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REVIEW ARTICLE

Agricultural trade deficit and its impact on Nepalese economy: A comprehensive review

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Abstract

International trade is essential for a country's economic development and modernization, driven by the dynamics of imports and exports. This review comprehensively examines Nepal's trade deficit and its impact on the national economy. Nepal's trade landscape is characterized by a significant imbalance, with imports consistently surpassing exports, as evidenced by an import-to-export ratio of 10.26 in the fiscal year 2022/23. This trade deficit has profound implications for national income, Gross Domestic Product (GDP) growth, inflation rates, and foreign exchange reserves. This review identifies key factors contributing to the trade deficit, including geographical constraints, limited export diversification, heavy reliance on imports, infrastructural deficiencies, insufficient promotion and advertisement, political instability, low productivity, and dependency on remittances. This study underscores the critical need for export diversification as a strategy for mitigating trade deficits. Developing sectors with high potential such as tourism, information technology, hydropower, and organic farming are essential. Additionally, improving the quality and value addition of exported goods, expanding market access through proactive trade diplomacy, and supporting small and medium enterprises are highlighted as necessary measures. This study also emphasizes the importance of substantial investments in infrastructure, education, and skill development to enhance productivity and competitiveness. Promoting a national brand and leveraging digital marketing platforms can boost Nepal's export profile. Sound monetary policies and a stable economic environment are crucial for addressing the adverse effects of exchange rate volatility and inflation. Political stability and a conducive business environment are vital to fostering long-term economic growth. The effective utilization of remittances through productive investments and reducing dependency on external aid are pivotal for achieving sustainable development. Through coordinated efforts across various sectors, Nepal can work towards reducing its trade deficit, enhancing economic stability, and achieving sustainable economic growth.

Keywords

Economic growth, export diversification, import-export imbalance, international trade, Nepalese economy, trade deficit

Introduction

International trade plays a pivotal role in the development of a country and serves as a key driver of economic growth and modernization. Imports and exports are the two major components of international trade (Breinlich and Criscuolo 2011). Every nation engages in export and import processes. Without international trade, it would be impossible for developing nations to modernize. It encourages economic growth by increasing competitiveness, growing the market, and supplying the industrial and agricultural sectors with cutting-edge machinery and technology (Mansuri 2021).

A country exports goods whose domestic prices are lower than the world price and imports those whose domestic prices are higher than the world price. If a country's exports outweigh its imports, it has trade surplus. By contrast, if imports outweigh exports, they have a trade deficit (Fig. 1). A trade deficit, often viewed as a critical economic indicator, reflects a nation's imbalance between imports and exports. When a country has a trade deficit, its import costs exceed its export revenue, which has a detrimental impact on its Gross Domestic Product (GDP). The sustainability of an economy is called into question when there is a continuous and significant imbalance in international trade (Silwal 2008).

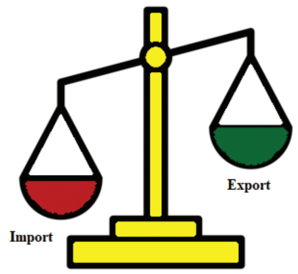

Figure 1. Trade deficit and the imbalance between imports and exports.

Nepal, a member of the World Trade Organization (WTO) and a founding member of the South Asian Free Trade Agreement (SAFTA), has established import and export trade agreements with numerous nations. Nepal's international trade was limited to Tibet and India until 1951. Trade relationships with Japan, the United States, Germany, Malaysia, Singapore, Thailand, Kuwait, France, Bangladesh, Spain, and other countries grew after 1951. Since Nepal lacks the resources necessary to produce its own capital and consumer goods, foreign trade has become a boon of globalization for poor countries like Nepal. However, as imports and exports continue to rise and decline, respectively, Nepal is dealing with a persistent trade deficit, posing significant challenges to its economic stability and development. Despite having memberships in numerous trade associations and agreements with numerous nations, Nepal lacks an atmosphere conducive to business and encourages producers and exporters to take full use of the opportunities provided by such agreements and memberships (Kafle 2017).

Nepal's economy is primarily based on agriculture, tourism, and remittances from Nepalese people working abroad (Sharma 2019). In terms of trade, Nepal's major export items include textiles, carpets, pashmina, readymade garments and other agricultural products, etc. while the key imports include petroleum products, machinery and electronics (Khanal and Khanal 2020). India is Nepal's largest trading partner followed by China. The contribution of trade to Nepal's GDP was reported to be 49.4% by 2022 (World Bank Group 2023). A significant obstacle to Nepal's economic stability is the trade deficit, which affects both the country's balance of payments and its overall economic health. The influx of remittances has increased people's purchasing power, leading to a higher consumption of luxury goods such as jewelry, cars, and electronics. However, economic instability and a sense of insecurity have contributed to a decline in commodity exports (Khanal and Khanal 2020). In Fiscal Year (FY) 2023/24, the share of imports and exports in total trade was 91.2% and 8.8%, respectively, indicating a negative trade balance (Nepal Rastra Bank 2024). Similarly, the export-to-import ratio was 9.7. Statistics show that the total imports for the fiscal year 2023/24 are approximately ten times greater than the total exports. Fig. 2 illustrates Nepal's percent share of import and export to GDP trends over two decades, from 2003/04 to 2022/23 (Nepal Foreign Trade Statistics 2023). The data reveal a consistent increase in imports, while exports of goods and services have declined over the years. This significant disparity between imports and exports has resulted in Nepal's substantial trade deficit. Nepal's growing trade deficit can be attributed to several factors.

