Nepal Rastra Bank

Research Department

Current Macroeconomic and Financial Situation of Nepal

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

Macroeconomic Outlook

1. Notwithstanding the damage caused by flood to the agriculture, the remedial measures adopted by the government to contain post-flood loss in paddy along with normal monsoon rains in subsequent period are likely to underpin the improved agriculture growth outlook.

2. The industrial capacity utilization is expected to expand on account of improved supply of energy and smooth supply of industrial raw materials. Some hydropower projects are in completion phase and expected to be completed during the current fiscal year. This will add electricity to national transmission grid leading to an increased power supply to industrial estates.

3. The tourism sector is expected to perform better as reflected in an increased hotel bed occupancy rate, encouraging hotel booking and registration of hotel and restaurants.

4. Parliamentary and provincial elections slated for November 26 and December 7, 2017 are expected to boost domestic demand through increased consumption expenditure. This development is likely to improve consumer and investors' sentiment generating positive impact on growth.

5. The legislative parliament has recently passed the Intergovernmental Fiscal Management Bill, 2017, along with National Natural Resources and Fiscal Commission Bill, 2017 and Employee Adjustment Bill, 2017. These legislative measures are expected to facilitate capital spending at local levels, spurring economic activities across the country.

Inflation, Salary and Wage Rate

Consumer Price Inflation

6. Consumer price inflation has risen to 3.4 percent in mid-September 2017 from 2.3 percent in mid-August 2017. The spike in prices of vegetables on accounts of floods and inundation in mid August 2017 has pushed

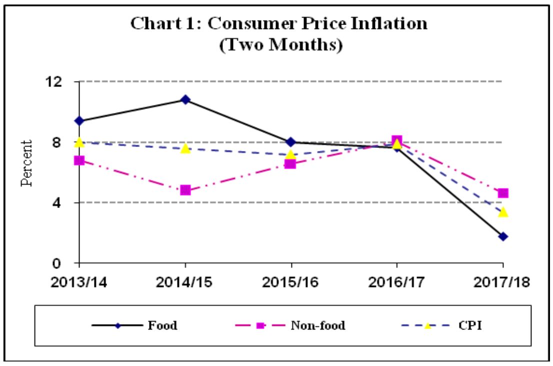


Chart 1: Consumer Price Inflation (Two Months)

overall prices a little bit up in the review month. However, such inflation is lower than the inflation of 7.9 percent recorded in the corresponding period of the previous year.

Food Inflation

7. Food inflation has eased to 1.8 percent in mid-September 2017 from 7.7 percent in the corresponding period of the previous year. A fall in prices of pulses and legumes by 23.7 percent together with spices by 4.2 percent has helped ease overall food inflation. Of food and beverage group, the prices of vegetables increased 8.9 percent and alcoholic drinks 8.8 percent in the review period.

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

Particulars		Inflation (Percent)	
		2073/74	2074/75
Food Inflation		**7.7**	**1.8**
1	Sugar and Sugar products	20.6	4.8
2	Fruit	16.6	0.2
3	Pulses and Legumes	14.4	(23.7)
4	Alcoholic drinks	13.4	8.8
5	Spices	12.6	(4.2)
6	Restaurant and Hotel	10.0	4.6

Source: National Consumer Price Index, Mid-September 2017

Non-food Inflation

8. Non-food inflation decelerated to 4.7 percent during the review period from 8.1 percent in the corresponding period of the previous year. The slower growth of prices of clothes and footwear, furnishing and household equipment, housing and utilities contributed to the moderation of non-food inflation in the review period.

Region-wise Consumer Price Inflation

9. The Mountain region witnessed relatively a higher rate of inflation of 5.4 percent followed by Terai region of 3.8 percent, Hilly region of 3.4 percent and the Kathmandu Valley of 2.8 percent in the review period. In the corresponding period of the previous year, these regions had witnessed inflation rates of 7.5 percent, 7.4 percent, 10.3 percent and 6.6 percent respectively.

