Macroeconomic Situation of Nepal

(During the First Nine Months of FY 2003/04)

Nepal Rastra Bank

May 2004

Press Communiqué of Nepal Rastra Bank on Current Macroeconomic Situation of Nepal

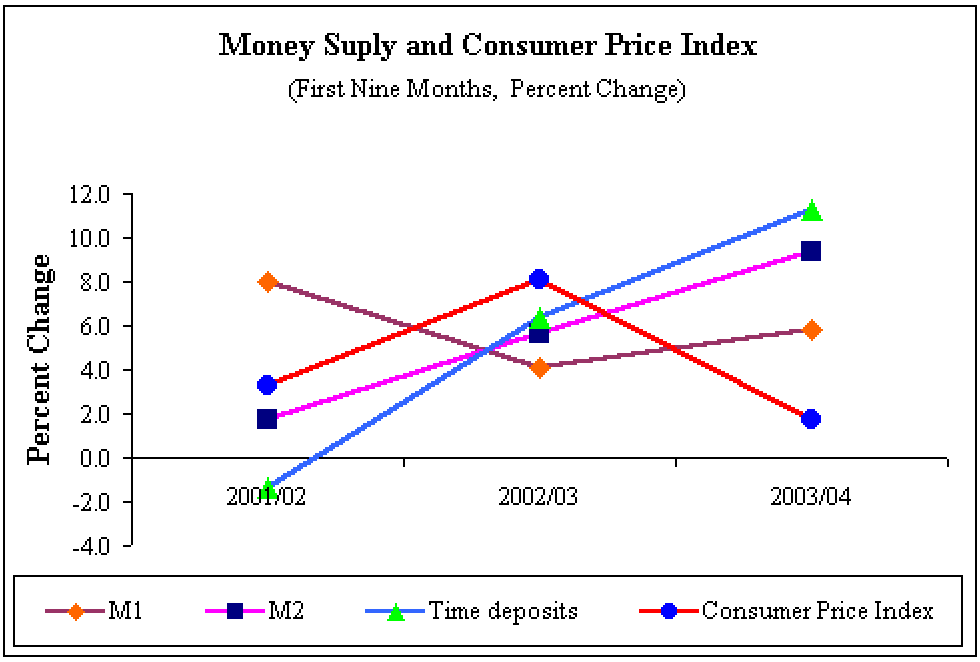
(*During the First Nine Months of FY 2003/04)*

<u>Major Points</u>

- FY 2003/04 saw higher growth both in narrow and broad money.
- The net claims on government decreased significantly.
- The weighted average treasury bills rates declined.
- The stock exchange transactions increased, while the NEPSE index decreased.
- Total government expenditure, on cash basis, increased.
- Resource mobilization increased faster than the total expenditure.
- Budget deficit increased due to the larger base of the expenditure.
- Price situation, on the point-to-point basis, decreased.
- Imports went up at a rate faster than the exports, resulting in the widened trade deficit.
- The sharp rise in grants and increase in the private remittances resulted in the current account surplus.
- The overall balance of payments (BOP) stood favorable due to huge current account surplus.
- The gross foreign exchange reserve reached Rs.122.5 billion, enough to cover merchandise imports of 11 months and merchandise and service imports of 9.3 months.

