

Current Macroeconomic Situation

(Based on the First Three Months' Data of 2008/09)

Monetary Situation

Money Supply

1. Broad money (M_2) expanded by 5.0 percent in the first three months of 2008/09. M_2 had expanded by 5.5 percent in the corresponding period of the previous year. Notwithstanding the substantial growth in net foreign assets, a lower rate of growth of net domestic assets compared to the same period of the last year on account of a deceleration in net claims on government and acceleration in net non-monetary liabilities lowered down expansion of M_2 in the review period.
2. Narrow money (M_1), which had grown by 3.8 percent in the first three months of the previous year, had declined by 0.4 percent in the review period. The decline in M_1 attributed to a reduction in growth of government expenditure relative to revenue in the review period. However, time deposits increased by 7.5 percent in the review period compared to 6.3 percent growth in the same period of the previous year.
3. Net foreign assets (NFA), after adjusting foreign exchange valuation gain/loss, increased by 4.5 percent (Rs 7.7 billion) in the review period against a decline of 4.2 percent (5.6 billion) in the previous year. NFA registered a substantial growth in the review period on account of encouraging inflow of remittances and an increase in growth of foreign assistance.
4. Net non-monetary liabilities, after adjusting foreign exchange valuation gain/loss, increased by 11.2 percent in the review period in contrast to a decline of 2.6 percent in the corresponding period of the previous year. An increase in capital and reserves, on account of a higher profit of commercial banks in 2007/08 compared to 2006/07, helped increase net non-monetary liabilities at a higher rate in the review period.

Domestic Credit

5. In the first three months of 2008/09, domestic credit expanded by 6.8 percent compared to a growth of 6.9 percent in the corresponding period of the previous year. Domestic credit increased at a lower rate due to a decline in net claims on government by 1.0 percent in the review period, against an increase of 8.9 percent in the same period of the previous year.
6. Private sector credit increased by 8.6 percent in the review period, compared to a growth of 6.8 percent in the same period of the previous year. Claims on non-government financial

institutions increased by 37.9 percent (Rs 1.15 billion) compared to a growth of 14.5 percent (Rs 276 million) in the same period of previous year. Claims on non-government financial institutions increased on account of a higher credit flow to finance companies and other financial institutions by commercial banks in the review period. However, the claims on government financial institutions declined by 6.7 percent in the review period.

7. Claims on non-financial government enterprises increased by 6.2 percent (Rs 349.5 million) in the review period compared to a decline of 17.3 percent (Rs 883.6 million) in the previous year. A higher credit amount used by Janakpur Cigarette Factory Ltd, Nepal Oil Corporation, Nepal Airlines Corporation, Janak Education Material Center Ltd and Nepal Electricity Authority contributed to such an increase in the claims on non-financial government enterprises in the review period.

Deposit Mobilization and Credit Flow of Commercial banks

8. Deposit mobilization of commercial banks increased by Rs 25.2 billion (6.0 percent) in the first three months of 2008/09 amounting to Rs 446.7 billion. The total deposit had increased by Rs 13.9 billion (4.1 percent) in the corresponding period of the previous year. Both saving and fixed deposits increased by 7.3 and 8.3 percent in the review period. Such deposits had increased by 5.3 and 5.9 percent respectively in the same period of the previous year.
9. Similarly, credit to the private sector expanded by Rs 29.8 billion (8.9 percent) in the review period compared to an increase of Rs 18.8 billion (7.1 Percent) in the same period of the previous year. In the review period, credit provided to iron and steel based industries of production sector, transportation equipment production and fittings, real estate, wholesale and retail business, services and consumer sectors remained higher. However, the credit to the construction sector increased at a lower rate in the review period. The higher credit flow relative to the deposit mobilization of commercial banks led to an increase in the credit-deposit ratio from 82.6 percent as in mid-July 2007 to 85.1 percent as in mid-Oct 2008.
10. The liquid funds of commercial banks increased by 17.9 percent in the review period compared to a growth of 1.6 percent in the same period of the previous year. Of the components of liquid funds, commercial banks' balance held with the NRB increased by 38.1 percent in contrast to a decline of 10.7 percent in the same period of the previous year. Likewise, commercial banks' balance held abroad increased by 6.0 percent amounting to Rs 43.6 billion compared to a growth of 2.8 percent to Rs 41.1 billion in the previous year.

