



Nepal Rastra Bank

Research Department

Current Macroeconomic and Financial Situation of Nepal

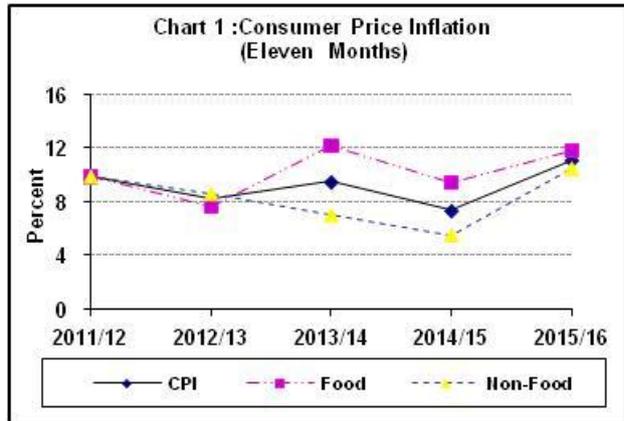
(Based on Eleven Months' Data of 2015/16)

Growth Outlook

1. The available data from different parts of the country maintained by the Department of Hydrology and Meteorology indicate the timely arrival of monsoon. The monsoon has become active since the end of June. The rainfall, so far, has been average in most parts of the country creating a conducive environment for better summer crops.
2. The construction activity of both the public and private sector has increased following the return of normalcy at the southern trade points. A pick up in capital spending of the government and the bank credit is the reflective of this.
3. Credit off-take of banks and financial institutions has risen 20.9 percent from mid-June 2015 to mid-June 2016 signaling a pickup in economic activities.
4. The industrial sector is expected to perform better in the latter part of the current fiscal year. This is mainly on account of the enhanced capacity utilization of industries owing to increased power supply with the beginning of rainy season and the absence of disturbances in the industrial sector during the review period.
5. According to Hotel Association of Nepal (HAN), the bed occupancy rate in hotels has been 45 percent due mainly to the seasonal slowdown. At the same time, the domestic tourism has also witnessed slackness for the time being due to the monsoon and plantation season of major crops. However, foreign tourists arrival is expected to gradually increase with the beginning of August 2016.

Inflation, Salary and Wage Rate

6. The consumer price inflation increased to 11.1 percent in mid-June 2016 from 7.4 percent a year ago. The rise in overall inflation was on account of double digit growth in food and beverage group inflation at 11.9 percent, non-food and services group inflation at 10.5 percent.



7. The higher rate of increase in price indices of vegetable sub-group, pulses and legumes sub-group, alcoholic drinks sub-group, clothes and footwear sub-group exerted an upward pressure on overall inflation during the review period.

8. Spikes in vegetable prices at 29.4 percent and of pulses at 21.5 percent drove up food inflation to the double digit level. Likewise, a pickup in prices of clothes and footwear at 17 percent, housing and utilities at 16.4 percent and alcoholic drinks at 15.9 percent contributed to the rise in non-food group inflation to the double digit level.

9. Geographically, the Kathmandu Valley witnessed a relatively higher rate of inflation at 13 percent followed by Hilly region at 12 percent, Mountain region at 10.2 percent and Terai region at 9.5 percent in the review period. In the corresponding period of the previous year, the Kathmandu Valley, Hilly region and Terai region had experienced the inflation rate of 7.8 percent, 8 percent and 6.7 percent respectively.

Inflation Wedge between Nepal and India

10. The y-o-y consumer price inflation of Nepal in the eleventh month of 2015/16 continued to remain at a higher level of 11.1 percent compared to that of India at 5.8 percent showing inflation wedge of 5.3 percent. Such inflation in Nepal was 7.4 percent compared to 5.4 percent in India reflecting a narrower inflation wedge of 2 percent in the corresponding period of the previous year.

Wholesale Price Inflation

11. The y-o-y wholesale price inflation rose to 6.4 percent in the review period from 5.4 percent a year ago. The wholesale price indices of agricultural commodities and domestic manufactured commodities showed a growth of 10.2 percent and 6.4 percent respectively, whereas such index of imported commodities had declined by 1.9 percent in the review period. In the corresponding period of the previous year, the increments in wholesale price indices of agricultural commodities and domestic manufactured commodities were 9.4 percent and 4.5 percent respectively, whereas the price index of imported commodities had seen a decline of 2.2 percent.

