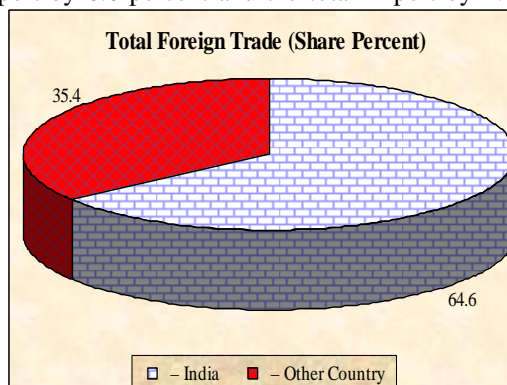


## 6. International Trade and Balance of Payments

6.1 On the basis of the statistics of the first eight months of FY 2006/07, both export and import have declined. During this period, the total foreign trade decreased by 2.6 percent amounting to Rs. 154.68 billion. The total foreign trade was worth Rs. 158.81 billion with an increase of 22.5 percent during the corresponding period of previous fiscal year. This decline of total foreign trade is due to the decline of total export by 6.6 percent and the total import by 1.1 percent during review period. Amount of trade deficit has been increased due to the highly declined rate of export in comparison of imports and the share of percentage of exports and imports in foreign trade is 25 percent and 74.1 percent respectively. During the review period, Nepal's foreign trade seems mostly governed by India alone as the share percentage of India in foreign trade is 64.6 and the other countries have only 35.4 percent. Despite the high economic growth rates of the neighboring countries like India, China and so many other countries of the world, Nepal's foreign trade volume has not increased which underlines the fact that Nepal has not been able to get the expected benefit from the world's high economic growth rate.



6.2 Although there seems slackness in foreign trade during the first eight months of FY 2006/07, there is savings in the current account during the review period due to the increase in net transfer income. This has resulted the balance of payments savings of Rs. 12.19 billion in the first eight months of this fiscal year. Analysis of the present situation of foreign exchange savings on the basis of the present level of savings and imports of this period shows the level of foreign exchange savings to be encouraging as the amount is sufficient to cover the import of goods for 12.4 months and imports of goods and services of 10.1 months.

### Box 6(A)

#### Efforts made for promotion of International Trade

- (a) With a view to ensuring the usual supply of qualitative gold in the Nepalese market, provisions have been made for the formally registered firm/company and 'A' class banking institution to import gold. Import procedure has been simplified as well, for this purpose.
- (b) The list of commodities having 91 harmonic code which could be imported from India through the payment of convertible foreign exchange has been expanded to 121 by April/May 2007.
- (c) The provision of allowing manufacturing industries and energy-oriented industries to purchase generator set not exceeding 5MW from India through the payment of convertible foreign exchange has been extended to include Schools, Colleges, University, Hospitals, Nursing Homes and other organized agencies (except individuals), for their own use (except for the commercial purpose) keeping in view

the existing load shading in Nepal.

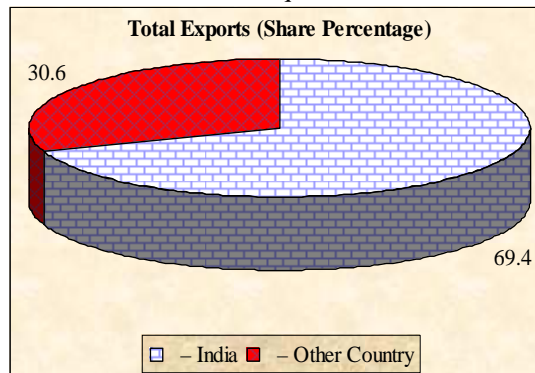
- (d) Technical work to install branch terminal of Swift in Nepal Rastra Bank has been completed with a view to ease and expedite the payment system in the export/import with ACU member countries.
- (e) Provision has been made to enable the related commercial bank to directly open more than one year **usance** letter of credit under deferred payment and suppliers credit against the prevailing provision of requiring the permission of NRB for more than one year from the countries other than India.
- (f) The concerned commercial bank themselves can accept excess figure up to the amount of either 2% of the prescribed sum in the letter of credit or US\$ 1000 whichever is more, in case of documents revealing the payment more than the actual amount to be paid in import letter of credit with a provision of payment in convertible foreign exchange. The prevailing provision requiring permission of Nepal Rastra Bank for more than that amount has now been cancelled and the concerned commercial banks can accept the amount without any limitation by themselves.

