



TRADE POLICY REVIEW

REPORT BY

NEPAL

Pursuant to the Agreement Establishing the Trade Policy Review Mechanism (Annex 3 of the Marrakesh Agreement Establishing the World Trade Organization), the policy statement by Nepal is attached.

Note: This report is subject to restricted circulation and press embargo until the end of the first session of the meeting of the Trade Policy Review Body on Nepal.

ACRONYM

AfT	: Aid for Trade
ADS	: Agriculture Development Strategy
ASYCUDA	: Automated System for Customs Data
BAFIA	: Bank and Financial Institution Act
BFI	: Bank and Financial Institution
BIPPA	: Bilateral Investment Promotion and Protection Agreement
BIMSTEC	: Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation
BPO	: Business Process Outsourcing
BRI	: Belt and Road Initiative
CBTL	: Cross Border Transmission Line
DFQF	: Duty-Free and Quota-Free
DPs	: Development Partners
DFTQC	: Department of Food Technology and Quality Control
DTAA	: Double Tax Avoidance Agreement
DTIS	: Diagnostic Trade Integration Study
e-GP	: Electronic Government Procurement
FDI	: Foreign Direct Investment
FITTA	: Foreign Investment and Technology Transfer Act
FY	: Fiscal Year
GDP	: Gross Domestic Product
GoN	: Government of Nepal
GSP	: Generalized System of Preferences
IBN	: Investment Board Nepal
ICD	: Inland Container Depo
ICP	: Integrated Check Post
ICT	: Information and Communication Technology
IEC	: International Electrotechnical Commission
IP	: Intellectual Property
ISO	: International Organization for Standardization
kWh	: Kilowatt Hour
LDCs	: Least Developed Countries
LLDCs	: Landlocked Least Developed Countries
MAPs	: Medicinal and Aromatic Plants
MHPs	: Micro-Hydropower Plants
MW	: Megawatt
MoICS	: Ministry of Industry, Commerce and Supplies
MoF	: Ministry of Finance
MoU	: Memorandum of Understanding
MRA	: Mutual Recognition Agreement
MTS	: Multilateral Trading System
MVA	: Motor Vehicle Agreement
NBSM	: Nepal Bureau of Standards and Metrology
NRs	: Nepalese Rupees

NTIS	: Nepal Trade Integrated Strategy
NRB	: Nepal Rastra Bank
PIA	: Project Investment Agreement
PPP	: Public Private Partnership
PTA	: Power Trade Agreement
RKC	: Revised Kyoto Convention
SAARC	: South Asian Association for Regional Cooperation
SAFTA	: South Asian Free Trade Area
SAPTA	: SAARC Preferential Trading Arrangement
SATIS	: SAARC Agreement on Trade in Services
SDG	: Sustainable Development Goals
SEZ	: Special Economic Zone
SPS	: Sanitary and Phytosanitary
TEPC	: Trade and Economic Promotion Centre
TFA	: Trade Facilitation Agreement
TPR	: Trade Policy Review
TSMP	: Transmission System Master Plan
UNCITRAL	: United Nations Commission on International Trade Law
UNCTAD	: United Nations Conference on Trade and Development
USD	: United States Dollars
VAT	: Value Added Tax
WTO	: World Trade Organization

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1 INTRODUCTION

1.1. Nepal's Second Trade Policy Review (TPR) at the World Trade Organization (WTO) covers the period between 2012 and 2018. Nepal joined the WTO on 23 April 2004 as the first least-developed country (LDC) through the full working party negotiation. Since 2012, Nepal has undergone significant transformation, which includes changes in the political system following the promulgation of the Constitution of Nepal in 2015. The review is being carried out at a time when Nepal has entered a new era of stability concluding its long political transition after a decade-long conflict. In this process, Nepal has set an exemplary model of conflict resolution through a unique home-grown and inclusive peace process.

1.2. The current Constitution of Nepal was promulgated on 20 September 2015 through the Constituent Assembly. The Constitution laid a new foundation for Nepal's socio-economic transformation. It embraces the principles of democracy, federalism, secularism, and inclusiveness. It has provisions of three levels of government: federal, provincial and local. Accordingly, there are seven provinces and 753 local levels. Governments have been formed at all three tiers after the successful completion of elections in 2017.

1.3. The Government of Nepal (GoN), which enjoys two-thirds majority in the Parliament, has a long-term goal of "Prosperous Nepal, Happy Nepali". To achieve this goal, the Government has set objectives of achieving high economic growth, balancing and strengthening the economy, and making it more inclusive and just, in the interest of all Nepali. The overall focus is on policies that promote innovation by developing a national economy to encourage trade, investment, production, and creation of employment.

1.4. The Constitution promotes the role of the private sector in the economy and envisages that Nepal shall pursue policies to maintain competition and fairness in the market. In particular, the Constitution encourages foreign capital and technological investment as well as development and expansion of industries in areas of comparative advantage. This economic ecology is backed by the Constitution which provides a comprehensive list of thirty-one fundamental rights, including economic, social and cultural rights. The Constitution, therefore, is instrumental in fixing the politics and bringing the focus on economic development agenda through the realization of Nepal's long-awaited goals and aspirations.

2 RECENT ECONOMIC DEVELOPMENT

2.1 Main Developments During the Review Period

2.1. Nepal is steadily moving in the path of economic transformation. Nepal's annual growth was 4.3% on average in the last decade, during which the agricultural and non-agricultural sectors grew at yearly average rates of 2.9% and 4.9%, respectively. During the review period, Nepal grew at an average GDP growth rate of 4.4%. The high economic growth rate of 7.4% in 2016/17 is expected to sustain at 5.9% in 2017/18. This positive growth trend has resulted in the size of the economy reaching NRs 3 trillion from just over NRs 1.5 trillion at the end of the last review period.

2.2. The Nepali economy suffered adversely from the devastating earthquakes in 2015 and its aftershocks as well as subsequent serious disruption of supplies (including fuel and other essentials) at the southern border. Nevertheless, Nepal's economic growth has rebounded and moved in positive directions due to political stability, availability of energy, improvements in supplies, expansion of the trade sector, acceleration of construction work, and high growth in industrial output and services sector. While the nominal per-capita GDP was only US\$702 at the end of the last review period, it is expected to cross the thousand mark and reach US\$1,004 in FY 2017/18. Bolstered by the political stability and positive outlook ahead, Nepal is aiming for near double-digit growth in the upcoming fiscal year (FY) and attaining double digit growth in the next five years. The gross capital formation to GDP ratio was 38.0% at the end of the last review period. It reached 45.7% in 2016/17 and is expected to increase further to 51.8% in 2017/18. The amount of Foreign Direct Investment (FDI) in Nepal is growing at a significant rate as it increased three-folds from 17 billion NRs. in 2016/17 to 61 billion NRs. in 2017/18. The following table summarizes some major macroeconomic indicators of Nepal.

Table 2.1 Some major macroeconomic indicators of Nepal

Fiscal year	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18 ^a
In NRs billion at 2000/01 prices							
GDP in basic prices	614.6	637.8	674.2	694.3	695.7	747.1	791.1
Agriculture	224.7	227.2	237.5	240.1	240.7	253.2	260.3
Industry	98.1	100.7	107.8	109.4	102.4	115.1	125.3
Services	318.5	336.8	357.7	374.3	383.1	411.6	438.9
GDP growth rate	4.6	3.8	5.7	3.0	0.2	7.4	5.9
Share of different sectors in real GDP (at current prices)							
Primary	35.8	34.4	33.2	32.4	32.2	29.4	28.2
Secondary	14.4	14.6	14.3	14.2	13.6	14.1	14.2
Tertiary	49.8	51.0	52.5	53.4	54.2	56.5	57.6
In nominal prices							
Total trade (in NRs billion)	536.0	633.6	806.4	860.0	843.7	1063.1	1324.5
Export f.o.b	74.3	76.9	92.0	85.3	70.1	73.0	81.2
Import c.i.f.	461.7	556.7	714.4	774.7	773.6	990.1	1243.3
Total expenditure (in NRs billion)	339.2	358.6	435.0	531.5	601.0	837.2	1082.9
Recurrent	243.5	247.5	303.5	339.4	371.3	518.6	738.9
Capital	51.4	54.6	66.7	88.8	123.3	208.7	234.6
Financing	44.3	56.5	64.8	103.3	106.4	109.9	109.4
Total income (in NRs billion)	288.0	333.9	396.9	450.4	531.4	647.5	770.3
Revenue	244.4	296.0	356.6	405.9	482.0	609.2	730.1
Foreign grants	40.8	35.2	34.0	36.4	32.5	31.9	15.3*
Foreign loan	11.1	12.0	18.0	25.6	33.2	59.0	35.1*
Total population (in million)	26.9	27.2	27.6	28.0	28.3	28.7	29.1
Per capita GDP (US\$)	702	708	725	766	748	866	1004
Exchange rate (NRs per US\$1)	81.02	87.96	98.21	99.49	106.35	106.21	102.96

a Yearly preliminary estimate* first eight months.