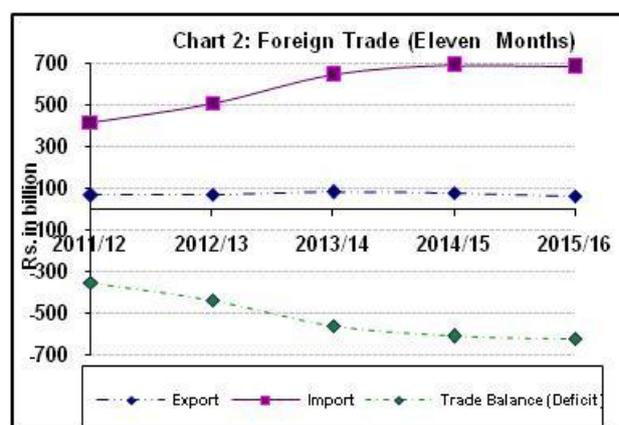
National Salary and Wage Rate

12. The y-o-y salary and wage rate index rose 5 percent in the review period compared to that of 7.5 percent in the corresponding period of the previous year. In the review period, the salary index increased 0.8 percent, while the wage rate index was up by 6 percent. The salary indices of bank and financial institutions, education and public corporations sub-groups increased 2.3 percent, 1.5 percent and 0.7 percent respectively in the review period. Likewise, wage rate indices of construction labourer, agricultural labourer and industrial labourer witnessed a growth of 11.1 percent, 5.7 percent and 5 percent respectively in the review period.

External Sector

Merchandise Trade

13. In eleven months of 2015/16, merchandise exports decreased 20.1 percent to Rs. 62.16 billion compared to a drop of 4.8 percent in the same period of the previous year. Exports to India and China decreased 31.8 percent, and 30.4 percent respectively whereas exports to other countries increased 4.9 percent in the review period.
14. Commodity wise, export of woolen carpet, cardamom, pashmina, readymade garments, tea, among others, increased whereas export of zinc sheet, GI pipe, polyester yarn, textiles, juices, among others, decreased during the review period.
15. Merchandise imports dropped 0.9 percent to Rs. 684.75 billion in the review period as against a growth of 7 percent in the same period of the previous year. The fall in imports was on account of a sharp drop in import of petroleum products in the review period. The import excluding of petroleum products increased 6.2 percent in the review period. Imports from China increased 12.4 percent whereas imports from India and other countries decreased 3.8 percent and 0.4 percent respectively in the review period.
16. Commodity-wise, import of vehicle and spare parts, gold, rice, medicine, mild steel (M.S.) wire, among others, increased whereas import of petroleum products, silver, aircraft spare parts, betel nut, among others, decreased during the review period.
17. Based on customs points, exports through Tribhuvan International Airport and Dry Port customs office, Birgunj increased whereas exports through other customs points decreased. On the import side, imports through Birgunj customs point decreased whereas imports through other customs points increased in the review period.
18. Total trade deficit in the review period expanded 1.6 percent to Rs. 622.60 billion compared to an expansion of 8.7 percent in the same period of the previous year. The export-import



ratio dropped to 9.1 percent in the review period compared to 11.3 percent in the corresponding period of the previous year.

Export-Import Price Index

19. The y-o-y unit value export price index based on customs data increased 20.8 percent while import price index decreased 4 percent in the eleventh month of 2015/16. Consequently, the TOT index increased 25.8 percent compared to an increase of 15.8 percent in the corresponding period of the previous year. Increase in price of export items such as carpet, betel nut, pulses caused the export price index to rise in the review period. Fall in the price of petroleum products resulted in a decline in import price index in the review period.

Services

20. The total services receipt declined 6.4 percent and expenses increased 5.6 percent in the review period. As a result, net services receipt decreased 61.1 percent to Rs. 9.45 billion in the first eleven months of 2015/16. The net services receipt was Rs. 24.32 billion in the same period of previous year.

Workers' Remittances

21. The workers' remittances grew 8.6 percent to Rs. 598.95 billion in the review period compared to a growth of 12.4 percent in the previous year. Consequently, net transfer receipt increased 10.1 percent to Rs. 695.30 billion in the review period. Such receipt had increased 10.4 percent in the same period of the previous year.
22. The number of workers going abroad for foreign employment, which directly affect the flow of inward remittances, decreased in the review period. The number of Nepalese workers leaving for foreign employment, based on final approval, decreased 20.6 percent in the review period. It had increased 4.2 percent in the same period of the previous year.

