Nepal Rastra Bank

Research Department

Current Macroeconomic and Financial Situation of Nepal

(Based on Seven Months' Data of 2017/18)

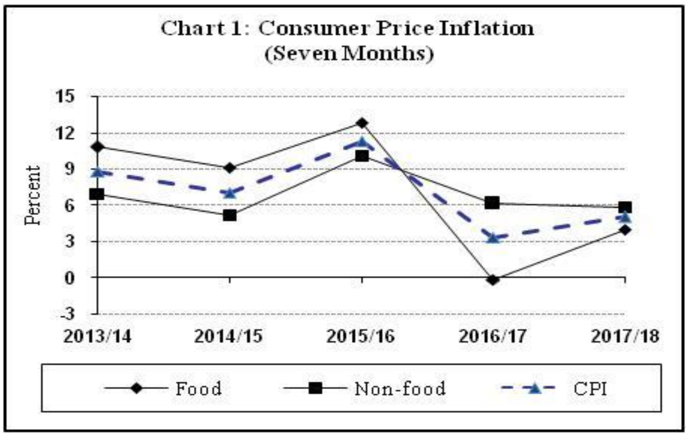
Macroeconomic Outlook

1. The available macroeconomic data of the first seven months of 2017/18 show a mixed macroeconomic outlook going forward. Incessant summer rains and widespread flood in the southern plains hit summer paddy production. Winter rains have remained scanty. As a result, the growth in farm output is expected to be less than that of last year.
2. On non-agricultural front, the performance of energy, construction and reconstruction, and tourism is expected to be better than that of last year. The completion of some hydropower projects is expected to enhance the industrial capacity utilization and help spur overall economic activities. A pick up in tourist arrival and an increase in investment in hotels underpin an optimistic outlook of overall hospitality industry. An uptick in foreign direct investment has ramped up the construction of some hydropower projects and the production of cement. On the top of these factors, the completion of elections and formation of governments at all three levels has created a congenial environment for private sector investment. Interaction of these developments is likely to result in a healthy growth outlook in 2017/18.
3. The year on year (y-o-y) consumer inflation has mildly gone up to 5 percent in mid-February 2018 from 3.3 percent a year ago. Although consumer inflation is on slightly upward trend, the average inflation is expected to remain below the annual forecast.
4. Financial conditions continue to remain tighter. A loss in the accumulation of international reserves on accounts of a deficit in overall balance of payments along with a significant rise in current account deficit has contributed to tighter financial conditions. A pick up in government expenditure is expected to ease financial conditions in days ahead.

Inflation, Salary and Wage Rate

Consumer Price Inflation

5. Consumer price inflation has accelerated to 5.0 percent in mid-February 2018 from 3.3 percent recorded in mid-February 2017. A rise in prices of food items mainly contributed to an upward trend in inflation in the review period.



Food Inflation

6. Food inflation rose to 4 percent in mid-February 2018 from the negative growth of 0.2 percent in the corresponding period of the previous year. A rise in prices of vegetables, milk products and eggs, fruits, meat and fish, ghee and oil, among others is responsible for increase in food inflation in the review period.

Box 1: Y-O-Y Food Inflation (Seven Months)

	Particulars	Inflation (Percent)	
		2073/74	**2074/75**
Food Inflation		**(0.2)**	**4.0**
1	Vegetable	(5.8)	25.5
2	Milk products and eggs	4.6	7.7
3	Fruit	0.7	3.8
4	Meat and fish	(2.4)	2.6
5	Ghee and oil	(8.4)	1.9

Source: National Consumer Price Index, Mid-February 2018

Non-food Inflation

7. Non-food inflation decelerated to 5.8 percent during the review period from 6.1 percent in the corresponding period of the previous year. Deceleration of non-food inflation is attributed to the slower growth of prices of clothes and footwear, furnishing and household equipment, education, among others, during the review period.

