

## China's Growing Footprint in Nepal: Challenges and Opportunities for India

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**ABSTRACT** China is extending its hand to Nepal, India's Himalayan neighbour, which for its part is understandably attracted to the prospects that are emerging on its Northern front. How does China's expanding footprint in Nepal affect India? This brief examines the possibilities for India's success in competing with China in Nepal, and posits two overarching factors: New Delhi's overall capacity to challenge China, and India's political will to address its own controversial approaches towards Nepal. It argues that in the changing geopolitical context, a strongly sovereign Nepal that can exercise an independent foreign policy is beneficial, and not detrimental to India.

*(This Issue Brief is part of ORF's series, 'Emerging Themes in Indian Foreign Policy'. Read all the papers in the series here: <https://www.orfonline.org/series/emerging-themes-in-indian-foreign-policy/>)*

### INTRODUCTION

Nepal is the world's 45th-biggest country in the world, with a population of 29 million people.<sup>1</sup> The country's total area is almost equal to that of Bangladesh and is double Sri Lanka's.<sup>2</sup> Thus, if only for its size, Nepal is too big a nation-state to be a vassal. The country takes pride in its history of never having been colonised and has an important geostrategic

position, with India and China on either side. However, contrary to conventional notions of a harmonious diplomatic relationship, there is a sharp difference in the way Nepal and India view each other.<sup>3</sup>

Following Independence, India emulated Britain's approach<sup>4</sup> in having a treaty-based

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relationship with Nepal, which led to Nepal's grudging acceptance of India's dominion. Nepal's ruling elite—particularly the monarchy that was emboldened by the West in the context of the country's privileged geostrategic credentials during the Cold War—were of the view that India did not treat Nepal as per the spirit of a “special relationship.” Ignoring Nepal's reservations, India managed to keep the Himalayan nation in its fold for several decades. The Indian establishment saw this as a success of its policies that yielded a stable relationship with its “little brother.” However, in the post-Cold War era, it was not India but Western institutions and non-governmental organisations (NGOs) that took the lead in keenly watching Nepal's governance. Now, with China making inroads into the new republic, India's success may be rendered unsustainable.

To be sure, China's engagement in Nepal is not new. More importantly — and contrary to how it is portrayed in Nepal — it is not entirely positive. However, the engagement is crucial, since China's newfound economic power is as yet unmatched.<sup>5</sup> This challenges India's privileged position in Nepal. Indian Prime Minister Narendra Modi has taken various initiatives and has indicated that he intends to address Nepal's concerns regarding India.<sup>6</sup> Whether India will succeed in effectively competing with China to safeguard its interests and maintain its sphere of influence, is going to depend on two overarching factors: New Delhi's overall capacity to challenge China, and India's political will to address its own controversial approaches towards Nepal.

## NEPAL'S POLICY DEPARTURE

Nepal's eagerness to engage with China has been of interest to observers and largely misinterpreted as Prime Minister Khadga Prasad Sharma Oli's strategy to acquire more from India. However, the current approach fits perfectly in Nepal's long tradition of pursuing a diversified foreign policy and partners, taking advantage of its key geostrategic position. Oli's government aims to keep Nepal's relationship with China independent of the one it shares with India. The question to ask is whether Nepal will be able to achieve this, given India's discomfort with the increasing Chinese proximity.

Nepal and China have both made it clear that they are working towards a serious engagement with the other. During Oli's recent visit to China, South Asia expert in Beijing Hu Shisheng said, “Our [China's] policy is clear – if you [India] want to work with us you are welcome, if not, then at least do not obstruct our work.”<sup>7</sup>

In light of this stance, it is important to understand Nepal's policy motivation. New Delhi was for long perceived in Kathmandu as “hawkish” and “selfish” in dealing with sensitive matters, which in turn projected an unlikeable image of India. The most notable instances of this include different river treaties, reluctance to respond to regular border-encroachment complaints, high-structure build-up along the border, inundation complaints, the armed border forces' harsh behaviour, trade and transit crises, and embargoes.<sup>8</sup> These experiences led Nepal to look for other options. Nepal's need for China far outweighs any potential challenges in the Sino-Nepal relationship, and

the Nepali “Citizens’ Mandate” to Oli reflects the same strong desire. Thus, the communist parties of Nepal have consistently protested against India, and the Nepali Congress too has shown reservations, indicating a broad political consensus on this approach to India.

