Freedom to Trade Internationally: Nepal Country Audit

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1. Introduction

The 'Freedom to Trade Internationally' component in the Economic Freedom Index[1], prepared by the Fraser Institute, primarily measures a country's openness to trade. It arrives at the final score by analyzing a country's tariffs, regulatory trade barriers, black market exchange rates, and controls of the movement of capital and people. Each category is further divided into sub-categories, and on a scale of 1 to 10.

The Economic Freedom Index 2024 ranks Nepal 132nd globally with a score of 6. Nepal's score places it in the fourth quartile, which suggests significant trade restrictiveness and higher costs of exporting and importing. The section that follows present an analysis of Nepal's performance and identifies explanatory factors for the score. All sub-categories of the "Freedom to Trade Internationally" except the back-market exchange rate are discussed in detail. Nepal scores a perfect ten in the black-market exchange rate category because it has adopted a full current account convertibility regime. As a result, this aspect is not discussed here.

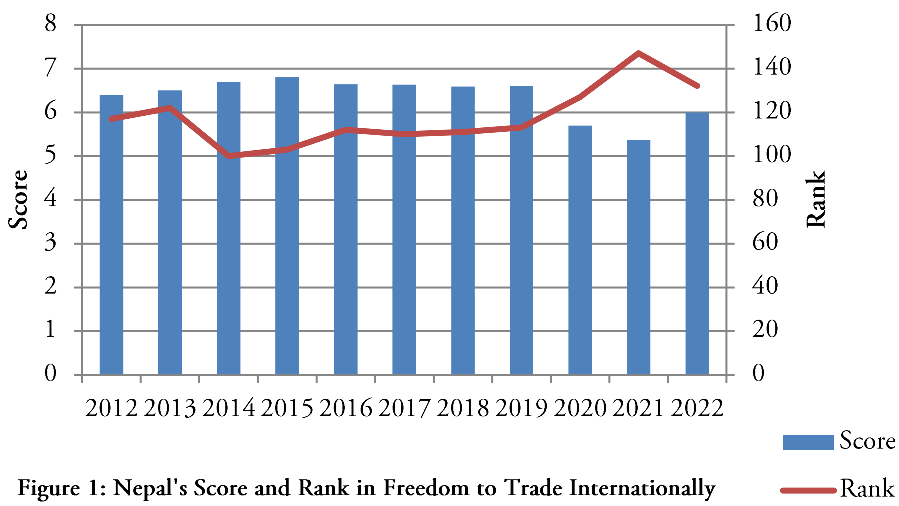

Figure 1: Nepal's Score and Rank in Freedom to Trade Internationally
Source: World Economic Freedom Report (2014-2024)

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[1] Overall, the Economic Freedom Index (EFI) evaluates a country's policies and institutions to determine whether they promote or hinder economic freedom across five broader areas: Size of Government, Legal System and Property Rights, Sound Money, Freedom to Trade Internationally, and Regulation.

2. Tariffs

The tariff sub-component measures the extent to which a country relies on taxation of trade. The sub-component score is derived from three indicators, i.e. revenue from trade taxes, mean tariff rates, and the standard deviation of tariff rates. Countries with lower revenue from trade taxes, tariff rates, and standard deviation receive higher scores, indicating greater freedom to trade internationally. As shown in Figure 2, Nepal's overall score has declined over the years, primarily due to its dependence on taxation-based revenue.

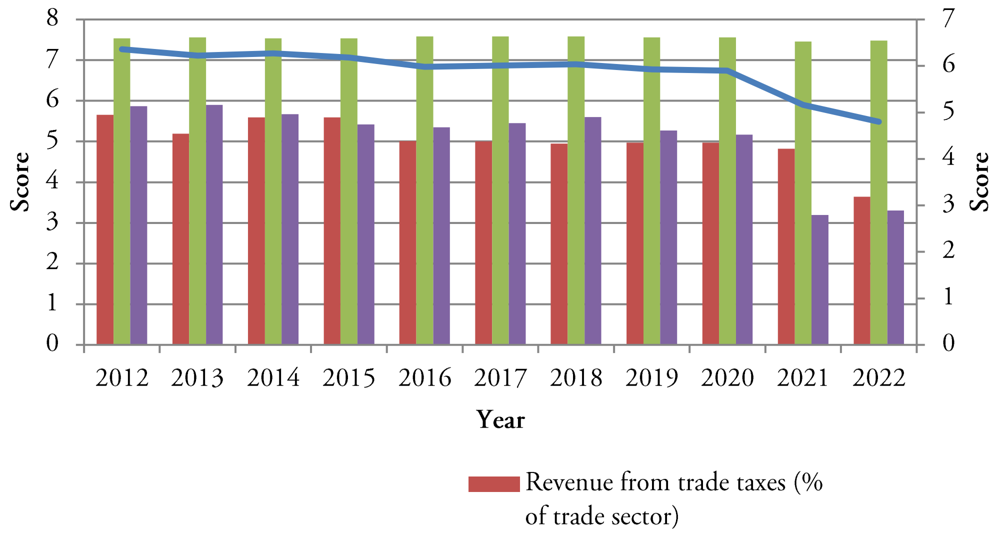

Figure 2: Nepal's Score on Sub-component Tariffs
Source: Economic Freedom of the World Report (2014-2024)

Whereas comparator countries such as India, Lao PDR, and Bangladesh have witnessed a reduction in their dependence on import taxes, Nepal has followed a different trajectory i.e. one of heavy taxation of imports (See Figures 3 and 4). Between 2012 and 2022, taxes on international trade as a share of total revenue increased by 5 percentage points. In FY 2023/24, import-based taxes contributed to 46.1 percent of total tax revenue, which includes excise duty and Value Added Tax (VAT) on imports (source: Economic Survey 2023/24, MoF)[2].

