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What drives the foreign investment in Nepal? Investors' perception analysis

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The study aims to identify the motives of foreign direct investment in Nepal and analyse the perceived strengths and weaknesses of investment climate. Additionally, it examines the experience of foreign investors in Nepal in terms of further investment plans and net promoter scores attributed to the host country. The study relies on primary data collected from the survey of 65 sampled industries with foreign direct investment, using structured questionnaires. Descriptive analysis has been used to assess the key factors motivating foreign investors. The findings reveal that labour cost, repatriation facility, industrial security, low operating costs, access to neighbouring market/trade openness, and investment and communal hospitality stand out as major motivating factors, while political instability, macroeconomic instability, availability of machinery and equipment, road access, and bureaucracy are the major precluding factors. The policy reforms in Nepal have notably shaped investors' perceptions. Acts like the Foreign Investment and Technology Transfer Act, 1992, and subsequent amendments such as the Foreign Investment and Loan Management, 2021, have significantly motivated investors by improving repatriation facilities and ease of VISA and work permit accessibility. Despite the efforts, land facilitation for foreign investors has been perceived as a weakness. The net promoter score for Nepal is 12 on a scale from −100 to +100, which is positive, albeit low, indicating a substantial gap to attain full promoters and needs to be improved by further enhancing the investment climate.

Introduction

Foreign direct investment (FDI) has become an important source of foreign capital for many developing countries and played an important role in economic development. Developing as well as emerging countries and countries in transition have increasingly viewed FDI as a vital means to finance economic development and modernisation, income growth, and employment (OECD 2002).

The global competition for FDI intensified, particularly after the tremendous development

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in telecommunication and information technology. Even small countries can compete for FDI by providing sufficiently attractive facilities for foreign investors (Das and Pant 2006). Consequently, most of the developing countries are making strategies to attract FDI inflows. However, the flow of foreign capital is influenced by numerous factors, varying across countries and over time. These factors comprise both political and non-political factors (Büthe and Milner 2008).

Countries are adopting various strategies to compete for foreign capital, recognising the multifaceted nature of the global economic phenomenon. Various types of incentives are offered and policies are revised and designed to attract foreign investment. Many countries have undergone structural reforms and formulated investor-friendly policies, ensuring a higher degree of protection and providing various incentives to make their countries attractive to potential investors (Páez 2011).

Like many other developing countries, Nepal has recognised the potential benefits of FDI and has been actively working to create a conducive environment for FDI since the economic liberalisation in Nepal started in the mid-1980s and accelerated with the start of the 1990s (Shrestha 2017). Economic liberalisation brought several policy changes. Nepal introduced its first foreign investment policy in 1992, officially opening its doors to foreign investors. To support the policy, the Foreign Investment and Technology Transfer Act (FITTA) was enacted in the same year. FDI inflow rapidly increased from 1992 to 1997 but failed to gain significant momentum until 2008. FDI inflows stood at Rs. 1621.0 million (equivalent to USD 28.43 million) in 1997, and took until 2009 to surpass this benchmark with FDI inflows of Rs. 1892.2 million (equivalent to USD 24.61 million) (NRB 2019). Nepal witnessed a remarkable surge in FDI inflows thereafter. Annual FDI inflows to Nepal grew by 203 per cent during the period 2011 to 2021, reaching Rs. 19.5 billion in 2021 (NRB 2022).

In order to appeal to foreign investors, the Government of Nepal (GoN) has been persistently working to attract foreign investment. GoN regularly revises its policies to align with the changing global scenario. Investment summits[1] are being regularly conducted to attract a pool of foreign investors. Similarly, the Investment Promotion Board and Investment Board were established to promote foreign investment. Likewise, a one-stop service centre was established at the Department of Industry (DOI) to provide all services required for investors promptly from a single window and electronically as announced in Budget 2021/22. GoN has embraced policy resilience and has reduced the minimum investment to NPR 20 million from the existing minimum investment of NPR 50 million (MoF 2022). Furthermore, approvals of foreign investments up to NPR 100 million are processed through an automated system (MoF 2022). Additionally, foreign investors can purchase land and buildings in the name of the companies after incorporating the company.

The 15th periodic plan of Nepal aims to attract FDI to mega infrastructure projects and large-scale production in collaboration with local investors (NPC 2020). The plan has set ambitious targets for FDI, aiming for 2.8 per cent, 2.6 per cent, 2.8 per cent, and 3.0 per cent of GDP in 2020/21, 2021/22, 2022/23, and 2023/24, respectively. The target for 2020/21 and 2021/22 in rupees terms roughly translates into NPR 119.76 billion and NPR 126.14 billion, respectively.[2] Consequently, FDI could significantly contribute to Nepal's progress towards graduating to lower-middle income by 2026.

Nepal's efforts to attract FDI are visible, but not remarkable. Nepal has been carrying out investment summits on a regular basis. Various policies are reformed after a long lag. For instance, FITTA was revised after three

[1] Nepal has organised three investment summits; the first investment summit was organised in 1992, while second and third investment summits were organised in 2017 and 2019, respectively.

[2] GDP of Nepal in 2020/21 and 2021/22 is Rs. 4277.30 billion and Rs. 4851.62 billion, respectively.

decades. The one-stop service centre is established to deliver services promptly and reduce hassles, costs, and time for investors. With the advent of Federalism, FDI inflows are increasing but not as expected. Actual FDI inflow is less than 20 per cent of FDI targeted by the 15th plan in 2020/21. FDI conversion has been gradually increasing; however, FDI realisation stood at 37.12 per cent of the pledged amount in the 2010s (NRB 2022). The low conversion rate, ineffectiveness of one-stop service centres, and unwillingness of foreign investors raise concerns about the current policy stances.

In this context, this paper aims to address a critical question: Why are foreign investors reluctant to invest in Nepal despite several policy initiatives? It aims to analyse the investors' perception, including their primary motives for investment in Nepal, the strengths and weaknesses of the investment environment, plans for further investment, and identify net promoter score.

The rest of the paper is structured as follows: Literature review section reviews some of the studies regarding the determinant of FDI in various contexts, Data and methodology section discusses methodology, Results section presents the major findings from the study, and the last section concludes the paper.

Literature review

Exploring the determinants of FDI from the perspective of investors has attracted greater attention of the researchers during recent years as evident in the growing literature on perception surveys. Such surveys have been used to assess the sentiments of foreign investors regarding various dimensions of investment, including economic, political, and legal aspects. Asiedu (2002), Biglaiser and Staats (2010), and Demirbag et al. (2007) highlighted factors such as adherence to the rule of law, political stability, low corruption, and private property rights in their perception surveys. Asiedu (2006) concluded that corruption, weak infrastructure, lack of access to the global market, and political and economic outlook are major investment constraints in sub-Saharan Africa.

