Current Macroeconomic Situation
(Based on the Eight Months' Data of 2009/10)

Monetary Situation

Money Supply

1. Broad money (M_2) expanded by 6.8 percent in the first eight months of 2009/10. M_2 had expanded by 13.7 percent in the corresponding period of the previous year. Narrow money (M_1), which had grown by 11.9 percent during the first eight months of 2008/9, grew by 4.6 percent in the review period. Despite a high growth of net domestic assets, decline in net foreign assets accounted for such a deceleration of monetary aggregates in the review period.

2. Of the components of narrow money, currency in circulation increased by 11.4 percent in the review period compared to an increase of 21.9 percent during the same period of the previous year. Demand deposits, which had declined by 6.6 percent in the first eight months of 2008/09, declined by 7.5 percent in the review period. Time deposits increased by 7.8 percent in the review period compared to a growth of 14.5 percent during the same period of the previous year.

3. Net foreign assets (NFA), after adjusting foreign exchange valuation gain/loss, declined substantially by Rs.23.5 billion in the review period. It had increased by Rs.34.8 billion in the same period of the previous year. An acceleration in trade deficits in the review period accounted for such a significant decline in net foreign assets.

Domestic Credit

4. In the first eight months of 2009/10, domestic credit expanded by 10.2 percent compared to a growth of 7.5 percent in the corresponding period of the previous year. Domestic credit increased at a higher rate on account of a significant increase in credit to private sector.

5. Net claims on government declined by 13.1 percent (Rs.13.7 billion) in the review period compared to a decline of 23.1 percent (Rs.20.1 billion) in the corresponding period of the previous year. An increase in resource mobilization relative to government expenditure contributed to a surplus in budget and hence a decline in claims on government in the review period. The government deposits as at mid-March 2010 stood at Rs. 823.1 million.

6. In the review period, claims on private sector increased by 16.5 percent (Rs. 71.9 billion) compared to a growth of 14.9 percent (Rs. 50.5 billion) in the same period a year ago.

7. Claims on non-government financial enterprises declined by 29.3 percent in the review period in contrast to a growth of 70.1 percent in the corresponding period of the previous year. The decline in investments of commercial banks on finance companies, pension funds, and insurance companies in the review period accounted for such a decline in credit to non-government financial enterprises.

8. In the first eight months of 2009/10, claims on non-financial government enterprises increased by 3.1 percent compared to a growth of 5.3 percent in the corresponding period of the previous year. Repayment of loans by National Trading Ltd., Nepal Airlines Corporation, Janak Education Material Centre Ltd., and Nepal Electricity Corporation attributed to a slow down in such credit in the review period.

Deposits Mobilization and Credit Flow of Commercial banks

9. In the first eight months of 2009/10, deposits mobilization of commercial banks increased by 4.2 percent (Rs.22.9 billion) amounting to Rs. 572.7 billion as at mid-March 2010. The total deposits had increased by 14.3 percent (Rs.60.2 billion) in the corresponding period of the previous year. Similarly, private sector credit of commercial banks grew by 16.5 percent (Rs.66.7 billion) compared to a growth of 16.3 percent (Rs 50 billion) in the corresponding period of the previous year.

10. Of the private sector credit, credit to the production sector increased by 9.5 percent in the review period compared to a growth of 12 percent in the same period of the previous year. Sugar, Cement as well as Iron and Steel industries witnessed a significant credit expansion under the **industrial** production sector credit. Similarly, credit to agriculture sector increased by Rs. 2 billion in the review period. In the review period, credit to wholesale and retail business as well as finance, insurance and fixed assets; and service sectors increased by 23.2 percent, 41.6 percent and 20.2 percent respectively. Credit to these sectors during the corresponding period in the previous year had increased by 10.1 percent, 23.6 percent and 11.9 percent respectively. Credit to real estate sector increased by Rs.14.9 billion in the first eight months of 2009/10 compared to Rs.7.7 billion in the same period a year ago.

Liquidity position of Commercial Banks

11. The liquid assets of the commercial banks stood at Rs. 167.9 billion as at mid-March 2010. Of the components of liquid assets, liquid fund declined by 9.7 percent. A decline in commercial banks' balance with the NRB as well as balance held abroad accounted for a contraction of liquid funds of commercial banks. In the review period, the balance held abroad declined by Rs. 4.3 billion amounting to Rs. 49.2 billion while the balance with NRB declined by Rs. 10.1 billion. Similarly, commercial bank' investments in government securities declined by 12.3 percent (Rs. 8.8 billion) in the review period.

