

Current Macroeconomic Situation

(Based on the First Five Months' Data of 2008/09)

Monetary Situation

Money Supply

1. Broad money (M_2) recorded a growth of 9.0 percent in the first five months of 2008/09 compared to a growth of 9.5 percent in the corresponding period of the previous year. Despite a significant growth of net foreign assets in the review period compared to that of the previous year, a lower growth of net domestic assets on account of a decline in a growth of net claims on government and an increase in net non-monetary liabilities contributed M_2 to grow by a lower rate in the review period.
2. In the review period, narrow money (M_1) grew by 4.7 percent, a similar growth in the corresponding period of the previous year. Notwithstanding a substantial growth of currency in circulation in the review period, a decline in demand deposits by 5.5 percent is attributed to a slower growth of M_1 in the review period. Time deposits grew by 10.9 percent in the review period compared to that of 11.8 percent in the corresponding period of the previous year.
3. Currency in circulation witnessed a substantial increase of 10.3 percent in the review period. Such currency had expanded by 5.9 percent in the previous year. An expansion of an elevated level of remittance inflows to the rural areas and a delay in the transfer of such inflows into the banking system due to the insufficient financial services in these areas contributed to a substantial increase in currency in circulation in the review period.
4. Net foreign assets (NFA), after adjusting foreign exchange valuation gain/loss, increased by Rs. 22.8 billion (13.3 percent) in the review period compared to a muted growth of Rs. 31.2 million in the same period previous year. An elevated level of remittance inflows accompanied by an expansion in foreign assistance contributed to a significant growth of net foreign assets in the review period.

5. Net non-monetary liabilities increased by Rs 6.8 billion (6.0 percent) in the review period compared to a growth of Rs 43.3 million in the previous year. An increase in paid-up capital of commercial banks by Rs 1.7 billion and general reserves on account of an increase in retained earnings by Rs 5.8 billion contributed to such an increase in net non-monetary liabilities in the review period.

Domestic Credit

6. In the first five months of 2008/09, domestic credit expanded by 6.5 percent compared to a growth of 10.4 percent in the corresponding period in the previous year. A decline in net claims on government by 7.8 percent as a result of a high cash deposits of Rs. 8.1 billion with Nepal Rastra Bank (NRB) on account of a higher resource mobilization relative to the government expenditure along with a redemption of a part of internal loan of the banking sector contributed to slowdown the growth of domestic credit in the review period.
7. Claims on financial institutions remained subdued in the review period. Such claims, which had increased by Rs 3.6 billion in the previous year increased by only Rs 76.9 million in the review period. A decrease in short-term investment in development banks and finance companies by commercial banks owed to a slowdown in claims on financial institutions in the review period.
8. The growth of private sector credit remained marginally lower in the review period compared to that of the previous year. Credit to the private sector increased by 10.1 percent in the review period compared to a growth of 10.9 percent in the corresponding period of the previous year. A slowdown in the credit to the production and construction sector contributed to a lower growth of private sector credit in the review period.
9. Claims on non-financial government enterprises increased by 6.7 percent (Rs. 375.6 million) in the review period compared to a growth of 5.7 percent (Rs 289.9 million) in the corresponding period of the previous year. A higher use of credit by Janakpur Cigarette Factory Ltd., Nepal Oil

Corporation, Nepal Airlines Corporation and Janak Education Material Center Ltd. contributed to such an increase in the claims on non-financial government enterprises in the review period.