Inflation Differential between Nepal and India

10. The y-o-y consumer price inflation was 3.4 percent in Nepal in mid-September 2017 compared to 3.3 percent in India, showing a marginal inflation wedge of 0.1 percent between the two countries. A year ago, the rate of inflation was 7.9 percent in Nepal compared to 4.3 percent in India, reflecting a wider inflation differential of 3.6 percent.

Wholesale Price Inflation

11. The y-o-y wholesale price inflation slowed to 1.5 percent in the review period from 5.3 percent a year ago. The wholesale price indices of agricultural commodities, domestic manufactured commodities and imported commodities grew 0.6 percent, 4.6 percent and 1.4 percent respectively in the review period. In the corresponding period of the previous year, wholesale price indices of agricultural commodities and domestic manufactured commodities had observed the growth of 7.9 percent and 6.2 percent respectively, whereas the price index of imported commodities had declined by 1.9 percent.

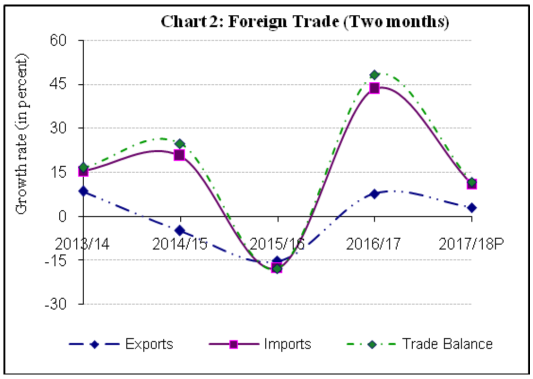
National Salary and Wage Rate

12. The y-o-y salary and wage rate index rose 5.8 percent in the review period compared to 15.1 percent in the corresponding period of the previous year. In the review period, the salary index increased 14.4 percent, while the wage rate index grew 3.7 percent. The salary indices of bank and financial institutions, education and public corporations sub-groups increased 10.6 percent, 5.8 percent and 0.8 percent respectively in the review period. Likewise, wage rate indices of agricultural laborer, industrial laborer and construction laborer witnessed a growth of 2.8 percent, 6.3 percent and 2.1 percent respectively in the review period.

External Sector

Merchandise Trade

13. In first two months of 2017/18, merchandise exports increased 3 percent to Rs. 13.58 billion compared to a growth of 7.7 percent in the same period of the previous year. In the review period, exports to India decreased 3.3 percent whereas exports to China and other countries increased 44.6 percent and 9.7 percent respectively. Commodity wise, the exports of cattle feed, thread, readymade garments, oil cake, vegetable ghee among others, increased whereas the export of juice, cardamom, woolen carpet, G.I. pipes, toothpaste, among others, decreased in the review period.



14. Merchandise imports increased 11 percent to Rs. 165.41 billion in the review period compared to a growth of 43.4 percent in the same period of the previous year. In the review period, imports from India, China and other countries increased 8.1 percent, 26.3 percent and 10.7 percent respectively. Commodity wise, imports of petroleum products, aircraft spare parts, gold, cement, telecommunications equipments & parts among others, increased whereas imports of agricultural equipment and parts, edible oil, silver, sanitary wares, electrical goods, among others, decreased.

15. Based on customs points, the exports through Birgunj Customs Office, Dry Port Customs Office, Bhairahawa Customs Office, Krishnanagar Customs Office and Kailali Customs Office decreased whereas exports through other customs points increased. On the import side, Bhairahawa Customs Office, Tribhuwan Airport Customs Office and Kanchanpur Customs Office decreased whereas imports through other customs points increased in the review period.

16. Total trade deficit in the review period widened 11.8 percent to Rs. 151.83 billion compared to an expansion of 48.1 percent in the same period of the previous year. The export-import ratio dropped to 8.2 percent in the review period from 8.8 percent in the corresponding period of the previous year.

Export-Import Price Index

17. The y-o-y unit value export price index based on customs data remained unchanged while import price index increased 4.4 percent in the first two months of 2017/18. Consequently, the TOT index decreased 4.2 percent compared to an increase of 22.5 percent in the corresponding period of the previous year. Increase in the price of petroleum products, tyres, lead acid battery, vehicles, biscuits resulted in increase in import price index in the review period.

