

Current Macroeconomic Situation

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

Monetary Situation

Money Supply

1. Broad money (M_2) grew by 21.0 percent in the first eleven months of 2008/09 compared to a growth of 20.2 percent in the corresponding period of the previous year. Despite a substantial growth of net foreign assets in the review period compared to that of the previous year, a lower growth rate of domestic credit than that of the previous year, contributed to M_2 growing only by a marginally higher rate in the review period.
2. Narrow money (M_1) grew by 21.8 percent in the review period. M_1 had grown by 16.5 percent in the previous year. The significant growth of M_1 in the review period compared to that of the previous year was on account of a substantial growth of currency in circulation and cash deposits of other financial institutions in the NRB. The currency in circulation increased by 22.8 percent in the review period compared to a growth of 19.8 percent in the corresponding period of the previous year. Demand deposits increased by 20.1 percent in the review period, which had increased by 10.1 percent during the corresponding period of the previous year. Likewise, time deposits grew by 20.7 percent in the review period compared to a growth of 21.9 percent in the previous year.
3. Net foreign assets (NFA), after adjusting foreign exchange valuation gain/loss, increased by Rs. 39.1 billion (22.8 percent) in the review period compared to a growth of Rs 24.7 billion (18.7 percent) in the same period of the previous year. An elevated inflow of remittance coupled with an increase in foreign assistance for the government of Nepal (GON), contributed to a significant growth of NFA in the review period.

Domestic Credit

4. In the first eleven months of 2008/09, domestic credit expanded by 17.0 percent compared to a growth of 17.6 percent in the corresponding period of the previous year. A sharp decline in net claims on government by 13.8 percent (Rs 12.0 billion) on account of a higher resource mobilization relative to the expenditure of the GON resulting to a cash deposits of Rs. 17.4 billion (including Rs 3.9 billion of the previous year) with Nepal Rastra Bank (NRB) in the review period contributed domestic credit to grow by a marginally lower rate in the review period. Net claims on government had declined by 2.1 percent in the previous year.
5. Claims on non-financial government enterprises declined by 13.2 percent (Rs. 744.4 million) in the review period against a growth of such credit by 3.6 percent (Rs 185.5 million) in the corresponding period of the previous year. A partial loan repayment by National Trading Ltd and Nepal Food Corporation and a full repayment of loan by Nepal Oil Corporation, contributed to decline the claims on such enterprises in the review period.
6. Claims on financial institutions grew by 20.4 percent (Rs 960.2 million) in the review period. Such credit had grown by Rs 2.1 billion in the corresponding period of the previous year. A decline in claims on government financial institutions accompanied by a slowdown in a short-term investment of commercial banks to the development banks and finance companies, contributed to a lower growth of claims on financial institutions in the review period.

7. The claims on the private sector grew by 25.4 percent in the review period compared to a growth of 23.0 percent in the corresponding period of the previous year. An inclusion of the credit disbursed by KIST bank, which upgraded from "C" class financial institution, contributed to a higher growth of private sector claims in the review period.

Reserve Money

8. Reserve money grew by 24.6 percent in the review period. The reserve money had increased by 15.1 percent in the corresponding period of the previous year. A substantial growth of NFA of monetary authority contributed to a higher growth of reserve money in the review period. The effect of higher growth of reserve money has been reflected in the currency in circulation and deposits of commercial banks and financial institutions with the NRB.