Custom duties in Nepal vary from 0 to 80%, with rates of 1%, 5%, 10%, 15%, 20%, 30%, 40%, 60%, and 70% in between, making a total of eleven tariff bands[3]. Tariff bands of 40%, 60%, and 70% are the most recent addition. Prior to FY 2018/19, there were only seven tariff bands, the

[2] The data is based on the Financial Comptroller General Office statistics from 2080 B.S. (2023 A.D.) and accounts data up to the month of Falgun.

[3] High-Level Tax Reform Committee. "Report of the High-Level Tax Reform Committee". (Kathmandu: 2023),

introduction of 1% band in FY 2018/19 [4] brought the number to eight and subsequent increases since then has increased the bands to 11.

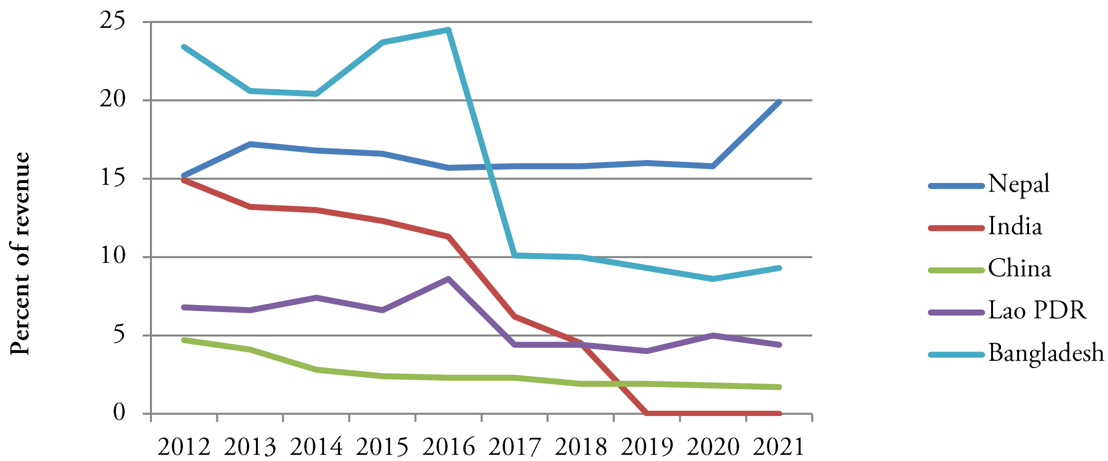

Figure 3: Taxes on International Trade (% of reveneue)
Source: World Development Indicators

Custom duties in Nepal vary from 0 to 80%, with rates of 1%, 5%, 10%, 15%, 20%, 30%, 40%, 60%, and 70% in between, making a total of eleven tariff bands[5]. Tariff bands of 40%, 60%, and 70% are the most recent addition. Prior to FY 2018/19, there were only seven tariff bands, the introduction of 1% band in FY 2018/19 [6] brought the number to eight and subsequent increases since then has increased the bands to 11.

[4] WTO Secretariat, 2018, "Trade Policy Review", (Geneva: WTO), https://www.wto.org/english/tratop_e/tpr_e/tp481_e.htm
[5] High-Level Tax Reform Committee. "Report of the High-Level Tax Reform Committee". (Kathmandu: 2023),
[6] WTO Secretariat, 2018, "Trade Policy Review", (Geneva: WTO), https://www.wto.org/english/tratop_e/tpr_e/tp481_e.htm

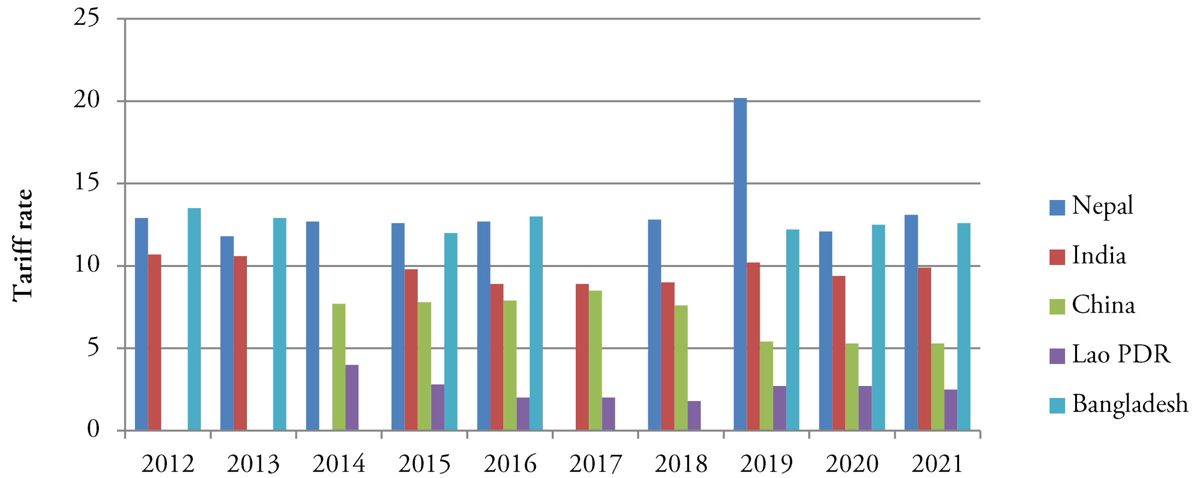

Figure 4: Cross-country Comparison of Tariff rates
Source : World Development Indicators

On paper, Nepal has a protectionist trade regime, evidenced by the number of tariff bands and an increase in duties applied to tariff lines. Specific duties are now applied to 113 tariff lines, compared to 51 tariff lines in 2018/19. Additional taxes and charges are also levied on imports such as customs service fees, agriculture service fees, and road construction fees, among others. These para-tariffs are either calculated as a percentage of the customs value or assigned as flat fees per shipment, which are updated regularly via the Finance Act.

