

THE ECONOMIC DIPLOMACY OF NEPAL

(From FY 2000/01 to FY 2008/09)

A Dissertation

Submitted to the Central Department of Economics, Faculty of Humanities

and

Social Sciences in Partial Fulfillment of the Requirements

for the Degree of

MASTERS OF ARTS

in

ECONOMICS

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September, 2009

LETTER OF RECOMMENDATION

This dissertation entitled “**The Economic Diplomacy of Nepal: From FY 2000/01 to FY 2008/09**” has been prepared by Mr. Ashok Adhikari under my supervision and guidance. I hereby recommend this thesis for examination by the Dissertation Committee as a partial fulfillment of the requirements for the Degree of Master of arts in ECONOMICS.

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APPROVAL LETTER

We certify that this dissertation entitled “**The Economic Diplomacy of Nepal: From FY 2000/01 to FY 2008/09**” submitted by Mr. Ashok Adhikari to the Central Department of Economics, Faculty of Humanities and Social Sciences, Tribhuvan University, in partial fulfillment of the requirements for the Degree of MASTER OF ARTS in ECONOMICS has been found satisfactory in scope and quality. Therefore, we accept this dissertation as a part of the said degree.

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ACKNOWLEDGEMENTS

First of all, I would like to express my sincere and deep gratitude to my Supervisor Lecturer Dadhi Adhikari and for his scholastic guidance, regular encouragement, and invaluable suggestions which proved to be highly important through out the preparation of my dissertation. I have no adequate words to thank him from the core of my heart. I am also thankful to Prof. Dr. Devendra Prasad Shrestha, Head of the Department and Prof. Dr. Madhavi Singh Shah, former Head of the Department for their administrative help during the thesis preparation.

I am grateful to my friends, Mr. Raghu Nath Dhital, Mr. E.N. Paudel, Mr. Sunil KC and Mr. Ganesh Kunwar for their continuous help and advices. I also would like to thank my elder brother Nabin Adhikari for his countless helps, and special and warmest thanks to my wife Mrs. Rita Bimali Adhikari without whose efforts and help I could not have completed my dissertation.

I take this opportunity to record my sense of gratitude to all those writers and publishers who were the source of inputs for the preparation of this dissertation. Also I would like to thank all my friends and the staffs of Central Department of Economics as well as other people who are directly or indirectly involved in the process of my thesis preparation.

Finally, I am deeply indebted to my dear parents and other family members for their continuous support and encouragement for the completion of my Masters' Degree in Economics from the Central Department of Economics (CEDECON), Tribhuvan University.

September, 2009

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ACRONYMS

ADB	Asian Development Bank
ASEAN	Association of South East Asian Nations
BIMST-EC	Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation
BIS	Bank of International Settlements
BOP	Balance of Payment
BS	Bikram Sambat
CBS	Central Bureau of Statistics
CIGI	Center for International Governance Innovation
CSIG	Centre for the Study of International Governance
DCs	Developing Countries
DFI	Direct Foreign Investments
EERCC	External Economic Relations and Coordination Committees
ERCD	Economic Relation Coordination Division
EU	European Union
FACD	Foreign Aid Co-ordination Division
FDI	Foreign Direct Investment
FHAN	Federation of Handicrafts Association of Nepal
FITUR	International Tourism Trade Fair
FNCCI	Federation of Nepalese Chambers of Commerce and Industry
FPTF	Foreign Policy Task Force
FTA	Free Trade Agreements
FY	Fiscal Year
FYP	Five Years Plan
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GoN	Government of Nepal
HIV/AIDS	Human Immunodeficiency Virus/ Acquired Immune Deficiency Syndrome
HLTF	High Level Task Force

HMG/N	His Majesty's Government/ Nepal
IBF	International Business Forum
ICAO	International Civil Aviation Organization
ICT	Information and Communication Technology
IDA	International Development Association
IFA	Institute of Foreign Affairs
IMF	International Monetary Fund
INGO	International Non-Governmental Organization
IR	Indian Rupees
IRDO	International Relation Desk Office
ITB	Internationale Tourismus Börse (German Language)
LDCs	Least Developed Countries
MDGs	Millennium Development Goals
MEAD	Multilateral Economic Affairs Division
MITT	Moscow International Travel and Tourism (Exhibition)
MoF	Ministry of Finance
MoFA	Ministry of Foreign Affairs
NAG	Nepal Aid Group
NDF	Nepal Development Forum
NEFT	National Electronic Fund Transfer
NGO	Non-governmental Organization
NLSS	National Living Standards Survey
NRB	Nepal Rastra Bank
NRN	Non Resident Nepalese
NTB	Nepal Tourism Board
ODA	Official Development Assistance
PATA	Pacific Area Travel Agency
PP	Producer's Price
PRGF	Poverty Reduction Growth Facility
PRS	Poverty Reduction Strategy
PRSC	Poverty Reduction Strategy Credit
PSG	Policy Study Group

SAARC	South Asian Association of Regional Cooperation
SAFTA	South Asian Free Trade Area
SANEI	South Asia Network of Economic Institutes
SAPTA	SAARC Preferential Trading Arrangement
SPS	Sanitary and Phyto-sanitary
TBT	Technical Barriers to Trade
TEC	Technical and Economic Cooperation
TU	Tribhuvan University
UK	United Kingdom
UNCITRAL	United Nations Commission on International Trade Law
UNDP	United Nations Development Program
UNO	United Nations Organization
UNWTO	UN World Tourism Organization
US	United States
USA	United States of America
USSR	Union of Soviet Socialist Republics
WB	World Bank
WTO	World Trade Organization
WW-I	First World War
WW-II	Second World War

CHAPTER 1

INTRODUCTION

1.1 General Background

Nepal is a least developed, landlocked and economically vulnerable country with enormous ecological diversity. It is predominantly an agrarian economy, and agriculture is the mainstay of life. The geo-political feature of Nepal is such that it is politically and economically in a 'Razor's Edge' situation. It is evident that the globally emerging powers, India and China and the developed western nations pose a great influence over Nepal's politics and also the economic policies. In such, the stature of Nepalese economy has always been puffed up by the balanced relations among India, China and the Western developed countries regardless of their diverse political ideologies.

In the past, the relationship of Nepal with neighboring and the West nations was usually ascertained with the vested political interest. When the cold war between United States of America (USA) and the then USSR ended, the political interests behind diplomatic ties gradually shifted toward commercial and economic interests. Meanwhile, such a shifting of interest to cooperation, commerce and economy enforced Nepal to reshape its foreign policy. As a result, the concepts of economic diplomacy gained its momentum on acquiring the economic means through bilateral and multilateral ties. The overwhelming development of the concept of globalization in the decades of 80's and early 90's apparently raised the importance of economic diplomacy to a new height. Coming across, the government of Nepal also declared economic diplomacy as a major foreign policy by 90's. While kicking off its policy of economic diplomacy, a major breakthrough by the government of Nepal came in 2052 B.S. after the submission of report to the government by the High Level Task Force (Hamal: 2002). Similarly the establishment of Economic Relation and Coordination Division (ERCD) and International Business Forum in the Ministry of Foreign Affairs, International Desk Offices at the line ministries such as Finance, Industry, Trade, Tourism, Water Resource and Labor etc. were also the major steps on the

establishment of economic diplomacy as an intricate component of Foreign Policy of Nepal.

1.1.1 Concept of Economic Diplomacy

The term 'economic diplomacy' is widely used in the jargon of present international political economy system. The term, also known as development diplomacy, is the establishment of bilateral or multilateral relation among and between nations on economic and commercial frontiers. The concept is gaining prominence in the global scenario of recent years. However it is not a novice practice. In the pre-world war days the bilateral or multilateral ties were established on more political and less economic motives. Thus the economic agendas were considered secondary matters while exercising diplomacy. Such diplomatic practice was pre-occupied to bring countries to either of blocs.

However the shifting of diplomacy from political to economic front was more prominently geared by the inception of Globalization, Liberalization, Privatization and the Free Market policies. Margaret Thatcher came up with these new doctrines in the decade of 1970 and thus known as Thatcherism and the Thatcher Revolution. The fall of the Political empires and the end of cold war between Capitalism and Communism represented by USA and the then USSR respectively in early 90's renovated the Bipolar world to a Unipolar. So far the Communism collapsed, the system of mixed economy also failed and hence the Thatcher Revolution galloped all across the continents providing a solid foundation for the paradigm shift in terms of practical diplomacy. Since then the term 'economic diplomacy' is used to emphasize only the economic aspects of the multi-faceted relations among and between nations.

Nepalese context

During the 18th and 19th centuries active trade policy was practiced in Nepal. For more than a century in Rana hegemony Nepal almost lacked any concrete mechanism for establishing international relation. Only after the great change of 1950's, marked its relation with international communities and thus started receiving foreign assistance in terms of aid and loans. During pre-restoration

period in 1989/90's the indo-centric diplomacy also failed and thus measure shift on the extension of international relation to new dimension was necessitated. As a result, after the restoration of Democracy in 1990's Nepal renewed and strengthened multilateral relations. Since then the government of Nepal has been following the strategy of economic diplomacy as a major foreign policy.

In post-restoration period Nepal opened up for Liberalization and Privatization policies. Along with the inception of these policies in 1990-91, the government also set prioritized sectors such as infrastructure, power, water, telecommunication, roads, tourism and highly rewarding agriculture. While to develop these sectors Nepal persistently required huge capital which was only possible through increased volume of foreign assistance, FDI, foreign trade and foreign employment. Thus in the context of globalization, the traditional means of diplomacy proved obsolete and the practice of economic diplomacy became inevitable to set a new trend in international relation to enhance aforementioned economic means.

Since economic diplomacy is a strategy to promote the economic aspirations by using diplomatic skills, it in its true term entails to involve in international financial institutions, markets and organizations primarily concerned with international and regional development (Adhikari: 2005). At present Nepal's tie with international communities is guided accordingly by the major thrust of government over manifold of current economic issues where the major issues can be outlined as;

- a. Foreign Assistance,
- b. Foreign Employment,
- c. Foreign Investment(Direct or Portfolio),
- d. Foreign Trade, and
- e. Tourism

These five issues are regarded as the major components of economic diplomacy. These areas identified as components of economic diplomacy have been playing a crucial role on shaping our overall economy.

1.2 Statement of the Problem

Nepal is characterized by its vulnerable economy and unstable political situation. The macroeconomic indicators of Nepalese economy indicate that it is characterized by several weaknesses such as underdeveloped infrastructures, lack of technological know how, lack of capital endowments, ineffective implementation of policies, poor manpower, slacking foreign trade particularly diminishing export and increasing imports and dwindling industries. Such shortcomings have enforced the economy to profoundly rely upon sectors such as Foreign Direct Investments, Balance of Trade, Foreign Assistance, Foreign Employment, and Tourism. And hence these are the prominent issues under economic diplomacy. Investment in water resources, which bears immense potentiality albeit, has been too low in the subsequent years after the breakout of insurgency.

In the FY 2006/07 the amount of foreign aid has been Rs. 25854.3 millions, out of which the multilateral aid is Rs. 9447.79 millions and the bilateral is Rs. 16406.4 millions. Foreign employment has been a major source of foreign currency earning in recent years. In the first eight months of FY 2007/08 the remittance piled up to Rs. 82.42 billions and the contribution has been marked as 16.5% to the national GDP.

While looking at the current situation of national economy, the Foreign Investment in the first eight months of FY 2007/08 has been opened up to 127 industries in which foreign investment has amounted Rs. 7719.99 millions. At present Nepal is excessively depending upon foreign aid which comprises more than 60% of development budget. Also, Nepal is in need of technological assistance and foreign capital to boost up its economic growth and fill the vacuum of rapidly dwindling grants and loans, and for it the foreign investment has always been the only alternative.

Similarly, in the first eight months of FY 2007/08 the quantity of export has reached to Rs. 38963.3 millions where the composition India as always has been greater. The export to India has amounted Rs 25860 millions and to other

countries Rs. 13103.3 millions. In the same FY the contribution of Tourism in National GDP has been 1.2%. Foreign exchange earning of tourism during the FY 06/07 remained Rs. 10125.0 millions.

Countries like Qatar and China have utilized the foreign assistance from multinational donor agencies such as ADB, WB and IMF to greater extend, resulting a higher growth rate of their economy. South Korea and Malaysia are examples of countries which have been successful in tapping the FDI. On the other hand India for instance is expanding its trade globally. The tourism industry in Switzerland and New Zealand has become the main source of their economy. Thus, these components are very crucial to drive the economy toward progress. The efficacy of economic diplomacy is in a way, one measure of making these components effective and thus propelling the momentum of economic growth. But in our case, how exactly the economic diplomacy playing role for fostering the development process of country is a pertinent question. The particular measures of government to ensure the efficacy of diplomatic means are capable of making a major thrust over national GDP. Although, Government has been always saying and doing to pay a due attention on sharpening the diplomatic measures, no such phenomenal achievements have been experienced over decades in the economic front. Having so much importance of it to foster development, what shortcomings have led to under-achieve the interest of national economy is a matter of study.

Considering these difficulties this study has tried to answer the following research questions regarding economic diplomacy:

- What roles is it playing to foster the national economy?
- Has it been successful to enhance the interests of our country?
- Does it bear any further relevance in present political economic context?

1.3 Objectives of the Study

The objectives of the study are:

- a) To identify the role and relevance of economic diplomacy in Nepal,

- b) To identify the approaches of the Government of Nepal to foster the efficacy of economic diplomacy, and
- c) To analyze the present situation of economic diplomacy in Nepal.

1.4 Significance of the Study

The components of economic diplomacy have a great impact and crucial role in the making of national economy. Today nations are more engaged in their economic drive for national development activities and hence, LDCs and developing nations are becoming more emphatic on the economic role of diplomacy. This signifies its growing importance in recent years.

The topic 'Economic Diplomacy of Nepal' is a new one and bears a great potential in further studies and researches in this area. The subject has broad social, economic and political implications. Thus, this study will help to provide several aspects of economic diplomacy including information in the situation of Nepalese economic diplomacy. It will also be useful for researchers, policy makers and general students to figure out the role and relevance of economic diplomacy in the present context of Nepal. This study aims to recommend some of the important prospects of economic diplomacy in the development process of 'New Nepal'. The study will be useful to identify the effectiveness and pitfalls of economic policies concerned with the economic diplomacy.

1.5 Limitations of the Study

The study deals with the major components of economic diplomacy which includes Foreign Aid, Foreign Employment, Foreign Investment, Foreign Trade and Tourism sector. The study analyses the role and situation of these components covering the period of FY 2000/01 to FY 2008/09. Simple ratio analysis of secondary data has been applied, but the accuracy of data has not been examined.

1.6 Organization of the Study

The study has been divided into six chapters. Chapter one is the introductory part comprising of general background, statement of the problem, objectives of the study, significance of the study, the limitations of the study and finally the

organization of the study. Chapter two is the Review of Literature, presenting chronological development of economic diplomacy along with views, definitions and concepts forwarded by prominent diplomats, economists, and political leaders. Chapter three presents the research methodology applied in the dissertation which includes research design, data source, data processing, data collection and analysis of the data. Chapter four reviews precisely the policy measures of Government of Nepal on economic diplomacy. Chapter five presents the efficacy of economic diplomacy in national economy of Nepal. And, finally chapter six presents the summary, conclusion and recommendations.

CHAPTER 2

REVIEW OF LITERATURE

2.1 Concepts of Diplomacy

The literary meaning of diplomacy is to conduct the international relations by means of negotiations and dialogue or by any other means to promote peaceful relation among and between states. The term diplomacy has been taken from Greek word 'diploma' which means a folded document. This indicates to a set of rules, institutional practices and discourses held or executed by those officials who have the right to use the folded document issued by the government, international organizations or agencies as an identity document in international affairs (Gautam, 2004).

Pradhan writes, "Diplomacy is a means devised for achieving the aims and objectives of a nation expressed in terms of foreign policy. That is, if the foreign policy is the end, diplomacy is the means". The Oxford Dictionary defines diplomacy as, 'the management of international relations by negotiations; the method by which these relations are adjusted and managed by ambassadors or envoys or diplomatic agents'. Thus it is clear from these definitions that the main task of diplomacy is to execute and implement national policy which envisages vast network of agencies and the techniques (Pradhan, 1996).

Satow defines diplomacy as "the application of tact and intelligence to the conduct of official relations between governments of independent nations" (Pradhan, 1996). The American Dictionary of Politics defines diplomacy as "An art and practice of conducting negotiations between sovereign state for the attainment of mutually satisfactory political relations, where a direct diplomatic negotiations between heads of state occasionally taken place but for the most part they are conducted through diplomatic agents".

World University Encyclopedia defines, "Diplomacy is an art of negotiating and arranging treaties between nations. It relates to the form of international

negotiations, the relations of independent state to one another, and the management of envoys accredited to foreign court”.

Thus by executing foreign policy the diplomatic representatives make negotiations, conclude treaties or agreements which are again ratified by independent states by the means of foreign policy as approved within the state. The nature of diplomacy is in continuous metamorphism along with the changing global scenario. Several modifications have been undergone in the traditional methods of establishing international relations with changing time and course. However, the diplomacy as a pivot remains always in the center of international relation, yet its inclination remains flexible as the world rolls on.

2.1.1 Classical Concept

The hundred years between the Treaty of Vienna (1815) and the First World War (1915) was the great period in which classical diplomacy was in full swing. During that period, the international diplomacy was mainly confined to the formation of alliances or bloc nations. The glamorous days of the classical diplomacy of the late eighteenth and early nineteenth centuries were characterized by the aristocratic behaviorism and typically the Europe Centered diplomacy. The players of diplomacy were treated as something dubious, sinister-looking and mysterious guys often dressed in heavily braided uniforms with sophisticated titles, glittering decorations and moving in the company of high circle gracious ladies, nobilities and dignitaries. They were the ones who thoroughly enjoyed all sorts of amenities and immunities, duty free stocks and unlimited privileges marking a sort of super-human beings as if they had the sole exclusive rights of conducting nation's external dealings. In classical period, the onus of laying down the foreign policy of a country and its guidelines was entirely the prerogatives of the ruler. The diplomat was responsible for its execution (Pradhan, 1996).

Dahal in his book *Foreign Policy and Diplomacy* has mentioned that the classical diplomacy concerned with national interests related to sovereignty, independence, territorial integrity and expanding power to other nations. Herald Nicholson has outlined the fivefold major characteristics of classical diplomacy. They are:

- a) Domination of Europe,
- b) Difference between the big and small powers,
- c) Liability of big power,
- d) Professional diplomatic service, and
- e) Continued and secret negotiations.

