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Monetary Policy focuses on Access to Finance

Governor Dr. Yuba Raj Khatiwada announced the monetary policy for the fiscal year 2010/11 amidst the economists, bankers, business persons, media persons and senior officers of NRB in the conference hall of central office Baluwatar on July 28, 2010.

The new and foremost policy, incorporated in the announcement was a provision regarding the commercial banks (CBs). As the proactive measure, CBs cannot open any interest earning account with other CBs and financial institutions within the country. Governor Dr. Khatiwada said, "This new system has been introduced in Nepal so as to discourage the activities like creating artificial measurement mechanism of liquidity by the CBs, which in turn weakens the principle of financial intermediary role of the CBs."

Monetary Policy (MP) of 2010 has mostly focused on increasing access to finance in those part of the country with limited presence of bank and financial institutions. MP has adopted expansionary policy in case of new bank licensing and branch extension.

Although licensing to A class FIs (commercial bank) is withheld, opening new other class FIs in the listed thirty two districts, where number of FIs is very few is prioritized. Those thirty two districts of remote areas of the country have almost low spread of branches of FIs.

Among them 16 districts have only one bank branch and 5 districts have 2 in each. In sighting above mentioned geographical existence of financial services to the remote part of the country, NRB has introduced special provision to open FIs in the listed 32 districts.

With a view to expand banking services in areas with limited access to financial services, the existing provision of additional paid up capital of Rs. 20 million to open a branch in Kathmandu Valley and Rs. 5 million to open a branch outside Kathmandu valley respectively will be waived for class 'C' financial institutions extending branches in municipalities or village development committees having two or less banks and financial institutions or their branches. With a view to enhance financial inclusion through expansion of financial services in lacking areas, the NRB shall provide an interest free loan upto Rs. 5 million and Rs. 10 million respectively to those banks and financial institutions opening branch in district head quarter and outside of district head quarter of 22 remote district,.

Governor Dr. Khatiwada clarified the queries of media persons on the newly incorporated policy measures adopted by the Monetary Policy. They made arguments on some rates and target made last year were not achieved. The BOP is in deficit and same unachievable targets have been repeated. Governor refused that it would not repeat this

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> "NRB will try to avoid the possibility of reverse flow of financial resources collected in rural areas to urban areas."

Door Open to Infrastructure Development Banks

Nepal Rastra Bank has continued its moratorium policy on licensing to new commercial banks, stated in the monetary policy announced on July 28, 2010. It has withheld to accept application to open new commercial banks as before until the next decision comes.

But it has eased and opened the door to such banks whose objective is to work on infrastructure development sector. That should come with the huge amount of foreign capital in joint venture. It has mentioned that a detail circular will come soon addressing paid up capital, business involvement and experience of promoters, corporate good governance, fit and proper test, share limit to promoters and access to the finance to the general public. ■

Congratulation received on the appointment of the new Governor

Managing Director from IMF, Dominique Strauss Kahn, Vice President, World Bank South Asia Group, Isabel M. Guerrero, Resident and Humanitarian Co-coordinator of United Nations Nepal Office, Robert Piper, and Governors from various central banks congratulated Dr. Yuba Raj Khatiwada on his appointment as a Governor of Nepal Rastra Bank (NRB). They expressed in their letter that NRB has got very efficient economist to head the organization.

Dr. Khatiwada was appointed as the 15th Governor of NRB on March 19, 2010. He is the successor of Mr. Bijaya Nath Bhattarai and his tenure is for 5 years. He received his Doctorate Degree in Monetary Economics from the Delhi School of Economics, India. Apart from this, he has got immense practical knowledge as served in the central bank for 26 years. During his service in the NRB, Government of Nepal has called him in the Ministry of Finance as Economic Advisor. Latter, he was deputed to the National Planning Commission (NPC) as a member.

In 2008, he moved to the UNDP and worked there for Social Policy and Decentralization. In 2009, he was appointed as the Vice-Chairman of NPC after the retirement from NRB. He came back to NRB as the Governor leaving the post of Vice-Chairman of NPC.

Governor Dr. Khatiwada receiving welcome garlands

He expressed that his efforts would be directed towards achieving monetary stability by maintaining financial discipline and good governance, increasing financial access to those who have been deprived from such services and initiating groundwork to define the role of the central bank in federal state structure in the ceremony when he was officiated on March 21, 2010.

In response to a question raised by the media persons on the optimal size of banking industry in the small economy like Nepal, Dr. Khatiwada noted, "number of commercial bank is not the prime factor but banking facility availability is the major". Currently, NRB has withheld issuing the license of opening new banks. ■

Continued from page 1....

... Monetary Policy

year as data show the improving and satisfactory trend. Adding on this, Board member of NRB Prof. Parthibeshwor Prasad Timilsina noted that the targeted and forecasted rate should be little higher in the developing countries like ours, so as to ensure the optimistic ideas.