Box 2: Number of Nepalese Workers going for Foreign Employment (Two Months)

a) Institutional and Individual (New and Legalized)

Country	(No. of Labor)		Percentage Share	
	2016/17	2017/18	2016/17	2017/18
Malaysia	14109	23362	20.1	35.8
Qatar	20839	14733	29.7	22.6
Saudi Arabia	20043	8868	28.5	13.6
U.A.E.	9838	10330	14.0	15.8
Kuwait	1198	2186	1.7	3.4
Bahrain	618	711	0.9	1.1
Oman	548	529	0.8	0.8
South Korea	777	1352	1.1	2.1
Lebanon	43	2	0.1	0.0
Israel	19	7	0.0	0.0
Afghanistan	0	398	0.0	0.6
Japan	500	110	0.7	0.2
Others	1712	2599	2.4	4.0
Total	70244	65187	100.0	100.0
Percentage Change	-10.0	-7.2	-	-

b) Renew Entry

Renew Entry	**30175**	**32271**	-	-
Percentage Change	15.3	6.9	-	-

Source: Department of Foreign Employment.

Services

18. The total services receipt increased 4.5 percent and expenses rose 9.2 percent in the review period resulting in a deficit of Rs. 6.77 billion in the review period. A year ago, such deficit was Rs. 5.31 billion.

19. Under the service account, travel receipt increased 8.2 percent to Rs. 8.11 billion in the review period. Such receipt had increased 33.1 percent in the same period of the previous year.

Workers' Remittances

20. The workers' remittances increased 0.7 percent to Rs. 115.55 billion in the review period compared to 6.6 percent in the same period of the previous year. Consequently, net transfer receipt increased 0.4 percent to Rs. 130.65 billion in the review period. Such receipt had increased 3.7 percent in the same period of the previous year.

21. The number of Nepalese going abroad for foreign employment (except renew entry) has been falling. The number of Nepalese seeking foreign employment decreased 7.2 percent in the review period. It had decreased 10 percent in the same period of the previous year. In the review period, the number of workers outbound to Malaysia jumped up while those to Saudi Arabia and Qatar shrank.

Current Account and BOP Position

22. The current account registered a deficit of Rs. 17.88 billion in the review period. Such deficit was Rs. 11.12 billion in the same period of the previous year. Similarly, the overall BOP remained at deficit of Rs. 5.87 billion in the review period compared to a deficit of Rs. 3.50 billion in the same period of the previous year.

23. In the review period, Nepal received capital transfer amounting to Rs. 1.84 billion and Foreign Direct Investment (FDI) inflow of Rs. 5.10 billion. In the same period of the previous year, capital transfer and FDI inflow had amounted to Rs. 1.54 billion and Rs. 2.19 billion respectively.

Box 3: External Sector (USD)*

(USD Million)

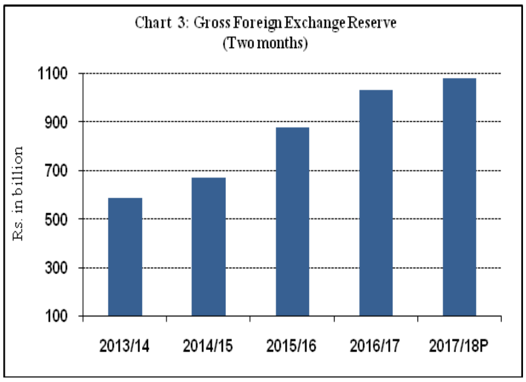
Particulars	2015-16		2016-17		2017-18	Percentage Change in Two months	
	Two Months	Annual	Two Months	Annual	Two Months	2016/17	2017/18
Goods Exports (FoB)	135.2	703.9	134.2	773.7	146.0	-0.8	8.8
Goods Imports (FoB)	982.5	7092.5	1363.4	9219.3	1580.0	38.8	15.9
Trade Balance	-847.3	-6388.6	-1229.3	-8445.6	-1434.1	45.1	16.7
Total Trade	1117.7	7796.3	1497.6	9993.0	1726.0	34.0	15.3
Travel Receipts	54.0	392.7	70.0	552.3	79.1	29.7	13.0
Workers' Remittances	1033.8	6253.4	1071.3	6556.3	1127.1	3.6	5.2
Current Account Balance	366.0	1338.8	-103.8	-93.5	-174.4	-	-
BOP (-Surplus)	-302.5	-1779.8	32.6	-777.1	57.3	-	-

