

# **Opportunities and Challenges of Tourism Financing**

**A Study on Demand and Supply; Status, Structure, Composition and  
Effectiveness of Tourism Financing in Nepal**

**Bishnu Prasad Gautam**

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*OPPORTUNITIES AND CHALLENGES OF*  
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**BISHNU PRASAD GAUTAM**  
MBA, Ph. D.

## PREFACE

Tourism as widely understood, being the temporary or short-term movement of people outside their normal place of residence has become an indispensable subject matter in various disciplines and emerged as an important sector in the economy of every country. It has become a subject of considerable interest for many scholars as well as for business entrepreneurs. It has been generator of income and employment. The economic impact of tourism is such that it not only attracts the attention of the people but also of the country.

The establishment, nursing and growth of the business require the finance. It is also required for the expansion, growth and sustaining of the business. Various aspects of tourism including the contribution, impacts, problems and prospects have been analyzed through academic research. On tourism financing scarcity of the academic literature was observed. This made it worthwhile to explore the status of tourism finance especially with reference to Nepal.

Despite the abundant potentialities for the development of tourism in Nepal, the country is not yet fully able to achieve the benefits from tourism industry. Realizing the high prospects of tourism development, the study is made in triangular form. The first is the impact of tourism and tourism financing on the development of tourism and economic growth. The second is views of the TBE (demand side) about the effectiveness of financing and the third is the views of the banks and financial institutions (supply side). The study also incorporated the magnitude of tourism financing, structure, pattern and the indicators of financing as well as the effectiveness of tourism financing.

The study is based on primary data collected from the tourism business enterprises as well as from banks and financial institutions using a structured questionnaire and also on secondary data collected from various publications.

It has employed various mathematical and statistical tools such as annual rate of change in percentage, ratio analysis, correlation coefficient, Phi-coefficient ( $r_{\phi}$ ), correlation coefficient, Chi-square ( $\chi^2$ ) test, t-Test for two sample means and regression analysis (OLS).

The present study is divided into seven chapters. Chapter 1 is an introductory chapter covering the background, concept of tourism and tourism financing, significance objectives and methodology of the study. Chapter 2 presents a theoretical underpinning for the tourism and tourism financing.

Chapter 3 presents the profile of the Nepalese tourism industry. Chapter 4 examines the sources of tourism financing and explores about the impact of tourism and tourism financing in the economy.

Based on the responses Chapter 5 analyses the structure of finance of various tourism business enterprises and examines the variation in the structure based on types and ownership of business. Chapter 6 analyses the responses of banks and financial institutions. It attempts to examine the methods of proposal analysis and techniques of credit appraisal.

Finally, chapter 7 summarizes the findings and conclusions of the research including the policy implications and suggestions.

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– Bishnu Prasad Gautam

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## ACRONYMS

ADB	=	Asian Development Bank
ADB/N	=	Agricultural Development Bank, Nepal
Banks	=	Commercial Banks
BFIS	=	Banking and Financial Institutions Statistics
BFI	=	Banks and Financial Institutions
C/D Ratio	=	Credit Deposit Ratio
CBS	=	Central Bureau of Statistics
Disb.	=	Disbursement
DW (d)	=	Durbin Watson 'd' statistics
ESCAP	=	Economic and Social Council for Asia and the Pacific
FADOT	=	Foreign aid disbursement in other sector including tourism
FDI	=	Foreign Direct Investment
FI (FIs)	=	Financial Institutions
FINCOOPS	=	Financial Cooperatives Societies
FINGO	=	Financial Non Government Organization
Forex	=	Foreign Exchange
FXET	=	Foreign Exchange Earning from Tourism
FY (F. Y.)	=	Fiscal Year (year ending mid-July)
GDP	=	Gross Domestic Product
GDPN	=	Nominal Gross Domestic Product
GDPT	=	Contribution of Hotel, Trade and Restaurant on GDP
GICA	=	Government investment in civil aviation
GIR	=	Government's internal revenue
GON	=	Government of Nepal
HAN	=	Hotel Association of Nepal
HMG/N	=	His Majesty's of Government of Nepal now Government of Nepal
ICC	=	International Chamber of Commerce
ICIMOD	=	International Centre for Integrated Mountaineering Development
IGIDR	=	Indira Gandhi Institute of Development Research
IMF	=	International Monetary Fund
INVT	=	Investment
IUCN	=	International Union for Conservation of Nature and Natural Resources
JV	=	Joint Venture
LDSCB	=	Service sector loan disbursement of Commercial banks
LDTNIDC	=	Tourism sector loan disbursement of NIDC
Ln. (ln.)	=	Log Value (base of 10)
M1	=	Money Supply (Narrowly defined)