Region-wise Consumer Price Inflation

8. The Terai region witnessed relatively a higher rate of inflation of 5.6 percent followed by inflation rate of 5.4 percent in Mountain, 5.1 percent in Hill and 4 percent in the Kathmandu Valley. In the corresponding period of the previous year, these regions had witnessed inflation rates of 3 percent, 3.2 percent, 5.9 percent and 1.1 percent respectively.

Inflation Differential between Nepal and India

9. The y-o-y consumer price inflation stood at 5.0 percent in Nepal in mid-February 2018 compared to 4.4 percent in India, showing an inflation wedge of 0.6 percent between these two countries. A year ago, the rate of inflation was 3.3 percent in Nepal and 3.7 percent in India, resulting in an inflation differential of 0.4 percent between these two countries.

Wholesale Price Inflation

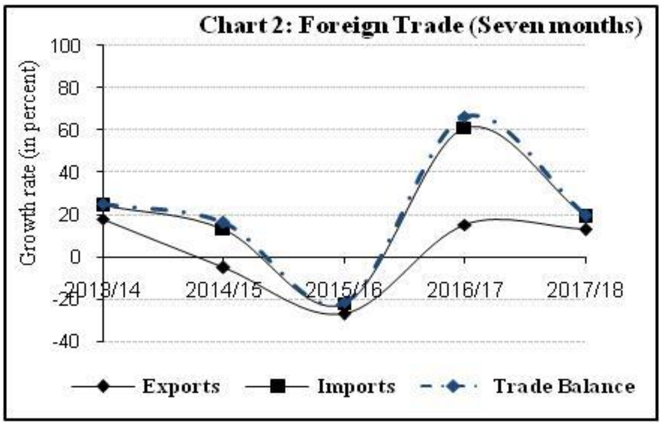
10. The y-o-y wholesale price inflation increased to 2.2 percent in the review period from 1.7 percent a year ago. The wholesale price indices of agricultural commodities fell by 0.1 percent whereas that of domestic manufactured commodities grew by 6.0 percent and imported commodities by 4.5 percent in the review period. In the corresponding period of the previous year, wholesale price indices of agricultural commodities, domestic manufactured commodities and imported commodities had recorded the growth of 0.8 percent, 4.7 percent and 1.6 percent respectively.

National Salary and Wage Rate

11. The y-o-y salary and wage rate index went up by 6.6 percent in the review period compared to a rise of 14.2 percent in the corresponding period of the previous year. In the review period, the salary index increased by 9.4 percent and the wage rate index grew by 5.8 percent. The salary indices of private institutions, education, and bank and financial institutions sub-groups increased by 36.3 percent, 5.8 percent and 1.3 percent respectively in the review period. Likewise, wage rate indices of agricultural, industrial and construction laborer registered a growth of 5.6 percent, 6.6 percent and 4.9 percent respectively in the review period.

External Sector

Merchandise Trade



12. In the first seven months of 2017/18, merchandise exports increased 12.9 percent to Rs. 47.62 billion compared to a growth of 15.2 percent in the same period of the previous year. In the review period, exports to India, China and other countries registered a growth of 12.4 percent, 72.3 percent and 10

percent respectively. Commodity wise, exports of cattle feed, jute goods, vegetable ghee, thread, readymade garments, among others, increased whereas export of juice, cardamom, G.I. pipes, woolen carpet, copper wire rods, among others, decreased in the review period.

13. Merchandise imports recorded a growth of 18.9 percent amounting to Rs. 661.23 billion in the review period compared to an increase of 60.8 percent in the same period of the previous year. In the review period, imports from India, China and Other countries rose by 18.7 percent, 19.7 percent and 18.9 percent respectively. Commodity wise imports of petroleum products, machinery and parts, vehicles, gold, polythene granules, among others, increased whereas imports of agricultural equipment and parts, aircraft spareparts, sanitaryware, zinc ingot, among others, declined in the review period.
14. Based on customs points, the exports through Birgunj Customs Office and Krishnagar Customs Office decreased whereas exports from other customs points increased in the review period. On the import side, imports through Dry Port Customs Office and Kanchanpur Customs Office decreased whereas imports through other customs points increased in the review period.
15. Total trade deficit in the review period widened 19.4 percent to Rs. 613.60 billion compared to a growth of 66.2 percent in the same period of the previous year. The export-import ratio remained 7.2 percent in the review period compared to 7.6 percent in the corresponding period of the previous year.