Source: GoN, Ministry of Finance (MoF), Economic Survey 2017/18, Central Bureau of Statistics, National Accounts, Nepal Rastra Bank (NRB), Quarterly Economic Bulletin.

2.3. The relatively smooth implementation of fiscal federalism has also been a key highlight of this review period. With the transformation from a unitary government structure to a federal one, Nepal's first federal budget was launched for FY 2018/19. In its federal budget, Nepal has prioritised creation of employment opportunities, promotion of domestic and foreign investment in sectors such as energy, infrastructure, tourism, agriculture, and improvement of public service delivery. Moreover, according to the constitutional provision, the seven provincial and 753 local governments also presented their budgetary outlays, prioritising sectors and activities. The complete list of federal, provincial and local level powers and concurrent powers are mentioned in annexes 5 to 9 of the Constitution.

2.4. Though trade is a key component of the economy, trade deficit has posed challenge to Nepal's development. After Nepal's accession to the WTO, share of export in total trade has decreased from 28.3% in FY 2004/05 to 6.9% in FY 2016/17. The share of import has increased from 71.7% in FY 2004/05 to 93.1% in FY 2016/17. As a consequence, export-import ratio has deteriorated from 1:2.5 in FY 2004/05 to 1:13.5 in FY 2016/17. Nepal's trade deficit has grown by more than ten-folds. The volume of trade has nearly trebled compared to the end of last review period. However, in the last five years, imports have grown at a yearly average rate of 17% while exports have only grown at 0.5% on average.

Table 2.2 Nepal's trade scenario 2004/05 – 2016/17

Fiscal Year	Exports (NRs billion)	Imports (NRs billion)	Trade deficit (NRs billion)	Export-import ratio
2004/05	58.4	148.3	-89.9	1:2.5
2005/06	59.8	160.7	-100.9	1:2.7
2006/07	58.9	195.8	-136.9	1:3.3
2007/08	58.5	237.0	-178.6	1:4.1

Fiscal Year	Exports (NRs billion)	Imports (NRs billion)	Trade deficit (NRs billion)	Export-import ratio
2008/09	68.6	291.0	-222.4	1:4.2
2009/10	60.9	375.6	-314.7	1:6.2
2010/11	64.6	397.5	-333.0	1:6.2
2011/12	74.1	498.2	-424.1	1:6.7
2012/13	77.4	601.2	-523.9	1:7.8
2013/14	91.4	722.8	-631.4	1:7.9
2014/15	86.6	784.6	-697.9	1:9.1
2015/16	71.1	781.1	-710.0	1:11
2016/17	73.1	986.0	-912.8	1:13.5

Source: GoN, Trade and Export Promotion Centre, A Glimpse of Nepal's Foreign Trade (Statistical Presentation) 2017.

2.2 Investment and Incentives for Investors

2.5. The Constitution promotes the role of private sector and encourages foreign capital and technological investment as an inherent feature. Several policies and acts have been developed in line with the Constitution to protect rights of the investors, including through Intellectual Property Policy, 2017, Foreign Investment Policy, 2015, and Industrial Enterprises Act, 2016, among others. Foreign Investment and Technology Transfer Act (FITTA), 1992 governs FDI. Foreign investors are allowed to invest up to 100% in almost all industries, except for few on the negative list. The Company Act, 2017 has made provisions for establishing, managing and administering companies in more simplified, convenient and transparent manner. The Industrial Enterprises Act, 2016 covers entry, operation and exit procedures for business and also outlines customs and tax payment requirement for investors. The Labour Act, 2017 has implemented no work no pay principle.

2.6. Nepal has signed Bilateral Investment Promotion and Protection Agreement (BIPPA) with six countries and Double Tax Avoidance Agreement (DTAA) with ten countries. As an LDC, Nepal has duty free market access in many developed and developing countries. However, these market access opportunities are yet to be fully realized. Hence, there is a dearth of FDI to boost production and productivity by utilizing market access advantages.

2.7. Several incentives are available to investors and there are further concessions for investment in certain priority sectors. Foreign investors are allowed to repatriate 100% of their profits after meeting legal requirements. Companies are allowed to hire foreign nationals. Tourist/non-tourist and business visas can be issued with recommendation from concerned government agencies and in case of investment of US\$100,000 or more, residential visa is granted directly to the investor. In terms of property rights, investors are allowed to buy or lease land in the name of their company.

2.8. Nepal's recent success in attracting foreign investment evidences improved investment climate in the country. Nepal has improved its Doing Business ranking and has the third most favourable business climate and fourth most competitive economy in South Asia. Nepal organized Investment Summit in 2017 to promote FDI as well as technology and skill transfer. The event was attended by more than 250 institutional and individual investors from 21 countries who pledged investment totalling US\$13.51 billion.

2.9. The Government is committed to attract foreign investment by treating foreign investment as complementary to national capital formation. It is making further legal, institutional and procedural reforms to reduce cost of doing business and ensure an investment-friendly environment. It is planning to make the whole process from business registration to closure predictable, simplified, transparent and based on information technology. It is also making provisions to deliver all services from one point in a time-bound manner. The Government is strengthening the Investment Board Nepal (IBN) as an institution for granting investment approval through one-door system, including for public private partnerships (PPPs).

2.3 Monetary Policy Management

2.10. Nepal Rastra Bank (NRB), the central bank of Nepal, has primary duties of maintaining macroeconomic and financial sector stability. While average consumer price inflation was 4.5% in

FY 2016/17, it has remained at 4.1% in the first eleven months of FY 2017/18. Inflation has remained within a reasonable range. Broad money supply (M2) increased by 15.5% in FY 2016/17 compared to 12.2% in FY 2010/11. Average growth of money supply remained at around 18.08% during the last five years. Foreign Exchange reserve stood at NRs 1094 billion as of mid-June 2018 compared to NRs 272.3 billion at the end of last review period. Similarly, while at the end of last review period, level of foreign exchange reserve was sufficient to cover 7.3 months of merchandise and service imports, the figure was 11.4 months for FY 2016/17.

2.11. Moreover, Monetary Policy, 2018/19 has made significant investment-friendly reforms by simplifying the process of repatriation of foreign investment earnings, introducing exchange rate hedging facility for foreign investors, provisioning for loan facilities for foreign investors, and making it possible for commercial banks to provide additional services such as escrow fund management for foreign investors.

2.4 Remittance

2.12. Remittance has been one of the drivers of Nepali economy and has played a significant role in lifting many Nepali above the poverty line. At present, around 4.3 million people are abroad to work, especially in Gulf countries, Malaysia, and South Korea. The ratio of remittance sent by Nepali working abroad to GDP remained around 26% during the review period and the figure has been relatively stable in recent years. Growth rate in the number of Nepali workers going for foreign employment has declined recently. Regardless, remittance sent by Nepali working abroad is a major source of foreign currency and has helped in maintaining a favourable balance of payment.

2.13. The Government's emphasis is on making foreign employment more secured and systematic while creating more decent and gainful jobs at home. In the short-run, its focus is on protecting migrants' rights, establishing formal and secure channels to send remittance and new avenues to invest it. In the long run, the focus is on developing industries and expanding opportunities in Nepal so that Nepali do not have to migrate abroad for employment.

2.5 Tax System - Corporate

2.14. Nepal has one of the lowest corporate tax regimes in South Asia making it an attractive investment destination. Tax rates for various entities according to their nature is summarised in the table below.

Table 2.3 Tax rates for various entities

Nature of Entity	Tax Rate
Normal rate for entities	25%
Special industries registered under section 3 of Industrial Enterprise Act, 1992	20%
Banks and Financial Institutions	30%
General insurance 30%, life insurance 25%	25% - 30%
Enterprises involved in petroleum businesses	30%
Saving and credit cooperatives located in urban areas	20%
Enterprises operating roads, bridges, railways hydropower stations, transmission lines, etc. on BOOT basis, etc.	20%

Source: Government of Nepal.

2.6 Private Sector Development and Privatization

2.15. Nepal's Fourteenth Periodic Plan recognizes private sector as the key driver of economic growth and aims to expand its activities and enhance its competitive capacity. It also intends to increase private sector investment for creating jobs and increasing economic growth. The Government has adopted strategies of promoting investment-friendly business environment, flexible labour laws, and collaborative investment in infrastructure, among others. Following the adoption of Privatization Act, 1994, PEs have been gradually privatized. However, PEs are not simply commercial enterprises as they hold other welfare objectives as well, including provision of basic goods and services for citizens. Moreover, as some privatized PEs have not performed satisfactorily, the Government is reviewing its privatisation policy.

2.16. Private sector occupies a major share of the economy. Following the adoption of liberal economic policies in the 1990s, private sector investment in services, including education and health took off. Private sector's involvement in the ICT sector, including broadcasting has also been exemplary. Moreover, Nepal has adopted Open Sky Policy resulting in large private sector involvement in the operation of airlines ensuring market competition. Furthermore, Nepal has set an example of hydropower development through the involvement of private sector, including PPP. Hence, private sector has significantly contributed to Nepal's economic growth.

