Current Macroeconomic Situation

(Based on the Four Months' Data of the FY 2010/11)

Monetary Situation

Money Supply

1. Broad money (M2) increased by 0.3 percent during the first four months of FY 2010/11 compared to a growth of 4.5 percent in the corresponding period of the previous year. The growth in monetary aggregates remained subdued during the review period on account of a marginal growth in time deposit mobilized by commercial banks due to the attraction of deposits towards other financial institutions.

2. Net foreign assets (after adjusting foreign exchange valuation gain/loss) declined by Rs. 5.0 billion (2.4 percent) during the review period compared to Rs. 15.8 billion (7.0 percent) in the corresponding period of the previous year. The improvement in merchandise export and workers' remittances together with the compressed growth in import were the factors responsible for the lower deficit in balance of payments (BoP) during the review period relative to that of the corresponding period of the previous year.

Domestic Credit

3. Domestic credit increased by 2.5 percent during the review period. It had expanded by 6.3 percent in the corresponding period of the previous year. During the review period, claims on private sector increased by 4.6 percent compared to a growth of 9.2 percent in the corresponding period of the previous year. The policy measures initiated to curb the excessive credit flow to unproductive sector and deceleration in import growth also contributed to slower growth in the bank credit to the private sector during the review period.

Deposit Mobilization and Credit Flow of Commercial Banks

4. The gap between deposit mobilization and lending by commercial banks continued during the first four months of FY 2010/11. For example, the deposit mobilization of commercial banks declined by Rs. 4.5 billion during the first four months of 2010/11 as against a growth of Rs. 19.0 billion in the corresponding period of the previous year. The decline in deposit mobilization by commercial banks was due to the diversion of deposit to other financial institutions on account of relatively

higher interest rate offered by them. Contrary to the decline in deposit mobilization, the bank credit to private sector increased by 19.9 billion during the review period.

5. The banks' credit to production sector increased by Rs. 9.5 billion during the review period compared to Rs. 3.6 billion in the corresponding period of the previous year. Similarly, banks' credit to wholesale and retail trade, construction and mining sectors increased by Rs. 4.9 billion, Rs. 758.0 million and Rs. 367.0 million respectively during the review period. On the contrary, credit to transportation, communication and public services declined by Rs. 1.6 billion.

Liquidity Management

6. The NRB mopped up net liquidity of Rs. 16.0 billion through secondary market operation during the review period. Liquidity of Rs. 2.0 billion was mopped up through outright sale auction and Rs. 19.0 billion through reverse repo auction during the review period. On the other hand, liquidity of Rs. 5.0 billion was injected through repo auction during the review period. Liquidity of Rs. 8.4 billion was mopped up through outright sale auction and reverse repo auction while Rs. 3.0 billion was injected through repo auction in the corresponding period of the previous year.

7. The NRB injected net liquidity of Rs. 55.9 billion through the purchase of the USD 768 million from commercial banks during the review period. A net liquidity of Rs. 26.6 billion was injected through the purchase of the USD 346.0 million from commercial banks in the corresponding period of the previous year.

8. The NRB purchased Indian currency equivalent to Rs. 51.2 billion through the sale of the USD 700 million in the Indian money market during the review period. INR equivalent to Rs. 54.5 billion was purchased through the sale of the USD 710.0 million in the corresponding period of the previous year.

Inter Bank Transaction and Standing Liquidity Facility

9. Inter-bank transaction of commercial banks reached Rs. 120 billion during the first four months of FY 2010/11 compared to Rs. 96.1 billion in the corresponding period of the previous year. Liquidity injection through the standing liquidity facility (SLF) amounted to Rs. 51.8 billion during the review period. Of the total SLF used during the review period, the outstanding amount was Rs. 2.5 billion as at mid November 2010. Liquidity injected through the SLF had amounted to Rs. 17.3 billion in the corresponding period of the previous year. The outstanding amount of SLF was Rs. 1.7 billion as at mid November 2009.

Short-term Interest Rates

10. The short-term interest rates remained higher during the review period relative to those in the corresponding period of the previous year. For example, the weighted monthly average 91-day Treasury bill rate stood at 7.73 percent in mid November

2010 compared to 4.67 percent a year ago. The weighted average inter-bank rate remained at 9.79 percent in mid November 2010 compared to 9.22 percent a year ago.

Securities Market

11. The year on year (y-o-y) NEPSE index declined by 25.0 percent to 424.9 points in mid November 2010. This index had stood at 566.9 in the same period last year. The decline in share prices was on account of the significant increase in the supply of securities.

