



THE POST-COVID INDIA-NEPAL ECONOMIC TRAJECTORY: POINTS OF ENGAGEMENT AND POTENTIALITY

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The COVID pandemic has painted a gloomy picture to the world economy as it has led to supply, demand and financial shocks from extensive lockdowns and distancing measures. The effect of the pandemic is slated to drive more than 49 million individuals into extreme poverty due to job losses and lack of access to basic resources. The issue is more acute in South Asia due to the large and dense population, weak social protection systems and high poverty rates. As India inches towards recovery, it is important for it to strengthen its outreach to its neighbours to ensure a swift and collective economic resurgence.

This would be an apt opportunity for India to strengthen its economic ties with Nepal, a country with which the recent past has been fraught with tension from border disputes and disagreements on Chinese involvement in Nepal. The Nepali Ex-Prime Minister stated in his June 2021 speech that ‘misunderstandings’ with India have now been resolved, indicating that it was time to move on to a more positive relationship between the two countries.

India and Nepal share long-standing economic and trade relations. India is Nepal’s largest export market, as well as the most significant source of import. However, India faces stiff competition in its ties with Nepal, from China which has made inroads into both, its political and economic fabric. Thus, it becomes important to highlight some of the key points of engagement in economic relations between India and Nepal and suggest ways to improve cooperation, keeping in mind a post-covid scenario.

Basis of Economic cooperation between India and Nepal

Historically, provisions of the 1950 Indo-Nepal Peace and Friendship Treaty, formed the basis of future economic cooperation. Article 7 of the Treaty highlights the emphasis on reciprocity when it says:

The Governments of India and Nepal agree to grant, on reciprocal basis, to the nationals of one country

in the territories of the other, the same privileges in the matter of residence, ownership of property, participation in trade and commerce, movement and other privileges of a similar nature.

Further, the provision in the treaty for National Treatment resulted in significant employment opportunities for many citizens coming from Nepal. It is being estimated that approximately 6 million people from Nepal are working in India. Unsurprisingly, the presence of such a large number of people from Nepal in India has resulted in significant remittances to Nepal.

Despite being a seminal document governing relations between the two countries, the Peace and Friendship Treaty of 1950 is no longer found to be acceptable to the Nepalese political leadership because it feels the treaty is outdated, out of sync with modern times and covers very little economic matters, and thus needs to be re-done. To correct the points of discontent in the treaty, an Eminent Person's Group (EPG) was formed by the two governments in 2014. However, the proposals are yet to be accepted and there is a lack of clarity in the overarching nature of friendship between the two countries.

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Currently, Nepal still relies on India for a major part of its trade. India is the largest trading partner of Nepal. Apart from this, 98 per cent of Nepal's transit trade takes place through India and 65% of Nepal's total trade is with India. So, there is a lot of dependency on India, as far as Nepal's economy is concerned, which makes a collaborative recovery process important for both countries. India in recognition of its long-standing ties with Nepal, has increased its share in financial aid to Nepal by 73 per cent from Rs. 375 crore in 2017-18 to 650 crore for the year 2018-19. Nepal's share in India's total financial aid was 12 percent in 2017-18, which stepped up to 18 percent in 2018-19.

Sectors of India-Nepal Economic Engagement

Nepal was the first country to receive India's development assistance, back in 1951. In 1954, the Indian Aid Mission was initiated, and approximately 75 developmental projects were agreed upon. In 1966, it was rechristened the India Cooperation Mission. India's objective with its aid program was to supplement the efforts of the local government in sectors like education, health and infrastructure. India has been actively involved in Small Development Projects focused on infrastructure and capacity building in areas of education, health and community development and are implemented by local bodies in Nepal.

In terms of connectivity and infrastructure projects, the Tribhuvan Rajpath is one of the first substantive connectivity projects undertaken by India. The 116 km highway construction was initiated in 1953 and was completed within three years in 1956.

In the telecommunications sector, India provided assistance for laying of the 904 km of Optical Fibre cable along the East-West Highway. For connectivity, India had helped in building and upgrading roads from highways to local rural constructions. It has also been

involved with construction of roads along the swampy Terai region of Nepal. Electrification, flood control and drinking water projects have also been undertaken by India even in remote villages in Nepal.

As far as cross-border projects are concerned, Government of India has committed to provide assistance to Government of Nepal for the establishment of Integrated Check-Posts (ICPs) at four major points along the India-Nepal border.

India's effort to build connectivity networks with Nepal is also happening in larger multilateral frameworks. The South Asian Association for Regional Cooperation (SAARC) framework did not make satisfactory progress. As a consequence, the regional cooperative efforts resulted in the emergence of new platforms, such as the Bangladesh-Bhutan-India-Nepal (BBIN) and the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC) or fora which do not include China. The emergence of these frameworks indicates growing confidence among the member countries on developing not only connectivity projects but also closer regional cooperation.

The China Factor in Nepal's Outlook

In ancient times, economic diplomacy started off as local trade between Tibet and Kathmandu. The first agreement on economic cooperation was the 1956 Agreement on Economic Aid. Among the joint bodies established to facilitate trade and commerce over the years, two are particularly important: the Inter-governmental Economic and Trade Committee (IGETC), established in 1982 to facilitate trade and investments and the Nepal-China Chamber of Commerce and Industry (NCCCI) founded in 1999, which promotes engagement between companies and entrepreneurs from the two countries.