Deposit Mobilizations and Credit Flow of Commercial Banks

9. In the first eleven months of 2008/09, deposit mobilization of commercial banks increased by Rs 88.1 billion (20.9 percent) amounting to Rs 509.6 billion as in mid-June 2009. Deposit mobilization of commercial banks had increased by Rs 67.7 billion (20.2 percent) in the corresponding period of the previous year. Saving and fixed deposits increased by 18.6 percent and 29.7 percent respectively in the review period. Such deposits had increased by 19.5 percent and 23.2 percent respectively in the corresponding period of the previous year.
10. The private sector credit of commercial banks expanded by a lower rate in the review period compared to that of the previous year. In the review period, credit to the private sector expanded by 27.0 percent compared to a growth of 29.0 percent in the corresponding period of the previous year. Of the credit disbursed to the private sector, the growth of credit to production, construction, metal production, machinery and electrical tools, transportation, communication and public services, wholesale and retail business and service sectors remained lower in the review period compared to that of the previous year. However, growth of credit to the transportation equipment production and fittings and consumable sectors remained higher in the review period.
11. Credit to the production and construction sectors increased by 14.2 and 36.2 percent in the review period compared to an increase of 20.0 and 58.4 percent respectively in the corresponding period of the previous year. Likewise, credit to wholesale and retail business and service sectors increased by 17.5 and 9.0 percent respectively compared to an increase of 18.6 percent and 18.9 percent in the previous year. The growth rate of the credit to the real estate declined in the review period, however, the amount of disbursement of credit is higher, which is 11.8 billion as in mid-June 2009 compared to a disbursement of Rs 7.4 billion in the previous year. In the review period, consumable loan increased by 36.9 percent (Rs 4.8 billion).
12. The liquid funds of commercial banks grew by 20.5 percent amounting to Rs 95.2 billion in the review period compared to a growth of 17.7 percent in the previous year. An elevated inflow of remittances contributed to an increase of commercial banks' balance held abroad and thus, an increase of liquid funds of commercial banks. Of the components of liquid funds, commercial banks' balance with the NRB increased by 16.6 percent compared to a muted growth of 1.1 percent in the corresponding period of the previous year. Likewise, the commercial banks' balance held abroad increased by 28.0 percent amounting to Rs 52.6 billion in mid-June 2009 compared to a growth of 26.8 percent a year ago.

Liquidity Management

13. In the first eleven months of 2008/09, the NRB mopped up net liquidity of Rs 9.7 billion through open market operations. Of the total liquidity of Rs 20.7 billion mopped up in the review period, Rs 7.5 billion was mopped up from outright sale auctions and Rs 13.3 billion from reverse repo auctions. Despite a substantial injection of liquidity through foreign exchange intervention in the review period, a total liquidity of Rs 11.0 billion has been injected through repo auctions in the months of mid-February, mid-March and mid-June of the review period on account of a shortfall in liquidity in these months, particularly due to a higher cash balance of the GON with the NRB and a higher expansion of currency in circulation in the review period. Net liquidity of Rs 7.5 billion had been mopped up in the corresponding period of the previous year through open market operation including Rs. 9.9 billion through outright sale auctions; Rs. 6.6 billion through reverse repo auctions and Rs 9.0 billion through repo auctions.
14. In the first eleven months of 2008/09, the NRB injected net liquidity of Rs 130.2 billion by net purchase of 1.7 billion US dollar from commercial banks through foreign exchange intervention. A net liquidity of Rs 89.1 billion had been injected through a net purchase of 1.4 billion US dollar from commercial banks in the corresponding period of the previous year. An elevated inflow of remittances necessitated such a substantial amount of intervention in the foreign exchange market in the review period.
15. The NRB purchased Indian currency (IC) of 65.2 billion through the sale of 1.4 billion US dollar in the review period. Indian currency of 56.0 billion had been purchased through the sale of 1.4 billion US dollar in the corresponding period a year ago. A depreciation of Indian currency vis-à-vis the US dollar helped to purchase more amount of IC relative to the previous year by selling same amount of the US dollar in the review period.

Standing Liquidity Facility and Inter Bank Transactions

16. In the first eleven months of 2008/09, commercial banks used standing liquidity facility (SLF) of Rs 107.8 billion compared to that of Rs. 102.1 billion in the corresponding period of the previous year. Likewise, the inter bank transactions of commercial banks stood at Rs 271.9 billion in the review period compared to that of Rs 242.4 billion in the corresponding period of the previous year.

Short-term Interest Rates

17. The short-term market interest rates increased in the eleventh month of 2008/09. The weighted average monthly 91-day Treasury bill rate stood at 6.0 percent as in mid-June 2009 compared to that of 5.41 percent a year ago. The weighted average monthly inter bank rate stood at 5.02 percent as in mid-June 2009 compared to that of 4.64 percent in the corresponding period of the previous year.
18. Along with an increase in short-term market interest rates, interest rates on deposits also increased in the review period. The maximum interest rate on saving deposits increased by 50 basis points to 7.50 percent as in mid-June 2009 from mid-May 2009. Likewise, the maximum interest rate on 3-month, 6-month, 1-year and two or more than two years fixed deposits increased by 25, 75 150 and 100 basis points respectively to 6.0 percent, 7.0 percent, 9.0 percent and 9.5 percent as in mid-June 2009 from rates effective in mid-May 2009. Likewise, maximum interest rates on agriculture and export credit declined by 100 and 50 basis points to 12.0 and 11.0 percent respectively as in mid-June 2009 from the rates of mid-May 2009.