2.7 Competition Policy

2.17. The Constitution provisions economic policy that provides for regulation to maintain fairness, accountability, and competition in all economic activities. It emphasizes protection of consumer interests by maintaining trade fairness and discipline by making the national economy competitive, while ending activities such as restricting competition, monopoly, and artificial scarcity. The Competition Promotion and Market Protection Act, 2007 and its corresponding 2010 regulation provide the legal framework for competitive market environment.

2.18. The Act aims to make the national economy more open, liberal, market-oriented and competitive. Its objectives are to maintain fair competition, protect markets against undesirable interference, and encourage competitive pricing, and control monopoly and restrictive trade practices. The Act has a provision of a Competition Promotion and Market Protection Board constituted under the Chairmanship of Secretary of Ministry of Industry, Commerce and Supplies (MoICS) to enhance fair competition in the market. Moreover, to further promote fair business practices, the Government is drafting Anti-Dumping Countervailing and Safeguard Bill.

2.8 Public Procurement

2.19. Nepal has made significant reforms in public procurement. The most important reform was the development of electronic government procurement (e-GP) system. At present, more than thousand public entities are active on this system. The system has helped to overcome challenges of inefficiencies arising from manual and paper-based procurement. This has resulted in increased access of people, transparency, and gains in efficiencies in public procurement. The Public Procurement Act, 2007 (with latest amendments in 2016) and the accompanying Public Procurement Regulations, 2007 provide the legal framework for public procurement in Nepal.

3 TRADE IN GOODS

3.1 Industry – Manufacturing

3.1. Nepal's industrial policy aims to enhance export of industrial goods by producing quality and competitive products, increase industrial sector's contribution by effectively utilizing local resources, raw materials, and skills, and make Nepal an attractive destination for investment. Although the contribution of industrial production as a percentage of GDP has declined in the last two decades, growth rate in industrial production has picked up in recent years, reaching 9.7% in FY 2016/17 and expected to be at around 8.0% in FY 2017/18.

3.2. Moving forward, Nepal plans to promote FDI in manufacturing industries with export potential and high value-addition in Nepal. Similarly, the Government has taken initiatives to further simplify industrial registration and provide tax incentives to manufacturing industries that start production within a stipulated time. The Government plans to increase industrial production by promoting investment in agriculture, forestry and mines-based sectors and other comparatively advantageous sectors with a policy to encourage establishment of big companies that can compete in the global market.

3.3. To further boost industrial production, ensure a competitive and investment-friendly environment, and simplify administrative procedures, the Government has created industrial estates and Special Economic Zones (SEZs). It is carrying out efforts related to infrastructure development to establish at least one industrial zone, and special economic zone in each province in coordination with provinces and in partnership with private sectors. There are 10 industrial estates at present and the Government intends to add further nine estates. Similarly, while one SEZ is already operational, feasibility studies are being carried out to establish further eight SEZs.

Product-specific zones for footwear, carpet, leather goods, handicrafts, and readymade garments are also being planned. The Government has plans to set up industrial villages in all local levels. Importantly, it is also planning to establish cross-border economic zones.

3.2 Energy

3.4. Nepal aims to sustainably utilize its rich energy potential by building on its success in solving the energy crisis during the review period. In the recent past, Nepal had experienced power shortage which slowed development activities. However, at present, the end to load shedding has been officially declared. The Government is focusing its efforts on developing and expanding hydroelectricity and all types of renewable energy to provide clean energy to all households within the next three years and avail smooth electricity supply across Nepal within the next five years. Accordingly, the Government has set forward a target to increase per capita electricity consumption up to 1,500 kilowatt hour (kWh) within the next 10 years by transforming consumption and distribution pattern so as to minimize the need for fossil fuels. To achieve these ambitions, it plans to produce 3000 megawatt (MW), 5000 MW and 15000 MW hydroelectricity within the next 3, 5 and 10 years, respectively, out of the economically feasible 43,130 MW, through public and private investment in small, medium and large hydroelectricity projects.

3.5. Nepal's private sector plays a vital role in hydropower development as it makes up nearly half of the total installed capacity of 1073 MW. Moreover, while 2200 MW of hydropower projects are under construction, 1300 MW of hydropower projects have undergone power purchase agreement which are awaiting financial closure. More than three thousand micro-hydropower plant (MHPs) have been installed so far in remote areas. The MHPs are owned and managed by communities and ensure a reliable alternative source of energy by providing off-grid access to a significant population.

3.6. The Government is integrating the electricity of completed projects into national grid system through the development of transmission lines. The Transmission System Master Plan (TSMP) unveiled in July 2018 aims to develop 6,867 kilometres of transmission line across Nepal. The Government plans to develop transmission lines, spreading along East-West and Mid-Hill Highway and along major river corridors spreading North-South. It is envisaged that these projects will be built through various models of private sector involvement. To open up electricity connectivity with northern neighbour, Nepal plans to develop Cross Border Transmission Lines (CTBLs) such as Galchhi-Rasuawagadi-Kerung transmission line connecting Nepal to China. To that end, cooperation agreement between Nepal Electricity Authority and State Grid Corporation of China has been concluded. Similarly, while one high voltage CTBL connecting Dhalkebar (Nepal) and Muzzaffarpur (India) is in operation, several other CBTL are being planned at different locations along the southern border of Nepal. Among the planned CBTL, the 400 kV Butwal (Nepal) – Gorakhpur (India) CBTL has been prioritized and is being pursued for construction. Government's focus on developing transmission lines is aimed at meeting Nepal's requirement in the short run and exporting power to neighboring countries in the long run.

3.7. Significant steps have been taken for increased energy co-operation with neighbouring countries. In November 2014, the South Asian Association for Regional Co-operation (SAARC) Framework Agreement on Energy Cooperation (Electricity), entered into force which paved way for relevant institutions in respective countries to develop transmission interconnectivity within the region to allow cross-border power supply. In the same year, Nepal and India signed a Power Trade Agreement (PTA) making way for free trade of power. In 2018, Nepal and China signed a Memorandum of Understanding (MoU) for establishing a mechanism on energy cooperation, furthering commitment of enhancing cooperation and creating an avenue for collaboration in the sector. Moreover, on 10 August 2018, Nepal and Bangladesh signed an MoU for cooperation in the energy sector paving way for Nepal to export surplus electricity to Bangladesh.

3.8. Ministry of Energy, Water Resources and Irrigation launched a white paper in May 2018 with an aim to attain self-sufficiency in electricity through overall development of electricity sector, reduce trade deficit through the replacement of other sources of energy by electricity, expand internal and external market for electricity, and deliver sustainable, reliable and clean energy to people. The white paper has stated Government's plan to amend Electricity Act and Nepal Electricity Authority Act and formulate the Renewable Energy Development Act. Immediate set up of Electricity Regulation Commission under the Electricity Regulation Commission Act, 2017 is

planned. The white paper also incorporates 'One Province, One Mega Project' strategy with an aim to build a mega hydro or solar project in each of the seven provinces.

3.3 Mines and Mineral Resources

3.9. Nepal's Mineral Policy seeks to sustainably utilize its immense potential in mineral resources and contribute to making the economy more competitive, dynamic and prosperous. Government aims to collaborate with the private sector in exploring, excavating and processing potential minerals and precious metals. Nepal lies in the centre of the 2,500 km Himalayan belt, which has favourable geography for various mines and minerals and hence offers a plethora of unparalleled opportunities for investors in the mining and mineral sectors. With 83% of the region being mountainous and hilly territory, Nepal is abundant in iron, limestone, talc, red clay, granite, marble, gold, precious and semi-precious stones (tourmaline, aquamarine, ruby and sapphire) and other construction minerals.

3.10. Notable developments have taken place in the sector. The cement industry has considerably expanded to a point where it has been able to fulfil a significant proportion of the domestic consumption and is expected to start exporting in a few years. Recently, significant FDI related to the cement industry has been approved and invested in Nepal. The IBN signed a Project Investment Agreement (PIA) worth US\$359.2 million with Hongshi-Shivam Cement, a Nepal-China joint venture company, to set up a mega cement factory in Nepal. The company has already started trial production. Similarly, during Prime Minister KP Sharma Oli's visit to China, IBN also signed PIA with Huaxin Cement Narayani to establish a US\$140 million cement plant. Moreover, the Government has identified exploration for many fuel minerals, including petroleum, natural gas, and methane gas. Various developments and reforms initiatives taken by the Government shows its commitment to promote higher trade and investment in the mines and minerals sector.

3.4 Agriculture

3.11. During the review period, the Agriculture Development Strategy (ADS) was brought with a vision for a self-reliant, sustainable, competitive, and inclusive agricultural sector that drives economic growth and contributes to improved livelihoods and food and nutrition security. Nepal's geography, topography, water resources and ample supply of labour give a comparative advantage in agricultural production. Nepal's economy is mostly dependent on agriculture, but the sector's contribution to GDP has been decreasing and is estimated to be at around 27.6% for 2017/18. Nevertheless, the sector absorbs about two-thirds of employment. The Government has put forward plans to double agricultural production in the next 5 years and shift a large population employed in the sector to non-agricultural sectors through modernization, diversification, commercialization, and restructuring of this sector.