The end of the WW-I in 1919 is considered as the decline of classical norms and practices of diplomacy. There by, the diplomatic approaches gained a new momentum and the advent of new diplomacy became possible (Dahal, 2006).

2.1.2 Modern concept

According to Nicholson (1969), the evolution of new diplomacy in the aftermath of The First World War (1919) is a transitional phenomenon of classical diplomacy rather than a contrast. Along with the end of the World War I, the Europe Centered diplomacy gradually declined and the USA emerged as a single super power of world and it became the center of world politics and diplomacy.

After the Second World War the world underwent a summersault transition. Many colonized states became independent. The world became united for the reconstruction of devastation created by the WW II. The establishment of UNO played a vital role on creating a platform to discuss on issues ranging from politics to economics. Democracy, Humanity, and Equality became the limelight of this era. The gradual democratization of political process, the growing sense of community among people, and the growing realization of importance of public opinion were major impetus on crafting new dimensions of modern diplomatic practices. On the same ground, Nicholson rightly remarked, “Public opinion became an ever increasing factor in the transition between the old diplomacy and the new” (Dahal, 2006).

Pradhan in his book ‘*Behavior of Nepalese Foreign Policy*’ views that the scope of diplomacy has changed dramatically since the WW II. In modern days, it has taken the shape of ‘New Diplomacy’ which extends beyond the customary functions of representing and reporting nature. Today it embraces responsibilities

for all state activities relating to foreign relations; and, as interactions between nations increase, the task of diplomacy also become more difficult. He further states that in contemporary world when the staggering range of activities engulfed the nations resulting into complex nature of external dealings, the tasks of diplomacy accordingly have become manifold and multifarious (Pradhan, 1996).

The grown up world consensus over democratization, parliamentary system and the shifting of the focal point of diplomacy toward economic issues were experienced in the decades of 50s and 60s. It was further nurtured by the inception of Thatcherism and globalization. The establishment of global and regional organizations such as UNO, WTO, EU, ASEAN, SAARC, BIMSTEC etc, consensus on fighting global poverty, convert of world as global village, role of communication and information technologies, establishment of WTO, paradigm shift in economy from welfarism to liberalization, privatization, and free market policies, active participation of private sector in economy, etc provided great impetus on the changing pattern of diplomacy. The advent of Economic Diplomacy was seen under these global changes. Thus the scope of diplomacy in present days has been enormously widened to economic aspects and is conducted more in foreground than in the background.

Acknowledging the changing pattern of diplomacy, Pradhan rightly remarked that, "One more prominent phenomenon gaining ground which we should recognize is that it is no longer confined to the political and economic matters only. Its activities are increasingly tending to embrace the facets of social and cultural life. Diplomacy is not that simply related to government to government dealings, not just between officials, but also at the popular level. The dimension of diplomacy thus has been greatly widened due to the rapid advancement in informal relations" (Pradhan, 1996). Hence the new era in international relations does not accept the crudities and strange behavior of the institutions of old diplomacy. The new diplomacy is a great departure from its past; and, in it, attempts are being made to cultivate direct link with the people and its increasing

dependence on mass opinion. As such, we find changes in tone, substance and communication in its operation.

2.2 Economic Diplomacy

Economic diplomacy is not a completely new concept in its true term, as it has been practiced by governments since antiquities. However, the course and the importance of it in the recent years have been persistently immense. In practice, diplomacy has been rather defined in terms of political process until the decade of 1970's. After the Thatcher Revolution that galloped across the continents of Europe, America, and not excluding other parts of the world, new measures were seek on extending bilateral and multilateral ties between nations to foster new doctrines of Liberalization, Privatization, Globalization and Free Market Policies. This phenomenon gave rise to the importance of 'economic diplomacy' and thereafter the terminology has become high sounding.

The historical records and the literature in this regard are quite inadequate despite its inalienable significance, in the sense that the practice of diplomacy was rather based on political grounds in earlier days. Thus the primary focus of earlier diplomacy did not give much space to economic matters which was only considered secondary. Regardless of its profound importance and relevance, not much attention has been paid on writing and discussing about it and, even less in our Nepalese context. However the undergone transition and the paradigm shift in diplomatic approach in the aftermath world of Thatcher Revolution and the decline of Cold War, the new perimeters were inevitably needed for reconciliation between diplomacy and the new international economic environment. Thus, the subject became cynosure of the time and hence the experts of economics, diplomacy, the political leaders, and scholars underwent a summersault on drafting new measures. This phenomenon forged ahead the experts to rethink, redefine and reshape the age-old stereotyped and out-of-date approaches of political diplomacy and revitalized it in economic perspective.

At present the world is undergoing an economic recession or the global downturn. The economic impact of this recession is such that the developed and the

developing nations are loosing their employment rate. Ranging from financial institutions to industries and employment, it has created a severe situation all around. As a result the fragile economies of the third world nations such as Nepal have been simultaneously knocked in particular by the mess of global downturn. Foreign employment is in sharp decline. The amount of bilateral and multilateral assistances and grants are also marginally declining. The foreign investors are reluctant to invest in such critical time in the third world. Along with this, the simultaneous effect is also on the foreign trade. Nepal is eventually loosing foreign markets for exportable goods. And the global downturn has created a situation whereby huge numbers of people are not earning handsome salaries or income globally. This certainly has affected the inflow of tourists and thus the tourism sector. In such the third world nations like Nepal must capitalize its economic diplomacy to counter the global downturn. Thus, in the recent global economic scenario, the relevance of economic diplomacy has become immense.

Here are some views of diplomats, economists, scholars, and the experts regarding Economic Diplomacy.

A Dictionary of Diplomacy (2001) compiled by Berridge and James, defines that, “Economic diplomacy is concerned with economic policy issues, e.g. work of delegations at standard setting organizations such as WTO and BIS. Economic diplomats also monitor and report on economic policies in foreign countries and advise the home government on how to best influence them. Economic Diplomacy employs economic resources, either as rewards or sanctions, in pursuit of a particular foreign policy objective. This is sometimes called economic statecraft”.

Regarding the growing importance of economic diplomacy, the Ex-Prime Minister of Israel Benjamin Netanyahu in the Caesarea Economic Conference on challenges, strategies and visions for the year 2000 AD addressed that, “Until now the Prime Minister of Israel dealt with the issues revolving around security, security, and security. It will now be economics, economics, and economics” (Pradhan, 2003).

Dahal *et al.* (2008), in a published book entitled '*Nepal, A Generic Guideline for Development through Economic Diplomacy*' have acknowledged the role of globalization on fostering economic diplomacy. In their words, "Economic globalization has increasingly made economic diplomacy a significant factor in foreign policy. Economic progress and prosperity depends on beneficial relationship with other countries and each country wants to penetrate into other countries with its goods, services, labor and investment. Global economic issues have great impact on domestic issues, and in the process, economic diplomacy involves global economic issues. Economic diplomacy is concerned with the prediction of outcomes of future trade regimes and therefore it will need an understanding of market factors at work in a given global economic environment, and in that process, a country will involve itself in making decisions in advancing economic interests. There is an awareness that economic diplomacy may strive for greater transparency, better information, greater clarity and more publicity. Private sectors give high priority to transparency. Economic diplomacy refers to the use of our political influence and relationships to promote international trade and investments; improve the functioning of markets; reduce the cost and risks of cross-border transactions; achieve internationally accepted standards; secure private property rights; develop international telecommunications, energy and transport networks; and of course consolidate the right political climate to facilitate and institute all of these objectives".

Hamal describes that the economic diplomacy includes aspects that serve economic interest of nations. Its inception was from the time of the very birth of nations and their interactions with outer world. However the term economic diplomacy is only in practice or in diplomatic jargon in recent years which gives more emphasis on only economic aspects of the multi-faceted relations between and among nations (Hamal, 2002).

He further illustrates that, "In the light of the precedence of global economic forces over the political ones, economic diplomacy has become a cynosure of the day. Nations have started reshaping their identity and national strategy vis-à-vis

other nations through increased economic co-operation. There is no doubt that the economic co-operation both at the government and private level through bilateral and regional arrangements as well as through pro-investment/trade policies can be a catalyst of growth in many countries. What is required is the conducive policy environment so as to activate the economic co-operation to give facelift to the economy of the country. Nepal's economic diplomacy needs to be geared to that end" (Hamal, 2002).

A freelance researcher Gautam quotes, "Economic Diplomacy at its core includes the foreign policy goals in terms of promoting trade and foreign investments. Its relation is directly with the economy of a nation. The concept of economic prosperity had emerged in 18th century which is known as classical free trade doctrine as propounded by Adam Smith and comparative cost theory of David Ricardo. However, this concept has been widely used only after 1970's as the process of liberalization, privatization, and later on globalization became stronger. Europe had pursued a traditional economic mechanism of protectionism until Margaret Thatcher in 1970's came with a new doctrine of liberalization. Ever since then many countries have been employing the term to use diplomacy not only for political purpose but also to economic purpose. Nepal has also been using the policy of economic diplomacy since a long and emphatically since 1990's" (Gautam, 2004).

Rashid in his address to the *Indian Economy and Business Update* quoted that, "In the traditional sense, diplomacy is political diplomacy. This means the diplomats are primarily engaged in political relations because close or strong political relations lead to relations in other areas including economic. Empirical evidence suggests that economic relations are not initiated in a significant way in a political vacuum in which there is a lack of trust" (Rashid, 2005).

Further he quotes, "Economic relations may act as glue to political relationships. There is a growing realization that if economic relationships are strong, they have an impact on political relationship and whatever ripples occur in political relations, it gets sorted out because both countries have a stake in not losing out

beneficial economic relationship. The term 'economic diplomacy' is of recent origin. Economic diplomacy was earlier known as Trade Diplomacy. Trade diplomacy came with the nationalization of industries in many countries from the 50s to the 70s. This resulted in gradual involvement of diplomats in trade matters, that is, to help sell products of nationalized industries. Meanwhile with the time elapsed, political leaders have realized that 'bread and butter' issues are the principal objectives for growth and prosperity of people. Added is that while strong economy exists, leaders can win successive elections”.

While defining term he says, “Now the term 'economic diplomacy' has become a buzz-word in all countries. In the process the term has raised confusion among many as to its exact meaning, although every one has a general idea about it. There is no exact definition of it but it can be described as formulation and advancing policies relating to production, movement or exchange of goods, services, labor and investment in other countries. A distinctive feature of economic diplomacy is that private sectors are involved in the decision-making process to influence negotiating position to remain in the global or regional competitive market. This is because firstly market developments are rigorously monitored by private sectors. Secondly, they are in the field and they know where and how to invest, sell, goods and services in the interests of a country. In the case of traditional diplomacy, it is the officials/diplomats who are involved in it and there is no participation or input from private sectors” (Rashid, 2005).

Minodora, a scholar in *The Academy of Economic Studies, Bucharest*, in his article defines the economic diplomacy in the context of present world of Information Technology. He quotes, “A major aspect of the new economic diplomacy is represented by the effort to set up certain actions regarding the international harmonization of general policies and legal framework, referring to: setting-up and sustaining an informatics' and communication infrastructure; private life and consumer protection; setting-up electronic payments systems and cooperation of the finance institutions; intellectual property protection. All these factors indicate that, in the future, the globalization will force each state to amend

the practices of the classical diplomacy, in order to have a pragmatic approach, based on re-orientation of the activity and diplomatic initiatives to social and economical development objectives. This type of diplomacy, more active and dynamic for new regional, bilateral and global partnerships, should participate to the economical development of each country. In the present context of globalization, the economic diplomacy represents an efficient instrument for a national external action, not only as a simple set of practices regarding the support of the exterior commerce. At the moment of 'globalization', the economical relations become more and more complex and the international relations remain, at least for now, based on the traditional military power and politics”.

In the similar tone Minodora further states, “Although the economic diplomacy is not a new phenomenon, it has become essential at the end of the 20th century, due to an increasing globalization regarding the new horizons opened and the modification of the states relations. The issue of power, influence or authority has always been the center of the international relations, but today it is not reflected anymore in the obsessive arming tendency during the Cold War. The present dominant expression of power is economical. This is the reason for new meanings in the economic diplomacy of informational and knowledge society. The present international context dominated by the power of economy is the scene for diplomatic missions, regarding a monitorization of different projects, from electronic commerce to telecommunications, environment issues or conquering new markets”.

Minodora opines that, “The evolution of the traditional diplomacy towards the new directions of the informational society is a dynamic and on-going process, based on the particularities of the globalization phenomenon, as well as on the diversity of the information processing and communication technologies which are present in the business environment as e-business, e-commerce, e-administration, e-government. The contemporary period and its international relations are defined by the concepts of globalization and informational economy (or digital economy)” (Minodora, 2006).

Dahal *et al.* in a jointly published book entitled '*Nepal, A Generic Guideline for Development through Economic Diplomacy*' have defined that, "Economic diplomacy is concerned with economic policy issues. Economic diplomats also monitor and report on economic policies in foreign countries and offer advice to the home government on how best to influence them. Economic diplomacy employs economic resources, either as rewards or sanctions, in pursuit of a particular foreign policy objective. This is sometimes called 'economic statecraft'. Economic diplomacy is the decision-making, policy-making and advocating business interests of the sending state. Economic diplomacy requires application of technical expertise that analyzes the effects of a country's economic situation on its political climate and on the sending state's economic interests. The sending state and receiving state, foreign business leaders as well as government decision-makers work together on some of the most cutting-edge issues in foreign policy, such as technology, the environment, and HIV/AIDS, as well as in the more traditional areas of trade and finance. Versatility, flexibility, sound judgment and strong business skills are all needed in the execution of economic diplomacy. Economic diplomacy engages contacts with foreign and sending states' institutions, businesses and international organizations to advance the sending state's economic interests; seeks to resolve bilateral trade disputes and negotiate with trading partners to liberalize world trade; seeks to formulate official policy for development and formulate recommendations for sending state; facilitates negotiation on trade-related agreements and treaties; and identifies and coordinates financial assistance to troubled areas. Economic diplomacy also engages development partners to raise standard of living in both sending and receiving states; co-ordinate trade policy, promote open markets, and promote sending states policies and interests in international and bilateral scientific, environmental, and technological arena" (IFA, 2008).

Schrumm and Antkiewicz in the conference report at CIGI organized in Ontario Canada presented that, ".Economic diplomacy can be conceived as the application of a nation's favorable economic conditions, by conferring rewards or penalties, toward particular foreign policy objectives. As an area of study, it explores the

multiplicity of tensions between politics and economics, between international and domestic pressures, and between governments, business and civil society. Existing literature largely focuses on how economic diplomacy is practiced in trade-related negotiations; however, emerging economies are increasingly employing it in wider policy arenas. In recent years, economic diplomacy has been used by both state officials and corporate leaders in rising powers to leverage foreign investment and integration in global supply chains into diplomatic power on political issues” (CIGI Report, 2008).

In the Report of the Policy Study Group of Institute of Foreign Affairs on ‘*Nepal’s Economic Diplomacy*’ it is defined that, “Economic diplomacy is essentially a process of mainstreaming economic dimension into our foreign policy perspective with the objective of further promotion of our economic interests with the cooperation of the outside world through well informed negotiation. Those who are involved in such negotiations should, therefore, be well-informed. Precisely for this reason, the mechanisms as envisaged in this study are intended to strengthen our system of ‘Communications and Coordination’ along with in-house training as a process of ‘learning-by-doing’. It is felt that regular and meaningful "Communications and Coordination" can considerably enhance our capability to conduct economic diplomacy in an effective manner” (IFA, 2002).

Shrestha in his report on ‘*Enhancing Economic Diplomacy*’ presented in September, 2005 has outlined that, “Economic diplomacy as an integral part of foreign policy is essentially an extension of domestic policies and priorities. Unless the appropriate government policies related to trade, tourism, foreign investment, official development assistance, employment and other economic policies are well in place, no instruments and mechanisms of economic diplomacy, however sound and efficient, can deliver the expected results. The instruments and mechanisms are only the means for implementation of the government policies both at home and abroad” (Shrestha, 2005).

Thus on the ground of above concepts of Economic Diplomacy we can conclude that the present situation of economic inter-dependency of nations for fostering development process and overall economic status within the nation is only possible by mutual relationships between nations. For, there is an urgent need of creating a platform whereby nations can discuss and exchange the opinions related to vices and virtues of their respective economies. The active role of organizations such as WTO, IMF, WB, ADB have rigorously served as such platform under which the economic diplomacy has gained a strong ground in present world scenario. And hence, Economic Diplomacy is that one medium by which the objectives of bilateral and multilateral ties between nations can be achieved. Also it can engage development partners to raise standard of living in both sending and receiving states; co-ordinate trade policy, promote open markets, and promote sending states policies and interests in international and bilateral scientific, environmental, and technological arena.

2.2.1 Nature of Economic Diplomacy

According to Rashid, the nature of economic diplomacy is classified accordingly to what level a nation operates it. It may operate at three levels:

- (a) Bilateral Diplomacy,
- (b) Regional Diplomacy, and
- (c) Multilateral Diplomacy.

Bilateral economic diplomacy forms a major part in economic relations, whether this consists of informal dealings between two countries on a range of issues or formal bilateral agreements on trade or investment or avoidance of double taxation. One of the areas of economic diplomacy is related to bilateral Free Trade Agreements (FTA). Different countries may use different levels of trade agreements. Since bilateral trade agreements have become the order of the day, many countries have concluded bilateral FTA.

Regional dimension in economic diplomacy is of growing importance. Regional economic agreements offer a more rapid way of opening markets. Liberalization of economy may be easier to accept for promoting national interests when it

occurs within a regional grouping of countries. For example, South Asian Free Trade Agreement (SAFTA) within the eight South Asian countries has been agreed by all member-countries. The number of FTAs constituting trade blocs has increased substantially in recent years. Regional agreements may suit neighboring countries and countries at the same level of economic and social development.

Multilateral economic diplomacy, ordinarily, takes place within the framework of World Trade Organization, International Monetary Fund and the World Bank. The conduct of economic diplomacy presupposes that there must be a pool of skilled persons in the government and private sectors to understand and negotiate key economic and trade issues from national perspective (Rashid, 2005).

2.2.3 Economic Diplomacy in Nepal

Economic diplomacy has become a critical component of foreign policy to eradicate poverty and achieve the Millennium Development Goals (MDGs) of the LDCs and DCs. It is quite obviously that the economic elements need to be incorporated into foreign policy and diplomacy. Most of the developing nations today are in a process of making economic diplomacy as major foreign policy.