Heavy taxation on imports usually stems from protectionist policies to protect domestic industries; however, this is not entirely the case in Nepal. Despite Nepal not having a domestic car manufacturing industry, motor vehicles are subject to a high tariff band of 80%. While electric vehicles are taxed relatively lower, the total taxes levied on petroleum cars can reach up to 288%[7]. The rationale for heavy taxation on imports is rather the generation of revenue evidenced by the fact that nearly 20 percent of the total revenue of the Government of Nepal is reliant on import taxation. Nepal's taxation-based revenue stems from the fact that its economy is driven by remittance-fueled consumption patterns. However, it also highlights Nepal's failure to realize its true potential in terms of export performance and revenue diversification. Moreover, the top three imports of Nepal—diesel,

[7] Dr. Biswas Gauchan,Dilasha Joshi, Yajju Pradhan, Sudikchya Rai, Bibhuti Thapa, 2024, "Policy Brief on: Re-evaluating Fiscal Incentives on Electric Vehicles." *IIDS* (Kathmandu: IIDS), https://iids.org.np/publications/details/reports/iids_policy_brief_on_re_evaluating_fiscal_incentives_on_electric_vehicles?id=304.

petrol, and LPG—are now subject to an extra green tax as per the budget 2024/25[8]. While the stated goal is to discourage the use of petroleum and coal products to fulfill its international commitment of reducing its carbon emissions, the policy appears contradictory, insofar as fiscal policy also increased the customs duty and excise duty of electronic vehicles, resulting in a higher duty and price for such vehicles[9].

At the same time, the export strategy is influenced by tariff loopholes. For instance, soybean oil has been reported as the top export product, with exports soaring to Rs. 18.91 billion in the first six months of the current fiscal year[10]. However, this increased export is the result of preferential trade agreements. Under the South Asian Free Trade Area and the Nepal-India Trade Treaty, exports from Nepal receive preferential treatment, making them cheaper for India. While this has led to a short-term export surge, it does not sustain trade in the long run. Meanwhile, the products identified with high export potential in Nepal Trade Integration Strategy (NTIS) show minimal growth of 3.75 percent[11]. Nepal's share in global export as per latest data in 2023 remains at 0.01%, which is consistent with its historical average from 1990 to 2023 (source: The Global Economy), and the export scenario over the years shows a dire picture of Nepal's exports compared to imports (See Figure 5).

Nepal has not been able to capitalize on many preferential arrangements and benefits it has been receiving so far. For example, under the Nepal Trade Preference Program (NTPP), Nepal received duty-free access to the US market for 77 products in December 2016. However, a SAWTEE study found no particular evidence that the NTPP increased exports of these products. In fact, their share in total US exports declined from 14 percent in 2012 to 7.8 percent in 2021, showing a downward trend.[12] The low-level firm competitiveness in the domestic market explains Nepal's export performance.

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8 Krishana Prasain, 2024, "Budget introduces green tax on petroleum products", *The Kathmandu Post*, May 29, https://kathmandupost.com/money/2024/05/29/budget-introduces-green-tax-on-petroleum-products.

9 Republica, 2024, "EVs' Prices Likely to go up by at Least 10 Percent With Revised Tax Rates in Budget For FY 2024/25," May 30, https://myrepublica.nagariknetwork.com/news/evs-prices-likely-to-go-up-by-at-least-10-percent-with-revised-tax-rates-in-budget-for-fy-2024-25.

10 Krishana Prasain, 2025, "An astronomical jump in Nepal's soyabean oil exports baffles experts." *The Kathmandu Post*, February 6. https://kathmandupost.com/money/2025/02/06/an-astronomical-jump-in-nepal-s-soyabean-oil-exports-baffles-experts.

11 *The Kathmandu Post*. 2025. "Nepal's Exports Surge 46.5 Percent, but High-value Goods Show Minimal Growth," March 10, 2025. https://kathmandupost.com/money/2025/03/10/nepal-s-exports-surge-46-5-percent-but-high-value-goods-show-minimal-growth.

12 Kharel, Paras and South Asia Watch on Trade, Economics and Environment. 2023. "The 66/77 Products Inside Out: The Long and Short of the United States' Nepal Trade Preference Programme." Working Paper. *SAWTEE Working Paper Series*. SAWTEE. https://www.sawtee.org/publications/WP23_Nepal-US_trade_PKharel_WP.pdf.