Monetary Situation

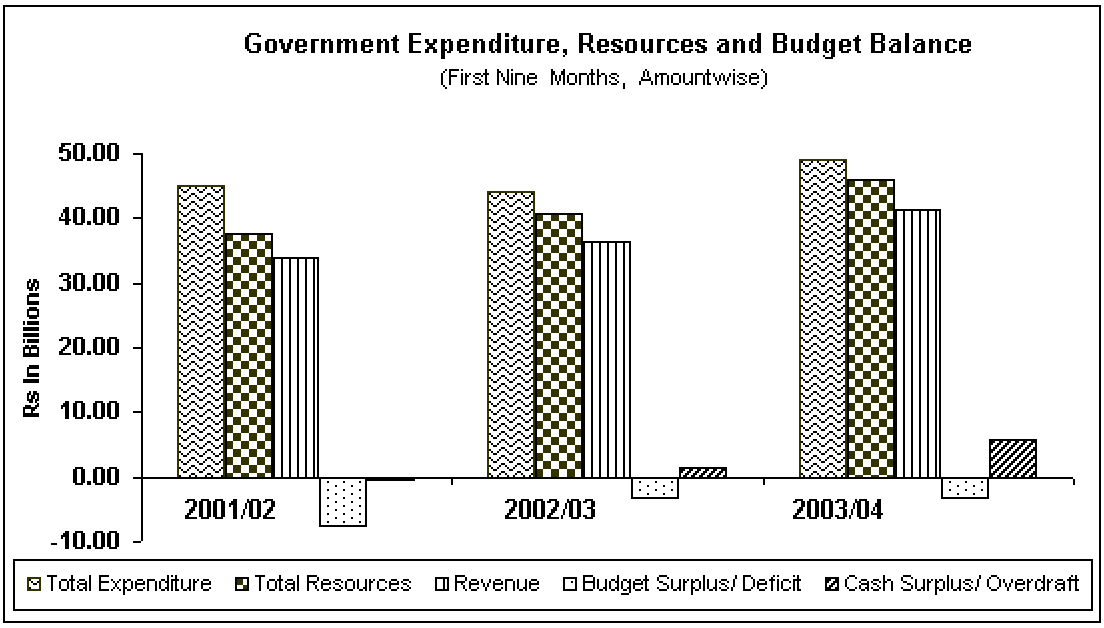
During the first nine months of FY 2003/04, broad money grew by 9.4 percent to Rs. 269.1 billion. Narrow money, a component of broad money, increased by 5.8 percent to Rs. 88.6 billion in comparison to the rise of 4.1 percent last year. Time deposits, the other component of broad money, went up by 11.3 percent to Rs. 180.4 billion compared to the rise of 6.4 percent last year. The net foreign assets (NFA) of the banking system (adjusting the foreign exchange valuation) surged by 16.2 percent compared to the rise of 6.4 percent last year. Domestic credit of the banking system increased by 2.0 percent to Rs. 233.1 billion compared to a growth of 5.8 percent last year. Credit to the private sector registered a growth of 6.6 percent to Rs. 160.8 billion. The share of net claims on government in the banking sector's total domestic credit declined from 27.6 percent in mid-April 2003 to 23.8 percent in mid-April 2004. Accordingly, the share of claims on the private sector rose from 66.0 percent in mid-April 2003 to 69.0 percent in mid-April 2004. The 91-day average treasury bills rate decreased to 1.70 percent in mid-April 2004 from 4.06 percent in mid-April 2003.



Government Budgetary Operation

Based on the cash flow data, the total expenditure of the government increased by 11.8 percent to Rs. 49.1 billion as against the decline of 2.6 percent last year. Of the total expenditure, regular expenditure increased by 8.4 percent to Rs. 37.9 billion compared to an increase of 8.0 percent last year. The development expenditure went up encouragingly, by 25.4 percent to Rs. 9.7 billion, in contrast to a sharp decline of 31.7 percent last year. The freeze account marked an increment of 22.1 percent to Rs. 1.6 billion as against the decline of 12.7 percent last year.

Total non-debt resources (revenue, non-budgetary and other receipts, and foreign grants) increased by 12.4 percent to Rs. 45.9 billion compared to a rise of 8.7 percent last year. Revenue, the major source of the government resources, went up by 13.8 percent to Rs. 41.5 billion compared to a slower growth of 7.0 percent last year. The rate of revenue mobilization improved mainly due to the rise in the imports. Foreign grants went up substantially to Rs. 2.8 billion as against just Rs. 1.5 billion mobilized last year. However, the non-budgetary receipts (net) declined by 45.5 percent to Rs. 1.3 billion. Despite the higher growth rate of non-debt resources vis-a-vis that of the total expenditure, the budget deficit increased by 3.3 percent to Rs. 3.2 billion compared to the decline by 58.7 percent last year due mainly to the broad base of the expenditure. To finance the deficit, HMG mobilized foreign cash loan amounting to Rs. 7.2 billion and domestic loan amounting to Rs. 3.0 billion this year. After meeting the deficit and adjusting Rs. 1.1 billion in the other headings of HMG account, HMG's cash transactions resulted in a surplus of Rs. 5.8 billion in mid-April 2004 as compared to a surplus of Rs. 1.3 billion last year.



