Nepal Rastra Bank

Research Department

Current Macroeconomic and Financial Situation of Nepal

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

Economic Outlook

1. The continued strikes in the Terai Region and unofficial blockade on trade routes in the southern parts of the country have impeded the whole supply system which, in turn, has seriously affected the overall economic activities in the country. In this context, while issuing the white paper the Government of Nepal (GoN) has revised the economic growth projection downward to 2 percent for 2015/16 from the initial target of 6 percent as stated in the Budget Speech.

2. The Ministry of Agriculture and Cooperatives has recently released estimates of paddy and millet production slated to decline by 10 percent and 2 percent respectively in the current fiscal year. However, the Ministry of Agriculture and Cooperatives has estimated maize production to grow by 4 percent during the review period. Winter crop especially wheat production is also slated to be adversely affected due to the obstruction in the supply of chemical fertilizer. In this situation, the Ministry of Finance, has downgraded the growth of agricultural output to 1 percent in the current fiscal year on account of delayed monsoon and the obstruction in supply system.

Box 1: Public-Private Partnership Policy, 2015

The GoN has recently issued the much awaited PPP policy aimed at encouraging an active participation of the private sector in the developmental works. The main goals and objectives of the policy are as follows:

Goals: To promote investment through public private partnership in the development and operation of public infrastructures for the overall social and economic development of the country.

Objectives: **(a)** To use professionalism, efficiency, entrepreneurship and skills of the private sector for providing qualitative public infrastructure services. **(b)** To initiate private-investment friendly environment in order to fulfill the capital and resources requirements through private sector for the development, reconstruction and operation of public infrastructure services.

Policies: **(a)** To apply internationally adopted norms and principles of public private partnership in the overall potential sectors, mechanism, bodies and organizations of the nation. **(b)** To create favorable environment for the private sector in order to make necessary and additional investment for the development of infrastructures. **(c)** To utilize the professionalism, entrepreneurship, skills, ability, capacity and innovation of the private sector in order to develop the infrastructure for the overall development of the country.

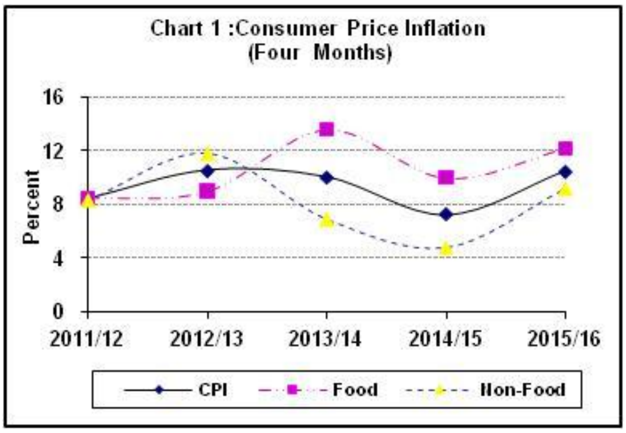
Source: Public-Private Partnership Policy 2015. Ministry of Finance.

3. Most of the industries in the Terai region remained almost closed during the review period due to the obstruction in the supply of necessary fuel and raw materials. Besides, a few operating industries have also been running in a very far below capacity. Likewise, the developmental works under government and private sectors have remained stalled. In this context, the growth rate of industrial sector is expected to be negative in the current fiscal year.

4. The tourism sector that remained almost inactive after the earthquake has further been affected due to the continuous strikes in the Terai region and the obstruction in highways. In the review period, occupancy rate in the hotels have been very low due to scanty tourist arrivals and their short stay. The road and air traffics have been affected due to the severe shortage of fuel. The schools and colleges in the Terai region remained near closed in the review period. These developments are likely to act headwinds to the growth in the service sector.

Inflation, Salary and Wage Rate

5. The y-o-y consumer price inflation rose 10.4 percent in mid-November 2015 compared to 7.2 percent in the corresponding period of the previous year. While food and beverage group inflation was 12.1 percent, non-food and services group inflation was 9.2 percent in mid-November 2015.



6. The proximate determinants of the surge in overall inflation have been the prices of pulses and legumes, ghee and oil and clothes and footwear groups. Of these groups, while prices of pulses and legumes shot up to 44.1 percent, prices of ghee surged to 41.1 percent. Prices of clothes and footwear also went up to 14.6 percent.

7. The underlying factors of the surge in overall inflation have invariably been the prolonged strikes in the Terai region, the unofficial blockades on trade routes in southern part of the country and ensuing hoarding of essential items. If the prevailing atmosphere procrastinates further, rise in prices of essential items is likely to get entrenched, leading to a situation of cost push inflation and stagflation. Although Nepal Rastra Bank has been managing liquidity with high priority, controlling inflation only through monetary management seems difficult until the supply system turns to normalcy.