The processes of democratization and liberalization of economy have pushed states to integrate into the mainstream of global economy. Nepal also has driven its economic policy to that end though it seems a Herculean task ahead. As we are driven to this task, very efforts are being exerted towards accelerating economic development through proper institutionalization of economic diplomacy. The decade long insurgency (1996-2006) has backlashed the Nepalese economy to a very fragile state. At this juncture, the need of proper diplomatic instruments toward fostering the fragile economy is inevitable. Since the economy of Nepal is not in a state of self sufficiency or self-sustained condition; for the reconstruction of destroyed and new infrastructures, investment on hydropower, communication, education, health, etc requires a heavy capital which can only be attained through bilateral or multilateral economic relations. Thus the importance and relevance of economic diplomacy is at high stake. Another important aspect of Nepalese economy at present is that it is undergoing a historic change politically and

structurally. Nepal has been declared a Democratic Republican State in June, 2008. Also, all the major political parties have acceded to follow a federal governing system. In such, the role of economic diplomacy is presumed to be an important instrument while financing the new system.

Here are some opinions regarding the importance, relevance and historical background of Economic diplomacy in Nepal.

Hamal in his book *'Ecology of Nepal's Foreign Policy'* mentions about the historical initiation of economic diplomacy in Nepal. In his words, "The concept of economic diplomacy gained ground after the submission of the report to the government by the High Level Task Force (HLTF) in 2052 B.S. The report had its major thrust that government should review its conventional diplomacy in order to concentrate on the economic interests of the country with requisite policy changes towards gearing the diplomatic machinery for export promotion, increased foreign direct investment, greater inflow of foreign aid, tourism promotion, and search for foreign employment for Nepalese nationals".

Pradhan comments, "For Nepal it has been a Herculean task ahead in view of its poor and backward economy. As we are driven to this task, every effort is being exerted towards accelerating economic development through the use of the instruments of economic diplomacy. Nepal, at present is passing through its transitional phase of economic development. Nepal, in the wake of its popular revolution for the restoration of democracy in 1989, when the Nepali Congress government was installed in the country after general election, the thrust for economic reforms was lunched; and, in the quest, HMG/N embraced the concepts of free market economy in its economic plans and programs. It was only after 1990, that government openly pronounced its open door policy towards liberalization and privatization which gained increasing momentum. But so far its tryst with the globalization front has not yet been productive as it should have been through the new economic diplomacy" (Pradhan, 2003).

Freelance researcher Gautam gives the historical perspective of economic diplomacy in Nepal. According to him, "During the 18th and 19th century Nepal

simply pursued an active trade policy and for about a century long Rana Hegemony Nepal had no policy at all. But after 1950's Nepal's relations with international community gradually pursued the concept of foreign aid and loans. During that time Nepal had no economic diplomacy in the sense we perceive it today. Today's world is entirely different in its economic phenomena. The indo-centric diplomacy has already failed in 1989/90's." He therefore suggests that, "the multilateral relations must be renewed and strengthened. This is an era of globalization when traditional mechanism proves to be obsolete and dynamic and digital technology has changed the old world view. We have to adapt accordingly if we want to exist in the struggle and prove our worth".

Illustrating the strategic efforts of Nepal on establishing economic diplomacy as a major foreign policy tool, he further clarifies, "Nepal has been following the strategy of economic diplomacy since 1990 as major foreign policy. As Nepal is in need of technology and foreign capitals to fill the vacuum of rapidly dwindling grants and soft loans, foreign investment both portfolio and direct has become the only alternative to boost up the national economy. Along with the liberalization policy of HMG/N in 1990/91, Nepal has also set some prioritized sectors like infrastructure, power, water, telecommunications, roads, tourism, and highly rewarding agriculture sector. Although Nepal as a LDC has similar weaknesses as observed in many LDCs and DCs, it has worked a lot in the field of telecommunication through information technology and establishment of financial institutions but still there are lots of areas where Nepal has to reform in order to prove its effectiveness in the marketplace. Nepal has to play a two-fold role while maintaining the leverage of a referee and formulate effective policies due to its LDC position and paucity of clear vision, while promoting DFI with its attendant managerial and technological transfer, it has also to solicit for bilateral aid and soft loans although aid and loans are not proper terms in economic diplomacy, Nepal's given fragile economy cannot not upgrade without it. Therefore, economic diplomacy has been an important component of Nepal's total foreign policy" (Gautam, 2004).

As the Nepalese economy has always been in sharp fluctuation over time, the measure of diplomacy in economic perspective has emerged as a major assuring weapon for stability. In the context of globalization and increasing competitiveness in the global marketplace, it is imperative that Nepal pursue effective economic diplomacy with other nations. It is indispensable to find a market for Nepalese exports, mark Nepal as a popular tourist destination, and enhance foreign investment in potential areas by adopting economic diplomacy as a major instrument.

“With fast and changing global policy on aid and trade, foreign aid is becoming highly competitive for recipient countries as evidenced by declining ODA, shift from grant to loan and growing preference for funneling aid through INGOs and local institutions (IFA, 2002). In Nepal economic diplomacy has to shift its focus increasingly from aid to trade, tourism and employment generation with the private sector playing a major role and MoFA and its Missions abroad acting as facilitators. Nepal has been striving to promote economic diplomacy, one of the pillars of foreign policy, through strengthening economic relations with friendly countries in the world” (FPTF, 2006).

2.2.2 Action Areas and the Functions of Economic Diplomacy

Former foreign ministers Dr. Prakash Chandra Lohani, Mr. Kamal Thapa and Dr. Ram Sharan Mahat were of the common consent on developing appropriate strategies in the conduct of Nepalese economic diplomacy. Dr. Lohani opined that the task of foreign ministry have to be able to comprehend the links between Nepal’s national economic interests to global trend. He added that the focus have to be more on trade and investment rather than bureaucracy and politics. Echoing similar feelings Mr. Thapa was more emphatic in saying that Nepal’s dependence on foreign aid, trade and investment for realization of development goals could be geared up by using foreign policy as a vehicle. Meanwhile Dr. Mahat was quite vocal to make Foreign Service as a special class separate service and personnel under it to be more skillful in negotiations and communications for economic means. Another prominent leader and the then prime minister Girija Prasad

Koirala opined that the foreign policy must be focused on to the economic aspects for mobilizing greater external resources enhancing foreign trade, FDI, Tourism and must seek for further integration of national economy to international (Pradhan, 2003).

After 1990s' the major policies and strategic measures for trade promotion adopted by government were Laissez Faire market economy, liberalization and privatization on tracking the path of globalization. At the mean time Nepal's accession to WTO, active participation as a member state on BIMSTEC summits, SAARC, becoming the member of SAARC Growth Quadrangle, setting the framework of SAFTA and its implementation from January 2006 etc. were some cornerstones on trade promotion activities. Meanwhile prioritizations of different types of Tourism such as pilgrimage tourism, linkage tourism, eco-tourism etc. were the slogan for promoting tourism in Nepal. Emphasis had been laid on creating an environment to attract the larger scale FDI, after the adoption of economic reform programs since 1991. Also, Nepalese government had set up prioritized sectors like infrastructures, hydropower, communication, roads, tourism and high rewarding agriculture sector (Hamal, 2002).

Another matter that merits attention is that millions of people of South Asian origin live in Western countries and most of them earn good money. One dimension of economic diplomacy has been to get them involved in economic and commercial activities within their home countries by disseminating information about investment climate. They can invest not only to earn good profits but also help develop their home countries on the road to economic development.

At present, Nepal's tie with other nations is guided accordingly by the major thrust of government over manifold of current economic issues which can be listed as: Foreign Trade, FDI, Foreign Employment, Foreign Aid, and Tourism Promotion. These are the issues economic diplomacy deals with. Hence the action areas and the function of economic diplomacy have always been to carry out the promoting role on foreign trade, foreign employment, foreign aid, foreign investment, and tourism.

The major economic tasks that diplomacy can play are:

- Trade promotion, with prime but not exclusive focus on exports.
- Investment promotion, mainly focused on inward investments, but not excluding the home country's outbound investments, where appropriate.
- Attracting suitable technologies, plus technology "harvesting".
- Management of economic aid, which is important for most developing countries as a "recipient", and for as a "donor" developed nations.
- Promotion of tourism which bears an immense potentiality in national economy.
- Promotion of foreign employment opportunities as a major source of foreign currency earnings.

There is also the larger task of country promotion, which supports all the above, and blends into image building. Enhancement of the image of the home country is one of the essential tasks of diplomacy that underpins and relates to a wide range of external activities (Mastanduno, 2001).

CHAPTER 3

RESEARCH METHODOLOGY

3.1 Introduction

Research Methodology is the most crucial and determining element for the soundness and reasonableness of research output in any field study including economics. Different techniques can be applied to achieve the objectives of the study. Research Methodology describes about the data collection, source of data, research design, reliability of instruments selected or constructed and statistical tools and procedures used in this analysis. This study is simply a descriptive type. There is no primary data analysis. It takes most reliable secondary data and other sources. The methodology adopted to achieve the objectives outlined above entails the following parts.

3.2 Research Design

This research is designed to examine the efficacy of Nepalese economic diplomacy. For this purpose the study has been carried out applying the quantitative and descriptive analysis. In chapter five the efficacy of Nepalese economic diplomacy and its components has been analyzed applying these methods.

3.3 Method of Data Collection

The methodology applied in this study is descriptive and analytical solely based on secondary data and information. Thus the required data have been collected by various issues of Economic survey published by ministry of Finance, Reports of NRB, MoFA, IFA, CBS and line ministries such as Tourism, Trade and Labor. Also some data are obtained from United Nation's annual reports, Reports of WB, IMF, ADB, and Issues of International Forum (monthly).

3.4 Sample Size

In order to study the efficacy of economic diplomacy in Nepal, 8 years data (FY 2000/01 to 2007/08) have been taken in to account.

3.5 Methods and Tools Used for Data Analysis

Data sets have been analyzed quantitatively. Most of the data are shown in tables. This study has been reached to conclusion by the description and analysis of the quantitative data. The uses of tools such as percentages, sum total, averages and ratio are widely applied while analyzing the data related to Foreign aid, foreign employment, FDI, foreign trade and tourism. For example: percentage annual growth of foreign aid, sum total of aid inflow, ratio of export to import etc are the modes of data analysis.

CHAPTER 4

POLICY MEASURES OF GOVERNMENT OF NEPAL ON ECONOMIC DIPLOMACY

4.1 Introduction

Economic Diplomacy was a declared policy of the Government of Nepal since the restoration of democracy in 1990s and has been a cynosure of GoN there onwards. Negotiation of liberal trading arrangements with key nations, large-scale national investments in major sectors of the country, focus on developing transport infrastructure, education, health, tourism, trade etc, and the focus on accompanying the global trends and cultures of Liberalization, Privatization, globalization, WTO, and the regional agreements such as SAFTA and BIMST-EC have significantly transformed our foreign policy template. This is an interesting turn of the wheel of history. Even a couple of decades back, economic diplomacy was seen as a 'black hole' by diplomats pursuing a fast-track career, and paled in comparison with political work. However, change in global context has added new impetus on the nurturing Economic diplomacy.

After the onslaught of Globalization, Liberalization, Privatization there was an urgency to carry on its overall national development projects based on the principle of Public-Private Partner-ship. This approach did not confine itself only within the domestic milieu but also called for a clear reflection on its external relations and behavior. To meet the pressing demands in home front, the nation needed to focus its attention to explore the viable avenues of comparative and competitive advantages. In this backdrop, the GoN has already kicked off its policy of economic diplomacy. Accordingly, some structural changes have been made in the MoFA such as the establishment of ERCS and set up of an IBF to interact with the private sector to evolve economic guidelines. Similarly IRDO have been established at the line ministries such as Finance, Industry, Trade, Tourism, Water Resources, and Labor. Nepalese Missions abroad have also been directed to pursue economic diplomacy vigorously (Hamal, 2002).

In the light of the precedence of global economic forces over the political ones, Nepal has started reshaping its identity and national strategy vis a vis other

nations through increased economic co-operation. The economical globalization is a real phenomenon and also the strongest reason for the actual international changes. The entire phenomenon can be described by an increase of the exterior commerce, regional economical entities, direct external investments, big global companies and strategic alliances. On the verge of this, Nepal is engaged in fierce competition for economic gains and at the same time seeking cooperation with other like-minded states in order to shape regulatory institutions in its favor. Nepal is also keen on to attract foreign investments (Direct or Portfolio) and gain international market access for its domestic products. The prime focus of its diplomacy today has been to look for suitable venues for its labor forces and to promote tourism, which always has been a major source of foreign currency earning. At the same time, it is also seeking for chunk of foreign assistance to cope with its lopsided development process.

4.2 Operational Mechanism

While invigorating for such viable goals Nepal has pursued several structural changes in the operational mechanism of diplomacy to make it a more economic oriented mechanism. Some institutional and structural measures or steps taken so far by the GoN on enhancing economic diplomacy have been outlined below:

- A High Level Task Force (HLTF) was constituted in November 1995 which made the following suggestions:
 - a) Restructuring of the MoFA to 9 Divisions with Bureaus and Desks under them,
 - b) Introducing Career Planning System for the employees of the MoFA (separate recruitment, training and promotional system)
 - c) Establishment and institutionalization of the Economic Relations and Coordination Division (ERCD) in the foreign ministry.
 - d) Enhancing the Nepalese missions abroad for economic diplomacy (briefing and de briefing, regular exchange of information and instructions to the missions, proper budgeting, etc.).
 - e) Expansion of Nepalese missions and posts therein.

- f) Establishment of an institute of foreign affairs.
 - g) Effective and improved administration in the foreign ministry.
 - h) Political coordination
- As suggested by the HTLF, a number of measures have been taken. The MoFA was restructured, though not exactly as suggested by the Task Force. The Economic Relations and Coordination Division (ERCD) was established in the Ministry. The roles of the ERCD envisioned were:
- a) to contribute to the integration of national economic policies into Nepal's foreign policy goals and strategies;
 - b) to develop a sense of full partnership with the sectoral ministries and the private sector in the conduct of economic diplomacy;
 - c) to support planning and organizing of all the commercial functions and activities to be undertaken by the missions;
 - d) to monitor and facilitate the aid management and business promotion activities being carried out in Nepal by donor countries and international organizations;
 - e) to help strengthen the bilateral Joint Economic Commission and identify opportunities for regional and sub-regional cooperation; and
 - f) to facilitate vertical and horizontal coordination of economic diplomacy function being executed by the diverse economic decision making centers.

In line with the suggestions made by the Policy Study Group (PSG) constituted in March 2002, the ERCD in the MoFA has been replaced by the Multilateral Economic Affairs Division (MEAD). An urgent need for proper coordination between and among various Ministries was felt, and, therefore, the Economic Diplomacy Coordination Committee, to be headed by the Prime Minister, was formed in 2002. It included ministers, secretaries and representatives from private sectors (FNCCI, NTB, and Chamber of Commerce). As mentioned above, this committee decided to include two more sectors (ICT and NRN) under the purview of economic diplomacy. It also decided to form the Economic Diplomacy Standing Committee under the MoFA, which was entrusted with the task of

coordinating activities of the MoFA, sectoral ministries, Nepalese Missions abroad and private sector (Adhikari, 2005).

The PSG Report concentrated in economic diplomacy with a sharp focus in institutional mechanism for communications, coordination and cooperation within the MOFA, on the one hand and between to MOFA and the sectoral Ministries and the private sector, on the other. Also it suggested the establishment of External Economic Relations and Coordination Committees (EERCC) at the political level with The Prime Minister as its Chairman and Multilateral Economic Affairs Division like the one suggested by the HLTF as well. The EERCC as well as its Standing Committee under the Chairmanship of the Minister for Foreign Affairs (not recommended by PSG) were constituted and remained non-functional after their first meetings was held (Shrestha, 2005).

4.3 Promotional Approaches

In the context of globalization, liberalization and increasing competitiveness in the global marketplace, it is imperative that Nepal pursue effective economic diplomacy with other nations. This is needed particularly to find a market for Nepalese exports, market Nepal as a popular tourist destination, and enhance foreign investment in potential areas. Government of Nepal has incepted various policy measures to enhance its capacity in export, tourism and investment. Also it has been eyeing for good employment opportunities abroad and chunk of foreign assistance to escalate its languished development process. The policy measures taken by GoN for promotion of aforementioned issues have been outlined below.

4.3.1 Promotion of Foreign Aid

Foreign aid plays a prominent role in the development Nepal's economy. Seeking its grave importance a separate division namely Foreign Aid Co-ordination Division (FACD) has been set up in the Ministry of Finance. The division has been established with the vision of mobilization and optimal utilization of resources through foreign aid in accomplishing the development goal of poverty reduction and realizing sustainable high economic growth. Also the division has prioritized strategic goals, objectives and activities to enhance the inflow of

foreign aid by incorporating strategic economic diplomacy. The policies regarding enhancement of foreign aid inflow through the platform of economic diplomacy include:

- a) Finding out the policy and priorities of donors cooperation and communicate it to concerned authorities,
- b) Participation in bilateral and multilateral aid related seminars,
- c) Regular consultation meetings with donor/s on issue of foreign aid,
- d) Refreshment training on negotiation skills for Officers,
- e) Establishing cooperation with donor communities to command their confidence and faith in the strategic policies,
- f) Maintaining effective communication link with donors,
- g) Matching donor's priority and excellence with development comparative advantages and programs in mobilizing aid,
- h) Encouraging and ensuring transfer of essential knowledge and technical know-how by providing special facilities,
- i) Informing the donors about the national priority sectors and projects/programs regularly,
- j) Organizing the meeting Nepal Development Forum (NDF) every two years etc.

4.3.2 Promotion of Foreign Employment and Remittance

It is estimated that the labor force in Nepal has been continuously increasing by approximately 300 thousand persons every year. Since the internal employment opportunities have not been able to provide works for growing labor force, great outflow of labor force have been experienced over years. On the same backdrop, GoN also has strategically enacted several policy measures to make foreign employment as a major source of foreign currency. Some of these measures are outlined below:

- a) GoN has made provision of foreign employment loan for marginally poor people from among affected by the conflict, disadvantaged, minorities and

women. Arrangement is made for providing 80 percent of such loan without any collateral.

- b) Since, last few years, money transfer institutions are being encouraged with the objective that the Nepalese workers engaged in foreign employment could send their foreign currency earnings easily to their family.
- c) In addition to purchase rate margin, commission of 15 Paisa per US dollar is permitted to such money transfer agencies in the private sector to encourage the inflow of convertible currency earned through foreign employment.
- d) Facility to open foreign currency account is given to agencies engaged in sending Nepalese for foreign employment and institutions eligible to accept payments in convertible currency against their services.
- e) Policy decision has been made to allow opening of convertible currency account to agencies licensed to conduct remittance transaction as per the prevailing rules.
- f) If a Nepal-based licensed agent/representative of any foreign-based money transfer company needs bank guarantee for the purpose of receiving advance payment from its principle company, a policy provision of making such facility available, within the specified limits, directly from the commercial banks has been initiated since FY 2004/05. This provision is expected to facilitate the licensed agents in making immediate payments of the remittance to the concerned parties.
- g) Policy provision is already in place to allow opening branch/representative office (in India and in other countries) to Nepalese foreign employment services agencies.