Export-Import Price Index

16. The y-o-y unit value export price index based on customs data decreased 1.2 percent while import price index increased 1.9 percent in the seventh months of 2017/18. Consequently, the Terms of Trade (TOT) index decreased 3.1 percent compared to an increase of 4.7 percent in the corresponding period of the previous year. Decrease in price of export items such as carpet, pasmina, cardamom, ghee, musuri dal caused the decrease in export price index in the review period. Whereas an increase in the price of petroleum goods, vehicles, tyre, refrigerator, laptop resulted in an increase in import price index in the review period.

Services

17. The total services receipts increased 9.6 percent but expenses rose 19.2 percent in the review period. As a result, net services receipts turned into a deficit of Rs. 2.82 billion in the review period as against a surplus of Rs. 4.59 billion in the same period of the previous year. Under the services account, travel receipts increased 26.5 percent to Rs. 37.78 billion in the review period. Such receipts had increased 30.1 percent in the same period of the previous year.

Workers' Remittances

18. The workers' remittances increased 1.7 percent to Rs. 401.35 billion in the review period compared to a rise of 5.2 percent in the same period of the previous year. However, net transfer receipts decreased 3.0 percent to Rs. 460.85 billion in the review period. Such receipts had increased 8.3 percent in the same period of the previous year.
19. Based on approval, the number of Nepalese workers going for foreign employment (except renew entry) fell by 4.9 percent in the review period. It had decreased 6.7 percent in the same period of the previous year, too.

Box 1: Outflow of Nepalese Workers for Foreign Employment (First Seven Months)

a) Institutional and Individual (New and Legalized)

Country	(No. of Labor)		Percentage Share	
	2016/17	2017/18	2016/17	2017/18
Malaysia	48674	68070	21.3	31.4
Qatar	76429	59282	33.5	27.3
U.A.E.	32671	35813	14.3	16.5
Saudi Arabia	49882	26592	21.9	12.3
Kuwait	7209	8796	3.2	4.1
Bahrain	2292	2923	1.0	1.3
South Korea	918	2785	0.4	1.3
Oman	1813	1689	0.8	0.8
Afghanistan	703	901	0.3	0.4
Japan	1777	437	0.8	0.2
Israel	79	77	0.0	0.0
Lebanon	103	10	0.0	0.0
Others	5579	9650	2.4	4.4
Total	228129	217025	100	100
Percentage Change	-6.7	-4.9	-	-

b) Renew Entry

Renew Entry	150882	148504	-	-
Percentage Change	13.2	-1.6	-	-

Source: *Department of Foreign Employment***.**

Current Account and BOP Position

20. The current account registered a deficit of Rs. 141.06 billion in the review period compared to a deficit of Rs. 10.66 billion in the same period of the previous year. The significant increase in imports and dividends payment for foreign investment led to such a widening in current account deficits. Similarly, the overall BOP remained at a deficit of Rs. 18.28 billion in contrast to a surplus of Rs. 36.95 billion in the same period of the previous year.
21. In the review period, Nepal received capital transfer amounting to Rs. 10.64 billion and Foreign Direct Investment (FDI) inflows of Rs. 14.34 billion. In the same period of the previous year, capital transfer and FDI inflows were Rs. 9.25 billion and Rs. 7.60 billion respectively.