Liquidity Management

11. The NRB mopped up net liquidity of Rs 9.0 billion from the secondary market in the review period. Of the total liquidity mopped up, Rs 3.5 billion was mopped up from outright sale auction and Rs 5.5 billion through reverse repo auction. Total liquidity mopped up from the secondary market in the same period of the previous year was Rs 5.6 billion. However, contrary to the same period of the previous year, liquidity had not been injected through open market operations (OMO_s) in the review period.
12. In the first three months of 2008/09, the NRB injected net liquidity of Rs 30.7 billions by net purchasing of 420.1 million US dollar from commercial banks through foreign exchange intervention. A net liquidity of Rs 14.0 billion was injected through the net purchase of 217.5 million US dollar from commercial banks in the same period of the previous year. A higher intervention in the foreign exchange market in the review period was required on account of a substantial inflow of remittances.
13. The NRB purchased Indian currency (IC) of IRs 11.9 billion through the sale of 270 million US dollar in the Indian money market in the first three months of 2008/09. IC of IRs. 12.9 billion was purchased through the sale of 320 million US dollar in the corresponding period of the previous year. Despite a widening trade deficit with India in the review period, a depreciation of IC vis-à-vis the US dollar in the review period accounted for a smaller sale of the US dollar for IC purchase in contrast to the same period of the previous year.

Standing Liquidity Facility and Inter Bank Transactions

14. Commercial banks used standing liquidity facility (SLF) of Rs 32.0 billion in the review period. The use of the SLF by commercial banks was Rs 13.8 billion in the corresponding period of the previous year. Likewise, commercial banks' inter bank transactions stood at Rs 68.3 billion in the review period compared to that of Rs 101.9 billion in the same period of the previous year.

Short-term Interest Rates

15. The weighted average monthly 91-day Treasury bill rate stood at 6.08 percent in mid-Oct 2008 compared to 2.35 percent in mid-Oct 2007. The weighted average monthly inter bank rate increased to 5.16 percent in mid-Oct 2008 from 3.35 percent in mid-Oct 2007. The short-term market interest rate increased as an effect of a higher liquidity mop up in the review period compared to the same period of the previous year. Likewise, the maximum interest rate on saving deposits increased by 0.25 percentage points in mid-Oct, 2008, to 6.75 percent.

Securities market

16. The year on year (y-o-y) NEPSE index increased by 8.4 percent to 933.97 points in mid-October 2008. This index was 861.37 a year ago. Likewise NEPSE sensitive index (based on July 2006) stood at 256.01 in mid-October 2008. This index was 225.82 in Mid-October 2007.
17. The NEPSE float index calculated on the basis of final transaction as of August 24, 2008 (at market price), remained 91.82 in mid October 2008.
18. The y-o-y market capitalization increased by 83.9 percent to Rs. 487.85 billion in mid-October 2008. Market capitalization to GDP ratio increased to 51.6 percent from 32.3 percent a year ago. Of the total market capitalization, bank and financial institutions, manufacturing and processing companies, hotels, business entities, hydropower and other economic sectors accounted for 71.4 percent, 1.6 percent, 1 percent, 0.3 percent, 4.6 and 21.3 percent respectively.
19. Total paid up capital of the listed companies stood at Rs. 46.1 billion in mid-October 2008 which had increased by 103 percent over the period of one year. This increase was largely due to the additional listing of securities. Of the total listed share, Nepal Stock Exchange Ltd., of Rs. 19.8 billion upto Mid-October 2008, bonus share, right share, ordinary share and bonds accounted for Rs. 104.2 million, Rs. 1.6 billion, Rs.15.5 billion and Rs. 2.7 billion respectively were listed. The ordinary share constituted the largest portion largely due to the share of Nepal Telecom.
20. The monthly turnover to market capitalization ratio remained at 0.40 percent in mid-October 2008 compared to 0.76 percent a year ago.
21. The total number of companies listed at the NEPSE increased to 144 in mid-October 2008, from 140 a year ago. Among the currently listed companies, 113 are bank and financial institutions (including insurance companies). Production and processing industries, hotels, business entities, hydropower and companies in other groups are 18, 4, 4, 3 and 2 respectively.
22. The twelve-months rolling standard deviation reflecting an increased volatility in the stock market. This stood at 112.4 in mid-October 2008 compared to that of 136.3 a year ago.