8. In terms of ecological regions, the price index in the Kathmandu Valley increased by 11.8 percent followed by 11.4 percent in Hilly region, 9.6 percent in Mountain region and 9.1 percent in Terai region during the review period. Such indices had increased by 7.1 percent in the Kathmandu Valley and 7.2 percent in both Hilly region and Terai region in the corresponding period of the previous year.

Consumer Price Inflation: Deviation between Nepal and India

9. The y-o-y CPI inflation of Nepal saw a surge of 10.4 percent compared to 5.4 percent in India showing an inflation wedge of 5 percent during the review period. A year ago, inflation in Nepal was 7.2 percent compared to 4.4 percent in India reflecting a narrower

inflation wedge of 2.8 percent. The rise in inflation wedge between Nepal and India was on account of lingering impact of April/May 2015 earthquakes, strikes in Terai and the recent unofficial blockade on trade routes in the southern parts of the country.

Wholesale Price Inflation

10. The y-o-y wholesale price index increased by 7.1 percent during the review period compared to a rise of 6.7 percent in the corresponding period of the previous year. The wholesale price indices of agricultural commodities and domestic manufactured commodities increased by 11.9 percent and 7.2 percent respectively, whereas such index of imported commodities decreased by 3.4 percent in the review period. The increments in agricultural commodities, domestic manufactured commodities and imported commodities were 8.7 percent, 6.2 percent and 3 percent respectively in the corresponding period of the previous year.

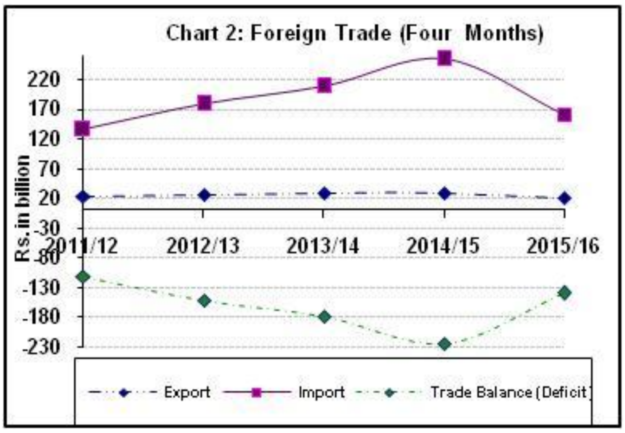
National Salary and Wage Rate

11. The y-o-y salary and wage rate index increased by 8.1 percent during the review period compared to an increase of 9.4 percent in the corresponding period of the previous year. Within the salary and wage rate index, while the salary index increased by 0.8 percent, the wage rate index rose by 10 percent. The salary indices of bank and financial institutions, education and public corporations sub-groups increased by 2.3 percent, 1.5 percent and 0.7 percent respectively during the review period. Likewise, wage rate indices of agricultural labourer, construction labourer and industrial labourer witnessed a growth of 13.2 percent, 9.8 percent and 3.6 percent respectively in the review period.

External Sector

Foreign Trade

12. Merchandise exports decreased significantly by 29.1 percent to Rs. 20.96 billion in the first four months of 2015/16 compared to a drop of 0.2 percent to Rs. 29.55 billion in the same period of the previous year. The total exports decreased due to a fall in exports to India, China and other countries on account of obstructions at the customs points.



13. Exports to India, China and other countries decreased by 38.7 percent, 67.9 percent and 7.8 percent respectively during the review period. The export of mainly zinc sheet, textiles, juice, GI Pipe to India, tanned skin, noodles, and readymade garments to China and pulses, tanned skin, tea, and handicrafts to other countries decreased in the review period.

14. During the review period, merchandise imports shrinked significantly by 36.8 percent to Rs. 160.99 billion. Such imports had gone up by 22.4 percent to Rs. 254.66 billion in the same period of the previous year. The decrease in imports is attributed mainly to a

decrease in imports of goods including petroleum products on account of strike in Terai region and unofficial blockade in the southern parts of the country.

15. Imports from India, China and other countries fell by 41.8 percent, 22.3 percent and 31.1 percent respectively in the review period. The import of mainly petroleum product, vehicles and spare parts, M.S. billet, machinery and parts from India, machinery and parts, television, steel rod and electrical equipments from China and silver, crude soybean oil, edible oil, and crude palm oil from other countries declined in the review period.

16. Total trade deficit during the review period contracted by 37.8 percent to Rs. 140.04 billion compared to an expansion of 26.1 percent in the same period of the previous year. Trade deficit with India, China and other countries narrowed down by 42.1 percent, 20.6 percent, and 36 percent respectively in the review period. The FOB based trade deficit decreased by 37.8 percent to Rs. 135.75 billion in the review period. In the corresponding period of the previous year, such deficit had increased by 27.6 percent.

