

Chapter 10

SUMMARY AND CONCLUSION

Nepal is one of the closest neighbours of India. The Indo-Nepali economic relation is an important factor for the stability of the region. Since 1950 the relationship between India and Nepal has been based on two treaties - the Treaty of Peace and Friendship and the Treaty of Trade and Commerce - by which each government agreed to acknowledge and respect each other's sovereignty. Both treaties reflected India's desire for a friendly and stable government in Nepal.

Further, due to long historical relations many people from Nepal migrate to India and many Indians migrate to Nepal for their livelihood. It has been stated that influx of Indians is about 1,00,000 each year. However, the Indian External Affairs Ministry put the number of Indian immigrants in Nepal at 3.8 million of which 2.3 million had already acquired Nepalese citizenship. On the other hand, Nepal is a population - exporting country. Since the middle of the 19th century thousands of young Nepalese migrated to India to serve in the Gurkha Regiment and others migrated to India to work as tea plantation labourers or cultivators in Darjeeling or Sikkim. The 1961 Census reports that there were nearly a half-million Nepali-born migrants in India and a total of one million who reported Nepali as their mother tongue. Thus, India and Nepal are bound by the forces of history, geography and population to

be friendly and sympathetic to each other's cause. Officially Nepal is a Hindu Kingdom. But Nepal is a very poor country. Over 90 per cent of Nepal's labour force is employed in agriculture and agriculturally related industries. In 1971 twentyfive countries (of which Nepal and fifteen others are land-locked) including Nepal were identified by the United Nations as the "least developed" in the world on the basis of a number of economic and social indicators. These countries in particular were dependent to an exceptional degree on one or two relatively more industrialised neighbour for the conduct of trade and in addition, traded heavily with these neighbours from a position of substantial balance of trade deficits as in the case of Nepal with respect to India.

Nepal's progress towards industrialisation is slow; contribution of modern industries to the total GDP of Nepal has been less than 3 per cent (2.7 per cent in 1981-82). The contribution of cottage industries to GDP has declined from 1.37 per cent in 1976-77 to only about 1.2 per cent in 1981-82. Nepal's industries - both large scale manufacturing and small scale cottage industries are still in a rudimentary stage. The structure of industries have not showed any significant change, on the contrary it has remained as it was two decades ago. The industrial production has not shown any improvement in quality. The industrial sector of Nepal is primarily an extension of agricultural sector and consists mainly of small scale and

cottage industries. Though the contribution of small scale and cottage industries to the GDP of Nepal is insignificant, it still plays an important role in the economy of Nepal as this sector only provides a viable alternative to agriculture. But this sector is exclusively reserved for the Nepalese investors and Indians are excluded from investing in this sector. Therefore, Indians and Indian investors can invest only in the large scale manufacturing sector.

Private foreign investment, mostly from Indian entrepreneurs has been generally shy in Nepal. Prior to 1950 very few private enterprises took place in Nepal. The factors which slowed private foreign investments in Nepal are chiefly political instability, landlockedness and poor infra-structural facilities, shortage of trained labourers, low purchasing powers and limited market. In spite of many schemes of incentive Indian investment in the private sector has not been of much significance. One basic reason for this shyness of Indian investment is that India is a bigger market than Nepal and India has already developed its basic infrastructure and an atmosphere for the private investment. Therefore, Indian investors do not find much enthusiasm in investing in Nepal. Most of the Nepalese industries, in the early phases depended on India for marketing. Nepal did not develop either the market or the capital market necessary for industrialisation. At present Indian private investment in Nepal is being confined to seven ventures, one each in brewery, manufactures of ghee, production of dry cells,

conversion of wood into splinters and in hotel business and two are engaged in mining operations.

There are various problems for the Indian private sector to establish industries in Nepal. The landlockedness of the country and limited purchasing powers of the majority of the people and thus small size of the domestic market has impeded the scope of establishing large-scale manufacturing in Nepal. Further, it has been perhaps more profitable for Indian entrepreneurs and businessmen to engage themselves in trade and commerce than to invest directly in industrialisation. Furthermore, the inadequate infrastructure relating to energy, roads and communications have slowed the movement of Indian investors in Nepal. These created problems of procurement of rawmaterials and marketing of final products. That is why we find the concentration of Nepalese industries in Kathmandu Valley and eastern zone of terai i.e. mainly in Biratnagar area. There is easy intercourse with Indians in terms of marketing and availability of rawmaterials in these border areas of Nepal. Indian capital outflow into Nepal is also restricted because domestic investments are not yet fully saturated i.e. local capital in India has not become surplus and can be fully utilised at home. Thus, inspite of the best intentions and promising opportunities, there is no significant inflow of Indian capital into Nepal.

