

Current Macroeconomic Situation

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

Monetary Situation

Money Supply

- 1 Broad money (M_2) grew by 11.0 percent in the first six months of 2008/09 compared to a growth of 10.3 percent in the corresponding period of the previous year. A significant growth of net foreign assets contributed to increase M_2 in the review period compared to that of the previous year.
- 2 In the review period, narrow money (M_1) grew by 9.2 percent compared to a growth of 6.2 percent in the corresponding period of the previous year. Notwithstanding a lower growth rate of demand deposits, a substantial growth of currency in circulation in the review period is attributed to a higher growth of M_1 in the review period. Currency in circulation recorded a higher growth of 12.7 percent in the review period compared to a growth of 5.6 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 in to the banking system due to the insufficient banking services in these areas contributed to a substantial increase in currency in circulation in the review period
- 3 Net foreign assets (NFA), after adjusting foreign exchange valuation gain/loss, increased by Rs. 28.5 billion (16.6 percent) in the review period compared to a decline of Rs. 2.0 billion in the same period of the 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.

Domestic Credit

- 4 In the first six months of 2008/09, domestic credit expanded by 5.7 percent compared to a growth of 10.2 percent in the corresponding period in the previous year. A decline in net claims on government by 18.8 percent as a result of a higher cash deposits of Rs. 22.6 billion with Nepal Rastra Bank (NRB) on account of a higher resource mobilization relative to the government expenditure along with a lower growth of credit to the private sector contributed to slowdown the growth of domestic credit in the review period.

- 5 Claims on financial institutions subdued in the review period. Such claims, which had increased by Rs 2.5 billion in the previous year increased by Rs 2.2 billion in the review period. A decline 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.
- 6 Claims on non-financial government enterprises increased by 6.2 percent (Rs. 349.1 million) in the review period compared to a growth of such credit by 4.7 percent (Rs 239.8 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, Nepal Electricity Authority and Janak Education Material Center Ltd. contributed to increase the claims on such enterprises in the review period.
- 7 The private sector credit grew at a lower rate in the review period compared to that of the previous year. The credit to the private sector increased by 11.4 percent in the review period. Such credit had increased by 14.0 percent in the corresponding period of the previous year. A slowdown in the credit to the production and construction sector contributed to such a lower growth of private sector credit in the review period.

Deposits Mobilization and Credit Flow of Commercial banks

- 8 In the first six months of 2008/09, deposits of commercial banks increased by Rs 54.3 billion (12.9 percent) amounting to Rs 475.8 billion. The total deposits had increased by Rs 37.9 billion (11.3 percent) in the corresponding period last year. A significant increase of remittance inflows and expansion of commercial bank branches contributed to such an increase in the total deposit mobilization in the review period. In the review period, saving and fixed deposits increased by 14.2 and 12.4 percent respectively. Such deposits had increased by 10.2 and 12.2 percent respectively in the corresponding period of the previous year.
- 9 In the review period, credit to private sector expanded by Rs 38.8 billion (11.5 percent) compared to an increase of Rs 42.6 billion (16.0 Percent) in the corresponding period of the previous year. Review period witnessed a slowdown in the credit flow to production, wholesale and retail business and construction sector. Credit to the production sector expanded by Rs 5.7 billion (7.1 percent) in the review period compared to an expansion of Rs 10.6 billion (17.0 percent) in the previous year. Credit to agriculture sector, real estates, transportation equipment production and fittings and consumer sectors remained

higher in the review period. A higher deposit mobilization relative to the credit flow of commercial banks lowered the credit-deposit ratio from 82.6 percent as in mid-July 2008 to 81.9 percent as in mid-January 2009.

- 10 The liquid funds of commercial banks grew substantially by 14.9 percent in the review period compared to a growth of 0.8 percent in the previous year. Workers' remittances inflows and slowdown in private sector credit contributed to increase the liquid funds of commercial banks in the review period. Of the components of liquid funds, commercial banks' balance held abroad increased by 29.3 percent amounting to Rs 53.1 billion compared to a rise of 2.0 percent in the corresponding period of the previous year. However, commercial banks balance with the NRB and cash in hand declined by 1.5 and 12.1 percent respectively in the review period.