17. The exports-imports ratio reached 13 percent in the review period on account of a fall in imports. Such ratio was 11.6 percent in the same period of the previous year.

Customs-wise Trade Situation

18. In the four months of 2015/16, the exports through Birgunj customs point dipped to Rs. 2.53 billion from Rs. 5.51 billion in the same period of the previous year and the export through Biratnagar customs point declined to Rs. 6.36 billion from Rs. 8.32 billion in the same period of the previous year.

19. The imports from customs points except Kailali customs declined in the review period. The imports through Birgunj customs point, Birgunj Dryport customs point and Biratnagar customs point declined to Rs. 43.32 billion, Rs. 14.29 billion and Rs. 24.70 billion respectively in the review period. In the corresponding period of previous year, imports through Birgunj customs point, Birgunj Dryport customs point and Biratnagar customs point stood at Rs. 106.05 billion, Rs. 28.48 billion and Rs. 31.82 billion respectively.

Export-Import Price Index

20. The y-o-y unit value export price index based on customs data increased by 8.7 percent while import price index decreased by 8 percent in the fourth month of 2015/16. Consequently, terms of trade (TOT) index increased by 18.1 percent in the fourth month of 2015/16 compared to an increase of 17.2 percent in the corresponding period of the previous year.

Services

21. The gross services receipts in the review period decreased by 4.7 percent to Rs. 42.26 billion while the total services expenses increased by 4.2 percent to Rs 43.31 billion resulting into net services deficit of Rs. 1.05 billion. In the corresponding period of the previous year, the net services had a surplus of Rs. 2.81 billion. The travel receipts and other services receipts decreased while the government receipts increased in the review period. The devastating earthquake of April 25, 2015 as well as the strike in the Terai region adversely affected the tourism and other service sectors leading to a fall in services income.

Transfer

22. The gross transfer receipt increased by 23.2 percent to Rs. 249.58 billion while such payment increased by 16.6 percent to Rs 835.9 million in the review period. Consequently, net transfer receipt increased by 23.2 percent to Rs. 248.74 billion. Such transfer receipt had declined by 3 percent in the same period of the previous year.

23. Workers' remittances increased by 19.4 percent to Rs. 215.39 billion in the review period compared to an increase of 0.8 percent in the same period of the previous year. In US dollar terms, the remittances increased by 11.6 percent to USD 2.06 billion compared to an increase by 2.7 percent in the same period of the previous year.

24. The number of workers going abroad for foreign employment, however, decreased in the recent months. The number of Nepalese workers seeking foreign employment, based on final approval for foreign employment, decreased by 20.9 percent in the first four months of 2015/16. It had increased by 28.8 percent in the same period of the previous year.

Box 2: 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	-
January	50032	45362	-
February	37285	48941	-
March	48552	44460	-
April	45854	52210	-
May	54173	31375	-
June	54926	37962	-
July	61717	26600	-
Total	**528232**	**512887**	**136576**
Percentage Change	16.5	-2.9	-20.9**

* Based on final approval for foreign employment.
** July/Nov. 2014-July/Nov 2015
Source:- Department of Foreign Employment, GoN

Current Account

25. The current account surplus registered a surplus of Rs. 121 billion during the review period in contrast to a deficit of Rs. 5.86 billion in the same period of the previous year due to decrease in imports and upsurge in remittances and grants. The current account surplus in US dollar terms was USD 1.15 billion in the review period.

Capital and Financial Account

26. The capital transfer amounted to Rs. 4.61 billion and Foreign Direct Investment (FDI) inflow amounted to Rs. 1.12 billion in the review period. In the same period of the previous year, capital transfer and FDI inflow stood at Rs. 1.75 billion and Rs. 934.8 million respectively.

27. Dividend payment to FDI companies, based on approval from Nepal Rastra Bank, amounted to Rs. 1.52 billion in the review period. The dividend payment was Rs. 7.21 billion in 2014/15.

