Current Macroeconomic Situation

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

Monetary Situation

Money Supply

1. Broad money (M_2) grew by 17.4 percent in the first ten months of 2008/09 compared to a growth of 19.3 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 subdued growth of net domestic assets on account of a decline in net claims on government and a rise in net non-monetary liabilities contributed to the growth of M_2 by a lower rate in the review period.
2. Narrow money (M_1) grew by 15.7 percent in the review period, a growth similar to that of the previous year. Though demand deposits, one of the components of $M_{1,}$ registered a muted growth of 1.6 percent in the review period compared to a growth of 11.6 percent in the previous year, M_1 witnessed a similar growth of the previous year on account of a substantial growth of currency in circulation. Such currency increased by 23.2 percent in the review period compared to a growth of 17.8 percent in the corresponding period of the previous year. Likewise, time deposits grew by 18.2 percent in the review period compared to a growth of 21.0 percent in the previous year.
3. Net foreign assets (NFA), after adjusting foreign exchange valuation gain/loss, increased by Rs. 43.1 billion (25.1 percent) in the review period compared to a growth of Rs 19.9 billion (15.1 percent) in the same period of the previous year. An elevated inflows of remittance accompanied by an increase in foreign assistance of the government of Nepal (GON) contributed to a significant growth of NFA in the review period.

Domestic Credit

4. In the first ten months of 2008/09, domestic credit expanded by 13.9 percent compared to a growth of 16.6 percent in the corresponding period of the previous year. A sharp decline in net claims on government by 18.2 percent (Rs 15.9 billion) on account of a higher resource mobilization relative to the expenditure of the GON, resulting in cash deposits of Rs. 21.6 billion (including surplus of Rs.3.9 billion for the previous year) with Nepal Rastra Bank (NRB) in the review period, contributed to a lower growth of domestic credit in the review period.
5. Claims on non-financial government enterprises declined by 8.8 percent (Rs. 490.0 million) in the review period compared to a decline of such credit by 6.9 percent (Rs 350.0 million) in the corresponding period of the previous year. A partly repayment of loan by National Trading Ltd and Nepal Food Corporation and a full repayment of loan by Nepal Oil Corporation contributed to the decline in the claims on such enterprises in the review period.
6. Claims on financial institutions grew by 16.3 percent (Rs 767.1 million) in the review period. Such credit had grown by Rs 9.9 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 was responsible for the lower growth of claims on financial institutions in the review period.
7. The review period witnessed a higher growth of claims on private sector compared to that of the previous year. The claims on the private sector grew by 22.4 percent in the review period compared to a growth of 19.5 percent in the corresponding period of the previous year. An inclusion of the credit disbursed by KIST Bank which was previously operating as a 'C' class financial institution, contributed to a higher growth of private sector claims in the review period.

Reserve Money

8. Reserve money grew by 25.9 percent in the review period. The reserve money had increased by 15.3 percent in the corresponding period of the previous year. A substantial growth of net foreign assets of monetary authority contributed to a higher growth of reserve money in the review period. On the demand side, the effect of higher growth of reserve money has been reflected in the currency in circulation and deposits of commercial banks with the NRB.

Deposit Mobilizations and Credit Flow of Commercial Banks

9. In the first ten months of 2008/09, deposit mobilization of commercial banks increased by Rs 81.9 billion (19.4 percent) amounting to Rs 503.5 billion as in mid-May 2009. Deposit mobilization of commercial banks had increased by Rs 63.5 billion (19.0 percent) in the corresponding period of the previous year. Saving and fixed deposits increased by 19.8 percent and 24.2 percent respectively in the review period. Such deposits had increased by 16.2 percent and 26.7 percent respectively in the corresponding period of the previous year.
10. Besides deposit mobilization, commercial banks increased the resource mobilization through means of injection of capital. Commercial banks injected additional capital of Rs 7.4 billion in the review period compared to an additional capital injection of Rs 6.6 billion in the corresponding period of the previous year. The share of total capital mobilized by the commercial banks to their total assets/liabilites stands at 5.79 percent as in mid-May 2009 compared to such ratio of 4.92 percent as in mid-May 2008. The ever-growing ratio of capital to total assets/liabilities is a positive sign for financial sector stability.
11. The review period witnessed marginally a lower growth of private sector credit from commercial banks compared to that of the previous year. In the review period, credit to the private sector expanded by 24.2 percent compared to a growth of 24.9 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, credit to the transportation equipment production and fittings and consumable sectors increased in the review period. Credit to the production and construction sectors increased by 14.9 percent and 34.9 percent in the review period compared to an increase of 18.0 percent and 49.7 percent respectively in the corresponding period of the previous year. Likewise, credit to wholesale and retail business and service sectors increased by 15.7 percent and 6.0 percent respectively compared to an increase of 16.8 percent and 16.3 percent in the previous year. Although, credit growth to the real sector also declined in the review period, the amount of disbursement of credit is higher, that is 11.0 billion as in mid-May 2009 compared to a disbursement of Rs. 6.0 billion in the previous year. In the review period, consumable loan has increased by 36.9 percent (Rs. 3.5 billion).
12. The liquid funds of commercial banks grew by 41.7 percent in the review period compared to a growth of 12.8 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 58.0 percent compared to a muted growth of 0.9 percent in the corresponding period of the previous year. Likewise, the commercial banks' balance held abroad increased significantly by 39.3 percent amounting to Rs 57.3 billion in mid-May 2009 compared to a growth of 15.0 percent a year ago. Including the investment of commercial banks on the government securities, total liquid assets of commercial banks increased by 19.2 percent amounting to Rs 180.1 billion as in mid-May 2009 compared to a growth of 3.51 percent in the previous year.