Securities market

19. The year on year (y-o-y) NEPSE index decreased by 27.1 percent to 678.74 points in mid-June 2009. This index was 930.65 a year ago. Likewise, NEPSE sensitive index (based on July 2006) stood at 182.32 points in Mid-June 2009. This index was 243.48 in mid-June 2008.
20. The NEPSE float index, calculated on the basis of final transaction as of August 24, 2008 (at market price) remained 65.56 in Mid-June 2009.
21. The y-o-y market capitalization increased by 39 percent to Rs. 451.17 billion in mid-June 2009. Of the total market capitalization, bank and financial institutions, manufacturing and processing companies, hotels, business entities, hydropower and other economic sectors accounted for 74.7 percent, 1.7 percent, 1.1 percent, 0.4 percent, 3.9 and 18.3 percent respectively.
22. Total paid up capital of the listed companies stood at Rs. 59.32 billion in mid-June 2009, increasing by 122.9 percent over the period of one year. This increase was largely due to the additional listing of securities. Of the total listed securities at Nepal Stock Exchange Ltd. of Rs. 33.56 billion up to mid-June 2009, bonus share, right share, ordinary share and bonds accounted for Rs. 1.9 billion, Rs. 9.3 billion, Rs.19.1 billion and Rs. 3.3 billion respectively. The ordinary share constituted the largest portion largely due to the share of Nepal Telecom.
23. The monthly turnover to market capitalization ratio remained at 0.48 percent in mid-June 2009, compared to 0.60 percent a year ago.
24. Total number of companies listed at the NEPSE increased to 159 in mid-June 2009 compared to 148 a year ago. Among them, 128 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, 3 and 2 respectively.
25. The twelve-month rolling standard deviation which reflect the volatility in the stock market, stood at 156.4 in mid-June 2009 compared to 109.2 a year ago.

Inflation

Consumer Price Inflation

26. The y-o-y inflation as calculated by the consumer price index rose to 12.3 percent in Mid-June 2009 from 11.0 percent in the same period of the previous year. The inflation, in the review period, was driven mainly by the rise of 19.0 percent in food and beverages group. The price index of non-food and service group increased by 5.1 percent. The price rise of food and beverages and non-food and services group, was 13.0 percent and 9.0 percent respectively in Mid-June 2008.
27. During the review period, of the items in the food and beverage group, price indices of sugar and sugar related products increased by a whopping rate of 62.3 percent as compared to an increase of 5.5 percent in the same period of last year. The price indices of vegetables and fruits increased by 55.5 percent. This is in sharp contrast to last year's decline of 3.3 percent. Similarly, the price indices of meat, fish and eggs as well as pulses sub-groups increased in reviewed period by 29.8 percent and 27.7 percent as compared to an increase of 12.6 percent and 11.1 percent in the same

period of last year. The subgroup of grains and cereal products also witnessed a price rise of 6.6 percent compared to an increase of 21.2 percent in the corresponding period of previous year.

28. Within the group of non-food and services, the index of tobacco and related products rose up by 17.5 percent during the review period compared to a rise of 10.5 percent respectively during the same period of last year.
29. Region-wise, the price rise in Kathmandu valley was 14.5 percent followed by 11.5 percent in both Terai and Hills in the reviewed period. Last year, the respective rates were 10.2 percent, 11.7 percent and 10.8 percent.
30. In the review period, the y-o-y core inflation rose to 12.6 percent from 8.3 percent a year ago.