Source: NRB

## Exports

- 6.3 Total exports during the first eight months of FY 2006/07 decreased by 6.6 percent totaling to Rs. 39.99 billion, compared to 13.3 percent growth in the corresponding period of FY 2005/06. In the first eight months of 2005/06, export value recorded was equivalent to 42.80 billion.

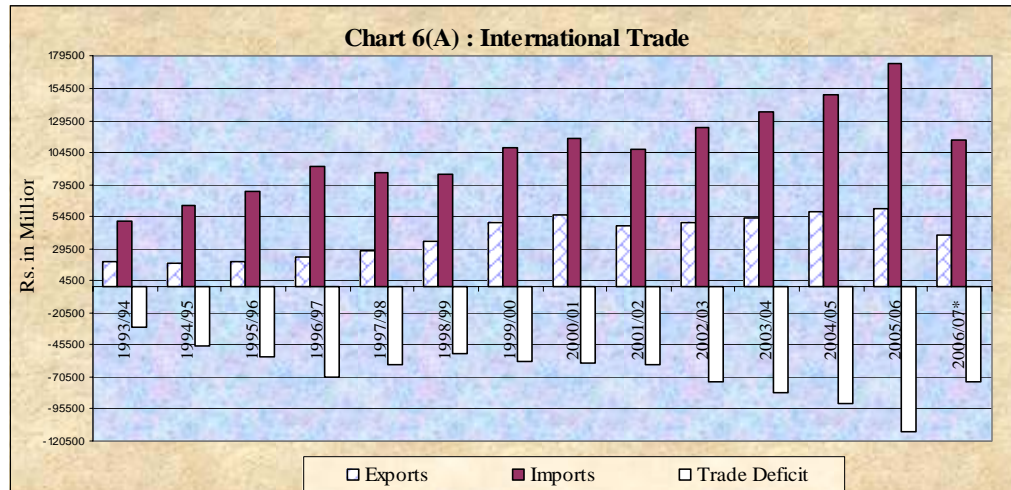
During the review period, the export to India has reached to 69.4 percent of total export while the exports to other countries stood at 30.6 percent as compared to 69.3 percent to India and 30.7 percent to other countries in the corresponding period of FY 2005/06. The negative impact in exports is due to the problem in industrial sector, electricity cut-off and Terai-bandh etc. On the basis of group formation, during the review period, the study shows that the share percentage of the primary



goods (edible goods and animals, tobacco and beverages, non-processed goods and non-edible goods, mineral fuels and greasy materials, animal and vegetable oils, fat) is 23.1% while the share percentage of manufactured goods (chemicals and medicine, classified finished products, transport and machinery equipments, miscellaneous finished goods and non-classified goods) is 76.9% in the total exports. During the same period of FY 2005/06, the percentage of primary goods and manufactured goods was 22.4 and 77.6 respectively.

- 6.4 Export to India, during the first eight months of FY 2006/07, decreased by 6.4% totaling Rs. 27.76 billion, as compared to an increase of 20.5% during the corresponding period of FY 2005/06. During the same period of the last fiscal year, the export to India was Rs. 29.66 billion. Although the export of ginger, cardamom, soap, vegetable ghee, yarn, M.S. pipe, corrugated sheets among the main export items to India was increased, the export to India was influenced negatively due to the tangible decrease of exports of polyester yarn, animal food

items, plastic made utensils, G.I. Pipe and garments by 43%, 86%, 56.7%, 74% and 31.6% respectively. Analysis of commodity wise classifications of exports to India shows that during the review period, the share of primary goods and manufactured goods is 29% and 71% respectively while it was 29.4% and 70.6% in the same period of the last fiscal year.