Liquidity Management

- 11 In the first six month of 2008/09, the NRB mopped up net liquidity of Rs 20.7 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 13.3 billion was mopped up through reverse repo auction. Net liquidity of Rs 4.8 billion was mopped up in the corresponding period of the previous year including Rs. 1.2 billion through outright sale auction, Rs. 5.6 billion through reverse repo auction and Rs 2.0 billion through repo auctions. However, liquidity has not been injected so far through the instruments of open market operations in the review period.
- 12 In the first six months of 2008/09, the NRB injected net liquidity of Rs 73.2 billion by net purchase of 963.6 million US dollar from commercial banks through foreign exchange intervention. A net liquidity of Rs 35.7 billion had been injected through the net purchase of 558.2 million US dollar from commercial banks in the corresponding period of the previous year. Workers' remittance inflows necessitated such a substantial amount of intervention in the foreign exchange market in the review period.
- 13 The NRB purchased Indian currency (IC) of 33.9 billion through the sale of 720 million US dollar in the review period. Indian currency of 26.3 billion was purchased through the sale of 660 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

14 In the first six months of 2008/09, commercial banks used standing liquidity facility (SLF) of Rs 38.2 billion compared to that of Rs. 47.0 billion in the corresponding period last year. Likewise, the inter bank transactions of commercial banks stood at Rs 146.8 billion in the review period compared to that of Rs 168.1 billion in the same period of the previous year. Adequate liquidity with commercial banks on account of the significant remittance inflows and slowdown in private sector credit contributed to such a lower inter bank transactions and lower use of the SLF in the review period.

Short-term Interest Rates

15 The weighted average monthly 91-day Treasury bill rate stood at 4.32 percent in mid-January 2008 compared to that of 3.86 percent a year ago. The weighted average monthly inter bank rate increased to 4.93 percent in mid-January 2008 from a rate of 3.37 percent in the corresponding period last year. Despite an adequate liquidity position in the economy, a competition among the commercial banks helped increase the interest rate on saving deposits by 25 basis points to 7.0 percent in mid-January 2008.

Securities market

16 The year on year (y-o-y) NEPSE index decreased by 31.2 percent to 659.81 points in mid-January 2009. This index was 958.91 a year ago. Likewise, NEPSE sensitive index (based on July 2006) stood at 173.11 point in mid-January 2009. This index was 248.77 in mid-January 2008.

17 The NEPSE float index, calculated on the basis of final transaction as of August 24, 2008 (at market price), remained 64.73 in mid- January 2009.

18 The y-o-y market capitalization increased by 19.9 percent to Rs. 361.92 billion in mid-January 2009. Of the total market capitalization, bank and financial institutions, manufacturing and processing companies, hotels, business entities, hydropower and other economic sectors accounted for 69.6 percent, 2.1 percent, 1.3 percent, 0.3 percent, 4.9 and 21.8 percent respectively.

19 Total paid up capital of the listed companies stood at Rs. 48.20 billion in mid-January 2009, an increase by 101.6 percent over the period of one year. This increase was largely due to the additional listing of securities. Of the total listed share at Nepal Stock

Exchange Ltd. of Rs. 25.07 billion up to mid-January 2009, bonus share, right share, ordinary share and bonds accounted for Rs. 561.6 million, Rs. 5.51 billion, Rs.15.69 billion and Rs. 3.30 billion respectively. The ordinary share constituted the largest portion largely due to the share of Nepal Telecom.

- 20 The monthly turnover to market capitalization ratio remained at 0.39 percent in mid-January 2009, compared to 1.0 percent a year ago.
- 21 Total number of companies listed at the NEPSE increased to 149 in mid- January 2009 compared to 145 a year ago. Among the currently listed companies, 118 are banks and financial institutions (including insurance companies). Production and processing industries, hotels, business entities, hydropower and companies in other groups number 18, 4, 4, 3 and 2 respectively.
- 22 The twelve-month rolling standard deviation reflecting, an increased volatility in the stock market, stood at 128.2 in mid-January 2009 compared to 195.7 a year ago.