There are historical reasons that explain the dynamics of the Nepal–India bilateral relationship. To maintain a sphere of influence, India needs sufficient soft power, as well as hard power, along with the confidence to act. As scholar Aparna Pande argues, “Managing a sphere of influence is not only a function of telling others what to do but being able to expend resources that deny space to competitors.”<sup>9</sup> The former Prime Minister Kirti Nidhi Bista of King Mahendra’s era once said, “India made him (PM Bista) lose his temper because during those times when India was economically insignificant, it still had undue demands over Nepal.”<sup>10</sup> A combination of economic limitations, India’s political manipulation, Chinese inroads, and the outreach of extra-regional powers to Nepal gradually increased its desire to diversify relations. Such ambitions have been the central element of successive governments in Nepal, leading to increased friction with India.

Indeed, the nature of India-Nepal relations has always been a mixed bag.<sup>11</sup> Due to its provisions and protocols, the 1950 treaty quickly became controversial and set the conflictive tone of the bilateral relationship. The provisions of the 1950 Indo-Nepal Peace and Friendship Treaty (1950 Treaty: Article 5, Letter of Exchange: Article 2, Indo-Nepal Security Cooperation Agreement, 1965: Article 5), constrained Nepal as an ally and a state under India’s security umbrella. In 1988,

King Birendra’s decision to purchase anti-aircraft guns from China prompted then Indian Foreign Secretary K.P.S. Menon to warn Nepal of its existential uncertainty.<sup>12</sup> Over the years, the incompatibility between the two countries only worsened in various domains.

## **AREAS OF CONTENTION: BORDER, WATER, COMMERCE**

Recent examples from different parts of the world show that free cross-border movement of labour in certain cases has effects that run counter to, and even harm, the very institution of integration. In turn, this gives rise to populism and extremism. Nepal represents one such case. Given the asymmetrical size of the two countries, and Nepal’s reservations towards India due to the treaty-based unequal treatment, the open border has always been a crucial area of contention, except for communities and business groups that benefit from it directly.

The practice of cross-border free movement has become the subject of mutual recrimination. Neither side grants the national treatment or the reciprocal treatment as provided in the treaty (Article 6 and 7). This has only multiplied grievances, and communities along the border as well as businesses have had to bear the brunt of the negative side-effects. The Letter of Exchange’s Article 3 shows that India agreed to temporary protection for Nepalis in Nepal from free competition with Indians. However, since the two sides never agreed on concrete terms, the implementation was stalled. India has been reluctant to deal with Nepal’s demand to revise

the treaty, given the matter's sensitive nature and its electoral implications as well as the potential departure of Nepal into a new direction. This unwillingness has had larger implications for India in the form of loss of popular support in Nepal.

Another area of grievance is trade and commerce. Because of its geographical constraints, Nepal has found itself heavily reliant on India, never acquiring the comparative advantage to increase exports. Local enterprises fail to grow, being simply unable to compete against lower-priced Indian products that flood the market. India's imposition of non-tariff barriers and lack of standard infrastructure have added to Nepal's discontent with India. The transaction costs for exports and imports are unsustainably high. It takes 42 days to reach export destination via Indian ports and 35 days to reach Nepal from the suppliers' point, which account for US\$2,700 shipping cost per container.<sup>13</sup> As a result, as of 2018, the country's trade deficit ratio is at a staggering 1:14.9. Nepal's largest trading partner is India (the total trade accounting for 65 percent), with whom Nepal runs the largest trade deficit.<sup>14</sup> There was an improvement following the amendment of the trade commerce treaty with India in 1996, as exports increased and the deficit dropped. However, in the subsequent extension of the treaty, India reverted to earlier provisions, partly prompted by the activities of unscrupulous entrepreneurs.