M2	=	Money Supply (Broadly defined)
MOCTCA	=	Ministry of Culture, Tourism and Civil Aviation
MOF	=	Ministry of Finance
MOL	=	Ministry of Law
MOTCA	=	Ministry of Tourism and Civil Aviation
NARA	=	Nepal Association of Rafting Agents
NATA	=	Nepal Association of Travel Agents
NBFI	=	Non Bank Financial Institutions
No.	=	Number
NRB	=	Nepal Rastra Bank
NTB	=	Nepal Tourism Board
OLS	=	Ordinary Least Square
QEB	=	Quarterly Economic Bulletin
RGDPT	=	Ratio of GDPT to Gross Domestic Product (GDPN)
Rs.	=	Rupees (Nepalese Currency)
TAAN	=	Trekking Agents Association of Nepal
TAX	=	tax revenue
TB	=	Tourism Business
TBE	=	Tourism Business Enterprises
TEXP	=	Development expenditure of government in tourism sector
TFSD	=	Tourism Financing (Supply)
TNHB	=	Total number of Hotel Beds
TNHR	=	Total number of Trained Human Resources
TNTB	=	Total number of Tourism Business
TRAV	=	Trade Volume (Total trade)
TTAR	=	Total number of Tourists Arrival
UN	=	United Nations
UNCTAD	=	United Nations Commission for Trade and Development
WB	=	World Bank
WDR	=	World Development Report

# I

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## CHAPTER

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## INTRODUCTION

- 1.1 BACKGROUND OF THE STUDY
- 1.2 CONCEPT AND SCOPE OF TOURISM
- 1.3 CONCEPT AND SCOPE OF TOURISM FINANCING
- 1.4 OVERVIEW OF NEPALESE ECONOMY
- 1.5 RATIONALE OF THE STUDY
- 1.6 OBJECTIVES OF THE STUDY
- 1.7 RESEARCH METHODOLOGY AND DATA SOURCES
  - Research Design and Sources of Data
  - Preliminary Survey, Interviews and Questionnaires
  - Population and Sample
  - Data Collection Procedure
- 1.8 METHOD OF ANALYSIS AND MODEL
- 1.9 POSSIBLE SOURCES OF BIAS
- 1.10 CHAPTER SCHEME OF THE STUDY

**CHAPTER**

**I**

**INTRODUCTION**

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**1.1 BACKGROUND OF THE STUDY**

Tourism has been considered as fundamental instrument for the economic development of the country. It should be the main reason that many governments, developing or developed are involved in the design, development and operation of the tourism industry. It has been a focal issue in most of their Periodical Plans. The investment, involvement and participation of the public sector have been a real fact over the years. Similarly, private sector has also equally been involved in this industry.

As tourism is growing rapidly, it has attracted the attention from several sectors, formal informal, public private and national international. Consequently, various aspects of tourism including contribution, impacts, problems and prospects have been analyzed by various scholars, such as Pearce Douglas (1981, 1989), Ritchie (1980) Ghali (1976), Diamond (1977) and Jamieson and Jamal (1997) etc. Several analysis have also been performed to find out the linkages of tourism by Emanuel de Kadt (1978), Goeldner, Ritchie and McIntosh (2000), Smith (1989), Douglas Frechtling (1987), Seaton and et al. (1994), John Tribe (1999), and Norbert Vanhobe (2005). Initiatives in tourism industry is aimed at creating awareness and cooperation among people, earning foreign currency, providing the employment opportunities, and thereby benefiting the people, society, country and region. Every investment is aimed at creation and accumulation of facilities, for ensuring the required services and proper infrastructures for the efficient operation and optimum utilization of the industry. For this purpose, financing is must. Proper modes of finance ensure proper growth, efficiency and effectiveness.

Tourism industry, unlike some other industries, is critical enough to be affected and often damaged by a change in weather/season, occurrence of incident and even by rumor or propaganda. Despite of joint efforts from public and private sectors to overcome problems and continuous investment, the outcome has been usually embarrassing.