There are instances in which Indian investors' selfish and harmful motives have been exposed. The main purpose of some Indian investors was the evasion of income or other taxes in India and to invest their "black money" in Nepal to earn quick profits from such investments. These industrialists are not eager in the industrialisation of Nepal. Many industrial units were established and then dismantled and some of these industries were totally irrelevant to the needs and requirements of Nepal.

There are also problems regarding Nepal government. The Govt. of Nepal has not cleared the dividing line between the public and private sector. Further, the Government of Nepal has taken a very simplistic view of the private sector especially started by the Indians. Programmes and targets of industrial development to be carried out by the private sector are fixed from above with the expectation that the private sector would automatically respond the government's call. This is very often a very erroneous approach because it fails to recognise that the actual investment in industrial enterprise is influenced by the decisions of individual investors and not by planners. Besides, the top-down approach of planning fails to capture private sector's interests and come to grip with the forces governing investment decisions and behaviours. The industrial plans have been constructed as mere financial plans with little regard to physical aspects. Even as regards to financial aspect, there are problems and private investors are not helped much by

the financial institutions of Nepal in general. In practice the financial institutions have tended to focus its lending operations to a few industrial fields notably hotels and other similar service sectors that command only a secondary importance from the view-point of national interest. Although the hotel industry constitutes the linchpin of tourism sector which has been the single important source of foreign exchange earnings, the question is whether this can be considered as a sound trend of industrialisation. Further, a study shows that about 35 to 40 per cent of gross earnings from the hotel sector "leaks out" of the country for paying the import bills of the industry itself.

Nepal Government, however, does not like "a free for all" for the Indian investors. Now-a-days joint ventures are gradually gaining importance in Nepal. Nepal Government prefers this type of venture to reduce its dependence on India. But, it is too early to say, how far and how much Indian investors would be keen to invest in Nepal if joint sector becomes the major type of management.

It is true to suggest Nepal is heavily dependent upon India for private investment, private loan and public assistance. Public assistance of India to Nepal is mainly directed towards building up the infra-structure of Nepal. India has done commendable job by preparing road, airfield and communication system with little Nepalese participation. Nepalese involvement

was limited to supplying unskilled labour. No effort was made to utilise the construction phase as a training period for Nepalese who would later take up the task of construction.

India's early economic aid to Nepal, at least, placed little emphasis on one of the major assumptions underlying (say) American assistance. India had little interest in building up de facto independence of the recipient of aid. In contrast to the American view that only a strong state was proof against subversion, India appears to have deduced that Chinese influence was best excluded from Nepal by the maintenance of the kingdom's "special relationship" with India. However, it took some years to change this pattern and in recent years, the pattern of Indian assistance is undergoing a blow but significant changes. The new approach is increasingly reflected in setting up technical institutes and to assist in the developmental programmes of the kingdom so that Nepal may be self-reliant in the field of development. But India's aid to Nepal has been basically guided by strategic factors and maintenance of political stability in Nepal. India's strategic interests from large in economic aid to Nepal. India's aid was mostly on the basis of programme and in the form of "grants" - the loan element being very small. But it is largely owing to Indian aid for the growth of infrastructure that Nepal has been able to register some amount of economic growth. Nepal, on the other hand, is keen to reduce her dependence on India. India's aid has declined though not

in absolute terms but in percentage. In the pre-plan period Indian assistance to Nepal in development was about 73.69% but in the end of the Fifth Five year plan this proportion is about 15.19%. India's contribution to Nepal has been declining.

A large section of Nepalese believe that the sole objective of India's aid to Nepal is strategic and for that purpose it wants to dominate their socio-economic and political life. It is also alleged that India government is not interested in the industrialisation of Nepal because India wants that the later shall remain an agricultural country so that it continued to be dependent on India. The Nepalese alleged that the construction of roads by India (for example) has only succeeded in facilitating the extension of Indian market. Further larger share of the facilities in irrigation and power had been taken by India. Regarding flood control measures, it is alleged that Nepal has been denied many of the benefits of which it is entitled.