** Data from BOP Presentation*

1. In the US dollar terms, total merchandise exports and imports increased 8.8 percent and 15.9 percent respectively in the first two months of 2017/18. Exports had decreased 0.8 percent whereas imports increased by 38.8 percent in the corresponding period of the previous year.
2. In the review period, travel receipts and worker's remittance increased 13 percent and 5.2 percent respectively. Travel receipts and workers' remittances had increased 29.7 percent and 3.6 percent respectively in the corresponding period of the previous year.
3. Current account recorded a deficit of USD 174.4 million in the review period compared to a deficit of USD 103.8 million in the corresponding period of the previous year. Likewise, Balance of Payments (BOP) recorded a deficit of USD 57.3 million in the review period compared to the deficit of USD 32.6 million in the corresponding period of the previous year.

Foreign Exchange Reserves

24. The gross foreign exchange reserves stood at Rs. 1079.97 billion as at mid-September 2017. It was at Rs. 1079.52 billion as at mid-July 2017. Of the total foreign exchange, reserves held by NRB decreased 0.4 percent to Rs. 923.98 billion as at mid-September 2017 from Rs. 927.27 billion as at mid-July 2017. Similarly, the reserves of banks and financial institutions (except NRB) increased 2.5 percent to Rs. 155.99 billion as at mid September 2017 from Rs. 152.26 billion as at mid-July 2017. The share of Indian currency in total reserves stood at 23 percent as at mid-September 2017.



Foreign Exchange Adequacy Indicators

25. Based on the imports of the first two months of the current fiscal year, the foreign exchange holdings of the banking sector is sufficient to cover the prospective merchandise imports of 13.3 months, and merchandise and services imports of 11.4 months. The ratio of reserve-to-GDP, reserve-to-imports and reserve-to-M2 increased to 41.5 percent, 94.6 percent and 40.9 percent respectively as at mid- September 2017. Such ratios were 41.5 percent, 95.3 percent and 41.7 percent as at mid-July 2017.

Price of Oil and Gold

26. The price of oil (Crude Oil Brent) in the international market increased 24.1 percent to USD 56.18 per barrel in mid-September 2017 from USD 45.26 per barrel a year ago. The price of gold increased 1.1 percent to USD 1322.85 per ounce in mid-September 2017 from USD 1308.35 per ounce a year ago.

Exchange Rate

27. Nepalese currency vis-à-vis US dollar appreciated 0.6 percent in mid-September 2017 from mid-July 2017. It had depreciated 0.1 percent in the same period of the previous year. The buying exchange rate per US dollar stood at Rs. 102.22 in mid-September 2017 compared to Rs. 102.86 in mid-July 2017.

Fiscal Situation*

Budget Deficit/ Surplus

28. In the first two months of 2017/18, the Government of Nepal (GoN) was at a surplus of Rs. 19.18 billion in its budget. Such surplus was Rs. 45.62 billion in the corresponding period of the previous year.