**1.2 CONCEPT AND SCOPE OF TOURISM**

Tourism nowadays has been an essential activity all over the world. The form of tourism can be of various types. It is an activity, discipline, industry or profession depending upon the application method and criteria. Most of the people are quite familiar with the meaning of tourism though they are not well aware about its prospects and consequences.

## 2 Introduction

The word tourism is related to “TOUR” which is derived from a Latin word “TORNUS”. It means a tool for describing a circle of turners’ wheel (Bhatia, 2002: 85). The notion of a round tour or a package tour has come from this word. In fact, it is the essence of tourism.

In 1910, Hermann Van Schullard, an Austrian economist has tried to clarify few points in his definition particularly for operation, sum of operation, related activities and defined tourism as “The sum total of operations mainly of an economic nature, which directly relate the entry, stay, and movement of foreigners inside and outside a certain country, city or region.” In 1937 the League of Nations proposed a definition of “tourist as one who travels for a period of 24 hours or more in a country other than that in which he usually resides” (Karma and Chand, 2004: 34 and Bhatia, 2002: 86). The definition obviously considers the purpose of visit including the individuals traveling for pleasure and or for other reasons.

Similarly, in 1942 two Swiss Professors Walter Hunziker and Kurt Krapf of Berne University defined Tourism as “the sum of the phenomena and relationships arising from the travel and stay of non-residents, in so far as they do not lead to permanent residence and are not connected with any earning activity” (Karma and Chand, 2004: 34; Sharma, 2004: 14). This definition is some how broader and incorporates both travel and stay with clear description of tourism, migration, earning activity and pleasures. International Association of Scientific Experts in Tourism (AIEST) later adopted it.

In 1963, International Union of Official Travel Organization (IUOTO) now the World Tourism Organization, issued various definitions and recommendations during the auspicious occasion of UN Conference on International Travel and Tourism held at Rome Italy. It introduced the terms like ‘visitor’ to describe any person visiting a country other than in which he has his usual place of residence (Kunwar, 1997: 8 and Bhatia, 2002: 88).

In 1976, Tourism Society of England defined tourism, as “Tourism is the temporary short term movement of people to destinations outside the places where they normally live and work and their activities during the stay at these destinations. It includes movement of people for all purpose as well as day visits or excursions” (Ghimire, 2002: 13).

Mathieson and Wall had defined tourism incorporating the basics of tourism as a temporary movement to destinations outside the normal home and workplace as well as the activities undertaken during the stay including the facilities created to cater for the needs of tourists (Karma and Chand, 2004: 34). Burkart and Medlik also provided similar definition of tourism as temporary, short-term movement of people to destinations outside the place where they normally live and work including their activities during their stay at these destinations (Sharma, 2004: 15)

Tourism is based on the desire for the pursuit of happiness (Enzensberger, 1996: 135). It is essentially a pleasure activity in which traveling from one place to another, country to country and region to region is involved. Similarly, it also involves money for the services and time for that. It basically, includes much travel. It is distinct with related concepts of leisure, recreation, travel and or migration. Therefore, tourism is the result of temporary movement of people from their normal places of residence and work. The activities undertaken during their stay in those places and the facilities provided to satisfy their needs results on tourism activity.

Tourism, in fact comprises the activities of persons traveling to and staying in places outside their usual environment. The period of visit should not be more than one year for leisure, business and other purposes and the exercise of an activity should not be remunerated from the place visited. The words like

visitor, traveler, wanderlust and tourist contain the instinct meaning describing a person traveling to a place other than his/her usual environment. The main purpose of the trip may differ with an activity carried out in the place visited.

Tourism is an ever increasing and expanding service industry both at national and international level. Nowadays it has become one of the crucial concerns not only of the nations but also of international community as a whole. It has come up as a decisive link in gearing up the pace of socio economic development world over (See McIntosh et al., 1995: 3). It is the temporary movement of people to destination(s) away from their usual habitat, the activities entered upon during their stay and the facilities developed to provide for their requirements. Tourism has intrigued many scholars, economic theorists, financial analysts and many others to probe into the various facets of tourism thus enabled the experts to be indulged deeper in the subject.

