

2022 USTR Annual Report to Congress on the Implementation of the Nepal Trade Preference Program (NTPP)

The Trade Facilitation and Trade Enforcement Act of 2015 (TFTEA) entered into force on February 24, 2016.¹ Section 915 of the TFTEA directed the President to establish a new country-specific preference program to grant Nepal duty-free treatment for a set of textile, apparel, and headgear products covered by 66 eight-digit tariff lines in the Harmonized Tariff Schedule (HTS), which otherwise were ineligible for duty-free treatment under the Generalized System of Preferences (GSP) program. The Nepal-specific program is referred to as the Nepal Trade Preference Program (NTPP). Following the determination that Nepal met certain eligibility requirements, the program was implemented by Presidential Proclamation on December 15, 2016. It provides Nepal non-reciprocal preferential trade benefits on the specified products through December 31, 2025. These preferences were provided to assist Nepal in its recovery from the devastating April 2015 earthquake and subsequent aftershocks. Due to changes in the U.S. Harmonized Tariff Schedule, the number of tariff lines for which Nepal is exempt from customs duties increased in July 2016 to 77 eight-digit tariff lines. In addition to the tariff preferences, the TFTEA directs the President to provide trade-related technical assistance to help Nepal implement the World Trade Organization (WTO) *Trade Facilitation Agreement*.

The TFTEA requires the President to present a report to Congress on the implementation of Section 915 of the TFTEA within one year of the enactment of the Act, and annually thereafter. The Office of the United States Trade Representative (USTR) submitted last year's report to the House Ways and Means and Senate Finance Committees on February 24, 2021, as required under the statute. This report includes overviews of the political, economic, labor, and trade conditions in Nepal; an assessment of Nepal's eligibility to receive preferential trade benefits; information on U.S. trade policy as it relates to Nepal; information related to Nepal's utilization of the trade preference program; and information on implementation of technical assistance.

Political Economy: Following the adoption of a new constitution and elections held at the local, provincial, and national levels in 2017, Nepal formed a new government in February 2018, with K.P. Sharma Oli appointed as Prime Minister (PM) and appeared to enter a period of relative political stability. However, political uncertainty has since taken over in recent years. On December 20, 2020, President Bidya Devi Bhandari dissolved Parliament at PM Oli's direction and announced a general election for April-May 2021. The dissolution of Parliament followed stalled negotiations between internal factions of the ruling Nepal Communist Party (NCP). The dispute was seen as primarily between PM Oli and Pushpa Kamal Dahal (Prachanda), the former PM and Co-Chairman of the NCP. Prachanda then petitioned the Supreme Court to challenge Oli's authority to dissolve Parliament. Nepal's Supreme Court announced on February 23, 2021 that the December dissolution of Parliament was unconstitutional. PM Oli again tried to dissolve Parliament in May 2021 and was overruled by the Supreme Court again. The Supreme Court ultimately appointed Nepali Congress (NC) President Sher Bahadur Deuba as the head of a coalition government on July 13. Oli's replacement by Deuba brought some progress on issues of bilateral interest to the United States, but little practical change in Nepal's governance. With under 25-percent of members of Parliament, PM Deuba has focused on procuring and delivering vaccines, passing a budget, tabling the Millennium Challenge Corporation (MCC) Compact in Parliament, and preparing for Nepal's planned 2022 local, provincial, and

¹ 19 U.S.C. § 4454; P.L. 114-125, 130 Stat. 122, 276-79 (Feb. 24, 2016).

parliamentary elections. At the time this report was being finalized, protests by some pro-China communist parties on the basis of a dis- and misinformation campaign (supported by the People's Republic of China) have made the prospect of Parliament's ratification of the MCC Compact unclear.