Similarly, an interim provision for facilitating Remittance from India to Nepal has been constituted with the joint initiative of Nepal Rastra Bank and Reserve Bank of India for remitting funds from India to Nepal through NEFT (National Electronic Fund Transfer) system. Remittances can be sent through any of 40, 000 NEFT enabled bank branches in India. Under this system, a Nepali worker can remit fund up to Indian Rupees (IRs) 50,000 at a time and will be allowed a maximum of 12 remittances a year.

4.3.3 Attracting Foreign Investment

Nepal's attempt to attract foreign investments (direct or portfolio) has been esteemed by the inherent characteristics of it as an ideal destination for foreign investors owing to its rich natural endowments, abundant and chief labor force, ongoing long term peace process, huge market in neighboring countries, growing internal market, a well-developed banking and non-banking financial institutions to cater investors needs for finance, fully convertible current account, peaceful industrial environment, preferential entry of products in India and investor-friendly government policy. Investment opportunities are open to almost every sectors of economy from Tea to Mining; except a few restricted ones.

Given the scarcity of domestic private capital, GoN has introduced several policy measures to allow foreign investment to promote industry-led economic growth and to correct the worsening BOP situation. These measures are:

- a) Open and liberal industrial policies,
- b) Privatization,
- c) Tax reform,
- d) Repatriation of output,
- e) Delicensing of industrial investment,
- f) One window facility,
- g) Visa facility
- h) Convertibility of Nepalese currency in current account,
- i) Market oriented fiscal and monetary policies, etc.

Similarly the Foreign investors are also provided with facilities such as:

- a) No government intervention in fixing prices of the products,
- b) Special facilities of electricity and infrastructures,
- c) Quick and effective service through One Window Committee,
- d) Technology transfer in all industries,
- e) Guarantee of security against the non-commercial risks like currency transfer, expatriation, breach of contract, and war and civil disturbances,
- f) Speedy project approval (within 30 days),

- g) No nationalization of industry and business as is prohibited by the constitution and the industrial enterprises act,
- h) Non-tax incentive such as no fees on electricity generated by the industries for their use,
- i) Use of forest areas by forest based industries on a lease- hold basis,
- j) Facilities of the industries of the Export Processing Zones to be given to industries exporting 90 percent or more of its products,
- k) Disputes Resolution by arbitration on the basis of UNCITRAL rules.

4.3.4 Export Promotion

Export promotion was a priority issue even before the introduction of the liberal market economy at the early 1970s. The government became seriously involved in export promotion and diversification, especially with the establishment of the Trade Promotion Center in 1972 (Shrestha, 1996). Much emphasis has been laid on export promotion after the 1990s along with the spread of the concept of economic liberalization. A number of policies have been introduced by the GoN for the export promotion. They are:

- a) Private of the public enterprises to enhance the role of the private sector in export trade,
- b) Strengthening of export competitiveness and capabilities,
- c) Country wise and commodity\service-wise diversification of trade,
- d) Liberal procedures for export promotion of industrial goods,
- e) Full convertibility of Nepalese Rupees on current account,
- f) Transparent and dynamic monetary, fiscal and foreign exchange policy,
- g) Institutional development such as the establishment of the Nepal Trade Promotion Centre,
- h) Development of information network, monitoring system and quality improvement, and
- i) Conclusion of various trade treaties and agreements.

There are also a number of strategies that have been adopted for the promotion of Nepal's export trade. These can be said to be in tune with the policy of economic diplomacy.

- a) Delicensing,
- b) Improvement of quota restrictions through appropriate tax measures,
- c) Improvement of transit transfer network and introduction of improved containerized system,
- d) Duty draw-back system on export products,
- e) Exemption of all taxes on export except service charges,
- f) Exemption of income tax on income from exports,
- g) Gearing up of Nepalese missions abroad towards export promotion activities, and
- h) Market promotion and entrepreneurship development programs.

4.3.5 Activities for Promoting Tourism

In order to enhance the image of Nepal as a fascinating tourist destination, long-term objectives have been set for the development of this industry, which include development of this sector as an important part of the overall economic development, establishment of Nepal as a premium destination of world tourism and expansion of the benefits of tourism to the village level. Efforts and measures that are adopted by the GoN are:

- a) A three-year plan has been prepared for tourism and sent to the National Planning Commission for approval.
- b) Selected tourist sites have been developed as pilot programs for integrated tourism development.
- c) In an effort to give clear direction to the tourism sector, preparation of an integrated tourism master plan and review and timely revisit of tourism policy are at the final stage.
- d) In accordance with the policy to encourage foreign investment in tourism sector, study on allowing foreign investment in tourism industries has been initiated.

- e) Preliminary work for construction of second international airport in Nijgadh of Bara district under private investment has started. Airport expansion activities at Gautam Buddha airport, Bhairahawa, and Chhinnedanda airport, Pokhara, have been initiated to convert into regional international airports.
- f) In order to conserve world heritage sites, the work of preparing the details of the houses and mapping of the road turns inside the site area is underway.
- g) In order to alleviate poverty, generate foreign and domestic employment opportunities, and for the welfare of victims of conflict, Dalits, indigenous communities, and victimized women, special trainings on hotel and tourism have been continued.
- h) Tourism Promotion Programs are being conducted focusing on potential tourist markets like India and China and other promotional programs including "Send A Friend Home" are taking place in countries like Japan, UK, Germany, Belgium, etc.
- i) In memory of Tenzing Norgay and Sir Edmund Hillary, the first humans on Mount Everest, May 29, have been declared and celebrated as the International Everest Day.
- j) Visit Year 2011: Year 2011 has been declared as visit year with a target of attracting more than a million tourists in the year.

(Source: Ministry of Culture, Tourism, and Civil Aviation)

4.4 Efforts on Global and Regional Cooperation

Nepal's membership of WTO, SAFTA, and BIMST-EC has opened up our economy to the outside world complying with the trend of globalization and regionalization. It is very likely that multilateral economic diplomacy ordinarily shapes within the framework of such global and regional cooperation. The year 2004 was featured by an accession to WTO and membership of South Asian Free Trade Area (SAFTA) and Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC) in the same year created a staunch base for liberalizing trade and investment in Nepal. Improvement in legal regimes

relating to export and import, customs valuation, transport and trade facilitation, and intellectual property rights were the new initiatives undertaken by the Government in course of meeting obligations of WTO. Since Nepal is a bonafide member of these organizations, amendments have been made compatible with globalization and liberalization in the Acts and Regulations pertaining to these priority areas.

4.4.1 WTO

In recent years the process of globalization is marching under the regime of WTO which was established in 1st of January 1995 incepted after the Uruguay Round of trade negotiations as a successor of GATT, it has been playing a pivotal role on fostering global trade. The prime objective of WTO is to provide the common institutional framework for the conduct of trade relations among its members. Other three objectives of WTO are:

- a) To help trade flow as freely as possible,
- b) To achieve liberalization gradually through negotiations, and
- c) To set up an impartial means of settling trade disputes.

Nepal accession to WTO is a cornerstone on shaping economic diplomacy as its key foreign policy. Nepal became the 147th member of WTO in 23rd of April 2004. Ever since Nepal's membership in WTO, several measures have been adopted to meet its obligations. Some of them are as follows:

- a) As per the WTO agreement, enquiry points such as, the Department of Food, Technology and Quality Control under the Ministry of Agriculture and Cooperatives as for Sanitary and Phyto-sanitary-SPS, and Nepal Bureau of Standards and Metrology under the Ministry of Industry, Commerce and Supplies for Technical Barriers to Trade – TBT have been established.
- b) Division of World Trade Organization under the Ministry of Industry, Commerce and Supplies has been serving as the entry point on service related issues.

- c) Different Acts such as Competition and Market Promotion Act, new Company Act, Multi-Modal Transportation Act, Crop Protection Act, Export/Import and Intellectual Property Rights Acts, Insolvency Act and new Customs Act have been issued. Also, discussions are on with the stakeholders in amending commercial policy and industrial policy.
- d) WTO Reference Center has been established to inform and disseminate information on the WTO. The center also holds monthly interactions on WTO issues with experts.
- e) A Focal Point has been formed for inter-governmental coordination in subjects concerned with the WTO and has been working with regular meets for fulfilling the commitments.
- f) Customs Duties have been accommodated each year in providing market access to products.
- g) Enhancing Nepal's Trade-Related Capacity Project, run by UNDP, has been working in boosting the trade-related capacity of the government and the private sector, involving the stakeholders in the formulation of policies pertaining to business and industries and in trade analysis, in skill development, and creating investment- friendly environment.
- h) Public awareness programs have been continuously launched on seizing opportunities by meeting the challenges. Such programs have been carried out at the central, regional and district levels through the coordination with private sector.

4.4.2 SAFTA

South Asian Free Trade Area is the broader form of previously established SAPTA. Accompanying the fact that the progress beyond a Preferential Trading Arrangement to move towards higher levels of trade and economic cooperation in the region was necessitated, SAFTA was forwarded to remove barriers to cross-border flow of goods in the region. The tenth SAARC Summit held in Colombo introduced SAFTA by replacing SAARC Preferential Trading Arrangement (SAPTA) and was approved in January 6th of 2004, during the 12th SAARC Summit held in Islamabad. The objectives of SAFTA is to strengthen intra-

SAARC economic cooperation to maximize the realization of the region's potential for trade and development for the benefit of their people, in a spirit of mutual accommodation, with full respect for the principles of sovereign equality, independence and territorial integrity of all states. In such Nepal as an active member state of SAARC has always been seeking to enact its policy measures with regard to preferences and obligations set up by SAFTA.

4.4.3 BIMST-EC

BIMSTEC was previously established (as BISTEC) in 6th of June, 1997 in Bangkok with the member states, Bangladesh, India, Sri Lanka and Thailand and later in 22nd of December, 1997 Myanmar was introduced. However in February 2004 Nepal and Bhutan were also included in the group and renamed it as Bay of Bengal Initiative for Multi-sectoral Technical and Economic Cooperation, BIMST-EC. It has been mullied over as a bridge between the two organizations, ASEAN and SAARC. Nepal as a member state has been seeking several benefits from BIMST-EC. Some of them are:

- a) Nepal is vying for the extension of its economic relations.
- b) It can be benefited from the agreement made on to develop the Region as a common hub for tourism.
- c) Nepal also can benefit from intra-regional transportation network that has been planed.
- d) Expansion of trade in the region is another important aspect Nepal is looking for.
- e) Foreign Investment can be attracted, since BIMST-EC has declared rather liberal policy than SAFTA and WTO.
- f) Private sector has been considered as an Engine of Growth, and accompanying this fact BIMST-EC has declared a policy of Private-Public Partnership. This also can be a handy move for the Private sector of Nepal.

4.5 Non-Resident Nepalese (NRN) Act, 2007

Another significant move made by the GoN for the establishment of economic diplomacy has been the enactment of NRN Act, 2007. Economic Diplomacy plays

a vital role to flow the capital accumulated by the Non Resident Nepalese in the development process of Nepal. The Act has defined 'Nepalese Living Abroad' as any Nepalese residing and engaged in any job, business or employment in a foreign country for at least two years. As per the Act, 'Non-Resident Nepali' refers to both 'Nepalese Living Abroad' as well as 'People of Nepali Origin'. The Act has made a provision for preparing a record of non-resident Nepalese and providing them with identity cards as well as permitting a 10-year visa for people of Nepali origin and their family. It allows NRNs to invest convertible foreign currency in sectors made open for foreign investment, to open an account in convertible foreign currency and to repatriate any earnings from such proceedings in convertible foreign currency. Likewise, the Act entitles People of Nepali Origin to buy/sale property in Nepal. Besides, with a view to attract NRN investment, the Act has granted tax exemption to NRN on their invested capital fund, fund remitted to close relative (up to Rs 1.5 million per year) and donations made for social, religious, cultural and non-profit works. Overall, the Act has made provision for providing business rights to NRNs similar to that provided to foreigners investing convertible currency and permitting people of Nepali origin to operate industry/business in Nepal like a Nepali citizen.

CHAPTER 5

ANALYSIS OF THE EFFICACY OF ECONOMIC DIPLOMACY IN NEPAL

5.1 Introduction

Nepal's Economic diplomacy has always been guided by the sets of external and internal factors including national economic and political philosophy and temperament. Over the years between I and II People's Movement (Janaandolan), Nepal experienced myriad of situations both in political and economic ground. Since June of 2008, Nepal has been declared a Republican State by abolishing two and a half century long Shah Reign. In this backdrop, the state is undergoing a restructuring phase in response to the people's interests, aspirations and expectations. People's welfare and economic development has been the prime agenda since people are at the centre of politics today. And thus it is inevitable that the interest of people must be invariably reflected in the foreign policies.

If we look at the period between two Mass Movements, we notice that several far-reaching changes have occurred in the politico-economic and social fabric of international relations causing a great metamorphosis in the traditional attitude of diplomacy. Since 1990s Nepalese economy has been into a drive to comply its economy with global trends; efforts to that end have been accelerated through the instrument of economic diplomacy. How much instrumental have been the tactics of economic diplomacy in Nepal is of a grave concern. This necessitates analyzing thoroughly the sectors such as foreign aid, foreign employment, foreign investment, foreign trade and tourism, which are the concern and key issues of economic diplomacy. To acknowledge the real situation of these sectors during the period of FY 00/01 to FY 08/09, they have been thoroughly discussed below.

5.2 Foreign Aid

Resource that is transferred from the advanced countries to the developing countries for the purpose of encouraging economic growth is the Foreign Aid. Billions of dollars is poured every year to the LDCs and DCs, through the channels of bilateral and multilateral frameworks. Thus it is one such area where

the diplomatic missions play a vital role to attract development assistance or foreign aid in a country. Mobilization of foreign aid in Nepal has remained a major policy in our diplomacy in view of the country's weak financial base. The Ministry of Finance and the high level Nepalese delegation to the perennial meeting of Nepal Development Forum have been playing catalytic role in the mobilization of development assistance to Nepal. Also, the Nepalese Missions abroad have been playing prominent roles in this connection.

Historically, the first aid in Nepal is recorded as back in the year 1855 B.S. for Amlekhgunj-Raksaul Railway by India. Later, for the establishment of Biratnagar Jute Mill in 1903 B.S. foreign aid was channeled to Nepal. Receiving of foreign aid from countries other than India was in the forms of money and technical assistance after signing a four-point program with the USA on January 23, 1951. Since then, Nepal has been receiving, generous assistance from its development partners. In the year 1976 the Nepal Aid Group (NAG) was formed to channelize the foreign aid flow; comprising Japan, USA, France, India, the Netherlands, Kuwait, ADB, IMF, IDA etc. and later it was renamed as Nepal Development Forum (NDF). The NDF provides Nepal with 98.5% of the total volume of foreign aid. In the subsequent years of advent of Development Planning, Nepal continually received handsome amount of aid.

The flow of foreign aid has been channeled for the task of economic development and national reconstruction. The Five Year Plans' (FYP) have been incessantly relying upon Foreign aid as the major source of development expenditure. Also, the yearly government Budget has been largely depending upon foreign aid till date. Following the inception of FYP in 2013 B.S. it was channelized on institutional basis.

Table 5.1 shows the nature of foreign aid in successive plans. There has been a steadily increase in the amount of aid since Fourth FYP. In Ninth and Tenth FYP the percentage of Foreign Aid was 58.8 and 57.7 respectively. The proportion of aid in the development plans has been more than half, averaging approximately 55% per annum. In the changed context after *Janaandolan- II* Nepal has

experienced a gross increase in the inflow of foreign aid in response to the prevailing peace process and election of the Constitutional Assembly.

If we closely analyze the pattern of aid over the years we can notice that the major contribution of donor countries has always been focused primarily on sectors such as agriculture, transportation infrastructures, power generation, health and education.

Table 5.1
Percentage of Foreign Aid in Five Year Plans

S.N.	Five Year Plan	% of FA in Total Development Expenditure
1.	First FYP (013 - 018)	90
2.	Second FYP (019 - 022)	80
3.	Third FYP (022 - 027)	56
4.	Fourth FYP (027 - 032)	45
5.	Fifth FYP (032 - 037)	48
6.	Sixth FYP (037 - 042)	68
7.	Seventh FYP (042 - 047)	71
8.	Eight FYP (047 - 054)	66
9.	Ninth FYP(054 - 059)	58.8
10.	Tenth FYP (059 - 064)	57.5
11.	Interim Plan (064 - 067)	78.6

Source: National Planning Commission

From 1950/51 till 1999/00 Nepal received Rs. 19.096 billions as foreign aid. Foreign aid peaked in 1991/92 standing at Rs. 21.1 billions and declined thereafter. The restoration of democracy followed by the new measures of economic policy has been the reason behind such sharp inclination of aid during 1991/92.

According to the Economic Survey 2000/01, in FY 2000/01, total foreign assistance amounted to Rs. 31.29 billions, which was 51.01% of improvement in foreign aid commitment compared to previous year. Of the total foreign aid, the bilateral assistance constituted Rs. 17.49 billions, whereas the multilateral assistance was equivalent to Rs. 13.79 billions. While classifying the foreign aid into grants and loans component for FY 2000/01, foreign grants amounted to Rs.

14.29 billions and foreign loans amounted to Rs. 16.99 billions. According to the Table 5.2 (B), in percentage, the bilateral assistance was 55.90%, while the multilateral aid was 44.10%. Similarly the grant amounted 45.35% and loans amounted 54.65%. Thus the bilateral aid was greater in amount than multilateral aid; at the same time, the amount of loans was greater than grants. In FY 01/02 out of total aid, Rs. 18.44 billions was committed through bilateral diplomatic means where as Rs. 14.79 billions was channeled through multilateral agreements. There was increased aid commitment by 6.2%. In percentage term, bilateral and multilateral aid amounted to 55.49% and 44.51% respectively, where as grants and loans were 70.24% and 29.76% respectively. The bilateral and multilateral aid commitments were also increased by 5.39% and 7.24% respectively compared to previous year's commitment. It shows that during the FY 01/02, as usual, the bilateral aid was greater in amount than multilateral aid; where as the amount of grant was more than double than the amount of loans.