Box 1: Number of Nepalese Workers Going Abroad for Foreign Employment *			
Mid-Month/Year	2013/14	2014/15	2015/16
August	45937	42309	37756
September	24214	51551	40275
October	31959	35550	35484
November	31949	43213	23061
December	41634	53354	38350
January	50032	45362	35389
February	37285	48941	34219
March	48552	44460	35701
April	45854	52210	31615
May	54173	31375	36778
June	54926	37962	37687
July	61717	26600	-
Total	528232	512887	386315
Percentage Change (first eleven months)	15.7	4.2	-20.6
* Based on final approval for foreign employment. Source:- Department of Foreign Employment, GoN			

Current Account and BOP Position

23. The current account registered a surplus of Rs. 130.08 billion in the review period compared to Rs. 95.29 billion surplus in the same period of the previous year. Similarly, the overall BOP recorded a significant surplus of Rs. 171.15 billion in the review period compared to a surplus of Rs. 127.20 billion in the same period of the previous year.
24. In the review period, Nepal received capital transfer amounting to Rs. 12.25 billion and Foreign Direct Investment (FDI) inflow of Rs. 4.80 billion. In the same period of the previous year, capital transfer and FDI inflow had amounted to Rs. 11.89 billion and Rs. 3.70 billion respectively.

Box 2: Dividend Payment to FDI Companies*
(Rs. in million)

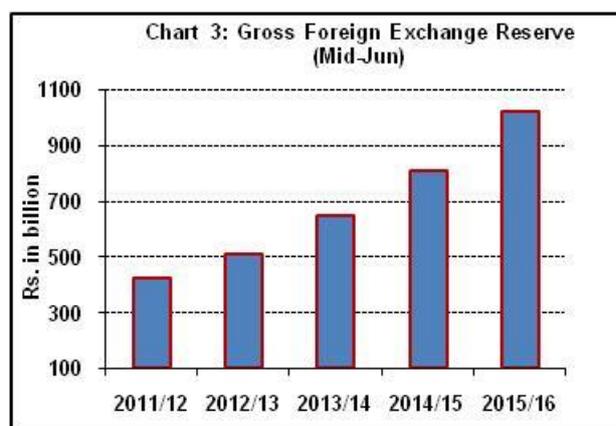
Sectors	2014/15 Annual	2015/16 Jul.- June.
Financial Sector	1794.43	14.8
Communication Sector	4.00	1692.8
Hydro Power Sector	2874.48	3154.3
Industry Sector	2299.19	1387.8
Services Sector	238.61	4.1
Total	7210.71	6253.8

**Based on approval from NRB*

25. Dividend payment to FDI companies, based on approval from Nepal Rastra Bank, amounted to Rs. 6.25 billion in the review period compared to the annual dividend payment of Rs. 7.21 billion in 2014/15.

Foreign Exchange Reserves

26. The gross foreign exchange reserves stood at Rs. 1021.74 billion as at mid-June 2016, an increase of 24 percent from Rs. 824.06 billion in mid-July 2015. Of the total foreign exchange, reserves held by NRB increased 23.6 percent to Rs. 869.32 billion as at mid-June 2016 from the level of reserves as at mid-July 2015. Similarly, the reserves of banks and financial institutions (except NRB) increased 26 percent to Rs. 152.42 billion in the same period. The share of Indian currency in total reserves stood at 21.9 percent as at mid-June 2016.



Foreign Exchange Adequacy Indicators

27. Based on the imports of eleven months of current fiscal year, the foreign exchange holdings of the banking sector is sufficient to cover the prospective merchandise imports of 16.8 months, and merchandise and services imports of 14.3 months. The ratio of reserve-to-GDP, reserve-to-imports and reserve-to-M2 increased to 45.4 percent, 119 percent and 47.7 percent respectively as at mid-June 2016. Such ratios were 38.9 percent, 93.3 percent and 43.9 percent as at mid-July 2015.