Box 2: External Sector (USD)*

(USD Million)

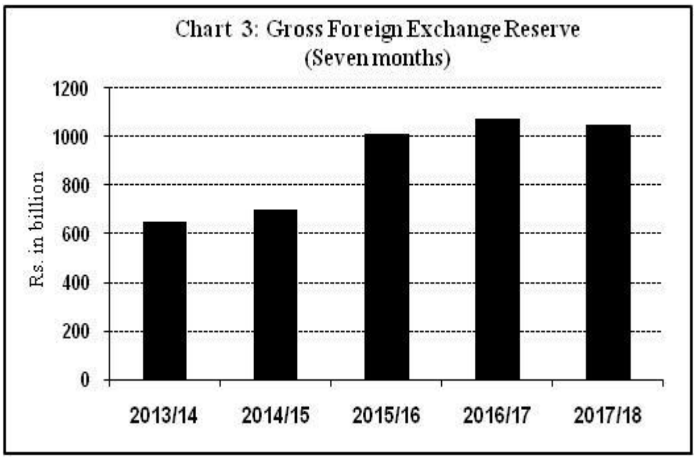
Particulars	2015-16		2016-17		2017-18	Percent Change in Seven month	
	Seven Months	Annual	Seven Months	Annual	Seven Months	2016/17	2017/18
Goods Exports (FoB)	366.2	703.9	438.0	773.7	522.3	19.6	19.2
Goods Imports (FoB)	3212.1	7092.5	5090.4	9219.3	6312.1	58.5	24.0
Trade Balance	-2845.9	-6388.6	-4652.4	-8445.6	-5789.9	63.5	24.4
Travel Receipts	217.4	392.7	277.4	552.3	366.3	27.6	32.0
Workers' Remittances	3553.8	6253.4	3664.3	6556.3	3898.6	3.1	6.4
Current Account Balance	1471.3	1338.8	-97.6	-93.5	-1373.3	-	-
BOP (-Surplus)	-1458.6	-1779.4	-343.4	-776.6	178.7	-	-

** Data from BOP Presentation*

1. In the US dollar terms, total merchandise exports and imports increased 19.2 percent and 24 percent respectively in the seven months of 2017/18. Exports and imports had increased 19.6 percent and 58.5 percent in the corresponding period of the previous year.
2. In the review period, travel receipts and workers' remittance increased 32 percent and 6.4 percent respectively. Travel receipts and workers' remittances had increased 27.6 percent and 3.1 percent respectively in the corresponding period of the previous year.
3. Current account recorded a deficit of USD 1.37 billion in the review period compared to a deficit of USD 97.6 million in the corresponding period of the previous year. Likewise, Balance of Payments (BOP) recorded a deficit of USD 178.7 million in the review period in contrast to a surplus of USD 343.4 million in the corresponding period of the previous year.

Foreign Exchange Reserves

22. The gross foreign exchange reserves decreased 2.8 percent to Rs. 1049.20 billion as at mid-February 2018 from Rs. 1079.43 billion as at mid-July 2017. Of the total foreign exchange reserves, reserves held by NRB increased 1 percent to Rs. 936.21 billion as at mid-February 2018 from Rs. 927.27 billion as at mid-July 2017. The reserves of banks and financial institutions (except NRB) decreased 25.7 percent to Rs. 112.99 billion as at mid-February 2018 from Rs. 152.17 billion as at mid-July 2017. The share of Indian currency in total reserves stood at 24.7 percent as at mid-February 2018.



Foreign Exchange Adequacy Indicators

23. Based on the imports of seven months of current fiscal year, the foreign exchange holdings of the banking sector is sufficient to cover the prospective merchandise imports of 11.3 months, and merchandise and services imports of 9.8 months. The ratio of reserve-to-GDP, reserve-to-

imports and reserve-to-M2 stood at 40.4 percent, 81.9 percent and 37.6 percent respectively as at mid- February 2018. Such ratios were 41.5 percent, 95.2 percent and 41.6 percent as at mid-July 2017.