### **1.3 CONCEPT AND SCOPE OF TOURISM FINANCING**

There are various sources of financing for the tourism business. In the first part, the discussion is focused on the sources of financing in terms of supply whereas in the second part the discussion continues in terms of demand for financing.

The development of any sector in the economy needs more and more investment. Tourism sector is not an exception; it certainly needs continuous and huge investment. Nepal being a developing country with limited infrastructure and lack of accumulated capital seriously requires huge investment in most of its socio economic sectors. Such investment is not an easy task, thus announces for the alternative sources and mechanisms of financing. Further, tourism being capital-intensive industry also requires huge amount of capital for the infrastructure and superstructure. In addition to this, more investment and financing is necessary for support services and for the promotion of related industries. Therefore, the investment financing is not necessary only for tourism infrastructure and superstructure but also for every facets of tourism industry.

The availability of finance to develop and promote the tourism industry is critically important for further growth and development of tourism industry and economy (Government of South Africa: 1996).

The establishment, nursing and growth of the trade, industry and commerce owes to the finance. Finance is rightly said to be the lifeblood of the business. Funds are required to commence and carry on the business. It is also required for the expansion, growth and sustaining (Siddiqui and Siddiqui, 2005: 273). Therefore, every business enterprise whether large or small needs finance to run the operation. Business enterprises require capital in various forms comprising a number of assets and of various types both fixed (permanent) and current nature (Mahat, 1981:1).

A firm secures whatever capital it needs and employs it in activities such as production, marketing and finance. It requires real assets and financial assets to carry on its business. Real assets include tangible assets (plant, machinery, office, factory, furniture and building) and intangible assets (technical expertise, technological collaborations, patents and copyrights) whereas financial assets include securities or financial instruments (shares and debentures), lease obligations and borrowing from banks or financial institutions (Pandey, 2004: 3-4).

#### 4 Introduction

Business finance includes money funds and capital. It includes both owned capital and borrowed capital. It is a wider term concerned with planning, acquisition, utilization and management of funds (Siddiqui and Siddiqui, 2005: 273). Though finance is must for the productive operation, the requirement or its magnitude basically, depends upon the nature and size of the enterprise.

The types of financing can be various based on purpose of financing, methods and time duration. It simply means that it can be classified as internal and external, formal and informal as well as domestic and foreign.

I. M. Pandey (2004: 442) viewed ordinary shares, preference share and debentures as important types of securities that the firms generally use to raise funds to finance their activities whereas Whitehouse and Tille (1993: 122) viewed the equity and borrowings as the main types of business finance in addition to the raising finance from internal sources. Similarly, Lawrence Gitman (2004: 522) viewed the total capital as composed of debt capital and equity capital.

Further, Whitehouse and Tilley (1993: 122, 135) have discussed the sources and types of finance dividing them in two broad categories of commercial and non-commercial sources of finance. Again, they have divided commercial finance in short and mid-term finance as equity, borrowing, debt factoring, invoice discounting leasing, hire purchase and bills of exchange) as well as medium and long-term finance such as venture capital, long-term borrowing (share issue, debenture).

Another classification of financing in internal and external source is based on the flow of funds. The internal source comprises the retained earning, reserves, surplus and depreciation whereas the external source comprises issuance of shares, debentures, borrowings from banks and financial institution as well as trade credits.

Financing policy, in simple words means to design the capital structure with appropriate proportions of debt and equity. Every business firm aims at maximizing the firm value by minimizing the overall cost of capital. In fact, the cost of capital is useful in deciding about the methods of financing at a point of time (Pandey, 2004: 168).

In such broader view, the central issue of financial policy is the wise use of funds and the central process involved is a rational matching of advantages of potential uses against the cost of alternative sources so as to achieve the broad financial goals, which an enterprise sets for itself (Soloman, 1969: 3).

The mix of debt and equity is called capital structure of the organization. As such, the financing policy of an organization has an important bearing upon the survival of the organization because it influences the flexibility in the operations of the business. Too much of debt in the organization means high fixed cost or interest obligations, which may even endanger the survival of the organization (Singh, 2001: 126). The importance of financial management in tourism industry can be hardly overemphasized (Singh, 2001: 124). Financing decisions are more crucial because it has an impact on profitability (Witt and et al, 1997: 103). Financing policy and system includes all activities pertaining to planning, acquisition and management and evaluation of the funding in the organization.