Mr. Krishna Hari Baskota, Revenue Secretary from Ministry of Finance also joined the question-answer session. He clarified the confusion raised by the media persons as how and why MP came before fiscal policy. Now government could not bring the full fledge budget for the fiscal year which starts in mid July every year. Mr. Baskota told that country is not running out of budget and fiscal policy. The difference is that last year's fiscal policy is acting and economy is not in the vacuum, he added.

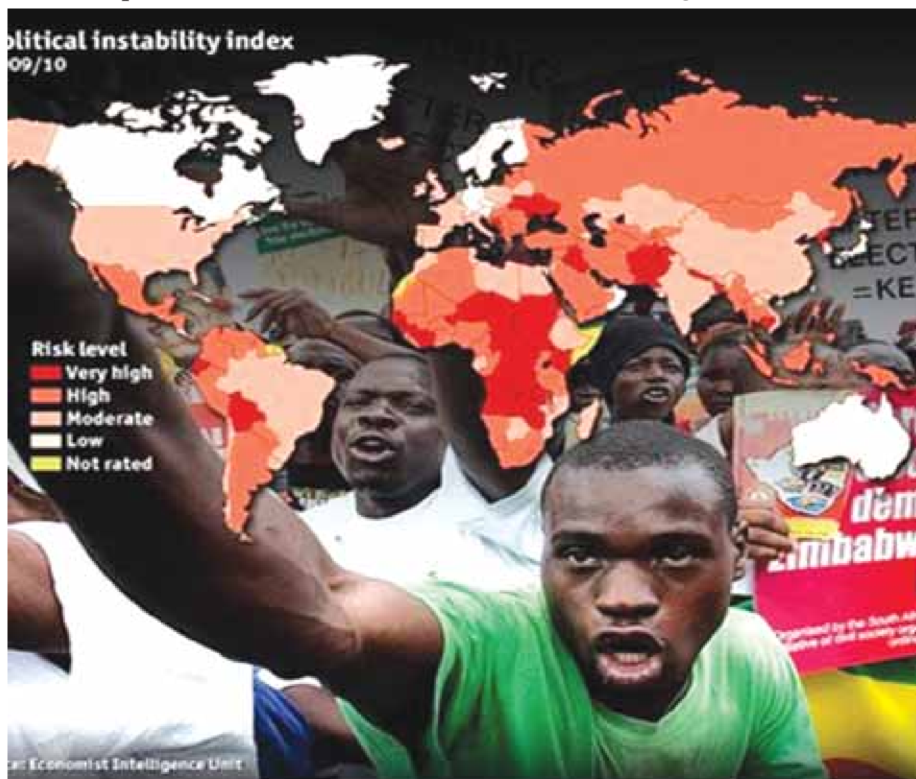
Program was started with welcome remarks of Deputy Governor Mr. Bi Bikram Rayamajhi. The policy has set the new mechanism to count statutory liquidity ratio. ■

Key Rates

As per Monetary Policy for 2010-11 of NRB	
1. CRR	= 5.5%
2. SLR	= 15.0% for CBs
3. BR	= 7.0%
As on July 27, 2010	
4. TBR (weighted average)	= 3.5809%
5. Inter Bank Rate	= 1.0%
6. Treasury Position as on July 30 (estimated)	= NRs. -15925.9 million

Political Instability Index

The threat posed to governments by social protest has increased in most countries since long time back. The Economist Intelligence Unit of the Economist magazine, London surveyed a total of 165 countries for its Political Instability Index. Out of which most of the Asian and some African countries poses a vulnerable situation. Some how Pakistan had come out of this but Nepal is suffering since long time. Talking about Nepal, we see very good example of stability in north and south, which has proven good base for comfortable economic development. We have alot natural resources and market as well around our country ring but alot remaining to do.



Analysing the research output and observing the given chart mapping (refer diagram) Nepal comes in the very high rating of risk level. In such situation how long only NRB (central bank of Nepal) can maintain macroeconomic stability in the country as country could not come up from political transitition phase in the given time. If the rating is worst to Nepal then that may hamper in various dimentions for the developing country like Nepal. As we are in the growing age of development and asking for foreign loan and grants and searching foreign investment, we should not be late in establizing new political arena . Every one understands the severity of political transforamation but being late on establising new system might pull the country in downward spiral and economic distress and underlying vulnerability to political unrest.

Impact of the political instability on monetary authority frontier of Nepal, It has severe influence in achieving monetary policy objectives. Due to instable political situation, investment in productive sector supressed which leads to low level of production, caused heavy import of consumable goods as well as decrease in export, resulted BOP deficit in FY 2009/10. Similarly, it affected the inflation, merely monetary instruments are not sufficient to control the inflation in Nepal. ■

Theory on twin deficit

KNOW-ABOUT

The twin deficits hypothesis, also called the double deficit hypothesis, it is a concept from that contends that there is a strong link between a national economy's and its government budget balance.