Price of Oil and Gold

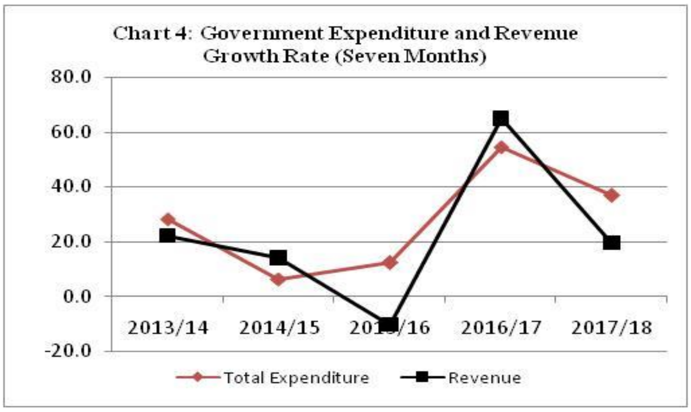
24. The price of oil (Crude Oil Brent) in the international market increased 12.7 percent to USD 62.20 per barrel in mid-February 2018 from USD 55.20 per barrel a year ago. The price of gold increased 7.7 percent to USD 1322.30 per ounce in mid-February 2018 from USD 1228.30 per ounce a year ago.

Exchange Rate

25. Nepalese currency vis-à-vis US dollar appreciated 0.1 percent in mid-February 2018 from the level of mid-July 2017. It had appreciated 0.1 percent in the same period of the previous year. The buying exchange rate per US dollar stood at Rs. 102.74 in mid-February 2018 compared to Rs. 102.86 in mid-July 2017.

Fiscal Situation*

Budget Deficit/ Surplus



26. In the first seven months of 2017/18, budgetary position of the Government of Nepal (GoN) was at a deficit of Rs. 26.47 billion. There was a budget surplus of Rs. 17.95 billion in the corresponding period of the previous year.

Government Expenditure

27. In the review period, total government expenditure on a cash basis stood at Rs. 428.88 billion. Such expenditure was Rs. 313.30 billion in the corresponding period of the previous year.
28. In the review period, recurrent expenditure stood at Rs. 349.75 billion, which was Rs. 237.54 billion in the corresponding period of the previous year. In the review period, capital

* Based on the data reported by 1 NRB office, 80 branches of Rastriya Banijya Bank Limited, 52 branches of Nepal Bank Limited, 34 branches of NIC Asia Bank Limited, 27 branches of Agricultural Development Bank Limited, 12 branches of Everest Bank Limited, 10 branches of Nepal Investment Bank Limited, 9 branches of Global IME Bank Limited, 7 branches of NMB Bank Limited, 3 branches of Bank of Kathmandu Limited and 2 branches each of Prabhu Bank Limited and Nepal Bangladesh Bank Limited and 1 branch each from Prime Commercial Bank Limited, Century Commercial Bank Limited, Sanima Bank Limited and Civil Bank Limited conducting government transactions and released report from 81 DTCOs and payment centers.

expenditure increased 28 percent to Rs. 60.08 billion. Such expenditure was Rs. 46.94 billion in the corresponding period of the previous year.

Government Revenue

29. In the review period, the government revenue collection increased 19.5 percent to Rs. 381.34 billion. Such revenue had increased 65 percent to Rs. 319.15 billion in the corresponding period of the previous year. The growth in the government revenue continues to remain sensitive to imports related to high tariff rate.