3.12. The Government also has plans to work with private sector to establish organic fertilizer, chemical fertilizer, pesticides and agriculture equipment factories to facilitate supply of agricultural inputs as well as industries based on herbal and forest materials. Building on Trade Policy, 2015, National Trade Integration Strategy, 2016 has identified agricultural products such as large cardamom, ginger, tea, and medicinal and aromatic plants (MAPs) together with other products and services as having high export potential. Development of these products along with other potential products such as coffee, fruits and vegetable juice, honey, and so on has been prioritized.

3.5 Sanitary and Phytosanitary (SPS)

3.13. The National Agriculture Policy, 2004 provisions for development of technical regulations and standards to control food quality and certify food products. ADS has put forward the Government's plans to adopt and implement internationally compatible food quality and safety standards. It also envisions an independent Food Authority following the preparation of a new Food Act and focuses on capacity strengthening of Department of Food Technology and Quality Control (DFTQC), Department of Agriculture, Department of Livestock as well as upgrading of laboratories under them to an internationally accredited level. The DFTQC continues to function as the SPS Enquiry point. It has responsibilities of collecting SPS related data and acting as a government agency through which SPS related rules, regulations, standards, and guidelines are regulated. Nepal has either fulfilled or is regularly fulfilling its SPS related obligations of WTO. However,

Nepali exporters continue to face SPS related hurdles while exporting goods to destined markets. The DFTQC has taken initiatives to enhance lab capacity and upgrade the overall quality of infrastructure. However, there are areas of improvement, especially in building capacity, strengthening quality of infrastructure, and improving accreditation through Mutual Recognition Agreement (MRA) among others.

3.6 Technical Regulations and Standards

3.14. To facilitate international trade, Nepal has adopted standards that are mostly based on international standards, such as International Organization for Standardization (ISO), International Electro-technical Commission (IEC), the Codex Alimentarius or well-recognized national standards such as the British Standard Institution, and the Bureau of Indian Standards. Nepal has been upgraded to full membership of the ISO, coming into effect from January 2014. The legal framework for standards and technical requirements is guided by Nepal Standards (Certification Mark) Act, 1980 while Standards Weights and Measures Act, 1969 guide metrology. 904 national standards have been developed by Nepal Bureau of Standards and Metrology (NBSM), out of which 51 standards on product, process, test methods and management systems have been developed after 2012. Also, out of the 904 national standards, more than 100 are adopted from ISO. Similarly, NBSM established bilateral cooperation agreement with Bureau of Indian Standards in 2017 and an MoU with Bangladesh's Standards & Testing Institution in 2016. Finally, development of National Accreditation Board and relevant legal instruments are in progress.

4 TRADE IN SERVICES

4.1 Tourism

4.1. Nepal offers world class destination due to its outstanding natural beauty, biodiversity, and rich cultural heritage. Lumbini, for example was rated by Lonely Planet as one of the top ten destinations in Asia to visit in 2018. The Travel and Tourism Competitiveness Report 2017 ranks Nepal high in terms of price competitiveness (19th), international openness/ visa requirements (8th) and abundance of natural resources (27th). Nepal offers majestic mountains (8 out of 14 highest peaks), socio-cultural diversity, World Heritage sites, religious sites (including Lumbini, Pashupatinath, Janakpur, Muktinath, etc.), natural heritage (including various national parks and wildlife sanctuaries) and adventure tourism opportunities, among others. The National Tourism Strategy, 2016-2025, launched in November 2016, seeks to tap into this potential by mobilizing domestic investment, promoting FDI in the sector, and implementing strategies such as branding, marketing, infrastructure development and improvement of quality of tourism. Some primary targets include increasing arrivals to 2.5 million per year after 5 years, average length of stay to 15 days, average spending per tourist per day to 90 USD, jobs in the tourism sector to 898,000, foreign exchange earnings from the sector to NRs 340 billion, and the sector's contribution to Nepal's GDP to 9.3%, by 2025. Similarly, Tourism Vision 2020 recognizes tourism as a sector with the most promise to contribute to Nepal's sustainable growth. It envisions tourism being Nepal's primary sector generating employment. It aims to achieve the target of welcoming 2 million tourists a year by 2020.

4.2. Tourism has continued to remain one of the most significant contributors to the national economy in terms of income, employment, foreign exchange and extending market for domestic production of both commodities and services. Nepal has seen consistent growth in number of tourists in the last 2 years with impressive growth rates of about 40% and 25% in 2016 and 2017, respectively. More than 1700 foreign investment projects have been started in the tourism sector with worth about NRs 137.7 billion in total and have created almost 65,000 direct jobs during the review period. The following table summarizes some of Nepal's data on tourists and tourism.

Table 4.1 data on tourists and tourism

Year	Total tourists	Total tourists by air	Total tourists by land	Average length of stay (in days)	Per day expenditure (US\$)	Receipts from tourists (US\$ million)	Number of hotels	Number of beds
2012	803,092	598,258	204,834	12.1	35.6	379	853	31,657
2013	797,616	594,848	202,768	12.5	42	388.9	1,026	34,523
2014	790,118	585,981	204,137	12.4	48	472.2	1,075	36,179

Year	Total tourists	Total tourists by air	Total tourists by land	Average length of stay (in days)	Per day expenditure (US\$)	Receipts from tourists (US\$ million)	Number of hotels	Number of beds
2015	538,970	407,412	131,588	13.2	70	544.3	1,073	36,950
2016	753,002	572,563	180,439	13.4	53	392.7	1,062	38,242
2017	940,218	760,577	179,641	12.6	54	510	1,101	39,833

Source: Ministry of Culture, Tourism and Civil Aviation/MoF.

Note: The figures do not include Indian tourists who travel to Nepal by land.

4.3. The Government recognises the need to address gaps in tourism-related infrastructure to truly unleash the potential of tourism sector in Nepal. Hence, it has prioritized development of tourism-related infrastructure, promotion of market and expansion of services and facilities for recreational, natural, historical, religious and adventurous tourism. It has highlighted plans to further expand the Tribhuvan International Airport, initiate Nijgadh International Airport, accelerate construction of Pokhara Regional International Airport, and complete and operate Gautam Buddha Regional International Airport. There are also plans to upgrade Biratnagar, Janakpur, Nepalgunj and Dhangadi airports as Regional Airport and start flights to neighbouring countries. Finally, necessary preparations are underway to organize 'Visit Nepal Year' in 2020 to attract more tourists. These plans represent enormous investment opportunities.

4.2 Transport

4.4. The transport sector has grown substantially and is expected to transform significantly given Government's priority in expanding transport infrastructure. Transport sector contributes about 7.97% of GDP and grew at a rate of 5.41% in FY 2017/18. Average growth rate of the sector in the past five years has been 6.32%. By FY 2017/18, length of strategic roads has increased to 29,639 km which includes 13,149 km black topped roads, 6,956 km gravelled roads, and 9,534 km earthen roads. Nepal also has 35 domestic airports in operation and an international airport in Kathmandu.

4.5. Nepal has gained significant achievements in cooperation for improved connectivity. Visakhapatnam has also been added as an additional port. Efforts are underway to further diversify the transit facility and connectivity through China and Bangladesh. In fact, in May 2017, Nepal signed the framework agreement on Belt and Road Initiative (BRI) with China. The MoU signed between Nepal and China seeks to strengthen cooperation in connectivity, including transit transport, logistics systems, transport network and related infrastructure development such as railway, road, and civil aviation, among others. Moreover, during high level visit by Prime Minister KP Sharma Oli to China, Nepal and China have agreed to intensify enhanced connectivity, such as ports, roads, railways, aviation and communications within the overarching framework of trans-Himalayan Multi-Dimensional Connectivity Network. Similarly, in 2015, Nepal, Bangladesh, Bhutan, and India signed a Motor Vehicles Agreement (MVA) for the Regulation of Passenger, Personnel and Cargo Vehicular Traffic.

4.6. The Government has put forward plans to develop important national highways as express highways and East-West and North-South roads of national importance as national strategic road network. There are plans to connect the centres of all local levels with black-topped roads in the next five years. To cater to the needs of growing population, development of mass public transportation systems – bus-rapid transit (BRT), monorails, airports, and railways, including Mechi-Mahakali Railway, Kathmandu-Birgunj Railway, and Rasuwagadhi-Kathmandu-Pokhara-Lumbini Railway, has been prioritised. Transport sector is open to domestic as well as foreign investment and is key in achieving infrastructure development goals.

4.3 Information and Communication Technology (ICT)

4.7. Nepal recognises the role of ICT as an enabler and driver of economic growth. Accordingly, there is an emphasis to focus the majority of domestic and foreign investment in the ICT sector. The Government aims to improve public service delivery by promoting the use of ICT to modernize areas, including public administration, professional areas, public and private services, database, statistics, financial transactions as well as for biometric information and national identity card.

Moreover, IT services and business process outsourcing (BPO) has been identified in NTIS, 2016 as one of the three priority service sectors with the most potential for exports. In addition, Nepal also recognises growing importance of e-Commerce for overall economic development. Recently, "e-Commerce National Action Plan" has also been proposed which highlights the Government's commitment to developing the sector.