Similarly, Biglaiser and Staats (2010) concluded that in case of US corporations in Latin America, adherence to the rule of law, private property rights, high level of political stability, low levels of government restrictions on investments and capital flows, and low level of corruption are major factors. In the case of Turkey, Demirbag et al. (2007) concluded that input quality, comparative cost advantages, and government regulations have a significant impact on perception of affiliates. Interestingly, political risk, financial incentives, and cultural distance do not have an impact on the perception.

The driving factors for FDI depend on various aspects of investment. Dunning (2002) identifies resource-seeking, market-seeking, and efficiency-seeking as common investment motivations. A plethora of literature has explored the motivational factors for FDI with various studies, including Baniak et al. (2005), Fernandez-Arias (1996), Harms and Lutz (2006), Kimura and Todo (2010), and Sekkat and Veganzones-Varoudakis (2007) exploring the determinants of FDI.

The flow of foreign investment into countries varies greatly across the country and time. The political as well as nonpolitical factors affect these flows (Büthe and Milner 2008). Stable political regimes, especially in democratic settings encourage investor confidence, while political volatility can deter foreign investors. Political consistency within democratic regimes generally assures investors about the government's commitment to support the functioning of economic entities (Dutta and Roy 2011). On the other hand, political volatility usually creates an adverse business climate, eroding investors' confidence in the host economy's investment and driving them away (Quazi 2007).

In existing literature, corruption has been a focal point of research. Some studies found that corruption negatively affects FDI inflows (Abed and Davoodi 2000; Drabek and Payne 2001; Habib and Zurawicki 2002;

Sadig 2009). Similarly, Quazi (2014) concluded corruption has adverse effects on FDI inflows in East and South Asia. However, other studies have found no significant impact of corruption on FDI inflow (Wheeler and Mody 1992; Alesina and Weder 2002). Similarly, Iloie (2015) analysed the relationship between FDI volume, CPI, and country risk assessments for Central and Eastern Europe, and Gupta and Ahmed (2018) found no significant correlation between FDI, corruption, and country risk assessments in South Asian countries. The levels of corruption neither induce FDI nor does it impede corruption, indicating that corruption does not matter in the determination of FDI flows in the South Asian countries: Bangladesh, Nepal, India, Pakistan, and Sri Lanka. The enlarging size of the economy stands out as the major motivational factor.

Macroeconomic stability is another critical motivating factor of FDI. A stable macroeconomic environment is favourable for capital accumulation and economic growth. Rising inflation, external debt, and government deficits are assumed to create uncertainty, worsen the business environment, and consequently reduce growth (Demekas et al. 2007). Similarly, stable economic environments with lower inflation and prudent fiscal policies tend to attract more FDI (Hess 2000; Wint and Williams 2002; Ismail 2009). Uncertainty generated by adverse macroeconomic conditions discourages foreign capital and also reduces the productivity of investment (Pruefer and Tondl 2008). High inflation rates in developing countries often coincide with low FDI inflows, emphasising the importance of macroeconomic stability (Sayek 2009).

Developing countries are devout of prerequisites for FDI, including financial developments, trade openness, and infrastructure developments, that restrict absorbing foreign investments and technologies (Hermes and Lensink 2003; Adams 2009; Alfaro et al. 2009; Sayek 2009) and openness to trade also act as a conditional factor for a positive FDI growth nexus (Alguacil et al. 2004; Alguacil, et al. 2002; Balasubramanyam et al. 1999). Quality infrastructures, including communication, electricity, and transportation facilities, also play a crucial role (Easterly 2001; Li and Liu 2005). Institutional system plays a crucial role in making investment decisions. Factors like property rights, rule of law, legal traditions, trust between individuals, democratic accountability of governments, and human rights impact FDI where the institutional system plays a role as a main attractor of FDI (Easterly 2001).

Shah (2013) on FDI determinants in Bangladesh and Mahbub and Jongwanich (2019) on firms conducting FDI in the power sector have identified determinants of FDI. The 10 determinants of FDI in Bangladesh are market size, economic environment, growth, trade performance, competitiveness, labour costs and productivity, infrastructure, political risk, tax, and regulatory policies. For individual factors, the government's commitment to contracts, land acquisition, and tax exemption are key decision-making factors, while road networks, gender diversity policies such as male predominance, and the right to freedom of association such as trade unions are considered the least important. Firm-level characteristics, including firm ownership, firm size, and contract period, are important in ranking the determinants of conducting FDI.

Other studies such as Harms and Lutz (2006), Kimura and Todo (2010), and Wheeler and Mody (1992) have reached similar conclusions that infrastructure, labour cost, availability of skilled labour, incentive factors, political risk, and economic factors are the major determinants of FDI. Moreover, studies focusing on FDI and political factors, including Abed and Davoodi (2000), Dutta and Roy (2011), Quazi (2007), and Sadig (2009) also have reached similar conclusions.

In the case of Nepal, Pant and Sigdel (2004) and UNCTAD (2003) conducted a perception survey to uncover the factors that motivate investors to invest in Nepal. Both of the studies have similar findings. Investment profitability, ability to repatriate, cheap labour, and market opportunities are pronounced as the motivating factors, while political instability, legal barriers, and corruption are the major hindering factors. Majority of national literature, including Adhikary (2015), Bista (2017), Jha et al. (2013), Phuyal and Sunuwar (2018), and Purbey (2019), attempts to examine the key determinants of FDI from macroeconomic perspectives.

After the recent reforms in foreign investment-related provisions including the amendments in the foreign investment act and related procedures, labour market reforms, and other policy initiatives of the government, no studies have been done regarding how the changes affected the perception of the foreign investors, This paper attempts to fill the gap through a perception survey by including the perception on the investment climate factors such as labour factors, input factors, infrastructure factors, governance factors, and foreign investment facilities. It also attempts to analyse the motives, strengths, and weaknesses of the investment climate as perceived by foreign investors in Nepal.

Data and methodology

Sample and data collection

We adopted a qualitative approach, which analyses the perceptions of the respondents using tools such as frequency and percentage. We started with the development of a questionnaire and collection of primary data on investment motives and perceptions of the investment climate in Nepal. This type of research design is often used in perception studies. We obtained the final qualitative data through interviews across four sectors: manufacturing, information technology, service, and tourism.

The survey administered in 2020 covered FDI industries under commercial operation[3] registered at the DOI up to FY 2018/19. It focused on the four major sectors mentioned above, excluding FDI in hydropower.[4] Using the list of 913 industries representing four sectors, we determined a sample of 65 firms using the Taro Yamane method by Yamane (1967). The sample size for all sectors is calculated separately for each sector. The sector-wise samples were proportionally divided into four sectors. The survey team selected random, diverse, and representative samples of 7 IT-based industries from 97 industries, 22 manufacturing industries from 305, 19 service industries from 273, and 17 tourism industries from 238 industries. Out of the sample industries, 13 industries entered the Nepali market before 2010 and the other 52 industries entered between 2010 and 2019. In addition, 32 industries had an investment of Rs. 10 million or less, 16 had an investment of Rs. 10–50 million, 8 had an investment of Rs. 50–100 million, and the rest 9 had an investment of Rs. 100 million and above. In terms of employment, 39 industries had an employment size up to 50, 8 industries had employment size between 50 and 100, 11 industries had employment size between 100 and 500, and 7 industries had employment size of 500 and above.