\* First Eight months

6.5 Third country exports in the first eight months of FY 2006/07 further declined by 7% totaling to Rs. 12.22 billion whereas in the corresponding period of last FY 2005/06, export saw a decline of 0.1% with the export worth Rs. 13.14 billion. Despite the growth in export of commodities like pulses, cardamom, herbs, Nepalese paper and paper made goods in third country, exports during this period declined mainly due to the reduction in the export of processed leather by (13.1%), carpet by (7.5%), readymade garment by (13.2%), handicrafts by (49.6%) and Pashmina by (35.8%). Analysis of commodity wise classifications of this export shows that in the review period, the share of primary commodities and final commodities remained 9.7% and 90.3% respectively as compared to 6.5% and 93.5% during the same period of last fiscal year.

**Box: 6(B)**  
**Activities on International Trade Sector**

- Government has established Trade and Export Promotion Committee in October 2006, after integrating the three institutions (Trade Promotion Center, Export Promotion Committee and Carpet and wool development Committee) which were established for the purpose of export promotion. Trade and export promotion center has been established to perform the functions of this committee.
- The preferential treatment for the carpet export, one of the main export commodities of Nepal, in the European market has been extended for additional two years. European Union has been providing the facility of immunity from the rule of origin to the Nepalese products since 1977. The period of this facility has been extended for further two years period as up to 31 December 2008, which was already terminated on 31 December 2006. Due to the facility provided with the provision in the rules of origin, there is no compulsion for Nepal to use domestic textile to produce readymade garments that are

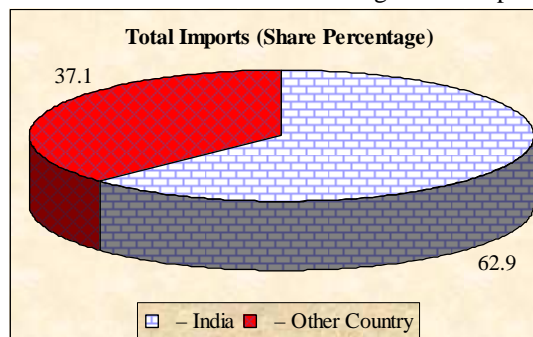
exported to the European Union member countries. Nepal may export readymade garments by using the imported textiles to these countries. Government of Nepal had requested European Union for the continuity of such facilities on the ground that tremendous decline of the export of readymade garments to other countries especially towards United States was taking place then. The share of European market, although little, in the total export of readymade garments, is gradually expanding. The export of Nepalese readymade garment is gradually falling down since 2005 after the end of the Quota system at the international textile trade. At this juncture, it is believed that such facility provided by European Union to Nepal will relieve to some extent.

- Nepal-India Commercial treaty has automatically been renewed for further next five years since 6 March 2007. As it was in the past, all the provisions of this treaty will be effective and the facilities provided by the treaty will continue.
- The 14th South Asian Association of Regional Cooperation (SAARC) Summit meeting was held in New Delhi on April 2007 making 30 points Declaration. This summit has given due emphasis on the full implementation of SAFTA along with the inclusion of service sector business. Similarly, the summit has emphasized to make road map of South Asian Customs Union and South Asian Economic Union. In this 14th SAARC summit, India has declared to bring zero customs rate by the end of 2007 to provide entry into its market to the four least developed countries of SAARC region. Similarly, India has declared to minimize the list of sensitive goods to enter India from these countries. But this provision may create additional difficulties for the Nepalese products, which were being exported with customs exemption facilities, to uphold the larger share of Indian market. Nepalese products will have to face painstaking competition with the products of Bangladesh, Bhutan and Maldives since the products of these countries also will have the same customs exemption facilities from 2008. Nepal has not been able to increase the competitive capacity and to reduce the cost of production of most of the commodities that are being exported to India. The export of vegetable ghee, jute products, polyester yarn and readymade garments will be mostly affected, as a result. As Bangladesh has gained expertise in the field of readymade garments, the product of Bangladesh will provoke a serious challenge in this region.