Consumer Price Inflation

23. The y-o-y inflation as calculated by the consumer price index rose to 14.1 percent in mid-October 2008 from 6.3 percent in the previous year. The inflation, in the review period, was driven both by the significant rise in food and beverages (15.2 percent) as well as non-food and services (12.9 percent) group. Last year's the price rise of food and beverages and non-food and services group, was 9.5 percent and 2.9 percent respectively.
24. Of the items in the food and beverages group, price indices of sugar and sugar related products as well as oil and ghee sub-groups increased on a y-o-y basis in mid-October 2008, by a whopping rate of 39.5 percent and 35.4 percent respectively. This is in sharp contrast to last year's increase of -18.4 percent and 12.8 percent respectively. The sub-group of grains and cereal products witnessed a y-o-y price rise of 21.3 percent in the review period compared to an increase of 11.2 percent in the corresponding period of previous year. Prices of rice and rice products of this sub-group increased with higher rate of 25.1 percent compared to an increase of 12.3 percent a year ago. The indices of pulses, meat, fish and eggs, restaurant meals, milk and milk products and spices rose up by 24.7 percent, 22.0 percent, 17.2 percent, 16.7 percent and 13.4 percent respectively in the review period compared to a rise of 14.6 percent, 5.3 percent, 4.2 percent, 5.9 percent and 7.3 percent respectively in mid-October 2007.
25. Within the group of non-food and services, the index of transport and communication, housing goods and services as well as tobacco and related products rose by 23.1 percent, 18.3 percent and 12.7 in mid-October 2008 compared to a rise of -0.5 percent, 2.5 percent and 3.2 percent respectively during the same period of last year.
26. Region-wise, the price rise in Kathmandu valley was 14.5 percent followed by 14.0 percent in Terai and 13.9 percent in the Hills. Last year, the respective rates were 6.1 percent, 6.5 percent and 6.1 percent.
27. In the review period, the y-o-y core inflation rose to 13.1 percent from 4.7 percent a year ago.

Wholesale Price Inflation

28. The y-o-y wholesale price inflation moderated to 9.3 percent in mid-October 2008 compared to 10.3 percent a year ago. Such moderation was mainly due to the decline in the price of cash crops and fruits and vegetables under agricultural commodities group in spite of high increase in the price of imported commodities. The index of domestic

manufactured commodities and imported commodities increased by 15.7 percent and 23.3 percent respectively in the review period as compared to 8.0 percent and 5.1 percent a year ago. However the price of agricultural commodities declined by 0.5 percent in the review period as compared to a rise of 14.1 percent during the same period of last year.

29. Of agricultural commodities, the price index of pulses, livestock production, food grains and spices increased by 26.6 percent, 18.3 percent, 15.1 percent and 10.4 percent respectively in the review period compared to a rise of 13.0 percent, 3.8 percent, 7.4 percent and 1.1 percent a year ago. On the other hand, the price index of cash crops and fruits and vegetables declined by 27.8 percent and 21.3 percent respectively in the review period compared to an increase of 8.3 percent and 41.7 percent respectively in the corresponding period of previous year.
30. Within the group of domestic manufactured commodities, the price index of food-related products and construction materials increased by 21.5 percent and 18.9 percent respectively in mid-October 2008 compared to a rise of 5.9 percent and 15.5 percent a year ago.
31. Of imported commodities, the price index of petroleum products and coal increased by a whopping rate of 39.4 percent on a y-o-y basis in mid- October 2008 compared to an increase of 1.9 percent a year ago. Likewise, the price indices of transport vehicles and machinery goods as well as chemical fertilizers and chemical goods also increased by 30.4 percent and 6.5 percent respectively in the review period compared to a rise of 5.1 percent and 16.4 percent in the corresponding period of previous year.

National Salary and Wage Rate

32. The overall y-o-y salary and wage rate index rose by 9.1 percent in mid-October 2008 compared to a rise of 11.9 percent a year ago. Of the salary and wage rate indices, the salary index remained unchanged in the review period compared to a rise of 10.9 percent in the corresponding period of the previous year. The y-o-y wage rate index increased by 12.2 percent in the review period compared to an increase of 12.4 percent in the same period of the previous year. Wages of agricultural, industrial and construction laborers increased by 19.0 percent, 2.5 percent and 10.1 percent respectively in the review period. Last year, these wage rates had increased by 8.3 percent, 19.5 percent and 10.3 percent respectively.

Fiscal Situation

Budget Deficit / Surplus

33. In the first three months of 2008/09, the government budget deficit stood at Rs.2.9 billion compared to a deficit of Rs 9.4 billion in the corresponding period of the previous year. An increase in revenue and foreign cash grants along with a reduction in government expenditure, accounted for such a reduction in budget deficit in the review period.

Government Expenditure

34. In the first three months of 2008/09, the total government spending decreased by 2.4 percent to Rs. 29.3 billion compared to an increase of 53.7 percent in the corresponding period of the previous year. The reduction of such spending was due to a decline in recurrent as well as capital expenditure.

