

Current Macroeconomic Situation

(Based on the First Two Months' Data of 2006/07)

Monetary Aggregates

1. In the first two months of 2006/07, broad money (M_2) increased by 2.0 percent compared to a growth of 0.6 percent in the corresponding period of the previous year. An increase in the growth of net domestic assets (NDA) contributed to such an increase in M_2 .
2. Of the components of M_2 , narrow money (M_1) declined by 1.5 percent in the review period compared to a decrease of 3.7 percent last year. Time deposits, another component of M_2 , increased by 3.7 percent in the review period compared to a growth of 2.7 percent in the previous year. Inflow of remittance contributed to the rise in time deposits in the review period.
3. NFA, a main source of monetary expansion, increased by 0.5 percent (Rs 657.1 million) after adjusting foreign exchange valuation gain/loss in the review period compared to a growth of 2.8 percent (Rs 3.0 billion) last year. Sluggish growth of exports contributed to such a slowdown in the growth of NFA in the review period.
4. Domestic credit, another component of monetary expansion, registered a modest growth of 0.8 percent in the review period in contrast to a decline of 0.4 percent in the previous year. Expansion of credit to government enterprises and other financial institutions from commercial banks contributed to the rise in domestic credit in the review period.
5. Of the credit aggregates, net claims on government experienced a decline of 7.1 percent compared to a decrease of 7.3 percent last year. The higher growth of revenue relative to the government expenditure resulted in a cash balance surplus with Nepal Rastra Bank (NRB) leading to a decline in the net claims on the government in the review period.
6. Claims on non-financial government enterprises increased by 11.6 percent in the review period in contrast to a decline of 15.2 percent in the previous year due mainly to the higher loan utilization by Nepal Oil Corporation, Nepal Food Corporation, Janakpur Cigarette Factory Ltd, Nepal Water Supply Corporation and National Trading Ltd from the commercial banks.
7. Claims on private sector increased marginally by 2.2 percent in the review period compared to a growth of 2.4 percent last year. The slowdown in industrial activities, decelerated growth of imports and emphasis on loan recovery by the commercial banks contributed to a lower rate of credit off-take by the private sector.

Reserve Money

8. Compared to a decline of 9.8 percent last year, reserve money (RM) decreased by 7.4 percent in the review period. A reduction in NDA of monetary authorities contributed to a further decline in RM in the review period.

Money Market

9. The net liquidity injection through the intervention in the foreign exchange market stood at Rs 11.3 billion in the review period compared to Rs 3.3 billion in the previous year. NRB made purchase interventions of the US dollar in the foreign exchange market in the review period.
10. In the review period, net liquidity of Rs. 6.4 billion was mopped up through open market operations in treasury bills compared to Rs 1.4 billion in the previous year. Of the monetary instruments used for secondary market operation, outright sale auction absorbed Rs 2.3 billion and reverse repo auction absorbed Rs 4.1 billion in the review period.
11. Compared to the use of Rs 950 million loan under standing liquidity facility (SLF) in the previous year, commercial banks borrowed Rs 370 million from NRB under this facility in the review period. The excess liquidity situation with the commercial banks lowered the use of SLF in the review period.
12. Because of the excess liquidity, weighted average of 91-day Treasury bills rate remained lower in the review period than that of the previous year. Such rate stood at 2.78 percent as at mid-September 2006 compared to 3.38 percent a year ago.

Securities Market

13. On the primary issue front, Nepal Securities Board granted permission to five financial institutions to issue ordinary shares amounting to Rs. 15 million and right shares amounting to Rs. 80 million in the first two months of 2006/07.
14. In the secondary market, the year on year (y-o-y) NEPSE index remained buoyant showing an increase of 30.4 percent to 382.56 points in mid-September 2006. Continuous rise in remittance inflow, lower interest rate, and the lack of alternative investment opportunities accounted for the expansion in the stock market activities.
15. The number of companies listed in the Nepal Stock Exchange Ltd reached 135 in mid-September 2006. This number was 125, a year ago. Out of the total listed companies, 88 were bank and financial institutions, which accounted for nearly 65.2 percent of the total listed companies. The number of production and processing industries was 29, hotel was 4, business entity was 8 and entity belonging to other group was 6. These groups comprised 21.5 percent, 3 percent, 5.9 percent and 4.4 percent respectively of the total listed companies.
16. The y-o-y market capitalization increased by 45.6 percent and reached to Rs. 96.4 billion in mid-September 2006. Market capitalization to GDP ratio increased to 16.5 percent in mid-September 2006 from 11.5 percent, a year ago. Of the total transactions, bank and financial institutions accounted for 82.3 percent, production and processing companies accounted for 6.1 percent, hotels accounted for 2.4 percent, business entities accounted for 0.8 percent and entities belonging to other groups accounted for 8.4 percent.

