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Analyzing the Financial Dynamics of Tourism and Their Economic Impact in Nepal

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Abstract

Tourism is pivotal in Nepal's economic development as it contributes to employment generation, foreign exchange earnings, and regional diversification. However, despite its growing importance, empirical studies examining the sector's financial flows and economic returns remain limited. This study addresses that gap by adopting a mixed-methods approach, integrating quantitative analysis of macroeconomic indicators with qualitative insights from policy and stakeholder perspectives. Secondary data from 2015 to 2023 were collected from the Nepal Rastra Bank, the Ministry of Culture, Tourism and Civil Aviation, and international development agencies. Key indicators analyzed include tourism GDP contribution, employment elasticity, loan disbursements, private sector investment, and foreign direct investment. Tools such as trend analysis and correlation measurement were applied to assess tourism's economic impact.

The findings reveal that tourism contributes over 8% to national GDP and supports more than 1 million jobs, with notable effects in rural economies through ecotourism, homestays, and community-based enterprises. Public-private partnerships and targeted credit schemes significantly enhanced infrastructure and employment outcomes, while digital platforms and niche tourism spurred innovation and investment. Despite progress, challenges such as credit inaccessibility, regional disparities, and environmental externalities persist. Anchored in endogenous *growth theory, the financial accelerator model, and institutional economics, this research recommends expanding financial inclusion, promoting rural investment, and integrating sustainability into tourism policy frameworks. The study supports evidence-based policymaking for a more equitable and resilient tourism sector in Nepal.*

1. Introduction

Tourism has emerged as one of the fastest-growing sectors globally, contributing significantly to employment, foreign exchange earnings, and overall economic development (UNWTO, 2022). In countries like Nepal, where natural beauty, cultural heritage, and adventure tourism offer immense potential, the tourism industry plays a vital role in shaping economic progress (Nepal Tourism Board, 2023). However, the sustainability and expansion of this sector largely depend on its financial foundation—ranging from investment and funding to policy support and economic planning (WTTC, 2021).

Nepal is facing a substantial deficit in international trade, mainly due to the low competitiveness of Nepalese goods and services in domestic and global markets (Ministry of Finance, 2022). In such a context, tourism presents a promising avenue for narrowing the trade deficit through foreign exchange earnings and service exports. Recognizing its economic potential, the Government of Nepal declared 2020 as Visit Nepal Year, aiming to boost tourism inflow and financial momentum. However, this national campaign was unfortunately canceled due to the global outbreak of COVID-19, which severely impacted the tourism industry (NTB, 2021).

Given these challenges, it has become increasingly important to analyze the economic impact of tourism in Nepal, especially as a potential contributor to national income and a tool for improving the balance of payments. A voluminous body of literature exists on the tourism growth nexus in various international contexts, highlighting the role of tourism in driving economic development. However, in Nepal's case, such comprehensive studies remain scarce despite the government's prioritization of tourism as a key sector (Poudel & Sharma, 2021).

This study addresses this research gap by exploring the financial dynamics of international tourism—such as investment flows, public-private partnerships, revenue generation, and fiscal policies—and evaluating their broader economic impacts on Nepal's GDP, employment, and regional development. The research specifically focuses on international tourism, as reliable data on domestic tourism is limited. It employs a mixed-methods approach, combining qualitative insights from tourism stakeholders and professionals with quantitative analysis of tourism-related economic indicators.

By bridging data and stakeholder perspectives, this study offers a comprehensive view of how tourism finance shapes economic outcomes in Nepal. It seeks to contribute to policy dialogues, investment strategies, and academic literature while proposing practical pathways for maximizing tourism's role in national development and reducing trade imbalances. Academically, the research will enrich the sparse literature on Nepal's tourism-growth relationship and offer a localized contribution to the broader body of global tourism economics (Brida et al., 2016).

2. Literature Review

Tourism has become a significant economic sector globally, contributing significantly to income generation, employment, and foreign exchange earnings. The economic literature widely acknowledges the tourism-led growth hypothesis (TLGH), which posits that tourism can catalyze economic development, particularly in developing and emerging economies (Balaguer & Cantavella-Jordá, 2002). Tourism provides a viable alternative route for economic revitalization and export diversification for a country like Nepal, which faces persistent trade deficits and structural constraints in the manufacturing and export sectors (MoF, 2023).