Table 5.2 (A)
Foreign Aid Commitments (Rs. in millions)

FY	Bilateral		Multilateral		Total Commitment	Total Disbursement
	Grants	Loans	Grants	Loans		
99/00	11293.4	--	1566.8	7587.8	20448	17523.9
00/01	14046	3449.9	243.0	13548.0	31287.0	18797.4
01/02	17292.2	1146.5	6048.0	8741.0	33227.7	14384.8
02/03	15183.1	129.3	12174.5	15715.8	43202.7	15885.5
03/04	8223.6	0.00	733.4	14781.0	23738.0	18912.4
04/05	21225.4	0.00	4167.3	12759.6	38152.3	23657.3
05/06	14755.5	0.00	3508.8	2659.9	20924.2	22041.8
06/07	17706.1	0.00	13154.1	6162.7	37022.9	25854.3
07/08	5620.9	7485.5	35443.3	636.5	49186.2	29300.6
08/09*	18814	3541.5	19440.8	1338	43134.3	-----

(* First Eight Months), Source: Economic Survey 08/09; MoF

According to the Table 5.2 (A) and 5.2 (B), in the FY 02/03 bilateral aid was 35.44% of the total aid, standing Rs. 15.31 billions. In the same FY the multilateral aid constituted 64.56%, i.e. Rs. 27.89 billions. The proportion of grants and loans were marked as 63.32% and 36.68%, accounting Rs. 27.36 and Rs. 15.84 billions respectively.

In the FY 03/04 the bilateral aid sharply declined by 44.37% to Rs. 8.22 billions constituting 34.64% of total aid. There was a decline of 45.05% in total aid compared to previous year. At the mean time, compared to the previous year, the multilateral aid was declined by 46.29% to Rs. 15.51 billions, constituting 65.36% of the total aid. There was no loan from the bilateral front in the FY 03/04, where as the multilateral loan agreements were made to inflow Rs 14.78 billions of loans which was 62.27% of the total aid that year. Similarly the commitment of grants was measured as 37.73% of total aid amounting Rs. 8.96 billions.

Outstanding increase of aid (60.72%) was experienced during the FY 04/05 compared to previous year. The total amount of aid committed that year was Rs. 38.15 billions, out of which 55.63% and 44.37% were the proportion of bilateral and multilateral aid respectively. The commitment of grants and loan were measured as Rs 25.39 and Rs. 12.76 billions respectively constituting 64.83% and 35.17% of the total aid.

Table 5.2 (B)
Foreign Aid Commitments (in %)

FY	Percentage			
	Bilateral	Multilateral	Grants	Loans
00/01	55.90	44.10	45.35	54.65
01/02	55.49	44.51	70.24	29.76
02/03	35.44	64.56	63.32	36.68
03/04	34.64	65.36	37.73	62.27
04/05	55.63	44.37	64.83	35.17
05/06	70.52	29.48	87.29	12.71
06/07	47.82	52.18	83.35	16.65
07/08	26.65	73.35	83.49	16.51
08/09*	51.83	48.17	88.69	11.31

(* First Eight Months), Source: Economic Survey 08/09; MoF

Similarly, Tables 5.2 (A), 5.2 (B) and 5.3 combinely show that during the FY 05/06, the foreign aid commitment sharply declined by 45.2% totaling to Rs. 20.92 billions as compared to FY 04/05. Of the total commitment, major chunk of aid (70.52%) was committed by bilateral channels, amounting to Rs. 14.75 billions and multilateral aid contributed Rs. 6.17 billions. While categorizing the total foreign aid, the share of grant assistance constituted 87.29% amounting Rs.

18.26 billions and loan assistance constituted 12.71% amounting Rs. 2.66 billions. In FY 05/06, the foreign grant assistance decreased by 28.02% whereas foreign loan decreased by 79.15% as compared to the previous FY.

The foreign aid commitment in FY 06/07 has increased by 76.9 % against a decline of 45.2% in FY 05/06. In FY 06/07, committed foreign assistance amounted to Rs. 37.02 billions compared to an amount of Rs. 20.92 billions in FY 05/06. Of the total foreign aid commitment, the bilateral assistance constituted Rs.17.71 billions, whereas the multilateral assistance was equivalent to Rs. 19.32 billions. While making a classification of the foreign aid into grants and loans; grants amounted to Rs. 30.86 billions and foreign loans amounted to Rs. 6.16 billions. In FY 06/07 as compared to the previous year, the foreign grants increased by 68.9% and the foreign loans increased by 131.69% respectively.

Table 5.3
Improvement in Foreign Aid Commitments

SN	FY	% increase with respect to previous year				
		Bilateral	Multilateral	Grants	Loans	Total
1	00/01	54.92	50.65	11.11	124.02	53.01
2	01/02	5.39	7.24	63.34	-41.83	6.2
3	02/03	-16.95	88.59	17.21	60.25	30.02
4	03/04	-46.29	-44.37	-67.26	-6.72	-45.05
5	04/05	158.1	9.1	183.49	-13.68	60.72
6	05/06	-30.48	-63.56	-28.07	-79.15	-45.2
7	06/07	19.99	213.14	68.96	131.69	76.9
8	07/08	-25.98	86.78	33.06	31.79	32.85
9	08/09*	70.57	-41.57	-5.65	-39.92	-11.37

(* First Eight Months), Source: Economic Survey 08/09; MoF

Foreign aid commitment in FY 07/08 was increased by 32.85% in comparison to 76.9% growth registered in FY 06/07 than its preceding FY. In monetary term, committed foreign aid accounted Rs. 49.19 billions. Of the total commitment, bilateral assistance constituted 26.93% amounting to Rs.13.106 billions, whereas the multilateral assistance constituted 73.07% totaling to Rs. 36.08 billions. The amount of grants marked Rs. 41.064 billions and loans Rs. 8.122 billions. As

compared to the previous FY, foreign grants rose by 33.06% and loans by 31.79% in FY 07/08.

In the first eight month of FY 08/09, foreign aid commitment decreased by 11.37% to Rs. 43.134 billions compared to the same period of the previous FY. Of the total foreign aid commitment, committed grants accounted Rs. 38.26 billions (88.69% of the total) and the loans Rs.4.879 billions (11.31% of the total). In the first eight months of FY 07/08, the committed foreign aid was amounted to Rs. 48.669 billion, of which grant was Rs. 40.548 billions and foreign loans was Rs. 8.122 billions. Of the total commitment, the shares of grants and loans were 83.31% and 16.69% respectively.

Over the years, the major chunk of foreign aid was distributed mainly in the sectors such as Agriculture, Electricity, Rural Development, Water Supply, Education and Health. Also it is notable that there has been a vast disparity in the aid commitment and disbursement. The last ten years data shows that the disbursement of aid through out the decade has been far below than the commitment. In the FY 00/01 the foreign aid disbursement was amounted to Rs. 18.797 billions which was less than the commitment of Rs. 31.287 billions made during that year. In the subsequent years too, the proportion of disbursement has remained comparatively very lower than the amount committed. According to the table 5.2 (A), during the FY 01/02, the utilization of foreign aid amounted to Rs.14.38 billions, but in the same FY the committed aid was Rs. 33.23 billions. In FY 02/03, the distribution of aid was made up to Rs. 15.89 billions. In the subsequent FY 03/04 and FY 04/05 the utilization of aid was measured to Rs. 18.91 and Rs. 23.66 billions respectively. This implies that the since FY 01/02, the utilization of aid has been continuously increasing till FY 04/05. However the difference in the commitment and disbursement had remained with the similar widening gaps. In FY 05/06 the disbursement exceeded the amount committed reaching Rs. 22.04 billions. Similarly, in the following FY 06/07, major chunk of committed aid was utilized. The amount of utilization recorded Rs. 25.85 billions and in the FY 07/08, the utilization marked Rs. 29.3 billions.

The above explanation shows that the utilization of aid has been considerably lower over the years. The greatest challenge for Nepal in those fiscal years has been the mobilization of aid. Nepal has been incapable of regulating the channeled aid to the targeted sectors. The major chunk of aid over the years has been defrayed for the maintenance of office works of projects and excessive paper-works. This has created a situation of near failure in the Nepalese economic diplomacy, in the sense; the donors have been skeptic of the importance and necessity of aid, and thus raising their concerns over the issue of low utilization of aid. Statistically, only 62.71% of aid has been utilized in the last 10 years period. Out of total aid committed, that is, Rs. 29.72 billions (From FY 99/00 to FY 07/08), only Rs. 18.64 billions have been utilized.

5.3 Foreign Employment

During the oil boom in the 1970s, the labour-surplus economies of South Asia were able to supply cheap labour to meet the growing labour demand in the Middle East Asia (Singh, 2006), although Nepal was a late entry in taking advantage of labour demands. The more formal and temporary migration began after people started to work in British Army following the Sugauli Treaty that was signed on 2nd of December, 1815. This treaty permitted British Gurkhas for military service. In the recent years the scope for out migration for military services has declined and more and more people have migrated for other types of jobs. It was only after the 1990s that policy makers and academicians began to fully acknowledge the importance of remittances send by Nepalese employed abroad for enhancing the livelihoods of the households, including those in rural regions (Pant, 2006).

Foreign employment has been a viable option for Nepal to absorb its growing labor force. While Nepal has been promoting, in recent years, foreign employment to provide jobs to its youth, both skilled and unskilled, the government has been reliant to diplomatic missions to explore employment opportunities for Nepali nationals in the countries of their assignment. These missions need relevant and updated information about the skills available in Nepal for employment abroad.

Needless to point out, foreign employment has become a major source of national revenue to meet both regular and development expenses through remittances amounting to more than 1.5 billions US dollars. The appointment of an economic consular or a labor attaché at diplomatic missions would greatly facilitate the promotion of foreign employment which has by now become an integral part of economic diplomacy.

The tempo of the foreign employment increased dramatically after 1996 due to shrinkage of economic opportunities in the country. At the same time the country was also introduced to the decade long conflict in 1996, which triggered the outflow of many youth workers to different countries. Another major reason for such rapid growth has been the massive unemployment within the country. Globalization norms at its zenith during late 90s and early of the new millennium opened up employment opportunities for professionals and labours in international job markets. On the other hand, the students seeking for higher studies abroad also flew to several countries across the globe in greater numbers, who later were to become the major sources of remittances.

Table 5.4
Country-wise Foreign Employment

S.N.	Country	Total till FY					Grand Total
		04/05	05/06	06/07	07/08	08/09*	
1	Saudi Arabia	131683	19507	30608	42,214	39,406	2,72,089
2	Qatar	148152	58233	48937	83,896	66,031	4,16,021
3	UAE	63585	17184	19442	43,828	26,890	1,76,659
4	Bahrain	4853	530	955	4,335	5,691	16,609
5	Kuwait	8760	738	1956	1,461	1,608	15,008
6	Oman	758	77	465	2,205	3,143	6,692
7	Hong Kong	3167	176	307	189	56	3,949
8	Malaysia	220505	84162	62948	49,445	30,036	4,58,177
9	S. Korea	5480	196	683	0	56	6,497
10	Other Countries	4457	1389	931	1,800	13,866	22,580
	Grand Total	591400	182192	167232	2,29,373	1,86,783	13,94,281

(* First Eight Months), Source: Economic Survey 08/09; MoF

Because of the insufficient employment opportunities, the number of Nepalese going abroad for employment is growing every year. The numbers of countries for

foreign employment opportunities have reached to 107 till mid-May of 2009. The rate to the Arabian countries excluding Malaysia and South Korea is considerably high. In the Table 5.4 it is shown that, by the end of FY 06/07, the total number of people going abroad with institutional approval reached 978,125. Likewise 229,373 people received approval during FY 07/08. In addition, 186,783 more persons received approval making the total of 1,394,281 employees abroad till first eight months of FY 08/09. Observation of the trend of Nepalese seeking jobs abroad, the majority of them, i.e. 458,177 persons (32.9 %) have gone to Malaysia followed by 416,021 (29.8 %) to Qatar. The third destination is Saudi Arabia 272,089 (19.5 %). Similarly, 176,659 (12.7 %) to U.A.E., 15,008 (1.1 %) to Kuwait, 16,609 (1.2 %) to Bahrain, 6,457 (0.5 %) to South Korea 6,692 (0.5 %) to Oman, 3,949 (0.3 %) to Hong Kong, and 22,580 (1.6 %) Nepalese have gone in other countries for employment. (See Table 5.4)

5.3.1 Remittances

Remittances are “the portion of international migrant worker’s earnings sent back from country of employment to the country of origin” (Puri and Ritzema, 1999). The term ‘remittance’ is normally limited to denote monetary and other cash transfers, transmitted by migrant workers to their families and communities (NLSS, 1996). The IMF has a broader definition, which includes three categories:

- Workers remittances or transfers,
- Compensation to employees or the wages, salaries, and other remuneration, in cash or in kind, paid to workers working in countries other than they legally reside,
- Migrant transfers that involve capital transfers of financial assets as they move from one country to another and stay for more than a year.

Foreign employment has been a perennial source of remittances in recent years, which has been instrumental in employing great number of unemployed Nepalese youths abroad. The prospects for foreign employment, especially of middle level Nepali manpower, have risen to greater extent in recent years. Earlier, Nepalese went abroad as semiskilled laborers, drivers or bricklayers, while recent trend

shows that even professionals and college graduates have been migrating increasingly to different parts of the world. However, the out-flows of such skilled personnel have frequently been restrained in their mobility by the rigorous immigration laws and regulations obliged by advanced economies contrary to the spirit of globalization and liberalization. In such, the diplomatic maneuver in solving these hindrances must be entertained to guarantee the easy access for migrant workers to foreign job markets. This is a viable approach for the country like Nepal. It is evident that the greater amount of remittance each year is a manifestation of hard work and commitment of Nepalese migrant workers.

The trend of remittance inflow in Nepal in the past shows that it has been a crucial part of the country's total GDP. According to the Table 5.5, as of the past record, Rs. 4.722 billions (10.3% of annual GDP) of remittance was recorded in FY 01/02. However, the remittance in the following FY 02/03 amounted to Rs. 4.754 billions rose just by 0.7% from previous year. In the same FY the contribution of remittance to GDP (at Producers Price) was measured as 11%. In the FY 03/04 the remittance increased by 14% to Rs. 5.420 billions, and the contribution to annual GDP was measured as 10.9%.

Table 5.5

Annual % Change in Remittance (Rs. in billions)

FY	Annual % increase	Annual Remittance	% of GDP at PP
01/02	--	4.722	10.3
02/03	0.7	4.754	11.0
03/04	14.0	5.420	10.9
04/05	8.1	5.859	11.1
05/06	11.9	6.554	14.9
06/07	49.05	9.769	13.8
07/08	2.51	10.014	17.4
08/09 ^e	82.75	18.301	19.1

^eAnnual Preliminary Estimates based on 8 months data;
Source: Economic Survey 08/09, MoF

Similarly according to Table 5.5, in the FYs 04/05 and 05/06 the change of remittance flow rose by 8.1% and 11.9% respectively than the previous year. In FYs 04/05 the total remittance reached Rs. 5.859 billions constituting the share of

11.1% of annual GDP at PP. In the following FY 05/06 remittance inflow was registered as Rs. 6.554 billions and the share of it on annual GDP was 14.9%. However, in the FY 06/07 the inflow recorded a phenomenal increase of 49.05% to Rs. 9.769 billions constituting 13.8% of real GDP. In the subsequent FY 07/08, only a minor increase of 2.51% over previous year was experienced leading to a collection of Rs. 10.01 billions constitute an outstanding share of 17.4% of GDP. The income from remittance, which amounted to Rs. 8.242 billions in the first eight months of the FY 07/08, has risen by 58.9% to Rs. 13.10 billions in the same period of FY 08/09.

The total annual remittance in the FY 08/09 has been estimated preliminarily to rise by 82.75% to Rs. 18.301 billions constituting a share of 19% of the total GDP in Producers Price. In a situation where cheap labor force or service is being exported due to absence of economic structure necessary for diversification of production and exports of goods and services, labors have been returning from a number of countries facing the global downturn. It is a challenge for the Nepalese diplomatic missions abroad to ensure the shrinking opportunities for nationals in the foreign job markets. This is possible only through appropriate diplomatic approach and thus the role of economic diplomacy is catalytic in this regard.

As a result of the present global downturn, the World economy is rapidly shrinking and the trickle-down effect is slowly making its impact in foreign employment opportunities and the inflow of remittance in Nepal. The share of remittance constitutes approximately 20% of the total national GDP; which provides a glimpse of its eminent role in the make over of fragile economy. Thus, seeking its indispensable contribution, the major thrust of economic diplomacy must be directed to cast down the possible long-term serious effects in the foreign employment opportunities and the inflow remittance, which has been a strong pillar of the Nepalese economy over the years. Hence, the promotion of foreign employment amidst this unfavorable situation is a major challenge of Nepalese economic diplomacy.

5.4 Foreign Investment

Foreign Investment (Direct and Portfolio) is defined as the transfer of foreign capital from one country and its national body or corporate into another for the primary purpose of profit to the investors. It is a component of an economic integration in the process of globalization towards the global village norms. Foreign investment in the developing countries plays a crucial role for the economic development process, as it brings capital, technology and marketing skills. In other words, foreign investment is one such boon which is capable of propelling the economic development in the countries which are intrinsically triggered by the deficiency of capital and technology.

Foreign investment shaped into today's form particularly after 1970s liberal economic policies. The establishments of multinational and transnational corporations, deregulation of domestic economy by the government, liberal economic policies, privatization of state-owned industries, competitive market economy and many other factors have made the strategy of foreign investment a strong economic trend in post cold war era. In nutshell, it can be said that the policies of liberalization and privatization were two such factors which motivated the practice of foreign investment. Today, governments of most of the countries offer protection, facilities or incentives to attract more foreign investment. However it is noteworthy that unlike in aid, the recipient government or country does not possess the capital invested into country. It simply monitors and regulates the inflow of foreign investment through policy formulation and imposition of rules which are not strictly unfavorable to the investors.

Foreign investment and technology transfer is essential for leading the nation's economic system towards attainment of self-sufficiency through building a robust, strong, dynamic and competitive economy through optimum utilization of available natural and human resources. Foreign investment fosters capital, modern technology, managerial and technical skills, access to international market, and culture of professional competition. In addition to this, the country heads for a strong and independent economy on the foundation of rapid industrialization and

internal revenue generation. In this backdrop, “the possible significant role of FDI in developing countries like Nepal makes it as an alternative source of foreign capital, in stead of foreign debt. Therefore, in Nepal, the structural adjustment adopting the philosophy of globalization, liberalization and privatization has been followed for attraction of FDI in the south regional competition” (Bista, 2005).