The objectives of this study are to analyze the overall trade scenario in Nepal, identify the causes of the trade deficit, examine the consequences of trade deficits on the Nepalese economy, and propose potential solutions to mitigate its effects on the economy. This study aims to evaluate Nepal's trade patterns. Nevertheless, this study had certain shortcomings. First, it primarily focuses on assessing Nepalese trade patterns, meaning that the findings may not be directly applicable to other countries with different economic structures, policies, and dynamics. Second, the validity of this investigation is contingent on the accuracy and reliability of the secondary data used.

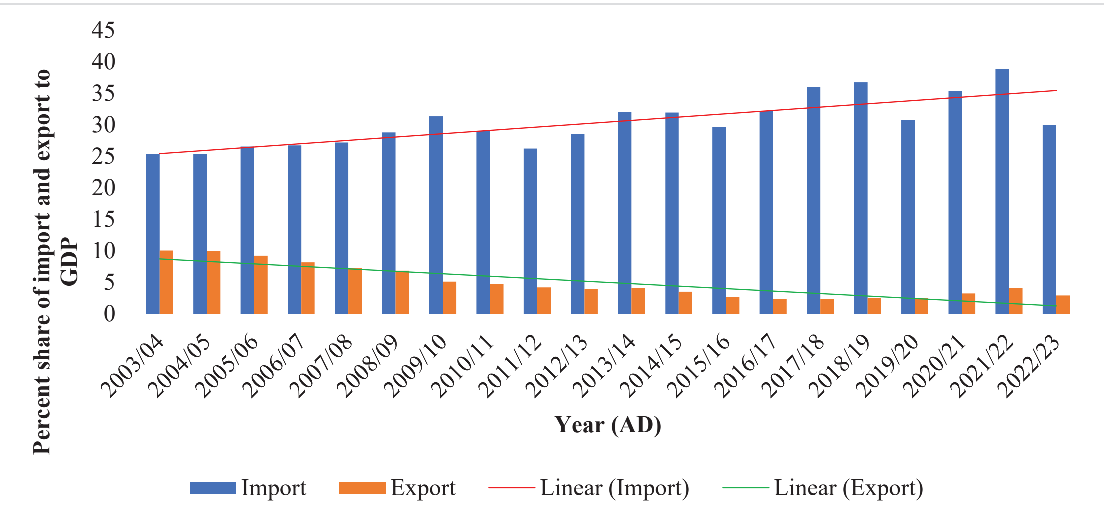

Figure 2. Import and export trend of Nepal.

Materials and methods

This review employs a descriptive research methodology to analyze the trade deficit and its impact on the Nepalese economy. This study relied exclusively on secondary data sources to ensure a comprehensive understanding of the topic. Data for this study were collected from a variety of reputable secondary sources, including publications from international organizations such as the World Bank; reports and statistics from the Ministry of Finance, Nepal; Nepal Foreign Trade Statistics; and articles and reports from newspapers, journals, and magazines. Documents from institutional websites and other credible online resources were used. Boolean operators were used to refine search queries, with keywords such as "Trade deficit," "Nepal," "International trade," and "Trade surplus" being employed to ensure the retrieval of relevant and specific information. The collected data and information were critically analyzed and synthesized to form a coherent narrative, identify key themes, draw comparisons, and integrate findings from various sources to provide a balanced overview. The analysis was conducted using Microsoft Excel 2019, employing simple statistical tools to effectively visualize the data. Graphical representations of data, such as tables, bar graphs, trend lines, and histograms, have been utilized to enhance the presentation of findings and convey complex information in an accessible and easily interpretable format.

Trade patterns and trends

Nepal's foreign trade is characterized by a significant imbalance between import and export volumes, with import volume consistently surpassing export volume. Nepal's export portfolio primarily comprises manufactured and agricultural items such as carpets, readymade garments, pashmina, handicrafts, jute products, and palm/vegetable oils. By contrast, the import sector is heavily dominated by fuel, metals, and crude oil products. Nepal's export market concentration is relatively narrow, focusing on countries such as India, China, the United States, and various European nations. This limited market scope, combined with the higher volume of imports, has perpetuated a persistent trade deficit in Nepal (Rana Magar 2021).

The total value of commodities exported from Nepal in the fiscal year 2022/23 amounted to Nepalese Rupees (NRs; 1 USD = 133.43 NRs.) 157.14 billion, a decline from NRs. 200.03 billion in the previous fiscal years. This decline highlights the challenges faced by Nepal in maintaining a robust export sector amid various economic and structural issues. Over the past decade, Nepal's export performance has shown variability, reflecting both internal and external economic pressure. Several factors contribute to export trends in Nepal. Dependency on a limited range of export goods makes the economy vulnerable to global market fluctuations and changes in demand. Inadequate infrastructure limited industrial capacity, and political instability further hinder the ability to expand and diversify exports. Despite efforts to enhance trade relations and enter new markets, the overall export growth remains constrained by these systemic challenges. On the import side, Nepal's heavy reliance on essential commodities such as fuel and metals underscore the structural limitations of the domestic economy. The lack of substantial domestic production capabilities necessitates large-scale imports to meet a country's needs. This dependency not only exacerbates the trade deficit, but also places a significant strain on the country's foreign exchange reserves.