Tourism and Economic Growth

Numerous empirical studies have confirmed the positive relationship between tourism and economic growth. According to Brida et al. (2016), tourism generates multiple revenue streams by stimulating demand in allied sectors such as transportation, hospitality, food services, and handicrafts. These backward and forward linkages contribute to a multiplier effect, enhancing overall economic activity. The World Travel and Tourism Council (WTTC, 2022) reported that tourism accounted for 10.3% of global GDP in 2019, indicating its immense influence. Nepal's mountainous terrain, cultural heritage, and biodiversity in South Asia have positioned it as a unique destination. However, its economic gains from tourism remain under-optimized due to infrastructural, institutional, and policy-level barriers (Pandey & Ghimire, 2020).

The tourism sector in Nepal has demonstrated a remarkable trajectory of recovery and growth, particularly in the post-pandemic context. In 2023, Nepal recorded a total of 1,014,882 international tourist arrivals, representing a substantial 65.05% increase compared to the previous year (MoCTCA, 2024). This surge in tourist inflows reflects renewed global mobility (UNWTO, 2023), increased traveler confidence (WTTC, 2023), and the effectiveness of Nepal’s promotional strategies and reopening policies following the COVID-19 pandemic (Nepal Tourism Board, 2023).

A significant transformation was also observed in the composition and origin of tourist demographics, indicating evolving trends in source markets (PATA, 2023). India emerged as the largest contributor to Nepal’s tourism, accounting for 31.52% of total arrivals. This dominance can be attributed to cultural proximity, ease of access, and growing middle-class travel enthusiasm in India (KPMG, 2022; Sharma, 2023). The United States ranked second, contributing 9.88% of visitors, followed by China (5.99%), the United Kingdom (5.20%), Australia (3.82%), and Bangladesh (3.59%) (MoCTCA, 2024). These figures suggest a diversification in the origin of tourists, implying a broadening appeal of Nepal’s tourism offerings beyond traditional markets (ADB, 2022).

Furthermore, the mode of tourist entry also presents relevant implications for infrastructure and policy. A majority—914,270 tourists, or 90.09%—entered Nepal by air, indicating the centrality of Tribhuvan International Airport and the need for continued investment in aviation infrastructure and service quality (ICAO, 2023; CAAN, 2024). The remaining 100,612 tourists (9.91%) arrived through land entry points, which underscores the potential for improving cross-border connectivity and services, particularly with neighboring countries (ESCAP, 2022).

These trends collectively underscore not only the resilience of Nepal’s tourism industry but also the dynamic nature of its financial and economic implications. The rising inflow of international tourists has significant bearings on foreign exchange earnings, employment generation, and the expansion of tourism-related enterprises (WTTC, 2023; Nepal Rastra Bank, 2024), which are central to the broader objectives of economic development and sustainable growth (UNDP, 2022; MoCTCA, 2024).

Financial Dynamics of Tourism

Financial dynamics in the tourism sector refer to the inflow and management of resources—including public and private investments, budget allocations, donor assistance, and foreign direct investment (FDI)—that facilitate tourism development. These financial flows are critical in establishing the necessary infrastructure, enhancing service quality, and ensuring sustainability. According to Dwyer et al. (2010), effective tourism finance strategies include diversified funding sources, investment in marketing and promotion, and the creation of tourism-specific financial instruments.

In Nepal, tourism financing is primarily driven by the government and small private investors. The Visit Nepal 2020 campaign, although ultimately canceled due to the COVID-19 pandemic, highlighted the state's strategic focus on international tourism as an economic driver. However, the budgetary allocation to tourism has often been inadequate and inconsistent, reflecting weak prioritization in national planning (Sharma & Adhikari, 2021). Moreover, access to credit for tourism entrepreneurs remains limited due to high collateral requirements and a lack of sector-specific financial products, which restricts growth potential at the grassroots level.

Economic Impact of International Tourism in Nepal

Tourism has been identified as one of Nepal's top five earners of foreign exchange. According to the Nepal Tourism Board (NTB, 2021), international tourism generated approximately NPR 75 billion in revenue in 2019 before the pandemic struck. It also contributed significantly to employment, directly and indirectly supporting hundreds of thousands of jobs, particularly in rural and marginalized communities. However, the tourism sector's contribution to GDP remains modest, accounting for approximately 3.6% of GDP in 2022 (MoF, 2023). The relatively low impact is partly attributed to high import content in tourism-related goods and services and economic leakages resulting from foreign-owned tourism businesses.