Liquidity Management

13. In the first ten months of 2008/09, the NRB mopped up net liquidity of Rs. 11.7 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 liquidity of Rs 9.0 billion has been injected through repo auctions in the seventh and eighth months of the review period on account of a shortfall in liquidity, 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 4.0 billion had been mopped up in the corresponding period of the previous year through open market operation including Rs. 6.5 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 ten months of 2008/09, the NRB injected net liquidity of Rs. 121.5 billion by net purchase of 1.6 billion US dollar from commercial banks through foreign exchange intervention. A net liquidity of Rs. 76.6 billion had been injected through a net purchase of 1.2 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 59.9 billion through the sale of 1.3 billion US dollar in the review period. Indian currency of 48.3 billion had been purchased through the sale of 1.2 billion US dollar in the corresponding period a year ago. A depreciation of Nepalese currency vis-à-vis the US dollar encouraged the import from India against the payment of Indian currency and, therefore, a higher amount of IC purchase was made as against a sale of the US dollar in the review period.

Standing Liquidity Facility and Inter Bank Transactions

16. In the first ten months of 2008/09, commercial banks used standing liquidity facility (SLF) of Rs 97.8 billion compared to that of Rs. 97.6 billion in the corresponding period of the previous year. Likewise, the inter bank transactions of commercial banks stood at Rs 248.2 billion in the review period compared to that of Rs 225.0 billion in the corresponding period of the previous year. A tightening of liquidity on account of a higher cash balance of the GON with the NRB and increase in currency in circulation in the review period contributed to the increase in the inter bank transactions and use of the SLF in the review period.

Short-term Interest Rates

17. The short-term market interest rates increased in the tenth month of 2008/09. The weighted average monthly 91-day Treasury bill rate stood at 6.73 percent as in mid-May 2009 compared to that of 5.32 percent a year ago. The weighted average monthly inter bank rate stood at 7.07 percent as in mid-May 2009 compared to that of 6.48 percent in the corresponding period of the previous year.
18. Along with an increase in short-term market interest rates, interest rates on deposits and credit also increased in the review period. The maximum interest rate on two or more than two years fixed deposits increased by 75 basis point to 8.75 percent as in mid-May 2009 from a rate of 8.0 percent in mid-April 2009. Likewise, minimum interest rates on industrial loans also increased by 25 basis points to 8.25 percent as in mid-May 2009 compared to that of mid-April 2009.

Securities market

19. The year on year (y-o-y) NEPSE index decreased by 18.0 percent to 660.96 points in mid-May 2009. This index was 806.26 a year ago. Likewise, NEPSE sensitive index (based on July 2006) stood at 174.13 points in mid-May 2009. This index had stood at 212.14 points in mid-May 2008.

20. The NEPSE float index, calculated on the basis of final transaction as of August 24, 2008 (at market price) remained 63.89 in mid-May 2009.

21. The y-o-y market capitalization increased by 54.5 percent to Rs. 423.5 billion in mid-May 2009. Of the total market capitalization, bank and financial institutions, manufacturing and processing companies, hotels, business entities, hydropower and other economic sectors accounted for 73.3 percent, 1.8 percent, 1.1 percent, 0.3 percent, 4.0 and 19.4 percent respectively.

22. Total paid up capital of the listed companies stood at Rs. 55.2 billion in mid-May 2009 and increased by 116 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. 27.56 billion up to mid-May 2009, bonus share, right share, ordinary share and bonds accounted for Rs. 1.58 billion, Rs. 5.6 billion, Rs.17.1 billion and Rs. 3.3 billion respectively. The ordinary share constituted the largest portion mainly due to the share of Nepal Telecom.

23. The monthly turnover to market capitalization ratio remained at 0.25 percent in mid-May 2009, compared to 0.70 percent a year ago.