#### **1.4 OVERVIEW OF THE NEPALESE ECONOMY**

Nepal is a small country with majority of its people engaged in agricultural (about 81 percent) activities. However, the agricultural sector contributes only 55 percent on the gross domestic product and 50 percent on the total export. It has received the top priority in every periodical plan and has enjoyed the

large amount of budget allocations over the years. The productivity has remained low because of various problems ranging from some structural problems to difficult topographical condition, lack of irrigation facility, traditional practice and lack of commercialization.

Similarly, manufacturing sector is also small providing the employment for 10 percent population and contributing about 20 percent in the gross domestic product. Many efforts are directed for the development of the industrial sector with priority and resources but the achievement has been embarrassing over the years.

Water and forest resources are the endurable resources of the country in contrast to the mineral resources. However, the deforestation problem over the last three decades raises concerns and cautions for conservation and utilization pattern. Notwithstanding, utilization of water resources requires huge investment. The foreign trade is characterized by an export of primary goods, lack of diversification and large trade deficit. Despite of large trade deficits, Nepal's external accounts have been partly offset by invisible surpluses. There are three major sources of convertible foreign exchanges in Nepal, foreign aid, merchandise exports and tourist expenditures (Shrestha, 1999: 6).

Tourism industry seems to be an endurable industry because of its vast potential. Some people may like to call Nepal as the unique museum in the world. It is one of the richest countries in the world in terms of bio-diversity. The elevation of the country ranges from 60 meter above from the sea level to the highest peak on the earth - Mt. Everest at 8848 meter, all within a distance of 150 km. With climatic conditions ranging from sub-tropical to arctic, this wild variation fosters the variety of ecosystem, tropical jungles, and wild life. Further, this spectacular geography is also one of the richest cultural landscapes anywhere. The country is a potpourri of ethnic groups and sub-groups who speak over 70 languages and dialects. It also offers an astonishing diversity of sightseeing attractions and adventure opportunities found nowhere else on the earth (Nepal Guidebook: 2002).

Moreover, the country offers numerous annual festivals that are celebrated throughout the year in traditional style highlighting various customs and beliefs (Nepal Guidebook: 2002). Hence, Nepal has a comparative advantage in the development of tourism because of its natural topography such as mountains, rich valleys, lovely landscapes and rich cultural heritage and so on.

With such vast potentials of the tourism, many countries around the world have enlisted it as a major destination. The "Observer" and the "Guardians" the famous British publications had rightly described Nepal as a second tourist state after the New Zealand in world tourism perspective.

Tourism industry has been considered as a major industry in Nepalese economy. More than 1.50 million people are employed directly or indirectly in this industry. This sector contributes more than 3 percent in GDP. Likewise, this sector earns more than 15 percent of total foreign currency and 30 percent of total revenue (NTB, 2005). With the perspective of foreign currency earning, employment generation, promotion of art and culture, conservation of heritage, promotion of cottage and small industry, increment in per capita income and transfer of know-how and awareness, the importance of tourism is over whelming.

The present status of tourism industry shows a slowdown, though it was remarkably important in Nepalese economy. With the recession in world economy, Nepalese economy is also facing some recessionary symptoms. The Maoist insurgency inside the country during the last 10 years and its

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consequences in law and order situation has an adverse impact in the tourism industry. As the rate of tourist arrival sharply decreased, some of the prominent effects started to prevail automatically drawing overall slackness and vulnerability in related business and other economic sectors.

Nepal has been paying an increased attention for the development of tourism from the very beginning since it welcomed foreign visitors after the advent of democracy in 1951. Therefore, tourism has a belated start in Nepal compared to other countries. Despite having enormous potentialities for tourism development, Nepal has not been able to develop it in a desirable manner (Shrestha, 1999: 3). The major reason behind this should be the lack of financing sources and mechanism.

### **1.5 RATIONALE OF THE STUDY**

Tourism has emerged as an important industry almost everywhere in the world. It has occupied a significant position and enjoyed the priority over the years.