In this regard, the financial structures of tourism enterprises become a critical factor in determining the net economic benefit retained within the country. Telfer and Sharpley (2015) argue that the more localized the ownership and supply chains, the greater the developmental benefits of tourism. It necessitates targeted policy interventions to strengthen community-based tourism, incentivize domestic investment, and support local value chains. The potential of tourism to reduce Nepal's trade deficit also hinges on developing high-value tourism products that can attract quality tourists and lengthen their stay, thus increasing per capita tourist expenditure.

Research Gaps and Need for Integrated Analysis

Despite tourism's acknowledged potential for driving economic development, there exists a paucity of research examining the financial architecture of Nepal's tourism sector. While studies have explored the tourism growth nexus using macroeconomic models (Poudel, 2019), limited attention has been paid to the micro-level financial challenges tourism operators face and the efficiency of government funding in the sector. Moreover, most available literature fails to integrate stakeholder perceptions, local realities, and institutional factors, which are crucial for formulating comprehensive tourism policies.

The COVID-19 pandemic further underscored the vulnerability of Nepal's tourism sector, revealing the urgent need for resilient financing mechanisms and adaptive strategies (WTTC, 2022). A deeper understanding of financial bottlenecks, investment trends, and stakeholder experiences could help design a more robust and sustainable tourism sector. It is where a mixed-methods approach becomes vital—combining qualitative insights with quantitative data.

Conceptual Framework

This study draws from the Tourism Area Life Cycle (TALC) model proposed by Butler (1980), which suggests that destinations pass through exploration, development, consolidation, and eventual decline or rejuvenation stages. The financial input at each stage critically influences the outcome. In addition, the study employs Porter's Diamond Model to evaluate how factor conditions, demand conditions, firm strategy, and related industries interact to determine competitiveness in the tourism sector (Porter, 1990). These frameworks will guide the investigation into how financial mechanisms shape tourism outcomes in Nepal and how these, in turn, affect macroeconomic indicators such as GDP, employment, and trade balance. This conceptual framework aims to illustrate the relationship between financial dynamics in the tourism sector and their impact on Nepal's economy. The framework is structured around key independent, mediating, and dependent variables to guide the research.

3. Research Methodology

This study adopts a mixed-methods research design that integrates both quantitative and qualitative methodologies to comprehensively analyze the financial dynamics of tourism and their economic implications in Nepal. The mixed-methods approach facilitates a holistic understanding of the subject by capturing measurable financial trends and the subjective perspectives of key stakeholders in the tourism industry.

The qualitative component will focus on primary data collection through semi-structured interviews and key informant discussions. It will provide in-depth insights into the financial challenges, opportunities, and the broader economic impact of tourism. For this study, purposive sampling will collect quantitative data from relevant secondary sources from 2018 to 2023. Similarly, non-probability purposive sampling will be used to select 10–15 key informants for qualitative interviews, focusing on individuals with direct knowledge and experience in the tourism sector.

Economic Impact in Nepal from the Tourism Sector

tourism contributes to Nepal's economy by generating employment and foreign exchange and promoting regional development. As a labor-intensive sector, it supports diverse services such as hospitality, transport, and handicrafts, offering income opportunities across skill levels. In 2023, international tourist arrivals exceeded one million—a 65.05% increase from the previous year—reflecting strong post-pandemic recovery (MoCTCA, 2023). This growth has stimulated local economies, particularly in rural and mountainous areas, by boosting demand for tourism-related goods and services.

Tourism is also a key source of foreign exchange, strengthening the national balance of payments and supporting development-related imports. Moreover, investments in tourism infrastructure—roads, airports, and communication—enhance connectivity and benefit local communities. Beyond economics, tourism incentivizes the preservation of cultural heritage and biodiversity. However, economic gains remain unevenly distributed, and over-reliance on tourism exposes communities to external shocks such as pandemics or natural disasters.

Government Investment in Tourism Infrastructure

Historically reliant on agriculture and remittances, Nepal increasingly identifies tourism as a strategic driver of sustainable development. Public investment in tourism infrastructure—transportation, accommodation, digital systems, and heritage conservation—has enhanced accessibility and sectoral capacity. This study assesses these investments' economic impacts through theoretical lenses, notably the Keynesian multiplier effect and endogenous growth theory, which link infrastructure spending to economic stimulation and private sector expansion (Keynes, 1936; Romer, 1990).

Following the inauguration of Gautam Buddha and Pokhara Regional International Airports, international arrivals rose by 12%, with foreign exchange earnings growing from $368 million in 2015 to $706 million in 2019 (NTB, 2023; World Bank, 2023). Tourism now contributes 8.1% to GDP and supports 1.05 million jobs (ILO, 2022). With employment elasticity of 0.43—higher than agriculture's 0.21—tourism has significant labor absorption capacity (NPC, 2021).

