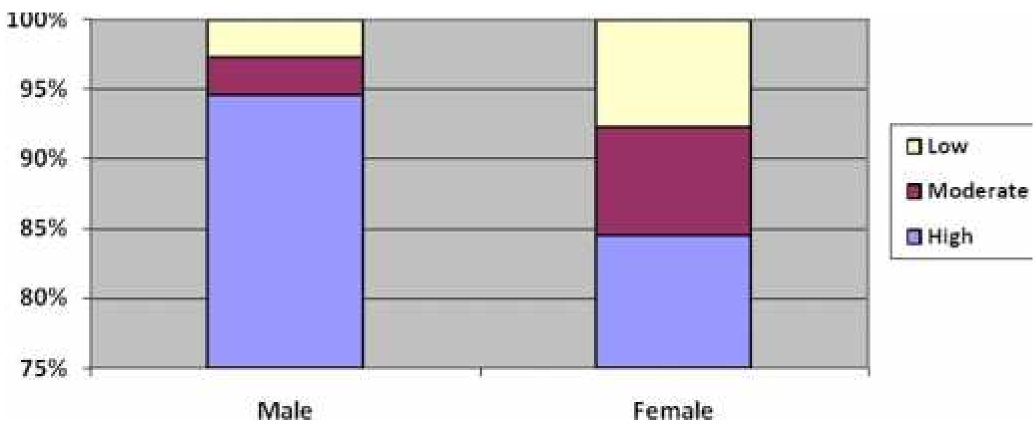
Opinion on Impact on Trade with India in Nepalese Economy

Opinion	Male	Ratio	Female	Ratio
High	35	94.59%	11	84.62%
Moderate	1	2.70%	1	7.70%
Low	1	2.70%	1	7.70%
Total	**37**	**100%**	**13**	**100%**

Source: Field Survey

Figure No.4.7.

Opinion on Impact on Trade with India in Nepalese Economy



Majority of the both the male and female respondents stated that there is a high impact of the trade of Nepal with India in an overall economy of the country. More than 90% of the total male respondents stated that there is a high impact in the overall economy of Nepal. Similarly, about 85% of the total female respondents stated that there is a high impact in the overall economy of Nepal by the trade volume and amount with India.

4.8. Reasons for High Trade Dependency of Nepal with India:

Table No.4.8.

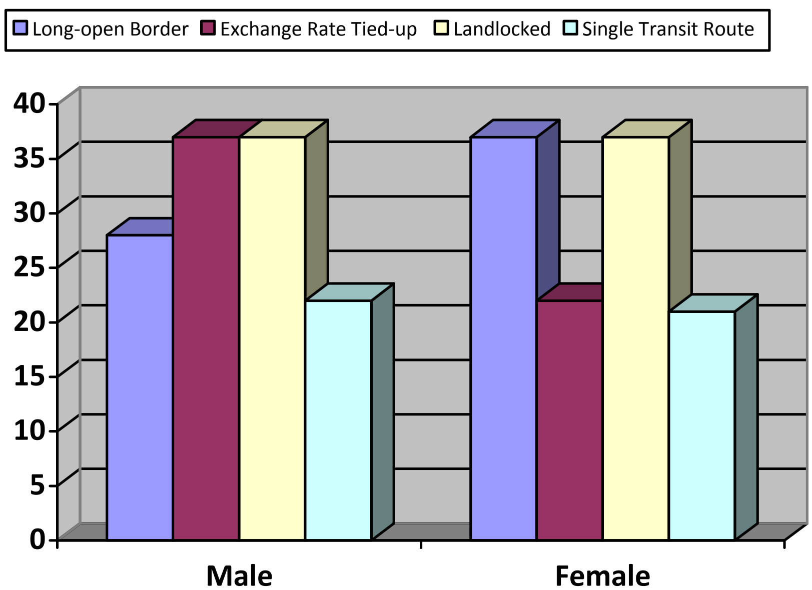
Reasons for High Trade Dependency of Nepal with India

Opinion	Male	Female
Long-open Border	28	37
Exchange Rate Tied-up	37	22
Landlocked	37	37
Single Transit Route	22	21

Source: Field Survey

Figure No.4.8.

Reasons for High Trade Dependency of Nepal with India



The male respondents stated the exchange rate tied-up and landlocked of the country as the main reasons behind the high dependency of the Nepal's trade with the neighboring country, India. The female respondents stated the long-open border and landlocked of the country as the main reasons behind the high dependency of the Nepal's trade with India. The other reason behind the dependency of trade with India was single transit route for third country trade of Nepal.

4.9. Test of Hypothesis:

4.9.1. Test on Correlation between the Trade between India & Overall Trade of Nepal:

Null Hypothesis (H_0): $\rho=0$, i.e. the variables in the population are uncorrelated.