One way to understand this process intuitively is by thinking through two different markets. First consider the Foreign Exchange market. At equilibrium the quantity supplied=the quantity demanded. Thus, Imports + Capital outflow=Exports + Capital Inflow. Rearranging this equation we find that Imports-Exports=Capital Inflow-Capital Outflow. Because Imports-Exports=Trade Deficit and Capital Inflow-Capital Outflow=Net Capital Inflow, we get the equation Trade Deficit=Net Capital Inflow (or Current Account deficit = Capital Account Surplus).

Next we must consider the market for loanable funds. The equilibrium here is Savings+Net Capital Inflow=Investment+Budget Deficit. However, taking the Forex market into consideration we know that the Trade Deficit is equal to Net Capital Inflow. We can thus substitute for:

Savings + TradeDeficit = Investment + BudgetDeficit.

Rearranging algebraically we find that:

BudgetDeficit = NetSavings + TradeDeficit - Investment.

The theory goes as like: Y = C + I + G + NX, where Y represents National Income or GDP, C is consumption, I is investment, G is government spending and NX stands for net exports. This represents GDP because all the production in an economy is used as consumption (C), investment (I), or government spending (G), and the leftover production is exported (NX). Another equation defining GDP using alternative terms is Y = C + S + T, where Y is again GDP, S is savings, and T is taxes. This is because national income is also equal to output, and all individual income either goes to pay for consumption (C), to pay taxes (T), or becomes savings (S). Since Y = C + I + G + NX, and Y = C + S + T, then C + I + G + NX = C + S + T, which simplifies to (S - I) + (T - G) = (NX). If (T-G) is negative, a budget deficit. Now, assume an economy already at potential output, meaning Y is fixed. In this case, if the deficit increases, and savings remains the same, then this last equation implies that either investment (I) must fall or net exports (NX) must fall, causing a trade deficit.

Though the economics behind which of the two is used to finance the government deficit can get more complicated than what is shown above, the essence of it is that if foreigners' savings pay for the budget deficit, the current account deficit grows. If the countries own citizens' savings finance the borrowing, it may cause a crowding out effect (in an economy at or near potential output, or full employment).

Source: Ghosh, Atish; Ramakrishnan Uma (December, 2006), Finance and Development vol. 43,(number 4) and Penguin Dictionary of Economics

Mitigating the Recessionary Impact on Nepal's Remittance Inflow

■ **Dr. Bhuwanesh Panta**
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"Remittances" primarily denote transfers, in cash or in kind, from a migrant to household residents in the country of origin. One of the salient features of the ongoing global recession has been its impact on remittances. Prior to the onset of the recession, remittances had proven to be a reliable source of income for households in developing economies, with robust growth regardless of the state of the business cycle. However, according to the World Bank, as the real-sector spillovers from the financial crisis were quite severe, the total quantity of remittances dropped in 2009 for the first time in decades. The World Bank estimated that remittance flows to developing countries dropped from US$ 336 billion in 2008 to US$ 316 billion in 2009, a decline by 6 percent. Because of improved prospects for the global economy, however, remittance flows to developing countries are expected to rise by 6.2 percent in 2010 and 7.1 percent in 2011.

Remittances, until recently, had been providing an important safety net for the economy both in terms of bringing stability to the external sector and helping to stabilize consumption levels of a significant number of households. At the household level, remittances had helped to reduce poverty and improve standard of living. Moreover, these inflows had been instrumental in maintaining the current account surplus despite a widening trade deficit. However, the deleterious impact of the global economic meltdown on Nepal's remittances has been evident in recent months.

In 2008/09, workers' remittances stood at Rs. 209.70 billion, a rise by 47.0 percent compared to 2007/08. Similarly, the remittances to GDP ratio went up from 17.4 percent in 2007/08 to 21.8 percent in 2008/09. As a matter of fact, Nepal was one of the top ten recipients in terms of share of remittances in GDP in 2008/09. These figures clearly divulge that any significant drop in receipts from remittances could disturb the structure of the economy from the macro level. And this is exactly what the data has been exhibiting since the beginning of 2009/10, thanks to the lagged impact of the global recession.

Consequently, in the first eleven months of 2009/10, remittances increased by just 11.8 percent to Rs. 211.17 billion compared to its significant growth of 51.0 percent in the corresponding period of the previous year. While both in 2007/08 and 2008/09 the upsurge in remittances was responsible for the huge surplus in the current account and the balance of payments (BoP), in the first eleven

"A separate ministry along the lines of those in other South Asian countries (such as the Ministry of Expatriate Welfare and Overseas Employment in Bangladesh, the Ministry of Overseas Indian Affairs in India, the Ministry of Overseas Pakistanis in Pakistan and the Foreign Employment Ministry in Sri Lanka) needs to be created and given the responsibility of dealing with all matters pertaining to the international migration affairs of Nepalis."

months of 2009/10 the dramatic slowdown in remittance inflows has led to a current account deficit of Rs. 34.59 billion, thereby weakening the overall BoP which also posted a deficit of Rs. 15.07 billion. Likewise, the gross foreign exchange reserves are sufficient for financing merchandize imports of only 8.1 months and merchandize and service imports of 6.8 months in mid-June 2010 compared to 12.0 months and 9.8 months respectively in mid-July 2009.