24. Total number of companies listed at the NEPSE increased to 157 in mid-May 2009 compared to 148 a year ago. Among them, 126 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 156.9 in mid-May 2009 compared to 151.7 a year ago.

Inflation

Consumer Price Inflation

26. The y-o-y consumer price index rose by 12.9 percent in mid-May 2009 compared to that of 9.2 percent in the same period of the previous year. The inflation, in the review period, was driven mainly by the rise of 16.5 percent in food and beverages group. The price index of non-food and service group increased by 8.8 percent. The price increases of food and beverages and non-food and services group, were 13.0 percent and 5.3 percent respectively in mid-May 2008.

27. In 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 66.9 percent. This is in sharp contrast to last year's decline of 0.5 percent. Similarly, the price indices of vegetables and fruits as well as meat, fish and eggs sub-groups increased by 33.5 percent and 27.5 percent respectively in the review period compared to an increase of 1.8 percent and 10.2 percent in the same period last year. The indices of pulses also rose by 26.3 percent compared to an increase of 12.1 percent in the same period of last year. The subgroup of grains and cereal products also witnessed a price rise of 6.3 percent compared to an increase of 21.0 percent in the corresponding period of the previous year.

28. Within the group of non-food and services, the index of tobacco and related products as well as transport and communication went up by 17.5 percent and 13.9 percent in the review period compared to a rise of 10.5 percent and 1.0 percent respectively in the same period last year.

29. Region-wise, the price rise in Kathmandu valley was 14.3 percent followed by 12.4 percent in Terai and 11.8 percent in Hills in the review period. Last year, the respective rates were 8.5 percent, 10.0 percent and 8.6 percent.

30. In the review period, the y-o-y core inflation rose to 12.7 percent from 7.5 percent a year ago.

Wholesale Price Inflation

31. In the review period, the y-o-y wholesale price inflation increased to 15.5 percent compared to 10.1 percent a year ago. The index of agricultural commodities, imported commodities and domestic manufactured commodities increased by 23.4 percent, 8.4 percent and 7.7 percent respectively in the review period compared to 10.3 percent, 8.9 percent and 11.7 percent a year ago.

32. Of the agricultural commodities, mainly the price index of cash crops increased by 59.0 percent in the review period, compared to a decline of 11.4 percent a year ago. Likewise, the price indices of livestock production, pulses and fruits and vegetables increased by 34.0 percent, 25.4 percent and 24.8 percent in the review period compared to an increase of 12.2 percent, 12.1 percent and 7.0 percent in the same period last year. Within the group of domestic manufactured commodities, the price index of beverages and tobacco increased by 17.3 percent compared to a rise of 5.8 percent a year ago.

33. Of the imported commodities, the price indices of textile related products increased by 20.8 percent in the review period, compared to a rise of 0.2 percent in the corresponding period of the previous year. Likewise, the price indices of transport vehicles and machinery goods increased by 14.2 percent compared to an increase of 11.7 percent a year ago.

National Salary and Wage Rate

34. The overall y-o-y salary and wage rate index rose by 21.1 percent in the review period compared to a rise of 7.0 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 22.5 percent in the review period compared to an increase of 5.9 percent in the same period of the previous year. Such an increase was due to the increase in the salary of civil servants. Wages of agricultural, industrial and construction labourers increased by 27.8 percent, 15.1 percent and 21.3 percent respectively in the review period. These wage rates had increased by 6.3 percent, 4.6 percent and 7.1 percent respectively in the same period of the previous year

Fiscal Situation

Budget Deficit / Surplus

35. In the first ten months of 2008/09, the government budget on cash basis remained at a surplus of Rs.6.0 billion in contrast to a deficit of Rs.6.0 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. 21.6 billion (including Rs. 3.9 billion of previous year) with Nepal Rastra Bank.

Government Expenditure

37. In the first ten months of 2008/09, the total government expenditure on cash flow basis, increased by 25.7 percent to Rs. 127.6 billion compared to an increase of 28.2 percent in the corresponding period of the previous year. Low growth rate of capital expenditure accounted for such a deceleration of total government expenditure.

38. In the first ten months of 2008/09, recurrent expenditure increased by 26.5 percent to Rs. 81.9 billion. In the corresponding period of the previous year, this expenditure had increased by 21.9 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 11.4 percent to Rs. 26.0 billion in contrast to an increase of 55.6 percent in the same period of the previous year. Delay in presenting budget, lack of representatives in local bodies, delay in the formulation of programs and directives of the approved projects under New Nepal movement, delay in contracts and procurement procedures as well as uncertain and irregular power supply situation accounted for such a low growth in capital expenditure in the review period.