Deposits Mobilization and Credit Flow of Commercial banks

10. In the first five months of 2008/09, deposits of commercial banks increased by Rs 34.3 billion (8.1 percent) amounting to Rs 455.8 billion. The total deposits had increased by Rs 32.5 billion (9.7 percent) in the corresponding period last year. Notwithstanding the significant inflows of remittances, an increase in the currency in circulation accompanied by a higher level of revenue mobilization of the government relative to the expenditure contributed to slowdown the rate of deposits mobilization in the review period. In the review period, saving and fixed deposits increased by 13.0 percent and 6.3 percent respectively. Such deposits had increased by 8.9 and 12.8 percent respectively in the corresponding period of the previous year.
11. In the review period, credit to private sector expanded by Rs 34.8 billion (10.3 percent) compared to an increase of Rs 31.3 billion (11.8 Percent) in the corresponding period of the previous year. Review period witnessed a slowdown in the credit flow to production and construction sector. Credit to the production sector expanded by 6.9 percent (Rs 5.5 billion) in the review period compared to an expansion of 14.0 percent (8.7 billion) in the previous year. Credit to agriculture sector, real estate, transportation equipment production and fittings, services and consumer sectors remained higher in the review period. A higher credit flow relative to the deposits mobilization of commercial banks increased the credit-deposit ratio from 82.6 percent in mid-July 2008 to 84.3 percent in mid-December 2008.
12. The liquid funds of commercial banks grew by 9.7 percent in the review period compared to a growth of 3.1 percent in the previous year. An elevated level of remittances inflow contributed to an increase in liquid funds of commercial banks. Of the components of liquid funds, commercial banks' balance with the NRB increased by 20.9 percent as

against a decline of 8.4 percent in the corresponding period of the previous year. The increase in CRR in the monetary policy of 2008/09 also contributed to a higher growth of commercial banks's balance with the NRB. Likewise, the balance held abroad by commercial banks increased by 4.8 percent to Rs 43.1 billion in mid-December 2008 compared to a growth of 6.8 percent a year ago.

Liquidity Management

13. In the first five month of 2008/09, the NRB mopped up net liquidity of Rs 16.5 billion through open market operations. Of the total liquidity mopped up in the review period, Rs 7.5 billion was mopped up through outright sale auction and Rs 9.0 billion was mopped up through reverse repo auction. Of the total of Rs 6.8 billion liquidity mopped up in the corresponding period of the previous year, Rs. 1.2 billion was mopped through outright sale auction and Rs. 5.6 billion was mopped up through reverse repo auction. However, as in the previous year, liquidity has not been injected through the instruments of open market operations in the review period.
14. In the first five months of 2008/09, the NRB injected net liquidity of Rs 59.7 billion by net purchase of 789.0 million US dollar from commercial banks through foreign exchange intervention. A net liquidity of Rs 29.8 billion had been injected through the net purchase of 464.9 million US dollar from commercial banks in the corresponding period of the previous year. An elevated level of remittance inflows necessitated such a substantial amount of purchase intervention in the foreign exchange market in the review period.
15. The NRB purchased Indian currency (IC) of 29.5 billion through the sale of 630 million US dollar in the review period. IC of 22.3 billion was purchased through the sale of 560 million US dollar in the corresponding period a year ago. A higher amount of payment made by Nepal Oil Corporation to Indian Oil Corporation attributed to a higher amount of IC purchase against a sale of US dollar in the review period.

Standing Liquidity Facility and Inter Bank Transactions

16. In the first five months of 2008/09, commercial banks used standing liquidity facility (SLF) of Rs 32.2 billion compared to that of Rs. 36.2 billion in the corresponding period last year. Likewise, the inter bank transactions of commercial banks stood at Rs 126.8 billion in the review period compared to that of Rs 143.8 billion in the previous year. Adequate liquidity with commercial banks on account of the significant remittance inflows slowed down the inter bank transactions and use of the SLF in the review period.

Short-term Interest Rates

17. The weighted average monthly 91-day Treasury bill rate stood at 4.72 percent in mid-December 2008 compared to that of 3.59 percent a year ago. The weighted average monthly inter bank rate increased to 4.73 percent in mid-December 2008 from 2.38 percent last year.

Securities market

18. The year on year (y-o-y) NEPSE index decreased by 28.4 percent to 734.85 points in mid-December 2008. This index was 1025.91 a year ago. Likewise NEPSE sensitive index (based on July 2006) stood at 191.17 points in mid-December . This index was 265.05 in mid-December 2007.