Source: Nepal Rastra Bank

## Import:

- 6.6 Total import during the first eight months of FY 2006/07 has remained Rs. 114.69 billion with a marginal decline of 1.1 percentage, whereas it was Rs. 116.01 billion during the same period of FY 2005/06 witnessing a significant rise of 26.3 percentage. Of the total import, during the review period, the share of import from India and from other countries was 62.9 % and 37.1 % respectively. The share of import from India and from other countries was 60.8% and 39.2% respectively during the same period in the previous year. Despite the marginal rise on the import from India during the review period, the total import figure witnessed a drop as the import from other countries recorded a considerable decline. GroupWise structure analysis



reveals the share of primary goods and finished goods to be 38.7 % and 61.3 % respectively against 41.1 % and 58.9 % during the same period of the previous fiscal year.

**Table 6 (a): Status of International Trade**  
(First Eight Months)

Particulars	Percentage Change		
	2004/05*	2005/06*	2006/07**
Export F.O.B.	4.6	13.3	-6.6
-India	19.5	20.5	-6.4
-Other Countries	-15.3	-0.1	-7
Import C.I.F.	6.2	26.3	-1.1
-India#	10.9	31.7	2.3
-Other Countries	0.3	18.7	-6.4
Balance of Trade	7.4	35.3	2.0
-India	4.5	41.2	8.6
-Other Countries	10.9	28.5	-6.2
Total Trade	5.7	22.5	-2.6
-India	13.5	28.2	-0.3
Other Countries	-4.2	13.9	-6.6
Share in Total Trade( percentage)			
-India	60.3	63.1	64.6
-Other Countries	39.7	36.9	35.4
Share in Total Export (percentage)			
-India	65.2	69.3	69.4
-Other Countries	34.8	30.7	30.6
Share in Total Import (percentage)			
-India	58.3	60.8	62.9
-Other Countries	41.7	39.2	37.1
Share in Total Balance of Trade (percentage)			
-India	53.5	55.8	59.4
-Other Countries	46.5	44.2	40.6

\* amended \*\* unprocessed

# since FY 1999/2000, import of petroleum products have been included in India rather than other countries.

Source : Nepal Rastra Bank

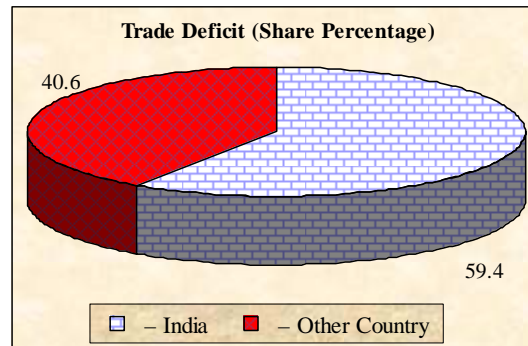
- 6.7 During the first eight months of FY 2063/64, the import from India has reached Rs. 72.12 billion with a marginal growth of 2.3 %. During the same period of the previous FY this figure was Rs. 70.51 billion with a rise of 31.7%. Petroleum products, the major import from India, recorded a higher growth of 41.8 % during the first eight months of 2062/63 whereas during the review period , it has recorded a decline by 1.9 % . During the review period, the major commodities imported from India have witnessed a decline as chemical fertilizer recorded a decline by 39 %, cosmetics by 38 %, plastic utensils by 68.9 %, steel sheet by 100 %, wire products by 46.2 %, vegetables by 29.2%, sugar by 97.1 %, rice by 51.4 %, readymade garments by 31.2 %, raw thread by 51.5%, coal by 36 % and fruits by 33.9 %. Among the

imports from India, during the first eight months of FY 2063/64, some commodities recorded a rise as vehicles and spare parts by 52.5 %, electric goods by 60.5 %, hot rolled sheet and coil by 57.7 %, agricultural inputs and spare parts by 75.9 %. Group-wise structure analysis reveals that during the review period, the ratios of primary and finished products remained 44.2% and 55.8 % respectively. These ratios were 48.6 % and 51.4 % respectively during the same period of the previous fiscal year.