Wholesale Price Inflation

31. During the review period, the y-o-y wholesale price inflation increased to 17.0 percent compared to 12.9 percent a year ago. The index of agricultural commodities, domestic manufactured commodities and imported commodities increased by 33.4 percent, 6.0 percent and 0.2 percent respectively in the review period as compared to 10.8 percent, 13.9 percent and 15.7 percent a year ago.
32. Of agricultural commodities, mainly the price index of cash crops increased by 76.9 percent in the review period, as against the decline of 16.3 percent a year ago. Likewise, fruits and vegetables, livestock production and pulses increased by 59.5 percent, 39.2 percent and 21.4 percent as compared to an increase of 10.6 percent, 14.5 percent and 15.3 percent during the same period of last year. Within the group of domestic manufactured commodities, the price index of beverages and tobacco increased by 13.5 percent compared to a rise of 9.3 percent a year ago.
33. Of imported commodities, the price indices of textile related products increased by 14.5 percent in the review period, compared to a rise of 1.1 percent in the corresponding period of previous year. Likewise, the price index of transport vehicles and machinery goods increased by 12.4 percent as compared to an increase of 11.4 percent a year ago. Price indices of petroleum products and coal declined by 16.2 percent in the review period, which had increased by 32.5 percent during the same period of last year.

National Salary and Wage Rate

34. The overall y-o-y salary and wage rate index rose by 21.5 percent in the review period as compared to a rise of 8.1 percent a year ago. Of the salary and wage rate indices, the salary index increased by 16.8 percent in the review period compared to a rise of 10.9 percent in the

corresponding period of the previous year. The wage rate index increased by 23.0 percent in the review period compared to an increase of 7.2 percent in the same period of the previous year. Such an increase was on account of increase in the salary of civil servants. Wages of agricultural, industrial and construction laborers increased by 29.0 percent, 15.4 percent and 17.8 percent respectively in the review period. These wage rates had increased by 9.6 percent, 3.3 percent and 9.0 percent respectively in the same period of last year.

Fiscal Situation

Budget Deficit / Surplus

35. In the first eleven months of 2008/09, the government budget remained at a surplus of Rs.1.7 billion in contrast to a deficit of Rs.9.3 billion in the corresponding period of the previous year. An impressive growth of resource mobilization relative to the government expenditure accounted for such a budget surplus in the review period.
36. In the review period, the government has significant cash surplus of Rs.17.4 billion (including the 3.9 billion of previous year) with Nepal Rastra Bank.

Government Expenditure

37. In the first eleven months of 2008/09, the total government expenditure increased by 24.6 percent to Rs.146.2 billion compared to an increase of 19.2 percent in the corresponding period of the previous year. Increase in all types of government expenditure contributed to such an expansion of total government expenditure in the review period.
38. In the first eleven months of 2008/09, recurrent expenditure increased by 27.1 percent to Rs.92.8 billion. In the corresponding period of the previous year, recurrent expenditure had increased by 19.1 percent. Upward revision of the salary of the government employees as well as an increase in non-budgetary expenditure led to such acceleration in the recurrent expenditure in the review period.
39. In the review period, capital expenditure increased by 17.5 percent to Rs.32.9 billion in contrast to an increase of 35.8 percent in the corresponding period of the previous year. The trend of increasing capital expenditure in the later months of the year, payment for the contracts, smoothness in public procurement processes, significant amount of budget release to the local bodies as well as significant amount spent on Small Farmers' debt waiver program contributed to such a growth in the capital expenditure in the review period.

Government Revenue

40. In the first eleven months of 2008/09, revenue mobilization of the government grew by 34.4 percent to Rs.121.2 billion compared to an increase of 26.5 percent in the corresponding period of the previous year. The Government's strong commitment in revenue leakage control, revenue administration reforms, Voluntary Discloser of Income Scheme (VDIS) and significant growth of

non-tax revenue contributed to such an impressive growth of revenue mobilization in the review period.

41. Of the total revenue mobilization, VAT revenue grew by 26.5 percent to Rs.35.2 billion in mid-June 2009. It had increased by 17.7 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.
42. In the review period, customs revenue rose by 29.9 percent to Rs.23.4 billion compared to an increase of 21.3 percent in the same period of the previous year. Reforms in customs administration as well as increase in imports of high tax yielding vehicles and parts contributed to such an increase in customs revenue.
43. In the review period, excise revenue increased by 47.8 percent to Rs.13.9 billion compared to an increase of 24.9 percent in the same period of the previous year. Reforms in excise administration and identification of newly excised goods accounted for such a growth of excise revenue in the review period.
44. Income tax revenue increased by 45.4 percent to Rs. 21.2 billion in the first eleven months of 2008/09. A remarkable receipt under VDIS program due to government's strong administrative and political commitment contributed to such an increase in income tax collection. Last year such revenue had risen by 30.0 percent.
45. In the review period, non-tax revenue grew by 24.9 percent to Rs.20.0 billion compared to an increase of 45.6 percent in the same period of the preceding year. Such an increase in non-tax revenue was on account of the increase in principal, interest and dividend paid by some public enterprises to the government.