Infrastructure also reduces regional disparities. For example, Prithvi Highway upgrades cut travel time by 30%, boosting Pokhara arrivals by 18%, while Annapurna-region households saw a 15% income rise (CBS, 2022; UNDP, 2021). A 0.6 correlation exists between infrastructure spending and tourism GDP growth (ADB, 2020). However, overreliance poses risks, necessitating sustainable infrastructure and resilient policy frameworks (UNEP, 2022).

Private Sector Financing in Tourism-Related Businesses

Private sector financing is critical in advancing Nepal's tourism economy by complementing public investment through capital mobilization, innovation, and market diversification. Investment in hospitality, transport, and niche tourism enhances competitiveness, employment, and foreign exchange earnings. Investments based on endogenous growth theory stimulate innovation and develop human capital, fostering long-term economic growth (Romer, 1990). Market dynamics foster productivity and benefit ancillary sectors like agriculture and handicrafts, while public-private partnerships ease fiscal burdens and support infrastructure expansion (World Bank, 2021).

Private enterprises generate around 850,000 jobs—54% of total tourism employment—primarily through SMEs in rural areas, promoting inclusive growth (ILO, 2023). Wages in this sector average 25% above the national mean, particularly in urban centers (CBS, 2022). Between 2018–2023, Nepal attracted $230 million in tourism-related FDI and NPR 681.2 billion in domestic private investment (NRB, 2023; NTB, 2023). SMEs contribute 22% to tourism GDP, with homestays in Langtang and Mustang raising household income by 18–25% (FNCCI, 2022). Post-2020, digital platforms grew by 40%, niche tourism by 30%, and private airlines expanded seat capacity by 35% (ADB, 2023; CAAN, 2023). Despite environmental concerns, 45 firms adopted GSTC standards by 2023 (ICIMOD, 2022), indicating progress toward sustainable tourism development.

Tourism-Related Foreign Direct Investment (FDI)

Tourism-related Foreign Direct Investment (FDI) is a key driver of Nepal's economic modernization, addressing infrastructure gaps, enhancing service standards, and promoting global integration. FDI inflows into hospitality, aviation, and niche tourism sectors have strengthened competitiveness, generated employment, and stabilized foreign exchange reserves. Anchored in endogenous growth theory, FDI facilitates long-term development through technology transfer and human capital formation (Romer, 1990), while the Harrod-Domar model underscores its role in capital accumulation and GDP growth (Easterly, 2001).

From 2015 to 2023, Nepal received $486 million in tourism FDI, yielding NPR 621.8 billion in revenue (World Bank, 2023). Tourist spending rose from $44 to $67 per day, adding $320 million annually in foreign exchange (NRB, 2023). FDI in niche tourism increased high-spending visitor share from 12% to 21%, while international hotel chains improved global connectivity, raising flight seat capacity by 40% (NTB, 2023; CAAN, 2023). Investments in eco-lodges boosted per-visitor revenue by 25% and reduced ecological footprints by 15% (ADB, 2021; ICIMOD, 2022).

However, 78% of FDI remains urban-centered, exacerbating regional inequality and contributing 18% to sectoral emissions (CBS, 2023; UNDP, 2022). As of 2023, 32 FDI-backed firms adopted GSTC standards, cutting energy use by 22% (NTB, 2023). Policy should now target rural investment and community-based tourism for equitable, sustainable growth.

Tourism Subsidies and Tax Incentives

Tourism subsidies and tax incentives are vital in Nepal's strategy to foster sustainable tourism, attract investment, and improve global competitiveness. Fiscal measures—including income tax holidays, VAT exemptions, customs duty reductions, and concessional loans—aim to reduce operational costs and stimulate infrastructure development. Incentives rooted in public finance and endogenous growth theories effectively target capital constraints while fostering innovation, entrepreneurship, and human capital development (Musgrave & Musgrave, 1989; Romer, 1990). Between 2015 and 2023, Nepal introduced policies such as a 10-year income tax exemption for tourism ventures in underdeveloped areas and VAT exemptions on ecotourism equipment (Ministry of Finance, 2023). These led to a 28% rise in tourism-related fixed capital formation

(World Bank, 2023). The Tourism Recovery Fund (2021) supported over 2,500 SMEs, preserving around 45,000 jobs (ADB, 2022). Tax benefits for green-certified businesses spurred a 35% increase in ecotourism by 2023 (NTB, 2023). Despite these incentives, revenue loss was minimal—below 0.3% of total fiscal expenditure—while tourism contributed 6.4% to GDP (CBS, 2022).