Economic Overview: Following three consecutive years of around 7 percent GDP growth, Nepal's economy contracted by 1.9 percent in fiscal year (FY) 2019/2020 as Nepal instituted a strict national lockdown in response to the COVID-19 pandemic.² In FY 2020/2021, economic growth is estimated to have rebounded and increased slightly by 1.8 percent.³ The initial 120-day lockdown, beginning in late March 2020, affected all aspects of the economy including industrial and agricultural production, consumer demand, as well as retail and wholesale trade. The pandemic also impacted Nepal through the tourism sector that accounts for approximately 8 percent of Nepal's economy, which effectively ground to a halt. Nepal had 80 percent fewer foreign tourist arrivals during 2020, which severely impacted the sector that employs directly and indirectly more than one million people. While the economy was recovering in early 2021 and initial estimates predicted economic growth of 4 percent, the second outbreak of COVID-19 in May-June 2021 led to a second lockdown and reduced growth expectations. Despite businesses now reopening, the economy is projected to grow by an estimated 3.9 percent in FY 2021/2022 as periodic COVID-19 disruptions continue and as the demand for tourism remains limited. On the other hand, the recovering economy has led to a surge in imports, starkly increasing the current account deficit and eroding the country's foreign exchange reserves. Even if COVID-19 is effectively controlled and the economy improves, the current political uncertainties will likely reduce growth prospects and erode foreign investor interest in Nepal in the near and medium-term. Low productivity, reduced export competitiveness, outward migration, and a reliance on remittances are expected to continue restricting Nepal's medium-term rate of economic growth.

Trade Overview: Nepal is a landlocked country with the Himalayan mountain range to the north. As a result, Nepal's trade is heavily reliant on India through its border to the south. Nepal's export costs are considered high with respect to air, rail, and truck cargo relative to other low-income countries, which limits export competitiveness. Trade flows were badly affected by the COVID-19 pandemic but have now recovered back to pre-pandemic levels. Nepali exports increased by approximately 44 percent to reach \$1.14 billion in Nepali FY 2020/2021.⁴ The majority of Nepali exports (73 percent) were destined for India, followed by the United States (10 percent), Germany (2.3 percent), Turkey (2 percent), and the United Kingdom (1 percent). In Nepali FY 2020/2021, Nepal's leading exports were soybean oil, cardamom, carpets, woven fabrics, and yarns.

Nepali imports increased by approximately 25 percent to \$12.9 billion in Nepali FY 2020/21.⁵ Nepal's largest import categories in Nepali FY 2020/2021 were energy products (diesel, gasoline, liquified petroleum gas, and coal), iron and steel products, crude soybean oil, rice, and mobile phones. India is the dominant supplier of goods to Nepal and accounted for 60 percent of total Nepali imports in Nepali FY

² Nepal's fiscal year runs from July 16 through the following July 15.

³ The World Bank and IMF

⁴ Government of Nepal, Ministry of Industry, Commerce, and Supplies, Trade and Export Promotion Center, Nepal Trade Information Portal. Currency conversion using Nepal Rastra Bank exchange rate of 1 U.S. Dollar to 119 Nepalese Rupee on December 31, 2021.

⁵ Ibid.

2020/2021. China is the second largest import source and accounted for 16 percent of total imports. The United States was Nepal's 8th largest import source, accounting for less than 2 percent of imports.

Eligibility: Nepal met the country eligibility criteria for 2021 for the Nepal Trade Preference Program under the GSP program and eligibility requirements referenced in the African Growth and Opportunity Act, as specified in the TFTEA.⁶ This assessment was based on an interagency review, chaired by USTR, to examine whether Nepal met the eligibility criteria. The eligibility criteria include, among others, establishing or making continual progress in establishing a market-based economy, the elimination of barriers to U.S. trade and investment, the rule of law, a system to combat corruption and bribery, and the protection of internationally recognized workers' rights. Nepal is also required not to engage in activities that undermine U.S. national security or foreign policy interests nor engage in gross violations of internationally recognized human rights.