Inflation

Consumer Price Inflation

- 23 The y-o-y consumer price inflation rose to 14.4 percent in Mid-January 2009 from 5.8 percent in the previous year. The inflation, in the review period, was driven both by the significant rise in food and beverages (18.3 percent) as well as non-food and services (10.3 percent) group. The price rise of food and beverages and non-food and services group, was 7.3 percent and 4.2 percent respectively in Mid-January 2008.
- 24 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-January 2008, by a whopping rate of 37.3 percent. This is in sharp contrast to last year's decline of 14.2 percent. Similarly, the price indices of pulses as well as oil and ghee sub-groups increased on a y-o-y basis in reviewed period by 25.6 percent and 25.0 percent as compared to an increase of 15.0 percent and 12.6 percent in the last year. The subgroup of grains and cereal products witnessed a y-o-y price rise of 16.5 percent in the review period compared to an increase of 11.3 percent in the corresponding period of previous year. Likewise, the indices of meat, fish and eggs as well as restaurant meal rose up by 22.5 percent and 21.5 percent respectively in the review period compared to a rise of 6.1 percent and 5.7 percent respectively in Mid-January 2008.

- 25 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 up by 20.7 percent, 15.1 percent and 11.0 percent in Mid-January 2009 compared to a rise of 0.5 percent, 7.5 percent and 5.5 percent respectively during the same period of last year.
- 26 Region-wise, the price rise in Kathmandu valley was 15.8 percent followed by 14.2 percent in Hills and 13.6 percent in Terai in the reviewed period. Last year, the respective rates were 5.3 percent, 5.6 percent and 6.0 percent.
- 27 In the review period, the y-o-y core inflation rose to 13.2 percent from 4.7 percent a year ago.

Wholesale Price Inflation

- 28 The y-o-y wholesale price inflation increased to 14.7 percent in Mid-January 2009 compared to 5.5 percent a year ago. The index of agricultural commodities, domestic manufactured commodities and imported commodities increased by 17.0 percent, 11.8 percent and 13.0 percent respectively in the review period as compared to 4.0 percent, 5.9 percent and 7.2 percent a year ago.
- 29 Of agricultural commodities, mainly the price index of fruits and vegetables, livestock production and pulses increased by 33.2 percent, 27.9 percent and 20.0 percent respectively in the review period compared to a rise of -10.2 percent, 3.6 percent and 9.4 percent a year ago. On the other hand, the price index of cash crops declined by -7.7 percent in the review period compared to an increase of 24.8 percent in the corresponding period of previous year. Within the group of domestic manufactured commodities, the price index of construction materials and food-related products increased by 12.9 percent and 12.0 percent in Mid-January 2009 compared to a rise of 7.4 percent and 7.8 percent a year ago.
- 30 Of imported commodities, the price index of transport vehicles and machinery goods increased by 22.2 percent on a y-o-y basis in Mid- January 2009 compared to an increase of 3.7 percent a year ago. Likewise, the price indices of textile related products also increased by 21.7 percent in the review period compared to a rise of -4.3 percent in the corresponding period of previous year.

National Salary and Wage Rate

31 32. The overall y-o-y salary and wage rate index rose by 15.4 percent in Mid-January 2009 compared to a rise of 9.1 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 16.4 percent in the review period compared to an increase of 8.5 percent in the same period of the previous year. Such an increase was on account of increase in the salary of civil servants and a rise in the wages of laborers because of the supply constraints due mainly to the migration of youths from rural areas along with the increasing trend of Nepalese youths seeking employment abroad. Wages of agricultural, industrial and construction laborers increased by 22.7 percent, 7.1 percent and 15.5 percent respectively in the review period. Last year, these wage rates had increased by 6.5 percent, 11.1 percent and 10.4 percent respectively.

Fiscal Situation

Budget Deficit / Surplus

32 In the first six months of 2008/09, the government budget remained at a surplus of Rs.7.4 billion in contrast to a deficit of Rs 3.3 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

33 In the first six months of 2008/09, the total government spending increased by 12.3 percent to Rs.65.5 billion compared to an increase of 30.2 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.

34 In the first six months of 2008/09, recurrent expenditure increased by 13.1 percent to Rs.43.2 billion. In the corresponding period of the previous year, recurrent expenditure had increased by 21.8 percent.

35 In the review period, capital expenditure declined by 23.4 percent to Rs7.9 billion in contrast to an increase of 66.3 percent in the corresponding period of the previous year.