- 6.8 During the review period, the total import from other countries has remained Rs. 42.57 billion with a decline by 6.4 %. This figure was Rs.45.40 billion during the first eight months of FY 2005/06 with a rise of 18.7 %. Import figure from other countries has declined during the first eight months of FY 2006/07 subsequently upon the decline on imports of palm oil by 88.9 %, readymade garments by 78 %, plastic granules by 35.3 %, other machinery and parts by 45.6 %, and electric goods by 37.9 %. Group-wise structure analysis reveals that during the review period, the share of primary and finished products remained 29.4% and 70.6% respectively against 29.5% and 70.5% during the same period of the previous fiscal year.

### Balance of Trade

- 6.9 During the first eight months of FY 2005/06, total export and total import recorded a rise of 13.3 % and 26.3 % respectively. As the rate of growth of import was quite higher than that of export, the total trade deficit volume reached to Rs.73.22 billion with a rise by 35.3 %. The trade deficit figure has further reached to Rs. 74.71 billion with a rise by 2 % during the first eight months of FY 2006/07. During the review period, the trade deficit with India has recorded Rs.44.36 billion with a rise by 8.6 % whereas the trade deficit with other countries has reduced to Rs.30.34 billion with a decline by 6.2%. During the same period of the previous FY, trade deficit with India and other countries were Rs.40.85 billion and Rs. 32.36 billion respectively. During the review period, of the total trade deficit, the share of trade deficit with India and other countries have remained 59.4 % and 40.6 % respectively against 55.8 % and 44.2 % during the same period of the previous FY.



### Balance of Payment

- 6.10 In the first eight months of FY 2006/07, due to the rise in net transfer income, current account has witnessed a surplus and the balance of payment as a whole has remained favorable. In comparison to the first eight months of the previous FY 2005/06, during the review of the current FY, the current account surplus has increased by 88 % reaching Rs. 10.45 billion.
- 6.11 During the first eight months of the current FY, total exports including the trade not registered in the customs has reduced to Rs.41.53 billion with a decline by 4.8 %, while the total import has reduced to Rs. 111.97 billion with a decline by 2 %. Consequently, the total trade deficit has remained Rs. 70.43 billion with a decline by 0.3 %. During the corresponding period of the previous fiscal year, trade deficit figure had increased by 39.2 %. During the first eight months of FY 2006/07, income from the tourism sector has declined by 1.6 %, while the income from other service sector has also declined by 1.3 %. However, total income from service sector has reached to Rs.21.52 billion with an increase by 18.2 % in comparison to the corresponding

period of the previous fiscal year. This increase is attributed to the considerable increase by 64.6 % in the Government revenue not included elsewhere. Payments for service have increased by 33.7 % because of the increase in the number of outgoing Nepalese people. Similarly, during the review period, as a result of increase in transport expenses and other payments, total service payments have increased by 16.8 % relatively to the corresponding period of the previous fiscal year, reaching Rs. 25.12 billion. Thus, the net service income during the review period has remained negative by Rs. 3.6 billion. So far as the transfer is concerned, private sector remittances have increased by 5.1 % and have reached Rs. 64.35 billion during the review period. Similarly, the grants and pensions have increased by 9 % and 7 % respectively. As a result, during the review period, the net transfer income has reached to Rs. 83.09 billion with a rise by 6.9 % as compared to the corresponding period of the previous fiscal year.