19. The NEPSE Float Index calculated on the basis of final transaction as of August 24,2008 (at market price), remained 69.45 in mid-December 2008.

20. The y-o-y market capitalization increased by 20.1 percent to Rs. 387.4 billion in mid-December 2008. Market capitalization to GDP ratio increased to 41.0 percent from 39.3 percent a year ago. Of the total market capitalization, bank and financial institutions, manufacturing and processing companies, hotels, business entities, hydropower and other economic sectors accounted for 68.8 percent, 2.0 percent, 1.2 percent, 0.3 percent, 4.7 and 23.0 percent respectively.

21. Total paid up capital of the listed companies increased by 95.4 percent to Rs. 46.6 billion in mid-December 2008 due mainly to the additional listing of securities in the Nepal Stock Exchange Limited. Of the total listed share of Rs. 22.8 billion, bonus share of Rs.556.3 million, right share of Rs.4.1 billion, ordinary share of Rs.15.5 billion and bonds of Rs.2.7 billion were listed. The remarkable increase in ordinary share was ascribed to the listing of Nepal Telecom's share of Rs. 15 billion.
22. Monthly turnover to market capitalization ratio remained at 0.48 percent in Mid-December 2008 compared to 0.85 percent a year ago.
23. Total number of companies listed at the NEPSE increased to 145 in mid-December 2008 compared to that of 142 a year ago. Among the currently listed companies, 114 are banks and financial institutions (including insurance companies). Production and processing industries, hotels, business entities, hydropower and companies in other groups are 18, 4, 4 and 3 and 2 percent respectively.
24. The twelve-month rolling standard deviation reflecting an increased volatility in the stock market stood at 116.9 in mid-December 2008 compared to 185.4 a year ago.

Consumer Price Inflation

25. The y-o-y inflation as calculated by the consumer price index rose to 14.1 percent in mid-December 2008 from 5.7 percent in the previous year. The inflation, in the review period, was driven both by the significant rise in food and beverages (17.2 percent) as well as nonfood and services (10.8 percent) group. Last year's the price rise of food and beverages and non-food and services group, was 7.1 percent and 4.1 percent respectively.
26. Of the items in the food and beverage group, price indices of sugar and sugar related products increased on a y-o-y basis in mid-December 2008,

by a whopping rate of 35.9 percent. This is in sharp contrast to last year's increase of -17.0 percent. Similarly, the price indices of oil and ghee sub-groups increased on a y-o-y basis in reviewed period by 26.2 percent as compared to an increase of 12.5 percent last year. The sub group of grains and cereal products witnessed a y-o-y price rise of 18.0 percent in the review period compared to an increase of 10.3 percent in the corresponding period of previous year. Likewise, the indices of pulses as well as meat, fish and eggs rose up by 25.7 percent and 21.5 percent respectively in the review period compared to a rise of 14.4 percent and 5.8 percent respectively in mid-December 2007.

27. Within the group of non-food and services, the index of transport and communication, tobacco and related products as well as housing goods and services rose by 21.7 percent, 15.1 percent and 12.3 in mid-December 2008 compared to a rise of 0.0 percent, 7.5 percent and 5.4 percent respectively during the same period of last year.
28. Region-wise, the price rise in Kathmandu valley was 16.2 percent followed by 13.6 percent in Hills and 13.1 percent in Terai. Last year, the respective rates were 4.9 percent, 5.3 percent and 6.2 percent.
29. In the review period, the y-o-y core inflation rose to 13.1 percent from 4.7 percent a year ago.

Wholesale Price Inflation

30. The y-o-y wholesale price inflation increased to 10.1 percent in mid-December 2008 compared to 6.1 percent a year ago. The index of imported commodities, domestic manufactured commodities and agricultural commodities increased by 14.9 percent, 12.3 percent and 6.1 percent respectively in the review period as compared to 7.1 percent, 6.3 percent and 5.3 percent a year ago.