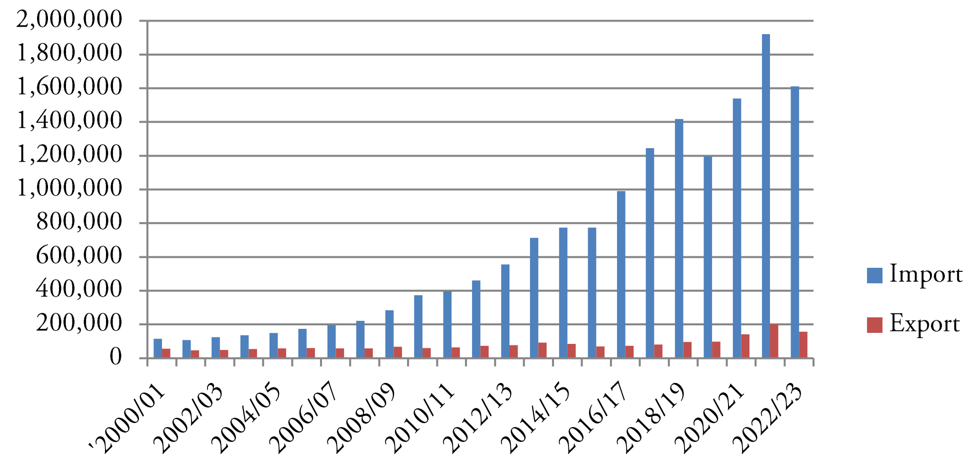

Figure 5: Nepal's Export Import in million RS
Source: Nepal Rastra Bank

Given the high costs of importing raw materials in Nepal, firm-level competitiveness is low. Imports are not just limited to finished or luxury goods. They also include essential input for value-added exports. However, the incentives tied to revenue targets for each customs office often prioritize tax collection on imports[13], and the revenue concerns at the Ministry of Finance (MoF) halt the facilitation of such goods in the country. For instance, in the case of export of Nepali tea, National Tea Policy (2000) had introduced provisions to promote auxiliary industries by levying minimum custom duty on the import of machineries for tea packaging industry, and duty drawback schemes for packaging materials[14]. However, studies have reported poor implementation of such provisions due to lack of coordination among institutions particularly the Ministry of Industry, Commerce and Supplies (MoICS), and Ministry of Finance (MoF). Such incentives are granted through the Industrial Enterprise Act under the MoICS but MoF oversees tax exemptions and duty drawbacks through legislations like Finance Act, Income Tax Act[15]. Another example is the government's restriction on the import, sale, distribution, and use of plastic materials below 40 microns[16]. This contributes to challenges in packaging and branding of Nepali products. For instance, exporters of dog chews – a fast-growing export product in recent years, have mentioned that their products are usually reprocessed

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[13] South Asia Watch on Trade, Economics and Environment (SAWTEE), 2017, "Trade and Transport Facilitation Audit: Nepal Country Report", (Kathmandu: SAWTEE), https://www.sawtee.org/Research_Reports/5_Trade-Facilitation-in-South-Asia_Nepal_fin.pdf.

[14] GIZ, 2012, "NEPALTRADE," May. https://enhancedif.org/system/files/uploads/nepal-trade-issue-3-english.pdf.

[15] Paras Kharel and Kshitiz Dahal, 2021, "Trade Policy Coherence and Coordination in Nepal: An Exploratory Assessment," *Trade and Competitiveness Assessment Volume I*, https://sawtee.org/publications/Trade-Policy-Coherence-and-Coordination-in-Nepal.pdf.

[16] Government of Nepal, 2021, "Nepal Gazette, Part 5, Number 21," Kathmandu: Ministry of Law, Justice and Parliamentary Affairs. http://rajpatra.dop.gov.np/welcome/book/?ref=24714

and packaged in the US before being distributed.[17] Such factors are responsible for reducing domestic firms' competitiveness which eventually results in low export performance.

High logistics costs in Nepal also significantly reduce firm-level competitiveness. In Nepal, traders bear logistic expenses amounting to 32 percent of the actual cost of goods, which covers transport, transit, delivery, storage, and official procedures. This significantly undermines competitiveness in the international market[18]. While Nepal's estimated logistic cost ranges between 14-25 percent of GDP[19], India's logistic costs are estimated between 14-18 percent, and the country is planning to bring this percentage down to 9 percent[20]. So far, Nepal has not made any concrete plans to reduce logistics costs. Absent concrete strategies to increase firm-level competitiveness, Nepal's revenue strategy is likely going to remain reliant on heavy taxation on imports.

Box 1: Round table Discussion Highlight (March 31, 2025)

The round table discussion raised concerns over the high logistic cost faced by Nepalese traders, where one of the consultants highlighted the difference between domestic supply side and cross-border export cost, emphasizing the burden borne by traders beyond the borders.

Factors	Within Nepal	Beyond border
Time	20 days	80 days
Cost	15%	85%
Procedural Compliance	40%	60%
Documents Compliance	55%	45%

[17] Based on consultation meeting held on March 31, 2025

[18] Republica, 2022, "Nepali Traders Face Additional Cost of up to 32 Percent Due to Poor Logistic Facility," December 26. https://myrepublica.nagariknetwork.com/news/nepali-traders-face-additional-cost-of-up-to-32-percent-due-to-poor-logistic-facility.

[19] Estimates of logistic cost as percentage of GDP vary depending on the methodology. This estimate is based on the heuristic benchmark, which sets the logistic cost of countries with efficient infrastructure at 8 percent of GDP, placing Nepal's logistic cost anywhere between USD 4 to 7.7 billion (14 to 25 percent of GDP).

Raskin Maharjan, 2021, "The Logistics-Tech Landscape in Nepal," December 7, 2021.

https://www.linkedin.com/pulse/logistics-tech-landscape-nepal-raskin-maharjan/.

[20] The Hindu, 2024, "Nitin Gadkari Says India's Logistics Cost Will Come Down to Single-digit Percentage in Two Years," October 17. https://www.thehindu.com/business/Economy/indias-logistics-cost-will-come-down-to-single-digit-percentage-in-two-years-gadkari/article68764060.ece.

Risk	30%	70%

3. **Regulatory Barriers**

Nepal performs relatively better in the regulatory barriers category. The index relies on two measures, i.e. non-tariff barriers and compliance cost of exporting and importing. Particularly, Nepal scores highest in the compliance cost of importing and exporting sub-category suggesting relatively lower compliance costs (See Figure 6). This ranking is based on the World Bank's Doing Business data, which measures time and cost associated with border compliance for importing and exporting.

