

## **Current Macroeconomic Situation**

*(Based on the first seven months data of 2008/09)*

### **Monetary Situation**

#### **Money Supply**

1. Broad money ( $M_2$ ) grew by 11.5 percent in the first seven months of 2008/09 compared to a growth of 10.8 percent in the corresponding period of the previous year. A significant growth of net foreign assets in the review period accompanied by a decline in net non-monetary liabilities was responsible for the higher growth of  $M_2$  in the review period compared to that of the previous year.
2. Narrow money ( $M_1$ ) grew by 10.8 percent in the review period.  $M_1$  had grown by 6.1 percent in the corresponding period of the previous year. Though demand deposits, one of the components of  $M_1$ , declined in the review period,  $M_1$  registered a higher growth on account of a substantial growth of currency in circulation. Such currency increased by 18.4 percent in the review period compared to a growth of 8.2 percent in the corresponding period of the previous year. Time deposits grew by 11.9 percent in the review period compared to a growth of 12.9 percent in the corresponding period of the previous year.
3. Net foreign assets (NFA), after adjusting foreign exchange valuation gain/loss, increased by Rs. 25.7 billion (15.0 percent) in the review period compared to a muted growth of Rs. 251.1 million in the same period of the previous year. An elevated inflows of remittance accompanied by an expansion in foreign assistance of the Government of Nepal (GON) contributed to a significant growth of net foreign assets in the review period.

#### **Domestic Credit**

4. In the first seven months of 2008/09, domestic credit expanded by 6.2 percent compared to a growth of 12.6 percent in the corresponding period of the previous year. A decline in net claims on government by 20.2 percent (Rs 17.6 billion) on account of a higher resource mobilization relative to the expenditure of the GON in the review period, leading to a cash deposits of Rs. 24.0 billion with Nepal Rastra Bank (NRB) and a slowdown in private sector credit contributed to a lower growth of domestic credit in the review period.
5. Claims on non-financial government enterprises increased by 8.3 percent (Rs. 466.6 million) in the review period compared to a muted growth of such credit by 0.8 percent (Rs 40.3 million) in the corresponding period of the previous year. A higher use of credit by Janakpur Cigarette Factory Ltd., Nepal Airlines Corporation, Janak Education Material Center Ltd. and Nepal Electricity Authority contributed to the increase in the claims on such enterprises in the review period.
6. Claims on financial institutions grew by 1.1 percent (Rs 50.0 million) in the review period compared to a growth of 57.1 percent (Rs 3.6 billion) in the corresponding period of the previous year. A subdued growth of credit to the financial institutions is ascribed to a slowdown in commercial banks' short-term investment in development banks and finance companies in the review period.

7. The private sector credit remained marginally lower in the review period compared to that of the previous year. The credit to the private sector increased by Rs 44.0 billion (12.9 percent) in the review period compared to an increase of Rs 44.8 billion (16.4 percent) in the corresponding period of the previous year. A removal of credit disbursed to small farmers and micro enterprise entrepreneurs by government-owned commercial banks from their private sector credit outstanding on account of government's decision to waive such loans contributed to a lower growth of private sector credit in the review period.

