International Journal of Academic Excellence and Research (IJAER)
e-ISSN: 3107-3913 || Peer Reviewed || Open Access
Publication Impact Factor (I2OR) : 2.015
Vol. 02, No. 02, April-June, 2026, pp 208-214

www.mgmpublications.com

Informal Trade at Raxaul-Birgunj Trade Point along India-Nepal Border: Socio-Economic Dynamics, Governance Challenges and Policy Pathways

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Citation: Bagaria, R. (2026). Informal Trade at Raxaul-Birgunj Trade Point along India-Nepal Border: Socio-Economic Dynamics, Governance Challenges and Policy Pathways. International Journal of Academic Excellence and Research, 02(02), 208–214. https://doi.org/10.62823/IJAER/02.02.236

Abstract: *India and Nepal maintain one of the most deeply intertwined bilateral relationships, which is shaped by open border, cultural ties and economic interdependence. The significant amount of informal economic activity occurs outside official channels between India and Nepal. The study highlights the socio-demographic profile of informal traders on the basis of primary survey data. The study assesses the investment patterns of informal trade income and the obstacles faced by the informal traders. The sample consists of petty traders, farmers, shopkeepers, brokers and daily wage carriers. The findings of the study reveal that informal trade serves as a critical livelihood source for border communities. The respondents invest their informal income on children's education, healthcare and housing. The findings reveal that corruption, unpredictable enforcement and financial exclusion, constrain traders and increase their vulnerability. The study concludes with policy recommendations for reducing informality by the ways of regulatory reforms, trade facilitation and inclusive financial access.*

Article History:
Received: 12 June, 2026
Revised: 19 June, 2026
Accepted: 25 June, 2026
Published Online: 29 June, 2026

Keywords:
Informal Trade, India-Nepal Informal Trade, Raxaul-Birgunj, Trade Facilitation, Open Border, Price Differentials, Livelihood.

Introduction

India and Nepal share one of the most distinctive and multidimensional bilateral relationships in South Asia. This relationship is ancient, cooperative, periodically contentious and institutionally complex. The connection of the two countries is defined by geographical proximity, common cultural traditions, extensive economic dependence and the legally guaranteed free border. An overview of India-Nepal relations is a crucial precondition for analysing the informal trade dynamics between the two nations (Ministry of External Affairs, Government of India). Table 1 presents the India-Nepal merchandise trade statistics over the last couple of years:

Table 1: India-Nepal Merchandise Trade Statistics

Sl.	Year	2020-21	2021-22	2022-23	2023-24	2024-25
1.	Export from India to Nepal *(US$ million)*	6,838.46	9,645.74	8,015.99	7040.98	7334.87
2.	Export from Nepal to India *(US$ million)*	673.16	1,371.04	839.62	831.11	1201.48
3.	Total Trade *(US$ million)*	7,511.62	11,016.79	8,855.61	7872.09	8536.35

Source: *Ministry of Commerce and Industry, Govt. of India.*

The concept of 'informal trade' is not homogeneous and has varying interpretations in empirical studies. The basic definition of informal trade is the trade in goods and services outside of officially regulated economic systems, without official records, without the enforcement of customs authorities and without the usual legal obligations such as tariffs, certifications and other necessary documentation (UNCTAD, 2019). This wide definition covers a diverse set of activities with very different economic, legal and social rationales. Based on the framework provided by Pohit and Taneja (2000), informal trade between India and Nepal can be broken down into three mutually distinct sub-categories:

- **Pure Smuggling (Illegal Trade):** The deliberate and secret transport of a commodity over an international boundary without regard for the law to evade the tariff and non-tariff barriers. This includes contraband items such as drugs, counterfeit money and illegally traded wildlife products as well as legal goods being traded without customs clearance and/or obeying regulations. Pure smuggling is motivated by the opportunity of arbitrage and is a conscious and deliberate attempt to break the law.
- **Parallel Market (Extra-Legal Trade):** It is a large part of the informal trade in the India-Nepal context that is technically illegal according to the law, but in practice, it is allowed by the authorities because of governance capacity constraints and social necessity of such exchanges. It also involves the transport of small amounts of everyday consumer products by local border dwellers that cross the border to buy more at a lower cost. This category is a merger of formal consumption of the individual and organised commercial activity.
- **Unregistered and Unlicensed Trade:** This category involves transactions undertaken by trading enterprises that are not registered, that do not have a licence or fail to meet labour and other applicable laws. These are not necessarily involved in direct smuggling across the border but operated in the informal sector by avoiding taxes, off-book financial transactions and employment of informal workers. In India-Nepal trade, these businesses are frequently located as middlemen between border crossing carriers and markets in the city.