31. Of agricultural commodities, the price index of livestock production and pulses increased by 26.5 percent and 23.1 percent respectively in the review period compared to a rise of 2.1 percent and 9.6 a year ago. On the other hand, the price index of cash crops declined by 28.0 percent in the review period compared to an increase of 6.4 percent in the corresponding period of previous year.
32. Within the group of domestic manufactured commodities, the price index of food-related products, construction materials, and beverages and tobacco related products are increased by 14.4 percent 11.6 percent and 11.2 percent respectively in mid-December 2008 compared to a rise of 5.2 percent, 11.1 percent and 6.0 percent a year ago.
33. Of imported commodities, the price index of transport vehicles and machinery goods increased by 21.3 percent on a y-o-y basis in mid-December 2008 compared to an increase of 4.6 percent a year ago. Likewise, the price indices of textile related products also increased by 20.4 percent in the review period compared to a rise of -3.8 percent in the corresponding period of previous year.

National Salary and Wage Rate

34. The overall y-o-y salary and wage rate index rose by 14.6 percent in mid-December 2008 compared to a rise of 8.0 percent a year ago. Of the salary and wage rate indices, the salary index increased by 12.6 percent in the review period compared to a rise of 10.9 percent in the corresponding period of the previous year. The y-o-y wage rate index increased by 15.3 percent in the review period compared to an increase of 6.9 percent in the same period of the previous year. Wages of agricultural, industrial and construction labourers increased by 22.7 percent, 4.7 percent and 15.1 percent respectively in the review period. Last year, these wage rates had increased by 3.0 percent, 12.4 percent and 9.8 percent respectively.

Fiscal Situation

Budget Deficit / Surplus

35. In the first five months of 2008/09, the government budget remained at a surplus of Rs.2.2 billion in contrast to a deficit of Rs 9.8 billion in the corresponding period of the previous year. An increase in revenue and foreign cash grants accounted for such a budget surplus in the review period.

Government Expenditure

36. In the first five months of 2008/09, the total government spending increased by 2.5 percent to Rs. 48.5 billion compared to an increase of 44.3 percent in the corresponding period of the previous year. The deceleration of such spending was due to a decline in the growth rate of recurrent as well as capital expenditure.

37. In the first five months of 2008/09, recurrent expenditure increased by 4.5 percent to Rs.32.3 billion. In the corresponding period of the previous year, recurrent expenditure had increased by 27.7 percent. A significant amount spent for the preparation of the Constitution Assembly Election in the previous year, but no occurrence of such expenditure in the current year accounted for such a deceleration in recurrent expenditure in the review period.

38. In the review period, capital expenditure declined by 34.3 percent to Rs 4.9 billion in contrast to an increase of 120.3 percent in the corresponding period of the previous year.

Government Revenue

39. In the first five months of 2008/09, revenue mobilization of the government grew by 33.1 percent to Rs.43.1 billion compared to an

increase of 21.0 percent in the corresponding period of the previous year. Such an impressive revenue mobilization was ascribed on the high growth of income tax, VAT revenue, excise, vehicle tax and registration fee as well as a high growth of non-tax revenue.

40. Of the total revenue mobilization, VAT revenue grew by 17.1 percent to Rs 14.2 billion in mid-December 2008. It had increased by 16.9 percent in the corresponding period of the previous year. The growth in VAT revenue was on account of growing imports and consumption induced by the rise in remittances and reforms in VAT administration.
41. In the review period, customs revenue rose by 13.7 percent to Rs 8.9 billion compared to an increase of 17.0 percent in the same period of the previous year. Reforms in customs administration and the increase in imports of high tax yielding vehicles and spare parts contributed to such an increase in customs revenue.
42. In the review period, excise revenue increased by 34.1 percent to Rs 5.4 billion compared to an increase of 31.5 percent in the same period of the previous year. Reforms in excise administration and increase in the imports of high tax yielding vehicles accounted for such a growth of excise revenue in the review period.
43. Income tax revenue increased by 23.9 percent to Rs 4.6 billion in the first five months of 2008/09. The evolution of the corporate culture on account of the growth in banks and financial institutions contributed to such a higher growth of income tax collection. Last year such revenue had risen by 17.7 percent.
44. In the review period, non-tax revenue grew by 125.2 percent to Rs 6.7 billion compared to an increase of 32.4 percent in the same period of the

preceding year. Such an increase in non-tax revenue was on account of the increase in dividend paid by some public enterprises.