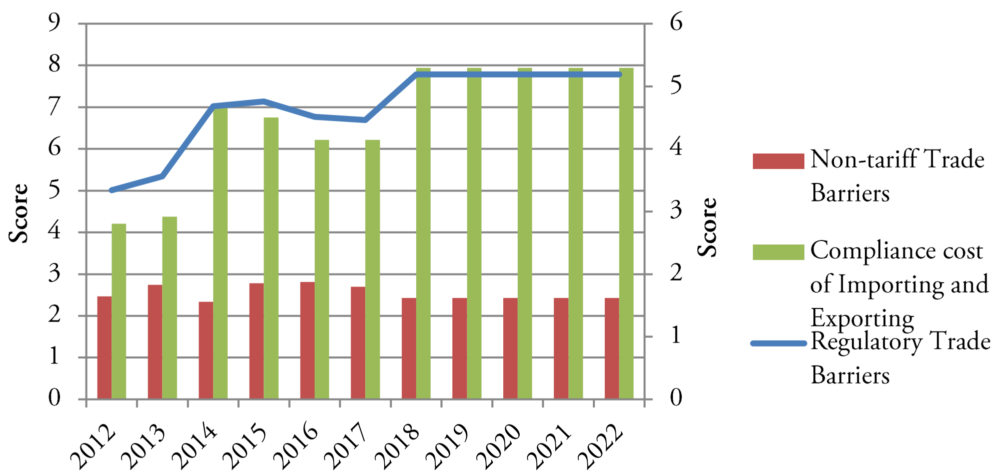

Figure 6: Nepal's Score on Regulatory Barriers Sub-Component
Source: Economic Freedom of the World Report (2014-2024)

Against the South Asian average, export compliance takes less time in Nepal. Export compliance time is less by 46.7 hours, resulting in an overall compliance cost of USD 103 compared to the South Asian average of 301.1. Across all indicators i.e. documentary compliance, import border compliance, Nepal performs better. The most recent round of Enterprise Survey reinforced this, admittedly Nepal performs better amongst other countries in South Asia and even amongst low income countries[21].

[21] World Bank, 2023, "Enterprise Survey: Nepal 2023 Country Profile," (Washington DC: World Bank), https://www.enterprisesurveys.org/content/dam/enterprisesurveys/documents/country/Nepal-2023.pdf.

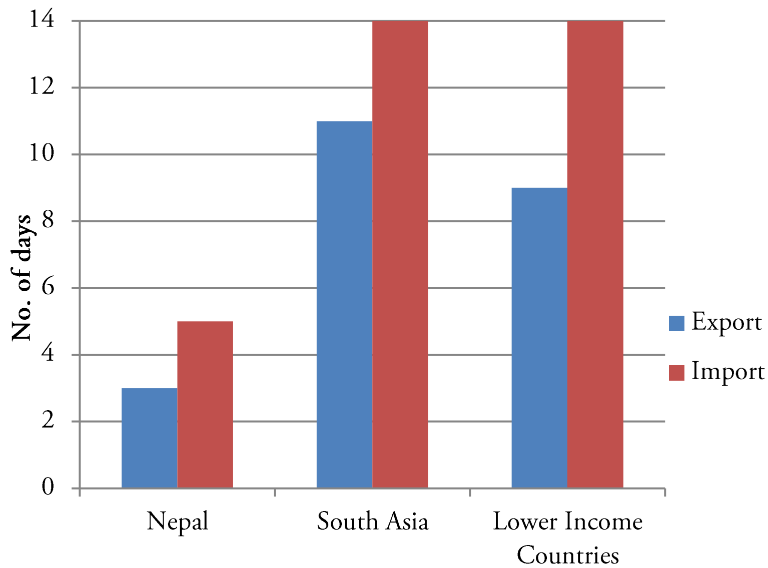

Figure 7: Average days to clear Exports and Imports
Source: Enterprise Survey, 2023

Table 1: Time and Cost of Export and Imports

Compliance Type	Nepal		South Asia	
	Time in hours	Cost in USD	Time in hours	Cost in USD
Export - Border Compliance	11	103	58.7	301.1
Export - Documentary Compliance	43	110	73.3	190.2
Import - Border Compliance	11	190	63.9	546
Import - Documentary Compliance	48	80	93.9	251.1

Meanwhile, Nepal scores lowest in the sub-category non-tariff barrier. This sub-category includes both tariff and non-tariff barriers based on the Global Competitiveness Report's perception index. The index measures public opinion on whether tariff and non-tariff barriers significantly restrict trade in the country. The Business Ready Report 2024 highlights that 74 percent of respondents perceive customs and trade regulations as constraints, which emphasizes the challenges particularly at the procedural, regulatory, and structural level[22] .

Complex documentation processes, the need for multiple certifications, and lengthy approval processes significantly increase compliance costs. The ITC (International Trade Centre) survey reports that around 51% of exporters encounter problematic NTMs, with the agriculture sector being particularly affected[23]. Testing and certification by other government agencies (OGAs) contribute to delays at customs. On average, these agencies, which include quarantine facilities and laboratories, take 19 hours and 46 minutes, accounting for 20 percent of the total clearance time[24]. Given that the facilities are located outside the customs area and because of the absence of a single window system for the OGA services, the time taken for testing samples and issuance of certificates is significant. Additionally, exporters often have to rely on Indian Labs to get approval from the Bureau of Indian Standards. The problems at the procedural level are largely due to Nepal's poor quality of national infrastructure.

While there has been some notable progress in trade-related infrastructure the quality of such infrastructure remains a concern. For instance, integration of ASYCUDA in 28 custom offices **(source: Department of Customs)**,construction of dry ports, integrated check posts, are some notable improvements. However, the full range of accreditation parameters required for a complete internationally accepted certification is missing, especially in government laboratories run by the Department of Food Technology and Quality Control (DFTQC) and National Bureau of Standard and Metrology (NBSM)[25]. As a result, traders rely on laboratories across the borders, increasing the cost of export and causing delays.

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22 World Bank, 2024, "Business Ready Report", (Washington DC: World Bank), https://www.worldbank.org/en/businessready

23 Paras Kharel, Kshitiz Dahal, and Nyingtob Pema Norbu, 2024, "NTMs in Nepal: Existing and New Issues in the Wake of LDC Graduation," *ESCAP Working Paper*, July 2024, https://www.unescap.org/sites/default/d8files/event-documents/ESCAP-2024-WP-NTMs-Nepal_0.pdf.