### **Deposit Mobilizations and Credit Flow of Commercial Banks**

8. In the first seven months of 2008/09, deposit mobilization of commercial banks increased by Rs 50.8 billion (12.0 percent) amounting to Rs 472.3 billion as in mid-February 2009. Deposit mobilization of commercial banks had increased by Rs 36.4 billion (10.9 percent) in the corresponding period of the previous year. In the review period, saving and fixed deposits increased by 13.7 percent and 14.8 percent respectively. Such deposits had increased by 11.1 percent and 12.6 percent respectively in the corresponding period of the previous year.
9. The review period witnessed a slowdown in credit flow of commercial banks to the private sector. In the review period, credit to the private sector from commercial banks expanded by Rs 44.6 billion (13.2 percent) compared to an increase of Rs 49.5 billion (18.7 percent) in the corresponding period of the previous year. The review period experienced a slowdown in credit flow to production, construction, metal production, machinery and electric tools, wholesale and retail business and service industries, while transportation equipment production and fittings, real estate and consumable loans while credit to agricultural sector declined in the review period.
10. The liquid funds of commercial banks grew by 11.8 percent in the review period compared to a growth of 5.1 percent in the previous year. An elevated inflow of remittances contributed to an increase in liquid funds of commercial banks. Of the components of liquid funds, commercial banks' balance with the NRB increased by 9.9 percent as against a decline of 5.6 percent in the corresponding period of the previous year. Likewise, the commercial banks' balance held abroad increased by 15.8 percent amounting to Rs 47.6 billion in mid-February 2009 compared to a growth of 5.1 percent a year ago.

### **Liquidity Management**

11. In the first seven month of 2008/09, the NRB mopped up net liquidity of Rs 16.7 billion through open market operations. Of the total liquidity mopped up in the review period, Rs 7.5 billion has been mopped up from outright sale auction and Rs 13.3 billion from reverse repo auction. Likewise, despite an elevated inflow of remittances, a liquidity of Rs 4.0 billion has been injected through repo auction in the seventh month of the review period on account of a short-term shortfall in liquidity particularly due to a higher cash balance of the GON with the NRB and a higher increase of currency in circulation in the review period. Net liquidity of Rs 190 million had been injected in the corresponding period of the previous year through open market operation including Rs. 1.2 billion through outright sale auction, Rs. 5.6 billion through reverse repo auction and Rs 7.0 billion through repo auctions.
12. In the first seven months of 2008/09, the NRB injected net liquidity of Rs 85.3 billion by net purchase of 1.1 billion US dollar from commercial banks through foreign exchange intervention. A net liquidity of Rs 42.2 billion had been injected through the net purchase of 660.0 million US dollar from commercial banks in the corresponding period of the previous year. An elevated

inflow of remittance necessitated such a substantial amount of intervention in the foreign exchange market in the review period.

13. The NRB purchased Indian currency (IC) of 40.2 billion through the sale of 850.0 million US dollar in the review period. Indian currency of 31.4 billion had been purchased through the sale of 790.0 million US dollar in the corresponding period a year ago. A higher amount of payment made by Nepal Oil Corporation to Indian Oil Corporation contributed to a higher amount of IC purchase against the sale of US dollar in the review period.

### **Standing Liquidity Facility and Inter Bank Transactions**

14. In the first seven months of 2008/09, commercial banks used standing liquidity facility (SLF) of Rs 50.3 billion compared to that of Rs. 72.5 billion in the corresponding period of the previous year. Likewise, the inter bank transactions of commercial banks stood at Rs 174.1 billion in the review period compared to that of Rs 180.4 billion in the corresponding period of the previous year. Adequate liquidity with commercial banks on account of a slowdown of credit to the private sector accompanied by an elevated inflows of remittances contributed to lower the inter bank transactions and use of the SLF in the review period.

### **Short-term Interest Rates**

15. The short-term market interest rates increased in the seventh month of 2008/09. The weighted average monthly 91-day Treasury bill rate stood at 6.64 percent as in mid-February 2009 compared to that of 5.79 percent a year ago. The weighted average monthly inter bank rate stood at 8.32 percent as in mid-February 2009 compared to a rate of 7.55 percent in the corresponding period of the previous year. A higher demand of liquidity in money market on account of an issue of initial public offering (IPO) of shares for the general public by Citizen Bank International Ltd and Bank of Asia in the seventh month of the review period contributed to the rise in short-term interest rates in that month.