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

28. The price of oil (Crude Oil Brent) in the international market decreased 21.5 percent to USD 47.88 per barrel in mid-June 2016 from USD 60.99 per barrel a year ago. The price of gold increased 9 percent to USD 1287.15 per ounce in mid-June 2016 from USD 1181.40 per ounce a year ago.
29. Nepalese currency vis-à-vis the US dollar depreciated 5.5 percent in mid-June 2016 from mid-July 2015. It had depreciated 6.2 percent in the same period of the previous year. The buying exchange rate per US dollar stood at Rs. 107.08 in mid-June 2016 compared to Rs. 101.14 in mid-July 2015.

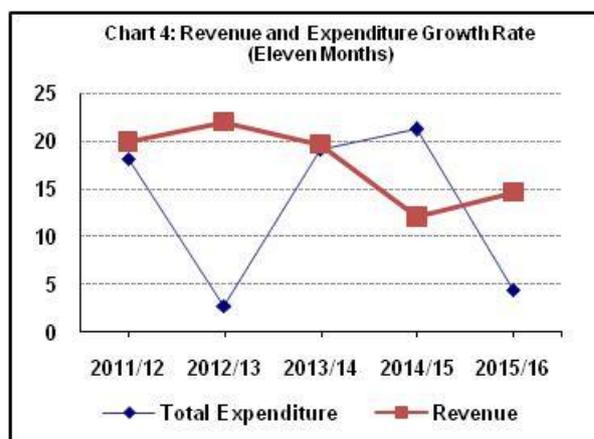
Fiscal Situation *

Budget Deficit / Surplus

30. In eleven months of 2015/16, the Government of Nepal (GoN) ran a surplus of Rs. 59.99 billion in its budget. Such surplus was Rs. 31.98 billion in the corresponding period of the previous year.

Government Expenditure

31. In the review period, total government expenditure on a cash basis increased 4.4 percent to Rs. 388.31 billion. This amount accounts for 47.4 percent of annual budget estimate of Rs. 819.47 billion. Such expenditure had increased 21.3 percent to Rs. 371.91 billion in the corresponding period of the previous year. Total expenditure saw a lower growth on account of slower recurrent and capital expenditure and negative growth rate in financial expenditure.



32. In the review period, recurrent expenditures increased 5.9 percent to Rs. 276.23 billion. Such expenditures had increased 8.5 percent in the corresponding period of the previous year. In the review period, capital expenditures increased only 20.9 percent to Rs. 55.76 billion. Such expenditures had increased 26.8 percent in the corresponding period of the previous year. The capital expenditure in the review period is only 26.7 percent of annual budget estimate of Rs. 208.88 billion

*

Based on the data reported by 8 NRB offices, 69 branches of Rastriya Banijya Bank Limited, 49 branches of Nepal Bank limited, 19 out of 22 branches of Agriculture Development Bank limited, 9 branches of Everest Bank Limited, 4 branches of Global IME Bank Limited and, 1 branch each from Nepal Bangladesh Bank limited, NMB Bank Limited, and Bank of Kathmandu Limited conducting government transactions and released report from 79 DTCOs and payment centers.

Government Revenue

33. In the review period, the government revenue collection increased 14.7 percent to Rs. 396.02 billion. Such revenue had risen 12.1 percent in the corresponding period of the previous year. Higher growth rate of income tax and excise duty contributed to the overall rise in revenue collection in the review period.

Heads	Budget Estimates (Rs. in millions)	Outturns in Eleven months	
		Rs. in million	As percent of budget estimates
Total Expenditure	819468.9	388306.0	47.4
Recurrent Expenditure	484266.4	276230.4	57.0
Capital Expenditure	208877.2	55755.5	26.7
Financial Expenditure	126325.3	56320.1	44.6
Revenue	475012.1	396019.6	83.4

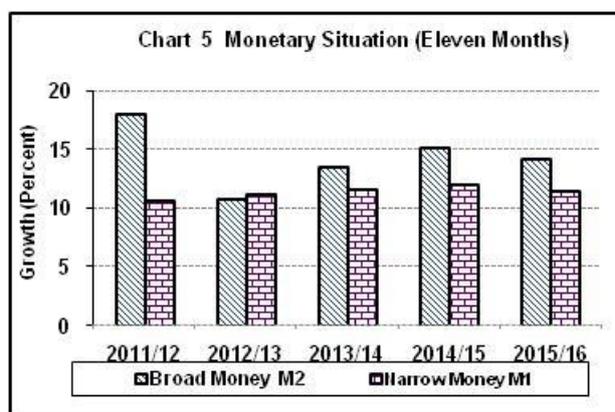
Public Debt and Cash Balance of the GoN

34. In the review period, the GoN has mobilized Rs. 87.66 billion domestic debt and made principal repayment of Rs. 26.30 billion of domestic debt. As a result, outstanding domestic debt increased to Rs. 258.15 billion in mid-June 2016 from Rs. 196.79 billion in mid-July 2015. Because of a slow pace of government expenditure relative to resource mobilization, the GoN accumulated cash balance of Rs. 217.47 billion at Nepal Rastra Bank as of mid-June 2016.