U.S. Government agencies monitored actions taken by the Nepali government during 2021 and considered information drawn from other interested stakeholders. The COVID-19 pandemic and political uncertainty continued to slow the pace of economic reforms pursued by Nepal in 2021. While regulations to implement the Foreign Investment and Technology Transfer Act were finalized, there was less progress on amending Nepal's intellectual property (IP) laws. Nepal has been drafting legislation to amend and consolidate Nepali IP laws, but the reforms have not yet been introduced in Parliament. In March 2020, Nepal temporarily banned imports of dry peas, betel nut, dried dates, black pepper, liquor, and vehicles valued over \$50,000 to stabilize its foreign exchange reserves (which were at risk of depleting precipitously due to potential loss of remittances as a result of the pandemic). Nepal subsequently rescinded the import ban of most of these products. However, given the state of Nepal's trade deficit and depleting foreign exchange reserves, import restrictions on additional goods remain a possibility. Nepal also continues to restrict or ban imports of energy drinks and sodas.

The Ministry of Industry, Commerce and Supplies (MOICS) utilized a provision in the Foreign Investment and Technology Transfer Act (FITTA) 2019 to make an amendment and allow foreign direct investment (FDI) in primary agriculture, but only if 75 percent of the products are exported. Nepal hopes that FDI will enable the modernization and mechanization of the agricultural sector. However, the matter remains sub judice at the Supreme Court.

Progress on tackling corruption and bribery was limited, and Nepal's ranking in Transparency International's 2021 Corruption Perceptions Index remained low as Nepal was ranked 117th out of 180 countries.

The NTPP and the underlying GSP program require that beneficiaries take steps to afford internationally recognized worker rights, including in the Special Economic Zones (SEZ). Nepal's labor law generally provides for freedom of association, the right to organize, and collective bargaining. However, in an apparent attempt to promote the competitiveness of Nepali firms, the SEZ Act of 2016 prohibits workers from striking in any SEZ. Forms of forced and compulsory labor are prohibited, and the government began collecting forced labor data to effectively target law enforcement efforts.

⁶ Although the authority to provide duty-free treatment under GSP lapsed on December 31, 2020 (19 U.S.C. § 2465), the GSP program's statutory eligibility criteria did not change and the NTPP still requires use of them as eligibility criteria for benefits under NTPP.

In 2021, the ILO and the Government of Nepal published national and provincial-level child labor estimates based on data from 2018. It is estimated that there were 1.1 million children engaged in child labor, including 200,000 in hazardous child labor. Although quantitative data has yet to be collected, reporting indicates that COVID-19 has led to an increase in child labor, particularly in agriculture, domestic service, and street employment. During the year the government did make progress to eliminate the worst forms of child labor, including allocating funds to increase the number of child labor free municipalities. Additionally, over 173 local Child Rights Committees were formed, a Child Welfare Officer was appointed in 93 local government bodies, and a Child Fund was created in 171 government bodies. However, Nepal's minimum age of 17 for hazardous work is not consistent with international standards and Nepal's hazardous work list for children is not comprehensive as it does not include brickmaking. The U.S. Department of Labor continues to report that forced and child labor is used to manufacture bricks, carpets, embellished textiles, and stones.

Although labor laws extend labor protections to workers in both the formal and informal sectors, law enforcement by Nepal's labor inspectorate remains weak. Following the creation of a federal system in Nepal, the federal government is still in the process of determining labor inspection responsibilities at the federal, provincial, and local levels. There are only 15 labor inspector positions in Nepal, and only 10 of these positions are currently filled, which is much lower than recommended by the ILO. The lack of human resources, capacity, and training on its labor laws inhibits robust monitoring to ensure full compliance with the labor laws and limits Nepal's ability to take meaningful actions against perpetrators of child labor and its worst forms.

While Nepal's constitution and law prohibit it, women and other vulnerable groups face discrimination, including in employment. Nepal made little progress in implementing anti-discrimination legal provisions to extend employment opportunities for lower-caste individuals. The United States will closely monitor developments related to discrimination and worker rights in Nepal as well as intensify engagement to ensure that Nepal is taking steps to enhance labor protections.

