

Nepal's Negotiations With China

Issue Brief

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A. Background and Context

Nepal and China have long-standing historical relationships—the earliest recorded contacts going back to the Lichhavi Period (450-750 CE) and Tang Dynasty (618-907 CE). Since the 1960s, China has been a major development partner for Nepal. Most of China's aid has come in the form of turnkey projects, where Nepal accepted whatever China offered with minimal negotiation.

In recent years, China is intensifying and diversifying engagements. Based on its diplomatic negotiations, China's fundamental interests in Nepal are guaranteeing its security and stability, pursuing economic interests, expanding regional influence, and fulfilling global ambitions, primarily through different types of connectivities. China is always negotiating to win. In order to do so, China makes use of strategic preparation, strategic timing, and demand for reciprocal concessions.

Nepal, similarly, has several expectations from China as a development partner, including economic development. However, the combination of the geopolitical environment and weak diplomatic capacity poses significant challenges. Nepal's negotiations capacity should be enhanced to promote and protect national interests, including economic development, debt sustainability, and principles of quality infrastructure investments.

CESIF Nepal has conducted a study to identify the significant features and trends of diplomatic negotiations between Nepal and China. In particular, the study focuses on the most important factors that shape the nature and outcomes of negotiations in Nepal-China bilateral relations. The key question is: How can Nepal strengthen its negotiating capacity to protect its core interests (eg, sustainable development, climate justice, economic equality, and democratic governance)?

As part of our research, we conducted case studies of eight episodes of negotiations and interviewed more than 40 politicians and officials who were engaged in negotiations with China. The case studies included the following: Belt and Road Initiative and Framework; High-level Diplomatic Exchanges (2018-2024); Trade and Transit Agreement and Protocols; Pokhara Regional International Airport; Chinese Aircraft Procurement; Budhi Gandaki Hydropower Project; Boundary, Border Regulation and Border Security; and Hongshi Cement.

This research seeks to fill a critical gap in our understanding, and offers insights for policy-makers, diplomats, government officials as well as for bureaucrats, politicians, academia and media. It suggests ways to develop more effective strategies to engage with China from a position of strength while maintaining strategic autonomy.

B. Key Findings: Case Studies

Power Dynamics. Significant power asymmetry affected Nepal's position in all the negotiations.

- In the case of BRI Nepal often struggled to put forward strong positions while China linked multiple initiatives (BRI, GSI, GDI, GCI) and strategic components, creating additional pressure. During high-level visits, power asymmetry favored China in agenda-setting and outcomes, especially as China developed close working relations with Nepal's political parties. Since 2018, Nepal consistently adopted reactive rather than proactive positions, although it showed growing confidence in recent years. New agreements, however, have typically aligned with Chinese priorities, and the joint statements issued during high-level visits have shown increasingly stronger language on Chinese interests.
- In the case of Pokhara Regional International Airport (PRIA), China displayed high-level political engagement: initially, the Chinese Assistant Foreign Minister and Premier discussed strategic interests and offered financial support. Interlocutors invoked the notion of "bilateral relations" framing the airport as being "critical" to Nepal-China relations. Later, China positioned the airport as part of BRI and THMDCN. Regional power dynamics, particularly with India, have affected the airport's commercial scope.
- China used diplomatic pressure by linking **aircraft deals** to broader bilateral relations. Nepali politicians transferred opposing officials to silence resistance in the face of the Chinese Embassy's active involvement and pressure tactics. The government expedited decisions based on perceived bilateral importance.
- **In Budhi Gandaki**, China's influence manifested through the Communist Party merger timing and pressure from senior communist leaders to award the contract to CGGC. India's influence was evident in its declaration not to purchase power from projects involving Chinese contractors.
- **Hongshi Cement**. Power dynamics were not obvious at the technical negotiation level, which started with trust and relationships building. The emphasis was on business-oriented trajectory over political considerations.

Negotiations Strategy. China made elaborate use of different negotiations strategies.

- In the case of BRI, China employed a methodical, multilayered approach with extensive groundwork through high-level visits. The Chinese side preferred secrecy and minimal public debate. Initial flexibility was followed by increasing rigidity, especially after Nepal's MCC ratification in 2021. However, the Chinese side showed eagerness to arrive at an agreement during the 2024 negotiations.
- In the case of high level visits, China employed sophisticated sequencing: political agreements first followed by technical discussions. China prioritized security and strategic agreements, especially regarding Tibet and border management. It used high-level visits strategically to advance core interests, while only implementing commitments selectively.
- In the case of trade and transit negotiations, China made meticulous preparation before negotiations, laid extensive groundwork through high-level visits, and adopted a methodical, multilayered approach. China showed rigid stances on technical matters and unwavering adherence to Beijing's directives. China strategically linked multiple initiatives (TTA to FTA, Nepali Ports, Highways) and has only selectively implemented the agreements.
- In the case of aircraft deals, China used strategic timing, during Nepal's period of vulnerability (insurgency) and communist governments. China arrived with detailed drafts and specific demands,

made strategic use of language barriers, controlled terminology in agreements, and claimed all decisions required Beijing's approval.