Nepal is basically, a developing country. Landlocked in between two giant economies of the world, India and China, Nepal has very small agrarian economy, lacks industrialization and possesses few natural resources. There are only two natural resources with comparative advantages and clear prospects namely water and tourism (ADB and MOTCA, 1990: 88). However, both of them are challenging because of resource constraints and geographical difficulties. The development of hydropower requires a huge amount of investment on one hand and prospective buyer on the other. India may be a potential buyer given that the cost of production is minimum and the selling price comparatively cheaper, along with long-term arrangements through mutual understanding. In other words, the exploitation of water resources requires huge financing and vast market which is not an easy task.

In contrast, tourism does not suffer from such problems and dependency and thus appears to be a potential sector for the economic growth and development of the country (ADB and MOTCA, 1990: 89). However, it is not out of challenges because it is delicate and depends mostly on others for the growth and development.

Tourism is a vital sector of Nepalese economy as it contributes to correct the adverse trade balance and to generate the employment opportunities. The earning from tourism as percentage of GDP is 2.6 in July 2003, which has gradually increased from 1% in 1975. Though the contribution is negligible in comparison to other countries, there is still enough possibility to increase it considering the huge prospects. However, it has been suffering continuously in terms of management and proper funding.

Similarly, tourism is an activity generating a number of economic and social benefits in the country. It not only augments foreign exchange earning, the scarce resources of the country but also creates employment opportunities such as direct, indirect and induced, through backward and forward linkages with other sectors of the economy such as agriculture, industry and other service sectors. Tourism being a labour intensive activity generates employment opportunities to the vast number of underemployed and unemployed people of the country.

The time has come to study the direct investment in the tourism sector and to analyze it in terms of requirement. Likewise, to account the lending in tourism sector from various commercial banks and other financial institutions and to perform the corresponding analysis research is must. Obviously, tourism sector is broad in its characteristics, includes various sub-sectors and activities such as hotel and resorts,

travels and trekking and mountaineering, transportation and production industries, and thus requires proper analysis.

Therefore, the study provides various results, draws some conclusions and attempts to answer the questions regarding sources of financing, the need of borrowing and prospects of tourism financing. Similarly, it provides the elaborative discussions about the trend of financing, the effectiveness of financing and impact of tourism as well as of tourism financing on the economic growth and development of the nation.

However, there have been some studies and research in tourism to open up its broad arena, further studies are lacking. Thus, the proposed research particularly concentrating on the financing policy, pattern, structure and assessment is new and urgent justifying the need of the study. It is also in line with the requirement for the development of tourism at desired level.

## **1.6 OBJECTIVES OF THE STUDY**

Despite the abundant potentialities for the development of tourism in Nepal, the country is not yet fully able to achieve the benefits from tourism industry. Realizing the high prospects of tourism development, the study is confined, mainly for the assessment of tourism financing from both side demand and supply.

The primary objective of the present study is to inquire about the demand for and supply of tourism financing; existing status, structure, pattern and composition of tourism financing as well as to assess the impact and effectiveness of the tourism financing. Precisely, the objectives of the present study can be put as follows:

1. To inquire about the scope and inter-linkage of tourism and tourism financing as well as the economic impact of tourism and tourism financing through the review of relevant literature.
2. To present the profile of tourism industry in Nepal. For this purpose, the study reviews the evolution of tourism, plans, policies and programmes related to this industry and undertakes the descriptive analysis for the data related to the industry and tourists' arrival. It lists out the tourism products and infrastructure, distribution of tourism business and the organizational structure of tourism in Nepal.
3. To inquire about the supply of tourism financing from various sources such as the budget allocation of the government, foreign aid and loan disbursement, the lending of banks and financial institutions as well as the foreign direct investment from the secondary sources of data.
4. To inquire into the role of tourism and tourism financing on the economic growth of the country.
5. To inquire about the role and impact of foreign exchange earning from tourism, total number of tourists' arrival, total no. of tourism business, total no. of trained human resources and total no. of hotel beds on the economic growth of Nepal.
6. To inquire about the role and impact of various sources of tourism financing such as the banks and financial institutions, the government, and foreign aid and loan disbursement on the economic growth of Nepal.