The questionnaire structure was designed based on an extensive literature review, primarily based on an investment survey conducted by Kudina and Jakubiak (2009), Loewendahl and Gutierrez (2013), and the World Bank Group (2018). Before administering it in the survey, we conducted a pilot test and fine-tuned the questionnaire. We conducted face-to-face interviews with foreign investors and authorised representatives of the industries to gather valid information. The respondents were senior executives and managers, such as Directors (23 per cent), General Managers (22 per cent), Managing Directors (17 per cent), CEOs (11 per cent), CFO (9 per cent), and other senior managers (18 per cent), actively involved in the internationalisation process of investment and management. Among the respondents, 72 per cent were

[3] While issuing industry registration certificates to the industry, DOI outlines fixed duration years as per category of industry under which industry must start its commercial operation and notify DOI regarding commencement of its commercial operation.

[4] Hydropower sector attracts huge FDI inflows but in small numbers, so we proposed to exclude hydropower sector.

foreign investors themselves while 28 per cent were industry representatives. The country-wise representations of the sample industries were the USA (21.5 per cent), China (16.9 per cent), India (10.4 per cent), Japan (9.2 per cent), United Kingdom (6.2 per cent), and 15 other countries representing less than 5 per cent each.

Motivation and investment climate factors to examine the perception

Prior literature has identified factors used to examine the perception of foreign investment climate. We adopted the framework used by Kudina and Jakubiak (2009), Loewendahl and Gutierrez (2013), and the World Bank Group (2018), which are survey research methods that analyse perceived motives for FDI. We categorised investment climate factors into labour factors, input factors, infrastructure factors, governance factors, and foreign investment facilities to analyse the motives, strengths, and weaknesses of the investment climate as perceived by foreign investors in Nepal.

Labour-related factors include the cost of labour, supply of skilled labour, and labour regulation. Input factors encompass the availability of raw materials, machinery and equipment, and access to electricity. Infrastructure-related factors include road access, transportation logistics, ICT infrastructure, industrial infrastructure, and construction permits. Governance factors comprise political stability, macroeconomic stability, communal hospitality, bureaucracy, access to domestic financial institutions, and rule of law. Similarly, market factors include domestic market and access to international market/trade openness. Foreign investment policy provides facilities such as repatriation, foreign currency exchange facility, Visa and work permit facilities, Double Tax Avoidance Agreement (DTAA), bilateral and multilateral agreements, industrial security, land facilitation, national treatment, one-stop service facility, and intellectual property rights protection (trademark, design, and patent).

Similarly, to examine the experience of foreign investors in Nepal, future plans on production level and net promoter score to the host country have been analysed. Future plans for production level in Nepal in the next 12–24 months have been analysed based on investors planning for production expansion or diversification, planning for the same level of production, or planning for exit due to growth constraints. The net promoter score (NPS) assesses the extent to which a respondent would recommend a certain company, product, or service to their friends, relatives, or colleagues (World Bank Group 2018). Based on the existing literature, we developed a NPS by subtracting the promoters with detractors ratings in four sectors. Respondents were asked how likely they were to recommend investing in Nepal to a friend or a colleague, using a scale from 0 to 10. The NPS is calculated as the difference between the percentage of promoters and detractors (World Bank Group 2018). Depending on the score, respondents are categorised into three groups: promoters (score 9 or 10), passive (score 7 or 8), and detractors (score from 0 to 6) (World Bank Group 2018). Moreover, we calculated sector-wise NPS and an overall NPS for Nepal based on the four sectors to analyse investor satisfaction with the investment climate in Nepal.

Results

Table 1 presents the investment and employment structure of the sample industries. Actual and committed amounts in both investment and employment is used to compute the realisation ratio in all sectors.

The contribution in total actual investment is highest in the service sector (56.93 per cent) while the percentage contribution in actual employment is highest in the IT sector (48.94 per cent). The highest investment realisation ratio is observed in the manufacturing sector (0.96) and the highest employment realisation ratio is seen in the IT sector (2.63). The lowest investment realisation ratio is seen in the

Table 1
Investment and employment in sample FDI industries under operation

Sectors	Committed investment (billion NPR)	Actual investment (billion NPR)	Investment realisation ratio	Percentage contribution in total actual investment (%)
Manufacturing	3.83	3.68	0.96	36.24
Information technology	0.34	0.23	0.69	2.29
Service	6.14	5.78	0.94	56.93
Tourism	0.72	0.46	0.64	4.54
Total	11.03	10.15	0.92	100.00
Sectors	**Employment commitment (numbers)**	**Actual employment (numbers)**	**Employment realisation ratio**	**Percentage contribution in total actual employment (%)**
Manufacturing	2350	3465	1.47	29.65
Information technology	2177	5719	2.63	48.94
Service	1476	1993	1.35	17.06
Tourism	692	508	0.73	4.35
Total	6695	11,685	1.75	100.00%

Tourism sector (0.64) and the lowest employment realisation ratio is also seen in the Tourism sector (0.73).

Table 2 presents the size of the sample industries in each sector by scale (or size). In the overall sample, 14.3 per cent of the industries are large industries, 11.1 per cent are medium industries, and 74.6 per cent are small industries. In the tourism and service sector, most of the sample industries are small, which is in line with the number of total industries registered in those sectors.

Table 2
Scale of the sample industries

Sectors	Scale		
	Large	Medium	Small
Manufacturing	43.7	6.3	50.0
IT	12.5	6.3	81.3
Service	0.0	12.5	87.5
Tourism	0.0	20.0	80.0
Overall	14.3	11.1	74.6

Perceived investment climate of Nepal

Strengths and weaknesses of the investment environment in terms of labour, input infrastructure, governance, market, and foreign investment policy factors have been recorded by the perception survey. Figure 1 shows the perception revealed by investors on foreign investment policy. Investors reveal that the repatriation facility, VISA and work permit facility, national treatment, and one-stop service facility are strengths and motivating factors for investment in Nepal for the majority of the investors. Results show that Foreign Investment Policy 2014 and FITTA 2019 have played a significant role in shaping this perception. On the contrary, land-related policy still needs to be revised as a significant share of investors consider it as a constraint to invest as land facilitation is not perceived as a strength. However, the majority of investors are neutral in this case.