Box 3: Dividend Payment to FDI Companies*

(Rs. in million)

Sectors	2014/15 Annual	2015/16 Jul.- Nov.
Financial Sector	1794.43	0.00
Communication Sector	4.00	1416.2
Hydro Power Sector	2874.48	0.00
Industry Sector	2299.19	103.5
Services Sector	238.61	0.00
Total	**7210.71**	**1519.7**

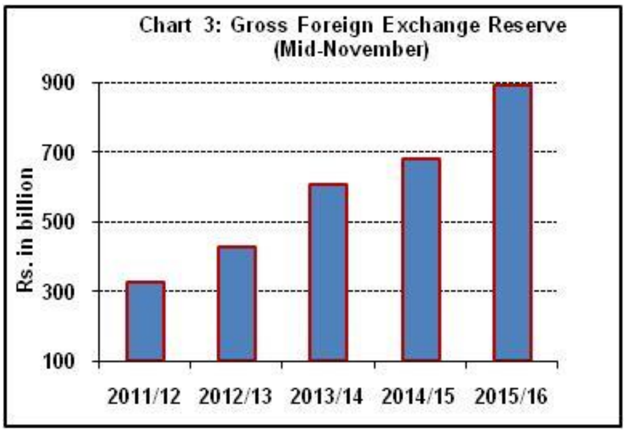
**Based on approval from NRB*

BOP Situation

28. The overall BOP recorded a significant level of surplus of Rs. 83.88 billion in the review period compared to a surplus of Rs. 6.18 billion in the same period of the previous year. In US dollar terms, the BOP recorded a surplus of USD 798.9 million.

Foreign Exchange Reserves

29. The gross foreign exchange reserves increased by 12.5 percent to Rs. 926.79 billion as at mid-November 2015 from Rs. 823.87 billion as of mid-July 2015. Such reserves had increased by 2.4 percent in the same period of the previous year. The gross foreign exchange reserves in US dollar terms increased by 7.9 percent to USD 8.79 billion in mid-November 2015.



30. The foreign exchange reserves held by NRB increased by 14 percent to Rs. 801.12 billion as at mid-November 2015 compared to mid-July 2015. Similarly the reserves of banks and financial institutions (except NRB) increased by 3.9 percent to Rs. 125.67 billion in the same period. The share of NRB in total reserves stood at 86.4 percent. The share of Indian currency reserves in total reserves stood at 21.2 percent.

Foreign Exchange Adequacy Indicators

31. The reserve adequacy indicators remained satisfactory in the review period. Based on the imports of the four months of the current fiscal year, the foreign exchange holding of the banking sector is sufficient to cover prospective merchandise imports of 23.4 months, and merchandise and services imports of 18.4 months. The ratio of reserve-to-GDP, reserve-to-imports and reserve-to-M_2 increased to 43.6 percent, 153 percent and 46.4 percent respectively as at mid-November 2015. Such ratios were 38.8 percent, 93.2 percent and 43.9 percent as at mid-July 2015.

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

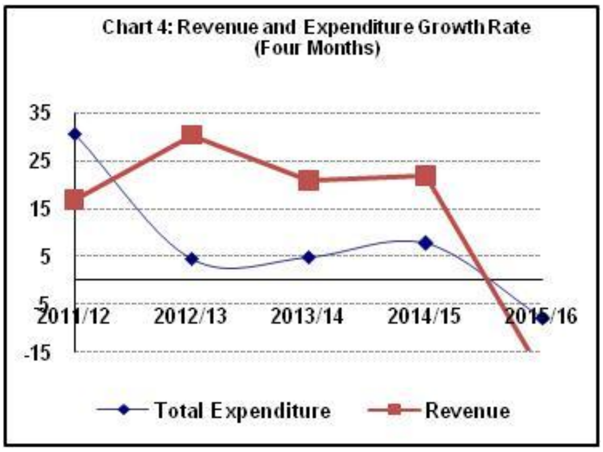
32. The price of oil (Crude Oil Brent) in the international market decreased sharply by 48 percent to USD 40.28 per barrel in mid-November 2015 from USD 77.51 per barrel a year ago. The decrease in the price of petroleum product is attributed to the decrease of demand for petroleum products in emerging and developing economies including China along with no reduction in production by the OPEC and USA. Similarly, the price of gold declined by 7.2 percent to USD 1084.75 per ounce in the mid-November 2015 from USD 1169 per ounce a year ago.

33. Nepalese currency vis-à-vis the US dollar depreciated by 4.1 percent in mid-November 2015 from mid-July 2015. It had depreciated by 2.6 percent in the same period of the previous year. The exchange rate per US dollar stood at Rs. 105.46 in mid-November 2015 compared to Rs. 101.14 in mid-July 2015.

Fiscal Situation *

Budget Deficit / Surplus

34. During the four months of 2015/16, government budget on cash basis remained at a surplus of Rs. 35.10 billion. Despite the slowdown in resource mobilization, a significant fall in government expenditure accounted for a surplus in the budget. Budget surplus was Rs. 44.82 billion in the corresponding period of the previous year.



Government Expenditure

35. During the review period, total government expenditure on cash basis dropped by 7.8 percent to Rs. 73.35 billion in contrast to an increase of 7.8 percent to Rs. 79.56 billion in the corresponding period of the previous year. Such decline in government expenditure in the review period can be attributed to the adverse impact of continuous Terai agitation and the unofficial blockade at customs points in the southern parts of the country.