Monetary and Financial Situation

Money Supply

35. Broad money (M2) increased 14.2 percent in the review period compared to an increase of 15.1 percent in the corresponding period of the previous year. On y-o-y basis, M2 expanded 19 percent in mid-June 2016.



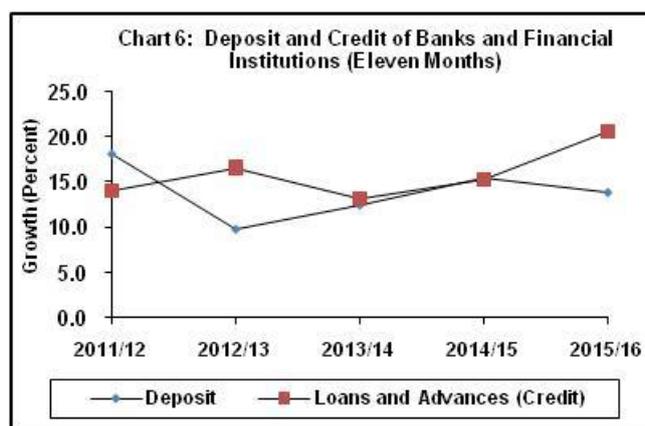
36. Net foreign assets (after adjusting foreign exchange valuation gain/loss) increased Rs. 171.15 billion between mid-July 2015 to mid-June 2016 compared to an increase of Rs. 127.2 billion in the corresponding period of the previous year.
37. Reserve money, which had increased 15.6 percent in the corresponding period of the previous year, declined 0.1 percent in the review period. On y-o-y basis, reserve money increased 3.5 percent in mid-June 2016.

Domestic Credit

38. Domestic credit expanded 8.9 percent in the review period compared to an increase of 10.6 percent in the same period of the previous year. An increase in the government deposits at this Bank resulted in a slower growth of domestic credit in the review period. On y-o-y basis, domestic credit increased 14.4 percent in mid-June 2016.
39. Claims of monetary sector on the private sector increased 19.4 percent in the review period compared to a growth of 18.5 percent in the corresponding period of the previous year. On y-o-y basis, claims on the private sector increased 20.3 percent in mid-June 2016.

Deposit Collection

40. Deposits at BFIs increased 13.9 percent in the review period compared to a growth of 15.4 percent in the same period of the previous year. Deposits at commercial banks and development banks increased 14.1 percent and 11 percent respectively while the deposits at finance companies declined 0.2 percent in the review period. On y-o-y basis, deposits at BFIs expanded 18.5 percent in mid-June 2016.



Credit Disbursement

41. Credit to the private sector from Banks and Financial Institutions (BFIs) increased 18.8 percent in the review period compared to an increase of 17.8 percent in the same period of the previous year. In the review period, private sector credit from commercial banks and development banks increased 21 percent and 15.8 percent respectively while that of finance companies decreased 8.9 percent. On y-o-y basis, credit to the private sector from BFIs increased 20.9 percent in mid-June 2016.
42. Credit to the agriculture sector increased 18 percent, industrial production sector 13.8 percent, construction sector 16.7 percent, service industries 14.5 percent, wholesale and retail trade sector 20.6 percent and transport, communication and public sector 32.3 percent in the review period.
43. Of the total outstanding credit of BFIs, 61.3 percent is against the collateral of land and building and 14 percent against the collateral of current assets (such as agricultural and non-agricultural products). Such ratios were 60.2 percent and 12.3 percent respectively in the same period of the previous year.
44. The credit from BFIs to real estate sector amounted to Rs. 242.61 billion (including Rs. 138.62 billion residential home loans less than Rs. 10 million each) in mid-June 2016. This is 14.9 percent of total credit exposure of BFIs. As at mid-June 2016, the BFIs' total margin lending extended against the collateral of shares stood at 2.1 percent (Rs. 34.19 billion) of their total credit exposure. Of the total lending of the commercial

banks, the credit to small and medium enterprises is only 2.5 percent (Rs. 33.37 billion) in the review period.