12. The y-o-y stock market capitalization decreased by 12.8 percent to Rs. 362.0 billion in mid November 2010. The ratio of market capitalization to GDP stood at 27.4 percent in mid November 2010. This ratio was 35.1 percent a year ago. Of the total market capitalization, the share of bank and financial institutions stood at 72.5 percent followed by manufacturing and processing companies (2.3 percent), hotels (1.5 percent), business entities (0.4 percent), hydropower (4.6 percent) and other sectors (18.7 percent).

13. Total paid-up capital of the listed companies stood at Rs. 90.1 billion in mid November 2010, registering an increase of 33.5 percent over the period of one year. This increase was largely due to the additional listing of securities at the NEPSE. As at mid November 2010, additional securities worth Rs. 14.6 billion (ordinary share of Rs. 5.3 billion, bonus share of Rs. 0.7 billion, right share of Rs. 3.6 billion and government securities of Rs. 4.9 billion) were listed at the NEPSE.

14. Total number of companies listed at the NEPSE increased to 186 in mid-November 2010 from 163 last year. Among them, 154 were banks and financial institutions (including insurance companies), followed by production and processing industries (18), hotels (4), business entities (4), hydropower (4) and companies in other groups (2).

Consumer Price Inflation

15. The y-o-y inflation as measured by the consumer price index (2005/06=100) moderated to 8.4 percent in mid November 2010 from 9.1 percent in the same period of the previous year. During the review period, the price index of food and beverage group grew by 13.3 percent and the price index of non-food and services group increased by 4.5 percent. The indices of these groups had increased by 16.6 percent and 3.1 percent respectively in the same period of the previous year.

16. During the review period, of the items under food and beverage group, price indices of spices sub-group increased by a whopping rate of 34.9 percent compared to an increase of 19.0 percent in the same period of the previous year. The price indices of sugar and sweets, which had increased by 50.3 percent in the same period of the previous year, have increased by 28.8 percent during the review

period. Similarly, the price indices of vegetables, cereals grains and their products, and restaurant and hotel increased by 15.9 percent, 15.4 percent and 15.0 percent during the review period compared to their respective increase of 45.4 percent, 7.6 percent and 19.7 percent in the same period of the previous year. During the review period, the price index of milk product, meat and fish and tobacco increased by 14.3 percent, 12.9 percent and 8.1 percent respectively, which had increased by 8.6 percent, 21.3 percent and 11.7 percent respectively in the same period of previous year. The price index of legume varieties declined by 9.8 percent during the review period as against the increase of 28.9 percent during the same period of the previous year.

17. Within the group of non-food and services, the price index of clothing and footwear increased by 10.0 percent. The price index of this group had increased by 8.2 percent in the corresponding period of the previous year. Similarly, the price indices of transport and housing and utilities increased by 7.8 percent and 7.4 percent respectively which had declined by 8.7 percent and 3.6 percent respectively during the same period of previous year. During the review period, the price indices of communication and recreation and culture declined by 9.5 percent and 2.8 percent respectively.

18. Region-wise, the price index increased highest in Kathmandu Valley by 11.5 percent followed by 9.4 percent in Hills and 5.8 percent in Terai during the review period. The respective growth rates were 8.5 percent, 9.4 percent and 9.3 percent in the same period of the previous year.

Wholesale Price Inflation

19. During the review period, the y-o-y wholesale price index increased to 7.4 percent compared to a rise of 16.9 percent in the same period of the previous year. The wholesale price indices of agricultural commodities and domestic manufactured commodities increased by 7.3 percent and 7.8 percent respectively during the review period compared to increase of 34.9 percent and 8.0 percent in the same period of the previous year. The wholesale price index of imported commodities increased by 7.5 percent during the review period, as against the decrease of 5.5 percent in the corresponding period of the previous year.

20. During the review period, within the group of agricultural commodities, the wholesale price index of spices increased by 42.9 percent compared to a rise of 36.6 percent in the same period of the previous year. Likewise, the wholesale price indices of food grains, fruits and vegetables and livestock production, increased by 21.1 percent, 12.2 percent and 18.8 percent respectively compared to an increase of 14.9 percent, 22.4 percent and 33.3 percent in the same period of the previous year. The wholesale price index of cash crops, however, declined by 30.7 percent as

against the increase by a whopping rate of 116.3 percent during the corresponding period of the previous year.

21. Within the group of domestic manufactured commodities, the wholesale price index of food related products increased by 8.7 percent compared to a rise of 8.9 percent in the same period of the previous year. Similarly, the index of beverages and tobacco increased by 8.8 percent as compared to a rise of 14.0 percent in the corresponding period of the previous year.

22. During the review period, within the imported commodities group, the wholesale price index of petroleum products and coal increased by 15.9 percent as against the decline of 16.7 percent in the corresponding period of the previous year. During the review period, the price index of electric and electronic goods, chemical fertilizers and chemical goods and transport and machinery rose by 6.4 percent, 3.7 percent and 2.8 percent respectively in contrast to a decrease by 6.2 percent, 7.9 percent and 0.4 percent respectively in the same period last year.