To withstand the adverse repercussions of the global recession, the country should push ahead with effective economic diplomacy and relationship management through its foreign missions so as to minimize the adverse effects of job losses. The government's policy to provide a labor attaché to a country with more than 5,000 Nepali workers needs to be broadened to include more countries.

In the present context, it is crucial to make an assessment of the impact of the worldwide financial meltdown on the economic situation in those destination countries where there are a large number of Nepali migrant workers. This would assist in forming the basis for estimating job losses for Nepali migrants and the number of returnees. Moreover, human capital should be developed in accordance with the demands of the international labor market.

for returnees must be accorded top priority. The government should welcome the returnees who will come back with skills, entrepreneurship and capital. Policies to re-integrate the returnees can include improving self-employment opportunities, support for small and medium-enterprises, and budget support to districts facing large returns.

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To conclude, remittances from workers abroad are a financial lifeline for Nepal. To reap benefit from this great potential remains a challenge for the country, especially amid the global recession. ■

New Lesson from Recent Crisis of Greece

■ **Ramu Paudel**
Deputy Director,
Research Dipartment

What happened?

Greece has been in the headlines since early December 2009 when credit rating agencies began to lower their ratings of Greece Sovereign debt. It was the second time in less than a year – recall the protest rallies that took place in the late 2008- than a country goes largely unnoticed and about which we noticed front news among the international Medias. Greece counts under 29th largest economy in the world by GDP and recognized as a developed high-income country. Greece's main industries are tourism, shipping and industrial products. Crisis of Greece thus is not only a fiscal crisis; moreover it is an economic crisis as a whole within the country and Euro Area. In the first quarter of 2010, the national debt of Greece was put at $413.6 billion, which is bigger than the country's economy. The dual problems of Greece are fiscal and competitiveness. With the budget deficit at 14 percent of GDP and public debt at 120 percent in 2009, adjustment is a matter of extreme urgency to avoid the debt spiraling further.

How:

Years of unrestrained spending, cheap lending and failure to implement financial reforms left Greece badly exposed when the global economic downturn struck. Both the debt levels and fiscal deficits that exceeded limits set by the Euro-zone were revealed & exposed. Greece entered the global recession with deep-rooted vulnerabilities. Amid slowing growth and reduced global risk appetite, the country's heavy dependence on foreign borrowing heightened concerns over long-standing fiscal and external imbalances. Public debt was commensurately increased current account deficits rose significantly and, inflation as well as external competitiveness problems rose. Economic growth turned negative in 2009 for the first time since 1993 and as a result of world financial crisis and uncontrolled spending prior to 2010. It covers up the extent of its massive budget deficit in the wake of world financial crisis, which reflected the failure on domestic resource management and undermining the credibility of the country leading to higher borrowing cost.

Moreover, persistence of wrong public policies on fiscal, social and financial sector including the effect of the global recession of the past two years, this country faced a prolonged period of weak growth and high unemployment. It has been living beyond its means in recent years, and its rising level of debt has placed a huge strain on the country's economy. The Greece government borrowed heavily and went on something of a spending spree during the past decade. Public spending soared and public sector wages practically doubled during that time. However, as the money flowed out of the government's treasury, tax income was hit because of widespread tax evasion. When the global financial downturn hit, Greece was ill-prepared to cope, budget deficits exceed and investors became wary of lending it more money, and demand higher premium

What Impacts?

Ratings agency downgraded Greece debt which means it views Greece as a highly risky place to invest. There are fears that the Greece problem could spread to other Euro zone countries, which are now anxious to bolster investor confidence. Greece is already in major breach of Euro zone rules on deficit management and with the financial markets betting the country will default on its debts; this reflects badly on the credibility of the Euro and infects other nations. The country has little in the way of a developed industrial base and its economy is heavily dependent on international services such as shipping and tourism. Tourism industry has already hit by a decline in the number of bookings because of lack of liquidity in the banks, means there's no cargo moving, and no movement for the ships. Unemployment and decline of social indicators, corruption and lack of prospects on improvement have driven Greece youth and broad layers of working people onto the streets in protest.