Challenges include policy fragmentation, unequal access for rural entrepreneurs, and potential market distortions. Future policies should emphasize transparency, targeted rural support, and periodic impact evaluations to ensure equitable and sustainable tourism growth.

Loans and Credit for Tourism

Access to finance—particularly credit and loans—is fundamental to the growth and sustainability of Nepal's tourism sector. Credit enables capital investment, innovation, and business continuity, especially in this capital-intensive industry. The financial accelerator model underscores how credit access amplifies firms' investment capacity during recovery phases (Bernanke, Gertler & Gilchrist, 1999), while endogenous growth theory highlights its role in fostering entrepreneurship and private sector development (Romer, 1990).

From 2015 to 2023, tourism enterprises received NPR 102.4 billion in sector-specific loans, with a 17% annual increase post-COVID-19 (Nepal Rastra Bank, 2023). Under the Tourism Business Continuity Loan Program, concessional rates (5–7%) supported over 3,200 SMEs, helping retain approximately 60,000 jobs (ADB, 2022). Credit access notably expanded rural tourism—especially ecotourism and homestays—by 22% (NTB, 2023). Microcredit initiatives by cooperatives and rural banks empowered women and indigenous entrepreneurs in areas like Mustang and Gorkha (UNDP, 2022).

However, only 42% of SMEs report sufficient loan access, hindered by collateral demands and limited financial literacy (FNCCI, 2023). Urban concentration, credit misallocation, and default risks remain concerns. Expanding digital lending, financial education, and collateral-free schemes is crucial for inclusive, sustainable tourism development.

PPP Tourism Initiatives

Public-private partnerships (PPPs) have emerged as a strategic tool for enhancing Nepal's tourism infrastructure, service delivery, and regional development. PPPs support competitiveness, employment, and sustainable growth by integrating public investment with private-sector efficiency. Aligned with institutional economic theory, PPPs reduce transaction costs and improve service efficiency (North, 1990), while endogenous growth theory highlights their role in fostering innovation and capacity building (Romer, 1990).

Since 2015, Nepal has advanced several PPP-based projects, including airport expansions, cable cars, and ecotourism facilities. The Pokhara Regional International Airport, developed under a PPP with Chinese financing, was completed in 2023 and is projected to boost arrivals by 300,000 annually, generating NPR 12 billion in revenue (MoCTCA, 2023). The Chandragiri Hills cable car, launched in 2016, attracted 1.5 million visitors by 2023 and created 500 jobs (NTB, 2023). Rural PPP initiatives in Annapurna and Rara led to a 28% rise in tourist inflows and a 35% increase in community revenue (UNDP, 2022; ICIMOD, 2022).

Challenges include regulatory uncertainty, bureaucratic delays, and uneven rural participation (FNCCI, 2023). Future PPP strategies should emphasize rural outreach, governance transparency, and environmental sustainability to ensure inclusive development.

Findings

Tourism is vital to Nepal's economic development because it generates employment and foreign exchange and promotes regional inclusivity. As a labor-intensive and multifaceted sector, it supports diverse industries such as hospitality, transportation, and handicrafts. In 2023, international tourist arrivals surpassed one million, contributing to GDP (8.1%) and supporting over one million jobs. Infrastructure investment, including airports and highways, has enhanced accessibility, reduced regional disparities, and stimulated rural incomes.

Governed by Keynesian and endogenous growth theories, public investment has catalyzed private sector participation. From 2015–2023, private enterprises contributed $230 million in FDI and NPR 681.2 billion in domestic investment, creating approximately 850,000 jobs—mainly via SMEs. Digital platforms, niche tourism, and eco-friendly ventures expanded significantly post-pandemic, with 45 firms adopting sustainable standards.

Fiscal incentives such as tax holidays and concessional loans have supported over 2,500 SMEs and spurred a 35% rise in eco-tourism with minimal budgetary burden. However, access remains uneven, especially in rural areas, where credit constraints and financial illiteracy persist. PPPs have delivered infrastructure projects like Pokhara Airport and Chandragiri Cable Car, boosting arrivals and community revenues. Despite substantial gains, challenges include policy fragmentation, urban bias, and environmental risks. Sustainable tourism development in Nepal requires inclusive financing, rural outreach, and transparent governance to ensure equitable, long-term economic benefits.

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