One of the significant challenges of informal trade is to quantify it. Because official statistics record only formal trade flows and informal trade operators have strong incentives to remain invisible to regulatory authorities. However, various indirect methodologies have been deployed by researchers to estimate the scale of informal trade between India and Nepal. These studies have provided consistent evidence that informal trade constitutes a substantial share of total bilateral economic exchange between two countries. Pudasaini (2025) analysed Nepal-India bilateral trade asymmetries and found that India accounts for approximately 59 percent of Nepal's total imports and over 80 percent of its exports. Aggregate import discrepancy indices stood at 4.2 percent with product level variation concentrated in textiles, consumer goods and medium duty products.

Commodity specific surveys and field studies provide more granular evidence on the composition of informal trade. In September 2022, India imposed export duty on rice and in July 2023, the country completely banned the export of white rice (excluding basmati rice). These measures severely affected the formal trade of the staple grain to Nepal. SAWTEE-IFPRI's research revealed that approximately 40 percent of the rice consumed in Nepal is imported formally, while the remaining 60 percent is imported informally, mostly by women and low-income groups who transport rice across the open border. This discovery shows that the unilateral food security policies of India can have macroeconomic consequences on the trade dynamics in Nepal (CSISA, SAWTEE, & IFPRI, 2025).

Review of Literature

Rao et al. (1997) from Research and Information System for Developing Countries (RIS) conducted multi-country comparative study that examined informal trade flows with Bangladesh, Nepal, Bhutan and Myanmar. They established that the scale of informal trade was correlated with the level of tariff differentials, the permeability of the border and cultural continuity of borderland communities. Taneja (1999) established the conceptual terrain and identified that informal trade persisted despite regional trade liberalisation under the South Asian Preferential Trade Arrangement (SAPTA). Because the transaction costs of formal trade remained prohibitively high for small and medium traders.

One of the most influential works of informal sector theory is William Maloney's (2004) 'Informality Revisited.' Maloney challenged the dominant view that the informal sector is a residual category of labour market failure having the features of low productivity, exploitation and involuntary exclusion from the formal economy. Based on evidence from Latin American labour markets, Maloney argued that many informal sector participants voluntarily choose informality because the regulatory costs of formal compliance such as taxation, licensing fees, labour regulations and bureaucratic burden, outweigh the benefits. This makes informality a rational entrepreneurial choice rather than a failure outcome.

Pohit and Taneja (2000) conducted primary surveys in three countries to map the institutional characteristics of informal trade markets. They found that ethnic ties and kinship networks played a dominant role in sustaining informal trade. The principal policy implication was that formal trade's transacting environment must be substantially improved to compete with the social infrastructure of informal channels. Taneja et al. (2004) argued that the persistence of informal trade is one of the most important explanations for the paradox of low formal intra-regional trade in South Asia. Because substantial economic exchange is already occurring through informal channels, the demand creating effect of formal trade liberalisation is partially captured by the existing informal system rather than generating entirely new trade flows.

The WIEGO (Women in Informal Employment Globalizing and Organizing) working paper (2010) provided the most comprehensive overview of the informal economy across five South Asian countries (Bangladesh, India, Nepal, Pakistan and Sri Lanka). They documented that an average of 60 percent of employment in developing countries is in the informal sector and that the informal economy in Nepal was approximately 40 percent of the official economy during the study period. Taneja (2010) examined how the treaty framework specifically the Treaty of Trade (2009) and the Treaty of Transit enabled and constrained informal trade. She argued that treaty provisions that create tariff asymmetries such as differential treatment of edible oils incentivise rule-of-origin violations. This analytical insight that the formal regulatory framework is internally contradictory with respect to informal trade is an important finding that informs policy recommendations of the present study.

Taneja et al. (2019) examined the bilateral trade and investment relationship between India and Nepal to identify policy measures that can enhance economic cooperation. They highlighted untapped trade potential, tariff and non-tariff barriers, underutilisation of tariff rate quotas, rules of origin constraints and physical infrastructure gaps at border crossings. They also reviewed trends in Indian foreign direct investment in Nepal. They found that despite India being Nepal's dominant trade and investment partner, substantial growth potential remains unrealised due to structural and regulatory impediments.