Some spillover effects have already started to manifest themselves. As Greece 10-year bonds fall and yields continue to remain above 6 percent. Greece crisis has made investors nervous about lending money to governments through buying government bonds. Take-home pay is likely to fall as it is eroded by rising taxes and everyone will have to work longer before they retire - by which time they are likely to find that their pensions have shrunk. The crisis is also set to slow down the embryonic economic recovery. People will affected much due to through tax bills, as Europe agrees to ride to the rescue and help Greece deal with its mounting public and foreign debts. Any assistance to Greece will come at a cost that will ultimately have to be borne by taxpayers in the nations that contribute.

What Plan to Overcome:

Due to fear about transmission of shock to other sectors and Area, special attention has already drawn by EU and IMF at the end of May, 2010. Greece got approval of financial assistance of □30 billion from the IMF through the Stand-by Agreement Program and □80 billion from EU. As a member country of EU, Greece should maintain its budget deficit below 3 percentage of point. Being a Euro zone country Greece doesn't have the choice of treating its internal and external crisis separately. Greece cannot print currency for deficit financing at home and devalue its currency to attempt to regain export competitiveness. Greece must cut on public expenditure to pay debts, import less and export more, sharply reduce wages and other benefits such as pension, social security and increase taxes like VAT. Greece also should have to give focus on further privatization of the economy, cutting taxes for business to spur investment and to weaken the process of collective bargaining so as to allow businesses to gain the upper hand in the hiring and firing process.

Greece requires maintaining the fiscal deficit and placing the debt-to-GDP ratio on a downward trajectory. Wages and social benefits have to be reduced and implement pro growth policies along with reforms to modernize the economy and open up opportunities for all. It also means that cost must be controlled and inflation reduced to regain price competitiveness. In line with these measures suggested by the EU and IMF, Greece has outlined plans to cut its budget deficit to less than 3 percent of its GDP by 2012 and pledged to make further spending cuts and tax increases. It has hiked taxes on fuel, tobacco, and alcohol, raised the retirement age by two years, imposed public sector pay cuts and applied tough new tax evasion regulations.

Way Forward:

The recent crisis in Greece is the new addition to the long list of causalities

refer page 6 for the remaining portion of this article

Glimpses upon SLR

In Nepal Statutory Liquidity Ratio (SLR) rate has fixed to 15% in case of commercial banks by the Monetary Policy of 2010-11. Which was 8% last year. But this 15% rate is inclusive of CRR 5.5%. Bank has defined the items: investment in government securities, cash in vault of FIs, Cash Reserve Requirement (CRR) and excess liquidity over CRR to be counted in SLR.

* CBs = 15%	FC = 10%
DBs = 11%	Dclass FIs (MFDBs)= 4%

NRB has reintroduced Statutory Liquidity Ratio (SLR), a monetary policy instrument from the fiscal year 2009/2010. Before this, it has used this measure in the year 1993. At that time commercial banks has to invest 34 % of the deposit collection as liquid assets. This provision of SLR was replaced later by CRR starting from 12-percentage basis point.

The objectives of SLR can be listed as given below:

- To restrict the expansion of bank credit
- To augment the investment of the banks in Government securities
- To ensure solvency of banks in general and strengthen liquidity position in particular.

SLR is commonly used to contain and fuel growth, by increasing or decreasing it respectively. This counter acts by decreasing or increasing the money supply in the financial system respectively. Following components are incorporated in the process.

Impact of change in Interest rate:

Government securities (G-Sec) held by banks are long-term fixed-rate bonds, which are sensitive to change in interest rates. Increasing interest rates can erode banks' income from trading in G-Sec. This was to increase lending by the banks to the corporate and resolve liquidity crisis. Providing economy with the much-needed fuel of liquidity to maintain the pace of growth rate. However the exercise became futile with banks being over cautious of lending in highly shaky market conditions.

It is better to gather few knowledge of difference between SLR & CRR so a few lines are written here for your reference.SLR restricts the bank's leverage in pumping more money into the economy. On the other hand CRR is the portion of deposits that the banks have to maintain with the Central Bank.

- The other difference is that to meet SLR, banks can use cash, gold or approved securities whereas with CRR it has to be only cash. CRR is maintained in cash form with central bank, whereas SLR is maintained in liquid form with banks themselves.
- Every bank in India has to maintain at the close of business every day, a minimum proportion of their net demand and time liabilities as liquid assets in the form of cash, gold and un-encumbered approved securities. The ratio of defined liquid assets to demand and time liabilities is known as Statutory Liquidity Ratio (SLR).
- In simple words, it is the percentage of total deposits banks have to invest in government bonds and other approved securities. As SLR bond also qualifies for the portfolio maintained by banks to meet the liquidity requirement. We can take an example of central bank of India that SLR now stands at 24%.