Though there might be some truth in some of these allegations, it is groundless to suggest that India is not interested in industrialisation of Nepal. It is to be understood that development of agriculture, power and transport facilities is the pre-requisite for the industrial development of any country and India is definitely participating in a big way for the industrialisation of Nepal. While it is true that aid promotes the economic development of Nepal, it is also significant

that Nepal is very often unable to make an effective use of the aid. In fact Nepal's own internal problems emanating from the deep-rooted tradition and vested interests have been largely responsible for the slow economic progress and faulty implementation of many projects. There are some structural problems in Nepal, primarily of land ownership and tenure, as well as those of taxation which put hurdles in the smooth working of development projects assisted by Indian government. Despite a population of 14 million, the effective market for manufactured industrial goods of Nepal is extremely limited. The market for industrial consumer goods is largely confined to small per cent of population living in urban and accessible areas of the country. Not only is the demand in local market small but the Nepalese goods are to compete with the Indian goods which are normally of better quality. The long open boundary of about 800 km. makes "protection" of domestic products difficult. Nepal's landlockedness has further increased these problems. Transshipment cost adds a significant margin to the price of Nepalese products. These constraints to industrial development have not been offset by Nepal's large and low cost labour force as the skill of the local labour is very low.

The major problem of industrial development in Nepal is its weakness in agriculture. Apart from the old feudalistic land-tenure system, the system of cultivation is primitive. The farmers are ignorant about the better technique of production;

the chemical fertiliser which is the key factor in the process of transition towards development is relatively unknown and even less than other developing countries. Agricultural yield per person per hectare has been declining. For example, production of foodgrains has declined by 2.2 per cent and productivity has gone down by 3.42 per cent over the 1975-79 period.

The land revenue system in Nepal has still remained old, pre-feudal or feudal. A common feature of all these systems was to create a privileged class of absentee landlords whose commitment to the rural development is minimal. Though a comprehensive land reform programme was introduced throughout Nepal during the mid-sixties, its results as yet have not been able to change the skewed pattern of distribution of income and wealth. In Nepal the control of farmland remains a principal key to wealth, status and power. A large majority or more than 90 per cent make a living in the rural areas in and around the subsistence level. It is generally true that a few individuals own a large share of land and they dominate local politics through their varied roles as land-lords, lenders and employers. Hundreds of thousands of families are struggling to improve their lives through agriculture but they lack secure access to the basis of agricultural life - farmland. Many sell their labour to more fortunate farmers for whatever pittance they can get; others rent land at exorbitant rates under conditions insecure enough to smother incentives for investment and technical progress; still others search what they produce they can from inadequately-produced,

often fragmented family plots in order to make both ends meet. Nepal is one of the poorest countries of the world.

Hence the extent of market is low. The production of industrial commodities is coloured by the demand of the newly emerging elites. On the other hand, the landless the insecure tenants and those owning marginal plots too small to support a family are deprived of basic needs of life - food, fuel, shelter, education, health care and family planning.

It is in this situation industrial development is difficult to achieve. There is neither the effective demand nor the supply. The market is limited. Hence, the allegation that India is mainly responsible for the poor growth of industrialisation in Nepal has to be accepted with caution. The "endogenous" factors are perhaps more important than the "exogenous" factors like the attitude and behaviour of the Indian investors in Nepal. Most of the masses in Nepal who live in the rural areas (about 95 per cent) maintain their livelihood below or near the poverty line. The purchasing power and hence the extent of the market is limited throughout Nepal. Due to such limited domestic market industrial base has remained stagnant. The industries that emerged during the planning period depend on foreign aid, foreign skill and the market of India. In fact Nepal's internal problems like policies of taxation, credit expansion, unscientific pricing, low agricultural development, minimal land reforms, difficult transportation system and limited market and inegalitarian society have been largely responsible for the slow industrialisation process.

It is in this context, Nepal has depended more and more on foreign aid. In the best of Nepalese circumstances, there is no realistic alternative to foreign aid, even though some regarded foreign aid as a "collusion between the national elite and the donors against the people". Nepal is heavily depended upon foreign aid and India is the largest donor.

It is true to suggest that all aids are somehow connected with the political bargaining power of the recipient country. Nepal is no exception. India's aid programme is connected with political stability of Nepal and to strengthen the "democratic forces" in Nepal. For India, Nepal is very important strategically and hence primary objective behind Indian aid to Nepal has been to keep away the kingdom from any inimical power and specially to counteract the Chinese penetration and thus to bring Nepal in India's own sphere of influence.