17. Total paid up capital of the listed companies reached Rs. 20.3 billion in mid-September 2006, showing an increase of 15.1 percent over the period of one year. The increase was due to the increase in listed companies in the Nepal Stock Exchange Ltd, and the issuance of ordinary and right shares by some of the financial institutions.

Inflation, Salary and Wage Rate

Consumer Price Inflation

18. The y-o-y consumer price inflation moderated to 6.6 percent in mid-September 2006. The y-o-y consumer price inflation was 8.2 percent in mid-September 2005. The moderation of consumer inflation was on account of the lower rate of rise in the prices of cereal products and the elimination of base effect of the petroleum price hike of September 2005.
19. A significant increase in the prices of pulses (22.0 percent) and spices as well as lagged effect of increased petroleum prices of March 2006 accounted for consumer price inflation at 6.6 percent in September 2006.
20. Region-wise, price level remained high in the Hills at 7.2 percent and Terai at 6.7 percent and relatively low in the Kathmandu Valley at 6.0 percent. The respective inflation rates were 9.1 percent, 8.8 percent and 6.8 percent a year ago.
21. In September 2006, the y-o-y core inflation edged up at 5.6 percent from 4.5 percent a year ago. Inflationary expectation accounted for a pick up in core inflation in the review period.

Wholesale Price Inflation

22. In September 2006, the y-o-y wholesale price inflation moderated to 8.7 percent from 9.6 percent a year ago. A significant price rise of cash crops, pulses and spices together with the lagged effect of the hike in prices of petroleum products in March 2006 accounted for wholesale price inflation at 8.7 percent in the review period. Group-wise, the prices of Agricultural Commodities showed an increase of 11.1 percent, manufactured goods at 7.3 percent and imported commodities at 6.0 percent.

Salary and Wage Rate

23. The y-o-y salary and wage rate index rose by 7.9 percent in September 2006. The growth of such index was 1.9 percent a year ago. The surge in wage rate on account of shortage of laborers owing to the Nepalese workers seeking foreign jobs and the 10 percent increment in the allowances of civil servants contributed to the rise in the national salary and wage rate index in the review period. In the review period, the wage rate and the salary indices increased by 8.5 percent and 6.6 percent respectively.

Fiscal Situation

Government Expenditure

24. On the fiscal front, total government spending recorded a growth of 22.5 percent to Rs 9.8 billion in the first two months of 2006/07. The government spending had gone up by 17.1 percent in the same period of 2005/06. A significant rise in recurrent expenditure largely accounted for a surge in overall government expenditure.

Government Revenue

25. The government revenue increased by 22.3 percent to Rs 10.8 billion in the first two months of 2006/07. Revenue had increased by 13.4 percent in the corresponding period last year. The rise in tax collection from VAT and customs accounted for such an increase in total revenue. An improvement in consumers' confidence backed by a continuous rise in private sector's remittance and an increase in customs revenue underpinned the growth of revenue in the review period.

Foreign Cash Grants and Loans

26. In the first two months of 2006/07, total foreign cash grants and foreign loans declined by 39.8 percent and 15.2 percent respectively in contrast to an increase of 65.8 percent and 54.3 percent respectively in the previous year.

Budget Deficit / Surplus

27. As a result of significant growth of revenue in the first two months of 2006/07, government's budgetary surplus expanded by 32.1 percent to Rs 2.8 billion in the first two months of 2006/07 compared to a lower growth of 1.7 percent last year.
28. Consequently, government's cash budget surplus with Nepal Rastra Bank went up by 22.9 percent to Rs 3.2 billion as at mid September 2006, compared to an increase of 9.0 percent in the corresponding period last year.