Another longstanding dispute between India and Nepal relates to the provisions of existing river treaties and their

implementation. Nepali stakeholders claim that India has taken undue advantage of its generosity in sharing water, by using ambiguous provisions and providing far less benefits than the upper riparian state duly deserves. They claim that India's handling of the issues involving the Koshi and Gandaki rivers has been far from satisfactory. The Mahakali agreement has remained in limbo for over two decades. In 2008, the collapse of Koshi's embankment unleashed massive flooding, highlighting India's failure to take precautionary measures and its refusal to take responsibility.

In 1991, when then PM Girija P. Koirala signed an MoU with India on the issue of Tanakpur, he was challenged in the Supreme Court in Nepal for what was seen as unacceptable concessions, particularly in granting 2.9 hectares of land to India for bund construction.<sup>15</sup> The court's verdict was submitted to parliamentary ratification, which eventually never happened. However, Tanakpur dam became a *fait accompli* as India constructed it. Nepal's bureaucrats and water experts are reluctant to talk about any new framework agreements due to past experiences.<sup>16</sup> The country appears to be in denial, as suggested by former Indian diplomat S.D. Muni in terms of India–Nepal water cooperation.<sup>17</sup>

Amidst such historically complicated relationship between the two neighbours, China has emerged as an ally for Nepal. The following sections discuss the new prospects that China's proximity has brought to Nepal.



Map 1



**Nepal sits between India and China. The Himalayas run along the Nepal-China border, and the Nepal-India border lies at the southern plains of the country.**

*Source: Google Maps*

## THE TRANS-HIMALAYAN RAILWAY

China and Nepal have agreed to “intensify implementation of the MoU on Cooperation under the BRI to enhance connectivity,” which includes ports, roads, railways, aviation and communications in the framework of the Trans-Himalayan Multi-Dimensional Connectivity Network.<sup>18</sup> India poses a legitimate question: Is the trans-Himalayan railway up to Kathmandu economically viable, since several costly tunnels are needed before the railway reaches the lower mountains and plains?<sup>19</sup> India might be overplaying the risk.

First, excluding Kathmandu, the Chinese Qinghai-Tibet railway—already fully

operational up to Shigatse (Xigaze)—is expected to soon reach the Nepal border (Rasuwagadi) in Kerung (Gyirong). From Kerung it will be a 100-km-long railway to Kathmandu. A combined transportation system of rail and truck via that route reduces the journey substantially; China has already started sending cargoes on freight train from Lanzhou to Kathmandu via Shigatse, where the merchandise is loaded on trucks. The whole journey takes only 10 days, much less than the 35 days it takes through the maritime route via Kolkata.<sup>20</sup> A Chinese railway in Kerung can thus elevate Sino-Nepal trade and commerce.

Second, the economic viability of the Kerung–Raxaul (India) route is uncertain,

Map 2



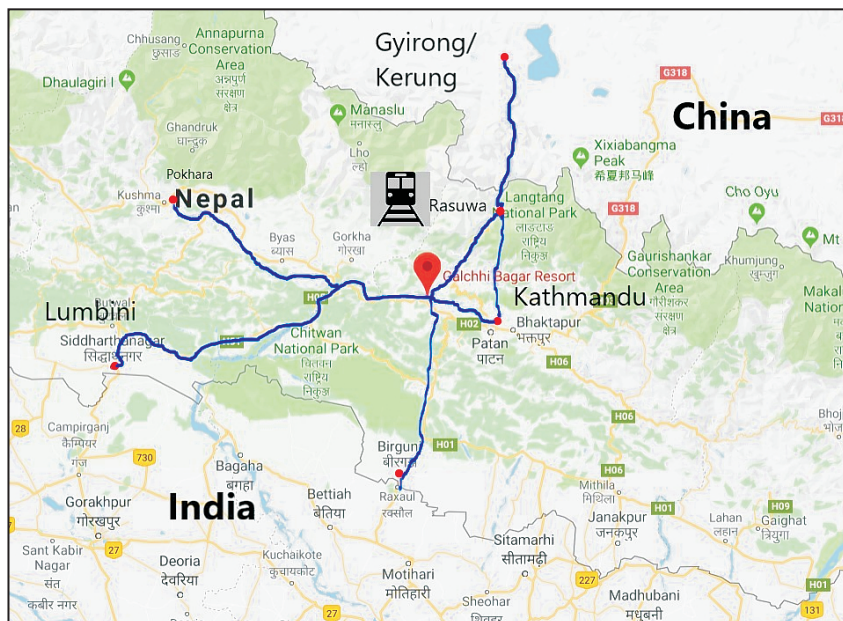
The planned extension of the Qinghai-Tibet railway to Kerung (Gyirong) and into Nepal.