Government Revenue

40. In the first ten months of 2008/09, revenue mobilization of the government grew by 39.9 percent to Rs.110.5 billion compared to an increase of 24.0 percent in the corresponding period of the previous year. The Government's firm commitment at revenue leakage control, revenue administration reforms, Voluntary Disclosure 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 24.5 percent to Rs. 31.2 billion in mid-May 2009. It had increased by 21.8 percent in the corresponding period of the previous year. The increase in VAT revenue was on account of growing imports and consumption induced by significant rise in remittances as well as the reforms in VAT administration.

42. In the review period, customs revenue rose by 29.2 percent to Rs. 20.9 billion compared to an increase of 21.5 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 a growth.

43. In the review period, excise revenue increased by 45.0 percent to Rs. 12.6 billion compared to an increase of 23.9 percent in the same period of the previous year. Reforms in excise administration and identification of newly excised goods accounted for such a growth.

44. Income tax revenue increased by 46.0 percent to Rs. 20.3 billion in the first ten months of 2008/09. A remarkable receipt under VDIS program due to government's firm administrative and political commitment contributed to such an increase in the income tax. Last year, such revenue had risen by 34.4 percent.

45. In the review period, non-tax revenue surged by 62.1 percent to Rs. 19 billion compared to an increment of 16.8 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. 3.2 billion and foreign cash grants of Rs. 18.8 billion in the first ten months of 2008/09. The same were Rs. 3.1 billion and of Rs. 13.7 billion respectively in the comparable 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. Exports shot up by 19.8 percent in the first ten months 2008/09 in contrast to a decline by 2.4 percent in the corresponding period of the previous year. While exports to India rose by 10.5 percent in 2008/09 as against a decline by 7.4 percent in the corresponding period of the previous

year, exports to other countries accelerated by 38.8 percent compared to an increase of 9.8 percent in the same period of the previous year.

49. The rise in the exports of readymade garments, textiles, G.I. pipe, catechu and tooth paste was largely responsible for the increase in exports to India. Likewise, the rapid increase in the exports to other countries can be attributed to the rise in the exports of pulses followed by pashmina, woollen carpets, readymade garments and handicraft.

50. Total imports went up by 25.4 percent in the first ten months of 2008/09 compared to an increase of 16.8 percent in the corresponding period of the previous year. Imports from India rose by 11.5 percent in the review period compared to a growth of 25.7 percent in the corresponding period of 2007/08; likewise, imports from other countries surged by 50.4 percent compared to a growth of just 3.7 percent in the preceding year.

51. A rise in the import of other machinery and parts, vehicles and spare parts, cold-rolled sheet in coil, cement and medicine, among others, from India and gold, electrical goods, MS billet, crude soyabean oil and other machinery & parts, among others, from other countries were largely responsible for the surge in total imports in the first ten months of 2008/09.

Balance of Payments

52. In the first ten months of 2008/09, the overall BOP posted a significant surplus of Rs. 43.1 billion compared to a lower surplus of Rs. 19.9 billion in the corresponding period of the previous year. The current account also recorded a huge surplus of Rs. 37.0 billion in the review period compared to a surplus of just Rs. 7.1 billion in the corresponding period of the previous year. The significant current account surplus in the review period was largely due to the rise in net transfers by 43.6 percent in the first ten months of 2008/09. Under transfers, workers' remittances soared by 55.5 percent in the review period compared to a growth of 35.5 percent in the corresponding period of the previous year. Similarly, grants rose by 28.4 percent in the review period in contrast to a decline by 4.6 percent in the corresponding period of the previous year.

Foreign Exchange Reserves

53. In mid-May 2009, the gross foreign exchange reserves stood at Rs. 283.4 billion, a rise by 33.3 percent compared to the level as at mid-July 2008. In the corresponding period of the previous year, such reserves had risen by 19.3 percent. On the basis of US dollar, gross foreign exchange reserves rose by 15.4 percent to US$ 3.6 billion in mid-May 2009. Such reserves had gone up by 15.5 percent in the same period of the previous year. The current level of reserves is adequate for financing merchandise imports of 12.4 months and merchandise and service imports of 10.1 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) fell by 54.7 percent to US$ 56.13 per barrel in mid-May, 2009 from US$ 123.83 per barrel in mid-May 2008. The price of gold, on the other hand, went up by 7.0 percent to US$ 925.25 per ounce in mid-May, 2009 from US$ 865.00 per ounce a year earlier.

55. In comparison to mid-July 2008, the Nepalese currency *vis-à-vis* the US dollar depreciated by 13.46 percent in mid-May 2009. It had depreciated by 3.21 percent in the corresponding period of the previous year. The exchange rate of one US dollar stood at Rs. 79.15 in mid-May 2009 compared to Rs. 68.50 in mid-July 2008.