Figure 2 shows the investors' perception on labour factors. Investors perceive that the cost of labour is a strength of the Nepalese economy and is one of the motivating factors for foreign investors to invest in Nepal. The average yearly income earned by Nepalese workers is Rs. 213,708 (equivalent

Figure 1
Perception on facilities provided by foreign investment policy

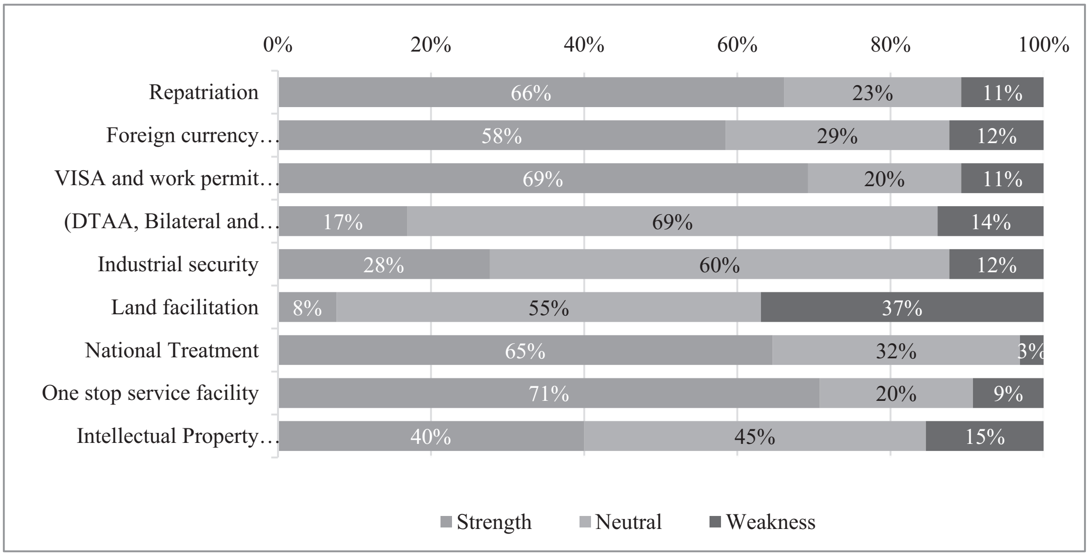
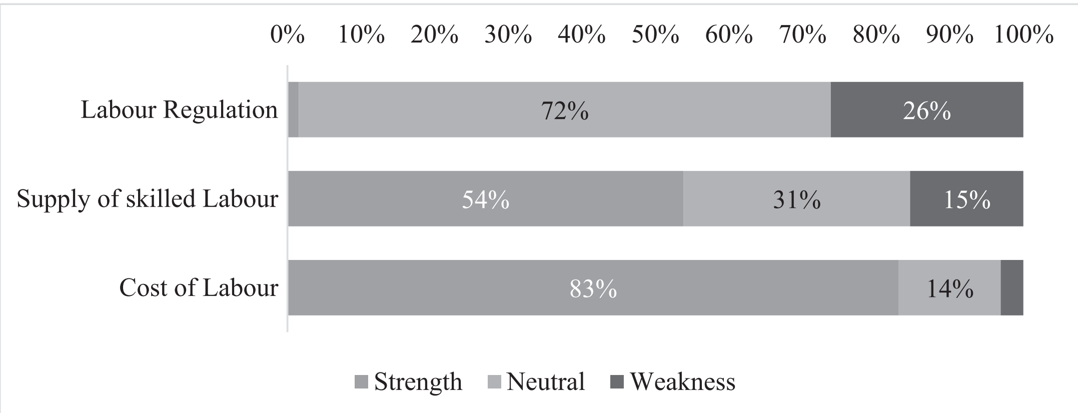


Figure 2
Perception on labour factors



to USD 1955[5] approximately), which also reveals the low cost of labour in Nepal (CBS 2018). However, the lack of proper labour regulation is a major hindrance to foreign investment in Nepal. About 26 per cent of the investors perceive labour regulation as a weakness.

In terms of the input factors, access to electricity and availability of raw materials have been perceived to be strengths (Figure 3).

[5] 1 USD = NPR 109.88. Average of buying and selling rate.

Figure 3
Perception on input factors

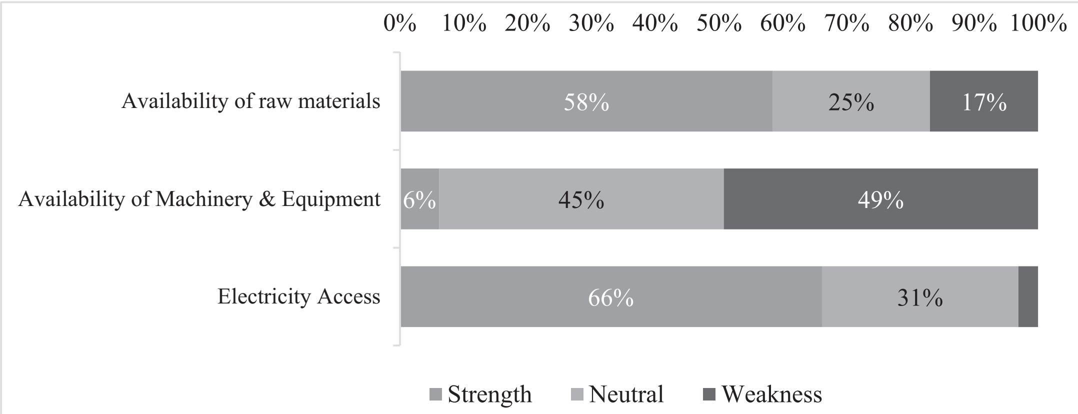
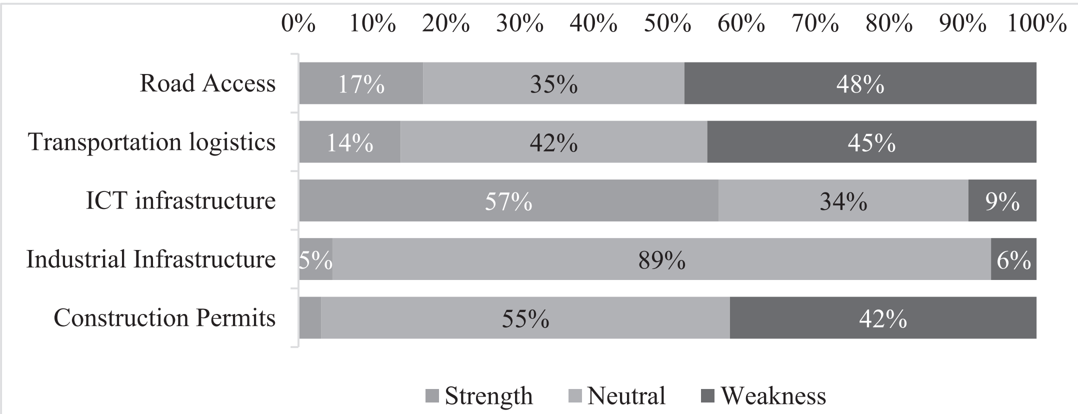


Figure 4
Perception on infrastructure factors



Industrial load shedding in Nepal ended in early 2018 (World Bank 2019b); consequently, the majority of investors perceive electricity access as a strength. Investors consider non-availability of machinery and equipment as a weakness. It implies that the GoN should focus on enhancing the availability of machinery and equipment.