Export trends over the past decade

Fig. 3 illustrates Nepal's export trends from 2013/14 to 2022/23 over the past ten years, highlighting the fluctuations and key changes in export volumes during this period. The export value was NRs. 91.36 billion in the fiscal year 2013/14 (Nepal Foreign Trade Statistics 2023). From this point, the export value demonstrated a general upward trend, reaching a peak for NRs. 200.03 billion in the

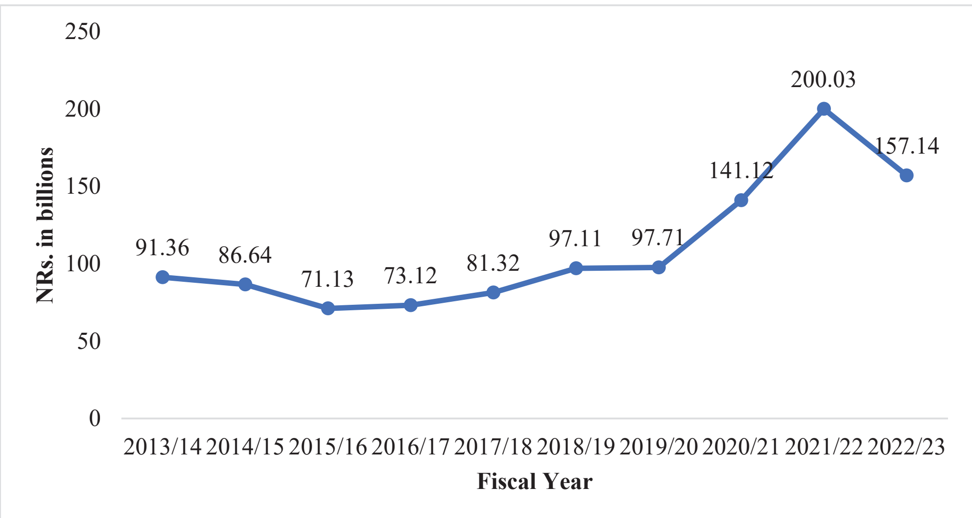

Figure 3. Exports trend of Nepal.

fiscal year 2021/22. This peak represents the highest export value within the observed period, indicating a phase of significant export growth and possibly reflecting favorable global market conditions, effective trade policies, and increased production capabilities during those years. However, in the fiscal year 2022/23, there was a notable decline in export value, dropping to NRs. 157.14 billion.

Fig. 4 shows the top ten most important exported commodities and their percentages of total exports (Nepal Foreign Trade Statistics 2023). In FY 2022/23, refined palm oil ranked first among exported goods. However, its contribution to the total exports decreased from 20.53 percent to 13.05 percent. Similarly, synthetic yarn was ranked as Nepal's second-most exported good. While it was only 6.3 percent in FY 2021/22, the proportion of synthetic yarn to total exports increased to 7.77 percent in FY 2022/23. Woolen Carpet is ranked third among exported goods in 2022/23. It accounted for 7.32 percent of Nepal's total exports compared to 4.79 percent in the previous year. From 24.06 percent in fiscal year 2021/22 to 5.39 percent in fiscal year 2022/23, refined soybean oil was exported at a lower percentage. It appears in the fourth ranking for fiscal year 2022/23 and is an emerging commodity in Nepal's export portfolio (Nepal Foreign Trade Statistics 2023). Large cardamom, one of the major exportable agricultural commodities from Nepal, has secured the fifth position in Nepal's export trade, with a percentage share of 5.27 percent in FY 2022/23 compared to 2.41 2021/22. Moreover, it is mentioned as an export product with the highest priority in both the Nepal Trade Integration Strategy (NTIS) 2023 and the Trade Policy 2015. Readymade garments are ranked sixth on the list of exports from Nepal. It accounted for 4.98% of the export share in FY 2022/23 and 3.57 percent share in FY 2021/22. The iron sheet is placed in seventh position in the list of Nepal's export trade in FY 2022/23, with an export share of 4.58 percent of Nepal's total exports. It constituted 1.28 percent of Nepal's total exports in the fiscal year 2021/22. Similarly, fruit juice and jamoth cloth were placed in the eighth and ninth positions, respectively, with export shares of 4.22 percent and 3.33%, respectively, in FY 2022/23. In contrast, the export shares of juice and jamoth cloth in FY 2021/22 were 3.04 percent and 2.47%, respectively. Jute fabric is ranked in the tenth position among the major exported goods in FY 2022/23. The export share of jute fabric has increased slightly from 3.02 percent in 2021/22 to 3.04 percent in 2022/23.

Import trends over the past decade

The total value of commodities imported into Nepal in FY 2022/23 amounted to NRs. 1611.73 billion, a decrease from the previous year's value of NRs. 1920.45 billion, as shown in Fig. 5 (Nepal Foreign Trade Statistics 2023). In FY 2013/14, imports were valued as NRs. 722.77 billion. Over the subsequent years, the import value exhibited a gradual increase, peaking at NRs. 1920.45 billion in FY 2021/22. However, this trend reversed in FY 2022/23, with the import value declining to NRs. 1611.73 billion.

Fig. 6 shows the top ten most important imported commodities and their percentages of total exports (Nepal Foreign Trade Statistics 2023). In FY 2022/23, diesel