Comparing CRR and SLR

S.N.	Country	CRR in %	SLR in %
1.	Nepal	5.5	15.00
2.	India	6.00	24.00
3.	Bangladesh	5.5	18.5

We can examine, what does a reduction in SLR mean? A cut in SLR in general means that the home, car and commercial loan rates will go down. An increase in SLR also restricts the bank's leverage position to pump more money into the economy. We can take another example of the central bank of Bangladesh that it has increased SLR recently by half a percentage point to 10.5 percent for Islamic banks to curb inflationary pressures on the economy. Under the new rules, the banks will have to maintain 10.5 percent SLR instead of the earlier 10 per cent from their total demand and time liabilities.

It is note worthy that Governor Dr. Khatiwada viewed in a program organized by forum of Nepalese Banks in Kathmandu on June 6,2010 that SLR was not appropriately defined in the last year Monetary Policy. According to him, SLR does not only mean government securities. He explained, liquidity as the type of instrument that can be changed for money readily without cost or at very little cost. He defined simply, cash is the most liquid assets, may be gold or government instruments. Obviously by extending definition of liquidity or defining SLR requirement in the banking system, it might not have to face any problem because of the liquidity stress. ■

* CBs = Commercial Banks
DBs = Development Banks
FC = Finance Company
MFDBs = Micro Finance Development Banks

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of the global economic crisis. Greece's debt crisis has put the EU under the scope, and it has shifted the attention to the efficiency and the success of the Euro-zone. It is considered as probably the biggest test the EU (and the EMU-in particular) has gone through. How the EU and Greece are handling the crisis through the whole bail-out plan will reflect to what extent the EU is able to function on its own as a powerful economic entity.

Euro zone countries and IMF have agreed a rescue plan for Greece. The IMF package is oriented towards more reform along with a huge financial support and technical assistance. The EU package, which could only be offered as a last resort, will involve co-ordinate bilateral loans from countries inside the common currency area. Crisis of Greece has taught the world financial and economic crisis that started in 2007, has called into question towards, the financial institutions as diverse as the public accounting system to the common currency policy of the Euro-Zone. This crisis has taught a separate lesson to the policy makers on debt management, fiscal consolidation measures and maintenance of competitiveness of the nation, which was not learned from the previous economic and 2008 financial crisis. Theoretically, if this crisis is observed from economic point of view it can be explained as a case similar to twin deficits*. It is hypothesized that a large budget deficit leads to a large current account deficit. ■

**Readers are requested to turn pg. no. 3 to gather detail information on twin deficit. The given formula (which is in red color font) on twin deficit was compiled by the writer himself.*

International Activities

Dr. Choongsoo Kim appointed as Governor of The Bank of Korea effective 1 April 2010. NRB news congratulates on his appointment.

Dr. Kim (left) meets Ben Bernanke, chairman of the U.S. Federal

Reserve on 21st July in Washington. The two heads of their respective central banks exchanged opinions on global economic issues and exit strategies.■

New Publication

A research book on "Investment in The SEACEN Countries in The Post-Crisis Era: Issues and Challenges" was published by Choon-Seng Lim, Vincent and Min B. Shrestha as a project work while in SEACEN. Dr. Shreshtha is the Director of Nepal Rastra Bank now working in the Nepal Rastra Bank, Pokhara.

Book review by SEACEN Center:

Since the 1997 Asian financial crisis, some SEACEN countries have been unable to achieve pre-crisis levels of investments. Many reasons were cited by the literature and these include a shift in investors' perceptions, weaker exchange rates which make prices of imported investment goods more expensive, over investment in various sectors of the economy, unsettled political and security conditions, weak financial systems and governance systems, implicit state guarantees and the 'hollowing out' effect where excessive outward foreign investment has reduced domestic investment.

Project Leader / Author: Choon-Seng Lim, Vincent and Min B. Shrestha
ISBN: 983-9478-76-1
Publish Date: August 2009
Pages: 385
Price: US$ 50.00

The SEACEN Centre has got two new EXCO members, Dato' Muhammad Bin Ibrahim, Deputy Governor of Bank Negara Malaysia and Mr. K G D D Dheerasinghe, Senior Deputy Governor of Central Bank of Sri Lanka.

Dato' Muhammad Bin Ibrahim, Deputy Governor of Bank Negara Malaysia, has been appointed to the Centre by the Bank as the new member of the SEACEN EXCO effective from 16 June 2010, replacing Dato' Ooi Sang Kuang, who has been appointed as Special Adviser to the Bank.

Mr. K G D D Dheerasinghe, Senior Deputy Governor, has been appointed to the SEACEN EXCO representing the Central Bank of Sri Lanka.

Executive Committee (EXCO) is the reporting body to the SEACEN BOG, the SEACEN EXCO oversees operational matters of The SEACEN Centre. The Chairman of the BOG is concurrently the SEACEN EXCO chairman. The EXCO members comprise Deputy Governors/ Assistant Governors of all the other member banks. The SEACEN EXCO meets at least once a year, normally at the central bank that holds the chair of the SEACEN BOG.