Source: Author's own, based on Google Maps

with India emphasising its own centrality in the project and China planning to reach out to the Gangetic plains via Nepal. For its part, Nepal views the Chinese railway as an

opportunity to bring Chinese pilgrims and tourists to Lumbini, the birthplace of the Buddha, and to the popular valley of Pokhara.<sup>21</sup> In recent years, due to the new train

Map 3



Nepal's East-West Railway Network, and the Kathmandu-Pokhara-Lumbini network, will be linked to China-Nepal railway at the Rasuwagadi-Kerung border.

Source: Author's own, based on Google Maps



connectivity and the increasing air connectivity between Lhasa and eastern China, Tibet has experienced a surge in domestic and international tourism.<sup>22</sup> Thus, the extension of the Tibet–Qinghai railway up to Nepal, and especially to Lumbini, will undeniably attract tourists from China and beyond. Incidentally, in the first quarter of 2018, for the first time, Nepal welcomed more Chinese than Indian tourists.<sup>23</sup>

Third, the Chinese railway can help enhance Nepal's overall economic capacity, a need that both China and Nepal seem aware of and which is amply reflected in the measures laid out in the joint communiqué issued during Oli's visit to China in June 2018.<sup>24</sup> The two countries signed several MoUs, including one on Investment and Cooperation on Production Capacity, another on Human Resource Development Cooperation, and a third on Economic and Technical Cooperation. China has agreed to "take positive measures to facilitate Nepal's export to China" and support "product development and post-harvest technology in agro-products" and wants to tap Nepal's resources such as "construction materials, water conservation and hydropower and organic agriculture and herbs" and cooperate on production capacity by building economic and trade cooperation zones.<sup>25</sup> Both sides have also agreed to finalise the China–Nepal Free Trade Agreement (FTA).

China has a thorough plan and the experience of domestic success makes such international projects a political priority, as laid out in the 18<sup>th</sup> National Congress of the Communist Party of China in 2012. Nepal, for its part, is inspired to be ambitious and has both the will and capacity to become an

important part of the BRI as a standalone country, not just because of its size. The two sides have already concluded trade and transit agreements, and Nepal is eyeing connections with the Chinese market and oil refineries as well as the global supply chain via Chinese ports: Tianjin seaport to the east, Central Asia to west and beyond.

The dynamics of Nepal's relations with India differ from that with China. Nepal views its engagement with China from a different perspective. Due to the much-debated "debt trap," Nepal is cautious and has asked China to fund the railway as a grant and not as a loan. China, for its part, has also learned from its international failures,<sup>26</sup> be it debt problems with host countries or political instability in some countries in Latin America and Africa where its plans did not materialise. Thus, it is understandable that China wants a stable Nepali government, and many have speculated that China is behind the merger of communist parties in Nepal.

Even without the rail connectivity and BRI, the China–Nepal engagement has strengthened in sectors such as hydropower, aviation, tourism, telecommunications, people-to-people relations, cultural exchanges, political exchanges, industry and technology.<sup>27</sup> The only uncertainty in all of this has to do with China's own economic health. Only three years ago, the world was talking about "the great fall of China," as it suffered a stock-market crash.<sup>28</sup> Although the predictions about China proved to be wrong, some projects did in fact fail.<sup>29</sup> To what extent China will engage in Nepal is also partially dependent upon the emerging larger understanding between India and China.