On the other hand, China wishes to demonstrate that she can maintain friendly relations with Nepal. So Nepal is interested to play one country against the other and extract the maximum from both the countries. So Nepal is receiving aid from both the countries. "It is only natural for the Chinese and the Indians to be interested in the roads connecting Nepal with their own territories and also in those that make a quick push towards' each other's territories. The Indian aid for the construction of the Kathmandu-Raxaul road (Tribhuben Rajmarg) and the Chinese aid for the construction of Kathmandu-Kodari road (Arnoko Rajmarg) can be easily explained in these terms". Foreign

aid in Nepal is indispensable and compelling than it is in. Some other developing countries, politics of aid is mixed up with the economics of development. Further, the Nepalese ruling class has encouraged and decided the priorities largely for reasons of their own internal security and political influence. Nepal, though a small country, can play one country against the other - India against China and vice-versa. Nepal is economically dependent on foreign aid and about 60 to 70 per cent of all Nepal's development expenditures come from foreign aid - most bilateral. Nepal's ruling class is interested to depend more and more upon foreign aid and give priority to road construction so that political control in the distant areas becomes easier. To the Nepalese government the highways developed with the aid have strengthened the strategic and security networks and provided a venue for the extraction of revenues in the form of taxes for the state coffers. The foreign aid has hardly improved the quality of life for the majority of the Nepalese people. Thus, although the people of Nepal have passed through three decades of planning, they are not much benefited. On the contrary, the income distribution has become highly skewed causing deficiencies of primary needs of human life. Majority of the Nepalese people live in the rural areas and almost 94 per cent of the total labour force depend on agriculture to-day as it did earlier. Per capita income in the rural areas of Nepal in 1977 (NEC Survey) were more than two-thirds lower than the urban areas. In spite of nearly forty years of planning the financial resources of Nepal are not

properly developed. A considerable part of the Nepalese economy is at the subsistence level without any surplus for exchange. In the rural areas agricultural output are exchanged as a barter trade for some basic necessities of life. Net revenue falls short of total expenditure and the government of Nepal has to depend upon external assistance to meet even the current expenditure necessary to maintain law and order. The gap between average savings rate and average investment rate in Nepal had been largely bridged through the inflow of foreign aid and external public debt. The tax-GDP ratio in Nepal was only at 7.5 per cent during 1975-80 which ranks her 45th among the 47 nations in terms of tax-efforts so to meet the increasing gap between government revenue and expenditure, the quantum of foreign aid has expanded steadily from Rs.22 thousand in 1951-52 to Rs.25 hundred million in 1983-84. The external public debt as per cent of GNP has increased heavily from 0.3 per cent in 1970 to 14.1 per cent in 1983 and debt-service ratio has reached 0.3 per cent of the GNP and 3 per cent of ~~exports~~ exports in 1983. Inspite of all planning only 32 out of 72 districts are identified as accessible and as many 43 districts suffer from inaccessibility and very low level of development. Under such situation, the vast areas of Nepal are segmented and isolated and there is hardly any interdependence between the areas. These are "pocket economies" and lack the organic linkage with the national economy, especially with Kathmandu where majority of the "elites" live.

"....In terms of development expenditure, a disproportionately large parts of total investment in the last two decades has gone

to Kathmandu valley and the subsistence economies of the hill areas of Nepal is growing similar to the gulf between the development have seen the emergence of a privileged stratum which skims the cream of development opportunities and benefits".

Nepal's uneven regional development which concentrates in the Kathmandu valley and now in the Terai region at the comparative neglect of the mountains and hills has its reflection in its political structure. To quote a Nepali writer - "Hill Communities such as Tamangs, Rais and Limbus are perhaps as poorly represented in the (Nepali) establishment, as say Tharus and Sataras of the Terai. For instance, an ethnic analysis of government positions above under-Secretary level showed the following distribution : these three dominant castes (Chhetris, Brahmans, Newars) are 93 per cent, the other hill groups 2.5 per cent and the terai groups : 3 per cent (in the power structure of Nepal)". This is, however, in stark contrast of the population structure of Nepal. Kathmandu valley has only 4.5 per cent of the total population of Nepal and the Terai districts 34.5 per cent of the total population and the mountains and the hills the rest about 61 per cent of the population. Further, while Kathmandu valley supporting only 4.5 per cent of population has 60 per cent of the total graduates of Nepal and the rest 95.5 per cent of population has 40 per cent of the graduates.