- 6.12 During the review period of this fiscal year, the capital account has recorded a capital transfer equivalent to Rs. 2.41 billion. Under financial account, other investment: assets have increased by Rs. 8.89 billion during the review period as compared to Rs. 10.77 billion during the corresponding period of the previous fiscal year. So far the other investment: liabilities are concerned, the government borrowing inflow amounts to Rs. 5.16 billion during the review period, while the repayment of the principal amount equals to Rs. 4.32 billion. Thus, during the review period the net government borrowing inflow amounts to Rs. 0.84 billion. During the first eight months of the current fiscal year, the net miscellaneous capital inflow amounts to Rs. 5.05 billion. Thus, the first eight months of the current fiscal year witnesses a Rs. 12.19 billion surplus in balance of payment.

### Foreign Exchange Reserves

- 6.13 The total foreign exchange reserves of the banking sector have reached Rs.177.8 billion with an increase of 7.2 percent during the first eight months of FY 2006/07, against the increase of 11.3 percent during the corresponding period of previous FY 2005/06. Out of the total reserves, the shares of Nepal Rastra Bank and the commercial banks are 80.2 percent and 19.8 percent respectively. The total foreign exchange reserves in terms of U.S. Dollars have reached the level of 2.51 billion with an increase of 12.7% during the first eight months of FY 2006/07 against the increase of 9.6% during the corresponding period of previous FY 2005/06. Share of convertible currency reserve in the total reserves was 94 percent in the month of February 2006 while it is 95.4 percent in the month of February 2007. Likewise, the share of non-convertible currency reserve has decreased to 4.6 percent from 6 percent. On the basis of the import of first eight months of FY 2006/07, present level of total foreign exchange reserve is adequate to cover imports of goods for 12.4 months and imports of goods and services for 10.1 months. So the level of foreign exchange reserve is quite convenient.

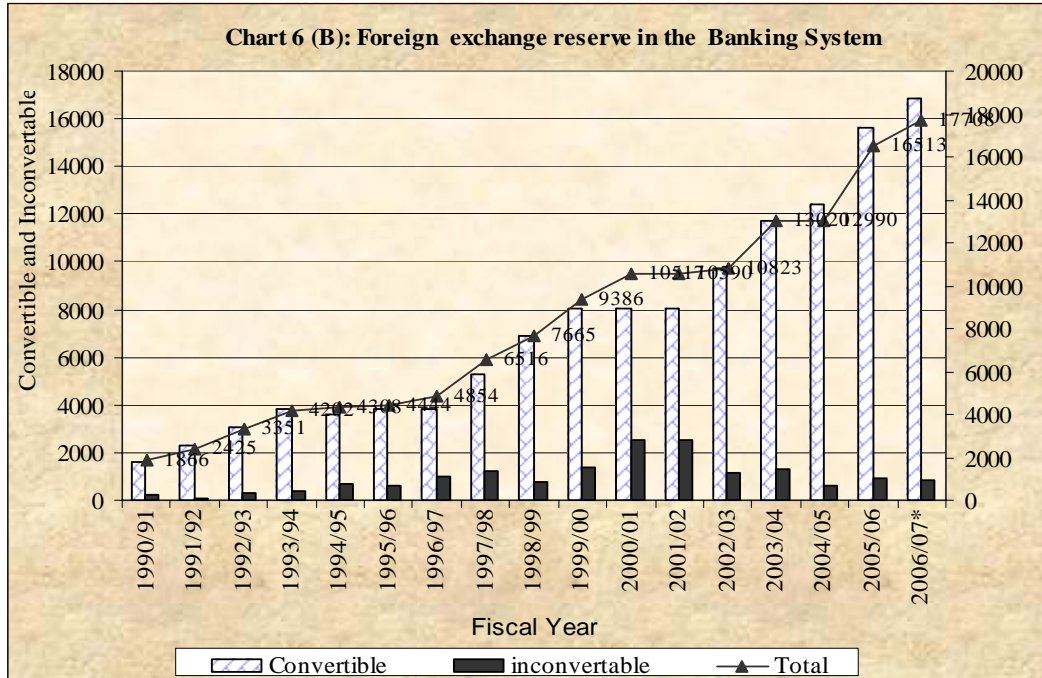
**Table 6 (b) : Total foreign exchange reserves**