12. The higher growth of commercial banks' loans and advances relative to their deposit mobilization changed their liabilities/assets structure. Loans and advances of commercial banks increased by 11.8 percent (Rs 60.9 billion) in the review period. As a result, the credit-deposit ratio increased to 90.2 percent in mid-March 2010 from 81.2 percent in mid-July 2009. Similarly, the liquidity-deposit ratio declined to 29.3 percent in mid-March 2010 from 34.2 percent in mid-July 2009.

Liquidity Management

13. In the first eight months of 2009/10, NRB injected net liquidity amounting to Rs.69.1 billion. During this period, Rs.7.4 billion and Rs.1.0 billion were mopped up through outright sale auction and reverse repo auction respectively, while Rs. 74.2 billion and Rs. 3.4 billion were injected through repo and outright purchase auction respectively. In the same period of the previous year, net liquidity amounting to Rs.11.7 billion was mopped up. Of the total liquidity mopped up, Rs.7.5 billion and Rs. 13.2 billion were mopped up through outright sale auction and reverse repo auction respectively, while Rs. 9 billion was injected through outright purchase auction.

14. In the first eight months of 2009/10, NRB injected net liquidity amounting to Rs. 55.2 billions through net purchase of USD 733.2 million from commercial banks. A net liquidity of Rs. 97.2 billion was injected through the net purchase of USD 1.3 billion in the same period last year.

15. The NRB purchased Indian currency equal to 63.6 billion through the sale of USD 1.4 billion in the Indian money market during the review period. Indian currency equal to 47.8 billion was purchased through the sale of USD 1 billion in the corresponding period of the previous year. An accelerated trade and payment deficits with India accounted for such a higher volume of Indian currency purchase in the review period.

Standing Liquidity Facility and Inter Bank Transactions

16. Inter-bank transactions of commercial banks stood at Rs.188.5 billion in the first eight months of 2009/10 compared to Rs.193 billion in the corresponding period of the previous year. Likewise, commercial banks used standing liquidity facility (SLF) amounting to Rs.85.2 billion in the review period. The use of the SLF by commercial banks had amounted to Rs.83.2 billion in the corresponding period of the previous year.

Interest Rates

17. The weighted average 91-day Treasury bill rate stood at 7.79 percent in the eighth month of 2009/10 compared to 6.83 percent in the eighth month of the previous year. Similarly, the weighted average inter-bank rate increased to 8.85 percent in the eighth month of 2009/10 compared to 6.38 percent in the eighth month of the previous year. In addition to the short-term interest rates, the deposits rate of commercial banks also increased in the review period. The maximum interest rate of two-year and more than two years' fixed deposits increased from 9.5 percent as at mid-July 2009 to 13 percent as at mid-March 2010. The shortfall of liquidity in the banking system contributed to increase the interest rates in the review period.

Securities market

18. The year on year (y-o-y) NEPSE index declined by 27.1 percent to 486.25 points in the first eight months of 2009/10. This index stood at 667.20 in the same period last year. Likewise, NEPSE sensitive index (based on July 2006) stood at 118.68 point in mid March, 2010 as against 176.90 point in the same period last

year. The NEPSE float index, calculated on the basis of final transaction as of August 24, 2008 (as base market value), remained at 45.93 in mid March 2010, a contraction of 28.4 percent compared to the same period last year.

19. The y-o-y market capitalization declined by 6.5 percent to Rs. 376.0 billion in mid March 2010. The ratio of market capitalization to GDP stood at 34.7 percent in the review period. It was 41.9 percent in the same period last year. Of the total market capitalization, bank and financial institutions accounted for 73.6 percent followed by manufacturing and processing companies (2.1 percent), hotels (1.3 percent), business entities (0.4 percent), hydropower (4.7 percent) and other economic sectors (18.0 percent).