36. During the review period, recurrent expenditures dropped by 20 percent to Rs. 58.05 billion. Such expenditures had increased by 7 percent in the corresponding period of the previous year. Although capital expenditures increased by 23.1 percent to Rs. 5.74 billion in the review period, the amount accounts for just 2.8 percent of the annual target of Rs. 209 billion. The annual target for capital expenditure, therefore, is less likely to be realised in 2015/16. In the four months of the previous year, capital expenditures had increased by 19 percent.

37. During the review period, disturbances at customs points have obstructed the overall supply system including that of fuel. Works of important projects have halted due to fuel shortage, and post-earthquake reconstruction has not got momentum due to lack of construction materials. Consequently, the capital expenditure of the GoN has not been as expected.

Government Revenue

38. During the review period, the government revenue mobilization dropped by 19.4 percent to Rs. 92.57 billion. Such revenue had risen by 21.8 percent in the corresponding period of the previous year. Contraction in imports and slowdown in economic activities due to disturbances at southern customs points led to decrease in VAT, customs revenue, excise duty as well as non-tax revenue mobilization. The income tax has, however, increased by 14.9 percent in the review period.

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* Based on the data reported by 8 NRB offices, 68 branches of Rastriya Banijya Bank Limited, 43 out of 47 branches of Nepal Bank limited, 19 branches of Agriculture Development Bank limited, 9 branches of Everest Bank Limited, 4 branches of Global IME Bank Limited and, 1/1 branch each of NMB Bank Limited, Nepal Bangladesh Bank limited and Bank of Kathmandu Limited conducting government transactions and released report from 79 DTCOs and payment centers.

Public Debt and Cash Balance of the GoN

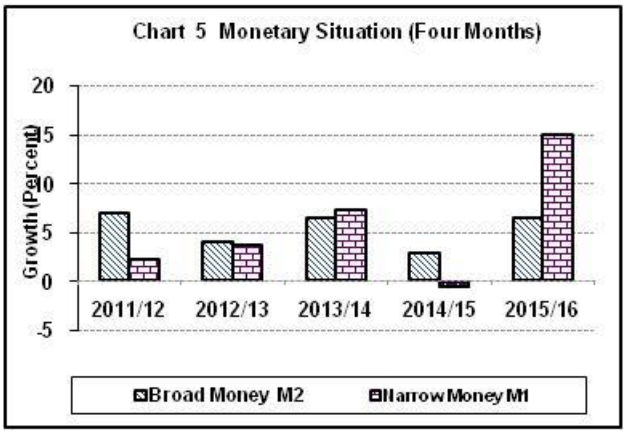
39. During the review period, the GoN made principal payment of Rs. 5.45 billion of domestic debt. As a result outstanding domestic debt decreased to Rs. 191.34 billion in mid-November 2015 from Rs. 196.79 billion in mid-July 2015.

40. Because of a slow pace of government expenditure relative to resource mobilization, the GoN accumulated cash balance of Rs. 80.82 billion at Nepal Rastra Bank as of mid-November 2015.

Monetary Situation

Money Supply

41. Broad money supply (M2) increased by 6.5 percent in the four months of 2015/16 compared to an increase of 2.8 percent in the corresponding period of the previous year. Narrow money supply (M1), which had decreased by 0.5 percent in the same period of the previous year, increased by 14.9 percent in the review period. On y-o-y basis, M2 expanded by 24.2 percent and M1 expanded by 38.2 percent in mid-November 2015.

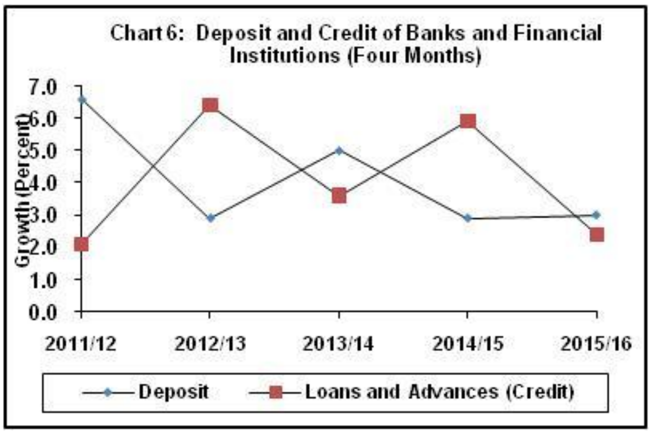


42. Reserve money, which had decreased by 11.3 percent in the corresponding period of the previous year, increased by 4.8 percent in the review period. On y-o-y basis, reserve money increased by 35 percent in mid-November 2015. Such growth of reserve money is attributed to the increase in the net foreign assets of this bank.