4.8. Nepal's telecom sector has been further liberalized through the adoption of various policies and regulations, including National Broadband Policy, 2015, Information and Communication Technology (ICT) Policy, 2015, Spectrum Policy, 2016, and Telecom Infrastructure Service Regulation, 2017. The ICT Policy, 2015 addresses issues of policy incongruence and is a positive step in unlocking the growth of IT, and IT-enabled service sector. Based on the Broadband Policy, Government has already started efforts to expand broadband network throughout the country, especially laying optical fibre in the rural areas by utilising Telecommunication Rural Development Fund. Following this, it has plans to develop information high-way at all local levels. Besides, other legal provisions, including National Broadband Master Plan, Telecommunication Frequency Distribution Regulation, and Regulatory Framework for Mobile Portability, are being drafted.

4.9. Significant improvements have been observed in the ICT sector, particularly in the participation of private sector. Private investment has increased in print and electronic media as well as distribution and cable network. Box office system with electronic ticketing for film distribution and exhibition has been introduced making collection of revenue such as Value Added Tax (VAT) in the film business and film development fee more systematic. The Government is also building e-Payment Gateway. Moreover, Nepal's ICT sector performed as one of the fastest emerging sectors during the review period and has shown immense potential for growth in upcoming years. Access to television and radio has reached around 80% and 90% of the population respectively and is expected to reach 100% within the next few years. Internet penetration rate has drastically increased from 35.70% in 2014 to 62.94% in 2017. Mobile penetration rate has reached 130% with mobile subscriptions increasing from 18.93 million in 2013 to 38.1 million in 2017.

4.10. Despite various positive developments, there are further opportunities for improvement through investment in the ICT sector in Nepal. UNCTAD's e-Trade Readiness Assessment of Nepal commends Government of Nepal's efforts in ensuring that young Nepali have good IT acumen and the coverage of ICT is good enough. Moreover, the report highlights areas that need more work. There are opportunities to invest for improvements in mobile network coverage, international internet bandwidth, and secured internet services. Similarly, opportunities lie in improving logistics by bundling existing products and services together and introducing new ones. Further innovation supported by a favourable legal and regulatory framework will facilitate growth of domestic and international e-Commerce. These developments can enable more than 100,000 Small and Medium Enterprises in Nepal, especially owned by women and young entrepreneurs, to grow globally. This growth is supported by an increasing youth population that is educated and has necessary digital skills to utilize the opportunities presented by ICT development.

4.4 Financial Services, Banking and Insurance

4.11. The Bank and Financial Institutions (BFI) sector has been a key driver of growth of Nepal's service sector. The Government aims to use BFI sector to support infrastructure and industrial development in Nepal. The BFI sector continued to grow during the review period. There are 28 commercial banks out of which seven are joint venture banks with foreign companies. The success of joint venture banks is evident from their relatively better performance in the Nepali market and consistently high and growing profits compared to BFIs in South Asia, collectively totalling NRs 13.41 billion in FY 2016/17. There are also 36 development banks, 25 finance companies, and 63 micro-credit institutions. As of March 2018, the number of insurance companies has reached 39, including 18 life insurance, 20 non-life insurance and one re-insurance company. Out of the 39 companies, three are branches of foreign insurance companies, three have been established with joint investment with foreign insurance companies, 30 are private, while three are Government-owned. Foreign investors have been able to make use of "Policy Provision for Opening Branch Offices by Foreign Bank or Financial Institutions in Nepal 2010" and continuously increasing their presence in Nepal's financial sector.

4.12. Reforms in the financial sector have also been carried out. NRB raised the paid-up capital of financial institutions, for example, from NRs 2 billion to 8 billion in the case of commercial banks.

This was carried out to strengthen the entire financial sector by promoting financial stability and mobilizing resources for long-term development and by expanding their coverage. The NRB Act Second Amendment, 2016 aims to strengthen and clarify the bank resolution powers of the central bank, increases the NRB's capital, and aligns accounting standards with international practice. Assigned capital required for foreign BFIs to open branches for wholesale banking has been reduced from US\$30 million to US\$20 million. The Deposit and Credit Guarantee Fund Act, 2016 enhances the legal framework for the deposit insurance scheme.

4.13. The Government has emphasized on achieving double-digit growth which needs increased investments in large infrastructure and energy projects. Hence, along with legal reforms, it is planning for further supportive policy measures. These include introduction of new institutions such as Private Equity, Venture Fund and Hedge Fund into the capital market, carrying out of credit rating assessment of Nepal, introduction of blended financing instruments, among others. Banks and Financial Institutions Act (BAFIA), 2017 has provisioned for and encouraged the establishment of Infrastructure Development Banks that have a minimum paid up capital of 20 billion rupees and foreign ownership of up to 85%. Policy provision 2017 has been issued to provide licence for such banks. The Government is accelerating the process of operating a planned Infrastructure Development Bank in collaboration with the private sector.

4.14. The number of BFI branches has significantly grown and has reached 6418. While each BFI branch covered approximately 9000 people on average in mid-June 2012, the population served by per branch of BFIs stood at 4490 in mid-June 2018. Similarly, the number of mobile banking and internet banking users has reached 4 million and 784 thousand, respectively. These figures represent a significant improvement in access to financial services but there are opportunities to improve further. The Government has initiated a policy to ensure presence of banks in all local levels. In this backdrop, opportunities exist to expand bank coverage and extend mobile and internet banking to the entire section of the population. Finally, further policy changes are required to incentivize mobilization of investment in the productive sector.

5 POLICY FOR AN EFFECTIVE TRADE REGIME

5.1 Trade Policy

5.1. Nepal has updated the trade policy to harmonize with other sectoral policies, create alignment between trade policy and NTIS, address increasing trade deficit, and promote exports by enhancing the supply-side capacities. Nepal's first comprehensive trade policy after joining the WTO was Trade Policy, 2009 which replaced Trade Policy, 1992. Trade Policy, 2009 embraced the principles of liberal, open and transparent economic system and had primary objectives to increase trade sector's contribution to the national economy and help reduce poverty and accelerate economic growth. However, results of the Policy remained mixed and hence have been replaced by Trade Policy, 2015.

5.2. The vision of Trade Policy, 2015 is to achieve economic prosperity by enhancing trade sector's contribution to the national economy through export promotion. The strategies focus on strengthening supply-side capacity, increasing exports of value-added competitive products and services in the world market, increasing access of goods, services, and intellectual property to regional and world markets, among others. The Trade Policy, 2015 also provisions for a Board of Trade under the Chairmanship of Minister of Industry, Commerce and Supplies. The Board includes the private sector and has responsibilities of assisting in formulating policies necessary for trade promotion, trade facilitation, policy monitoring and inter-agency coordination.

5.2 Nepal Trade Integration Strategy (NTIS), 2016

5.3. Nepal has introduced its third-generation trade integration strategy to strengthen trade and export enabling environment, focus on product development and strengthen supply capacity of priority products, strengthen institutional capacity, trade negotiation and inter-agency coordination, and build and enhance trade related infrastructures. Previously, Nepal had launched the Diagnostic Trade Integration Study (DTIS) in 2004 that could not be appropriately implemented due to various reasons. Later, DTIS was revised as NTIS and released in 2010 to complement the Trade Policy, 2009. This was further updated in 2016 in line with the updated Trade Policy, 2015.

5.4. NTIS 2016 aims to enhance Nepal's export competitiveness by addressing seven cross-cutting strategic areas: trade capacity, trade and investment environment, trade and transport facilitation, standards and technical regulations, SPS, intellectual property rights, and trade in services. NTIS 2016 focuses on value chain development of priority export products, including four agro-based (large cardamom, ginger, tea and MAPs), five craft and manufacturing (all fabrics, textile, yarn & ropes, leather, footwear, chyangra pashmina, and knotted carpets), and three services (skilled & semi-skilled professionals at various categories, IT & BPO, and tourism). It has identified one hundred and ninety actions to be implemented within the time-frame of five years.

5.3 Industrial Policy

5.5. Continuing its efforts to make industrial policy relevant and supportive of industrial development, Nepal introduced Industrial Enterprises Act, 2016 to further simplify and clarify procedures for entry, operation and exit of industrial enterprises as well as introduce much-needed reforms. Nepal's first industrial policy was released in 1957 and later updated and replaced in 1960, 1974, 1981, 1987, 1992 and 2010, respectively. Industrial Policy, 2010 guides Nepal's overall policy related to the industrial sector. Its objectives are to enhance export of industrial goods, improve industrial sector's contribution to the economy by using local resources, make industrial enterprises sustainable and dependable through application of innovative and environment-friendly technology, make Nepal an attractive destination in South Asia for investment, and protect intellectual property rights of industries. Industrial Policy, 2010 is supported by the Industrial Enterprises Act, 2016 which replaced Industrial Enterprises Act, 1992. Some salient features of the Act are: tax incentives, concession and benefits of VAT and custom duties, facilities to acquire land, provisions ensuring no nationalisation of industries, and creation of a single window service for foreign investors. The Act has provided various fiscal incentives to industries, including, an effective tax rate of 16% for almost all manufacturing industries and 25% discount on export income from export of goods.