Alternative Hypothesis (H_1): $\rho\neq0$, i.e. the variables in the population are correlated. (two-tailed test)

Decision: Since the calculated value of t is greater than tabulated value of t, the alternative hypothesis, H_1 is accepted. Hence, the variables in the population are correlated. ***Source: Annex-I***

4.10. Major Findings:

The major findings of the study are pointed out below:

i. In the F/Y 1995, the volume of trade with India & other countries were at Rs. 2808.12 thousands & Rs. 6625.44 thousands but from F/Y 2001/02 the situation was just opposite & the volume was at Rs.8457.83 thousands for India & Rs.6975.55 thousands for other countries.

ii. The rate of trade with the other countries was more than 70% during the F/Y 1995/96. But the rate has been reversed and it was 64.34% for India & 35.66% for other countries in the F/Y 2007/08.

iii. The ratio of export F.O.B. from Nepal to India is also seen in increasing trends. The ratio was at only 18.52% in the F/Y

1995/96 & it start to increase tremendously and reached up to 70.27% in the F/Y 2006/07.

iv. The import C.I.F. from India to Nepal has been increasing tremendously in a last decade. In F/Y 1996/97, the import C.I.F. from India to Nepal was only 26.57% in the F/Y 1996/97. But it reached two-fold in the recent years.

v. In the majority of the years, Nepal is facing the trade deficit with India except the F/Y 1999/2000 & F/Y 2000/01. In these two F/Y, the trade balance with India is seen surplus.

vi. More than 80% & 76% of the total male and female respondents respectively stated that the dependency of the Nepal's trade with India is high.

vii. Majority of the both the male and female respondents stated that there is a high impact of the trade of Nepal with India in an overall economy of the country.

viii. The male respondents stated the exchange rate tied-up and landlocked of the country as the main reasons behind the high dependency of the Nepal's trade with the neighboring country, India. The female respondents stated the long-open border and landlocked of the country as the main reasons behind the high dependency of the Nepal's trade with India.

ix. The trade between India & overall trade of Nepal is seen correlated from the test of hypothesis.

CHAPTER-V

SUMMARY & CONCLUSION

5.1. Summary:

International trade is in principle not different from domestic trade as the motivation and the behavior of parties involved in a trade do not change fundamentally regardless of whether trade is across a border or not. The main difference is that international trade is typically more costly than domestic trade.

Nepal is a landlocked nation, surrounded by India on 3 sides and by Tibet (now a province of China) in the north. Historically, international trade before the 1950s was with these countries. Exports have consisted of primary agricultural produce, while everything not produced locally has been imported. Throughout the years of development, these imports have included industrial inputs, fertilizers, and petroleum.

Nepal is China-locked in the North. However, Chinese ports are about 5,000 km away from Nepalese border. The snowy range of Himalaya stands as a transit barrier between these two countries. Tibet, which is one of the nearest neighbors, is just in the earliest stage of its economic development. Nepal has transit agreement with Bangladesh also; it is about 16 kms away compared to Calcutta port. Therefore, Nepal has no alternative transit route for its cargo except India's Calcutta port, which provides very poor physical facilities to Nepal traders.

Nepal's merchandise trade balance has improved somewhat since 2000 with the growth of the carpet and garment industries. In FY

2000/01 exports posted a greater increase (14%) than imports (4.5%), helping bring the trade deficit down by 4% from the previous year to $749 million. Recently, the European Union has become the largest buyer of Nepali readymade garments (RMG). Exports to the EU accounted for "46.13 percent of the country's total garment exports".

The annual monsoon rain, or lack of it, strongly influences economic growth. From 1996 to 1999, real GDP growth averaged less than 4%. The growth rate recovered in 1999, rising to 6% before slipping slightly in 2001 to 5.5%.

Strong export performances, including earnings from tourism, and external aid have helped improve the overall balance-of-payments situation and increase international reserves. Nepal receives substantial amounts of external assistance from the United Kingdom, the United States, Japan, Germany, and the Scandinavian countries. Several multilateral organizations, such as the World Bank, the Asian Development Bank, and the UN Development Programme also provide assistance. In June 1998, Nepal submitted its memorandum on a foreign trade regime to the World Trade Organization and in May 2000 began direct negotiations on its accession

The diversification in the foreign trade of the country has not been feasible in context to Nepal after being the member of WTO. The country has not been capable to get benefit in the economy directly or visible through the membership of the WTO. Still, the foreign trade is highly concentrated with the neighboring country, India. The trade with a third country is seen not so diversified still today also. The traditional trade partners have been remained same.