Box 3: The Budget Performance of 2017/18
(Rs. in million)

Heads	Budget Estimates	Outturns in Seven Months*	As percent of Budget Estimates
Total Expenditure	**1278994.9**	**428883.5**	**33.53**
Recurrent	803531.5	349753.7	43.53
Capital	335176.0	60084.3	17.93
Financial	140287.4	47616.5	13.58
Revenue	**730055.6**	**381343.2**	**52.23**

* On cash basis

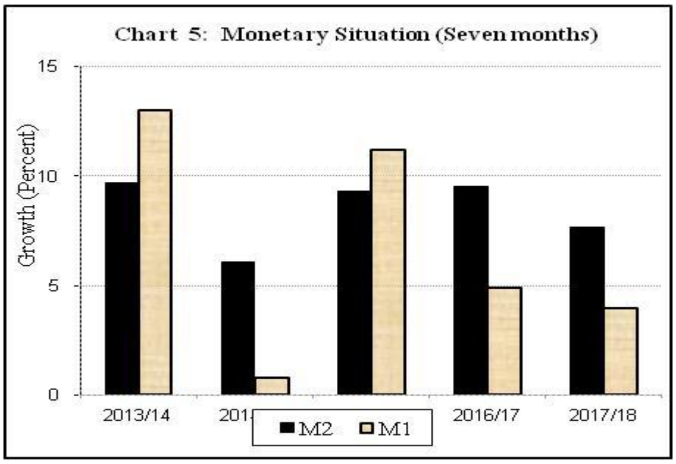
Treasury Position of the GoN

30. GoN treasury surplus amounted to Rs. 301.64 billion (including Rs. 84.35 billion balances on Local Authorities' Accounts) as of mid-February 2018.

Monetary Situation

Money Supply

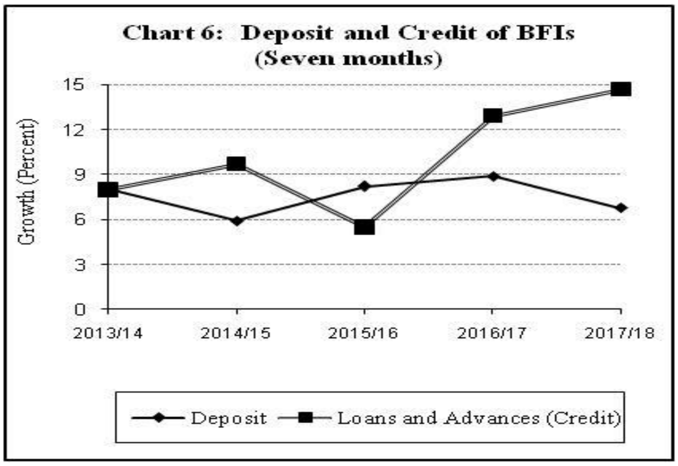
31. Broad money (M2) increased 7.7 percent in the review period compared to a rise of 9.5 percent in the corresponding period of the previous year. On y-o-y basis, M2 expanded 13.5 percent in mid-February 2018.



32. The net foreign assets (NFA after adjusting foreign exchange valuation gain/loss) decreased Rs. 18.28 billion (1.8 percent) in the review period compared to an increase of Rs. 36.95 billion (3.9 percent) in the corresponding period of the previous year.
33. Reserve money decreased 5.2 percent in the review period compared to an increase of 4.3 percent in the corresponding period of the previous year. On y-o-y basis, reserve money increased 9.2 percent in mid-February 2018.

Domestic Credit

34. Domestic credit increased 9.2 percent in the review period compared to an increase of 9.3 percent in the corresponding period of the previous year. On y-o-y basis, domestic credit increased 20.5 percent in mid-February 2018.



35. Claims of monetary sector on the private sector increased 14.1 percent in the review period compared to a growth of 15.4 percent in the corresponding period of the previous year. On y-o-y basis, increase on such claims stood 16.7 percent in mid-February 2018.

Deposit Collection

36. Deposits at Banks and Financial Institutions (BFIs) increased 6.8 percent in the review period compared to a growth of 8.9 percent in the corresponding period of the previous year. On y-o-y basis, deposits at BFIs rose 11.8 percent in mid-February 2018.
37. Out of the total deposits at the BFIs, the share of demand deposits marginally increased from 8.1 percent to 8.2 percent and fixed deposits from 35.1 percent to 43.9 percent in mid-February 2018 compared to a year ago. However, the share of saving deposits decreased to 36.6 percent from 38.7 percent a year ago.
38. The share of institutional deposits in total deposit of BFIs stood at 44 percent in mid-February 2018. Such a share was 48.5 percent a year ago.