## IMPLICATIONS FOR INDIA

China's active outreach to Nepal in recent years has been partly prompted by India's increasing force posturing along its border, which, in the first place, was in response to China's activities along the border. Interestingly, the timing of former PM Manmohan Singh's government considering border-force enhancement for defensive purposes roughly coincided with the spike in China's interest in Nepal, which further increased after the Tibetan protests during the Beijing Olympics in 2008. Some argue that the evolving Indo-US relationship also played its part. China's engagement in Nepal is either directly correlated with India's action vis-à-vis China, or completely independent of the same. In either scenario, India's strategy to keep Nepal's engagement with China to a minimum is no longer a viable option.

In the case of an India–China war, it is uncertain whether Nepal will take India's side as per the spirit of the 1950 treaty (as well as subsequent treaties), given Nepal's reluctance to do so in the past. While, on paper, Nepal remains an ally of India, it has constitutionally asserted that its foreign policy is “based on the Charter of the United Nations, non-alignment, principles of *Panchsheel* (and) international law.”<sup>30</sup> Major parties have often reiterated this, and the overall national spirit reflects Nepal's desire to remain neutral, as it did during the Doklam standoff in mid-2017.<sup>31</sup>

Moreover, the sheer scale of China's plan and its economic clout is shifting the tide of global order. The US position in Latin America increasingly resembles India's current situation vis-à-vis Nepal. So much so

that Panama, once considered to be America's “colony,” has now ended its relations with Taiwan upon Beijing's request.<sup>32</sup> El Salvador has done the same. Now, the 60<sup>th</sup> annual meeting of Inter-American Development Bank, headquartered in Washington D.C., is going to be held in Chengdu, China. The bank's board made this decision despite several warnings from then Secretary of State Rex Tillerson.<sup>33</sup>

Finally, India's stance on Oli's government puts it in an undue negative light. Despite Oli's “ultranationalist” election rhetoric, he has responded positively to Modi's and Finance Minister Sushma Swaraj's overtures. Modi and Oli have established a relationship of trust, negotiating some important agreements during their visits. The agreement on the historically controversial Arun III hydel project, and their cooperation in revitalising BIMSTEC (or the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation), are some of the indicators of Oli's good intentions regarding India.

## THE WAY FORWARD

The recent joint communiqués between India and Nepal seem to have all the right words and tone for a constructive move forward in their bilateral relations. Immediately after the successive visits of Modi and Oli to Nepal, there has been unprecedented progress in several areas. For instance, a joint inspection team visited the bordering areas prone to flooding, something that has not happened in the past. Similarly, contrary to expectations, the joint Eminent Persons Group (EPG) has finalised their recommendations on the revision of the 1950 treaty, and submitted



them to the two prime ministers for possible implementation. Another joint meeting has agreed to finalise modalities to implement the grand project of water connectivity, and India is willing to provide financial and technical support. The Oli government wants ships to enter Nepali waters by 2020. The MoU on the Raxaul–Kathmandu railway has also been well-received.

However, despite generous announcements, India continues to send mixed signals. First, in terms of the land and air connectivity, the response has been sluggish: the gap between providing access to Vizag Port and new air routes to Nepal is two years. Nepal's request to access India's west ports is at a nascent stage and will take some more years. Second, while Modi has hit all the right chords in his talks, India is still unwilling to cooperate on power trade with Nepal in the way Nepal would like it to, or to provide electricity at lower rates. The message that Nepal remains India's "client state" will not be helpful to the aims of working towards a higher level of cooperation. India must formulate an integrated approach towards Nepal to reflect the current reality.