U.S. Trade and Investment Policy with Respect to Nepal: U.S. trade and investment policy with respect to Nepal focuses on increasing bilateral trade to promote economic development in both countries. The primary venue for implementing this policy is through the United States-Nepal Trade and Investment Framework Agreement (TIFA) Council. Following a TIFA intersessional meeting in November 2020, the fifth TIFA Council meeting was held virtually on December 15, 2020 and covered a wide range of economic issues. Following the 2020 TIFA meeting, the United States engaged with Nepal periodically throughout 2021 on a range of bilateral trade issues, including customs and trade facilitation, IP, digital trade and electronic commerce, labor, financial services, and market access for agricultural goods. Both governments have agreed to deepen their engagement in 2022 through intersessional meetings and to hold the 6th TIFA Council Meeting in Kathmandu, Nepal, as soon as travel conditions permit.

U.S. Imports from Nepal under Preference Programs: During 2021, U.S. imports from Nepal totaled \$108 million (see Table 1), increasing by 25 percent compared to 2020. Nepali exports to the United States are concentrated in a few major products, including carpets and other textile floor coverings (\$30.4 million), dog and cat food (\$14.2 million), and certain other textile articles (\$10.8 million). Certain products from Nepal receive preferential duty-free access to the U.S. market through both the GSP program and the NTTP. Even though the GSP program expired at the end of 2020, importers claimed

GSP preferences on \$18 billion worth of trade from Nepal in 2021 in the event that Congress reauthorizes GSP benefits retroactively.

Table 1: U.S. Imports from Nepal by Program (\$1,000)

Import Program	2017	2018	2019	2020	2021
Imports For Consumption (No program claimed)	80,694	85,731	74,973	73,829	86,292
GSP*	8,575	9,226	12,643	10,063	18,036
Nepal Preference	2,368	3,199	3,180	2,465	3,939
Total	91,638	98,156	90,796	86,357	108,267

*While the authority to provide duty-free treatment under the GSP program lapsed on December 31, 2020 (19 U.S.C. § 2465), importers continued to claim GSP benefits in the event that Congress reauthorizes GSP retroactively, consistent with past precedent.

Sources: U.S. International Trade Commission, Dataweb

Note: Totals may not add due to rounding.

The NTPP provides duty-free access to a total of 77 tariff lines, including 56 textile tariff lines, ten leather and footwear tariff lines, nine clothing tariff lines, and two tariff lines for other manufactured products. The average Most-Favored-Nation (MFN) duty for the products covered by the NTPP was 9.7 percent in 2017, with duties ranging from 1.2 percent to 20 percent. Of the 77 NTPP tariff lines, 31 tariff lines receive duty-free treatment under the GSP program. Many of these products were not GSP-eligible at the time TFTEA was passed in 2015 but became GSP-eligible in June 2016.

During 2021, the fifth full year the NTPP has been in place, total imports under the program were \$3.9 million and accounted for 3.6 percent of total U.S. imports from Nepal. The largest import categories were container bags and boxes (\$1.6 million), hats and other headgear (\$727,000), and carpets and floor coverings (\$482,000).

Utilization of the NTPP rebounded in 2021 and was the highest it's been since the program was implemented (see Table 1). The U.S. Embassy in Kathmandu continues to promote the NTPP by conducting media outreach and publishing a dual-language NTPP manual to help small businesses understand the steps required to export to the United States. During the 2020 TIFA Council meetings, USTR and Nepal discussed how to promote the program to traders. Nepal continues to believe that many of the currently eligible products are not feasible for Nepal to export but expressed interest in continuing to discuss ways to expand the use of the program. Nepal also presented a "Concept Paper" for how to increase utilization of the program, which informed the U.S. Agency for International Development's (USAID) Trade and Competitiveness program that is now underway.