Foreign Cash Loans and Grants

45. The government received foreign cash loans of Rs 2.1 billion and foreign cash grants of Rs 5.7 billion in the first five months of 2008/09. The government had received foreign cash loans of Rs 2.2 billion and foreign cash grants of Rs 3.4 billion in the corresponding period of the previous year.
46. The government did not mobilize any domestic borrowing in the review period.

Foreign Trade

47. Exports rose by 30.9 percent in the first five months of 2008/09 in contrast to a decline of 4.4 percent in the corresponding period of the previous year. While exports to India increased by 15.1 percent in 2008/09 as against a decline by 9.0 percent in the corresponding period of the previous year, exports to other countries soared by 64.0 percent compared to an increase of 6.9 percent in the same period of the previous year.
48. The rise in the exports of readymade garments, shoes & sandals, tooth paste, G.I. pipe and noodles was primarily responsible for the increase in exports to India. Likewise, the rapid increase in the exports to other countries can be attributed to the upsurge in the exports of pulses, woollen carpets, pashmina, readymade garments and herbs.
49. In the first five months of 2008/09, total imports went up by 32.6 percent compared to an increase of 8.2 percent in the corresponding period of the previous year. While imports from India increased by 17.1 percent in the

review period compared to a growth of 10.7 percent in the corresponding period of 2007/08, imports from other countries surged by 57.2 percent compared to a growth of 4.5 percent a year earlier.

50. An increase in the import of petroleum products, vehicles & spare parts, cold rolled sheet in coil, other machinery & parts and textiles, among others, from India, and gold, MS billet, electrical goods, other machinery & parts and computer & parts, among others, from other countries were largely responsible for the rise in total imports in the first five months of 2008/09.

Balance of Payments

51. In the first five months of 2008/09, the overall BOP recorded a significant surplus of Rs. 22.8 billion compared to a surplus of Rs. 31.1 million in the corresponding period of the previous year. The current account also posted a surplus of Rs. 12.3 billion in the first five months of 2008/09 compared to a deficit of Rs. 7.5 billion in the corresponding period of the previous year. Such current account surplus was primarily attributed to the surge in net transfers by 60.9 percent in the first five months of 2008/09. Under transfers, workers' remittances soared by 65.8 percent in the first five months of 2008/09 compared to a growth of 17.6 percent in the corresponding period of the previous year.

Foreign Exchange Reserves

52. In mid-December 2008, the gross foreign exchange reserves stood at Rs. 235.6 billion, with an increment of 10.8 percent compared to the level as at mid-July 2008. Such reserves had barely risen by 0.1 percent in the corresponding period of the preceding year. Gross foreign exchange reserves in US dollar declined by 1.8 percent to US\$ 3.1 billion in mid-December 2008. In the same period of the previous year, such reserves had

risen by 2.7 percent. The current level of reserves is adequate for financing merchandise imports of 10.2 months and merchandise and service imports of 8.2 months.

Price of Oil and Gold in the International Market and Exchange Rate Movement

53. In the international market, the price of oil (Crude Oil Brent) fell by 52.2 percent to US\$ 44.51 per barrel in mid-December, 2008 from US\$ 93.19 per barrel in mid-December, 2007. Likewise, the price of gold increased by 4.6 percent to US\$ 826.00 per ounce in mid-December, 2008 from US\$ 789.50 per ounce a year earlier.

54. Compared to mid-July 2008, the Nepalese currency *vis-à-vis* the US dollar depreciated by 11.38 percent in mid-December 2008. It had appreciated by 2.53 percent in the corresponding period of the previous year. The exchange rate of one US dollar stood at Rs. 77.30 in mid-December 2008 compared to Rs. 68.50 in mid-July 2008.