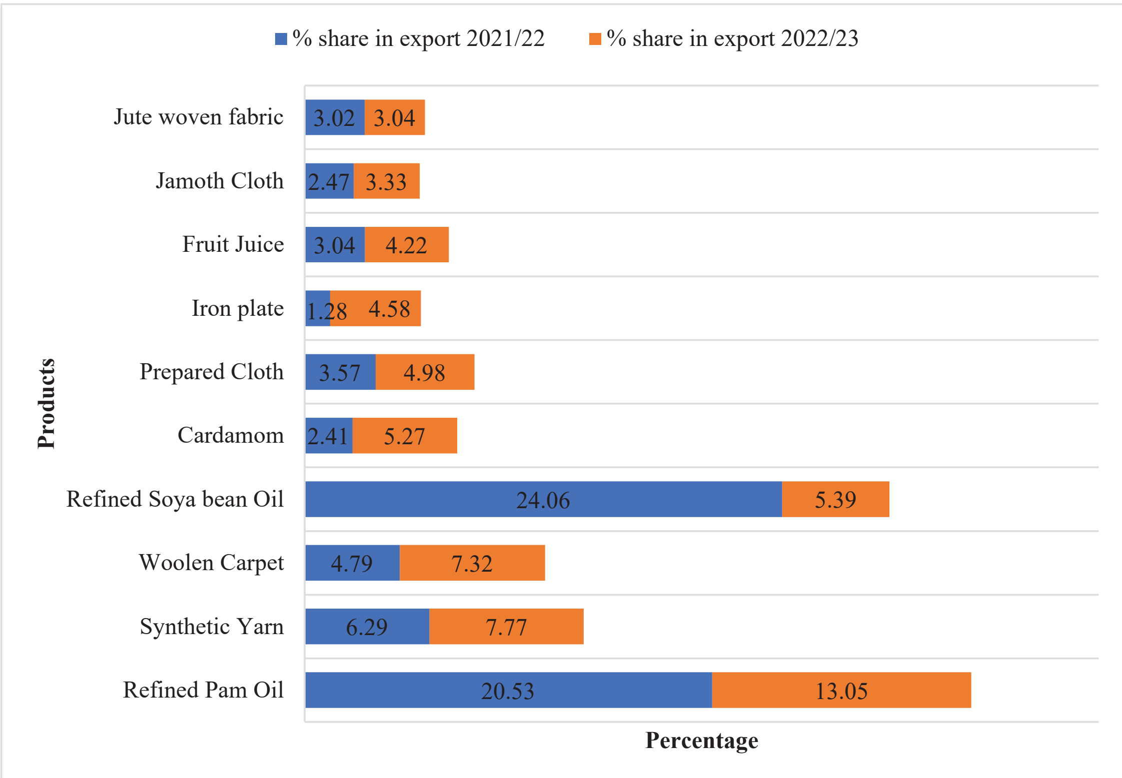

Figure 4. Share of major export commodities of Nepal.

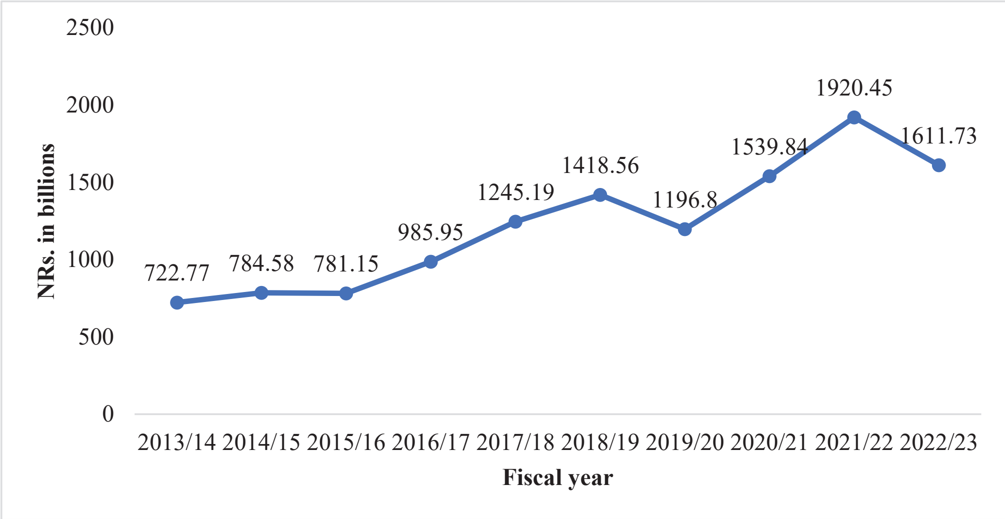

Figure 5. Imports trend of Nepal.

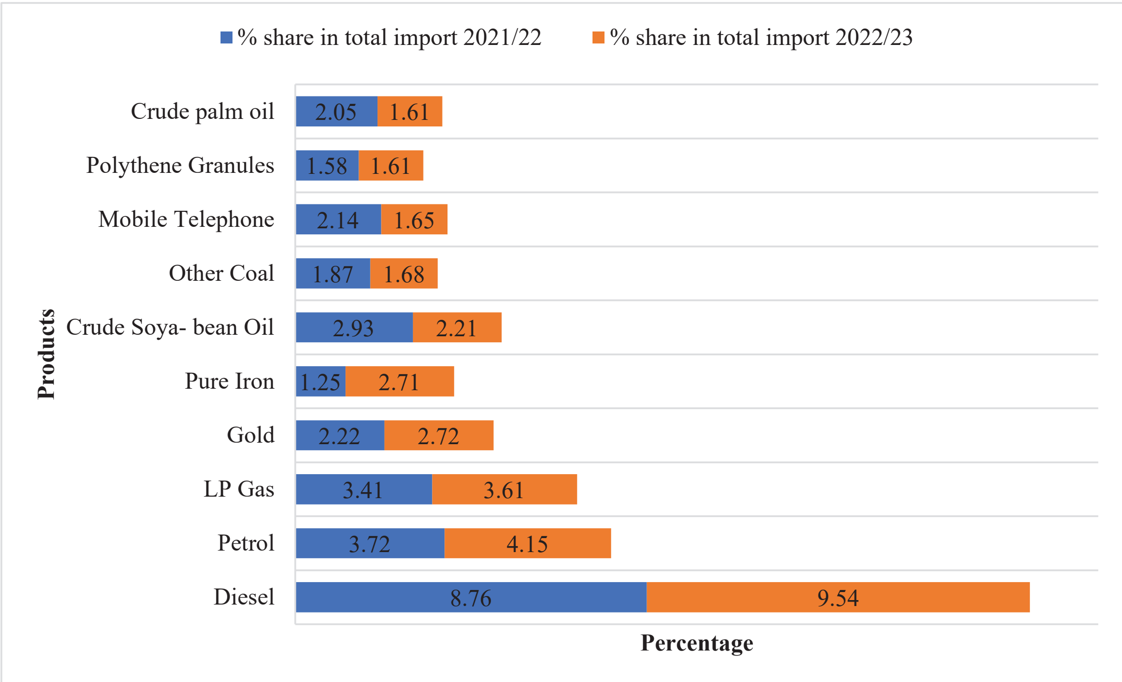

Figure 6. Share of major import commodities of Nepal.