35. In the first three months of 2008/09, recurrent expenditure decreased by 13.2 percent to Rs.18.5 billion. In the corresponding period of the previous year, recurrent expenditure had increased by 35.6 percent. A significant amount was spent for the preparation of the Constitution Assembly Election in the previous year, there was no occurrence of such expenditure in the current year which accounted for such a decline in recurrent expenditure in the review period.

36. In the first three months of 2008/09 principal repayment expenditure increased by 20.8 percent to Rs.4.2 billion mainly on account of the payment of treasury bills amounting to Rs.2.8 billion.

Government Revenue

37. In the first three months of 2008/09, revenue mobilization of the government grew by 16.0 percent to Rs.22.3 billion compared to an increase of 18.8 percent in the corresponding period of the previous year.

38. In the review period, income tax, VAT revenue and registration fee recorded a higher growth whereas customs, excise and vehicle tax revenue recorded a lower growth compared to that of the corresponding period of the previous year. Moreover, non-tax revenue witnessed a decline of 59.7 percent.

Foreign Cash Loans and Grants

39. The government received foreign cash loans of Rs 936.7 million and foreign cash grants of Rs 2.5 billion in the first three months of 2008/09. The government had received foreign cash loans of Rs 845.7 million and foreign cash grants of Rs 1.2 billion in the corresponding period of the previous year.
40. The government did not mobilize any domestic borrowing in the review period.

Foreign Trade

41. In the first three months of 2008/09, exports went up by 27.1 percent in compared to a rise of just 4.3 percent in the corresponding period of the previous year. Of the total exports, export to India increased by 10.1 percent in 2008/09 compared to an increase of 0.6 percent in the same period of 2007/08. Exports to other countries soared by 58.3 percent compared to an increase of 11.9 percent in the same period of the previous year.
42. The rise in the exports to India was attributed to the upsurge in the exports of readymade garments, shoes & sandals, polyster yarn, copper wire rod and G.I. pipe. Likewise, the rise the exports to other countries was ascribed to the upsurge in the exports of pulses, woolen carpets, pashmina, herbs and tanned skin.
43. Total imports increased by 30.6 percent in the first three months of 2008/09 compared to a lower increase of 13.1 percent in the corresponding period of the previous year. Imports from India augmented by 19.3 percent in the review period compared to a growth of 13.7 percent in the corresponding period of 2007/08, imports from other countries expanded by 48.5 percent compared to a growth of just 12.1 percent.
44. An increase in the import of petroleum products, vehicles & spare parts, cold rolled sheet in coil, hot rolled sheet in coil and cement, among others, from India and gold, MS billet, telecommunication equipment & parts, computer & parts and polythene granules, among others, from other countries led to the surge in total imports in the first three months of 2008/09.

Balance of Payments

45. The overall BOP recorded a surplus of Rs. 7.7 billion in the first three months of 2008/09 in contrast to a deficit of Rs. 5.6 billion in the corresponding period of the previous year. The current account also posted a surplus of Rs. 8.8 billion in the first three months of 2008/09 as against a deficit of Rs. 6.6 billion in the corresponding period of the previous

year. Such current account surplus was primarily attributed to the surge in net transfers by 75.5 percent in the first three months of 2008/09. Under transfers, workers' remittances soared by 80.7 percent in the first three months of 2008/09 compared to a growth of only 17.2 percent in the corresponding period of the previous year.

Foreign Exchange Reserves

46. The gross foreign exchange reserves stood at Rs. 230.8 billion in mid-October 2008, an upsurge by 8.5 percent compared to the level as at mid-July 2008. Such reserves had gone down by 4.1 percent in the corresponding period of the preceding year. In terms of US dollar, gross foreign exchange reserves declined by 3.9 percent to US\$ 3.0 billion in mid-October 2008. In the same period in the previous year, such reserves had gone down by 1.6 percent. The current level of reserves is adequate for financing merchandise imports of 10.1 months and merchandise and service imports of 8.0 months.

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

47. The price of oil (Crude Oil Brent) in the international market declined by 23.2 percent to US\$ 64.02 per barrel in mid-October, 2008 from US\$ 84.14 per barrel in mid-October, 2007. Similarly, the price of gold rose by 5.2 percent to US\$ 802.50 per ounce in mid-October, 2008 from US\$ 762.50 per ounce a year earlier.

48. In comparison to mid-July 2008, the Nepalese currency *vis-à-vis* the US dollar depreciated by 11.50 percent in mid-October 2008. It had appreciated by 2.6 percent in the corresponding period of the previous year. The exchange rate of one US dollar stood at Rs. 77.40 in mid-October 2008 compared to Rs. 68.50 in mid-July 2008.