Amount Rs. in 10 millions

Description	2003 July	2004 March	2004 July	2005 March	2005 July	2006 March	change in percent July- March	
							2005	2006
Nepal Rastra Bank	10792	10591	10443	11342	13206	14206	8.6	7.6
Commercial bank	2229	2587	2547	3110	3307	3502	22.1	5.9
Total foreign exchange reserves	13021	13178	12990	14452	16513	17708	11.3	7.2

Source: Nepal Rastra Bank

- 6.14 The foreign assets of banking sector increased by 11.2 percent during the period of FY 2005/06 whereas it has been increased by 6.9 percent only in the current FY amounting Rs 177.73 billion. The gross foreign asset was 166.2 billion in mid July 2006.



- 6.15 On the basis of analysis of income and expenditure of convertible foreign exchange, the total income was 88.73 billion and total expenditure was 78.27 billion upholding the saving of 10.46 billion in the first six months of FY 2005/06. The total saving during the review period of last year was Rs 6.93 billion.

**Foreign exchange rate, Crude Petroleum Product and Gold Price**

- 6.16 Nepalese currency has been appreciated with the main international currencies in the first eight months period of current FY. In comparison to the rate of mid July 2006 with that of mid March, Nepalese rupee appreciated by 5.11 percent against U.S. dollars which was depreciated by 1.47 percent during the corresponding period of last fiscal year. In comparison to the rate of mid July 2006 with that of mid March 2007 Nepali rupee appreciated by 0.19 percent, 1.07 percent 4.34 percent and 6.32 percent against sterling pound, Euro, Swiss Frank and Japanese Yen respectively.

- 6.17 The price of crude oil Brent in the international market per barrel was U.S. dollar 63.08 in March 2006 whereas the rate decreased by 3.3 percent and reached to U.S. dollar 61.02 per barrel in March 2007. The price of gold per ounce increased by 15.6 percent and reached to U.S. dollar 643.25 in March 2007 from U.S. dollar 556.5 in the same period of 2006.

## Challenges

- 6.18 The world economy has become more liberalized, broadened and integrated in the recent years. On one hand, this has amplified competition among the countries to get market of their goods and services in the international economic sector and on the other, the economic event occurring in one part of the world may aggravate possibility of immediate direct contaminated effect to the other parts of the world. The flow of increasing capital and technology has changed the foreign capital structure which has augmented the possibility of economic external instability. In the mean time, the old concept of international assistance is emerging into new concept as "trade not assistance". In this changed context in the world, it is challenging to strengthen the balance of payment for external stability and promoting trade getting integrated gradually and taking maximum advantage of broad market and its potentials.
- 6.19 After taking the membership of World Trade Organization (WTO), it is of utmost necessity to promote and develop the modern management, use new skills, utilize advanced technology, enhance technical skill and entrepreneurship in order to take comparative advantage and face the challenges ahead. For this purpose, it has become crucial to attract foreign investment and investment of Non-resident Nepalese (NRN) in national economy. In this context, observing the remarkable role of investment of non-resident citizens that has played to boost the economy of China, India, Sri Lank and Pakistan, it has become a challenging task also for the Government of Nepal to prepare a policy in different sectors of economic development for attracting the foreign and Non-resident Nepalese investments.
- 6.20 The country-wise and product-wise area of export trade of Nepal seems narrow. On the country-wise basis, the main markets are India, USA, and Germany. On the product-wise basis, export of other products than readymade garments, Pasmina and Woolen Carpets to the third country export basket is nominal. The export trade of low volume, high value products like herbs, ornaments, and precious stones has been shrinking day by day. The export of agricultural sector is also decreasing. The "knowledge and research based" trade system has not been developed estimating the changes in demand of client, to provide goods and services accordingly. For this, it is necessary to pay attention on utilization of information technology and to develop the skilled manpower in the private and government agencies related to international trade.
- 6.21 Quality control is inevitable for competition. Only few industries have got ISO- 9000 certification in Nepal. Deficit of ISO-9000 certification may hinder the access in the markets of developed countries like European Union, USA, and Japan etc. Therefore, it is necessary to appraise the quality of goods which will be exported to the international market and formulate the program to support it.
- 6.22 The establishment and operation of Export Processing Zone (EPZ) would be of great help to enhance the export of non- traditional goods, to increase production and trade of the high-tech products and to create employment opportunities. If EPZ could be established in the various regions of the country, it would be highly supportive to produce and export the exportable products in the international market. Therefore, the task to formulate and carry out necessary rules and regulations related to EPZ is quite challenging.
- 6.23 The quota system has completely ended from 2005. So, the government need to focus with priority on expansion of standard Nepalese fabric industries by improving and rectifying the quality of production according to the test of the clients, minimizing the cost of production and enhancing competitive capacity of the Nepalese ready made garment industries in order to