5.4 Intellectual Property Rights

5.6. Nepal has achieved significant success at policy domain of intellectual property (IP) rights regime. Nepal's Constitution guarantees intellectual property rights by including IP within the fundamental rights chapter. Article 25 of the Constitution ensures rights of all Nepali citizens to "acquire, own, sell, dispose, acquire business profits from, and otherwise deal with property," where property means any form of property including movable and immovable property and intellectual property. Moreover, Nepal released its first National Intellectual Property Policy in 2017.

5.7. The Policy aims to create a balanced IP system in Nepal and has a vision of a creative nation through preservation and provision of intellectual property protection. The Policy's objectives are to: encourage protection, promotion, and development of IP, develop a balanced IP system, create awareness about social, economic and cultural aspects of IP, encourage commercialization of IP, and strengthen legal, administrative and human resources to ensure protection and enforcement of IP. The Policy revises existing legal framework, recognizes for an enactment of law related to patent, industrial design, trademark, utility model, geographical indications, traditional and indigenous knowledge, folklore, traditional knowledge, integrated circuit, plant variety protection, trade secrets and biodiversity. It aims to create awareness and promote intellectual property rights. It also addresses the need to curb IP infringement and recommends revising penal provisions under existing legal framework. The Policy also envisions a National Intellectual Property Council consisting of members from ministries concerned, civil society, and experts to facilitate and advise on policy issues. Building on the IP Policy, at present, the Intellectual Property Rights Bill is in the process of being drafted.

5.8. Other relevant reforms have also been carried out. Nepal has carried out reforms related to royalty collection from users in the music industry, whereby, music artists receive royalties from their music broadcasted on various media channels, including radio, FM, television, telecom, transportation, and other channels. This reflects the Government's commitment in protecting intellectual property rights of innovators and investors. Department of Industry and Nepal Copyright Registrar's Office are two directly relevant public institutions that look into matters related to intellectual property.

5.5 Foreign Investment Policy

5.9. Nepal has taken significant strides in reforming its investment regime to support trade. Foreign Investment and One Window Policy, 1992 was replaced with Foreign Investment Policy, 2015. The Policy's objectives are to: mobilize foreign capital, technology, skill and knowledge in priority sectors for broad-based economic growth, employment creation, and utilisation of local resources, allowing entry of modern technologies, managerial and technical skills along with foreign capital for increasing domestic production and productivity, and establish Nepal as an attractive investment destination.

5.10. The Policy seeks to achieve these objectives through 19 policy instruments and 36 working policies. Some significant provisions for foreign investors are: repatriation of dividend, profits and salary of employees, national treatment in respect of incentives and facilities, facilities in terms of deductible income in income taxes, accelerated depreciation, options to raise financial resources within and outside the country, visa facilitation, additional security measures and facilitation in land acquisition, among others. Importantly, the Policy has assured national treatment and non-nationalization of investment, provided ground for mediation and arbitration as per UNCITRAL rules and simplified exit procedures. Two high-level institutional mechanisms have been formed to facilitate foreign investment – Investment Board, chaired by the Prime Minister of Nepal and the Industrial Promotion Board, chaired by the Minister of Industry, Commerce and Supplies. As per, the aspiration of the Policy, new draft of Foreign Investment and Technology Transfer Act has been prepared.

5.6 Other Major Policies Related to Trade and Investment

5.11. A key development has been the operationalization of the IBN. Nepal had enacted Investment Board Act, 2011 and Regulations, 2012 with the objectives of mobilizing domestic and external private resources, promoting PPP, supporting development of physical infrastructures and enhancing the industrialization process. The Act has constituted a high-powered investment board under the chairmanship of Prime Minister of Nepal. The Board is empowered to formulate policy on investment, select priority areas for investment seek proposals from potential investors, decide terms and conditions of investment, facilitate investment, provide financial and non-financial services and incentives, promote coordination among various government agencies, and provide fast-track problem-solving services and market Nepal as investment destination, among others. IBN has been mandated for approval, management and facilitation of wide-ranging projects, including hydro-electricity projects with more than 500 MW generating capacity, and infrastructure and services industries worth more than NRs 10 billion. IBN has already been successful in facilitating export-oriented projects in hydropower and manufacturing sectors.

5.12. Going forward, the Government seeks to encourage foreign investment further to make Nepal an attractive destination for foreign investment by treating it as a complement of national capital formation. Recently, an act has been proposed that seeks to reform and unify laws related to foreign investment. The act aims to make the national economy further competitive, liberalized, and employment-oriented and promote export and attract foreign investment. As such, the proposed act is even more outward-looking. Moreover, recent budget has put forward proposals to strengthen the IBN further by developing it as an institution for granting investment approval through a one-door system, including for PPPs.

6 REFORMS AND IMPROVEMENTS

6.1 Legal and Policy Reforms

6.1. Significant legal reforms have been made to further mainstream trade in national development process. A major achievement is promulgation of the Constitution which acts as the Mega Policy. Based on the Constitution, Government is making necessary legal provisions to implement fundamental rights such as rights related to consumer protection, social security and employment. Trade and industrial sector is well reflected in the Constitution. An important reform was the enactment of Muluki Ain (Civil Code) Act, 2017 which replaced Civil Code (Muluki Ain), 1853 (revised in 1962). The Act has important provisions of reforms that brings paradigm shift in social practices.

6.2. Other relevant legal reforms include policies and acts such as Trade Policy, 2015. Foreign Development Cooperation Policy, 2014; Foreign Investment Policy, 2015; Intellectual Property Policy, 2017; Industrial Enterprise Act, 2016; Special Economic Zone Act, 2016; Labor Act, 2017; and BAFIA, 2017. Reforms have been made in the areas of procurement with amendments to Public Procurement Act in 2016 and amendments to Public Procurement Rules in 2017. The Export Import Management Act is being amended and Safeguard, Antidumping & Countervailing bill has been drafted. Similarly, to support export promotion and Special Economic Zone Rules, 2017 have been brought about. Sectoral reforms have been made through the introduction of Agricultural Development Strategy, 2015, National Mining Policy, 2017, and Information and Communication Technology Policy, 2015. In the electricity sector, reform has been introduced through the enactment of Electricity Regulatory Commission Act, 2017 and subsequent regulations are under preparation.

6.2 Structural Reforms

6.3. Nepal has carried out transformative structural reforms with the promulgation of the Constitution and enhanced development diplomacy. A key focus has been on transit and connectivity, including signing of Transit Transport Agreement with China, signing of MoU on Belt and Road initiative, PTA with India, additional transit port (Visakhapatnam) of India. The issue of power shortage has been addressed and at present there is no more load-shedding. A key development was the operationalization of electronic e-GP system by Public Procurement Monitoring Office (PPMO). Similarly, the Government has introduced online business firm registration system. Nepal trade information portal has also been functional. Nepal's parliament has ratified the Trade Facilitation Agreement (TFA) as well as the Revised Kyoto Convention (RKC). Hence, through its various efforts, Nepal has shown its commitment to Multilateral Trading System and moved in the direction of transforming its economy structurally.

6.3 Customs Reforms

6.4. Various customs-related policies and institutional reforms have been carried out for trade-facilitation. The Government through Department of Customs (DOC) has been introducing Customs Reform and Modernization Strategies and Action Plan (CRMSAP) since 2003. Implementation of the 5th CRMSAP started in 2017 and continues until 2021. The 5th CRMSAP envisions essential reform strategies, including, expedited legitimate trade facilitation, enhanced customs automation & data management, streamlined coordinated border management, organizational restructuring to support risk-based clearance, among others.

6.5. E-Customs master plan has been implemented. Web-based ASYCUDA world system has been implemented in 15 customs offices, covering about 98% of total trade. Implementation of the system in the remaining five customs offices is in the process. The development of Nepal National Single Window (NNSW) is in progress and is expected to be completed in 2019. Risk-based selectivity module (green, yellow and red channel) has been implemented. Moreover, Trade Facilitation Committee as well as Client Service Centre has been formed at DOC and Customs Offices. Following Nepal's ratification of the TFA in January 2017, Nepal acceded to the RKC in February 2017, and the parliament has ratified the RKC. This shows Nepal's commitment in implementing modern and effective Customs procedures adapted to the international trade environment and its efforts towards trade facilitation.

6.4 Reforms Related to Trade Infrastructure

6.6. Nepal has been able to significantly improve its trade related infrastructure. To simplify customs clearance procedures and make more efficient for trade facilitation, Integrated Check Posts (ICPs) are being built in main border-crossing points between India and Nepal, namely Bhairahawa (Rupandehi), Nepalgunj (Banke) and Biratnagar (Morang). The ICP Birgunj came into operation during the review period. While, Nepal also has four Inland Container Depots (ICDs) in operation, namely Bhairahawa, Birgunj, Biratnagar and Kakarbhitta (Jhapa), three are under construction in Chobhar (Kathmandu), Timure (Rasuwa) and Tatopani (Sindhupalchowk), and a feasibility study is being conducted for additional port in Dodhara Chandani. While Birgunj is railway-linked with Indian seaports, all other ICDs are road-based. Moreover, Electronic Cargo Tracking System (ECTS) has been introduced in the traffic in transit of Nepal passing via India.