The quality of life has hardly increased inspite of four decades of planning. Less than 15 per cent of total

population was categorised as literates in 1971; however, among males the proportion reached almost 24 per cent while among the females the proportion was less than 5 per cent. Almost 97 per cent of the population aged 6 years and older has no formal education. Among females over 99 per cent fall into this category followed by 94 per cent of the males. The disparity is accentuated further when age is controlled. In the youngest age groups the differences are greatest and throughout the entire age structure the proportion of females in any of the education groups never even reaches the level of 1 per cent.

The distributional pattern of urban population is quite uneven. Out of the total urban population of the country Kathmandu alone comprises 20 per cent. Similarly Biratnagar and Lalipur, the second and the third most populated cities together comprise the next 20 per cent. On the other end of the continuum 15 towns together support a population equal in number to that Kathmandu alone. The pattern of spacing of urban centres is not uniform, the Himalayan region as a whole and the far-western hills did not have a single town with a population of 9000 or more. All facilities seem to be agglomerated in Kathmandu. The absence of well planned rural development programmes and their integration with the urban development strategies of the government of Nepal, only a few urban centres are prospering. Therefore, the pace of urbanisation is even and so the pace of modernisation.

Therefore, there are considerable internal problems of Nepal. This problem is very often reflected in its relation to India - one of the closest neighbours. Very often the ills emanating from the domestic policies are attributed to India. Allegations are made that India is not interested in the industrialisation of Nepal. These charges may be true upto a limit. But problems of Nepal's industrialisation have to be solved by Nepal itself. No foreign country, however proximate it might be, solve the problems of Nepal's industrialisation programme. Nepal's internal situations created by its own planning and political processes are equally to be blamed for poor growth of Nepal's economy. In the successive plans Nepal's dependency on foreign aid have increased. It ranks among the lowest in the proportion of internal resources used for development. Geo-political considerations rather than Nepal's absorptive capacity have largely determined the volume and sources of aid. The distribution of income is highly skewed. There are serious regional imbalances. The fruits of development have been largely usurped by the elites and the intelligent among them. The vast majority live under abysmal poverty.

It is in this situation Nepal wants to diversify her sources of aid and direction of trade. Diversification has resulted in certain peripheral changes. The broad structure of Nepal's ^{economy} ~~economy~~ remains same. Diversification has not resulted in any basic and fundamental change of the Nepalese economy.

In the first fourteen years of planning (1956/57 to 1969/70) India had a dominant share in Nepal's foreign trade. In fact, for all practical purposes, India was the only trading partner as more than 90 per cent of imports and exports were from India. During the same period Chinese contribution did not exceed 0.8% and other overseas countries supplied about 4% of the total Nepalese imports. It is worthwhile to mention that upto 1970 Nepal had virtually no trade relations with other South Asian countries except with India.

But Nepal wanted to reduce her dependence on India and started concluding various trade and aid agreements with countries like China, the U.S.A., the U.S.S.R. and other Western European countries. This diversification policy started to be felt from the late seventies and at the beginning of the eighties India shared only half of Nepal's foreign trade. In spite of this trade deficits with India have increased. In order to have freedom in the currency regulation Nepal did not devalue (1966) when India devalued by about 36.5 per cent. But this policy led to various dislocation in Nepal's economy. In fact this policy led to a period of economic stagnation and Nepal had to devalue to face the reality of the situation.

As part of diversification policy Nepal introduced various schemes like "Gift Parcel Scheme", "Export Exchange Entitlement Scheme" "Bonus Voucher Schemes" etc. These schemes

remained a bone of contention between India and Nepal. The objectives of all these schemes were to increase trade with other countries and not with India. But the complicated system of management led to corruption in a large scale. The schemes "stressed only the geographical aspect of diversification without consideration of commodity diversification. The incentives thus granted also led to a distortion in the country's allocation of resources in a very unforeseen way". These schemes were replaced by Dual Exchange Rate Policy in 1978 and followed two different exchange rates - one valid for India and the other for the rest of countries. Naturally, this system led to corruption and mismanagement. These schemes were substituted by single exchange rate system in 1981 with subsidies to exporters who would export to other countries and not to India. It appears that Nepal is progressing through various trials and errors to reduce her dependence on India. But this policy led to serious distortion and Nepal had to devalue in 1985.