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7. To inquire about the pattern and structure of financing of TBE.
8. To examine the variations in the structure of financing between various tourism businesses.
9. To examine the operating performance of the surveyed TBE.
10. To assess the effectiveness of the financing on TBE.
11. To inquire about the borrowing need of the TBE and prospects of tourism financing.
12. To examine the experience of the BFIs for lending to tourism industry.
13. To inquire about the practice of loan processing and credit disbursement.
14. To understand the credit appraisal process and to assess the relative importance assigned by the BFIs for the business and financial aspects of the borrowing company.
15. To examine the association, if any between the importance assigned to various business and financial aspects as well as to undertake the cross verification of the importance assigned between the business and financial aspects.
16. To inquire about the quality of tourism sector loan in the portfolio of the banks and financial institutions.
17. To inquire about the perception of the lending institutions and analyze the data related to the effectiveness of tourism financing.

## **1.7 RESEARCH METHODOLOGY AND DATA SOURCES**

### **A. RESEARCH DESIGN AND SOURCES OF DATA**

Data forms the basis of analysis. The secondary data, published by various authorities and agencies are important for forming a base, as well as to analyze the macro economic scenario. For the purpose of this study, data published by Nepal Rastra Bank, Ministry of Finance, Ministry of Tourism and Civil Aviation, Nepal Tourism Board and Central Bureau of Statistics are used. To carry out analysis at micro level, and to understand the finer aspects of tourism financing and tourism investment firm level data were gathered through questionnaires addressed to different types of units of tourism business (Appendix: A.1) and banks and financial institutions (Appendix: A. 2).

### **B. PRELIMINARY SURVEY, INTERVIEW AND QUESTIONNAIRES**

In the beginning, the general information related to the tourists' arrival, foreign exchange earning from tourism as well as the distribution of the tourism business enterprises and bank/financial institutions was collected in June 2005. Later, particularly during October - November 2005, some informal interviews were conducted. The pilot survey was also conducted through the use of the questionnaire. The questionnaires were fine-tuned based on feedback received during pilot survey.

Two sets of questionnaires were designed one for tourism business enterprises and another for banks and financial institutions. The questionnaire for the tourism business enterprises has four parts viz. introduction, existing financial structure, effectiveness of financing and business prospects and borrowing need. The second part is particularly designed to inquire about structure, pattern and magnitude of financing. It contains the figures for six years from Fiscal Year 1999/2000 to 2004/2005. The third and fourth part largely contain the questions to inquire about the perception of the tourism business enterprises regarding the effectiveness and prospects of financing.

The questionnaire for commercial banks and financial institutions has four parts viz. introduction, loan processing, analysis and effectiveness. The first part attempts to collect the data for 14 years, i.e. from Fiscal Year 1991/1992 to 2004/2005 about loan disbursement and loan outstanding total as well as for tourism sector. The questionnaire further attempts to inquire the perception about effectiveness of finance. Moreover, the information is also gathered about the quality of loan finance and the loan restructuring.

### **C. POPULATION AND SAMPLE**

In order to assess the status, funding sources, patterns and effectiveness of tourism financing; the study enquires it from both demand and supply side. In July 2005, there were 948 travel agencies, 740 trekking agencies, 92 rafting agencies, and 1006 hotels, comprising both star and non-star (MOCTCA, 2005: 78). The exhaustive population of the tourism business enterprises (in the demand side) thus comes to 2,786. Based on discussion with information supplier, it was observed that the details were not updated about the continuity of the organization.

In order to determine the population size, the study employed three simple but deliberate criteria. These criteria are related to (i) the registration of the business as a tourist service provider in the tourism industry division, Ministry of Tourism, (ii) operation of the business at least for three years and (iii) the subscription of the membership in related tourism trade association. Further, these enterprises are expected to be legally updated and renew their license of operation and membership in respective department and trade associations respectively. With the application of these criteria, the population size comes down to 925. In addition to this, the study intended to include some of those tourism business enterprises dealing their business largely with the tourists such as restaurant, curio and gift shops, handicraft, airlines<sup>1</sup> and so on accounting 255. Thus, the potential population of the study (after the adjustment), in demand side (of finance) is 1180 tourism business enterprises as on July 2005. Table: 1.1 presents the population and selected sample of tourism business enterprises.

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<sup>1</sup> Some Airlines operate most of their flights considering the demand of the tourists.