Regarding China's inroads into Nepal, an option for India would be to defend the status quo by attempting to block Nepal's options to diversify its cooperation with neighbours, through projects such as the infrastructure development by Chinese investment. However, such a policy is bound to fail because Nepal is determined to take advantage of cooperation opportunities with foreign partners, including China. Addressing the issue of external interference, Nepali Foreign Minister P. Gyawali recently said, "We want to

draw a clear boundary line, stating that internal matters will never be the issues in a bilateral discussion with India, China and others."<sup>34</sup>

China is winning hearts and minds in Nepal through generous strategic charity. After the 19<sup>th</sup> Party Congress, it will continue to "use economic diplomacy as the foundation of its foreign policy."<sup>35</sup> Therefore, the way forward for India would be to depart from its exclusively traditional security angle and be proactive with innovative strategies and policies.

The first step is to identify the major cause of Nepal's behaviour towards India. Why has the Nepali establishment consistently resisted India while being so welcoming to China? This is a particularly crucial question, since Nepal has growing trade deficits with both countries.

Second, India must introduce new economic, developmental and infrastructure initiatives with Nepal that will not only bring tangible benefits to Nepali citizens but also address the vulnerabilities that will emerge in Nepal as the country engages with China. It is time that India translates into action PM Modi's repeated endorsement of PM Oli's objective of "happy Nepal, prosperous Nepal." Nepal's emphasis on India needing to deliver on its promises comes from its awareness of India's own need to keep Nepal closer to itself than China.

As things are, Nepal cannot dispense with its reliance on India. India is and will remain vital for the country in many ways. However, Nepal is now a member of China's massive BRI, which puts India in a difficult position. As ORF


analysts, Harsh V. Pant and Abhijnan Rej rightly put it, “New Delhi has found itself utterly unprepared to deal with an assertive Chinese foreign policy under Xi Jinping.”<sup>36</sup> India must figure out where it stands vis-à-vis Nepal and what is the way for forward in the short, medium and long term, given the shifting regional and global structure, technological breakthroughs, as well as new threats such as terrorism. Nepal, for its part, has lived through a historic political transformation but continues to face huge challenges in terms of managing its population and economy; remittance makes up to about 30 percent of the country’s GDP and mostly originates in the Gulf. There is an increasingly strong Nepali diaspora in many parts of the world. Therefore, India and Nepal must figure out in what new ways they can move forward in the best interest of both parties.

## CONCLUSION

Analysts are not entirely accurate in their apprehensions about Nepal’s independent foreign relations. A strongly sovereign Nepal is beneficial, not detrimental, to India’s security. Nepal shares a 1,400-km-long border with the Tibetan Autonomous region of China, perhaps the only section in the Himalayas where there are no security threats. In a way, Nepal has taken away India’s burden, allowing India to avoid the need to deploy thousands of troops and military hardware to this extra 1,400 km for its force posturing. India has had to do so

along the 4,000 km China border,<sup>37</sup> which too has not deterred China from building infrastructure on contested land, Doklam being the case in point.<sup>38</sup> Emphasising Nepal’s sovereign status and independent policy choices, and helping Nepal exercise these is in India’s interest. Similarly, there are concerns in some quarters of Kathmandu about the possible trilateral or 2+1 cooperation, that Nepal’s sovereign interests are being undermined in the India–China deals. It will help build trust if India manages to translate its good will into meaningful action.

As long as the principles of non-interference and peaceful co-existence are respected and a high level of political engagement is pursued, there will be bonhomie and cooperation between the leaders of India and Nepal. At the same time, it will assuage China’s unease about its security in Nepal. Disregarding India’s traditional muscular diplomacy, PM Modi seems to have been following this line of cooperative diplomacy. The results are evident: the good rapport between Modi and Oli, and Nepal’s increasing cooperation in Modi’s initiatives, which would have been impossible just a year ago.

Nepal is equally eager about the prospects of being road-connected with Myanmar and Thailand through BIMSTEC as it is with the BRI on the northern front. Therefore, India may want to institutionalise the current approach, which seems to be in the best interest of both. 

### ABOUT THE AUTHOR

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