Table 2: U.S. Imports under the Nepal Trade Preference Program (\$1,000)

HTSUS Number	Product Description	2021
4202.92	CONTAINER BAGS, BOXES, CASES AND SATCHELS NESOI, WITH OUTER SURFACE OF SHEETING OF PLASTICS OR OF TEXTILE MATERIALS	1,625
6505.00	HATS AND OTHER HEADGEAR, KNITTED OR CROCHETED, OR MADE UP FROM LACE, FELT OR OTHER TEXTILE FABRIC, IN THE PIECE (BUT NOT IN STRIPS); HAIRNETS	727
5701.10	CARPETS AND OTHER TEXTILE FLOOR COVERINGS, KNOTTED (WHETHER OR NOT MADE-UP), OF WOOL OR FINE ANIMAL HAIR	482
4202.22	HANDBAGS, WHETHER OR NOT WITH SHOULDER STRAP OR HANDLES, WITH OUTER SURFACE OF PLASTIC SHEETING OR OF TEXTILE MATERIALS	302
6214.20	SHAWLS, SCARVES, MUFFLERS, MANTILLAS, VEILS AND THE LIKE OF WOOL OR FINE ANIMAL HAIR, NOT KNITTED OR CROCHETED	284
4202.32	ARTICLES NORMALLY CARRIED IN THE POCKET OR HANDBAG, WITH OUTER SURFACE OF SHEETING OF PLASTICS OR OF TEXTILE MATERIALS	113
5702.49	CARPETS AND OTHER TEXTILE FLOOR COVERINGS, WOVEN, NOT TUFTED OR FLOCKED, NESOI, OF PILE CONSTRUCTION, MADE-UP, OF TEXTILE MATERIALS NESOI	112
4202.29	HANDBAGS, WHETHER OR NOT WITH SHOULDER STRAP OR HANDLES, WITH OUTER SURFACE OF MATERIALS NESOI	61
5703.10	CARPETS AND OTHER TEXTILE FLOOR COVERINGS, TUFTED (WHETHER OR NOT MADE-UP), OF WOOL OR FINE ANIMAL HAIR	48
6117.80	MADE-UP CLOTHING ACCESSORIES NESOI, KNITTED OR CROCHETED	45
All Other:		140
Total		3,939

Source: U.S. International Trade Commission, Dataweb

Technical Assistance: The TFTEA directs the President to provide trade-related technical assistance to Nepal, a function which was delegated to USAID, in consultation with the State Department and USTR. In 2019, USAID supported the UN International Trade Center’s Sustainability Map to Nepal, connecting over 2,300 Nepali producers (ginger, tea, coffee) to international supply chains and global buyers as well as providing information related to international standards. The UN platform provides support to these producers for branding and marketing as well as information on voluntary international certification standards. In January 2022, USAID launched a five-year, \$18.9 million activity called USAID Trade and Competitiveness to increase the competitiveness of Nepal’s private sector and unlock new sources of financing and investment for sustainable and inclusive economic growth. USAID Trade and Competitiveness will strengthen enterprises in targeted sectors with high potential for growth and employment creation, with a focus on agro-processing, digital services, and tourism, while supporting the private sector to recover from the impacts of COVID-19. Through this new activity, USAID will increase the competitiveness and sales of 1,500 high-growth Nepali firms through greater access to finance and catalyze \$175 million in new investment. USAID Trade and Competitiveness plans to improve management practices, adoption of standards and technology, and inclusive human capital practices while supporting an investment climate and business enabling environment that is conducive to market entry and trade.

The U.S. Department of Commerce’s Commercial Law Development Program (CLDP) has been working with the Office of the Investment Board of Nepal (OIBN) since 2019 to develop and improve processes related to infrastructure projects. In 2021, CLDP and OIBN agreed to focus on technical assistance related to investment promotion, including project preparation, project due diligence, project evaluation, and methods for attracting investors.