Under this system, movement of Nepal bound cargo can be tracked so as to increase their time-efficiency.

6.7. Recently, Nepal and India have also agreed to review Trade Treaty, Transit Treaty and Railway Service Agreement which will help in addressing issues related to transit and trade. Nepal has also carried out reforms to improve roads that are most important for trade. The work for constructing Fast Track (Nijgadh-Kathmandu) has begun. Other roads such as Jogbani-Dharan, Kohalpur-Nepalgunj, Bhairahawa-Butwal, and Narayanghat-Mungling are being improved.

6.8. Nepal has taken reform initiatives in the areas of inland waterways. Nepal concluded a landmark agreement with India to develop inland waterways for cost-effective and efficient cargo movement, within the framework of trade and transit arrangements, providing additional access to sea for Nepal. Work is already under way to carry out relevant study on both sides. Moreover, with an aim to bring waterways of 200 kilometres in total length into operation in Koshi, Gandaki and Karnali rivers within the next five years, Nepal is preparing necessary policies, laws and institutional arrangements.

7 TRADING ARRANGEMENTS

7.1 Bilateral - Trade with India, China and Bangladesh

7.1. Nepal envisages balanced and responsible international relations that respect various bilateral, regional, and multilateral agreements. It believes in maintaining amicable and mutually beneficial trade relations with its neighbouring countries, China and India which are its largest trading partners. Nepal and India share open borders and have a multi-dimensional friendly relationship in various economic spheres, with trade and transit being core elements. India is not only Nepal's largest trading partner with almost two-thirds of share in Nepal's total trade but also the largest market for Nepali goods consisting of almost 57% of its total export. Total trade volume with India in FY 2016/17 was NRs 687.52 billion out of which Nepal's exports to India was worth NRs 41.5 billion whereas imports were NRs 646.02 billion. Major products exported to India are coffee, vegetables, cardamom, juices & iron and steel whereas major imports are fuel (petroleum, diesel, and kerosene), vehicles & cement clinkers, etc. Nepal's trade deficit with India has been an increasing challenge, a fact that is recognised by both governments. Therefore, efforts are underway to revise the terms of various bilateral co-operations to make bilateral relations more equal and respectful and undertake various reforms to modernize and align trade relations with current requirements of international trade.

7.2. Trade and investment relations with China has significantly grown in recent years. In fact, in the first eight months of FY 2017/18, Chinese investors constituted 28.7 percent of the total number of industries that got approval for foreign investment. China is Nepal's second largest trading partner. Total trade volume with China in FY 2016/17 was NRs 135.23 billion out of which total exports to China was worth NRs 2.04 billion and imports were NRs 135.23 billion. Major products exported to China are essential oils, base metals, carpets, sugar etc. and major products imported are electrical equipment and machinery, nuclear reactors, boiler, fertilizers, telephone, etc. The Government expects new avenues of bilateral collaboration following the signing of the MoU on Co-operation under BRI 2017 and further bilateral understandings agreed this year. In particular, areas such as infrastructure and cross-border connectivity are expected to be enhanced through the co-operation.

7.3. Bilateral trade relations with Bangladesh gained momentum after the operationalization of Kankadhitta-Phulbari-Banglabandh transit route, and over the years Bangladesh has increasingly been an important trade partner of Nepal. In FY 2016/17, trade volume with Bangladesh stood at NRs 5.28 billion out of which exports comprised NRs 1.05 billion and imports comprised NRs 4.23 billion. Major products exported to Bangladesh are lentils, vegetables and major products imported are juice, jute, medicaments etc. Nepal is working together with Bangladesh to enhance trade cooperation, including power trade and to narrow down trade imbalance.

7.2 Regional - SAFTA and BIMSTEC

7.4. Nepal has joined two regional agreements -South Asian Free Trade Area (SAFTA) and Bay of Bengal Initiative for Multi-Sectoral, Technical and Economic Cooperation (BIMSTEC). While SAFTA

focuses on the South Asian region, BIMSTEC connects South Asia with South East Asia. The SAFTA Agreement, which succeeded South Asian Preferential Trade Agreement (SAPTA), was signed in 2004 and came into force from 2006. It aims to deepen trade and economic cooperation among member countries by promoting fair competition through removal of barriers to facilitate cross-border movements of goods. During the last review period, SAFTA members had gradually been reducing tariff to 0-5% on all tariff lines except the sensitive lists as per trade liberalization program of the Agreement. The sixth meeting of the SAFTA Council in 2012 took the initiative to reduce the number of products on the sensitive lists by 20%; Nepal has already achieved the relevant target by 2014. Similarly, during the 16th Summit in 2010, the SAARC Agreement on Trade in Services (SATIS) was signed which came into force with effect from 2012. SATIS recognises the regional growth potential of trade in services and is focused on expanding intra-regional investment and trade liberalization.

7.5. BIMSTEC was founded in 1997 for accelerated growth through cooperation in various areas of shared interest. Nepal joined BIMSTEC in 2004, the year in which a framework agreement with provisions of liberalizing trade in goods and services and negotiating agreement related to cross-border investment facilitation was also signed. In 2016, BIMSTEC came up with the *Outcome Document* and *16-point Agenda of Action* highlighting priority actions to be implemented. Recent meetings have seen members re-affirm their commitments to finalize agreements in various sectors. Energy co-operation has been a key feature of BIMSTEC agenda. The process of negotiations for reducing and eliminating tariff is underway. Nepal has been playing a significant role in giving momentum to BIMSTEC and is hosting BIMSTEC Summit, the highest policymaking body in BIMSTEC, in August 2018.

7.3 Multilateral Trading Arrangements

7.6. Nepal is a strong supporter of Multilateral Trading System (MTS) and believes in rule-based, transparent, and predictable MTS. Despite various constraints, Nepal has been engaging actively in the WTO and continuously fulfilling its obligations since its accession to the WTO in 2004. Nepal is also resolutely representing LDCs group at the WTO. Currently, it is working as a focal point on Trade Facilitation within LDCs group. Similarly, it is taking part in various development activities for the LDCs, including Aid for Trade (Aft) initiatives. Nepal is also in the process of implementing the various measures from TFA Section 1 as mandated by the agreement. Nepal has already notified Categories A, B, C as per the agreement to the WTO for the implementation of TFA. The Government perceives TFA as an opportunity to reduce costs and time related to trade and transit. Nepal has been adopting open and liberal economic policies and is committed to world trading system. However, Nepal's export performance could not be improved as per the expected level. The country's export import ratio 1:2 in 2004 (while accessing to the WTO) increased to 1:14 in 2018.

8 CONSTRAINTS

8.1. Nepal still faces several constraints to economic growth, some of which are being addressed through the Government's sincere efforts while others continue to be challenging for its development. Nepal's most serious constraint is its geography. On the one hand, trade and transit costs are higher for Nepal as it is a landlocked country. On the other hand, Nepal's difficult terrain due to geophysical features of high mountains and hills adds to the costs of developing infrastructure, promoting production, and doing business.

8.2. Supply-side capacity constraints as well as trade deficit and non-diversified nature of trade have remained key challenges for Nepal. In the last five years, trade deficit has nearly doubled. In fact, share of total export in the GDP has halved from about 10% to 5% in the past decade. The liberalization of the external sector increased imports. However, various constraints have held back Nepal from successfully exporting products with comparative advantage, at the same pace. Increasing consumption pattern, low level of production and productivity, heavy reliance on import of raw materials and fuel, and export of low value products, among others are some of the key contributors to ballooning trade deficit. Moreover, Nepal relies heavily on two major trading partners, India and China, and trade deficit with both has widened.

8.3. Nepal's trade performance has also been affected by inadequate economic, social, and trade-related infrastructure. Challenges included in the areas of road infrastructure, vocational and

technical education and certification mechanisms. Nepal is yet to fully utilize its potential for exporting various products by making use of concessional market access provided by many of its trading partners. Moreover, Nepal has not been able to take full advantage of incentives provided to LDCs, including GSP and DFQF initiatives, mostly because of stringent and complex requirements that needs to be fulfilled as an exporting country, and partly due to supply-side constraints.

8.4. Nepal is committed to overcoming trade-related infrastructure challenges to fully utilize its export potential and productive capacity. This would require significant investments. Despite Aft initiatives through the WTO, interest and support from development partners (DPs) for helping Nepal achieve its trade-related ambitions could be further enhanced. Moreover, various difficulties related to effective implementation of Aft in Nepal have been noted. Some of them are: disparities in the demand and supply of support, gaps in the levels of commitment and disbursement, poor coordination and duplication of donors' programmes, and lack of sustainability. Similarly, Aft has been more focused on soft part while Nepal continues to face challenges related to productive capacity and trade related infrastructure.