National Salary and Wage Rate

23. The overall y-o-y salary and wage rate index rose by 14.9 percent during the review period compared to an increase of 22.2 percent in the same period of the previous year. In the salary and wage rate indices, the salary index remained unchanged during the review period as against the increase of 32.8 percent in the corresponding period of the previous year. However, during the review period, the overall salary and wage rate index increased mainly due to the increase in wage rate index. During the review period, the wage rate index increased by 20.0 percent compared to an increase of 18.9 percent in the same period of the previous year. The indices of wages of agricultural labourers, industrial labourers and construction labourers increased by 27.3 percent, 7.7 percent and 17.4 percent respectively during the review period. These wage rates had increased by 21.7 percent, 16.5 percent and 11.8 percent respectively in the corresponding period of the previous year.

Fiscal Situation [*]

Budget Deficit / Surplus

24. During the first four months of FY 2010/11, government budget remained at a surplus of Rs. 4.64 billion. A low growth rate in recurrent and capital expenditure relative to growth rate of revenue mobilization accounted for such a government

[*] Based on data reported by 8 offices of NRB, 52 out of total 65 branches of Rastriya Banijya Bank Limited, 26 out of total 42 branches of Nepal Bank Limited, 5 branches of Everest Bank Limited and 1-1 branches each from Nepal Bangladesh Bank Limited and Global Bank limited conducting government transactions.

budget surplus during the review period. In the corresponding period last year, budget surplus had stood at Rs. 3.40 billion.

Government Expenditure

25. During the review period, total government spending increased by 1.8 percent to Rs. 51.54 billion compared to an increase of 36.5 percent in the corresponding period of the previous year. As recurrent expenditure increased by only 0.9 percent and capital expenditure declined by 3.8 percent, the growth rate of total government expenditure during the review period remained lower than the previous year. Delay in the announcement of the annual budget also attributed for the decline in the growth rate of the government expenditures.

Revenue

26. During the review period, revenue mobilization of the Government of Nepal (GoN) grew by 9.8 percent to Rs. 51.25 billion compared to an increase of 41.6 percent to Rs. 46.69 billion in the corresponding period of the previous year. The impact of the delay in announcement of the annual budget coupled with the low growth rate of import growth compared to the same period of the previous year affected the growth rate of revenue mobilization of the government.

27. Of the total revenue mobilization, VAT revenue grew by 32.2 percent to Rs.20.66 billion in mid November 2010. It had increased by 29.9 percent in the corresponding period of the previous year.

28. During the review period, custom revenue rose by 6.5 percent to Rs.10.98 billion compared to an increase of 42.9 percent in the same period of the previous year. The growth rate of custom revenue declined mainly due to delayed announcement of the government budget and low growth rate of import compared to the same period of the previous year.

29. During the review period, excise revenue increased by 16.3 percent to Rs. 8.39 billion compared to an increase of 73.7 percent in the same period of the previous year. The growth rate of excise revenue declined due mainly to the low growth rate of imports of high excise tax yielding vehicles.

30. Income tax revenue increased by 35.8 percent to Rs.6.86 billion during the review period. Such revenue had risen by 37.1 percent in the corresponding period of the previous year.

31. During the review period, non-tax revenue decreased by 60.9 percent to Rs.2.16 billion compared to an increase of 62.8 percent in the same period of the previous year. Such a decline in non-tax revenue was due mainly to decrease in revenue received by the government from repayment of principal, forest sector and passport fees.

Foreign Cash Loans and Grants

32. During the four months of the FY 2010/11, foreign cash loans of Rs. 1.30 billion and foreign cash grants of Rs. 5.54 billion were received by the GoN. The GoN had received foreign cash loans of Rs. 1.11 billion and foreign cash grants of Rs. 4.86 billion in the corresponding period of the previous year.

External Sector Situation

Foreign Trade

33. Merchandise exports increased by 8.3 percent to Rs. 21.64 billion during the four months of the FY 2010/11. Such exports had declined by 22.9 percent to Rs. 19.97 billion in the same period last year. On a monthly basis, exports declined by 23.1 percent in October/November of the current fiscal year compared to the value of the previous month.

34. Exports to India increased by 10.7 percent during the four months of the FY 2010/11 in contrast to a drop of 18.9 percent in the same period last year. Likewise, exports to other countries increased by 4.6 percent in contrast to a plunge of 28.5 percent in the same period last year. The increase in the exports to India was mainly ascribed to the increase in the exports of M.S. pipe, thread, jute goods, plastic utensils, wire, textiles, zinc sheet, ayurvedic medicine, and juice among others. Likewise, exports to other countries increased due mainly to the rise in the export of woolen carpet, readymade garments, tanned skin and leather products among others.