continued to be the most imported item with an import share of 9.54 percent. It was also ranked first in FY 2021/22, accounting for 8.76 percent of total imports. On the other hand, the least imported commodity in FY2022/23 was crude palm oil. Palm oil's import share dropped dramatically from 2.05 percent in FY 2021/22 to 1.61 percent in FY 2022/23, placing it in 10th place among all imported goods in terms of total import value.

Major trading partner countries of Nepal

Table 1 provides a detailed breakdown of Nepal's total foreign trade by major trading partners over three fiscal years: 2020/21, 2021/22, and 2022/23. The data includes the total foreign trade value in billions of Nepalese Rupees (NRs.) and the percentage change in trade value for FY 2022/23 compared with the previous fiscal year. The principal trading partners of Nepal include India, China, Indonesia, the United States, the United Arab Emirates, Argentina, Malaysia, Australia, Ukraine, Qatar, and Thailand. These countries collectively accounted for approximately 90.0% of the total foreign trade in FY 2022/23.

The data indicate a broad downturn in Nepal's overall international trade, from FY 2021/22 to FY 2022/23. The total value of trade with these major partners decreased by 17.0% from NRs. 1917.8 billion in FY 2021/22 to NRs. 1591.5 billion in FY 2022/23 (Nepal Foreign Trade Statistics 2023). Correspondingly, the overall total trade value declined by 16.6% from that of NRs. 2120.5 billion to

Table 1. Nepal's total foreign trade by major trading partners.

Partner countries	Value of total foreign trade (NRs. in billion)			% Change
	FY 2020/21	FY 2021/22	FY 2022/23	2022/23
India	1078.0	1355.4	1134.5	-16.3
China	242.6	273.5	231.5	-15.4
Indonesia	17.4	53.4	42.1	-21.1
United States	33.3	68.0	39.0	-42.7
United Arab Emirates	37.5	48.4	33.3	-31.2
Argentina	41.9	39.7	24.9	-37.3
Malaysia	9.7	17.1	22.7	32.6
Australia	17.5	25.7	20.2	-21.2
Ukraine	17.2	21.2	18.4	-13.1
Qatar	0.4	3.4	13.4	300.0
Thailand	9.7	12.0	11.4	-5.5
Subtotal	**1505.2**	**1917.8**	**1591.5**	-17.0
Total Trade	**1681.0**	**2120.5**	**1768.9**	-16.6
Share of Subtotal	**89.5**	**90.4**	**90.0**	

NRs. 1768.9 billion. Country-specific trends in Nepal's foreign trade reveal varying degrees of change among its major trading partners. Trade with India, Nepal's largest trading partner, decreased by 16.3%, dropping from NRs. 1355.4 billion in FY 2021/22 to NRs. 1134.5 billion in FY 2022/23. Similarly, trade with China, the second largest partner, saw a decline of 15.4% from NRs. 273.5 billion to NRs. 231.5 billion. Indonesia experienced a significant reduction of 21.1%, with trade values falling from that of NRs. 53.4 billion to NRs. 42.1 billion. The United States exhibited the largest decrease among the top partners, with a substantial 42.7% drop from NRs of 68.0 billion to NRs. 39.0 billion.

Trade with the United Arab Emirates also declined markedly, by 31.2%, from NRs. 48.4 billion to NRs. 33.3 billion. Argentina saw a decrease of 37.3%, with trade values falling from NRs. 39.7 billion to NRs. 24.9 billion. Australia's trade with Nepal decreased by 21.2% from that of NRs. 25.7 billion to NRs. 20.2 billion, while Ukraine saw a smaller decline of 13.1%, with trade values falling from NRs. 21.2 billion to NRs. 18.4 billion. Trade with Thailand saw a slight reduction of 5.5% from NRs. 12.0 billion to NRs. 11.4 billion. Conversely, Malaysia was an exception to the general trend, experiencing a notable increase of 32.6% in trade value from NRs. 17.1 billion to NRs. 22.7 billion. A significant outlier was Qatar, which experienced an extraordinary increase in trade of 300.0%, rising from NRs. 3.4 billion to NRs. 13.4 billion. These trends reflect a broad downturn in trade with most Nepal's major partners, indicating economic challenges and the need for diversified and strategic trade policies. The exceptional increase in trade with Qatar and Malaysia suggests potential areas for strengthening and expanding trade relationships. The significant decrease in trade values with several key partners highlights the need for strategic trade policies and the diversification of trade relationships to stabilize and enhance Nepal's foreign trade performance.

Causes of trade deficit in Nepal

Landlockedness

Nepal is a landlocked country bordered by China to the north and by India to the south, east, and west. The absence of direct access to seaports significantly affects trade efficiency. The reliance on neighboring countries' ports for international trade imposes additional costs and logistical complexities. Goods must transit through India or China, incurring extra tariffs, fees, and extended transportation times. These additional costs make Nepalese exports less competitive in the global market and increase the price of imports, contributing to a trade deficit. Moreover, the vulnerability of perishable goods to degradation further heightens insecurity (Mahat and Shamsher 2021).