More than half of the investors (57 per cent) perceive ICT infrastructure as a strength while a significant per cent of investors perceive difficulty in road access and transportation logistics (Figure 4). Such perception is consistent with World Bank (2019a) which concludes that Nepal does not have reliable and adequate access to infrastructure services. This implies that the GoN should prepare a national transport master plan, allocate sufficient budget to projects, and control the huge time and cost overruns.

Figure 5 shows the investors' perception on governance factors. More than 60 per cent of investors perceive political instability and macroeconomic instability as weakness, while they perceive communal hospitality as strength. Likewise, cumbersome bureaucracy and lack of proper rule of law too are the major hurdles to investors. However, policies aimed at enhancing financial access in the domestic market seem effective as investors perceive access to domestic financial institutions as a strength. Only a small portion of investors perceive bureaucracy and rule of law as strength, which is consistent with the findings by Shrestha (2019), which points out that weak public institutions and service delivery is one of the key challenges of governance in Nepal.

Investors are optimistic regarding the access to the market. More than 50 per cent of the investors perceive domestic as well as international markets as strength (Figure 6). Nepal is a good place for investors in terms of both the domestic market as well as the international market. Given the low penetration of foreign investment in the country and increase in consumption supported by remittance inflows, investors might have taken the increasing domestic market size as one of the strengths. This shows that access to market or market size is not the factor that demotivates foreign investors from investing in Nepal.

Labour cost, repatriation facility, VISA and work permit facility, and domestic market size are the principal motives of FDI in Nepal. However, investors perceive the ineffectiveness of trade agreements, one-stop service facilities, intellectual property rights protection, development of industrial infrastructure, and tax regimes. It shows that the GoN should focus on developing robust industrial infrastructures, make arrangements for land facilitation, and ensure the availability of raw materials.

Motives of foreign direct investment in Nepal

The principal motives for investors choosing Nepal for their investments are in this section. Figure 7 illustrates the principal drives/reasons for investment decisions in Nepal. The most frequently cited motives for foreign investment in Nepal include labour cost (89 per cent), repatriation facility (85 per cent), visa and work permit facility (83 per cent), and domestic market size (83 per cent). Similarly, 77 per cent of the surveyed industries

Figure 5
Perception on governance factors

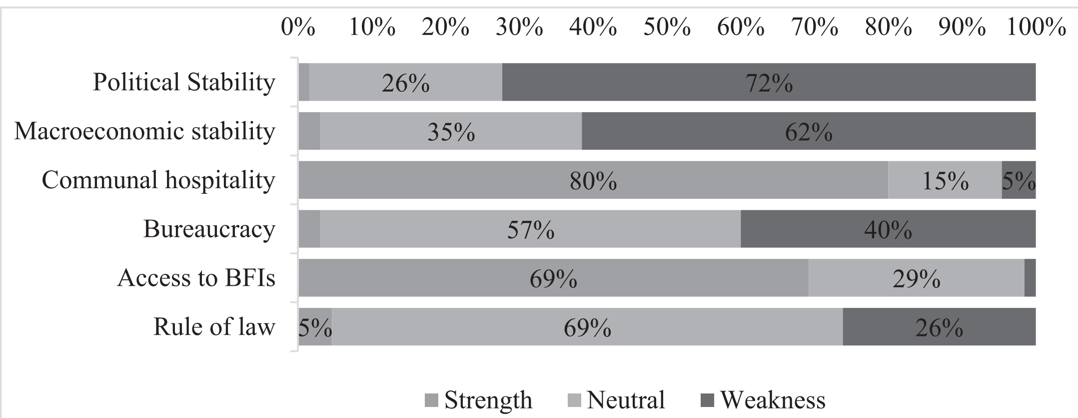


Figure 6
Perception on market factors

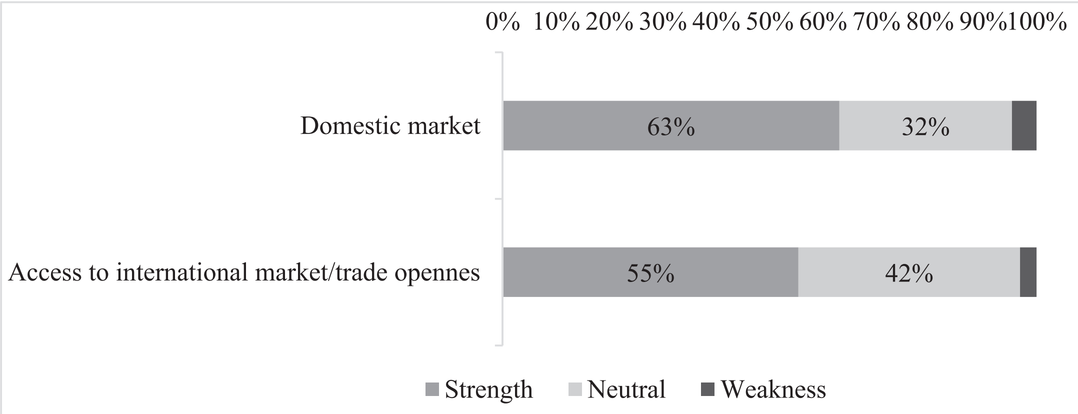
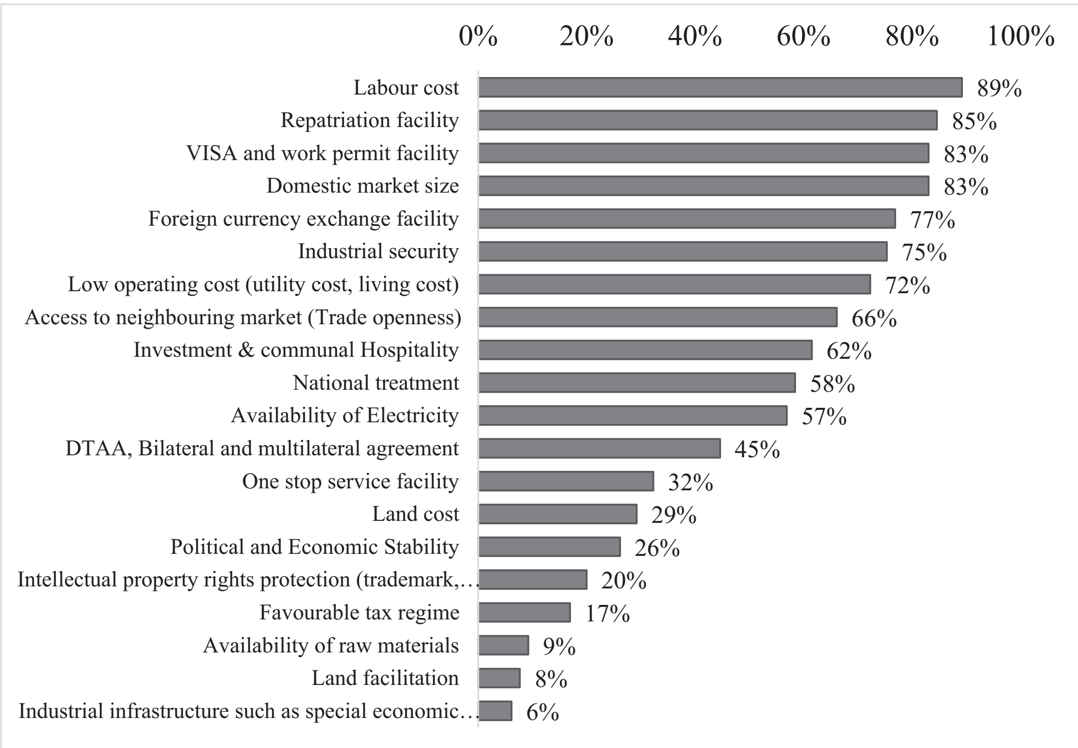