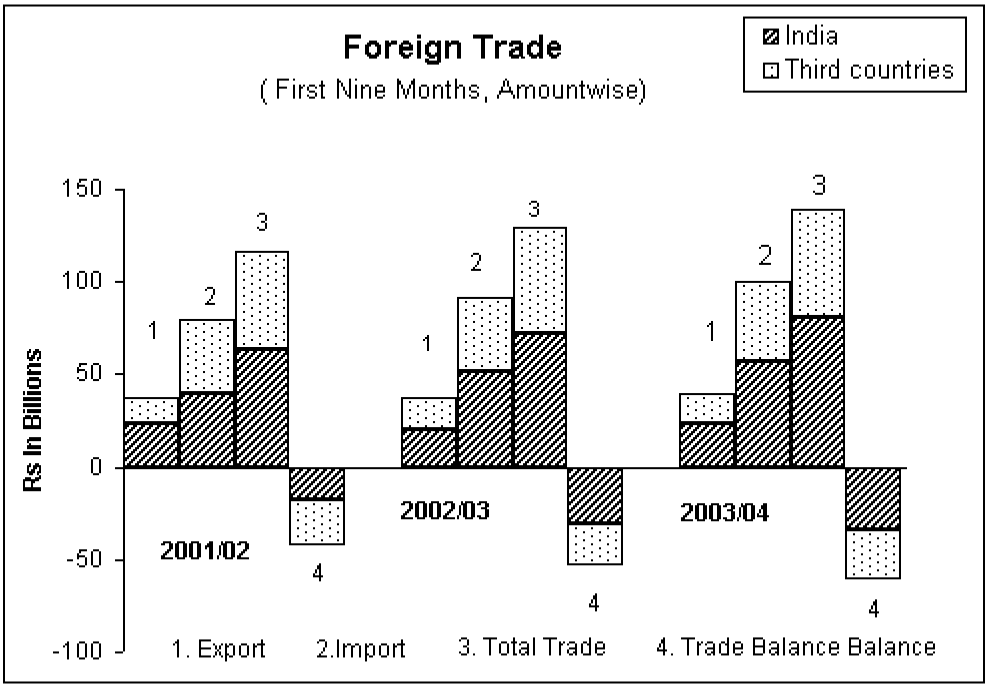
Price Situation

The national urban consumer price index, on the annual point-to-point basis, increased by 1.7 percent in mid-April 2004 compared to the rise of 8.1 percent in mid-April 2004. The slow growth in the price index is mainly attributable to the strong supply situation of foodgrains and vegetables in conjuction with the subsiding effect of the rise in the price of petroleum products last year. On point-to-point basis, the index of food and beverages group increased by 2.4 percent compared to the rise of 7.9 percent last year. The indices for oil and ghee (10.4 percent), meat, fish and eggs (7.2 percent), sugar and related products (6.6 percent), spices (6.1 percent), restaurant meals (5.1 percent), pulses (2.7 percent), milk and milk products (1.5 percent) and grains and cereals products (0.3 percent) went up while the indices of vegetables and fruits (2.5 percent) and beverages (0.6 percent) declined. The index of non-food and services group increased by 1.1 percent compared to an increase of 8.4 percent last year. The indices for education, reading and recreation (4.6 percent), medical and personal care (3.6 percent), cloth, clothing and sewing services (1.7 percent) and tobacco and related products (1.5 percent) increased while the indices for transport and communication (1.9 percent), housing (1.4 percent) and footwear (0.1 percent) declined. Regionwise, the price indices of the Terai, Hills and Kathmandu Valley rose by 0.1 percent, 0.8 percent and 5.3 percent respectively compared to the corresponding rise of 9.5 percent, 7.1 percent and 6.6 percent last year. The national urban consumer price index, on an average basis, increased by 4.7 percent during the first nine months of this year as against the rise of 4.1 percent last year.

The national wholesale price index, on the annual point-to-point basis, increased by 2.6 percent this year compared to an increase of 8.9 percent last year. The indices for domestic manufactured, agricultural and imported commodities increased by 7.7 percent, 1.5 percent and 0.9 percent respectively. The average national wholesale price index for the first nine months increased by 4.5 percent as against the rise of 2.1 percent last year.

Foreign Trade

Total exports increased by 3.8 percent to Rs. 39.4 billion compared to the rise of 2.0 percent last year. Exports to India, witnessing a reversal, increased by 14.0 percent to Rs. 23.5 billion in contrast to the decline of 9.8 percent last year. Exports to other countries, which had gone up by 20.8 percent last year, declined by 8.3 percent to Rs. 15.9 billion. The exports of woollen carpets, tanned skin and jewellery to other countries increased while that of readymade garments and Pashmina declined.



Total imports increased by 9.8 percent to Rs. 100.3 billion compared to the rise of 15.0 percent last year. The growth of imports from India decelerated to 11.6 percent from 28.3 percent last year, while imports from other countries increased by 7.5 percent as against the slower growth of 1.4 percent last year. Imports of M.S. billet, salt, pulses, wheat, vehicles and spare parts, industrial chemicals, chemical fertilizers, M.S. wire rod, cold-rolled sheets and other machinery parts from India and that of edible oil, nut, yarn, zinc ingot, steel sheet, copper wire and sheet, crude soybean oil, tire and tube, electrical equipment, cloths, cosmetics, other machinery parts, raw wool, plastic granules, chemical fertilizers, pesticide as well as agricultureral equipment from other countries went up this year.