Limited export diversification

Nepal's export base is relatively narrow and dominated by a few sectors such as garments, carpets, and handicrafts. The heavy reliance on key products and markets, combined with barriers to market entry and insufficient value addition, constrains Nepal's export potential. The lack of diversification in exports limits a country's ability to earn foreign exchange, resulting in an imbalance between exports and imports. Nepal's export portfolio is heavily concentrated on a few key products, primarily manufactured and agricultural items such as carpets, readymade garments, pashmina, handicrafts, jute products, and vegetable oils. This narrow focus makes Nepal vulnerable to fluctuations in global demand for and prices of these goods. Any decline in the demand or price of these products can significantly impact a country's export earnings, contributing to a trade deficit.

Dependency on imports

Nepal relies heavily on imports of various goods, including petroleum products, machinery, vehicles, electronics, and consumer goods. The country's domestic production capacity is not sufficient to meet the demands of its growing population and industries, leading to higher import dependency. The lack of domestic production capacity for these critical items means importing them to meet economic and developmental needs. This reliance on imports of essential goods significantly inflates the import bill, contributing to the trade deficit. Nepal imports a large volume of consumer goods such as electronics, automobiles, luxury items, and household products. The increasing purchasing power driven by remittances from Nepalese working abroad fuels the demand for imported consumer goods. This rising demand for imports exacerbates the trade deficit, as the country spends more on foreign goods than on exports.

Infrastructural constraints

Inadequate infrastructure, including poor transportation networks and energy shortages, hampers the competitiveness of Nepalese exports. This further increases production costs and reduces the quality and quantity of goods available for exports. Nepal's transportation infrastructure is underdeveloped with a limited network of roads, railways, and airports. The mountainous terrain of the country complicates the construction and maintenance of transport routes, leading to significant logistical challenges. Existing road networks are often in poor condition, and frequent landslides and other natural disasters disrupt transportation. This inadequate infrastructure increases transportation costs, delays shipments, and hampers the efficient movement of goods within the country and international markets. Nepal lacks adequate storage and warehousing facilities, particularly for agricultural and perishable goods. This deficiency leads to high levels of waste and spoilage, reducing the quantity and quality of the goods available for export.

Insufficient promotion and advertisement

There is a deficiency in marketing, promotion, and advertising in the Nepalese context. Nepal boasts of a diverse range of distinctive products that are imbued with traditional and cultural significance. One of the primary issues is limited global awareness of Nepalese products. Many high-quality Nepalese goods, such as handicrafts, pashmina, and organic tea, fail to gain international recognition because of inadequate promotion. The globally renowned Pashmina Shawl is a prime example. In today's digital age, leveraging online platforms is crucial to reach global audiences. However, many Nepalese businesses lack expertise and resources to effectively use digital marketing tools such as social media, search engine optimization (SEO), and e-commerce platforms. This digital divide prevents Nepali exporters from tapping into the vast potential of online markets and expanding their customer bases.

Branding plays a critical role in differentiating products in a competitive global market. Nepalese products often lack strong brand identities that are essential for building consumer trust and loyalty. Without effective branding strategies, high-quality products struggle to compete against well-branded international competitors. However, Nepal has failed to showcase the features, quality, pricing, and other aspects of its products in the international market. Consequently, exports of such items are limited (Dahal Chettri 2021).

Political instability and uncertainty

Political instability and uncertainty significantly contribute to Nepal's trade deficit by undermining economic confidence, disrupting trade policies, and deterring foreign investments. Frequent changes in government have led to shifts in trade and economic policies, creating uncertainty for businesses and making long-term planning difficult. Bureaucratic inefficiency and corruption are often exacerbated by political instability and complicated trade processes, which lead to delays and increased costs. Political instability also deters foreign direct investment (FDI), which is crucial for developing export-oriented industries, thereby limiting a country's capacity to build and expand such industries. Social unrest and strikes disrupt production and trade activities, causing delays and increasing costs, which damages the reliability and reputation of Nepalese suppliers. Political turmoil can stall infrastructure projects that are essential for enhancing trade efficiency. The negative perception of Nepal as a politically unstable country further discourages potential trading partners and investors.

Low productivity and lack of competitiveness

Low productivity and lack of competitiveness significantly contribute to Nepal's trade deficit, undermining its ability to produce goods that can compete effectively in the global market. These challenges arise from outdated technology, limited access to quality input, and inadequate workforce skills. Many industries rely on traditional production methods, leading to inefficiency and low output. Inconsistent supply of quality raw materials forces manufacturers to depend on imports and increase costs. The workforce often lacks the necessary skills due to a mismatch between education and industry needs, further diminishing productivity. High production costs, driven by inadequate infrastructure and energy shortages, prevent Nepalese products from being priced competitively. This low productivity limits market access, making it difficult for Nepal to enter lucrative international markets that give lower export earnings than import expenditure, contributing to the trade deficit.

Remittance

Remittances play a crucial role in Nepal's economy, significantly impacting the trade deficit, while providing essential financial support to households. With a large portion of the Nepalese workforce employed abroad, remittances have become a primary source of income, often exceeding export revenues and accounting for a substantial share of the country's GDP. This influx enhances purchasing power, leading to increased consumption of both essential and luxury goods, which drives up imports and exacerbates trade imbalances. While remittances provide critical financial resources, they also create a dependency that can hinder local economic development, as many households prioritize immediate consumption over long-term investments. Additionally, the focus on overseas employment often results in labor shortages in certain sectors, further impeding productivity and competitiveness. This reliance on remittances to finance imports can create economic vulnerability.