**Table 1.1**  
**Population and Sample of Tourism Business Enterprises**

Type of tourism business	Exhaustive Population *	Adjusted Population #	Sample	
			Number	Percent
Travel Agency	<b>948</b>	<b>223</b>	<b>28</b>	<b>12.6</b>
Adventure	<b>832</b>	<b>480</b>	<b>38</b>	<b>7.9</b>
Trekking	740	432	30	
Rafting	92	48	8	
Accommodation	<b>1,006</b>	<b>222</b>	<b>48</b>	<b>21.6</b>
Total	<b>2,786</b>	<b>925</b>	<b>114</b>	<b>12.3</b>
Other business	-	255	16	6.3
Grand Total	<b>2,780</b>	<b>1,180</b>	<b>130</b>	<b>11.0</b>

Source: Nepal Tourism Statistics, 2005

# Please refer Appendix: A.3

In July 2005, there were 17 commercial banks, 26 development banks (including 5 regional rural development banks) and 59 finance companies. Though there were other financial institutions comprising 20 financial cooperatives, 47 financial non-government organizations as well as non-bank financial institutions comprising 17 insurance companies, one Employees Provident Fund, one Citizen Investment Trust and another one Deposit Insurance and Credit Guarantee Corporation the study did not find them to be much relevant as potential population and sample for the tourism financing. Thus, the potential population of the study, in supply side (of finance) is 102 banks and financial institutions as of July 2005. Table 1.2 summarizes the distribution of the population and sample in the supply side of tourism financing.

**Table 1.2**  
**Population and Sample of Banks and Financial Institutions**

Financing Institutions	Population		Sample	
	Number	Percentage on Total	Number	Percentage on Population
Commercial Banks	17	16.7	17	100.0
Development Banks	26	25.5	4	15.4
Finance Companies	59	57.8	13	22.0
Total	102	100.0	34	33.3

In the process of selection of samples, the population details, which were made available according to the clusters by various administrative offices and trade association, were used as a base. From amongst this the selection of the sample was based on convenience. Thus, this is the convenience sampling within the clusters.

On examining representativeness of sample, it is found to be representative (Chapter – V, paragraph 5.2).

#### **D. DATA COLLECTION PROCEDURE**

The data for the tourism business enterprises are collected from primary survey undertaken during the period February - April 2006. Similarly, the data from Ministry of Finance, Nepal Rastra Bank, Ministry of Tourism, Nepal Tourism board, and respective banks and financial institutions as well as from tourism business enterprises were collected and used extensively in the study.

The study employs the data comprising both published and unpublished as well as other information related to the study.

### **1.8 METHODS OF ANALYSIS AND MODEL**

The data collected from the primary survey during February – April 2006 as well as from secondary sources were tabulated. The analysis has been performed on microcomputer using the software like, Microsoft Office Excel, SPSS for windows and E-Views. In order to achieve the first objective, the study reviews the earlier research works with descriptive analysis whereas for the second one it computes annual rate of change in percentage and proportion in addition to the descriptive analysis.

For the objective number 3, the study analyses the secondary data along with the computations of ratio and rate of change in percent. Further, for objective no. 4, 5, and 6; it runs the regression using Ordinary Least Square (OLS) method in simple and log linear or in both the forms based upon the selection of the better model of analysis. Different variables are used for different equations and in different combinations (including jointly) in order to find out the determinants and to reach the representative model. In addition, the study inquires about the presence or absence of autocorrelation and initiates the remedial measures to correct the model of analysis.

Objectives 7 to 11 relates to tourism business enterprises. For objective 7, the study employs the data from the primary survey to discuss the pattern of financing and computes the absolute figures in common size statements to study the structure of financing. In order to check the variability (difference) between the distributions among the various types of business and ownership pattern (objective no. 8), it performs one way ANOVA and t-Test for two sample means.

The study employs ANOVA using direct method. Here, one needs to undertake the calculation in following four steps (Aryal and Gautam, 2001):

Step 1: Calculate the variance between the samples (SSC)

$$SSC = \sum_{i=1}^k n_i (\bar{x}_i - \mu)^2$$

Step 2: Calculate the variance within samples (SSE)

$$SSE = \sum_{i=1}^k \sum_{j=1}^{n_i} n_i (\bar{x}_{ij} - \bar{X}_i)^2$$

Step 3: Calculate total sum of square (TSS) i.e. TSS = SSC + SSE or

$$TSS = \sum_{i=1}^k \sum_{j=1}^{n_i} (X_{ij} - \mu)^2$$