Box 4: The Budget Performance in the First Two Months of 2017/18 (Rs. in million)

Heads	Budget Estimates	Outturns in Two Months*	As percent of Budget Estimates
Total Expenditure	**1278994.9**	**72376.1**	**5.66**
Recurrent	803531.5	70256.4	8.74
Capital	335176.0	1548.9	0.46
Financial	140287.4	570.8	0.41
Revenue	**730055.6**	**88791.1**	12.16

* On cash basis

Government Expenditure

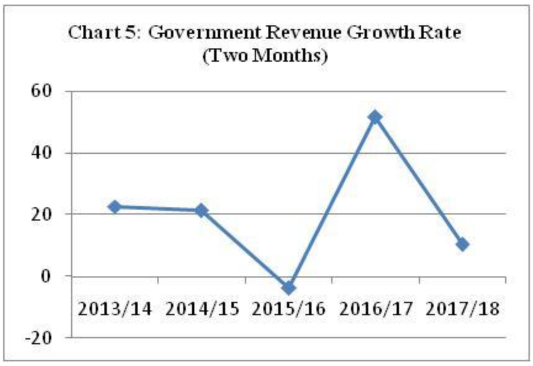
29. In the review period, total government expenditure on a cash basis stood at Rs. 72.38 billion. Such expenditure was just Rs. 31.55 billion in the corresponding period of the previous year.

* Based on the data reported by 6 NRB offices, 76 branches of Rastriya Banijya Bank Limited, 49 branches of Nepal Bank Limited, 25 branches of Agricultural Development Bank Limited, 12 branches of Everest Bank Limited, 10 branches of Nepal Investment Bank Limited, 9 branches of Global IME Bank Limited, 8 branches of NIC Asia Bank Limited, 2 branches of Bank of Kathmandu Limited and 1 branch each from NMB Bank Limited and Century Commercial Bank Limited conducting government transactions and released report from 79 DTCOs and payment centers.

30. In the review period, recurrent expenditure stood at Rs. 70.26 billion. Such expenditure was Rs. 29.58 billion in the corresponding period of the previous year. In the review period, capital expenditure increased 20 percent to Rs. 1.55 billion. Such expenditure was Rs. 1.29 billion in the corresponding period of the previous year.

Government Revenue

31. In the review period, the government revenue collection increased 10.3 percent to Rs. 88.79 billion. Such revenue had increased 51.6 percent to Rs. 80.47 billion in the corresponding period of the previous year. The government revenue collection has been less than targeted. The growth in the government revenue continues to remain sensitive to high tariff rate related imports.



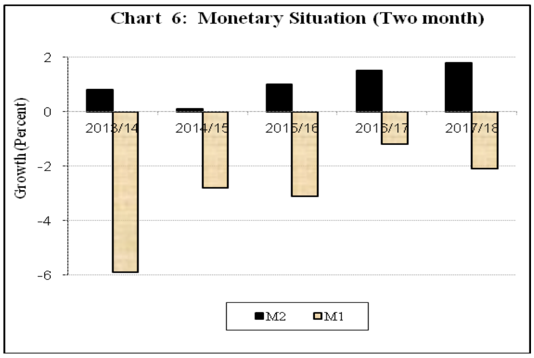
Treasury Position of the GoN

32. Because of a slow pace of government expenditure relative to resource mobilization, the treasury surplus amounted to Rs. 258.38 billion as of mid-September 2017.

Monetary Situation

Money Supply

33. Broad money (M2) increased 1.8 percent in the review period compared to a rise of 1.5 percent in the corresponding period of the previous year. On y-o-y basis, M2 expanded 15.9 percent in mid-September 2017.



34. The net foreign assets (NFA after adjusting foreign exchange valuation gain/loss) decreased Rs. 5.87 billion (0.6 percent) in the review period compared to a decrease of Rs. 3.50 billion (0.4 percent) in the corresponding period of the previous year.

35. Reserve money decreased 13.3 percent in the review period compared to a decrease of 6.3 percent in the corresponding period of the previous year. On y-o-y basis, reserve money increased 11 percent in mid- September 2017.

Domestic Credit

36. Domestic credit decreased 0.7 percent in the review period in contrast to an increase of 0.1 percent in the corresponding period of the previous year. On y-o-y basis, domestic credit increased 18.5 percent in mid- September 2017.

37. Claims of monetary sector on the private sector increased 3.2 percent in the review period compared to a growth of 4.3 percent in the corresponding period of the previous year.