Credit Disbursement

39. Credit to the private sector from BFIs increased 13.5 percent in the review period compared to a growth of 15.1 percent in the corresponding period of the previous year. In the review period, private sector credit from commercial banks, development banks and finance companies increased 13.2 percent, 18.8 percent and 4.8 percent respectively. On y-o-y basis, credit to the private sector from BFIs increased 16.7 percent in mid-February 2018.
40. Of the total outstanding credit of BFIs, 61.5 percent flowed against the collateral of land and building and 14.6 percent against the collateral of current assets (such as agricultural and non-agricultural products). Such ratios were 60.2 percent and 14.4 percent respectively in the corresponding period of the previous year.

41. Trust receipt loan extended by commercial banks increased 61.8 percent (Rs. 39.86 billion) to Rs. 104.39 billion in the review period compared to an increase of 14.3 percent in the corresponding period of the previous year.
42. In the review period, hire purchase loan increased 8.4 percent and overdraft loan rose 10.9 percent. Likewise, real estate loan (including residential personal home loan) increased 10.7 percent in the review period.

Liquidity Management

43. In the review period, NRB mopped up Rs. 130.25 billion liquidity through open market operations. Of which, Rs. 42.35 billion was mopped up under deposit collection auction, Rs. 3.15 billion through 14 days deposit collection auction under interest rate corridor and Rs. 84.75 billion through reverse repo auction on a cumulative basis. Rs. 101.10 billion liquidity was mopped up in the corresponding period of the previous year.
44. In the review period, Rs. 90.40 billion liquidity was injected. Of which, Rs. 54.05 billion was injected through 14 days repo auction under interest rate corridor and Rs. 36.35 billion through outright purchase auction. In the corresponding period of the previous year, Rs. 42.38 billion liquidity was injected.

45. In the review period, BFIs utilized Rs. 24.08 billion Standing Liquidity Facility (SLF). In the corresponding period of the previous year, BFIs had utilized such facility of Rs. 54.83 billion.
46. In the review period, NRB injected net liquidity of Rs. 238.38 billion through the net purchase of USD 2.31 billion from foreign exchange market. Net liquidity of Rs. 251.12 billion was injected through the net purchase of USD 2.33 billion in the corresponding period of the previous year.
47. NRB purchased Indian currency (INR) equivalent to Rs. 284.79 billion through the sale of USD 2.72 billion and Euro 40 million in the review period. INR equivalent to Rs. 265.53 billion was purchased through the sale of USD 2.36 billion and Euro 95 million in the corresponding period of the previous year.

Refinance

48. NRB has been providing refinance facility aimed at expanding credit to the productive sector along with promoting exports. As of mid-February 2018, the outstanding refinance amounted to Rs. 11.84 billion.
49. A sum of Rs. 1.28 billion housing loan at a concessional interest rate of 2 percent has been extended by the BFIs to the earthquake victims as of mid-February 2018. NRB provides refinance facility to BFIs at a zero percent interest to extend housing loans to earthquake victims.

50. As of mid-February 2018, the number of beneficiaries from the 5 percent interest subsidized lending scheme of the GoN stood at 6203. They availed subsidized loans for selected agriculture and livestock businesses. Under this provision, Rs. 6.91 billion loan extended by BFIs has been outstanding and Rs. 337.3 million interest subsidy has been provided.

Inter-bank Transaction

51. In the review period, inter-bank transactions among commercial banks recorded at Rs. 694.16 billion and among other financial institutions (excluding transactions among commercial banks) Rs. 14.38 billion. Such transactions were Rs. 699.02 billion and Rs. 239.88 billion respectively in the corresponding period of the previous year.