- In Boundary and Border negotiations, China consistently maintained the upper hand, setting the agenda, timing, and terms of engagement. China's approach was to set a comprehensive agenda, push for unified agreements, and control border point operations. China employed a sophisticated multi-layered strategy. It combined security cooperation with infrastructure development and economic incentives, linked economic engagement with border management, and transformed traditional relationships into state-regulated interactions.
- **In the case of PRIA**, informal agreements were made with political leaders before formal processes began. A MoU was signed in secrecy, promising support to a Chinese company in the tender process. China's Exim Bank made tough and hard bargains and showed a dominating attitude. During implementation, Nepali regulators facilitated corruption.
- In the case of **aircraft deals** and **Budhi Gandaki HEP**, China used intermediaries and commission agents in influencing decisions and applied political and diplomatic pressure.
- In the case of **Hongshi Cement**, the Chinese company adopted a methodical and phased strategy throughout negotiations. It preferred private channel discussions before official institutional engagement. It handled issues in a sequential manner rather than conducting simultaneous multi-agenda negotiations. The company focused on profitability and operational viability over everything else.

China's negotiations practices with Nepal reflected the primacy of the Chinese Communist Party, tactics to maintain control, the balancing of long-term strategy vs temporary arrangements, and use of cultural dimensions. China always seeks to create a negotiating environment where it can exert external influences, use power asymmetry, practice assertive commercial diplomacy, and make use of proactive public diplomacy.

Financial Models. Many of the projects had a combination of grants and concessional loans. In the case of PRIA, China's Exim Bank provided funding tied to Chinese contractors and demanded an escrow account for CAAN's revenues. The recommended Chinese companies were often a condition for securing loans. In some cases, loan amounts were pre-determined with project selection coming later. Loan terms were not favourable to Nepal especially as Nepal bore most operational risks and the insurance costs were almost two and half times the normal rates (4.7% vs normal 2%).

The case of Hongshi, on the other hand, showed that the private investment model proved more effective than public-private partnerships or G2G models, especially regarding economic viability, market development, technology/knowledge transfer, and operational practices.

C. Nepal's Negotiations with China: Practices, Challenges and Weaknesses

Nepal's Negotiations Practices

During BRI, deep political divisions were seen regarding engagement with China. Communist party leaders showed a softer stance toward Chinese proposals; party-to-party relations influenced and overrode formal diplomatic channels. Coalition politics, especially between Nepali Congress and CPN-UML, shaped the

final agreement. While the UML appeared to endorse the Chinese draft, Nepali Congress produced its own draft.

In the later phases, Nepal preferred grants over commercial loans, required competitive bidding, resisted Chinese currency use and Free Trade Agreement, put increased emphasis on commercial viability, and limited the focus in five areas: economic cooperation; financial sector cooperation; transport, connectivity and logistics cooperation; trade, industrial capacity, and investment cooperation; and customs cooperation.

During high-level visits, Nepal focused primarily on infrastructure and economic cooperation, showed institutional weaknesses in negotiating capacity, and often accepted proposals and terminologies without adequate homework. Senior officials acknowledged that Nepal lacked preparations and was hasty in signing agreements and joint statements.

During trade and transit negotiations, Nepal lacked adequate technical preparation. Limited mandate was given to negotiators resulting in a reactive rather than proactive stance. Nepal struggled to put forward strong positions, although Nepal showed a more assertive stance since 2019 and displayed willingness to reject or renegotiate projects. These negotiations displayed limited trust between political leadership and civil servants. Politicians often transferred key personnel and sidestepped bureaucratic expertise. Deep political divisions affected negotiations.

In the case of PRIA, sponsored protests and local pressure played a crucial role in pushing the project forward. Nepal lacked independent feasibility studies and commercial viability assessments and did not sufficiently consider long-term debt servicing capacity.

In the case of aircraft deals, Nepali officials had limited space for real negotiations. Technical and operational issues revealed poor pre-agreement assessment, technical negotiators lacked proper certification capabilities and did not have sufficient knowledge about aircraft specifications during negotiations resulting in lack of due diligence in technical assessment.

The case of Budhi Gandaki showed that the early negotiation process frequently circumvented established institutional frameworks. For example, proper ministerial discussions were bypassed, cabinet-level deliberations were overlooked, legal frameworks were violated (including the Public Procurement Act 2007).

The project has now evolved into a public company model with mixed funding sources. The project underwent multiple policy reversals after initial award to CGGC without competitive bidding. The negotiations revealed close interactions between political and commercial interests leading to allegations of corruption and commission-based partnerships.

In the case of Border and Boundaries, Nepal has taken a cautious position and has been unable to address issues of: border pillar locations and boundary disputes, treatment of cross-border movements, and timeline for implementing joint inspections.