Although the agriculture sector has been prioritized in Nepal, the distribution and incident of FDI inflow has been characteristically greater in the manufacturing sector than any others. Diplomatic missions have been driven to attract more FDI in the areas such as hydropower, tourism, biodiversity and education where Nepal has both comparative advantage and competitive edge. Despite the several efforts to attract as much FDI as possible through an attractive package of incentives, a lot has remained to make the effective promotional activities in such areas.

Some of the important government measures for ensuring foreign investment in Nepal can be summed up in the following lines. Foreign Investment and Technology Transfer Act has been amended to ensure effectiveness and align it with changing times and for opening the door for foreign investment in new sectors. One-Window Committee has been reformed for an easy access to tax exemption and duty drawback facilities for industries. With the objective of granting necessary permission, services and facilities to foreign investors through one-window system for attracting foreign investment as per the existing Act to achieve rapid economic growth in the country, Foreign Investment Promotion Committee Working Procedure (2005), is already in effect. Likewise, considering foreign investment, which is essential for country’s economic growth, new industrial and foreign investment policy has been targeted to introduce in the FY 2008/09 to achieve the economic growth rate as envisaged through Public–Private Partnership. Special attention has been paid for easy processing, promotion of technology transfer, flow of foreign investment, productivity and enhancement of industry’s work efficiency of the private sector to be able to compete in global market by utilizing the comparative advantage as per the proposed policies (Economic Survey, 2009).

At present, all areas have been opened up for foreign investment in Nepal, with the exception of traditional cottage industries and other few specific types of industries related to defense, public health and environment. The policies of Government of Nepal to attracting foreign investment have produced some positive output. This can be known by the fact that foreign investment in 59 industries in 1988 reached to 503 in 1999 with the total foreign investment of Rs. 63.29 billions. Also, these industries generated more than 70,000 direct employment opportunities.

The history of foreign investment goes back with the establishment of first modern mill namely Biratnagar Jute Mill in 1936. In this mill Indian industrialist Radha Krishna Chamadiya had invested 60% share and the then Prime Minister Juddha Shamsheer, other high class Ranas and high level non-Rana officials have invested 40%. After the establishment of jute mill the same investor had invested in cotton mill, sugar mill, chemical industries and rice mill in the different years (Ojha, 2000).

Only after mid 1970s the joint venture industries started to increase satisfactorily particularly in medium scale industries. At the end of Panchayat regime in 1989 the number of industries having foreign investment reached 71 (Gautam, 2006). After the restoration of democracy in 1990s along with the commencement of liberal economic policies, the number of foreign invested industries began to rise significantly. However, the manufacturing sector accounted more than half of the investments followed by tourism, service and agriculture. Of the late, interest of the foreign investors has shifted to hydropower, communication and education.

The dominance of India has ever remained at top in the country-wise investments. India is followed by countries such as USA, UK, Japan, China, Germany etc. in the list of the higher investments. However in recent years some of the EU member countries, Australia, South Korea etc. are also vigorously investing in Nepal. Tables 5.6 and 5.7 show the recent trend of countries investing in Nepal.

In FY 2000/01 a total of 96 Joint Venture industries were issued permits with the total project cost of Rs. 7.9 billions. Out of these 96 industries, 54 were related with production of goods, 19 with hotel and resort, 13 with service industries, 4 belonged to electricity, drinking water, and cooking gas and 6 were related with transport and communication, housing and construction and agro forestry. The country wise involvement revealed that India invested in 37 industries, China in 15, Japan in 8, UK and USA each in 7, South Korea in 5, Austria, Finland, Spain and Switzerland each in 2 and other 9 countries involved in one each industry.

According to Table 5.6, a total of 76 enterprises with the project cost amounting to Rs. 3.31 billions were granted permission for foreign investment in FY 2001/02. Out of 76 industries permitted, 37 were related with production of goods, 13 with hotels and resorts, 20 with service industries, 1 with energy and 5 belonged to construction and agriculture. Observation of country-wise involvement in industries revealed that Indian investment turned out to be in 20, Chinese in 12, Japanese in 8, United States of America in 7, South Korea and Germany each in 4, United Kingdom, Italy, Israel and Poland each in 2, and other 12 countries were involved in one each enterprise.

In FY 2002/03, 71 such industries with the total project cost of Rs. 4.88 billions were approved. Rs. 1.77 billions was the foreign investment in this FY. Out of total industries, 27 were industrial production, 22 tourism, 11 services, 3 energy and 8 construction and agriculture industries. Foreign Investment in 23 industries were from India, 12 from China, 7 from Japan, 5 from USA, 6 from S. Korea, 4 from Germany, 2 each from France and Pakistan. Other 10 countries also invested in one each industry.

In the table 5.6, it is shown that, of the total 78 industries approved in FY 2003/04, each of 24 industries were related to production and service sector, 27 to hotel & resort, 1 to construction and 2 to the energy sector. Analyzing the investment on country-wise basis, foreign investment in 16 industries were from China, 10 from India, 9 each from Japan and South Korea, 4 each from UK and USA, 3 each from France and Switzerland, 2 each from Taiwan, Bangladesh,

South Africa, Singapore and Hong Kong and 10 from other countries. The total project cost of these industries accounted Rs. 4.32 billions with foreign investment of Rs. 2.76 billions.

Table 5.6
Country-wise Foreign Investment in Industries

SN	Countries	FY 01/02	FY 02/03	FY 03/04	FY 04/05	FY 05/06	FY 06/07	FY 07/08	FY 08/09*
1	India	20	23	10	15	31	28	37	27
2	China	12	12	16	12	21	38	39	46
3	Japan	8	7	9	5	10	15	5	5
4	USA	7	5	4	3	9	23	13	7
5	UK	2	-	4	3	8	14	19	9
6	S. Korea	4	6	9	7	9	15	23	4
7	Germany	4	4	-	3	3	7	11	2
8	Netherlands	1	-	-	1	3	-	6	2
9	France	-	2	3	-	3	7	3	4
10	Others	18	12	23	13	19	41	56	30
	Total	76	71	78	64	116	188	212	136

(* First Eight Months), Source: Various issues of Economic Survey, MoF

According to Table 5.6, 64 industries with foreign investment of Rs. 1.8 billions were permitted to operate in FY 2004/05. The total foreign investment in this FY accounted Rs. 1.64 billions. Out of total, 25 industries were related to production sector, 24 to service, 12 to tourism, 2 to construction and 1 to agriculture sector. From the points of view of the country-wise investment, India was involved in 15 industries, China in 12, South Korea in 7, Japan, USA, UK and Germany in 3 industries each, Russia in 2 and other 13 countries were involved in one each.

In the FY 05/06 India, China and Japan were the major three countries investing on 31, 21 and 10 industries respectively. The same year USA and South Korea invested in 9 industries each followed by UK in 8 industries. In totality the FY 05/06 accounted 116 foreign invested industries with the total project cost of Rs. 4.12 billions and the foreign investment of Rs. 2.61 billions. Among these 116 industries, 33 were related to the industrial production, 40 were related to service industry, 38 to tourism, 2 to construction and 3 were related to energy sector.

In the subsequent FY 06/07, the total number of foreign invested industries alarmingly grew to 188 with the fixed capital of Rs. 2.65 billions, the project cost of Rs. 3.43 billions and the foreign investment of Rs. 3.23 billions, out of which India, China and USA invested in 28, 38 and 23 industries respectively. Japan and South Korea invested in 15 industries each followed by UK in 14. Among these 188 industries, 40 were related to the industrial production, 88 service, 55 tourism, 2 construction, 1 each were Energy, Agriculture and Mines industry.

In the FY 07/08 total of 212 industries were granted permission to establish on joint venture with fixed capital of Rs. 16.90 billions, project cost of Rs. 20.40 billions and foreign investment of Rs. 9.81 billions. Of the total industries granted permission for foreign investment in the FY 2007/08, 51 were related to industrial production, 55 were service industries, 67 were tourism industry, 13 were construction industries, 8 were energy, 11 were agriculture, and 7 were mining industries. From country-wise investment perspective in these industries, China invested in 39 industries, India in 37, South Korea in 23, UK in 19, USA in 13, Germany in 11, Australia in 8, Netherlands in 6, Japan in 5 and others in 40.

In the first eight months of the current fiscal year 08/09, permission has been granted to 136 industries with the fixed capital of Rs. 6.62 billions, project cost of Rs. 7.49 billions and foreign investment of Rs. 5.14 billions to establish industry in foreign and joint investment. Of the 136 industries permitted for such investment, 25 are in production sector, 38 are in service industry, 45 are tourism, 7 are energy, 3 are agriculture, and 17 are in mineral sector. Country-wise, 46 industries are invested by China, 27 by India, 9 by UK, 7 by USA, 5 by Japan, 4 each by France, Singapore and S. Korea and 2 each by Germany, Netherlands, Spain and Switzerland and 24 by others. (See Table 5.6)

To attract foreign investment through adoption of relevant, practical and liberal policy, in totality 1,743 industries were granted permission until the first eight months of FY 2008/09. Fixed capital of those industries stands at Rs. 108 billions with their total project cost of Rs. 131 billions. A total of Rs. 52 billions as foreign

investment in these industries has been recorded. Once in operation, these industries are capable of generating 139,592 employments for Nepalese citizens.

If we look at the sector-wise distribution of foreign investment, the production industry has greater attraction. Till the mid March of 2009, total of 634 production industries has been permitted for foreign investment with the total project cost of Rs. 44.73 billions. The fixed capital of these industries has been Rs. 31.85 billions with a total of 38.51% foreign investment with respect to total project cost. The foreign investment amounts Rs.17.23 billions in these industries which are expected to generate 72,941 employments.

Table 5.7
Industries Permitted for FI by mid-March 2009 (Rs. in millions)

Types of Industry	Nos.	Total Project Cost	Total Fixed Capital	Foreign Investment	% of Foreign Investment	Expected no. of Employees
Production	634	44,726	31,852	17,225	38.51	72,941
Service	482	25,033	20,586	11,497	45.93	25,285
Tourism	479	18,372	17,307	6,850	37.28	22,099
Construction	40	3,436	2,548	2,595	75.52	2,890
Energy	37	4,372	3,822	2,651	60.64	2,848
Agriculture	21	5,400	4,094	2,881	53.35	4,219
Mines	50	29,359	27,526	8,444	28.76	9,310
Total	1743	1,30,698	1,07,735	52,143	39.9	139,592

(* First Eight Months), Source: Economic Survey 08/09, MoF

Similarly, next better opted sector has been Service followed by Tourism. In both of these sectors, foreign investments have been made in 482 and 479 industries respectively. The total project costs of permitted industries of service and tourism sector have been Rs. 25.03 billions and Rs. 18.37 billions with the total fixed capital of Rs. 20.59 billions and Rs. 17.31 billions respectively. In these two sectors, the foreign investment of 45.93% and 37.28% of total project cost amounting Rs. 11.497 billions and Rs. 6.85 billions respectively have been made. These industries are capable of producing more than 48 thousand employments.

In the late years Mining industry has emerged as one of the major foreign investing sectors. According to Table 5.7, in totality 50 industries which have

been permitted in the mine sector have the total project cost of Rs. 29.36 billions with the fixed capital of Rs. 27.53 billions. The amount of foreign investment in these industries is Rs. 8.44 billions which is 28.76% of the total project cost. By the commencement of these industries, 9310 jobs will be created. On the other hand Construction, Energy and Agriculture are those sectors in which foreign investors have the share of more than half of the total project cost. More precisely, in Construction, Energy and Agriculture sectors the numbers of industries permitted for foreign investment are 40, 37 and 21 respectively. These industries have the total project costs of Rs. 3.44 billions, Rs. 4.37 billions and Rs. 5.4 billions respectively, out of which 75.52%, 60.64% and 53.35% of respective costs are managed through foreign investments. These industries have the total fixed capital of Rs. 2.55 billions, Rs. 3.82 billions and Rs. 4.09 billions respectively. The foreign investments in the industries related to sectors like Construction, Energy and Agriculture have been Rs. 2.59 billions, Rs. 2.65 billions and Rs. 2.88 billions respectively and are capable of producing approximately 10 thousand jobs.

In nutshell, the foreign investment in Nepal has been characteristically increasing every year. However, the inflow has remained greater within the manufacturing, service and tourism sector over the years. Only a small scale of foreign investment has been poured into construction, mining and agro-based industries compared to the industries of other sectors. Foreign investment in areas such as hydro power, human resources and biodiversity has greater prospects as ever, though, has remained very low. The major reason behind it has been the breach in peace for a decade since 1996 to 2006. However, the ongoing peace process is at the core of attention of the foreign investors. Since the political soundness is sine quo non for enhancement of inflow of foreign investment, the investors are eagerly waiting for the logical conclusion of the ongoing peace process. Peace is the prerequisite for the conducive environment for foreign investment. It is evident from the fact that in the FY in the FY 07/08 the amount of foreign investment significantly increased from Rs. 3.23 billions of previous FY to Rs. 9.81 billions. Similarly in the review period of FY 08/09 the foreign investment accounted Rs. 5.14 billions.

This concludes that along with the diplomatic maneuver the internal stability is also essential for creating a better investing environment for foreign investors.

5.5 Foreign Trade

The notion of 'Trade, not Aid' is prevalent in the present world. It is no doubt a more powerful catalyst of sustained development than any others. Thus, participation in as many regional and international trade fairs as possible has been the motto of Nepal in recent years. The fact is that the economic progress and prosperity depends on beneficial relationships with other countries particularly in trade. Each country at present wants to penetrate into other countries with its goods, services, labor and investment. The philosophy of economic globalization and liberalization has also made it increasingly difficult to draw a clear-cut distinction between what is domestic and what is international. Thus the foreign trade issue has greater impact on other economic issues and in this process, economic diplomacy involves in enhancing greater possibilities in the former. Since Nepal's ties with the immediate neighbors as ever have remained in a balanced and harmonious basis, the prospect of foreign trade in these countries has also remained soaring over the years. However, the fate is that no such phenomenal improvements in tapping the trade benefits have been possible. As a result of this, the foreign trade in Nepal has always been characterized by the growing deficit. In this light, the promotion of export trade is inevitable and thus it has gained priority on Nepal's economic diplomacy.

Seeking the immense importance of foreign trade the Nepalese missions abroad have been constantly directed to carry out activities to promote foreign markets for Nepalese products in the host countries. "Export promotion was a priority issue even before the introduction of the liberal market economy at the early 1970s. The government became seriously involved in export promotion and diversification, especially with the establishment of the Trade Promotion Center in 1971" (Shrestha, 1996). The effort gained greater momentum after the restoration of democracy while tracking the concept of globalization. The inception of liberalization of economy in the dawn of 1990s decade also added

impetus on expanding the foreign trade in export promotion front. Since then a number of policies and strategies have been introduced.

Now or then, the share of foreign trade has been heavily dependent upon India. Other countries include USA, Germany, Switzerland, Bangladesh, China, Japan, UK, France, other EU member countries etc. The major exporting items from Nepal to these trading nations are: Handmade Woolen Carpets, Pashmina Products, Handicrafts, garments, Pulses (Lentils), Gold and Silver Jewelries, Cardamom, Coffee, Beetle-nuts, tea and coffee and Floriculture, goatskins, etc. The situation of foreign trade in Nepal has been thoroughly discussed in the following paragraphs with tables.

According to Tables 5.8 and 5.9, in the FY 2000/01, the share of India revived by 17.02% than the previous FY and remained 41.58% accounting to Rs. 71.24 billions, and the share of third countries also improved by 2.70% and remained 58.42% accounting to Rs. 100.1 billions in the total volume of trade. As a result of this the net trade increased by 8.22% to Rs. 171.34 billions. Of the total export of Rs. 55.65 billions which was increased by 11.70%, the share of India and of third countries remained 46.77% and 53.23% accounting to Rs. 26.03 and Rs. 29.62 in billions with the increase of 22.66% and 3.57% respectively. Similarly, on imports, the share of India and third countries remained 39.08% and 60.92% accounting Rs. 45.21 and Rs. 70.48 in billions with the increase of 14% and 2.37% respectively out of the total imports of Rs. 115.69 billions which was increased by 6.62%. The trade balances with India and the third countries remained deficits, accounting Rs. 19.18 and Rs. 40.85 in billions with the share of 31.95% and 68.05% respectively of the total deficit of Rs. 60.03 billions with 2.30% increase.

In the following FYs 01/02 and 02/03 the share of India in exports became more than half of the total. The export to India was measured 59.55% and 52.93% accounting Rs. 27.96 billions with increase of 7.4% and Rs. 26.43 billions with the decline of 5.46% respectively in the successive FYs. The share of the third countries was accounted to Rs. 18.89 billions with the sharp decline of 35.9% and

Rs. 23.50 billions with the increase of 23.76% which were 40.45% and 47.07% of the total exports of Rs. 46.9 and Rs. 49.93 in billions respectively in the successive FYs. In those two FYs the imports to India also were more than half of the total imports. India shared 52.73% and 57.03% of imports accounting to Rs. 56.62 and Rs. 70.92 in billions with the respective increases of 25.24% and 25.26%. Similarly, the third countries shared 47.27% and 42.97% of the total imports accounting to Rs. 50.76 billions with the decline of 27.97% and Rs. 53.42 billions with the increase of 5.24% respectively in the successive FYs of 01/02 and 02/03. The share of India in the total trade in these FYs improved by 18.73% and 15.11% and reached to Rs. 84.58 billions (54.8%) and Rs. 97.35 billions (55.86%) respectively and the share of the third countries declined by 30.31% to Rs. 69.76 billions (45.2%) in FY 01/02 and improved by 10.28% to Rs. 76.93 billions (44.14%) in the next FY 02/03. The total trade declined by 9.93% in FY 01/02 and improved by 12.94% in FY 02/03, accounting Rs. 154.33 and Rs. 174.28 in billions respectively. (See table 5.8 and 5.9)

Table 5.8
Share of Foreign Trade (in %)

FY	Export To (%)		Import From (%)		Total Trade (%)	
	India	Other Countries	India	Other Countries	India	Other Countries
00/01	46.77	53.23	39.08	60.92	41.58	58.42
01/02	59.55	40.45	52.73	47.27	54.80	45.20
02/03	52.93	47.07	57.03	42.97	55.86	44.14
03/04	57.09	42.91	57.78	42.22	57.58	42.42
04/05	66.29	33.71	59.34	40.66	61.29	38.71
05/06	67.59	32.41	61.65	38.35	63.18	36.82
06/07	70.27	29.63	59.51	40.49	62.03	37.97
07/08	65.05	34.95	64.15	35.85	64.34	35.66
08/09*	60.32	39.68	56.85	43.15	57.55	42.45

(* First Eight Months), Source: Various issues of Economic Survey, MoF

The trade balances with India and the third countries remained deficits in FY 01/02, accounting Rs. 28.67 billions with the increase of 49.45% with India and Rs. 31.78 billions with the decline of 28.55% with third countries and with the respective shares of 47.43% and 52.57% of the total deficit of Rs. 60.44 billions

which increased by 0.68%. Similarly, in FY 02/03, the deficits with India increased by 55.21% to Rs. 44.49 billions and with the third countries it declined by 5.82% to Rs. 29.93 billions. The total deficit during this FY remained Rs. 74.42 billions with the increase of 23.12%. The export and import ratio remained 43.7% and 40.2% in the successive FYs and the role of exports and imports on GDP in producer's price remained 10.2% and 23.4% respectively in the FY 01/02 and 10.1% and 25.3% in the FYs 01/02 and 02/03 respectively. The BOP situations in these two FYs were Rs. 3.34 billions deficit and Rs. 4.36 billions surplus in the respective FYs of 01/02 and 02/03. It is noteworthy that, since FY 00/01, estimates of remittance have been presented in a new format of BOP.