Focal Issues and Instruments

This study examines the nature of informal trade at the Raxaul-Birgunj border which is one of the commercial trade points between India and Nepal. The site was selected considering the factors like commercial importance, easy access and its ability to represent the broader patterns of informal trade. The study aims to identify socio-demographic profile of respondents engaged in informal trade. It highlights the effect of informal trade income on local communities engaged at border trade points. The study identifies regulatory, financial and institutional challenges faced by informal traders and policy interventions to effectively address these challenges. Data for this study were gathered through a structured questionnaire survey. A total of 100 respondents from the Indian side of the border were selected to understand their experiences and views on informal trade. Respondents were selected through purposive sampling. Mean scores and standard deviations were calculated to rank the challenges and the perceptions.

Socio-Demographic Profiles

The socio-demographic profiles such as gender, age, education and occupation, provide vital information of the sample. These variables are essential for understanding their challenges, experiences and policy preferences. There is significant participation of females (38 percent) in informal trade. Their participation seems to be substantial due to their greater reluctance to engage in survey processes. The 62 percent male respondent' share reflects the greater representation of men in the informal trade. The age distribution reflects that informal trade at Raxaul-Birgunj is dominated by working age adults. The 30-40 years age group constituting the largest group (33 percent), followed by the 40-50 years age group (26 percent) and the 20-30 years age group (22 percent).

The educational profile of respondents is skewed significantly toward lower educational levels. A combined 33 percent of respondents are either completely illiterate (12 percent) or have education only up to primary level (21 percent). The largest single educational attainment group is secondary school completers (38 percent). The combined share of respondents educated up to Class X or below stands at

71 percent. However, 29 percent of respondents have education at higher secondary or graduate level. The occupational distribution is among the most important findings in the socio-demographic section. The 38 percent of respondents are full-time informal cross border traders. Farmers & traders (28 percent) represent the next largest group followed by Small shopkeepers and retailers (17 percent), Brokers and intermediaries (the dalals) (9 percent) and Daily wage labourers (8 percent).

Impact of Informal Trade

The data pertaining to investment of informal income as a resultant of informal trade engagement is the most significant finding of the study. The study found that 69 percent of informal traders have used their income from informal trade to support their children's education.

Table 2: Investment Enabled by Informal Trade Income

Area of Investment / Improvement	Freq.	Percent (%)
Children's education.	69	69.0
Healthcare expenditure for family.	58	58.0
Better housing or home improvement.	51	51.0
Starting or expanding a small business.	36	36.0
Purchase of livestock or productive assets.	29	29.0
Agricultural land purchase or improvement.	21	21.0
None of the above.	8	8.0

This investment pattern has significant implications for policymakers and practitioners working in the field. Table 2 suggests that informal trade income is playing a real and significant role in keeping children in school. Healthcare (58 percent) and housing (51 percent) follow as the second and third most commonly cited investment pattern which confirm that informal trade income is being channelled into durable welfare improvements. Business investment (36 percent) demonstrates the forward linkage effects of informal trade income. More than a third of respondents have used informal trade income to start or expand commercial operations such as shops, transport and service businesses. Only 8 percent reported no investment enabled by informal trade income.

Challenges Faced by Informal Traders

The regulatory challenge data confirm an alarming governance reality at Raxaul-Birgunj border. The most severe regulatory challenge is requirement to pay unofficial fees or bribes. It indicates that corruption based extraction from informal traders is not an occasional event but a structural at this corridor. Unpredictable enforcement is rated the second most severe regulatory challenge. It is more dangerous for informal traders as unpredictability makes it impossible to plan commercial operations or price risk.

Table 3: Mean Severity Scores of Regulatory and Administrative Challenges

Regulatory/Administrative Challenge	Mean	S.D.
Requirement to pay unofficial 'fees' or bribes.	4.44	0.71
Unpredictable enforcement - notice/confiscation.	4.28	0.80
Harassment by customs or excise officials.	4.17	0.85
Different rules on the two sides of the border.	3.86	0.99
Lack of a formal grievance redressal mechanism.	3.74	1.03
Language barriers.	2.38	1.17

Harassment by customs officials is associated with bribery and unpredictability findings of the study. The officials use harassment as a tool by the ways of applying extortion and deploying enforcement. The different rules on the two sides of the border create confusion among informal traders. The goods classified one way in Indian customs are classified differently in Nepali customs. Language barriers receive the lowest rating due to linguistic continuity of the Terai borderland.