43. Net foreign assets (after adjusting foreign exchange valuation gain/loss) increased by Rs. 83.88 billion (11.2 percent) in the review period compared to an increase of Rs. 6.18 billion (1 percent) in the corresponding period of the previous year. Remarkable increase in remittance inflows along with the contraction in imports at a higher rate resulted in a large expansion of net foreign assets in the review period.

Domestic Credit

44. Domestic credit contracted by 0.2 percent in the review period in contrast to an increase of 2.2 percent in the same period of the previous year. On y-o-y basis, domestic credit increased by 12.9 percent in mid-November 2015. A rise in government deposits at this bank and the decelerated growth in monetary sector's claims on private sector resulted in a decline in domestic credit in the review period. Claims of



monetary sector on the private sector increased by 3.3 percent in the review period compared to a growth of 6.4 percent in the corresponding period of the previous year. On y-o-y basis, claims on the private sector increased by 15.9 percent in mid-November 2015 compared to a growth of 19.7 percent a year ago.

Financial Resources Mobilization

45. Albeit deposits at the bank and financial institutions (BFIs) expanded in the review period nearer at a similar rate of the previous year, loans and advances increased at a lower rate.

Deposit Collection

46. Deposits at BFIs increased by 3 percent (Rs. 51.51 billion) in the review period compared to a growth of 2.9 percent (Rs. 40.11 billion) in the corresponding period of the previous year. Deposits at commercial banks and finance companies increased by 3.6 percent and 4 percent respectively in the review period, while that of deposits at development banks decreased by 1.2 percent. On y-o-y basis, deposits at BFIs expanded by 20.3 percent in mid-November 2015.

Credit Disbursement

47. Credit to the private sector from BFIs increased by 2.7 percent (Rs. 36.35 billion) in the review period compared to an increase of 6 percent (Rs. 66.52 billion) in the same period of the previous year. Private sector credit from commercial banks and finance companies increased by 3.6 percent and 4.9 percent respectively in the review period. However, such credit of development banks decreased by 2.8 percent. On y-o-y basis, credit to the private sector from BFIs increased by 16.2 percent in mid-November 2015.

48. There has been a lower growth in credit disbursement in major areas such as industrial production, wholesale and retail trade, construction and agriculture. Credit to the industrial production sector, wholesale and retail trade sector, construction sector and transport, communication and public sector increased by Rs. 1.73 billion (0.7 percent), Rs. 4.19 billion (1.4 percent), Rs. 3.75 billion (2.5 percent) and Rs. 5.61 billion (9.3 percent) respectively in the review period. However, credit to the agriculture sector decreased by Rs. 546 million (0.8 percent) in the review period.

49. In the four months of 2015/16, banks and financial institutions extended 59.7 percent of their total credit against the collateral of land and building, and 12.6 percent against the collateral of current assets (such as agricultural and non-agricultural products). Such ratios were 58.8 percent and 13.6 percent respectively in the same period of the previous year.

50. Of the total lending of commercial banks, the credit to small and medium enterprises is only 2.6 percent (Rs. 29.81 billion) in the review period. Insufficient collateral has been one of the major constraints for SME finance in Nepal. Therefore, to address this problem, it is necessary to establish the secured transaction registry office for the implementation of secured transaction registry.

Liquidity Management

51. In the four months of 2015/16, the NRB mopped up Rs. 242.65 billion liquidity through various instruments. These consist of Rs. 157.25 billion liquidity through deposit collection auctions, Rs. 76.30 billion through reverse repo auction and Rs. 9.10 billion

through outright sale auction on a cumulative basis. The outstanding deposit collection auction amounted to Rs. 100 billion in mid-November 2015. In the corresponding period of the previous year, Rs. 40 billion was mopped up through deposit collection auction and Rs. 198 billion through reverse repo auction. In the four months of 2015/16, total interest expenses incurred in mopping up liquidity through various instruments reached Rs. 447.3 million.

Box 4: The Cost of Liquidity Absorption (Rs. in million)

Liquidity Absorption Instruments	2014/15 (Annual)		2015/16 (Four Months)	
	Amount	Interest Expenses	Amount	Interest Expenses
Deposit Collection Auction	155000	170.5	157250	412.2
Reverse Repo Auction	315800	2.8	76300	6.1
Outright Sale Auction	6000	17.3	9100	29.0
Total	**476800**	**190.6**	**242650**	**447.3**

52. In the review period, the NRB injected net liquidity of Rs. 154.28 billion through the net purchase of USD 1.48 billion from foreign exchange market (commercial banks). Net liquidity of Rs. 100.98 billion was injected through the net purchase of USD 1.10 billion in the corresponding period of the previous year.