One of the major turning points in India's relationship with Nepal and a key inroad for China, was the 2015 blockade on the Madhesi issue. This ensured that relations took a turn for the worst, and the biggest beneficiary as a result of ensuing tensions, was China. China was able to use this situation to build closer ties with Nepal and parade as an all-weather partner. On the other hand, New Delhi objected to Nepal's new constitution for allegedly discriminating against the Madhesi ethnic people who have close ties to India. Rioting broke out and India imposed an unofficial blockade on imports of fuel and essential supplies at a time when Nepal was already reeling from a recent earthquake. Kathmandu blamed New Delhi for the disruption, and China stepped in with emergency oil supplies. The announcement of demonetisation in India further dented relations between the two countries as Nepal relies greatly on remittances from expatriate workers in India.

The inroads made by China was used to aggressively push the Belt and Road Initiative into Nepal. The BRI is China's Marshall Plan in the region and was initiated in 2013. It involves a combination of a 'belt' of overland corridors and 'road' of maritime shipping lanes. Apart from being an economic corridor, it is also seen as a strategic tool since the ports and transport infrastructure being built could be utilised for both commercial and military purposes.

Involvement in the BRI was considered important for Nepali policy makers as it appeared to provide provide innumerable opportunities to sharpen its domestic infrastructure. The two

sides have already concluded trade and transit agreements, and Nepal is eyeing connections with the Chinese market and oil refineries as well as the global supply chain via Chinese ports.

While China does not have people to-people interactions on par with India, it has a long history of deploying overseas assistance to Nepal. Recently proposed Chinese projects, such as a railway line connecting Tibet with Kathmandu, will have significant geopolitical as well as geo-economic implications for India. Similarly, China has also announced scaling up of road networks into Nepal. Further, China has proposed multilateral frameworks, such as the China-Nepal-India corridor and Trans-Himalayan Developmental Cooperative Framework, wherein Nepal assumes a central location. However, the Chinese connectivity projects in Nepal need to overcome two significant challenges. First, their economic viability is contingent on their ability to access the Indian market. Second, they will have to traverse the Terai region, which enjoys a close socio-cultural relationship with India.

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The Way Ahead

Nepal's economic ties with India need to be focused because of the looming post-COVID scenario. Differences need to be ironed out and a more collaborative approach needs to be taken. The envisioned growth rate of 8 per cent for Nepal in 2021 looks highly unlikely. The widening fiscal deficit could look to expand even further with the government having to spend more to bail out troubled sectors. It could also mean greater overseas borrowing, thus increasing its debt burden for Nepal. This may be an opportunity for its neighbours like India and China to expand support to Nepal.

One of the key areas for future engagement between Nepal and India would be cooperation in the power sector. This would involve building cross border transmission lines, allowing greater access for Nepal based power producers to the Indian market and even developing an integrated grid. Further, although hydropower cooperation has historically been a key point of engagement, timely project completion is important for the Indian government as China has simultaneously been able to make inroads into the hydropower sector in Nepal. Apart from the hydropower sector, India has signed ambitious MoUs in the transport sector with Nepal. For example, MoUs for building the Raxaul-Kathmandu broad gauge railway link and principle agreements to allow Nepal to use three inland waterways (Kolkata-Kalughat, Raxaul; Kolkata-Sahebgunj ; Kolkata-Varanasi-Raxaul) have been decided. The implementation is needed on these fronts in a phased, comprehensive and time-bound manner.

For Nepal, its trade deficit with India has been a major point of concern. Among the factors responsible for this are the lack of competitiveness of Nepali goods in the Indian market, administrative hassles and large amount of unauthorized trade via open borders. Options that can be explored to remedy the situation include-increasing value addition capacity to

products being exported from Nepal, prioritizing goods with competitive advantage such as shawls, handicrafts and carpets which are labour intensive products.

India's trademark skill development projects in Nepal can also be made more robust with the changing times. Training in new age skills like Artificial Intelligence and robotics can provide an important skill set to the youth to tackle the challenges of future jobs. Engaging multilateral platforms devoid of the China factor, such as BIMSTEC is also important to progress relations. The feasibility of a BIMSTEC FTA must be undertaken in order to provide optimal trade opportunities in the region.

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One of India's main priorities should be to manage Chinese influence in Nepal. Although China and India's areas of assistance and investment are very similar in Nepal, India enjoys the advantage of longer and more sustained cooperation over decades. India has often been perceived negatively as a 'Big Brother' to Nepal due to its close involvement in Nepali politics, especially after 2015. India's geographical size and importance in the world as one of the fastest growing economies, relative to Nepal does not make the situation easier. Dispelling this image by invigorating unique cultural, ethnic and historical ties and strengthening India's grassroots-based development programs is key to improving ties with Nepal and restraining the pro-China tilt. India thus, looks to fight a battle on two fronts, against China: one of competitiveness of economic assistance and the other is of dispelling perceptions. China's aid giving practices often give off the perception of a horizontal partnership and equal power dynamic, but in actuality comes with unmistakable geopolitical ambitions. India's 'Neighbourhood First' policy must thus prioritise one of its key pillars, in the coming months: finding economic complementarities with Nepal and strengthening them.

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Notes:

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