Figure 7
Principal motives of foreign direct investment in Nepal



mentioned that foreign currency exchange facilities were key reasons for investing in Nepal, followed by industrial security (75 per cent), low operating cost (72 per cent), access to neighbouring markets, and trade openness (66 per cent), investment and communal hospitality (62 per cent), national treatment (58 per cent), and availability of electricity (57 per cent). Majority of foreign investors are attracted to invest in Nepal foreseeing the growing connectivity with India and China, which are one of the world's largest markets. While the majority of investors perceive the one-stop service facility as a strength of FDI, only 32 per cent of these investors perceive it as a principal motive. One-stop service facility came into operation in July 2019. Therefore, investors have perceived it as a strength with the expectation of gradual improvements in this facility. Thus, the departure between perception and actual motive is plausible.

Further investment plans

In this section, we discuss the future plans of the industries regarding the production level in Nepal over the next 12–24 months. As shown in Figure 8, more than 36 per cent of industries are planning to expand or diversify their production, while 55 per cent of the industries have plans to maintain the same production level. Additionally, it is also observed that 9 per cent of the sample industries are planning to exit due to growth constraints.

Figure 9 provides a sector-wise breakdown of expansion plans. The manufacturing sector is the largest, with 59 per cent planning expansion, followed by the IT sector (31 per cent) and the service sector (31 per cent). However, it is also observed that 18.8 per cent of the tourism sector firms are considering exiting due to growth constraints, followed by the IT sector (13 per cent) among the sample industries.

Net promoter score

As illustrated in Table 3, Nepal's NPS is found to be 12 on a scale from −100 to +100. Among the overall sample of surveyed industries, 40 per cent are likely to recommend

Figure 8
Expansion plans of sample industries

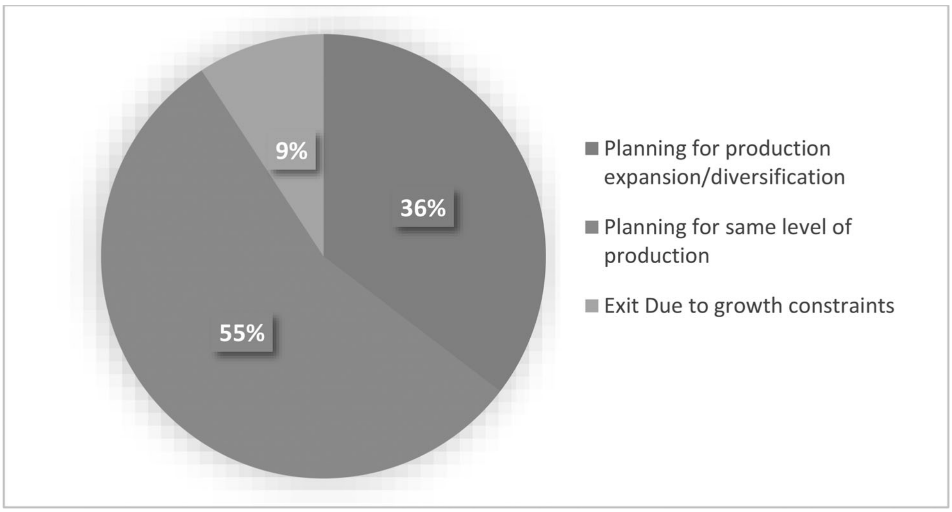


Figure 9
Expansion plans in sector wise sample industries

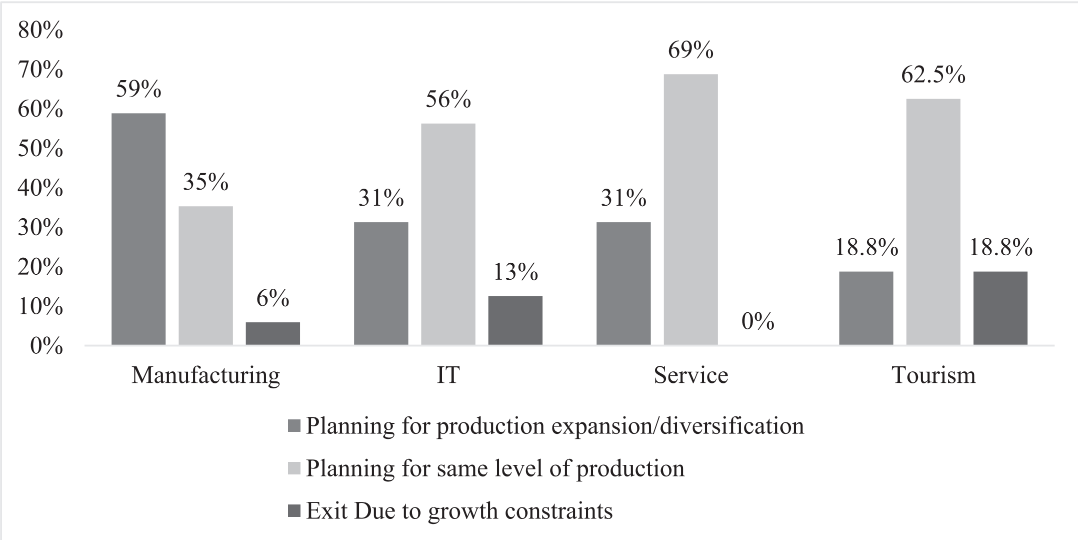


Table 3
Nepal net promoter score (NPS) score

Sectors	NPS = promoters% − detractors%	Promoters (9–10)	Passive (7–8)	Detractors (1–6)
Manufacturing	18	41%	35%	24%
IT	19	50%	19%	31%
Service	6	38%	31%	31%
Tourism	6	31%	44%	25%
Overall sectors	12	40%	32%	28%

prospective foreign investors to invest in Nepal, while 32 per cent are passive, and 28 per cent are detractors who are unlikely to recommend. A positive NPS indicates that investors in Nepal generally report satisfaction with their investment experience and that there are more existing investors likely to promote Nepal for investment than to deter other investors. The highest NPS, 19, is observed in the IT sector, followed by the manufacturing sector with a score of 18. Meanwhile, the lowest NPS score of 6 is observed in both the Service and Tourism sectors. Therefore, industries in the IT sector and manufacturing sector are more likely to be recommended as investment destinations compared to the service and tourism sectors as of the study period.