Foreign Cash Loans and Grants

46. The government received foreign cash loans of Rs.3.5 billion and foreign cash grants of Rs. 20.7 billion in the first eleven months of 2008/09. Such amounts were Rs.3.2 billion and Rs.14.7 billion respectively in the corresponding period of the previous year.
47. The government mobilized domestic borrowing of Rs. 8.7 billion in the review period, which was Rs. 13.3 billion in the corresponding period of the previous year.

External Sector

Foreign Trade

48. In the first eleven months of 2008/09, exports increased by 15.4 percent in contrast to a decline by 2.1 percent in the corresponding period of the previous year. Exports to India rose by 8.5 percent in 2008/09 as against a decline by 8.2 percent in the corresponding period of the previous year; likewise, exports to other countries expanded by 28.8 percent compared to an increase of 12.3 percent in the same period of the previous year.
49. The increase in the exports of readymade garments, textiles, G.I. pipe, catechu and shoes & sandals was largely responsible for the increase in exports to India. Similarly, the surge in the

exports to other countries can be attributed to the rise in the exports of pulses followed by pashmina, woolen carpets, handicraft and herbs.

50. In the first eleven months of 2008/09, total imports soared by 26.3 percent compared to an increase of 14.3 percent in the corresponding period of the previous year. Out of total imports, imports from India increased by 12.9 percent in the review period compared to a growth of 23.8 percent in the corresponding period of 2007/08; similarly, imports from other countries surged by 50.5 percent in comparison to a growth of just 0.5 percent in the preceding year.
51. An upsurge in the import of vehicles and spare parts, other machinery and parts, cold-rolled sheet in coil, cement and medicine, among others, from India and gold, electrical goods, MS billet, crude soybean oil and other machinery and parts, among others, from other countries were, to a great degree, responsible for the expansion in total imports in the first eleven months of 2008/09.

Balance of Payments

52. The overall BOP posted a significant surplus of Rs. 39.06 billion in the first eleven months of 2008/09 in comparison to a lower surplus of Rs. 24.67 billion in the corresponding period of the previous year. The current account also recorded a massive surplus of Rs. 39.58 billion in the review period in comparison to a surplus of Rs. 15.98 billion in the corresponding period of the previous year. The significant current account surplus in the review period was largely attributed to the rise in net transfers by 38.5 percent in the first eleven months of 2008/09. Under transfers, workers' remittances soared by 51.0 percent in the first eleven months of 2008/09 in comparison to the growth of 37.3 percent in the corresponding period of the previous year. Similarly, grants rose by 22.3 percent in the review period in comparison to a growth of just 6.6 percent in the corresponding period of the previous year.

Foreign Exchange Reserves

53. In mid-June 2009, the gross foreign exchange reserves stood at Rs. 271.68 billion, an increment of 27.8 percent compared to the level as at mid-July 2008. Such reserves had risen by 25.2 percent in the corresponding period of the preceding year. On the basis of US dollar, gross foreign exchange reserves went up by 15.8 percent to US\$ 3.59 billion in mid-June 2009. Such reserves had risen by 18.6 percent in the same period of the previous year. The current level of reserves is adequate for financing merchandise imports of 11.8 months and merchandise and service imports of 9.6 months.

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

54. In the international market, the price of oil (Crude Oil Brent) plummeted by 48.1 percent to US\$ 70.45 per barrel in mid-June, 2009 from US\$ 135.78 per barrel in mid-June 2008. The price of gold, on the other hand, increased by 8.2 percent to US\$ 937.25 per ounce in mid-June, 2009 from US\$ 866.00 per ounce a year earlier.
55. In comparison to mid-July 2008, the Nepalese currency *vis-à-vis* the US dollar depreciated by 9.39 percent in mid-June 2009. It had depreciated by 5.26 percent in the corresponding period of the

previous year. The exchange rate of one US dollar was Rs. 75.60 in mid-June 2009 compared to Rs. 68.50 in mid-July 2008.