Exchange rate volatility

Exchange rate volatility significantly impacts Nepal's trade deficit, influencing the costs of imports and exports. As a landlocked country, Nepal relies heavily on imports to meet its domestic needs, making it particularly sensitive to exchange rate fluctuations. A depreciating Nepalese rupee increases the cost of imported goods, leading to higher prices for consumers, and contributing to a widening trade deficit. This volatility also affects export competitiveness, and a weaker currency can make exports cheaper for foreign buyers. Unpredictable exchange rates create uncertainty for exporters, complicating pricing strategies and negotiating contracts. Exchange rate fluctuations can deter foreign investment because investors seek stability in the currency when making long-term commitments. Increased uncertainty in the exchange rate environment can lead to reduced investment in export-oriented sectors, further hampering economic growth and exacerbating trade imbalances. In addition, businesses that rely on imported raw materials face increased operational costs, making it challenging to maintain competitive pricing in both domestic and international markets.

Impact of trade deficit in Nepal

Impact on national income

National income is the value of all final goods and services produced in a country per year. According to Keynesian theory of national income, this is represented by Equation 1.

$$\text{National income} = G + C + I + (X - M) \qquad (1)$$

Where G is government expenditure, C is consumption, I is investment, X is total exports, and M is total imports (Tuovila 2020).

Trade deficit significantly affects Nepal's national income, influencing economic growth and overall prosperity. When a country imports more than exports, currency outflow can lead to a reduction in GDP, as domestic industries may struggle to compete with cheaper foreign goods. This imbalance can hinder the growth of local businesses, resulting in lower levels of investment and productivity, ultimately impacting national income. A persistent trade deficit can lead to increased borrowing and reliance on foreign aid to finance the deficit. This reliance can create a cycle in which national income is adversely affected, as funds that could have been used for domestic development are allocated to servicing debt. Additionally, the increased demand for foreign currency can lead to inflationary pressures, further eroding purchasing power and negatively impacting the standard of living. Trade deficits can restrict the government's ability to invest in critical sectors, such as infrastructure, education, and healthcare, which are essential for sustainable economic growth. As national income stagnates or declines, the government may face challenges in maintaining social welfare programs, ultimately affecting citizens' overall quality of life.

Impact on GDP

GDP is one of the primary components of the trade balance. Trade deficits have a significant impact on GDP, influencing overall economic performance and stability. When imports consistently exceed exports, the resulting currency outflow leads to a decrease in GDP growth rates. This imbalance often signifies reliance on foreign goods, which can stifle the development of domestic industries and reduce their contribution to the national economy. A persistent trade deficit may also necessitate increased borrowing to finance this gap, leading to higher public debt levels. This reliance on external financing can create economic vulnerability and hinder GDP growth, as funds that could be invested in local infrastructure or industry development are used to service debt obligations. Additionally, the pressure on foreign currency can contribute to inflation, diminish consumer purchasing power, and affect the overall economic output. Trade deficits can signal underlying structural issues in the economy such as low competitiveness and limited export diversification. These factors can hinder sustainable GDP growth and lead to economic stagnation. If local businesses struggle to compete with cheaper imports, this can result in lower productivity and investment, further negatively affecting GDP.

Impact on price of commodities

Trade deficits affect supply and demand dynamics. When imports consistently exceed exports, increased demand for foreign goods can lead to higher prices for imported commodities. As businesses and consumers rely more on imports to meet their needs, this heightened demand can increase costs, making essential goods less affordable for the average citizen. A persistent trade deficit can contribute to currency depreciation, further exacerbating this situation. When the Nepalese rupee weakens against foreign currencies, the cost of imported goods increases, leading to inflationary pressure. This inflation not only affects the prices of imported commodities but can also spill over into the prices of domestically produced goods, as local producers may raise prices in response to the increased costs of imported inputs, as illustrated in Fig. 7. Volatility in exchange rates can create uncertainty in business pricing strategies, making it difficult for them to maintain stable prices. This instability can lead to erratic price fluctuations that affect consumer confidence and purchasing decisions. In sectors heavily reliant on imports such as fuel and machinery, price volatility can have a particularly detrimental impact on the overall economy.

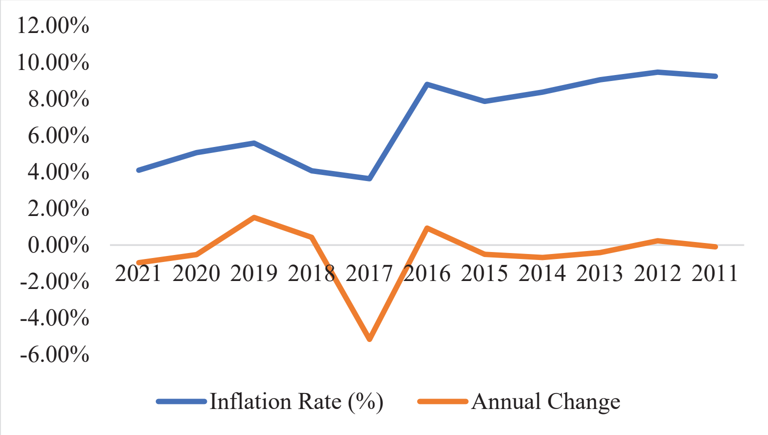

Figure 7. Trend of inflation rate of Nepal.

Impact on employment

This disparity may have a major impact on employment in a deficient nation. Displacement of the indigenous industry is one of the main ways in which a trade deficit affects employment. When consumers choose less expensive imported items over those made domestically, industries in deficit countries may find it difficult to compete, which could result in job losses and a reduction in employment prospects. Furthermore, the demand for associated jobs in supporting sectors such as manufacturing, transportation, and logistics may decrease if domestic industries contract. Furthermore, a sustained trade imbalance may be a factor in a country's declining economic competitiveness, which could result in slower economic expansion and fewer jobs created in a variety of industries.