Policy reform and its impact on investor's perception

Foreign Investment and One-Window Policy was introduced in 1992, which aimed to boost FDI in the country. The one-window policy for investors was introduced to expedite administrative processes such as approvals, facilities, and other administrative services for investors. Additionally, the revised Foreign

Investment Policy 2014 focused on strengthening the investment board and promoting foreign investment, particularly in the establishment of a one-stop service centre, and in technology-driven, environmentally friendly industries.

To further support foreign investment and streamline the processes, the GoN introduced the FITTA in the same year. FITTA aimed to facilitate the repatriation of funds received from the sale of foreign investment shares, enhancing the ease of investing in Nepal. It also offered industrial security to foreign industries on par with domestic industries, fostering a sense of security among investors.

In 2019, the Public-Private Partnership (PPP) and Investment Act was introduced with the goal of fostering collaboration between the public and private sectors for sustainable development. This act not only established mechanisms for PPP but also aimed to facilitate through the creation of a one-stop service centre. The act also introduced the concept of Viability Gap Funds (VGFs) and project preparation facility funds. Moreover, the GoN supported the development of credit flow mechanisms for long-term financial sources required for the private sector to make investments in physical infrastructure and services. The revised PPP Act, 2018 further aimed to provide a one-stop service centre at the office and establish the VGF for the construction, operation, and expansion of the projects that yield positive returns.

In addition to these acts and policies, the Industrial Enterprise Act 2020 came into effect in order to build a dynamic and robust economy. The act sought to create an industry-friendly environment with a focus on import substitution and export promotion. It incentivised investments with over NPR 1 billion and created direct employment to more than 500 people throughout the year, offering substantial income tax exemptions (100 per cent) for the first five years, and 50 per cent exemptions for the subsequent three years. Similarly, the tourism industry with an investment of more than NPR 2 billion, offers 100 per cent income tax exemption for the first five years and a 50 per cent exemption for the next three years. The revised act has even brought more opportunities for the investors, an exemption of 20 per cent on tax to be levied on income earned and an additional 5 per cent of the rate of tax to be levied on income earned by exporting its products, a 25 per cent exemption on the rate of income tax to be levied on royalty income earned from exporting an intellectual property right. Moreover, an industry producing intermediate goods used for the industrial goods to be exported is entitled to a refund of the customs duty paid by that industry on the produced goods based on the quantity of export.

Furthermore, the Foreign Exchange Act came into effect to smoothen the investment in foreign currency. It allowed foreign individuals investing in Nepalese stock to repatriate profits, dividends, and interest abroad. The act also enabled the transfer of securities owned by foreign individuals, firms, or institutions that paid taxes in foreign currency.

These policy reforms have significantly influenced investor decisions to invest in Nepal. The introduction of various policies and acts has significantly impacted the perception of foreign investors in Nepal. The Foreign Investment and Technology Act, 1992 has motivated investors, particularly regarding repatriation facilities, VISA and work permit accessibility, and the establishment of the one-stop service centre. Subsequently, the Foreign Investment and Loan Management, 2021 enhanced the repatriation facility, further motivating the investors.

The policy reforms also included the provision of land facilitation for foreign investors. However, this has been perceived as a weakness. Furthermore, the Industrial Enterprise Act and Industrial Policy provided industrial security to foreign industries and ensured national treatment, enhancing investor motivation. Tax incentives, however, motivated only a small percentage of investors.

The policy reforms have played a vital role in influencing investor perception. Table 4 summarises the impact of these policy reforms on investor perception.

Table 4
Policy reforms and investors' perceptions

Act/Policy	Point	Perception	Remark
Foreign Investment and Technology Transfer Act	A foreign investor can repatriate: (i) The amount received by the sale of the share of foreign investment as a whole or any part thereof. (ii) Amount received as profit or dividend. (iii) Amount received as a principal of and interest to any foreign loan.	66 per cent of investors perceive repatriation facilities as strengths. 85 per cent of investors are motivated to invest due to easy repatriation.	Foreign Investment and Loan Management By Law 2021 provided more leverage to the repatriation facility.
Foreign Investment and Technology Transfer Act	Foreign investor making an investment in an amount no less than one hundred thousand USD or in convertible foreign currency and his family shall be granted a residential visa until such investment is retained. Non-tourist visas not exceeding six months shall be granted to a foreign citizen who visits Nepal to make a study, research or survey for foreign investment.	69 per cent of investors perceive VISA and work permit facilities as a strength. 83 per cent of investors are motivated to invest due to easy VISA and work permit facility.	FITTA has eased foreign investors in obtaining a VISA and work permit.
Foreign Investment and Technology Transfer Act	Services to be provided through single-stop service centre (new).	71 per cent of investors perceive one-stop service centre as a strength.	Government of Nepal must enhance the efficiency and thereby enhance the effectiveness on one-stop service centre.
Foreign Investment and Technology Transfer Act	Foreign investors shall have to manage land by purchasing it on their own. Foreign investment approving bodies shall make necessary recommendations, coordination, and facilitation in case the investor is unable to purchase land or requires land excess of the ceiling (new).	37 per cent of investors perceive land facilitation as a weakness.	The Government of Nepal should welcome foreign investment by assuring land facilitation. Moreover, the Land Acquisition Act 1977 (amendment 2010) empowers the government to acquire land for any public purpose and sets out procedures for determining compensation and for appeal.
Industrial Enterprise Act/Industrial Policy	Government of Nepal provides industrial security to any industry.	60 per cent of the investors are neutral in case of industrial security. However, due to industrial security, 75 per cent of investors are	Policies empower the government to form industrial security forces and provide security to industries.

(Continues)

Table 4
Continued

Act/Policy	Point	Perception	Remark
		motivated to invest in Nepal.	
	National treatment to the management, maintenance, use, transfer, and sale of any foreign investment made in Nepal is no less favourable than that accorded to any investment made by a Nepali person (new).	65 per cent of investors perceive that national treatment as the strength. 58 per cent of investors invest in Nepal due to national treatment.	UNCTAD (2003) also concluded that no discrimination between domestic and foreign investment appears.
	An investment with more than 1 billion by providing direct employment to <500 throughout the year is provided 100% income tax exemption for the first five years and 50% exemption for the next three years.	Only 17% of investors are motivated to invest in Nepal due to the tax regime.	Tax rebate and concession are available at the cost of a huge investment. The investment cap must be reduced to motivate investors.
	Tourism industry with an investment of more than 2 billion Nepalese Rupees is entitled to 100% income tax exemption for the first five years and 50% exemption for the next three years.		
	Permission may be granted to an industry in operation with foreign investment to import goods produced by its principal company abroad for a certain period on such terms and within such ceiling as prescribed, for development and promotion of the market for new goods.		