In the case of Hongshi Cement, Nepal displayed a stronger institutional capacity and issue handling. Institutions developed robust monitoring mechanisms through monthly committee meetings, engaged international expertise (UK law firm Herbert Smith Freehills), showed strong inter-institutional cooperation between IBN and Nepal Rastra Bank, developed comprehensive investment guidelines and focussed on technical negotiations and transparency.

Challenges and Weaknesses

Nepal showed significant weaknesses in diplomatic capacity. While the negotiations exposed limited technical expertise at bureaucratic level, frequent government changes affected negotiating consistency. During high level visits, the Nepali side failed to secure implementation of priority projects. Development priorities often remained at memorandum stage and many agreements were repetitive across visits.

In trade and transit negotiations, Nepal's poor documentation practices and poor institutional memory affected negotiations. Negotiations relied on personal relationships and individual capability rather than institutional capacity. Nepali institutions also displayed weak follow-up mechanisms and limited capacity to secure implementation.

The cases of PRIA, procurement of Chinese Airplanes and the Budhi Gandaki Project, have shown Nepal's institutional weaknesses in controlling corruption, ensuring economic benefits, and securing favourable terms. It means that Nepal continues to remain vulnerable to political rather than national interest-based decisions.

Even in the case of Hongshi cement, limited government resources affected infrastructure development, and resistance from the domestic private sector through anti-lobbying efforts showed vulnerability. IBN's dual oversight has also created potential conflicts of interest between PPP and Private Investments.

In summary, Nepal's negotiations practices display weaknesses at the policy and strategy level, political and institutional frameworks, negotiation process and capabilities and implementation and support. At the strategic and policy level, Nepal shows power asymmetry in regional relations, strategic deficits, policy inconsistency, inadequate understanding and recourse to informal and non-transparent negotiations.

At the political and institutional level, there is widespread political fragmentation and interference. Political dominance often marginalizes bureaucracy, leading to institutional weaknesses as well as lack of mandate and political support. Corruption and governance issues are other major bottlenecks.

Regarding negotiation process and capabilities, Nepal often lacks adequate preparation and capacity for negotiation. Other problems relate to language and communication, trust-building, negotiating under pressure, time pressure, and success metrics. Nepal also does not seek help from academic and technical experts and rarely has mechanisms to address implementation challenges.

D. Way Forward

Strategic Foundation. In order to manage asymmetric power relations with China, Nepal's starting point for negotiations should be to maintain good relations while adopting strategic positioning and institutional relations with strategic partners (eg, regional initiatives and international partnerships). Another way to respond to asymmetric power relationships is to minimize geopolitical influence through clear principles and strategic autonomy. Nepal must prioritize interest-based negotiations over conventional bargaining and stop asking for favours in order to adopt give-and-take principles.

Institutional Framework. Given the flaws in Nepal's negotiations practices, it is necessary to uphold institutional framework over informal or party-to-party negotiations, ensure proper coordination between different actors and institutions, build institutional memory, give clear mandates and support to the negotiations team, ensure ministerial expertise and document all negotiations experiences.

Negotiation Strategy. Successful negotiators invest heavily in understanding their counterparts' interests, positions, and cultural context before entering negotiations. Nepal must establish clear strategic objectives and bottom lines before entering negotiations with China. This requires developing maximum and minimum negotiating positions, identifying core national interests, and determining non-negotiable aspects of any agreement. Nepal should also develop clear alternatives (BATNA - Best Alternative to a Negotiated Agreement) and establish specific conditions under which Nepal would pause negotiations for further consultation, seek alternative solutions, or walk away from unfavourable terms.

Layered Negotiation. Nepal should adopt a layered negotiation strategy that mirrors China's methodical approach, testing waters through informal channels and visits before proceeding with formal proposals. Political leaders need to maintain involvement in the negotiation process while respecting the technical nature of working-level discussions.

Skills. In asymmetrical power relations with China, Nepal must focus on developing what experts call "dancing skills"-- the ability to navigate complex negotiations despite power disparities. This requires enhancing multiple competencies among diplomats, lawyers, and technical experts. Nepal also needs to build tactical adaptability in relation to process constraints like time pressure, control mechanisms, confidentiality pressures, and use of informal channels.

Process management. In order to strengthen negotiation outcomes, Nepal must also manage the process, which includes creating a level playing field, ensuring transparency, building trust and influence and building cultural competence. Process management also includes developing procedural expertise and protection mechanisms.

Protection mechanisms. Protection mechanisms include establishing clear protocols for exchanging concessions, maintaining detailed records of agreements, and ensuring proper documentation of all understandings. Negotiators must be particularly vigilant about verbal agreements, as these hold limited value without proper documentation. The negotiating framework must account for future implications of current agreements, particularly because concessions won in present negotiations could be eroded by future bilateral negotiations.

Implementation focus. To match China's skilled negotiators, Nepal must prioritize thorough preparation and composition of a proper team before entering bilateral talks. To improve implementation, Nepal should establish a clear matrix of actions with defined responsibilities, systematic monitoring mechanisms, regular progress review meetings, and accountability measures.