Potential solution

Export diversification

Nepal can reduce its reliance on a limited number of export products and markets, thereby enhancing its economic resilience and stability by expanding the range of exported goods and services. The current export portfolio is heavily concentrated in sectors such as textiles, carpets, and agricultural products. To diversify, Nepal could explore and develop other sectors with high potential, such as tourism, information technology, hydropower, and organic farming. Improving the quality of exported goods and focusing on value addition, such as processing agricultural products into higher value goods, can significantly boost competitiveness. In addition, engaging in proactive trade diplomacy and establishing new trade agreements with countries beyond traditional partners can expand market access. Supporting small and medium enterprises (SMEs) through access to finance, technical assistance, and market information can empower these businesses to innovate and enter new markets. Investing in infrastructure such as transportation networks and port facilities is critical for facilitating export diversification and reducing costs. Education and training programs aimed at developing skills that are relevant to export-oriented industries can improve productivity and innovation. Promoting a national brand that emphasizes quality, sustainability, and cultural uniqueness along with leveraging digital marketing platforms can attract international buyers. Through coordinated efforts across various sectors, Nepal can achieve export diversification, reduce its trade deficit, and achieve sustainable economic growth.

Infrastructure development

Infrastructure development plays a crucial role in overcoming Nepal's trade deficit by enhancing the country's competitiveness and facilitating trade. Transportation costs can be reduced, and the efficiency of transferring goods to and from production hubs and export markets can be increased by improving transportation networks, such as roads, trains, and ports. Similarly, industry production costs can be decreased by investments in energy infrastructure, increasing the competitiveness of Nepalese exports in international markets. Additionally, strengthening the internet and telecommunications infrastructure can enhance communication and information access, enabling firms to enter new markets and conduct commerce. All things considered, a developed infrastructure fosters economic progress, makes it possible for enterprises to prosper, and eventually aids Nepal in growing its export market and closing the trade deficit.

Strong legal framework

Establishing a robust legal framework and policies in Nepal can serve as a vital framework for reducing trade deficits by fostering a conducive business environment and promoting trade competitiveness. This entails implementing transparent and enforceable trade laws and regulations to facilitate trade. Policies that align with global trade standards, remove trade barriers, and promote value-added production can assist Nepal in realizing its unexplored export potential, luring foreign investment, and reducing trade deficits. Ultimately, these measures can support sustainable economic growth and development.

Skill development of human resources

Nepal has a comparative advantage in terms of cheap labor. The availability of inexpensive labor allows Nepalese firms to produce goods at lower costs, making their products more competitive in international markets. Through targeted training programs and education initiatives, Nepal can empower its labor force with the technical expertise, innovation capabilities, and adaptability required to thrive in evolving industries. Moreover, investing in skill development not only enhances individual livelihoods and job prospects, but also strengthens Nepal's overall economic resilience and capacity to diversify its export base, ultimately fostering sustainable economic growth.

Quality standard compliance

Quality standards compliance serves as a pivotal solution for mitigating Nepal's trade deficit by enhancing the competitiveness and marketability of Nepali exports globally. Adhering to international quality standards ensures that Nepalese products meet the expectations and requirements of foreign consumers, thereby bolstering their acceptance and demand in international markets. Nepali exporters can cultivate a reputation of reliability and excellence, which can lead to increased sales, market penetration, and customer loyalty by maintaining high-quality standards. Moreover, compliance with quality standards can mitigate trade and regulatory obstacles, facilitating smoother access to foreign markets and fostering long-term trade relationships. Ultimately, prioritizing quality standards compliance not only elevates the standing of Nepali products on the global stage but also contributes to sustainable export-led economic growth, thereby helping address the trade deficit challenge in Nepal.

Conclusion

Nepal has been dealing with a fast-growing trade deficit over the past several years because of its poor export performance, presenting serious obstacles to its development and economic stability. The persistent trade deficit in Nepal poses significant challenges to its economic stability and growth. In Nepal's fiscal year 2022/23, the total value of commodities exported amounts to NRs. 157.14 billion, whereas the total value of goods imported into Nepal during the same period was NRs. 1611.73 billion. Nepal is landlocked between two huge countries, followed by limited export diversification, dependency on imports, infrastructural constraints, remittance, political instability, and uncertainty, which are the prime causes of trade deficit in Nepal. The imbalance between agricultural imports and exports has led to reduced national income, hindered GDP growth, increased inflationary pressure, and strained the country's foreign exchange reserves. Therefore, it is critical for Nepal to minimize its steadily rising trade deficit. Export diversification has emerged as a critical strategy, necessitating the development of sectors with high potential such as tourism, information technology, hydropower, and organic farming. Improving the quality and value addition of exported goods, expanding market access through proactive trade diplomacy, and supporting small and medium enterprises are essential measures. Furthermore, substantial investments in infrastructure, education, and skill development are imperative to enhance productivity and competitiveness. Promoting a national brand and leveraging digital marketing platforms can also help to position Nepalese products in the global market. Sound monetary policies and a stable economic environment are crucial for mitigating the adverse effects of exchange rate volatility and inflation. Political stability and a conducive business environment are essential to fostering long-term economic growth. Effective utilization of remittances through productive investments and reduction of dependency on external aid are vital for achieving sustainable development.

Statements

Author contributions

Conceptualization: PK, SG, AA. Data curation: SG, AA, PK. Formal analysis: AA, SG, PK. Funding acquisition: AA. Investigation: AA, SG, PK. Methodology: PK, AA, SG. Project administration: PK, SG, AA. Resources: PK, SG, AA. Software: PK, SG, AA. Validation: PK, AA. Visualization: AA. Writing - original draft: AA, SG. Writing - review and editing: SG, AA.

Data availability

No data was used for the research described in the article.

Conflict of interest

The author declares no conflict of interest.

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