The South East Asian Central Banks (SEACEN) Research and Training Centre was first established as a legal entity in 1982 with eight member central banks (Bank Indonesia, Bank Negara Malaysia, Central Bank of Myanmar, Nepal Rastra Bank, Bangko Sentral ng Pilipinas, Monetary Authority of Singapore, Central Bank of Sri Lanka, and Bank of Thailand). It has grown to 16 members with the inclusion of The Bank of Korea in 1990; Central Bank of the Republic of China (Taiwan), in 1992; The Bank of Mongolia in 1999; Ministry of Finance, Brunei Darussalam in 2003; Reserve Bank of Fiji in 2004; Bank of Papua New Guinea in 2005; National Bank of Cambodia and State Bank of Vietnam in 2006. The SEACEN Centre is located in Kuala Lumpur, Malaysia. ■

NRB Activities

International Participation

Deputy Governor Mr. Bir Bikram Rayamajhi attended Asia Pacific Group (APG) on anti money laundering-APG's 13th Annual Meeting and Technical Assistance Forum organized by APG in Singapore. A five-day meeting was commenced on July 10, 2010 and completed on July 18, 2010.

Mr. Dharm Raj Sapakota, Director of Legal Division, Mr. Chinta Mani Siwakoti, Director of Foreign Exchange Management Department and Mr. Hari Kumar Nepal, Assistant Director of Legal Division, accompanied him.

Executive Director of Micro-finance Department Mr. Vishnu Nepal participated a training on "Boulder Micro-finance" organized by ILO in Turin, Italy. Boulder micro-finance is apex training in Micro finance being organized by ILO. The training is scheduled from July 16 to August 9, 2010.Director of the same department Mr. Janak Bahadur Adhikari is also participating in the same training.

Executive Director of Human Resource Management Department, Mr. Gokul Ram Thapa participated in a workshop event on "Latest Trends and Challenges in Central Bank Governance". The Bank of England organized the program from June 26 to July 7, 2010 in London, UK.

Executive Director of Corporate Planning Department Mr. Ramjee Regmi attended a seminar on "Central Bank Governance" organized by Deutsche Bundes Bank in Frankfurt, Germany. The seminar began on July 3 and ended on July 12, 2010. The same bank conducted a seminar on "Controlling at Central Banks" from June 19 to 28, 2010 at the same place. Controlling Central Banks covers the various topics related to the central bank. Executive Director of Financial Management Department Mr. Manmohan Kumar Shrestha participated the seminar.

Transfer of Senior Officials

Director Dr. Nephil Matangi Maskey has moved to NRB Siddharthanagar Office, Bhairahawa from Research Department. He has assumed his new office as the Chief Manager. Prior to this, this post was headed by Director Mr. Kesab Raj Acharya. Now Mr. Acharya was posted to the Internal Audit Department in Kathmandu.

39th Board Meeting of ACU Convened at Thimphu

The 39th meeting of the Board of Directors of the Asian Clearing Union (ACU) was successfully concluded on June 12, 2010 in Thimphu, Bhutan.

The 39th meeting was inaugurated by the Finance Minister of Bhutan, Mr. Wangdi Norbu on June 11, 2010. The Managing Director of the Royal Monetary Authority of Bhutan, Chairman of the Board of Directors of the ACU, chaired the meeting.

At this meeting, the Secretary General of the ACU, Mrs. Lida Borhan Azad, presented the Report on the operations of the ACU during the year 2009, followed by deliberations of the Board on the recommendations of the two technical committees on improvement of the ACU mechanism and expansion of the scope of the Union.

The meeting decided to form an assessment committee for establishment of ACU Trade and Development Bank. That meeting also scheduled the

The meeting elected Governors of Reserve Bank of India and Central Bank of Islamic Republic of Iran as the Chairman and the Vice Chairman for the year 2011 respectively.

Governor of Nepal Rastra Bank Dr. Yuba Raj Khatiwada participated the meeting as a member from Nepal. During the program, he discussed with the Governor of RBI about smooth supply of IC. He also discussed with the Governors of the member central banks about enhancement of cooperation on bilateral trade and payment settlement.

The ACU is a payment mechanism through which the participants settle payments for intra-regional transactions on a multilateral basis. The total volume of transactions channeled through the ACU mechanism during the year 2009 was about USD 28 billion, representing a decline of 33% over the previous year.

The ACU members are Bangladesh Bank, Royal Monetary Authority of Bhutan, Reserve Bank of India, Central Bank of the Islamic Republic of Iran, Central Bank of Myanmar, Nepal Rastra Bank, State Bank of Pakistan and the Central Bank of Sri Lanka. Maldives Monetary Authority is the most recent member, who joined the ACU in the 38th Board meeting held at Colombo, Sri Lanka in 2009. ■

Extract | From | **The Economic Times** July 28, 2010

RBI GUV SAYS HE DOESN'T WANT TO SIGNAL AN UPWARD BIAS

HOURS after raising interest rates, RBI governor Duvvuri Subbarao took on question from the media on issues ranging from inflation, managing liquidity, property prices and new bank licenses. Excerpts of the Q&A:

You have revised your inflation forecast to 6%. Do you feel there is an upward bias to that?