As far as the economic challenges are concerned, financial exclusion is rated at the highest. The importance of this constraint for scale and safety of informal trade operations is very vital. This presents a gap in the financial inclusion landscape of border communities. The availability of micro-finance and credit products for informal traders will attract them to formal ways of cross border trade operations.

Table 4: Mean Severity Scores of Economic & Market Challenges

Economic/Market Challenge	Mean	S.D.
No access to formal credit or loans for trading capital.	4.16	0.88
Price fluctuations making it hard to predict profits.	4.03	0.91
Lack of storage/warehousing facilities at the border.	3.78	0.99
Competition from large-scale formal or informal traders.	3.61	1.04
Loss of goods due to spoilage/damage in transit.	3.41	1.08

Price fluctuation is rated the second highest economic challenge. It creates commercial uncertainty in goods such as rice, vegetables, edible oil and petroleum; and particular in perishable agricultural goods. Lack of storage and warehousing infrastructure is also rated a challenge for informal traders at the border as it increases the price fluctuations. In the absence of cold chain or storage capacity, traders in perishable goods sell their goods at lower prices.

Policy Perceptions and Suggestions

The policy priority ranking provides a clear, direct and actionable message from the informal trader community at Raxaul-Birgunj border.

Table 5: Policy Priority Ranking by Informal Traders

Policy Measure	Mean Rank	S.D.	Primary Beneficiary
Reduction or elimination of customs duty on key informally traded goods.	1.94	1.12	All traders, especially commodity traders & carriers.
Simplification and digitisation of cross-border documentation for small traders.	2.21	1.19	Educated small traders; shopkeepers; farmer-traders.
Access to micro-credit and financial services for informal traders.	2.49	1.22	Female traders; daily wage carriers; new entrants.
Establishment of designated small-trader corridors at border crossings.	2.88	1.26	Foot-carriers; bicycle transporters; vegetable traders.
Joint India-Nepal border markets with formal and informal vendor sections.	3.48	1.29	Long-tenure brokers; dalals; organised traders.

Duty reduction on key informally traded goods emerges as the overwhelming top priority. It is consistent with the earlier determining factor analysis of the study, where price differentials and duty avoidance were rated as the two most powerful economic drivers of informal trade. The traders are demanding a policy in which tariff-induced price eliminates informal trade economic rationality. This step will reduce their incentive for using informal channels. Documentation simplification and digitisation is rated the second highest priority which reflects traders' direct experience of the procedural inaccessibility of formal channels. Access to micro-credit and financial services measure reflects the acute credit constraint and is particularly urgently demanded by the most economically marginalised traders.

Designated small-trader lanes at border crossings reflect a practical infrastructure demand with high face validity. It emphasises on the creation of fast, low-hassle crossing lanes at the Raxaul ICP for small traders. It will reduce the unofficial payment burden, exposure to harassment and encourage voluntary use of formal channels for small consignments. Joint India-Nepal border markets receive the lowest priority reflects traders' scepticism about the political feasibility of such institutional arrangements under current bilateral diplomatic conditions.

Conclusion

The study focuses that informal trade at the Raxaul-Birgunj corridor is a structured livelihood system embedded in socio-economic fabric of border communities. The findings of the study reveal that income generated through informal trade activities is invested on children's schooling, healthcare and housing improvements. The findings also reveal economic and regulatory challenges faced by informal traders at the border. The key challenges are demands for unofficial payments, random confiscation and harassment by customs and other border officials. The financial exclusion which limits trade operations is also being faced by the informal participants. The study suggests actionable measures such as duty rationalisation on key informally traded goods, simplified documentation, access to credit and designated small-trader crossing lanes. Reducing informality at Raxaul-Birgunj is a pathway to improved bilateral economic relations and enhanced border community welfare along India-Nepal trade corridor.

Acknowledgement

This study is the part of Seed Money Project sanctioned and funded by Mahatma Gandhi Central University, Motihari (Bihar) under Research Promotion Scheme (A scheme to award seed money to faculty members at the level of Assistant Professor). **The author acknowledges the financial assistance provided by the University under the scheme.**

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