45. T. R. (Trust Receipt) loan extended by commercial banks increased 36 percent (Rs. 19.83 billion) in the review period compared to a growth of 15.8 percent in the same period of the previous year.

Liquidity Management

46. In eleven months of 2015/16, the NRB mopped up Rs 527.55 billion liquidity, on a turnover basis, through various instruments. These consist of Rs. 297.50 billion liquidity absorption through

Box 4: Cost of Liquidity Absorption (Rs. in million)				
Liquidity Absorption Instruments	2014/15 (Annual)		2015/16 (Eleven Months)	
	Amount	Interest Expenses	Amount	Interest Expenses
Deposit Collection Auction	155000	170.5	297500	650.1
Reverse Repo Auction	315800	2.8	210950	8.1
Outright Sale Auction	6000	17.3	9100	36.2
Total	476800	190.6	517550	694.4

deposit collection auctions, Rs. 210.95 billion through reverse repo auction, Rs. 10 billion through NRB Bonds and Rs. 9.10 billion through outright sale auction on a cumulative basis. In the corresponding period of the previous year, Rs. 105 billion was mopped up through deposit collection auction, Rs. 290.8 billion through reverse repo auction and Rs. 6 billion through outright sale auction.

47. In the review period, the NRB injected net liquidity of Rs. 423.9 billion through the net purchase of USD 4.01 billion from foreign exchange market (commercial banks). Net liquidity of Rs. 354.76 billion was injected through the net purchase of USD 3.62 billion in the corresponding period of the previous year.
48. The NRB purchased Indian currency (INR) equivalent to Rs. 342.8 billion through the sale of USD 3.12 billion and Euro 110 million in the review period. INR equivalent to Rs. 315.46 billion was purchased through the sale of USD 3.18 billion in the corresponding period of the previous year.

Refinance and Productive Sector Lending

49. The NRB has been providing a refinance facility aimed at expanding credit to the productive sector. In the review period, the use of such facility has increased. In the review period, a total refinance of Rs. 7.52 billion including general refinance of Rs. 6.22 billion and export refinance of Rs. 1.30 billion was availed. In the corresponding period of the previous year, a total refinance of Rs. 7.44 billion including general refinance of Rs. 4.75 billion and export refinance of Rs. 2.69 billion was utilized. Moreover, the bank has introduced a provision of refinance facility at zero percent interest rate to the BFIs with an objective of providing concessional housing loan to earthquake victims. Under this scheme, a sum of Rs. 21.5 million has been extended as of mid-June 2016.
50. There is a policy-provision for commercial banks to disburse 20 percent of their total credit in the productive sector. Such credit of commercial banks out of their total loans and advances stood at 16.83 percent in mid-June 2016. BFIs have extended 5.53 percent credit to

deprived sector in mid-April 2016 compared to 5.08 percent in the same period of previous year.

51. As of mid-April 2016, a total number of 2342 farmers obtained Rs. 1.99 billion loan under the 6 percent interest subsidized lending scheme for selected agro-businesses. Under this provision, Rs. 41.9 million interest subsidy has been provided.

Inter-bank Transaction and Standing Liquidity Facility

52. In the review period, inter-bank transactions of commercial banks stood at Rs. 862.17 billion and those of other financial institutions (excluding transactions among commercial banks) amounted to Rs. 94.79 billion. Such transactions were Rs. 355.74 billion and Rs. 207.82 billion respectively in the corresponding period of the previous year. The BFIs used the standing liquidity facility (SLF) of Rs. 8.55 billion in the review period compared to Rs. 10.21 billion in the same period of previous year.

Interest Rates

53. The weighted average of 91-day Treasury Bill rate decreased while that of inter-bank transaction rate of commercial banks increased in the eleventh month of 2015/16 compared to a year ago. The weighted average 91-day Treasury Bill rate decreased to 0.12 percent in the review month from 0.37 percent a year ago. Weighted average inter-bank transaction rate among commercial banks, which was 0.24 percent a year ago, increased to 0.36 percent in the review month. Weighted average inter-bank rate among other financial institutions decreased to 2.55 percent from 3.86 percent a year ago.
54. In the eleventh month of 2015/16, the weighted average interest rate spread between deposit and lending rate of commercial banks inched up to 5.04 percent from 4.79 percent a year ago and the average base rate came down to 6.27 percent from 7.69 percent a year ago.