20. Total paid up capital of the listed companies stood at Rs. 73.88 billion in mid March 2010, an increase of 43.85 percent over the period of one year. This increase was largely due to the additional listing of securities at the NEPSE. As at the eighth month of 2009/10, additional securities worth Rs.17.41 billion (ordinary share of Rs.3.55 billion, bonus share of Rs. 2.59 billion, right share of Rs.5.52 billion and government securities of Rs.5.75 billion) were listed at the NEPSE.

21. Total number of companies listed at the NEPSE increased to 168 in mid March 2010 compared to 152 during the same period last year. Among them, 136 are banks and financial institutions (including insurance companies), followed by production and processing industries (18), hotels (4), business entities (4), hydropower (4) and companies in other groups (2).

Inflation

Consumer Price Inflation

22. The year on year (y-o-y) inflation as measured by the consumer price index moderated to 11.2 percent in mid-March 2010 compared to 13.1 percent increase in the same period last year. In the review period, the price index of food and beverages group increased by 15.7 percent whereas the index of non-food and services group rose only by 5.9 percent. The index of food and beverages and non-food and services group had risen by 17.1 percent and 8.8 percent respectively in the same period last year.

23. Of the items in the food and beverage group, price indices of sugar and sugar related products increased by 61.0 percent compared to an increase of 53.0 percent in the same period last year. Similarly, the price indices of spices, pulses, meat, fish and eggs as well as restaurant meal increased respectively by 33.7 percent, 29.6 percent, 23.8 percent and 17.3 percent in the review period compared to their respective increase of 10.9 percent, 24.6 percent, 25.2 percent and 19.3 percent in the same period last year. The index of grains and cereal products also witnessed an increase of 12.3 percent compared to an increase of 13.0 percent in the corresponding period of the previous year.

24. Within non-food and services group, the index of both tobacco and related products as well as education, reading and recreation each increased by 11.1 percent during the review period compared to their respective increase of 16.3 percent and 8.3 percent during the same period last year.

25. Region-wise, the price index of Hills rose by 12.5 percent followed by 11.3 percent in Terai and 10.2 percent in Kathmandu Valley in the review period. The respective rates were 12.4 percent, 13.3 percent and 13.4 percent during the same period last year.

Wholesale Price Inflation

26. During the review period, the y-o-y wholesale price inflation increased by 12.2 percent compared to a rise of 12.3 percent a year ago. The indices of agricultural commodities , domestic manufactured commodities and imported commodities increased by 19.2 percent,12.1 percent and 1.2 percent respectively in the review period compared to 15.3 percent, 8.8 percent and 10.0 percent increase, a year ago.

27. Within the agricultural commodities group, the price index of spices, livestock production, pulses and foodgrains respectively increased by 36.4 percent, 35.5 percent,33.7 percent and 22.2 percent compared to an increase of 9.2 percent, 23.2 percent, 15.4 percent and 4.5 percent respectively during the same period last year.

28. Within the group of domestic manufactured commodities, the price index of food-related products increased by 18.5 percent compared to a rise of 7.7 percent a year ago. Within the imported commodities group, the price indices of chemical fertilizers and chemical goods declined by 11.9 percent in the review period compared to an increase of 8.1 percent in the corresponding period of the previous year.

National Salary and Wage Rate

29. The overall y-o-y salary and wage rate index rose by 13.7 percent in the review period compared to a rise of 19.3 percent a year ago. Of the salary and wage rate indices, the salary index increased by 13.8 percent in the review period compared to a rise of 16.8 percent in the same period of the previous year. The increase in basic salary and allowances by the government of Nepal for civil servants and its simultaneous effect on salary of the private sector contributed to such an increase in salary index. The wage rate index increased by 13.6 percent in the review period compared to an increase of 20.1 percent in the same period of the previous year. Wages of agricultural, industrial and construction laborer increased by 17.0 percent, 8.8 percent and 10.6 percent respectively in the review period. These wage rates had increased by 26.9 percent, 10.6 percent and 18.1 percent respectively in the same period last year.

Fiscal Situation*

Budget Deficit / Surplus

30. In the first eight months of 2009/10, government budget surplus on cash basis stood at Rs.4.94 billion compared to a surplus of Rs 11.30 billion in the corresponding period of the previous year.

* Based on the reports of 40 and 25 branches of RBB and NBL out of their 65 and 42 respective branches performing government transaction in addition to the Nepal Rastra Bank, Everest Bank Ltd. and Nepal Bangladesh Bank Ltd.