Government Revenue

- 36 In the first six months of 2008/09, revenue mobilization of the government grew by 25.5 percent to Rs.59.5 billion compared to an increase of 25.4 percent in the corresponding period of the previous year. Such a growth of revenue mobilization was ascribed on the increase in income tax, VAT revenue, excise, vehicle tax and registration fee as well as a high growth of non-tax revenue.
- 37 Of the total revenue mobilization, VAT revenue grew by 14.9 percent to Rs 17.2 billion in mid-January 2009. It had increased by 18.8 percent in the corresponding period of the previous year. The increase in VAT revenue was on account of growing imports and consumption induced by the rise in remittances and reforms in VAT administration.
- 38 In the review period, customs revenue rose by 14.8 percent to Rs 11.1 billion compared to an increase of 23.7 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.
- 39 In the review period, excise revenue increased by 33.2 percent to Rs 6.6 billion compared to an increase of 31.1 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.
- 40 Income tax revenue increased by 34.6 percent to Rs 11.3 billion in the first six months of 2008/09. The evolution of the corporate culture on account of the growth in banks and financial institutions contributed to such an increase in income tax collection. Last year such revenue had risen by 39.8 percent.
- 41 In the review period, non-tax revenue grew by 31.2 percent to Rs 9.5 billion compared to an increase of 16.7 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 including the NRB and Nepal Telecom.

Foreign Cash Loans and Grants

- 42 The government received foreign cash loans of Rs 2.8 billion and foreign cash grants of Rs 11.0 billion in the first six months of 2008/09. The government had received foreign cash loans of Rs 2.4 billion and foreign cash grants of Rs 5.2 billion in the corresponding period of the previous year.

43 The government mobilized domestic borrowing of Rs 8.7 billion in the review period.

Foreign Trade

44 Exports rose by 18.6 percent in the first half of 2008/09 in contrast to a decline by 3.2 percent in the corresponding period of the previous year. While exports to India rose by 0.9 percent in 2008/09 as against a decline by 7.4 percent in the corresponding period of the previous year, exports to other countries soared by 55.9 percent compared to an increase of 7.1 percent in the same period of the previous year.

45 The rise in the exports of readymade garments, G.I. pipe, shoes & sandal, tooth paste and catechu was, to a large degree, attributed to the increase in export to India. Likewise, the rapid increase in the exports to other countries can be ascribed to the rise in the exports of pulses, woollen carpets, pashmina, readymade garments and herbs.

46 In the first half of 2008/09, total imports went up by 23.6 percent compared to an increase of 14.2 percent in the corresponding period of the previous year. While imports from India increased by 10.9 percent in the review period compared to a growth of 16.6 percent in the corresponding period of 2007/08, imports from other countries surged by 44.2 percent in comparison to a growth of 10.5 percent a year earlier.

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

Balance of Payments

48 In the first six months of 2008/09, the overall BOP recorded a significant surplus of Rs. 28.5 billion compared to a deficit of Rs 2.0 billion in the corresponding period of the previous year. The current account also posted a surplus of Rs. 16.7 billion in the first half of 2008/09 compared to a deficit of Rs. 10.9 billion in the corresponding period of the previous year. Such current account surplus was primarily attributed to the surge in net transfers by 59.9 percent in the first half of 2008/09. Under transfers, workers' remittances soared by 65.3 percent in the first six months of 2008/09 compared to the growth of 18.2 percent in the corresponding period of the previous year.

Foreign Exchange Reserves

49 In mid-January 2009, the gross foreign exchange reserves aggregated Rs. 254.5 billion, an upsurge by 19.7 percent compared to the level as at mid-July 2008. In the corresponding period of the previous year, such reserves had declined by 0.2 percent. On the basis of US dollar, gross foreign exchange reserves rose by 5.5 percent to US\$ 3.27 billion in mid-January 2009. Such reserves had increased by 2.9 percent in the same period in the previous year. The current level of reserves is sufficient for financing merchandise imports of 11.4 months and merchandise and service imports of 9.1 months.

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

50 In the international market, the price of oil (Crude Oil Brent) plummeted by 53.9 percent to US\$ 43.31 per barrel in mid-January, 2009 from US\$ 93.97 per barrel in mid-January 2008. Similarly, the price of gold fell by 8.4 percent to US\$ 826.50 per ounce in mid-January, 2009 from US\$ 902.00 per ounce a year earlier.

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51 In comparison to mid-July 2008, the Nepalese currency *vis-à-vis* the US dollar depreciated by 11.9 percent in mid-January 2009. It had appreciated by 3.1 percent in the corresponding period of the previous year. The exchange rate of one US dollar stood at Rs. 77.75 in mid-January 2009 compared to Rs. 68.50 in mid-July 2008.