Foreign Trade

29. In the first two months of 2006/07, total foreign trade increased by 6.7 percent in comparison to a growth of 22.4 percent in the corresponding period of 2005/06. Exports grew by just 0.1 percent compared to an increase of 16.9 percent in 2005/06. Of the total exports, export to India rose by just 0.6 percent in 2006/07 in comparison to a significant growth of 34.7 percent in the same period of 2005/06. Exports to other countries declined by 1.0 percent in the review period compared to a decrease of 8.2 percent in the corresponding period of the previous year.
30. The deceleration in the growth rate of exports to India was attributed to the decline in the exports of polyester yarn, plastic utensils, zinc sheet, wire and cattle feed. Likewise, the decline in the exports to other countries was due to the decrease in the export of woolen carpet, silverware & jewelleryes, and handicrafts.

31. Total imports rose by 9.1 percent in the first two months of 2006/07 compared to a growth of 24.7 percent in the same period of the previous year. While imports from India went up by 11.3 percent in the review period in comparison to a higher growth of 38.0 percent in the corresponding period of 2005/06, imports from other countries rose by 5.5 percent in comparison to a growth of 7.6 percent a year ago.
32. A rise in the import of petroleum products, vehicles & parts, medicine, paper and MS billet from India and crude palm oil, medicine, aircraft spare-parts, copper wire & rod, and computer parts from other countries led to the rise in total imports in the first two months of 2006/07.
33. As per the reserve management policy of the NRB, the increase in the number of commodities for import from India on the payment of convertible currency led to the increase in such import by 10.2 percent to Rs. 2.2 billion in the first two months of 2006/07. The major commodities imported under such arrangement included hot-rolled sheet in coil, cold-rolled sheet in coil, M.S. billet, M.S. wire and industrial chemicals. In the corresponding period of the previous year, such import was of Rs 2.0 billion.
34. In the first two months of 2006/07, trade deficit rose by 14.5 percent compared to an increase of 29.9 percent in the corresponding period of 2005/06.

Balance of Payments

35. The overall BOP registered a surplus of Rs. 657.2 million in the first two months of 2006/07 compared to a surplus of Rs. 3.0 billion in the corresponding period of 2005/06.
36. Current account recorded a deficit of Rs 1.8 million in the first two months of 2006/07 compared to a deficit of Rs 2.9 billion in the corresponding period of the previous year.
37. In the first two months of 2006/07 remittances inflow increased significantly by 35.9 percent compared to a rise of 12.8 percent last year.
38. On the capital account front, Rs. 676.0 million was received as capital transfer. Under the financial account, the government received Rs. 546.4 million as foreign loan and repaid Rs. 201.9 billion in amortization.

Foreign Exchange Reserves

39. In comparison to mid-July 2006, gross foreign exchange reserves increased by 0.5 percent to Rs. 166.0 billion in mid-September 2006. Such reserves had risen by 2.8 percent in the corresponding period of the preceding year. The share of convertible reserves in the total reserves rose slightly to 95.5 percent as at mid-September 2006 from 94.7 percent in mid-September 2005, resulting in a corresponding fall in the share of the non-convertible reserves to 4.5 percent from 5.3 percent. The current level of reserves is adequate for financing merchandise imports of 11.5 months and merchandise and service imports of 9.3 months.

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

40. The price of oil (Crude Oil Brent) in the international market declined by 1.6 percent to US\$ 60.26 per barrel on September 15, 2006 from US\$ 61.25 per barrel in mid-September 2005. Likewise, the price of gold rose by 26.1 percent to US\$ 573.60 per ounce on September 15, 2006 from US\$ 454.80 a year earlier.
41. In comparison to mid-July 2006, the Nepalese currency vis-à-vis the US dollar appreciated by 0.68 percent in mid-September 2006. It had depreciated by 0.92 percent in the corresponding period of the previous year. The exchange rate of one US dollar stood at Rs. 73.60 in mid-September 2006 compared to Rs. 71.00 in mid-September 2005.