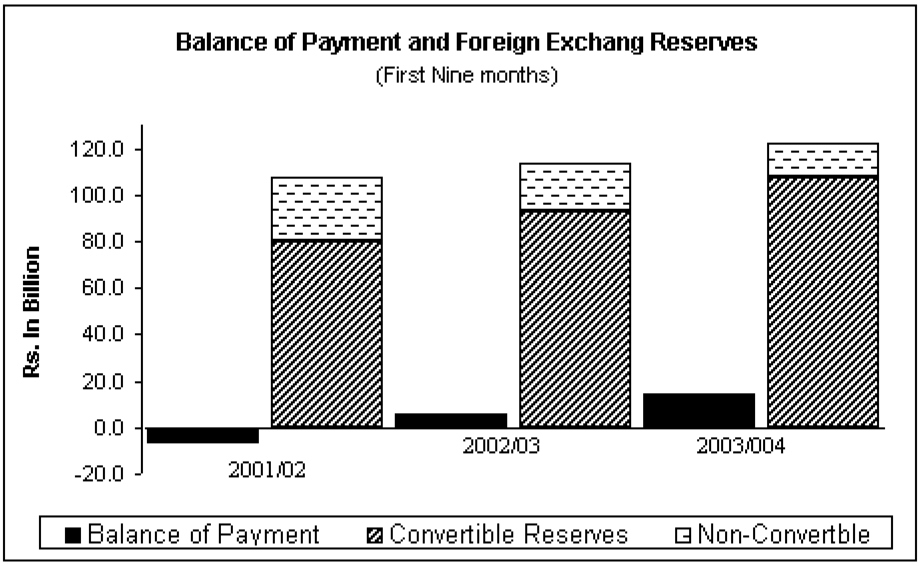
The higher growth of imports relative to that of the exports resulted in the trade deficit of Rs. 60.9 billion compared to the deficit of Rs. 53.4 billion last year. Trade deficit with India increased by 9.9 percent compared to the substantial rise of 78.7 percent last year. Trade deficit with other countries widened by 19.6 percent in contrast to the decline of 9.7 percent last year. The overall export/import ratio, which was 41.5 percent last year, came down to 39.3 percent this year. The export/import ratios for India and other countries respectively changed to 40.9 percent and 37.1 percent this year compared to the respective level of 40.1 percent and 43.5 percent last year.

Balance of Payments

According to the BOP statistics for the first seven months of FY 2003/04, trade deficit expanded by 13.9 percent to Rs. 43.2 billion on account of the higher growth of imports vis-à-vis the exports. Service receipts increased at a rate higher than that of payments, resulting in the surplus in the service sector. Despite the surplus in the service sector, the goods and services accounts aggregated at a deficit of Rs. 37.9 billion. The income (net) was also unfavourable at Rs 1.1 billion. Notwithsanding this, the current account recorded a surplus of Rs. 13.3 billion due to the increased inflow of foreign grants and private remittances. Despite a substaintial deficit in the financial account, the BOP remained favorable by Rs. 11.3 billion on account of the surplus in the current account as well as in the residual items. The BOP had recorded a deficit of Rs. 1.1 billion during the same period last year. On the basis of the monetary statistics for the first nine months, the BOP recorded a surplus of Rs. 14.8 billion as against the corresponding surplus of Rs. 5.6 billion last year.

Foreign Exchange Reserve

The gross foreign exchange reserve in mid-April 2004 reached Rs.122.4 billion. The convertible reserve increased by 15.4 percent to Rs.107.6 billion whereas the non-convertible reserve (Indian currency) declined by 25.6 percent to Rs. 15.0 billion. The share of convertible reserve in the total



reserve reached 87.8 percent from 82.3 percent last year, resulting in a corresponding decline in the share of non-convertible reserve to 12.2 percent. The rise in the share of the convertible reserve is attributable to an increased inflow of foreign grants and the private remittances. Despite the sharp decline in the non-convertible reserve, the overall reserve position is quite comfortable as it is sufficient to finance merchandise imports of 11 months and merchandise and service imports of 9.3 months.

Share Market Transactions

Major indicators of the stock market showed a mixed trend. Both the number of share transactions and their value increased. The market capitalization of the listed companies rose by 9.1 percent to Rs. 38.5 billion. However, the NEPSE index declined from the mid-April 2003 level of 214.08 by 12.86 index points (6.0 percent) to 201.22 in mid-April 2004.

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