On y-o-y basis, claims of monetary sector on the private sector increased 16.8 percent in mid- September 2017.

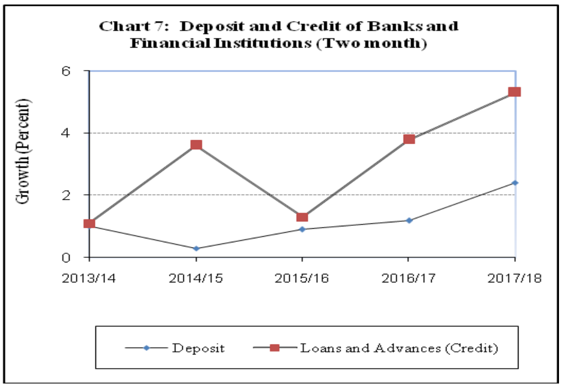
Deposit Collection

38. Deposits at banks and financial institutions (BFIs) increased 2.4 percent in the review period compared to an increase of 1.2 percent in the previous year. On y-o-y basis, deposits at BFIs expanded 15.4 percent in mid- September 2017.

39. Out of the total deposits at the BFIs, the share of demand deposits decreased from 8.6 percent to 8.3 percent and saving deposits from 43.9 percent to 35.6 percent in mid-September 2017 compared to a year ago. However, the share of fixed deposits increased to 43.1 percent from 30.1 percent in the review period.

Credit Disbursement

40. Credit to the private sector from BFIs increased 2.1 percent in the review period compared to a rise of 3.5 percent in the corresponding period of the previous year. In the review period, private sector credit from commercial banks, development banks and finance companies increased 1.8 percent, 4.8 percent and 1.3 percent respectively. On y-o-y basis, credit to the private sector from BFIs increased 16.6 percent in mid-September 2017.



41. Credit to the agriculture sector increased 2.1 percent, industrial production sector 2.4 percent, construction sector 3.0 percent, wholesale and retail trade sector 3.3 percent, service sector industries 2.8 percent and transport, communication and public sector 2.8 percent in the review period.

42. Of the total outstanding credit of BFIs, 60.9 percent is against the collateral of land and building and 14.2 percent against the collateral of current assets (such as agricultural and non-agricultural products). Such ratios were 60.6 percent and 15.2 percent respectively in the corresponding period of the previous year.

43. Of the total outstanding loan of commercial banks, credit to small and medium enterprises was 2.4 percent (Rs. 48.23 billion) in mid-September 2017.

44. Trust receipt (T.R.) loan extended by commercial banks increased 15.9 percent (Rs. 10.27 billion) to Rs. 74.80 billion in the review period compared to an increase of 9.2 percent in the corresponding period of the previous year.

45. In the review period, hire purchase lending increased 1.4 percent while that of overdraft loan decreased 1.6 percent. Similarly, residential personal home loan (up to Rs. 15 million) increased 3.8 percent and real estate loan 0.4 percent.

Liquidity Management

46. In two months of the fiscal year 2017/18, the NRB mopped up Rs. 104.90 billion through open market operations. Of which, Rs. 35.15 billion under deposit collection auction and Rs. 69.75 billion through reverse repo auction on a cumulative basis. In the corresponding period of the previous year, Rs. 85.05 billion liquidity was absorbed. This consisted of Rs. 31.50 billion through deposit collection auction (90 days deposit collection auction and 14 days deposit collection auction) and Rs. 53.55 billion through reverse repo auction.

47. In the review period, the NRB injected net liquidity of Rs. 46.54 billion through the net purchase of USD 531.2 million from foreign exchange market. Net liquidity of Rs. 57.50 billion was injected through the net purchase of USD 537.5 million in the corresponding period of previous year.

48. The NRB purchased Indian currency (INR) equivalent to Rs. 67.66 billion through the sale of USD 660 million in the review period. INR equivalent to Rs. 77.47 billion was purchased through the sale of USD 640 million and Euro 75 million in the corresponding period of previous year.