The regular trend of a growing deficit in Nepal's trade with India is an outcome of high amount of the negative balance of payment between the two countries. The increasing amount of the import volume from India to Nepal has made Nepal to use the other foreign currencies to purchase Indian currency which has directly hampered in the balance of payment of the country.

Thus, the transit points of India become the most valuable for Nepal. As well as the trade volume with India is the highest among the trade partners of Nepal.

5.2. Conclusion:

The trade relation with India and Nepal is very old. There is a historical background as well as the trade-relations with these two countries. The Indo-Nepal relation is really an exceptional bilateral relation of the country in the world.

Due to long open border with India and Nepal as well as the cultural tie-up between the citizens of the two nations, the relation is completely patched up.

Relations between India and Nepal are close yet fraught with difficulties stemming from geography, economics, and the problems inherent in big power-small power relations, and common ethnic and linguistic identities that overlap the two countries' borders. In 1950 New Delhi and Kathmandu initiated their intertwined relationship with the Treaty of Peace and Friendship and accompanying letters that defined security relations between the two countries, and an agreement governing both bilateral trade and trade transiting Indian soil. The 1950 treaty and letters stated that "neither government shall tolerate any threat to the security of the other by a foreign aggressor" and obligated both sides "to inform each other of any serious friction or misunderstanding with any neighboring state likely to cause any breach in the friendly relations subsisting between the two governments." which granted the Indian and Nepali People don't mandatory to have Work permit for any economic activity such as work and business related activity. These accords cemented a "special relationship" between India and Nepal that granted Nepal preferential economic treatment and provided Nepalese in India the same economic and educational opportunities as Indian citizens.

As stated earlier, the trade relation of Nepal with India is completely dependable. The volume of the trade of Nepal with India is increasing every year. In the F/Y 1995, the volume of trade with India & other countries were at Rs. 2808.12 thousands & Rs. 6625.44 thousands but from F/Y 2001/02 the situation was just opposite & the volume was at Rs.8457.83 thousands for India & Rs.6975.55 thousands for other countries. The ratio of trade with India & other countries of Nepal was reversed form the F/Y 2001/02. The proportion of trade with India went to 54.80% & with other countries at 45.20%. Just a year earlier the ratio was 41.6% for India & 58.4% for other countries.

The import from India to Nepal as well as export to India from Nepal volume and proportion are also seen increased heavily in the recent years. This shows the heavy dependency of foreign trade of Nepal with a neighboring country India.

The trade balance of the country will be either surplus or deficit. If the import in the country is higher than the export from the country, the trade is considered deficit and vice versa. In the majority of the years, Nepal is facing the trade deficit with India except the F/Y 1999/2000 &

F/Y 2000/01. In these two F/Y, the trade balance with India is seen surplus.

Most of the respondents respectively stated that the dependency of the Nepal's trade with India is high. Majority of the both the male and female respondents stated that there is a high impact of the trade of Nepal with India in an overall economy of the country. The exchange rate tied-up and landlocked of the country were the main reasons behind the high dependency of the Nepal's trade with the neighboring country, India. Similarly, the long-open border of the country has also seen the reason behind the high volume trade of Nepal with India.

Recently, the new agreement between India and Nepal is signed during the visit of the Prime Minister of Nepal. The Bilateral Investment Promotion and Protection Agreement (BIPPA) have been signed by the two sides for the promotion and the protection of the trade between India & Nepal. This brings to a close days of hectic negotiations and speculations over the fate of BIPPA, which India has sought to protect security for its investments in Nepal. Provisions have also been made in the agreement for grant of compensation to the investors whose investments suffer losses owing to war, armed conflict and a state of national emergency. A section of the bureaucracy had expressed reservations over this provision, fearing that it could lead to huge liabilities to the Nepali state. According to a Nepali official, many more issues will be covered in a joint communiqué.

5.3. Recommendations:

i. There is a need for the trade diversification for Nepal as soon as possible.

ii. The trade and transit treaty with India should be revised as per the current situation as soon as possible.

iii. The Birgunj Dry Port should be run effectively and efficient to reduce the transit cost for the Nepalese importer.

iv. The settlement for the tax payment in India by the Nepalese businessmen should be made smoother.

v. Effective agreement should be made with India & Bangladesh to run the Fulbari transit points to diversify the trade with Bangladesh as well.

vi. Major steps should be taken to promote the export-based industries to reduce the trade deficit.

vii. Promotion for the agro-based and small-scale industries should be done to boost the export of the country.

viii. Multinational companies of India should bring in Nepal to utilize the resources of Nepal & export towards the India and other countries.

ix. The concept of entrapot should be developed by the Nepalese traders to boost the foreign trade of the country.

x. Strict custom regulations should be developed to increase the revenue from the foreign trade.