I don't think we want to give it an upward bias at the moment. We are very confident about the number. There are a number of upside factors. First, is the south-west monsoon. We should expect some dampening impact on food prices. Second, how many more petroleum products are deregulated and how soon that happens. Third, the demand side factors. Capacity utilisation is not at its cyclical peak, but we are very close to that. Also spare capacity around the world could lead to softening in prices. Finally I hope that monetary policy actions since January will start playing in now.

Bankers said that they do not intend to increase rates immediately. Is monetary transmission bothering you?

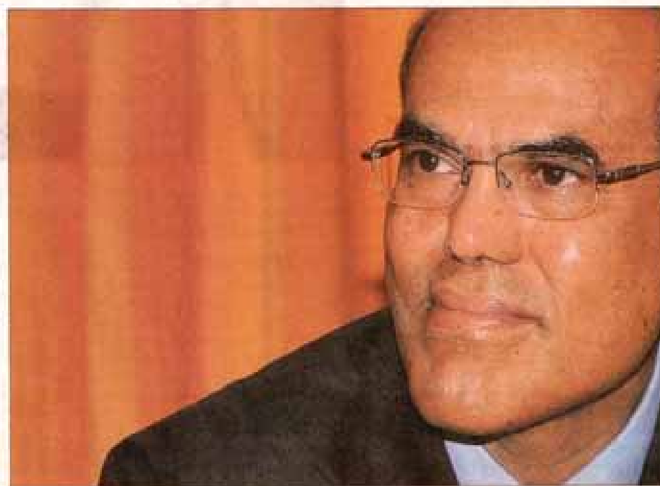
I wouldn't say it's disturbing, but we have been talking about it. While it is important that the signals are transmitted, there are good reasons why it has not happened so far. One reason is that demand for credit was sluggish and also because there was some concern about the transition from the PLR system to the base rate. Some of these factors are behind us. As credit demand picks up, as liquidity becomes tighter and as other policy actions start playing out we expect both deposit rates and lending rates go up. Bankers have told us that deposit rates will go up before lending rates.

Would you say your policy rates are normalised for your growth and inflation targets?

In the April policy statement we have talked about whether we have reached there. One thing is clear we have not reached there yet. The way economists describe neutral rates is that it is a rate that is consistent with the potential growth rate and low and stable inflation. In an economy that is growing very fast, there is no stable neutral rate. If we take the movement of policy rates in the highest point before the crisis, it was 9% for repo rate and lowest point it went to was 4.75%. The neutral rate is somewhere in-between that rate say plus minus around that.

Your have been silent on deposit growth. Do you maintain your April forecast of 18%?

I should think so, though I realise that deposit growth is lower. The number we put out in the



document is 15.2%, but yesterday, after we sent the policy documents to the press we got a number that is slightly lower. We have spoken to banks. Deposits have gone down because of public sector oil companies and mutual funds withdrawing also individuals holding more currency because of inflation. But we expect 18% deposit growth.

How will you manage liquidity actively?

It would not necessarily be open market operations. We expect the current liquidity situation that has occurred because of 3G payments to ease by month end. However, the absorption mode that we saw for the last two years has changed. We expect that the operative rate will be the repo rate and the system will be in the injection mode because that way monetary transmission will work better.

What is your outlook on world economic growth?

The IMF's sunny outlook is not widely shared. There is somewhat disappointing news coming from around the world — about sovereign debt crisis in Europe and Bernanke's statement that conditions are unduly uncertain. What is of concern is that in the last few weeks subdued outlook is spreading to emerging markets. Three months ago we were talking about capital flows coming in a flood. That has changed. If uncertainty persists it has implications for the market, the economy and exports.

You have expressed concern on real estate rates, but there is no mention of the sector in your policy.

Asset prices is something we had taken into account. Among asset prices we have noted that equity prices had gone up last year and continues to go up this year. Gold is at an all time high. Information on real estate that has come to us is that in Mumbai and Delhi asset prices have overshot their pre-crisis peak in other cities they are still below the peak but inching up. Real estate prices have always been part of calculation that go into monetary policy.

India Inc is awaiting guidelines on new bank licences.

The discussion paper is on track, we expect the paper at the end of this month or first week of August. There has been a number of issues have come up like - What should be the entry level capital? What should be the promoters capital? What should be the dilution norms? Whether we should allow corporates to come in? Whether we should allow NBFCs to come in automatically? We will marshal international and our own experience. The discussion paper will include all that and thereafter we will take your feedback.

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