Similarly, as shown in the Tables 5.8 and 5.9, the total trade during the FY 03/04 increased by 9.13% to Rs. 190.19 billions, out of which the shares of India and the third countries increased by 12.49% and 4.87% to Rs. 109.52 and Rs. 80.67 in billions with the share of 57.58% and 42.42% respectively. This was followed by the improvement of 9.46% in total trade to Rs. 208.18 billions in the FY 04/05. Of the total, share of India improved by 16.51% to Rs. 127.59 billions with the share of 61.29% and there was a slight decline of 0.1% to Rs. 80.59 billions with the share of 38.71% of total trade to third countries in the same FY. Mean while, exports during the FY 03/04, which improved by 7.97% to Rs. 53.91 billions, also revived in the FY 04/05 with a net gain of 8.89% reaching Rs. 58.71 billions. Exports to India increased by 16.45% to Rs. 30.78 billions, but that to third countries declined by 1.56% to Rs. 23.13 billions in FY 03/04. In the following FY 04/05, export to India increased significantly by 26.45% to Rs. 38.92 billions, but that to third countries declined by 14.46% to Rs. 19.79 billions. As a result, shares of India and the third countries in FY 04/05 were 66.29% and 33.71% against that of 57.07% and 42.91% respectively of the previous FY 03/04.

As shown in the Table 5.9, in terms of imports, it improved by 9.7% to Rs. 149.47 billions in FY 04/05 which was improved by 9.6% to Rs. 136.28 billions in the previous FY 03/04. Imports from India and the third countries increased in the FY 03/04 by 11.02% and 7.69% to Rs. 78.74 and Rs. 57.54 in billions, i.e. in share

terms it is 57.78% and 42.22% of total imports respectively. This was followed by the corresponding improvements of 12.62% and 5.67% to Rs. 88.68 billions and Rs. 60.79 billions, with the respective share of 59.34% and 40.66% of the total imports in FY 04/05. During the FY 03/04 the trade deficit with India grew up by 7.79% to Rs. 47.96 billions followed by a smaller increase of 3.75% to Rs. 49.76 billions in the FY 04/05. With third countries the deficit grew up by 19.2% to Rs. 41.01 billions in the FY 04/05, which was increased by 14.96% to Rs. 34.40 billions in the previous FY. The total deficits in the FYs 03/04 and 04/05 accounted Rs. 82.37 billions and Rs. 90.77 billions with the respective increase of 10.68% and 10.2% respectively. On the other hand, imports from the third countries during these two successive FYs increased by 7.7% and 5.67% to Rs. 57.54 and Rs. 60.79 in billions with the share of 42.22% and 40.66% respectively.

Table 5.9
Share of Foreign Trade (Rs. in billions)

FY	Export To			Import From			Trade Balance (With)			Total Trade (With)		
	India	Others	Total	India	Others	Total	India	Others	Total	India	Others	Total
00/01	26.03	29.62	55.65	45.21	70.48	115.69	-19.18	-40.85	-60.03	71.24	100.10	171.34
01/02	27.96	18.99	46.94	56.62	50.77	107.39	-28.67	-31.78	-60.44	84.58	69.76	154.33
02/03	26.43	23.50	49.93	70.92	53.43	124.35	-44.49	-29.93	-74.42	97.35	76.93	174.28
03/04	30.78	23.13	53.91	78.74	57.54	136.28	-47.96	-34.40	-82.37	109.52	80.67	190.19
04/05	38.92	19.79	58.71	88.68	60.80	149.47	-49.76	-41.01	-90.77	127.59	80.59	208.18
05/06	40.71	19.52	60.23	107.14	66.64	173.78	-66.43	-47.12	-113.55	147.86	86.16	234.01
06/07	41.73	17.65	59.38	115.87	78.82	194.69	-74.14	-61.17	-135.31	157.60	96.48	254.08
07/08	38.56	20.71	59.27	142.38	79.56	221.94	-103.82	-58.85	-162.67	180.93	100.27	281.20
08/09*	26.72	17.58	44.29	100.07	75.95	176.02	-73.35	-58.38	-131.73	126.79	93.53	220.32

(* First Eight Months), Source: Various issues of Economic Survey, MoF

According to Table 5.9, the trade deficits with India and the third countries in FY 03/04 increased by 7.79% and 14.96%, accounting Rs. 47.96 and Rs. 34.4 billions with the respective shares of 58.23% and 41.77%. The total deficit accounted Rs. 82.37 billions with the increase of 10.68%. Similarly, in FY 04/05 deficits increased by 3.75% and 19.2%, accounting Rs. 49.76 and Rs. 41.01 in billions with the respective shares of 54.82% and 45.18% with India and the third countries. The total deficit accounted Rs. 90.77 billions with the increase of

10.2%. The export and import ratio remained 39.6% and 39.3% in the successive FYs. The role of exports and imports on GDP in producer's price remained 10.1% and 25.3% in the FY 03/04 and 10% and 25.4% respectively in the FYs 04/05. The BOP situations in these two FYs remained surplus of Rs. 16.01 and Rs. 5.74 in billions in the successive FYs.

It is shown in the Tables 5.8 and 5.9 that, during the FY 05/06 the trade with India was improved by 15.88% to Rs. 147.86 billions which is 63.18% of the total trade, followed by a less increase of 6.59% to Rs. 157.6 billions, which is 62.34% of the total trade in FY 06/07. The trade with third countries also increased by 6.91% and 11.98% to Rs. 86.16 and Rs. 80.59 in billions, which are the share of 36.82% and 37.97% of the total trade in the FYs 05/06 and 06/07 respectively. As the result of it, both the FYs experienced increases in the size of overall trade. In the FY 05/06 total trade reached to Rs. 234.01 billions with an increase of 12.41% with respect to previous FY, where as in the following FY 06/07, it reached to Rs. 254.08 billions by an increase of 8.57% than the previous FY.

While looking at the exports in FYs 05/06 and 06/07, the share of India increased in both the years with 4.62% and 2.49% to Rs. 40.71 and Rs. 41.73 in billions which were 67.59% and 70.27% of the total export respectively. However the share of third countries declined both the years with 1.36% and 9.56% to Rs. 19.52 and Rs.17.65 in billions in the successive FYs 05/06 and 06/07. The share of third countries in total export accounted 32.41% and 29.63% respectively. In totality the export in the FY 05/06 increased by 2.60% and reached to Rs. 60.23 billions, where as in FY 06/07 declined by 1.41% and reached Rs. 59.38 billions.

Similarly as shown in the Table 5.9, in the imports front, the share of India in FYs 05/06 and 06/07 reached to Rs 107.14 and Rs. 115.87 in billions with the increase of 20.83% and 8.15% respectively. The share of India in the total import accounted 61.65% and 59.51% in the successive FYs of 05/06 and 06/07. During the same FYs, the import from third countries accounted Rs. 66.64 and Rs. 78.82 in billions with the respective increase of 9.60% and 18.29%. The shares of third countries were measured 38.35% and 40.49% in these FYs respectively. Thus the

overall imports in these successive FYs accounted Rs. 173.78 billions with an increase of 16.26% and Rs. 194.69 billions with an increase of 12.03%.

On the other hand, the balance of trade, both the FYs 05/06 and 06/07 experienced heavy increase of trade deficits as shown in Table 5.10. In these successive FYs, the trade deficits grew up by 25.09% and 19.17% to Rs. 113.55 and Rs. 135.31 in billions respectively. With the sharp increase of 33.50% and 11.61%, the share of India in the total trade deficit accounted Rs. 66.43 and Rs. 74.14 in billions in the successive FYs. Similarly the share of third countries accounted Rs. 47.12 and Rs. 61.17 in billions with the increase of 14.9% and 29.82% in the successive FYs.

Table 5.10
Annual % Change in Foreign Trade

FY	Annual % Change of Export			Annual % Change of Import			Trade Deficit increase %	Ex/Im Ratio	BOP (Rs. In Billions)	% per GDP in PP	
	India	Third Countries	Total	India	Third Countries	Total				Export	Import
00/01	22.66	3.75	11.7	14.0	2.37	6.62	2.3	48.1	5.21	13.6	28.2
01/02	7.4	-35.9	-15.7	25.24	-27.97	-7.2	0.68	43.7	-3.34	10.2	23.4
02/03	-5.46	23.76	6.4	25.26	5.24	15.8	23.12	40.2	4.36	10.1	25.3
03/04	16.45	-1.56	7.97	12.62	7.7	9.6	10.68	39.6	16.01	10.0	25.4
04/05	26.45	-14.46	8.89	5.67	5.67	9.7	10.2	39.3	5.74	10.0	25.4
05/06	4.62	-1.36	2.6	20.83	9.6	16.26	25.09	34.7	25.7	9.2	26.6
06/07	2.49	-9.56	-1.41	8.15	18.29	12.03	19.17	30.5	5.9	8.2	26.7
07/08	-7.6	17.31	-10.7	22.87	0.94	13.99	20.22	26.7	29.66	7.5	26.6
08/09*	3.6	46.13	17.1	13.12	48.67	26.1	29.47	24.1	30.01	7.2	28.1

* Based on first eight months data with comparison to the same period of previous FY

Source: Various issues of Economic Survey, MoF

The trade deficits with India and the third countries in FY 05/06 increased by 33.5% and 14.9%, accounting Rs. 66.43 and Rs. 47.12 in billions with the respective shares of 58.5% and 41.5%. The total deficit accounted Rs. 113.55 billions with the increase of 25.1%. Similarly, in FY 06/07 deficits increased by 11.61% and 29.82%, accounting Rs. 74.14 and Rs. 61.17 in billions with the respective shares of 54.79% and 45.21% with India and the third countries. The total deficit accounted Rs. 135.31 billions with the increase of 19.17%. The export

and import ratio remained 34.7% and 30.5% in the successive FYs. The role of exports and imports on GDP in producer's price remained 9.2% and 26.6% in the FY 05/06 and 8.2% and 26.7% respectively in the FYs 06/07. The BOP situations in these two FYs remained surplus of Rs. 25.7 and Rs. 5.9 in billions in the successive FYs. The export import ratio had been 34.7 in FY 05/06, followed by 30.5% in the FY 06/07. There had been an expansion of total trade by 10.68% to Rs. 281.2 billions during the FY 07/08. The volume of trade with India was increased by 14.8% to Rs. 180.93 billions which is 64.34% of the total trade, whereas the trade with third countries increased by 3.93% to Rs. 100.27 billions with the share of 35.66% of the total trade. (See Tables 5.9 and 5.10)

According to Table 5.9, during the review period of FY 08/09, the volume of foreign trade grew up by 24.2% reaching to Rs. 220.32 billions. The growth of foreign trade for the same period of last FY was 37.1% with 17.1% increase in export and 26.1% increase in imports. The share of export in total foreign trade was 20.1% with the major chunk of 79.9% to the import during the first eight months of the FY 08/09. The trade with India during this period was increased by 10.97% to Rs. 126.79 billions with the share of 57.55%, where as the trade with third countries increased by 48.18% to Rs. 93.53 billions with the share of 42.45% of the total trade as compared to the same period of previous FY 07/08. Similarly, in the review period of FY 08/09, the total export increased by 17.1% to Rs. 44.30 billions, against the decrease of 2.9% to Rs. 37.81 billions in the same period of the previous FY 07/08. The total export in the FY 07/08 accounted to Rs. 59.27 billions with 10.68% decline than in the previous FY 06/07. The increasing tendency of export to third countries had been significant whereas it was just negative with India since FY 06/07. Consequently, in the review period of FY 07/08, the share of export to India was 68.2%, accounting to Rs. 25.79 billions, followed by 60.3%, accounting to Rs. 26.72 billions in the same period of FY 08/09. By the end of FY 07/08, the share of India remained Rs. 38.56 billions which was 65.05% of the total export with the decline of 7.60%. However it increased by 3.6% during the first eight months of the FY 08/09 against the decline of 6.9% during the same period of the previous FY. Similarly, the share of

export to third countries was 31.8%, accounting to Rs. 12.03 billions in the review period of FY 07/08, followed by 39.7% accounting to Rs. 17.58 billions in the same period of FY 08/09. By the end of FY 07/08, the share of third countries remained Rs. 20.71 billions which was 34.95% of the total export with the increase of 17.31%. Again, it increased by 46.13% during the review period of FY 08/09 against the increase of 6.9% during the same period of the previous FY.

In case of imports, the total import in the FY 07/08 increased by 13.99% to Rs. 221.94 billions. Also, it increased 26.1% to Rs. 176.02 billions in the first eight months of the FY 08/09 in comparison to the increase of 19.2% during the same period of the previous FY. The imports from India increased by 22.87% to Rs. 142.38 billions, which is 64.15% of the total imports in FY 07/08. Even though the imports from India increased by 13.12% in the first eight months of FY 08/09 than the previous FY, the share of it dropped to 56.9% of the total imports, accounting Rs. 100.07 billions from 63.4% of the same period of previous FY. On the other hand, the share of import from the third countries in FY 07/08 increased by 0.94% to Rs. 79.56 billions, which is 35.85% of the total. The third countries shared 43.15% of import accounting to Rs. 75.95 billions in the review period of the FY 08/09 which was measured 36.6% in the same period of previous FY.

As shown in the Tables 5.9 and 5.10, during the FY 07/08, the trade deficit was measured Rs. 162.67 billions with the substantial increase of 20.22% than the previous FY. In the first eight months of the FY 08/09, the total trade deficit increased by 29.5% amounting to Rs.131.73 billions because of the substantial rise in imports and diversification of its bases as compared to total exports. The trade deficit in the corresponding period of the previous FY had increased by 30.2% amounting to Rs. 101.75 billions. During the review period of FY 08/09, the trade deficit with India touched Rs. 73.35 billions with 17.02% growth, whereas the trade deficit with third countries totaled Rs. 58.38 billions with a notable growth of 49.43%. The trade deficit with India rose by 45.2% in comparison to the 17% rise in trade deficit with other countries during the corresponding period of the previous fiscal year. The role of exports and imports

on GDP in producer's price remained 7.5% and 26.6% during the FY 07/08 and 7.2% and 28.1% during the first eight months of FY 08/09. The export import ratio had been 26.7 in FY 07/08/06, followed by 24.1% in the first eight months of FY 08/09.

In the light of various trade constraints, the overall picture of foreign trade in Nepal has been far behind than satisfaction. The political turmoil and the lack of economic diplomacy are major reasons which have hindered the growth of trade particularly the export promotion. It is evident from the above analysis that import from trading nations has overwhelmingly surpassed the export, as a result of this the deficits every year is growing in a steadfast manner. There is urgent need of improving the slacking situation of the industries producing exportable goods. The prevailing peace process somehow has shown good symptoms with the encouraging environment for investment in the industries producing exportable goods. The organizations such as FNCCI and FHAN have been incessantly urging the government of Nepal to appoint Attaché in the trading nations like USA, Japan, EU countries etc. to boost the economic diplomacy. Also in the light of accession to the membership of trade organizations such as WTO, BIMST-EC and SAFTA, no major benefits have been tapped so far. The gravity of GoN in these 'must-to-do' issues certainly can lead to a favorable environment for betterment and steadfast growth of balanced foreign trade.

5.6 Tourism

Since time immemorial Nepal has been vividly portrayed as a country with unparalleled natural beauties. The exotic natural panorama has become the mainstay of its identity. The long range of Himalayas form east to west in the northern part of the country has been identical to attract as many tourists every year. Along with this, the abundance of floras and faunas, friendly people, good facilities, typical lifestyle, religious and cultural dictum of "*Athiti Debo Bhawa*" are some of the characteristics which have manifested the real potentialities of tourism industry in Nepal. The strength of Nepal's cultural and natural heritage has been widely recognized. Yet, the country has not been able to make the

maximum use of its tourism potentials and market our products as a package for tourist attractions.

The economic diplomacy has accorded priority on the promotion of tourism in Nepal. The main reason behind it is that, the tourism industry in Nepal is capable of earning large chunk of foreign currency. Given the identity 'Shangri-la', 'a land of yeti', 'paradise for tourists', etc. the potentiality of tourism in Nepal is so immense which can be developed in a viable manner. The role of economic diplomacy in this accord is very imperative to recognize Nepal as a fascinating tourist destination. Nepal compares more favorably than other tourist destinations in the world in many areas, which include: adventure travel destination, wildlife destination, adventure tourism, culture, pilgrimage, value for money, and overall experiences. Thus in order to enhance and popularize these specialties of tourism, economic diplomacy must be driven to that end. Furthermore, economic diplomacy must be entertained to attract more foreign investments in the tourism industries. Seeking its great contribution to the national economy the government must launch timely and appropriate promotional strategies and programs and thus expand the benefits of tourism to the village level. And, the role of private sector in the tourism industries is also viable and the private sector has been in recent years eyeing in the business of tourism.

Despite the fact that tourism industry is a requisite part of national economy and is capable of boosting the national economy, there occurs myriad of problems hindering the prospects of its growth. Breach in the peace, infrastructural constraints, pollution in the major cities, political instability etc have diverse effect in the development of tourism industry. But the optimism still exists, because even in the times of slackness of tourism in the South Asian region, the industry in Nepal witnessed progress in the later part of the 1990s decade. Eventually, the prevalence of widespread conflict within the country drove this sector to transitory slackness in the starting of the new millennium. Along with the celebrated declaration of a Democratic Republic of Nepal with jubilation, the rays of hope do exists in the tourism industry that, it is one such sector which is

capable of accelerating the national economy because of its huge potentiality. While, the GoN has been keen on to promote tourism. As for examples, in the FY 08/09 Nepal participated in ITB-2009 held in Berlin, Germany which is the world's largest tourism fair. Likewise, Nepal participated in World Mart organized in UK, MITT-2009 in Moscow, Russia, FITUR-2009 organized in Spain, North India Sales Mission, Sales Mission organized in China PATA Annual Meeting, UNWTO conference in Teheran, aviation concerned ICAO seminar in Canada. Various fairs and celebrations were organized through Nepal Tourism Board by branding “Naturally Nepal: Once is Not Enough” for promoting tourism in Nepal.