53. The NRB purchased Indian currency (INR) equivalent to Rs. 79.19 billion through the sale of USD 760 million in the review period. INR equivalent to Rs. 115.13 billion was purchased through the sale of USD 1.18 billion in the corresponding period of the previous year.

Financial Broadening

54. Expansion in branch network of BFIs has widened the access to finance. The branch network of BFIs reached 3,968 in mid-October 2015 from 3,617 a year ago. Likewise, the growth in the deposit and loan accounts has also contributed to broaden the financial access (Box 5).

Box 5: Financial Broadening Indicators

Headings	Mid-October 2014	Mid-October 2015
Number of BFIs	197	194
Branches of BFIs	3617	3968
Number of ATM/Debit Card	41,45,405	42,86,455
Number of Credit Card	59,352	45,554
Number of Deposit Accounts	1,44,16,701	1,52,79,909
Number of Loan Accounts	9,49,777	10,27,089

Refinance and Productive Sector Lending

55. The NRB has been providing refinance facility to expand productive sector lending. Utilization of such facility has slightly decreased in the review period. In the review period, a total refinance of about Rs. 1.53 billion including general refinance of Rs. 1.39 billion and export refinance of Rs. 0.14 billion has been provided. In the corresponding period of the previous year, a total refinance of Rs. 2.80 billion including general refinance of Rs. 1.68 billion and export refinance of Rs. 1.12 million was utilized.

56. This bank has issued necessary directive to provide refinance facility to banks and financial institutions aimed at promoting the housing loan at 2 percent concessional interest to the earthquake victims. It is expected that the demand for this loan will take

place along with the commencement of the government led rehabilitation and reconstruction work.

57. 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 15.7 percent in mid-November 2015.

Inter-bank Transaction and Standing Liquidity Facility

58. In the review period, inter-bank transactions of commercial banks stood at Rs. 231.50 billion and those of other financial institutions (excluding transactions among commercial banks) amounted to Rs. 23.70 billion. Such transactions had amounted to Rs. 126.74 billion and Rs. 61.33 billion respectively in the corresponding period of the previous year. The BFIs did not use standing liquidity facility (SLF) in the review period.

Interest Rates

59. Weighted average of 91-day Treasury Bill rate and inter-bank transaction rate has decreased in the fourth month of 2015/16 compared to a year ago. The weighted average 91-day Treasury Bill rate decreased to 0.29 percent in the review month from 0.52 percent a year ago. Similarly, the weighted average inter-bank transaction rate among commercial banks that was 0.42 percent a year ago declined to 0.36 percent in the review month. Likewise, the weighted average inter-bank rate among other financial institutions decreased to 1.49 percent from 2.41 percent a year ago.

60. Weighted average interest rate spread between deposit and lending rate of commercial banks inched up to 4.57 percent from 4.49 percent a year ago and the average base rate came down to 7.04 percent from 7.46 percent a year ago.

Status of Merger and Acquisition of Banks and Financial Institutions

61. 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", 83 BFIs have merged with each other resulting in the formation of 31 BFIs as of mid-November 2015. Likewise, 2 finance companies were acquired by a commercial bank and one development bank was acquired by another development bank.

Regulatory Measures

62. In the review period, the NRB has issued directives pertaining to branch acquisition of problematic bank by another 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 approval from the NRB. Further, additional directives relate to including 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, among others. Likewise, the existing provision for submitting the net clearing position of BFIs through electronic channel by Nepal Clearing House Ltd. to Banking Office has been modified in five

specified sessions from the existing ones. Similarly, BFIs are required to make their capital plan, as per the monetary policy provision, public through their own websites.

63. NRB has issued further directives addressing unusual situation caused by unrest in Terai region and trade-transit disturbances in Indo-Nepal Transit points. Such directives include continuation of deferred loans as pass loans until mid-January 2016 and exemption from penalty for such loans, rescheduling or restructuring of loan up to one year for one time within mid-January 2016 if borrowers of service sector (industry, trade, education, health, tourism and energy) submit work-plan, provision for including accrued interest received until mid-November 2015 in income statement of the first quarter and extension of time period of T.R. (Trust Receipt) loans from 120 days to 180 days, among others.

Macro prudential Regulation

64. There is a provision to limit credit in real estate sector at 25 percent of total credit disbursement. Such credit flow of BFIs amounted to Rs. 213.13 billion (including Rs. 123.40 billion residential home loans less than Rs. 10 million each) in mid-November 2015. This is 15.3 percent of total credit exposure of BFIs. As at mid-November 2015, the BFIs' total margin lending extended against the collateral of shares stood at 1.9 percent (Rs. 25.97 billion) of their total credit exposure.