make the export business sustainable and competitive. In order to compete in the world market, Nepal need to pay attention and implement with priority to improve the technology as well as develop the skills, enhance the capacity of producing new attractive and qualitative products and establish ready made garments processing centers with necessary trainings.

- 6.24 The remittances are functioning as "Safety Valve" in the Nepalese economy. Remittance has become the main source of earning foreign currency in the country. So it is essential to compose its correct estimation and build the flow of maximum portion of remittance in the country through institutional channel. In order to educate Nepalese labor force working abroad on the procedure of sending remittance through banking channel, it looks necessary to provide them trainings in coordination with department of labor, commercial bank, manpower agencies and related NGOs. Residential and non residential Nepalese diplomatic missions need to take necessary initiatives for this purpose. Similarly, Nepalese diplomatic missions abroad need to take initiatives with concerned agencies on a regular basis to identify the possible employment opportunities, required skills and provide the know-how of the steps and measures to be taken for its utilization, creating the environment conducive.
- 6.25 Although Bangladesh has allowed Nepal to use Banglabandh Marg for the trade purpose and India has provided transit facility through Phulbari-Banglabandh Marga to Mongla sea port, there has been least use of this port due to the lack of infrastructure. Therefore, it is necessary to improve the infrastructure in this region to make import-export trade more effective.
- 6.26 Nepal is supposed to be one of the significant places in the world for possessing different types of high breed and rare herbs. But, most of the herbs have not been identified so far, due to the lack of necessary study and research. Herbs, that are already identified, are also not been utilized properly. Difficulty may arise in future in producing and utilizing the bio-diverse products on our own because of the probability of claiming the Patent Rights by others on the traditional bio-products of Nepal. Therefore, it seems necessary to pay attention towards conservation of bio-diversity through study and research in time. Similarly, on the basis of comparative benefit, it is sought after the necessity to establish modern herbs processing center for the promotion of herbs export, which has occupied significant place in Nepal's export trade.
- 6.27 It is of utmost importance to take additional steps forward for the rapid improvement of the activities in tourism industry which has not shown speedy progress in the present context, but is one of the major contributors to the income of service trade sector. In spite of several potentials of domestic and external tourism development in different places of the country including Kathmandu Valley, the country could not fetch expected outcome from this industry because of lack of adequate advertisement, lack of promotion of existing tourist areas, lack of discovering new tourist areas and non-exploration of new tourism roads and its use. Therefore, identifying further promising tourist areas, maintaining the existing tourist areas, proper emphasis on preservation and sanitation, developing additional tourism roads, improving the level of quality services to be provided to the tourists and the task of improvement in peace and order has been inevitable.