24 Paras Kharel and Kshitiz Dahal, 2021, "Trade Policy Coherence and Coordination in Nepal: An Exploratory Assessment," *Trade and Competitiveness Assessment Volume I*, https://sawtee.org/publications/Trade-Policy-Coherence-and-Coordination-in-Nepal.pdf.

25 Paras Kharel, Kshitiz Dahal, and Nyingtob Pema Norbu, 2024, "NTMs in Nepal: Existing and New Issues in the Wake of LDC Graduation," *ESCAP Working Paper*, July 2024, https://www.unescap.org/sites/default/d8files/event-documents/ESCAP-2024-WP-NTMs-Nepal_0.pdf.

Similarly, issues in the design of Inland Clearance Depots and Integrated Check Posts — inadequate size and poor layout to cater to import export volumes — hinder the smooth flow of cargo and are incompatible with the standard custom process[26]. None of the dry ports in Nepal has been recognized by the World Maritime Organization (WMO), which hinders the operation of dry ports in a full-fledged manner[27]. The immediate consequence of this is that Nepalese traders cannot issue the bill of lading at ports, forcing them to separately arrange for land transportation. Transportation infrastructure remains another significant barrier, as highlighted by SAWTEE's trade facilitation audit[28].

Freight Forwarders are exposed to significant risks given absence of clear policies. International commercial terms (INCOTERMS) defined by the International Chambers of Commerce (ICC) lay out the responsibilities and liabilities in cross-border trade. The terms are recognized poorly in Nepal's trading practices. For instance, goods in Nepal are transferred under the widely used Cost, Insurance and Freight (CIF) term. This implies that the seller is responsible for contracting and paying for freight and the insurance until the goods are boarded for destination[29]. A bill of lading serves as proof that the seller has successfully transferred its liability to the shipping company. But given the lack of recognition of Nepalese dry ports because of their poor quality[30], traders in Nepal are unable to issue a bill of lading. This deprives freight forwarders of their rights to transfer cost, risk, title, and ownership of goods, thereby exposing them to risk. In the absence of clear liability transfer laws or provisions for multimodal insurance, Nepali traders are placed in a weaker position[31].

The regulatory framework, particularly the Multimodal Transportation of Goods Act (2006), also fails to acknowledge the difference in point of liability between freight forwarders and multimodal

[26] Paras Kharel and Kshitiz Dahal, 2021, "Trade Policy Coherence and Coordination in Nepal: An Exploratory Assessment," *Trade and Competitiveness Assessment Volume I*, https://sawtee.org/publications/Trade-Policy-Coherence-and-Coordination-in-Nepal.pdf.

[27] South Asia Watch on Trade, Economics and Environment (SAWTEE), 2017, "Trade and Transport Facilitation Audit: Nepal Country Report", (Kathmandu: SAWTEE), https://www.sawtee.org/Research_Reports/5_Trade-Facilitation-in-South-Asia_Nepal_fin.pdf.

[28] South Asia Watch on Trade, Economics and Environment (SAWTEE), 2017, "Trade and Transport Facilitation Audit: Nepal Country Report", (Kathmandu: SAWTEE), https://www.sawtee.org/Research_Reports/5_Trade-Facilitation-in-South-Asia_Nepal_fin.pdf.

[29] Ben Thompson, 2025, "Incoterms Guide [Updated 2025] With Free PDF Download," *IncoDocs*, January 17, 2025. https://incodocs.com/blog/incoterms-2020-explained-the-complete-guide/.

[30] Rajan Sharma, 2025, "Supply Chain Risk and Mitigation for Landlocked Nepal," *Republica,* February 6. https://myrepublica.nagariknetwork.com/news/supply-chain-risk-and-mitigation-for-landlocked-nepal-82-82.html#:~:text=Supply%20Chain%20Risks%20in%20Nepal&text=Forgery%20and%20Fraud%3A%20Forged%20certificates,legitimate%20shipments%20are%20common%20risks.

[31] Rajan Sharma, 2023, "Controlling Supply Chain Fraud | the Annapurna Express," *The Annapurna Express*, April 13. https://theannapurnaexpress.com/story/40877/.

transport operators[32]. According to the act, multimodal transport operators are held responsible for the goods throughout the route until received at the destination. They are liable for any damages incurred during the transit and are required to obtain insurance. In line with global practices, they usually opt for TT club – an international transport and logistics insurance provider – to deal with cross-border logistic processes. However, the Insurance Act (2022) complicates compliance with multimodal insurance. The act states that any insurance-related transaction must be carried out through companies that have obtained a license under the act[33], making it difficult for freight forwarders to comply with trading norms.

Nepali traders frequently encounter demurrage charges and detention of the consignment. A key reason for this problem is the absence of Nepal based shipping companies and agents at transit points, which disrupt the timely flow information. For example, minor shortfalls in documents and payments may not be communicated in time for verification, resulting in costly delays[34]. Additionally, the custodian rights of Nepali goods are in the hands of Indian clearing agents, who are empowered by Indian traders and their respective banks[35]. Such arrangements put Nepali traders in a vulnerable position, contributing to the risk of doing business. Also, when coupled with absence of the right INCOTERMS, this creates uncertain trading practices and manipulation such as, forgery of documents, smuggling, and price distortion. In extreme cases, the goods valued at $7000 are subject to distortion at various points, ultimately reaching the Nepali market at an inflated price close to $100,000[36]

Efforts to connect Nepal with its neighbours and the rest of the world through projects like Asian Highway Network and Trans-Asian Railway Network have not yielded anticipated results. In addition, cost and scope analyses of Belt and Road Initiative also offer limited optimism[37]. Moreover, in efforts to diversify its transit routes for third country trade, Nepal signed a Trade and Transit Agreement with China in 2016, which provided access to four Chinese seaports, along with three land ports[38]. However, none of them are operational. So far, only one container of noodles has been

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[32] While freight forwarders may act as Multimodal Transport Operators if registered, they are not essentially the same. Freight forwarders are responsible for coordinating the logistics chain and are not liable for the goods unless they assume the role of a carrier.