Merger/Acquisition and Resolution

55. The number of BFIs opting for merger has been increasing after the introduction of merger policy aimed at strengthening financial stability. After the issuance of the "Bank and Financial Institutions Merger By-law, 2011", 96 BFIs have merged with each other resulting in the formation of 35 BFIs as of mid-June 2016. Likewise, 2 finance companies were acquired by a commercial bank and one development bank was acquired by another development bank.
56. As of mid-April 2016, eleven institutions including 2 development banks and 9 finance companies are under resolution process. Total deposits and loans of such institutions stood at Rs. 3.43 billion and Rs. 6.77 billion respectively. The overall capital fund of these institutions is negative by 38 percent and non-performing loan stood at 95 percent.

Regulatory Measures

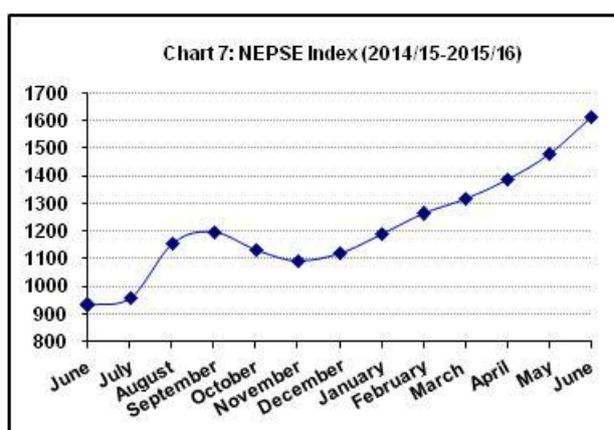
57. In the review period, the NRB issued directives pertaining to branch acquisition of problematic bank by another bank under specified provisions, special refinance facility up to Rs. 0.5 million for extending credit to agriculture and small enterprises in the specified 10 districts of high poverty incidence and bordering VDCs and municipalities of specified

districts in the Southern regions and opening branches in these areas without prior approval from the NRB. Likewise, additional directives relate to the credit extended to the organized sector operating public city transport services under productive sector lending and replacing magnetic strip cards by chip-based card.

58. NRB also issued directives addressing unusual situation caused by the unrest in Terai region and trade-transit disturbances in Indo-Nepal Transit points. Such directives include the continuation of deferred loans as pass loans until mid-April 2016 and exemption from penalty for such loans, rescheduling or restructuring of loan up to one year for one time if borrowers of service sector (industry, trade, education, health, tourism and energy) submit work-plan within mid-April 2016, provision for including accrued interest received by mid-February 2016 in income statement of the second quarter and extension of time period of T.R. loans (import loans) from 120 days to 180 days, among others.
59. In order to enhance the confidence of public in banking system through minimizing risk of banking transaction, this bank has introduced "New Capital Adequacy Framework-2015" based on BASEL III. Commercial banks are required to implement it in parallel run since mid-January 2016 and fully since mid-August 2016.
60. A "Rehabilitation Fund" of Rs. 100 billion, to be operationalized by this Bank, has been established. The fund can be used to provide interest subsidy of 4 percent up to the credit of Rs. 100 million and 2 percent for more than Rs.100 million for the specified sectors to revive economic activities contracted by the disruption in border points and the unrest in southern plain. Likewise, the fund can be used to provide credit from BFIs to earthquake victims up to 5 percent interest rate for specified business and for which refinance facility from this bank is provided at 1.5 percent interest rate.

Capital Market

61. The NEPSE index reached 1,614.2 points in mid-June 2016. The index was 933.7 points in the corresponding period of the previous year. The stock market has been continuously gaining a momentum due to the capital hike policy for financial institutions, full dematerialized transactions from mid-January 2016 and confidence among investors regarding the end of political transition.



62. The total turnover of the securities reached Rs. 30.1 billion in mid-June 2016. Likewise, the total paid-up capital of the listed companies reached Rs. 308.42 billion in mid-June 2016. Total additional securities worth Rs. 26.79 billion were listed in the NEPSE during mid-July 2015 to mid-June 2016. These consist of ordinary shares Rs. 1.95 billion, right shares Rs. 3.62 billion, bonus shares Rs. 19.52 billion and the debentures Rs. 1.70.