9 OPPORTUNITIES AND WAY FORWARD

9.1 Political Stability

9.1. Nepal's entry into an era of political stability represents an enormous opportunity for economic growth and sustainable development. The promulgation of the Constitution in 2015 followed by elections at all three levels has addressed long-held political aspirations and the country is now focused on achieving socio-economic prosperity. Political stability also opens an opportunity to strengthen further global partnership that would significantly contribute to achieving Sustainable Development Goals (SDGs) and also reaching to middle income country by 2030 along with graduation from the LDC status.

9.2. The Government has presented its vision for Nepal's transformative economic growth and aims to create an economy that fosters innovation, trade and investment. To support this vision, going forward, Nepal is firm in protecting, strengthening and positively utilizing democratic achievements. The Government aims to build a country that is free from any type of corruption, and that respects human and fundamental rights. To this end, Nepal has vowed to adopt policy of zero tolerance against corruption. Nepal is already taking measures to break restrictive business practices.

9.2 Macroeconomic Stability and Restructuring

9.3. Nepal has been able to maintain a stable economic environment even after facing natural disasters, trade disruptions and changes in government structure. This portrays the resilience of Nepal's economy and provides opportunities to thrive for people and enterprises. With overall positive outlook to trade, economic growth and minimized macroeconomic risks, opportunities for trade and investment are bound to grow. The Government aims to double Nepal's per capita income in five years' time. Rising income of Nepali will increase Nepal's market size and create profitable investment opportunities. Most importantly, the Constitution provisions for reallocation and redistribution of resources among various levels of governments on the recommendation of the National Natural Resources and Fiscal Commission. This ensures equitable distribution of resources, promotes balanced growth, maintains fiscal discipline and efficiency of the governments, increases economic activities and creates further trade and investment opportunities across the country.

9.4. Further restructuring of the economy is essential. This can be achieved by increasing contribution of industrial output in the GDP, doubling agricultural production in the next five years, transferring additional workforce from agriculture to industry and service, and encouraging investments in all sectors. Additionally, ensuring fiscal discipline at all levels of government, particularly local and provincial, is important. There is a need to use rigorous evidence in policy making and project prioritization. Moreover, the country needs to tap into the demographic dividend through the creation of an enabling environment for young entrepreneurs. To ensure this, Nepal needs to focus on areas such as extending financial access to the entire population and enabling creation of gainful jobs.

9.3 Conducive Trade and Investment Environment

9.5. Nepal has significantly reformed its trade and investment regime, further integrating Nepal into the global economy and presenting more opportunities for growth and investment. The Constitution promotes growth of amicable trade and investment environment, accordingly reviewing and revising several acts, rules and regulations. Nepal has updated its trade policy with a greater focus on export promotion and creating better alignment with cross-sectoral policies. Moreover, improvements in intellectual property rights regime, public procurement, guarantee of protection for businesses, flexible labour laws, and access to foreign markets provide opportunities for investors. Furthermore, Nepal has been showing its strong support and belief in the rule-based trading system and commitment towards an open and liberal economic policy.

9.6. It is important to carry out further reforms for increased investment-friendly climate. Nepal needs to focus its efforts on reducing cost of doing business, especially by improving its trade and industrial infrastructure. Moreover, there is also a need to accelerate the process of legal reforms particularly in the area of trade and investment. Realizing the risks of alarming trade deficit, Government aims to enhance exports capacity through various measure including supply side capacity enhancement and import management.

9.4 Energy and Infrastructure Development

9.7. Nepal has abundant opportunities in energy sector, especially in hydropower, and infrastructure development. Nepal has put a heavy emphasis on achieving double-digit growth which needs increased investments in large infrastructure and energy projects. The Government has plans to develop transport infrastructure, including railways, waterways, airports, expressways, tunnel ways, and cable cars and energy infrastructure, including mega hydroelectricity projects, transmission lines along with expansion, reinforcement and modernisation of distribution system. Recent reforms in financial sector have encouraged the establishment of Infrastructure Development Banks in collaboration with the private sector, introduction of new instruments in financial services such as blended financing, private equity, venture fund, hedge fund, credit rating, among others are expected to support the development of hydro power and infrastructure.

9.8. In order to exploit the available opportunities, various policy reform especially on PPP law, improving mega project management, enhancing coordination among government agencies concerned and stakeholder, and participation and support of people are essential.

9.5 Improved Economic Diplomacy

9.9. Increased connectivity and improved bilateral, regional, and multilateral relations through economic diplomacy provides Nepal with a lot of opportunities. Nepal signed important agreements for trade and transit connectivity and investment facilitation with its neighbouring countries. Nepal also signed the BBIN MVA along with Bangladesh, Bhutan and India to further strengthen sub-regional connectivity. These initiatives present better access opportunities to tap into the huge market of neighbouring countries as well as regional and global markets. Significant steps have been taken for increased energy co-operation. Nepal has signed PTA with its neighbouring countries and also SAARC Framework Agreement on Energy Cooperation at regional level. Nepal has been playing an active role in WTO in order to advancing the agenda of rule based trading system.

9.10. Nepal needs to work with its neighbours and regional partner countries to further enhance bilateral and regional cooperation. Nepal's focus needs to be on accelerating the implementation of various bilateral agreements. Nepal also needs to take a lead role in realizing the aspirations for increased regional connectivity and cooperation through effective implementation of regional agreements.

9.6 Governance Reform

9.11. Nepal's transition from a unitary form of government to a federal structure presents unprecedented opportunity to make public service delivery more responsive. It is also likely to provide more opportunities for doing business in a stable policy environment. The reformed

governance structure is expected to improve economic policy-making and performance via greater emphasis on local opportunities and challenges. In fact, provincial governments have already started to take initiatives in attracting businesses through various incentives, presenting new opportunities for investors and businesses.

9.12. Restructuring of Government ministries in line with the constitutional provision has been carried out and MoICS has been formed by merging the then three ministries, which has also become supportive to ensure all intervention in trade, industry and investment complementing each other. In this context, several laws and rules related to trade and investment regime are being reviewed and reengineering of institutions is being carried out which will help Nepal navigate better in a changed governance context.

9.13. Against this background, it is important to leverage digital technology for improved governance. There are already some government agencies and services that are integrated into digital technology. To realize the aim of a 'Digital Nepal', it is crucial that more government agencies provide services digitally as well.

9.7 Trade Facilitation and Infrastructure

9.14. Significant developments have taken place in the areas of trade facilitation. Nepal has signed trade and transit agreements with its neighbouring countries. Nepal has also ratified the WTO TFA. Nepal's participation in such initiatives helps facilitate trade and investment. The improvements in trade related infrastructure provide Nepal opportunities to charter a path of high economic growth through trade and investment in the coming years.

9.15. As a landlocked developing country (LLDC), geographical constraints have significantly contributed to Nepal's under performance in trade, depriving Nepal from its rightful share in the global trading system. The Vienna Programme of Action would be instrumental in addressing this fundamental problem with a focus particularly on trade and transit facilitation, once implemented effectively. Similarly, it is very pertinent to intensify the implementation of the TFA agreement.

9.8 Aid for Trade

9.16. Aft is complementary initiatives that can help Nepal achieve its SDG goals by 2030. Nepal can only be benefited by Aft through a very effective and sustainable mechanism with an improved donors' coordination and national ownership. It is crucial that the support provided by Aft is harmonized along with the Government's vision and priorities. Aft needs to focus on development of trade related infrastructure. Nepal has been benefiting from the WTO/ Enhance Integrated Framework (EIF) and it expects continuous support for trade capacity building of the country.

9.9 E-Commerce

9.17. Nepal's success in expanding access to ICT to a large section of the population presents unparalleled opportunities for growth in the area of e-Commerce. E-Commerce can bring down traditional socio-cultural, economic and geographical barriers and help bringing Nepal closer to the world. In this way, e-Commerce, through its effective network, can help Nepal transform itself into a middle-income country and attain SDGs by 2030.

9.18. Increased investment in e-infrastructure is required to ensure wider geographic coverage. It is also imperative to develop and bring into use National Payment Gateway. The development of e-Commerce also needs to be facilitated by an effective delivery mechanism. Small and medium enterprises also need support to carry out e-Commerce by ensuring secure internet services and hence effective cyber-security guidelines need to be developed and implemented. Finally, a supportive legal framework, one that matches the pace and dynamism of e-Commerce development, is required.

10 CONCLUSION

10.1. Nepal has continuously fulfilled its international obligations and has been engaging actively in the WTO. It is committed to utilizing international trade to meet its sustainable development objectives. Since the last TPR in 2012, Nepali economy has undergone many challenges, not least the earthquakes in 2015 and the subsequent trade disruption. Nepal was heavily impacted in the immediate aftermath but has already shown significant recovery. With the promulgation of the Constitution in 2015 and the election of stable governments at all three levels: federal, provincial and local, Nepal has committed to structurally transforming its economy to make it production-focused, employment-generating, self-sufficient, and export-oriented. The various initiatives and reforms carried out during the review period add further avenues for achieving socio-economic development.