[33] See Section 24 of the Insurance Act 2022. The provision requires a license to be issued by the National Insurance Authority, established under this Act.

[34] Based on roundtable discussion held on March 31, 2025

[35] Rajan Sharma, 2023, "Controlling Supply Chain Fraud | the Annapurna Express," *The Annapurna Express*, April 13. https://theannapurnaexpress.com/story/40877/.

[36] Based on roundtable discussion held on March 31, 2025

[37] Based on round table discussion held on March 31, 2025

[38] Rajan Sharma, 2023, "The Way Forward in Nepal-China Trade," *The HRM Nepal,* October 27. https://thehrmnepal.com/opinion/the-way-forward-in-nepal-china-trade/.

exported to Japan[39], and one container of turmeric has been imported from Vietnam[40] via this trade route.

The prospect of using Chinese trade routes as an alternate transit option remains impossible given Nepal's geographical proximity to India. For instance, the shortest third-country transit point via India, Haldiya port, is approx. 700 km away, while the farthest Vishakhapatnam, is about 1700 km away. In contrast, the shortest Chinese transit point is over 3,500 km away. Chinese transit routes can serve as an additional option that too only after being effectively utilized. Participants of the consultative meeting, undertaken to inform this audit collectively noted that the China Transit Treaty exists primarily because of China's strategic interest. One of the key bargaining points in return for access to Chinese ports was China gaining access to the Birgunj-Kakarbhitta route, which would connect them with India and Bangladesh. However, Nepal restricts the export of transit and thus has missed the opportunity to leverage China's interest. So far, access to Chinese transit points has served as a negotiation tool against India, without substantial benefit. However, this does not mean the negotiation with the southern neighbour comes without any challenges. For instance, India's refusal to allow open wagons to cross the border has also negatively affected the use of the railway line. The refusal for open wagons stands against the provisions in the Treaty of Transit between Nepal and India[41]. Nepal's limited capacity to translate agreements reflects a broader issue of weak diplomatic performance. If Nepal is to benefit from its geographical positioning then it must adopt a more assertive diplomatic strategy.

4. Controls on the movement of Capital and People

Trade is not only linked with the movement of goods but also with movement of capital and people. Composed of four indicators – financial openness, capital controls, freedom of foreigners to visit, and protection of foreign assets – this sub-component measures how open a country is to cross-border financial flows and movement of people for business and tourism purposes.

[39] Dilip Paudel, 2024, "Nepali Products Reach Japan for the First Time via China Trade Route," *Republica,* January 29. https://myrepublica.nagariknetwork.com/news/nepali-products-reach-japan-for-the-first-time-via-china-trade-route.

[40] Republica, 2023, "Nepal Imports Goods From Third Country Through Chinese Ports After Seven Years of Transit Agreement," September 9. https://myrepublica.nagariknetwork.com/news/nepal-imports-goods-from-third-country-through-chinese-ports-after-seven-years-of-transit-agreement

[41] South Asia Watch on Trade, Economics and Environment (SAWTEE), 2017, "Trade and Transport Facilitation Audit: Nepal Country Report", (Kathmandu: SAWTEE), https://www.sawtee.org/Research_Reports/5_Trade-Facilitation-in-South-Asia_Nepal_fin.pdf.

Nepal has scored zero in the indicator Capital Controls throughout the years due to restrictions placed by Nepal Rastra Bank (NRB). In contrast, it has scored a perfect ten in the indicator freedom of foreigners to visit in most years. However, this score dropped in years 2020 and 2021 due to COVID, which significantly affected the aggregate score for this sub-component. Overall, the stagnant performance suggests lack of meaningful efforts in creating a conducive environment that supports financial openness and protects investments over the past decade (See Figure 8).

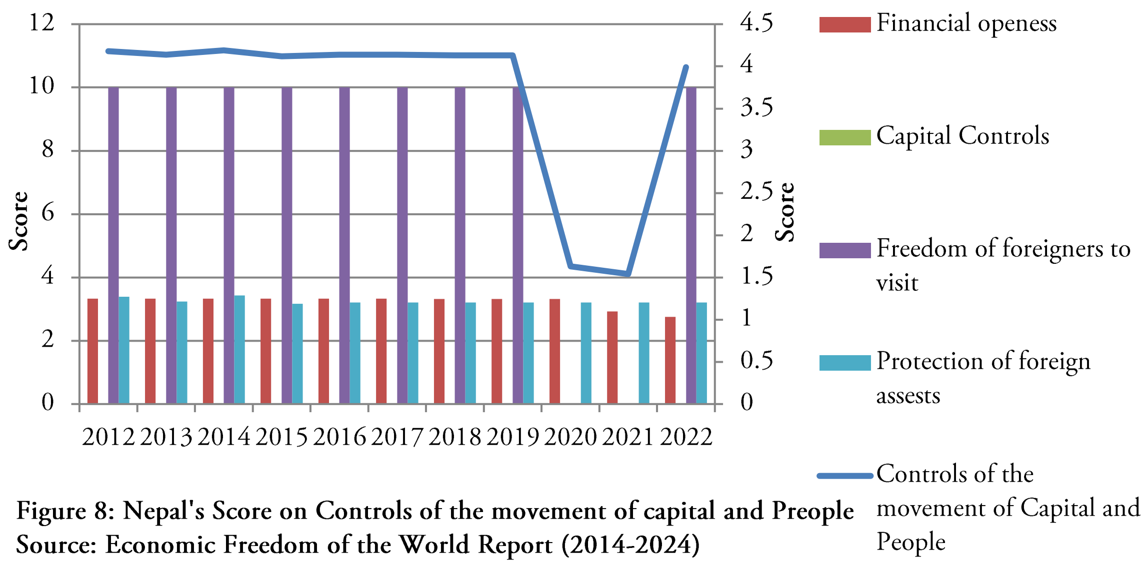

Figure 8: Nepal's Score on Controls of the movement of capital and Preople
Source: Economic Freedom of the World Report (2014-2024)