Interest Rates

52. The weighted average 91-day Treasury bill rate increased to 3.93 percent in the seventh month of 2017/18 from 2.64 percent a year ago. The weighted average inter-bank transaction rate among commercial banks, which was 4.13 percent a year ago, increased to 4.31 percent in the review month. Likewise, the average base rate of commercial banks increased to 10.19 percent in the review month from 7.80 percent a year ago.

Merger/Acquisition

53. The number of BFIs involved in merger and acquisition has been increasing after the introduction of merger/acquisition policy aimed at strengthening financial stability. So far, 158 BFIs (including 'D' class) were involved in merger and acquisition. Out of which, the license of 118 BFIs was revoked, thereby forming 40 BFIs.

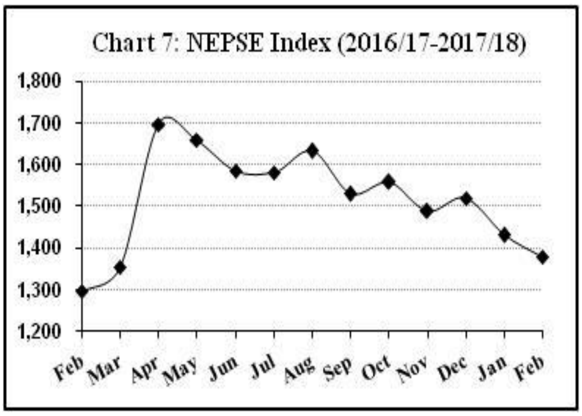
Financial Access

54. Of the total 753 local levels formed in the process of implementing federalism, commercial banks have their presence in 374 local levels as of mid-February 2018. Province wise presence of commercial banks in local levels is presented in Box 4.

Box 4: Province wise Presence of Commercial Banks in Local Bodies (As of mid-Feb 2018)

Province	No. of Local Bodies	No. of Banks/ Branches
Province 1	137	71
Province 2	136	63
Province 3	119	71
Province 4	85	45
Province 5	109	66
Province 6	79	25
Province 7	88	33
Total	**753**	**374**

Capital Market



55. The NEPSE index on y-o-y basis increased 6.5 percent to 1380.3 points in mid-February 2018. This index had increased 2.6 percent to 1296.2 points in mid-February 2017. Such index was 1582.7 points in mid-July 2017.

56. The stock market capitalization on y-o-y basis increased 10.7 percent to Rs. 1614.17 billion in mid-February 2018. This had increased 7.2 percent a year ago. The ratio of market capitalization to GDP of 2016/17 stood at 62.1 percent in mid-February 2018. This ratio was 64.9 percent a year ago. In the total market capitalization, the share of banks, financial institutions and insurance companies stood at 81.1 percent, hydropower 4.7 percent, manufacturing and processing companies 2.7 percent, hotels 1.7 percent, trading 0.1 percent, and others 9.7 percent respectively.

57. During the seventh month of 2017/18 the total turnover of the securities decreased 26.4 percent to Rs. 5.92 billion. The turnover of the securities had decreased 14.3 percent to Rs. 8.04 billion in the corresponding period of the previous year.

58. Due to the merger and acquisitions of BFIs, total number of companies listed at the NEPSE decreased to 192 in mid-February 2018 from 216 in mid-February 2017. Of the listed companies, 145 are BFIs (including insurance companies), 18 manufacturing and processing industries, 17 hydropower companies, 4 each hotels and trading institutions and 4 other sectors.

59. On y-o-y basis, total paid-up value of the listed shares increased 35.5 percent to Rs. 333.07 billion in mid-February 2018. Total additional securities worth Rs. 89.12 billion were listed in the NEPSE during the review period. These consisted of ordinary shares of Rs. 16.62 billion, right shares of Rs. 26.32 billion, bonus shares of Rs.10.43 billion and government securities of Rs. 35.14 billion.