Nepal's attempt to diversify trade did not yield the desired results. For example, the terms of trade deteriorated sharply with the policy of diversification. Trade concentration with India gave Nepal a better terms of trade and diversification led to its worsening. Hence the welfare gains of diversification, purely in economic terms, are not that large as is often presumed. Further, the dual exchange rates and subsidies led to corruption and smuggling on a wide scale.

Trade deficits of Nepal should be a great concern for India because of the fact that such huge gap in bilateral trade, may affect the economic, strategic and political interests between India and Nepal. India has to introduce suitable flexibility in her foreign economic policies vis-a-vis Nepal. This flexibility is conspicuous by its absence. India, being a big neighbour, can always liberalise the terms of trade and transit facilities and also increase the volume of imports from Nepal. India being a relatively big power in the region must not misuse her "dominant" position in trade relation with Nepal. India should use bilateral aid in ways that are as supportive as possible of economic reform and structural adjustments supported by the World Bank and International Monetary Fund. India should try to orient the institutions of Nepal toward efficient use of market and enlargement of market and where feasible to co-ordinate with other donors. India should continue to encourage co-financing and market mechanism which make available greater sums of private money for development on terms that Nepal can prudently sustain. Government action in Nepal, sometimes, have become powerful deterrent to its own private sector.

Nepal wants to reduce her dependence on India. For this Nepal has taken various measures. Indo-Nepal economic relations underlines the problems of relationship between a big country and a small country. History and geography have moulded

a relationship between these two countries which none of them can wish away. If sacrifices have to be made, it is proper that India should do it. This is because India is bigger - many times bigger than Nepal. India should try to assist Nepal, inspite of all hurdles. After all Nepal being a small country has various complexes regarding India - The same is true of various small Latin American Countries with respect to the U.S.A. The relationship between a small country and a big country is a very complex one.

The above stated variable have conditioned the way Nepalese react to international pressures and pulls and pursue its national interests. The developments after the World War Two convinced the Nepalese ruling elite that the days of isolation were over and it must seek its destiny by coming out of it. For obvious reasons the regional context was most important for it. The entire gamut of Nepalese national life is overwhelmingly dependent on South. Nepal has to take India into consideration for everything, and even today the international personality of Nepal stands out mainly in the context of its relations with India. This sense of being gagged by India has given rise to what has been termed elsewhere by me as Claustrophobia, which is reflected in Nepal's international behaviours in a number of ways. It has championed the course of landlocked states in various international forums. It has tried to diversify its trade and aid and reduce dependence on India. It has tried to bring in a number of powers to increase

its options and thus balance India. And above all, it has tried to make use of its contiguity to China. However, it has also to be understood that despite geographical contiguity China is no counterweight to India. And, yet, for psychological reasons China is brought in^{to} to impress India and look more important in the eyes of the southern neighbours. Indeed, it is a national necessity to create some power or bogey of a power in the north. This is reflected in the policy of the Shahs, the Ranes, the democrats, and King Mahendra and Birendra. All have imported problems from north to impress the south. This claustrophobia explains Nepal's relations not merely with India, but also China, Pakistan, Bangladesh, and rest of the world.

While geo-cultural and other constraints are serious enough, politico-economic developments since 1945 blurred Nepal's national identity greatly. Nepalese dependence of the British was only for limited purposes, which increased manifold and almost for every thing on independent India. The sense of utter dependence on India aroused self-pity and became a national concern. This obsession has gone simultaneously with a realization that India alone can play really significant role in Nepal.

Nepal's perception of China is also conditioned by its geographical situation and historical experience. A Nepalese scholar has rightly commented that :

Whatever the Indians do in actual practice is not considered as important as what the Nepalese think the Indians mean. With the Chinese, however, it is a different story. Historically, the Nepalese had ~~to~~ few occasions to become acquainted with the Chinese mind that they are still in the process of observing Chinese overt behaviour between India and China in recent years, Nepali elites are still disinclined to probe into Chinese intent and motives.