Nepal has a history of capital controls, but the government has taken some steps to ease restrictions in recent years. Since the 1960s, Nepal has had in place legislations—Act Restricting Investment Abroad (ARIA) and Foreign Exchange Regulation Act—that control outward investments. ARIA 1964 prohibits investments in foreign securities and foreign firms unless authorized by the Government of Nepal. Whereas FERA 2019 authorizes NRB to regulate foreign exchange transactions along with granting approvals for businesses and individuals wishing to invest abroad or open bank accounts abroad.[42] NRB permitted exporting firms to open their branches or showrooms in foreign countries in 2016 But with a condition that exporters of goods and services must have a proper plan for at least three years to come, and they could only spend 5% of their total foreign exchange earnings annually at their foreign outposts. Later, this provision was reinforced through budget 2023/24

[42] Business 360, 2024, "Unveiling Outward Investment: A Nepali Law Perspective," *B360 :: Business 360°*, September 27, https://www.b360nepal.com/detail/23525/unveiling-outward-investment-a-nepali-law-perspective-2024-Sep-27-637000.

increasing the expense limit to 10%, but it remained unclear whether this applied only to IT companies[43]. Such ambiguity can hardly yield substantial results, even if reforms are in place.

Moreover, the government has also made other changes that have eased restrictions on movement of capital. Most recently, the government amended a few legislations through ordinance. The most notable amendment concerning foreign outbound investment is in FERA (2019), under Section 10A(2)[44]. According to the amendment, specially exempted industries under ARIA 1964 and IT industries are now allowed to invest abroad so that they can compete with foreign markets and generate foreign currency for Nepal. Similarly, earnings from foreign employment can be invested abroad.

To encourage inbound foreign investment, approval process for venture capital and Specialised investment funds has been streamlined. Before the amendment, the repatriation of funds from SIFs, was subject to approval from Nepal Rastra Bank and recommendation from the Department of Industries. This has been discarded with the addition of Section 20 (2) and 20 (6A) in FITTA, and now foreign investors only need SEBON's approval[45]. Likewise, access to loans from foreign financial institutions is now possible after approval from the NRB.

5. Recommendations

It is important to prioritize policies that stress on ease of doing business and enhance firm level competitiveness of such industries. Excessive tariffs and para-tariffs, even on raw materials, as well as high transportation and logistic costs, are responsible for weakening firm-level competitiveness. Nepal Trade Integration Strategy (NTIS) also seems to focus on sector competitiveness, often overlooking strategies to strengthen firms themselves. Moving forward, the goal should be realign Nepal's tariff regime based on competitive advantage.

Greater emphasis must be placed on improving inter-ministerial coordination. NTIS as a document, appears comprehensive, but its execution depends on the coordination between and within ministries. In practice, there appears to be a gap between the multilateral and bilateral trade divisions

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[43] Dikshya Singh, 2023, "Is It Time to Consider Opening Outward FDI?," *Trade, Climate Change and Development Monitor* 20 no. 5, May, https://sawtee.org/opinion-in-lead/is-it-time-to-consider-opening-outward-fdi.html
[44] Sariman Shakya, 2025, "What Does the New Ordinance on the Economy and Investment Entail? | Farsight Nepal," *Farsight*, January 30, https://farsightnepal.com/news/330.
[45] Vidhi Legal Concern, 2025, "Amendments Made to Foreign Investment and Technology Transfer Act 2019 by Ordinance to Amend Some Nepal Acts Relating to Improving Economic and Business Environment and Investment Promotion 2025,"
https://vidhilegal.com/amendments-made-to-foreign-investment-and-technology-transfer-act-2019-by-ordinance-to-amend-some-nepal-acts-relating-to-improving-economic-and-business-environment-and-investment-promotion-2025/

within the MoICS, which hinder the smooth execution. Since many challenges are also tied to logistics, it requires strong coordination with the Ministry of Physical Infrastructure and Transport (MoPIT).

Recognizing Freight forwarders as distinct entities separate from Multimodal transport operators is important. Since freight forwarders can manage the entire end-to-end supply chain, their contribution is crucial in revenue maximization (estimated at NPR 14 billion). Therefore, it is crucial to formally recognize freight forwarders as distinct entities. Formal recognition of Incoterms in trading practices, especially by financial institutions, could further support trade facilitation by clarifying responsibilities and reducing disputes in international transactions.

Nepal could benefit from recognizing private labs for testing and certification. Nepal has drafted and endorsed an accreditation bill, but the absence of a regulatory body to implement and monitor it continues to hinder progress. International practices permit the operation of private labs under the regulatory framework. Setting up a regulatory body and recognizing private labs could potentially decrease accreditation costs borne by traders in Nepal.

The multiple tariff bands should be revisited. The High-Level Tax Reform Commission's recommendations highlight that multiple layers of customs duty contribute to confusion and potential revenue leakages. The report suggests the restructuring of tariff lines in multiple phases, along with merging multiple para-tariffs into a single green tax to simplify the tax regime. On one hand, this would address the problem of revenue leakage and on the other help in stabilizing consumer prices. Additionally, the proposed amendment to the Custom Bill incorporates provision of the General schedule of the Kyoto Protocol and custom related provisions of the Trade Facilitation Agreement. Expediting the bill in the parliament should be a priority to strengthen Nepal's trade facilitation framework.