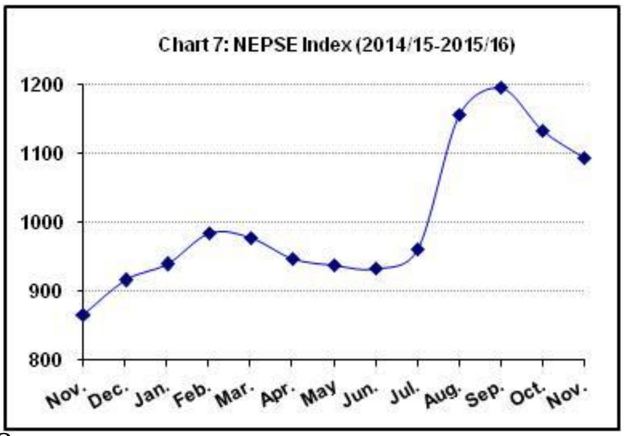
65. Mandatory credit-deposit (local currency deposit and including core capital) ratio is 80 percent. Such ratios of commercial banks, development banks and finance companies stood at 68.86 percent, 70.62 percent and 73.30 percent respectively as at mid-October 2015. This shows that BFIs have additional room for credit disbursement.

66. Commercial banks are required to maintain 10 percent capital fund ratio of the risk weighted assets and development banks and finance companies are required 11 percent each. Such ratios of commercial banks, development banks and finance companies were 11.94 percent, 16.47 percent and 21.49 percent respectively as at mid-October 2015. BFIs are required to maintain capital buffer of 1 percent or more in addition to capital adequacy ratio (CAR) before they distribute dividend.

67. While there is no limit for commercial banks in deposit collection, development banks and finance companies can collect financial resources up to 20 times and 15 times of their core capital respectively. Accordingly, development banks' and finance companies' resources collection stood at 6.4 times and 5 times of their core capital respectively as at mid-November 2015.

Capital Market

68. The NEPSE index on y-o-y basis increased by 26.3 percent to 1,094.2 points in mid-November 2015. This index had increased by 44.3 percent to 866.2 points a year ago. The index, which soared during the first two months of 2015/16 with the expectation of the end of political transition and the capital-hike provision of monetary



policy, has been declining continuously since mid-September 2015 due to the ongoing strike in Terai region and disruptions at Indo-Nepal transit points.

69. The twelve months' rolling standard deviation of NEPSE index increased by 4.2 percent in mid-November 2015. On the basis of daily (sector-wise) transactions from mid-October to mid-November 2015, the hydropower sector's index shows the highest volatility followed by the insurance sector.

70. The stock market capitalization on y-o-y basis increased by 30.1 percent to Rs. 1156.13 billion in mid-November 2015. This had increased by 45.8 percent a year ago. The ratio of market capitalization stood at 54.4 percent in mid-November 2015 compared to 45.8 percent a year ago. In the total market capitalization, the share of banks and financial institutions (including insurance companies) stood at 81.2 percent, hydropower 5.3 percent, manufacturing and processing companies 2.9 percent, hotels 2.1 percent, trading 0.1 percent, and others 8.4 percent respectively.

71. On y-o-y basis, the total turnover of the securities decreased by 66.9 percent to Rs. 3.29 billion in mid-November 2015. The turnover of the securities had increased to Rs. 9.95 billion a year ago. In the total turnover, the share of commercial bank was 52.8 percent, development bank was 13.1 percent, promoter share was 11.7 percent, insurance companies was 11.4 percent, hydropower sector was 5.5 percent, insurance companies was 3.6 percent, hotel and other sectors were 0.6 percent each, mutual fund was 0.4 percent and manufacturing and processing industries was 0.3 percent.

72. Total number of companies listed at the NEPSE decreased from 235 in mid-November 2014 to 225 in mid-November 2015 due to the merger of some BFIs.

73. On y-o-y basis, total paid-up capital of the listed companies increased by 31.1 percent to Rs. 232.73 billion in mid-November 2015. In the fourth month of 2015/16, total securities worth Rs.6.47 billion were listed in the NEPSE. These consist of ordinary shares Rs. 1.63 billion, right shares Rs. 1.22 billion, bonus shares Rs. 2.52 billion and the debentures Rs. 1.10 billion.

Contractual Saving and Investment

74. On y-o-y basis, the total fund collected by Citizen Investment Trust increased by 28.7 percent to Rs. 69.78 billion in mid-October 2015. In the review period, the investment made by the Trust increased by 34.6 percent to Rs. 41.21 billion while loan disbursement decreased by 33.9 percent to Rs. 11.5 billion.

75. On y-o-y basis, the Provident Fund amount at Employees Provident Fund increased by 14.7 percent to Rs. 194.73 billion in mid-October 2015. In the review period, the investment and loan made by the Fund increased by 33.2 percent and 9 percent to Rs. 58.11 billion and Rs. 136.81 billion respectively.