Government Expenditure

31. In the review period, total government spending increased by 32.4 percent to Rs.121.43 billion compared to an increase of 14.2 percent in the corresponding period of the previous year. The high growth in recurrent as well as capital expenditure accounted for such an increase in the government expenditure.

32. In the review period, recurrent expenditure increased by 29.3 percent to Rs.79.37 billion. In the corresponding period of the previous year, the recurrent expenditure had increased by 20.1 percent. An upward revision in the salary and allowances of the civil servants and teachers by the Government of Nepal mainly attributed to such a rise in the recurrent expenditure. Likewise, increasing expenditure on special security plan, growing amount of subsidies to public school and increment in the distribution of economic assistance expenditure accounted for such a rise in the recurrent expenditure.

33. In the review period, capital expenditure increased by 53.3 percent to Rs.22.45 billion in contrast to a decline of 15.9 percent in the corresponding period of the previous year. However, such amount of capital expenditure accounted for only 21.1 percent of the budget estimate. Delay in the approval of budget, lingering in the contract process, absence of representatives in local bodies as well as weak law and order situation in the country are mainly responsible for the lower than expected performance of capital expenditure in the review period.

34. In the first eight months of 2009/10, principal repayment expenditure declined by 6.9 percent to Rs.9.44 billion. In the corresponding period of the previous year, such expenditure had increased by 7.3 percent.

Government Revenue

35. In the review period, revenue mobilization of the government grew by 25.6 percent to Rs.105.58 billion compared to an increase of 38.6 percent in the corresponding period of the previous year. A positive impact of "Tax Compliance year", increase in PAN number holders, mobilization of tax volunteers, growth in imports, control in revenue leakages and tax administration reforms mainly contributed to such an increase in the revenue mobilization.

36. Of the total revenue mobilization, Value Added Tax (VAT) grew by 43.5 percent to Rs.33.63 billion in mid March 2009. It had increased by 20.1 percent in the corresponding period of the previous year.

37. In the review period, custom revenue rose by 43.0 percent to Rs.21.91 billion compared to an increase of 19.3 percent in the same period of the previous year. Reforms in custom administration and the increase in imports of high tax yielding vehicles and spare parts contributed to such a high growth of customs revenue.

38. In the review period, excise revenue increased by 65.0 percent to Rs.14.84 billion compared to an increase of 41.4 percent in the same period of the previous year. Reforms in excise administration and increase in the imports of high excise tax yielding vehicles accounted for such a growth of excise revenue in the review period.

39. Income tax revenue increased by 20.7 percent to Rs.17.52 billion in the review period. In the corresponding period last year such revenue had risen by 42.6 percent. A positive impact of tax compliance year and increase in PAN number holders accounted for such an increase in the income tax revenue mobilization.

40. In the review period, non-tax revenue declined by 29.2 percent to Rs.12.0 billion compared to an increase of 96.0 percent in the same period of the preceding year.

Foreign Cash Loans and Grants

41. The government received foreign cash loans amounting to Rs.2.53 billion and foreign cash grants amounting to Rs.15.74 billion in the first eight months of 2009/10. In the corresponding period of the previous year, the government had received foreign cash loans and foreign cash grants amounting to Rs.2.87 billion and Rs.15.64 billion respectively.

External Sector

Foreign Trade

42. Nepal's merchandise exports during the first eight months of 2009/10 declined by 8.0 percent to Rs. 40.41 billion in contrast to a growth of 16.2 percent in the corresponding period of 2008/09. On a monthly basis, the merchandise exports, however grew by 8.9 percent in Feb/Mar as against a decline of 0.8 percent in the corresponding month of the previous year.

43. In terms of destination, exports to India dropped by 2.9 percent in the first eight months of 2009/10 as against a growth of 3.7 percent in the corresponding period of the previous year. Likewise, exports to other countries plummeted by 16.0 percent as against a growth of 42.9 percent in the same period of the previous year. The drop in the exports to India was mainly ascribed to the decrease in the exports of readymade garments, zinc sheet, plastic utensils, pulses and GI pipe among others. Likewise, exports to other countries decreased considerably due mainly to the decline in the export of pulses, woolen carpet, readymade garments, silverware and jewelleries and herbs among others.

