Nepal Trade Brief

Trade Policy

In the 1990s, a series of market-oriented reforms—partly tied to the country's World Trade Organization (WTO) accession bid—opened up Nepal's economy to trade in goods and services, technology, and investment. Nepal's trade policy remains somewhat restrictive toward imports, as judged by the MFN Tariff Trade Restrictiveness Index (TTRI)[1] for overall trade of 16.4 percent, compared to the averages of 11.7 percent for the South Asia region and 11.6 percent for the low-income countries. Based on the MFN TTRI, Nepal ranks 121st out of 125 countries (where 1st is least restrictive). Agricultural goods have a significantly lower TTRI (11.3 percent) than non-agricultural goods (17.5 percent). The simple average of the MFN applied tariff rate has decreased slightly since 2005 to 12.5 percent. Nepal has not changed its maximum tariff of 80 percent on all goods (excluding alcohol and tobacco) in the past several years. The trade policy space, as measured by the wedge between bound and applied tariffs (the overhang), has remained consistent in the past several years, now standing at a relatively low 13.9 percent, compared with 54.8 percent on average for its regional neighbors and 50.9 percent for low-income countries. Regarding the extent of its commitment to trade liberalization in services, Nepal ranked 56th out of 148 countries on the GATS Commitment Index.

In response to rising food prices, Nepal instituted several export bans on food staples in April 2008, including rice, maize, and wheat.[2] In January 2009, the government lifted a ban on imports of milk products from China, put in place after samples of the milk were found to contain a toxic chemical.[3]

Unless otherwise indicated, all data are as of August 2009 and are drawn from the World Trade Indicators 2009/10 Database. The database, Country Trade Briefs and Trade-at-a-Glance Tables, are available at http://www.worldbank.org/wti.

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External Environment

Nepal's exports do not face very favorable treatment by its trading partners when compared with its regional neighbors. The Market Access TTRI[4] (including preferences) is 17.5 percent for all goods, with the level for agricultural products almost three times that of non-agricultural goods. This is considerably higher than the average for both the South Asia region and low-income countries, which are 7.6 and 5.6 percent, respectively. The simple average of the rest of the world tariff faced by Nepalese exports is 9.6 percent. When taking into account the volume of exports it is 3.0 percent, with the rate faced by agricultural goods and non-agricultural goods significantly different, at 13.1 and 2.7 percent, respectively. Nepal's Central Bank maintains a currency peg to the Indian rupee. Over the course of 2008 the Nepalese rupee depreciated by 5 percent against the U.S. dollar, making exports relatively less expensive.

Nepal is a member of the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC), a grouping of countries in the region which aim at creating a free trade area by 2017. In addition, Nepal belongs to the South Asian Free Trade Agreement (SAFTA), which came into effect in 2006 and is intended to be implemented by Nepal in 2015. This agreement between seven of the eight countries in the South Asia region (Afghanistan is not yet a member) is designed primarily to reduce tariffs on intraregional trade.

Behind the Border Constraints

In terms of the conduciveness of its institutional environment to business, Nepal ranked 123rd out of 183 countries in the 2010 Ease of Doing Business index. The Logistics Performance Index, a measure of the extent of trade facilitation, rates Nepal at 2.14 on a scale from 1 to 5 with 5 being the highest performance. It ranked 130th in the world and 6th in the South Asia region (with India leading the regional group). The area in which it performed the best was domestic logistics costs and its weakest performance was in the quality of transport and IT infrastructure for logistics. Nepal faces transportation challenges for

manufactured goods because of the fact that it is landlocked and most of its goods must travel through India.[5]

Trade Outcomes

Slow rates of growth in total trade since 2004 continued for Nepal in 2008, when total trade grew by only an estimated 4.2 percent in real (constant 2000 U.S. dollars) terms. Real export growth rose to an estimated 5 percent, while imports grew by an estimated 3.5 percent. Expectations are that exports and imports will continue to grow in 2009 by 1 and 3 percent, respectively.

In nominal U.S. dollar terms, total trade grew by an estimated 20 percent in 2008, which was a slight increase over the 11 percent in 2007. With more than 65 percent of its exports sent to neighboring India in 2008, the performance of the economy of Nepal is contingent on how the economic downturn affects India. With peace, total exports increased by an estimated 8.2 percent in 2008 compared to 1.2 percent in 2007. Remittance-led consumption increased imports from India by 33.3 percent, and this growth trend is expected to continue. There was less than 1 percent growth in exports to India, but exports to other nations have grown after a dip in 2007. The poor performance in exports to India was driven in large part by the decrease in vegetable oil, textiles, chemicals, and readymade garments exports, affected by the appreciation of the currency. Exports to countries other than India increased by 27 percent mostly due to re-exports of pulses.[6] Readymade garments and woolen carpets, the top two exports in 2007, have declined in recent years. Nepal has been adversely affected by the liberalization of global quotas in 2005, according to the WTO's Agreement of Textiles and Clothing (ATC). Competing more directly with other garment exporters in its region has been difficult since Nepal must import raw materials and pay high transport costs. Total imports grew by an estimated 23.6 percent in 2008, due to rising commodity prices and remittance-led demand.[7] Nepal is dependent on oil imports, which make up the largest share of imports. Total remittances are important for Nepal and were 21.7 percent of GDP in 2008 (all in U.S. dollar terms). In spite of the global recession, remittances actually increase in 2008, from 16.7 percent of GDP in 2007.

Notes

1. TTRI calculates the equivalent uniform tariff that would keep domestic welfare constant. It is weighted by import shares and import demand elasticity.
2. FAO, 2009.
3. ESCAP, 2009, p. 4.
4. MA-TTRI calculates the equivalent uniform tariff of trading partners that would keep their level of imports constant. It is weighted by import values and import demand elasticities of trading partners.
5. EIU, 2009, p. 20.
6. NRB, April 2009.
7. NRB, April 2009.

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