Discussion

The primary objectives of the paper are to examine the foreign investment climate of Nepal as perceived by foreign investors and to understand the motives driving foreign investment. Additionally, the study aims to assess the strengths and weaknesses of Nepal's investment climate and examine the experiences of foreign investors including their future investments.

The survey of the industries has revealed important insights. The primary motives for FDI in Nepal are found as labour cost, followed by repatriation facilities, Visa and work permit facilities, and domestic market size. Furthermore, 77 per cent of the sample industries considered foreign currency exchange facilities as key reasons to invest in

Nepal, with industrial security, low operating costs, and access to neighbouring markets and trade openness also playing significant roles.

These findings support the observations by UNCTAD (2003), which also identified the ability to repatriate capital and earnings, low cost of doing business, low labour cost, and the size of local markets as primary driving factors of investment in Nepal. Moreover, the perception analysis of investors regarding the foreign investment climate in Nepal identified major strengths, including labour cost factor, communal hospitality, one-stop service facility, Visa and work permit facility, access to domestic financial institutions, electricity access, repatriation options, national treatment, market size, and international market/trade openness.

On the other hand, the survey unveiled several weaknesses within Nepal's investment climate. Mostly governance factors, such as political stability, macroeconomic stability, rule of law, and bureaucracy efficiency were found as constraint factors. Additionally, infrastructure-related factors, including road access, construction permits, transportation logistics, land facilitation, and industrial infrastructure, posed significant challenges. Availability of machinery and labour regulation factors are also perceived as weak factors. These findings are consistent with ILO (2017) which points out corruption, accountability, transparency, rule of law and enforcement of property rights, and good governance as the main challenge for attracting FDI in Nepal. The study, in line with this paper, suggests improvement in infrastructure to address the geographical barrier. In addition, it is supported by the findings of Adhikari (2013), which found political instability, poor infrastructure, and labour union militancy as major determinants of long-term foreign investment in Nepal. Furthermore, Pant and Sigdel (2004) identified undeveloped infrastructure, corruption, political instability, and bureaucratic hurdles as principal problems in promoting FDI in Nepal.

World Bank (2019c) points towards some other issues besides the improvement in governance and infrastructure including amendments in laws, procedural simplification in FDI approval, repatriation facility, conflict resolution and others. Most of these have been addressed by the amendments in the foreign investment and other related acts, establishment of one-stop facility, and policy initiatives of the government as well as the Central Bank. This might be the reason for the optimistic picture of the perception survey in contrast to World Bank (2019c).

The survey shows that 40 per cent of the investors are likely to recommend Nepal as a suitable destination, while 32 per cent were passive, and 28 per cent were detractors, unlikely to make such recommendations. As a result, Nepal's NPS has been found to be 12 (difference between the percentage of promoters and detractors) on a scale from −100 to +100. While this score is positive, it indicates that there is a substantial gap in achieving support from promoters who endorse Nepal as a favourable FDI destination. A comparison with a similar survey conducted by the World Bank Group in Rwanda in 2018, resulted in an NPS score of 31.2. A relatively high value of Rwanda's NPS is reflected in FDI inflow data published by UNCTAD in 2020, which reported FDI inflows of 420 million USD in Rwanda compared to Nepal's 185 million USD in 2019.

Conclusion

The perception analysis has provided valuable insights and offered significant policy implications. The survey has identified a range of motivations or demotivation to foreign investment in Nepal. The presence of resources seeking motives is significant. Notably, labour cost, and low operating cost play a significant role in attracting investment, while land cost is still a challenging issue. Similarly, a significant market-seeking motive is observed, with an orientation on domestic market size and access to neighbouring market/trade openness, as a key motivator for investment. Similarly, efficiency-seeking motivations, indicated by the importance of policy incentives such as repatriations facilities, visa and work permit facility, foreign currency exchange facility, industrial security, national treatment and DTAA, bilateral and multilateral agreement, serve as motivations to FDI.

Conversely, several challenges and deterrents have been identified, including governance and infrastructure factors. Investors perceived significant challenges associated with political instability, macroeconomic instability, rule of law, and bureaucratic hurdles. Infrastructure-related issues, encompassing poor road access, construction permits, transportation logistics, land facilitation have been major demotivates to invest. This shows poor institutional quality, as observed in the majority of developing countries, has been a major obstacle to foreign investment inflows in Nepal.

However, the NPS for Nepal is positive, with 40 per cent of surveyed industries likely to recommend prospective foreign investors to invest in Nepal. 32 per cent are passive and 28 per cent detractors. Nepal's NPS was found to be 12 on a scale from −100 to +100. This suggests that there is an opportunity to improve and further enhance the investment climate. However, there exists a large gap in attaining full promoters which needs to be fulfilled by further enhancing the investment climate.

These findings offer a set of policy implications for enhancing Nepal's foreign investment climate. Establishing good governance practices can create an environment conducive to FDI. Second, mobilising resources to develop modern infrastructure and enhance transportation connectivity, including internal and international cargo industries, is essential. Similarly, regular tripartite dialogues between industry, employee union, and labour office can improve the labour market barrier and foster a more attractive investment environment.

The survey also shows the need to enhance the NPS, which although positive, indicates room for improvement in the investment climate. After-care services, particularly in sectors like tourism and services, can contribute to this improvement. Transparency and simplification measures include making standard operating procedures available online, providing clear formats for document submissions, and ensuring the availability of human resources for efficient one-stop service operations. The implementation of an integrated digital automation system, reducing approval time lags, and streamlining foreign investment recording can further expedite processes and reduce bureaucratic burdens.

In addition, coordinated land facilitation, the issuance of investor identity cards, follow-up services, and facilitating contract manufacturing and the establishment of unit industries can significantly enhance Nepal's attractiveness as an FDI destination. Contract manufacturing and ease of setting unit industries should be allowed for forward and backward linkage to the main industry. Instead of the current provision which requires a long process of registering a unit industry separately, there should be provision of a single industry registration system with unit industries being mentioned in a single industry registration certificate.

Author contributions

Rohan Byanjankar: Software; data curation; formal analysis; visualization; writing – review and editing; validation. **Pujan Adhikari:** Conceptualization; methodology; data curation; writing – original draft; formal analysis. **Surya Subba:** Data curation. **Siddha Raj Bhatta:** Methodology; writing – review and editing; formal analysis; validation. **Prayush Man Shrestha:** Data curation.

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