Analysis of the purpose of tourists visit to Nepal reveals that majority of tourists come to Nepal for trekking and mountaineering, trading and business, official visit and pilgrimage. On the other hand the majority of tourists’ arrivals are mainly from India and other Asian countries including the Western Europe, North America, Australia and the Pacific Region, Eastern Europe, Central and South America and Africa. The overall situation and contributions of tourism industries in the economy of Nepal along with the starting of the new millennium have been discussed thoroughly in the following paragraphs.

Table 5.11
Tourist Arrival & Their Duration of Stay

Year	Airlines	Land	Total	Growth %	Duration of Stay
2000	376914	86732	463646	-5.67	11.88
2001	299514	61723	361237	-22.1	11.93
2002	218660	56808	275468	-23.7	7.92
2003	275438	62694	338132	22.7	9.60
2004	297555	87962	385297	13.9	13.51
2005	277346	98052	375398	-2.7	9.09
2006	283819	100107	383926	2.3	10.2
2007	360713	165992	526705	37.2	11.96
2008	374660	125617	500277	-5.0	11.78

Source: Economic Survey 08/09

The performance of tourism sector measured in terms of tourists’ arrival and the average duration of stay showed the less satisfactory results in the calendar year

2000 than in year 1999. According to Table 5.11, the number of tourist arrivals by air registered a decline of 10.52% to 376,914 persons. The number of tourist arrivals by land declined by 7.23% to 86,732 persons. The decline was mainly attributed to the outbreak of insurgency. Similarly the average duration of stay also declined to 11.88 days from 12.8 days of previous year. The total tourists' arrival was declined by 5.67% to 463,646 persons. In the FY 00/01, the total foreign currency earning was measured 11.72 billions with a decline of 2.96% than the previous FY. As shown in Table 5.12, of the total foreign exchange earnings, the share of tourism was scaled 7.4% with the contribution of 2.7% of the national GDP.

While analyzing the number of tourists visiting Nepal in the calendar year 2001, as shown in Table 5.11, the number of tourists had declined by 22.08% to 361,237 persons. The arrivals from air and land were measured 299,514 and 61,723 with the respective declines of 20.54% and 28.83%. The number of tourists' arrival in the calendar year 2002 further declined by 23.7% to 275,468 with the respective declines of 26.99% to 218,660 by air and 7.96% to 56,808 from land. The duration of stay in these two years also declined to 11.93 and 7.92 days respectively. According to table 5.12, the foreign currency earned during the FYs 01/02 and 02/03 were measured Rs. 8.65 billions with the decline of 26.8% and Rs. 11.75 billions with the increase of 35.7%. Of the total foreign currency earnings, 6.1% and 8.2% of were earned from tourism sector and the contribution on national GDP were 1.9% and 2.4% respectively.

As the arrivals by air and from land in the successive years increased, the inflow of tourists' in the calendar years 2003 and 2004 were increased by 22.7% and 13.9% accounting 338,132 and 385,296 persons respectively as shown in Table 5.11. Compared to previous years, the duration of stay in these both years increased to 9.6 days and 13.51 days respectively. As the result of above the foreign currency earning in the FY 03/04 increased significantly by 54.5% to Rs. 18.15 billions with the share of 11.4% of the total foreign earnings. The contribution to the national GDP was also measured a significant 3.4%. However

in the FY 04/05 the Forex earnings from tourism accounted Rs. 10.46 billions with a sharp decline of 43.3% and with the lesser share of 6.1% of the total Forex earnings. The contribution of tourism earnings to the national GDP was declined to 1.8%. (See Table 5.12)

In the calendar years 2005 and 2006, the tourists' arrivals were measured 375,398 persons with decline of 2.7% and 383,926 persons with the increase of 2.3% respectively. The duration of stay in those successive years were 9.09 and 10.2 days respectively. In the Forex earnings front, during the FYs 05/06 and 06/07, it was accounted Rs. 10.13 billions with decline of 8.7% and Rs. 10.13 billions with the increase of 6% respectively. The shares of Forex earnings from tourism to the total Forex earning were scaled to 4.6% and 4.5% with the contributions of 1.5% and 1.4% to the national GDP respectively in the FYs 05/06 and 06/07.

Table 5.12
Foreign Exchange Earning from Tourism

Rs. in billions

FY	Total Forex Earnings From Tourism	% Change In Income	As % of Total Forex Earnings	As % GDP
00/01	11.72	-2.96	7.4	2.7
01/02	8.65	-26.8	6.1	1.9
02/03	11.75	35.7	8.2	2.4
03/04	18.15	54.5	11.4	3.4
04/05	10.46	-43.3	6.1	1.8
05/06	9.56	8.7	4.6	1.5
06/07	10.13	6.0	4.5	1.4
07/08	18.65	84.2	6.7	2.3
08/09*	16.83	54.5	7.2	1.8

(* First Eight Months), Source: Economic Survey 08/09

According to Table 5.11, while analyzing the number of tourists visiting Nepal, their growth trend and length of stay, the number of tourists had increased by 37.2% to 526,705 during 2007. The number of tourists in 2008 totaled 500,277 with a decline of 5%. In 2007, the average length of tourist stay was 11.96 days, while this came down to 11.78 days in 2008. On the other hand, as shown in Table 5.12, the foreign exchange earnings in FY 07/08 had increased by 84.2% totaling to Rs. 18.37 billions from tourism sector than that of the preceding year.

Likewise, during the first eight months of FY 08/09, foreign exchange earnings reached Rs. 16.83 billions which is 54.5% more than the earnings during the same period of the preceding year. The foreign exchange earned in the first eight months of FY 2008/09 was equivalent to 7.2% of the total foreign exchange earnings. The contribution of tourism earnings to the national GDP was measured 2.5% during the review period of FY 08/09.

Even though the great potentiality of tourism industry does exist in Nepal, the achievement of it in the past has been directly related to the existing internal political situation. Time and again this sector of economy has been acknowledged as a very thriving industry. But the graveness of decade long insurgency had directly impacted the tourists' inflow. The industry floundered during those years of conflict. However, the continuous decline of tourism was halted along with the advent of new political system in 2006. This implies that peace is the bottom-line of tourism development. Also, there is need of grave concern to formulate appropriate policies and long terms strategies in order to boom this industry.

In nutshell, Nepal can be developed as a premium destination of tourism. The adventurous tourism such as rock climbing, hot air ballooning, river rafting, jungle safari etc. are typical of alluring greater numbers of tourists from around the globe. At this juncture, the role of economic diplomacy would be to sort out massive publicity of country in the international markets. Also, a deliberate interplay between NTB, foreign diplomatic missions, Ministry of Culture, Tourism, and Civil Aviation and other line ministries of Government of Nepal can augment the tourism industry to greater benefits.

CHAPTER 6 SUMMARY, CONCLUSION AND RECOMMENDATION

6.1 Summary and Findings

6.1.1 In the FY 00/01 the GDP growth was measured as 4.9%. Some of the major activities while promoting economic diplomacy were: implementation of the Foreign Employment Regulation 1998, Foreign Employment Internal Operational Manual, Mobilization of Diplomatic missions abroad for the promotion of foreign employment; Guarantee of investment protection and repatriation of returns, provision of granting commercial visa to investors in an easy process, settlement of disputes under the conciliation rules of the United Nations Commission on International Trade Law, Fast Track Committee and One Window Committee to provide facilities and privileges etc. In the FY 00/01, despite the internal instability, improvement in bilateral and multilateral aid commitments with the gross increase of 53.01% was experienced. The foreign employment permission was granted to 55,025 persons with 59.07% increments. Government focused into the basic infrastructures as expected by the international investors, and thus FDI reached to 96 enterprises while, 11.7% of progress was achieved in the export promotion front. Thus the diplomatic endeavor remained satisfactory except in the tourism sector which experienced a decline of 5.67% in the tourists' inflow in the FY 00/01.

6.1.2 In the FY 01/02 the annual GDP at PP was measured a growth of 0.1%. Foreign aid inflow was improved by 6.2% with minor improvements in bilateral and multilateral aids. The first ever meeting of the NDF in Nepal in 2002 was concluded with continued commitments of donor countries and organizations to Nepal's development, and also a pledge of US\$ 500 millions for the basis of aid utilization and performance results under PRS was made. In the foreign investment front, 76 enterprises were permitted for FDI; while 242,005 persons were permitted for foreign employment. Export trade was declined by 15.7%, mainly due to decline in exports to third countries by

35.9%. In the same way, tourists' arrival was declined by 22.1% in 2001. A Memorandum of Understanding between Nepal and China was signed to facilitate the visit of Chinese Citizens to Nepal. Nepal became the first nation in South Asia to receive Approved Destination Status by China in the process of promoting tourism. Visa system had also been amended to easier two types: Single Entry and Multiple Entry, from existing three types. Despite these efforts no significant improvements had been experienced.

6.1.3 In the FY 02/03 the GDP growth was measured 3.9%. Along with the enforcement of Foreign Aid Policy 2002, the aid commitment increased by 30.02%. Also, the policy of encouraging Donors to undertake joint programming of development assistance and joint funding in the case of large projects requiring multi-donor involvement were applied. In the same FY, as a result of positive impacts of policy reform measures in the various sectors of the economy, the World Bank upgraded Nepal's status in its funding programme from low case to base case. Under a low case, Nepal was entitled to borrow up to US\$ 50 million annually, but under a base case status, it can borrow up to US\$ 100 million annually. In the foreign employment front 67,365 persons were permitted. The trade deficit significantly increased by 23.12% even though the export expanded with 6.4%. Some of the major activities and policies on tourism promotion were: opening of 13 additional snow peaks, waiving of the royalty, formulation of Mountaineering Expedition By-law 2002, Internet Homepage, International Year of Everest Golden Jubilee Celebration, Destination Nepal Campaign etc. Despite these efforts the tourists arrival in 2002 declined by 23.7%. However, the economic growth was comparatively better in FY 02/03.

6.1.4 In the FY 03/04 the annual growth of GDP (at PP) was measured 4.7%. However, there was a sharp decline of 45.05% in foreign aid with decline in both bilateral and multilateral aids. Second NDF meeting was held in 2004. Commitments on the developmental works were demonstrated by the donors. In the foreign investment front, 78 enterprises were permitted for FDI. While, the foreign employment permissions were granted to 106,660

persons. On the other hand, the total export trade improved by 7.97% even though the export to third countries declined. In tourists' arrival, a further improvement of 13.9% was observed in the calendar year 2004. This was due to several government activities and policies such as: 63 new summits opened up, 43rd meeting of South Asia Commission under the World Tourism Organization was held in Kathmandu, Visa exemption for Chinese and SAARC visitors etc. In addition, efforts for the accession to the WTO, implementation of Poverty Reduction Growth Facility (PRGF) and Poverty Reduction Strategy Credit (PRSC) were major activities. Thus, meaningful outcomes were achieved and the economic indicators improved in FY 03/04.

6.1.5 The economic growth in the FY 04/05 was measured by 3.5% improvement of GDP at PP. The foreign aid significantly increased in FY 04/05 by 60.72% with the improvements in both bilateral and multilateral aids. Significant chunk of remittance inflow with almost 11.1% contribution to GDP was observed. The foreign employment seekers rose to 137,678 persons with significant rise of 29.08%. There was a growing concern of implementing procedural reforms to wipeout the anomalies of foreign employment. The prime focus was to maintain peace and security. In this backdrop, foreign investment was permitted only to 64 enterprises implying that foreign investors were not much eager to invest. On the other hand the export trade rose by 8.89%. However, export to third countries continuously dwindled, even in FY 04/05 by 14.46%. Along with the diminishing arrival of tourists', the foreign income from tourism slacked by 43.3% despite several promotional programs like organizing *Melas*, Interaction among tour operators, press conferences, road shows, production of feature films, organizing tourism festivals, production and distribution of materials etc. for international exposures. Destination Nepal was the slogan of government. However, there still was negative growth in tourism and slacked foreign trade leading to less than satisfactory economic growth in FY 04/05.

6.1.6 FY 2005/06 could not be a satisfactory from the standpoint of national economic performance. Threat to peace and security caused less

concentration in the issues like international trade, foreign direct investment and tourism promotion. However the flow for foreign employment continued to grow and 182,192 persons were granted for foreign employment. On the other hand, the foreign aid dwindled by 45.2%. Despite the slacking exports to third countries, total export trade expanded by 2.6%. However, the trade deficit alarmingly rose by 25.09%. The promotional measures such as: Preparation of Foreign Employment Act, Labor and Employment Policy 2005; Working Procedure for Foreign Investment Promotion Committee 2062 etc. were carried out. Also renewal of the treaty on transit between Nepal and India, signing of an agreement between Nepal and China to provide free customs facilities in exported goods from Nepal to China, formation of The High Level Direction Committee to make Nepal transit point between China and India, 12th SAARC Summit in Islamabad, the Ministerial level meeting of BIMSTEC in Bangkok deciding to form Trade Negotiating Committee, Ministerial level meeting of WTO held in Hong Kong etc. were the major activities or involvements of the government. Despite these many efforts, no concrete achievements were attained during the FY 05/06.

6.1.7 Change in the political system brought rays of hope in the economic front too. The decade long insurgency halted with the peoples' movement in 2006. Thus the slogan of 'New Nepal' got momentum. However, in the years between 06/07 and current FY 08/09, progress less than expectation was observed. In the FY 06/07 growth of economy was 3.3% at PP which grew significantly by 5.3% in FY 07/08. While, it is estimated to grow by 4.7% in the FY 08/09. The inflow of foreign aid increased by 76.9% and 32.85% in the FYs 06/07 and 07/08. However in the first eight months of FY 08/09, it diminished by 11.37% compared to the same period of previous FY. In the foreign employment front, in these years, 583,388 persons were granted permission with significant rise of numbers in successive years. Eventually the contribution of remittance has reached to 19.1% of the GDP in the review period of FY 08/09. Similarly, 536 industries have been granted

permission for FDI. Thus the peace process has been favorable to FDI; however problems such as regular strikes, breaching of law and order, *Nepal Bandhs etc.* are rising as obstacles in FDI growth. In the export trade, a decline of 1.41% and 10.7% in the successive FYs 06/07 and 07/08 were experienced. It showed progress of 17.1% in the review period of FY 08/09. The trade deficits as usual increased by 19.17% and 20.22% in the successive FY 06/07 and 07/08. It further rose to 29.47% in the review period of FY 08/09. The arrivals of tourists during these years have significantly increased to more than half a million per successive FY.

The major promotional measures and activities during these FYs were:

The 14th SAARC Summit in New Delhi on April 2007 which emphasized SAFTA, an extension of The Preferential Treatment for carpet export in European markets for additional two years in 2006, several amendments in accordance with the accession to WTO, implementation of NRN Act in 2007, New Provision for facilitating Remittance from India, several tourism promotion programs across the world, promotions by electronic media, writings, documentaries etc., participation in tourism fairs and exhibitions held in several part of the world etc. The enactment of new Foreign Trade Policy 2008 has embraced the norms of WTO and regional arrangements on trade, and also envisaged to establish Special Economic Zone (SEZ) for export promotion.

6.2 Conclusion

The average economic growth in the period between FY 00/01 and the review period of FY 08/09 has remained below 5% which is not satisfactory. The inflow of aid, foreign employment opportunities, size of trade, foreign investment and tourist arrival has improved a lot than what their situation were prior to FY 00/01. However, seeking the potentialities of these sectors, there is a lot to be done or much could be done. Nepal has been unsuccessful on tapping the benefits of significantly improving neighboring economies. Foreign trade for example has not been expanded to curb rising deficits. Foreign aid and tourism in the later years have been improving satisfactorily, but again the benefits from them have not

been experienced in village and rural levels. Foreign investment in mining and water resources are those areas which bear great potentiality in present context and foreign investors are also attracted to these areas, though no conducive environment has been created for this resulting lesser progress than what could have done. Hence FDI in such areas have rather remained in slogans. In nutshell, the diplomatic endeavor has been moderate in these years and the efficacy of economic diplomacy in the development process of Nepalese economy has remained below satisfaction despite its grave relevance. It can be concluded so because the targets set by government have not been achieved over the years. On the other hand, the remittances are functioning as "Safety Valve" in the Nepalese economy. Remittance has become the main source of earning foreign currency in the country. However the diplomatic missions on monitoring and solving the problems concerned with security and guarantees of jobs for employees traveling abroad have been a central question in the efficacy of economic diplomacy.

6.3 Recommendations

- 6.3.1 Foreign Aid should be received on the selective basis for areas of priority with enhanced absorption capacity. Areas such as water resources, biodiversity, mining, infrastructures and agriculture are capable of fetching greater benefits. Thus aid must be channeled to these areas of importance. Government missions must be initiated to this end.
- 6.3.2 Since the question of low utilization of aid is floating in surface, Nepalese missions abroad should apprise the donors about the recent policies and commitments of government to optimize the utilization.
- 6.3.3 For diversification of foreign employment Nepali missions should explore job markets ensuring attractive salary and rights of Nepali manpower in the work place and intensive interaction and collaboration with manpower receiving countries. On the other hand the remittance income must be pooled for the industrial development of Nepal.
- 6.3.4 Ministry of Foreign Affairs through its missions should play a catalytic role in mobilization of foreign direct investment in water resources, enhancement

of foreign employment for Nepali citizens, expansion of volume and value of exports, promotion of tourism, and expansion of business contacts. Also investments from foreign and NRN investors should be attracted and channeled to the areas of greater importance.

6.3.5 Government should create favorable market access to immediate neighbors for the products of foreign investments project through trade agreements.

6.3.6 The development of entrepreneurship, use of advanced technology, and promotion of technical capacity have to be encouraged in order to reap benefits and face challenges emerging after the WTO membership and the SAPTA, SAFTA, and BIMSTEC agreements.

6.3.7 Government officials, while on foreign visits, should be accompanied by agenda on publicizing and expanding Nepalese exports and exploring new markets accesses. This can be carried out through meetings with business people and government officials.

6.3.8 The missions abroad should organize events like cultural programs documentaries, filming etc. to advertise and promote tourism in Nepal. Also participation in international fares and seminars is another way of encouraging tourism.

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