44. The merchandise imports, on the other hand, grew by 43.9 percent to Rs. 253.74 billion in the first eight months of 2009/10 compared to a growth of 26.3 percent in the corresponding period of the previous year. On a monthly basis, the growing trend of the merchandise imports continued during the month of Feb/Mar. During this month, the merchandise imports soared by 57.6 percent compared to a growth of 30.5 percent in the same month of the previous year.

45. Imports from India grew by 38.5 percent in the review period compared to a growth of 12.1 percent in the corresponding period of the previous year. Likewise, imports from other countries grew at the same rate of the previous year i.e., by 50.9 percent. The growth in the import of vehicles and spare parts, M.S. billet, M.S. wire and rods, hot rolled sheet incoil and electrical equipment among others, from India and gold, telecommunication equipment and parts, other machinery and parts, steel rod and sheet and polythene granules among others, from other countries contributed significantly in the rise of total imports in the review period.

46. Total trade deficit during the first eight months of 2009/10 expanded by 61.2 percent to Rs. 213.33 billion. Trade deficit had risen by 30.1 percent in the corresponding period of the previous year. Trade deficit with India rose by 53.8 percent in the review period compared to a growth of 15.6 percent in the corresponding period of the previous year. Likewise, trade deficit with other countries expanded by 70.1 percent compared to a growth of 53.4 percent in the corresponding period of the previous year.

47. As a result of the slowdown in exports and accelerated import growth, the ratio of export to import dropped to 15.9 percent in the first eight months of 2009/10 from 24.9 percent a year earlier.

Balance of Payments

48. In the first eight months of 2009/10, the overall BOP recorded a deficit of Rs. 23.53 billion as against a surplus of Rs. 34.81 billion in the corresponding period of the previous year. The current account also registered a deficit of Rs. 32.58 billion as against a surplus of Rs. 28.94 billion in the corresponding period of the previous year. The increase in trade deficit and the slowdown in the growth of remittance inflows resulted for such deficit in the current account.

49. In the first eight months of 2009/10, the FOB-based merchandise trade deficit grew by 62.9 percent to Rs. 206.07 billion compared to a growth of 29.5 percent in the corresponding period of the previous year. The transfer account registered a surplus of Rs. 175.51 billion in the review period compared to a surplus of Rs. 157.52 billion a year ago. Under the transfers subgroup, grants declined by 11.9 percent to Rs. 15.52 billion while pension receipts rose by 74.9 percent to Rs. 17.77 billion. Likewise, the workers' remittances increased only by 9.9 percent to Rs. 143.96 billion compared to its significant growth of 58.9 percent in the corresponding period of the previous year. On a monthly basis, the remittance inflows however dropped by 9.1 percent in Feb/March in contrast to a growth of 61.0 percent in the same month of the previous year.

Foreign Exchange Reserves

50. The gross foreign exchange reserves dropped by 15.6 percent to Rs. 236.34 billion in mid-March 2010 from a level of Rs. 279.99 billion as at mid-July 2009 as against a growth of 27.4 percent in the corresponding period of the previous year. Of this, NRB's reserve declined by 17.1 percent to Rs. 185.91 billion from a level of Rs. 224.19 billion a year earlier. The gross foreign exchange reserves in dollar terms declined by 9.0 percent to USD 3.26 billion in mid- March 2010 as against a growth of 5.7 percent in the corresponding period of the previous year. The widening of the current account deficit resulted in the drawdown of foreign exchange reserves in the review period. The current level of reserves is sufficient for financing merchandise imports of 7.6 months and merchandise and service imports of 6.6 months.

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

51. The price of oil (Crude Oil Brent) in the international market went up by 75.8 percent to USD 79.43 per barrel in mid-March 2010 from USD 45.18 per barrel in mid-March 2009. Similarly, the price of gold also surged by 19.2 percent to USD 1106.25 per ounce in mid- March 2010 from USD 928 a year earlier.

52. Compared to mid-July 2009, the Nepalese currency vis-à-vis the US dollar appreciated by 7.80 percent in mid-March 2010. It had depreciated by 17.02 percent in the corresponding period of the previous year. The exchange rate of one US dollar stood at Rs. 72.40 in mid-March 2010 compared to Rs. 78.05 in mid-July 2009.