Nepalese think that situated well within the Indian defence perimeter a military threat from north cannot be directed against Nepal alone. At best it would be a steppingstone for a further advance towards the south. An invasion of that order is precluded because of the long distance and difficult terrain. This is also their historical experience that the Chinese have not liked to cross the Himalayan ranges militarily, and even in modern times they have detested from going so. Behind this belief there are also formal and informal understanding with India that it would come to Nepal's rescue in the event of a threat from China.

A more likely threat, Nepalese regard, emanates from another source. Situated between the giants there is a possible danger of Nepal's becoming a victim of their rivalry. If it seems to lean towards either of them the other might take steps to restore the balance. This is, of course, more true of India, which has higher stakes in Nepal than China. However, Nepalese understand that even China wants a government in Nepal which would

not allow its territory to be used against the Chinese interests. That is why Nepal has sought its security against China by trying to win over its friendship and by ensuring Chinese interests in the kingdom.

However, from another point of view China assumes great importance in the Nepalese calculations. Given the Nepalese situation China is the only effective source which can be used to scare and restrain India and help the Nepalese search for national identity. They also understand that India is more important in their national development than China; and hence, China has not been brought in as a substitute to India.

From economic considerations Nepalese do look towards Tibet for the restoration of their historical entrepot between north and south.

Admittedly in the Nepalese perception, its relations with India and China are of supreme importance. Yet they have tried to use other South Asian countries, particularly Bangladesh through SAARC to break the hold of bilateralism in its relations with India. This has been so clearly demonstrated recently in negotiations going on between India and Bangladesh and Nepal and India on the use of river waters. Similarly, the Major Powers and international forums have been brought in to buttress the Nepalese independence and increase its options. For example, it is conceivable that Nepal and Bangladesh in SAARC with

other smaller states might have entertained the hope of exercising greater leverage with, the more dominant partner, India, in respect of several unsettled contentions bilateral issues. India, however, anticipating such a move made it quite explicit that such issues could have no place in a regional forum. A clause in the joint communique issued at the end of the First meeting made it clear in no uncertain terms. It was only after a tacit agreement on this point had been reached that India agreed to participate in the regional forum like SARC.

If sacrifices have to be made it is India which should do it and there is no reason to be skeptical about the economic benefits of foreign assistance to Nepal. Foreign assistance can take many forms - from general advice on economic policy by transitory advisers to long term training of individuals and building of institutions; from soft loans or grants to so-called hard loans at market rates. Asking whether Indian assistance really helps Nepal is too general a question. The important questions are whether some forms of foreign aid can assist the process of economic development in Nepal and if they can, how quickly it can be achieved. In fact the case of liberal foreign aid from India to Nepal depends upon concepts such as additionality, catalysis, leverage and infrastructure.

Additionality refers to the notion that for Nepal the extra foreign exchange needed for some useful investments can be

found only outside and mainly in India. Catalysis refers to the idea that even for a country with a reasonable level of domestic savings and openness to foreign investment, the capital for some economically important projects might not be forthcoming without government involvement to pull the project together or to provide a key element. Leverage refers to the concept that donors of aid can educate, encourage cajole or otherwise inveigle the government of Nepal into using investable resources or preferably allowing them to be used more effectively. Infrastructure refers to the importance for development of skilled manpower, of certain types of institutions and of such basic facilities as roads, sewers and water.

Investment in infrastructure is widely held to be an appropriate role of government. Linking remote producers to markets and providing power, communications and education is recognised to be conducive to development. In fact India is doing the same in Nepal for the last thirty years inspite of many ups and downs of the bilateral political relations.

These considerations do not prove that in practice foreign assistance from India is actually effective. They merely suggest that it might be. They do not even suggest, however, that foreign aid from India is the key to economic development. India could pour massive amounts of assistance to no avail into a country hell bent on destroying itself. The economic policies

of Nepal are without question the key to development. Nepal with sound economic policies can benefit from well conceived foreign aid. Nevertheless the fact is that bilateral assistance is likely to remain the bulk of Indian assistance programs for the foreseeable future and that political and strategic consideration will continue to be major factors in allocation. India should endeavour to see that the funds are spent in ways that promote growth that will be lasting, self-sustaining and broadly based.

The essential requirement for economic growth is good economic policies in Nepal. Without that, there is little which aid can accomplish. With good policies, properly conceived aid from India can help to accelerate development. Properly used, aid can help to encourage and support good policies or at least avoid ~~an~~ undercutting them. Nevertheless, there are many pitfalls - pitfalls which are difficult to avoid when political and strategic concerns predominate.