Refinance

49. The NRB has been providing refinance facility aimed at expanding credit to the productive sector along with promoting export. As of mid-September 2017, the outstanding refinance amount stood Rs. 7.14 billion including general refinance of Rs. 6.46 billion and export refinance of Rs. 681.3 million.

50. A sum of Rs. 904.7 million housing loan at a concessional interest rate of 2 percent has been extended by the BFIs to the earthquake victims. NRB provides refinance facility to BFIs at a zero percent interest to extend housing loan to earthquake victims.

Inter-bank Transaction

51. In the second month of 2017/18, inter-bank transactions among commercial banks stood at Rs. 93.93 billion and among other financial institutions (excluding transactions among commercial banks) amounted to Rs. 7.08 billion. Such transactions were Rs. 167.79 billion and Rs. 45.59 billion respectively in the corresponding period of the previous year.

Interest Rates

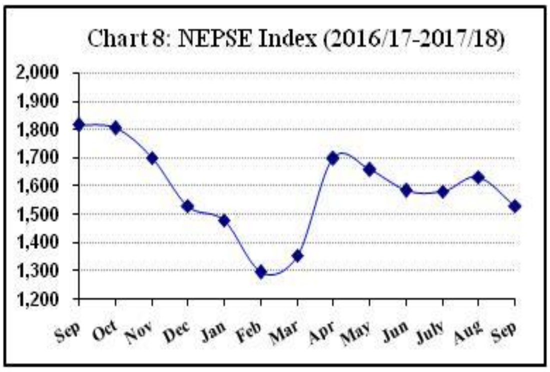
52. The weighted average 91-day Treasury Bill rate decreased to 0.48 percent in the second month of 2017/18 from 2.05 percent a year ago. The weighted average inter-bank transaction rate among commercial banks, which was 2.56 percent a year ago, decreased to 0.39 percent in the review month. In contrast, the average base rate of commercial banks increased to 10.13 percent in the review month from 6.23 percent a year ago.

Merger/Acquisition

53. The number of BFIs involved in merger and acquisition has been increasing after the introduction of merger/acquisition policy aimed at strengthening financial stability. So far, 151 BFIs (including 'D' class) were involved in merger and acquisition since this bank

introduced the regulatory procedure regarding merger and acquisition. Of which, the license of 112 BFIs was revoked thereby forming 39 BFIs.

Capital Market



54. The NEPSE index on y-o-y basis decreased 15.7 percent to 1,530.3 points in mid-September 2017. This index had increased 51.8 percent to 1815.2 points in mid-September 2016. Such index was 1582.7 points in mid-July 2017.

55. The stock market capitalization on y-o-y basis decreased 11.4 percent to Rs. 1775.59 billion in mid-September 2017. This had increased 62.6 percent a year ago. The ratio of market capitalization to GDP of 2016/17 stood at 68.3 percent in mid-September 2017. This ratio was 89.1 percent a year ago. In the total market capitalization, the share of banks, financial institutions and insurance companies stood at 84.2 percent, hydropower 4.3 percent, manufacturing and processing companies 2.6 percent, hotels 1.8 percent, trading 0.1 percent, and others 7.0 percent respectively.

56. During the second month of 2017/18, the total turnover of the securities decreased 42.6 percent to Rs. 13.57 billion. The turnover of the securities had substantially increased 93.2 percent to Rs. 23.62 billion in the corresponding period of the previous year.

57. Due to the merger and acquisitions of BFIs, total number of companies listed at the NEPSE decreased to 196 in mid-September 2017 from 227 in mid-September 2016. Of the listed companies, 151 are BFIs (including insurance companies), 18 manufacturing and processing industries, 16 hydropower companies, 4 each hotels and trading institutions and 3 other sectors.

58. On y-o-y basis, total paid-up value of the listed shares increased 40.6 percent to Rs. 295.28 billion in mid-September 2017. Total additional securities worth Rs. 22.28 billion were listed in the NEPSE during the review period. These consist of ordinary shares Rs. 1.10 billion, right shares Rs. 13.74 billion, bonus shares Rs. 431 million and government securities Rs. 7 billion.