35. Merchandise imports, on the other hand, grew by 2.0 percent to Rs. 121.35 billion during the four months of the FY 2010/11. Such imports had grown by 27.3 percent to Rs. 118.95 billion in the same period last year. On a monthly basis, the merchandise imports declined by 11.1 percent in October/November 2010 compared to the value of the previous month.

36. Imports from India grew by 27.7 percent during the review period compared to a growth of 30.3 percent in the same period last year. Likewise, imports from other countries declined by 28.4 percent in contrast to a growth of 23.8 percent in the same period last year. The import of petroleum product, M.S. billet, chemical fertilizers, hot rolled sheet in coil, vehicles and spare parts, other machinery and parts, medicine, electrical goods and vegetables among others increased from India whereas import of gold, betelnuts, polythene granules, still rod and sheet, crude soybean oil, thread and electrical goods declined from other countries in the review period.

37. Total trade deficit during the four months of FY 2010/11 increased marginally by 0.7 percent to Rs. 99.71 billion. Trade deficit had risen by 46.5 percent in the same period last year. Trade deficit with India rose by 31.7 percent during the review

period compared to a growth of 51.7 percent in the same period last year. On the contrary, trade deficit with other countries declined by 33.9 percent compared to a growth of 41.1 percent in the same period a year ago.

38. The improvement in exports coupled with deceleration in import growth contributed to an increase in the ratio of export to import to 17.8 percent in the review period from the ratio of 16.8 percent a year ago.

Balance of Payments

39. The overall BOP recorded a deficit of Rs. 5.03 billion during the four months of FY 2010/11 compared to a deficit of Rs. 15.78 billion in the same period last year. The current account also registered a deficit of Rs. 1.92 billion compared to a deficit of Rs. 14.78 billion in the same period last year. Deceleration in the growth rate of trade deficit and an improvement in the growth rate of transfer income particularly grants and remittances led to such a decline in the current account deficit.

40. The FOB-based merchandise trade deficit grew marginally by 0.4 percent to Rs. 96.55 billion during the first four months of FY 2010/11. Such deficit had grown by 48.9 percent in the same period last year. The service account deficit declined significantly by 38.9 percent to Rs. 3.59 billion during the review period. Service account deficit had declined by 6.0 percent to Rs. 5.87 billion in the same period last year. The net transfer account registered a growth of 13.8 percent to Rs. 95.55 billion in the review period compared to that of a year ago. Under the transfers sub-group, grants increased by 19.9 percent to Rs. 8.52 billion while pension receipts rose by 4.8 percent to Rs. 10.88 billion. Likewise, the workers' remittances increased by 13.6 percent to Rs. 76.88 billion compared to its growth of 6.6 percent in the same period last year. On a monthly basis, the remittance inflows declined by 16.3 percent in October/November compared to the value of the pervious month of this fiscal year. Likewise, under the financial account foreign direct investment of Rs 3.42 billion recorded in the review period compared to the level of Rs 744 million in the same period a year ago.

Foreign Exchange Reserves

41. The gross foreign exchange reserves declined by 2.8 percent to Rs. 261.45 billion in mid November 2010 from a level of Rs. 268.91 billion as at mid July 2010. Such reserves had decreased by 10.3 percent to Rs. 257.07 billion in the same period last year. Analyzing monthly basis, foreign exchange reserve of Rs 4.38 billion increased in the month of October/November from the level of the previous month of this year. Out of total reserve, NRB's reserves declined marginally by 0.4 percent to Rs. 204.55 billion in the review period from a level of Rs. 205.37 billion as at mid-July 2010. The gross foreign exchange reserves in US dollar terms increased marginally by 0.5 percent to USD 3.63 billion in mid November 2010 from a level of USD 3.63 billion as at mid-July 2010. Such reserves had decreased by 9.1

percent in the same period last year. Based on the trend of import during the four months of the current fiscal year, the current level of reserves is sufficient for financing merchandise imports of 8.8 months and merchandise and service imports of 7.5 months.

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

42. The price of oil (Crude Oil Brent) in the international market went up by 14.5 percent to USD 86.11 per barrel in mid November 2010 from USD 75.22 per barrel in mid November 2009. Similarly, the price of gold also surged by 24.0 percent to USD 1368.5 per ounce in mid November 2010 from the level a year ago.

43. Nepalese currency vis-à-vis the US dollar appreciated by 3.39 percent in mid November 2010 from the level of mid July 2010. It had appreciated by 5.47 percent in the corresponding period of the previous year. The exchange rate of one US dollar stood at Rs. 72.00 in mid November 2010 compared to Rs. 74.44 in mid July 2010.