### **Securities market**

16. The year on year (y-o-y) NEPSE index decreased by 18.5 percent to 663.52 points in mid-February 2009. This index was 814.43 a year ago. Likewise, NEPSE sensitive index (based on July 2006) stood at 171.95 point in mid-February 2009. This index was 209.58 in mid-February 2008.
17. The NEPSE float index, calculated on the basis of final transaction as of August 24, 2008 (at market price), remained 64.15 in mid-February 2009.
18. The y-o-y market capitalization increased by 53.5 percent to Rs. 399.81 billion in mid-February 2009. Of the total market capitalization, bank and financial institutions, manufacturing and processing companies, hotels, business entities, hydropower and other economic sectors accounted for 71.2 percent, 1.8 percent, 1.2 percent, 0.3 percent, 4.1 and 21.4 percent respectively.
19. Total paid up capital of the listed companies stood at Rs. 51.36 billion in mid-February 2009, an increase by 110.9 percent over the period of one year. This increase was largely due to the additional listing of securities. Of the total listed share at Nepal Stock Exchange Ltd. of Rs. 25.46 billion up to mid-February 2009, bonus share, right share, ordinary share and bonds accounted for

Rs. 872.8 million, Rs. 5.59 billion, Rs.15.69 billion and Rs. 3.30 billion respectively. 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 0.25 percent in mid-February 2009, compared to 0.46 percent a year ago.
21. Total number of companies listed at the NEPSE increased to 149 in mid-February 2009 compared to 145 a year ago. Among the currently listed companies, 118 are banks and financial institutions (including insurance companies). Production and processing industries, hotels, business entities, hydropower and companies in other groups, number 18, 4, 4, 3 and 2 respectively.
22. The twelve-month rolling standard deviation, reflecting an increased volatility in the stock market, stood at 138.7 in mid-February 2009 compared to 187.8 a year ago.
23. Nepal Stock Exchange Limited has been classifying the listed companies as 'A' class category which complies with the norms and conditions prescribed by Dhitopatra Suchikaran Biniyamawali, 2053 (Stock Listing Bye Law, 2053) since fiscal year 2053/54. Nepal Stock Exchange Ltd. has classified 78 listed companies as 'A' class companies for the current fiscal year 2065/66.

## **Inflation**

### **Consumer Price Inflation**

24. The y-o-y inflation as calculated by the consumer price index rose to 13.7 percent in mid-February 2009 from 6.4 percent in the previous year. The inflation, in the review period, was driven both by the significant rise in food and beverages (18.1 percent) as well as non-food and services (9.1 percent) group. The price rise of food and beverages and non-food and services group, was 7.9 percent and 4.8 percent respectively in mid-February 2008.
25. Of the items in the food and beverage group, price indices of sugar and sugar related products increased by a whopping rate of 46.7 percent in mid-February 2009. This is in sharp contrast to last year's decline of 10.7 percent. Similarly, the price indices of pulses as well as meat, fish and eggs sub-groups increased in the review period by 26.5 percent and 22.9 percent respectively as compared to an increase of 13.4 percent and 6.4 percent respectively in the previous year. The price rise of grains and cereal subgroup stood at 14.7 percent in the review period compared to an increase of 13.5 percent in the corresponding period of previous year. Likewise, the indices of oil and ghee as well as restaurant meal rose up by 19.8 percent and 19.7 percent respectively in the review period compared to a rise of 18.8 percent and 7.3 percent respectively in mid-February 2008.
26. Within the group of non-food and services, the index of tobacco and related products as well as transport and communication rose up by 16.3 percent and 13.5 percent respectively in mid-February 2009 compared to a rise of 8.3 percent and 1.1 percent respectively during the same period of last year.
27. Region-wise, the price rise in Kathmandu valley was 13.9 percent followed by 13.8 percent in Terai and 13.2 percent in Hills in the review period. Last year, the respective rates were 6.2 percent, 6.4 percent and 6.5 percent.

28. In the review period, the y-o-y core inflation rose to 13.0 percent from 5.5 percent a year ago.

#### **Wholesale Price Inflation**

29. The wholesale price inflation increased to 15.0 percent in mid-February 2009 compared to 4.3 percent a year ago. The index of agricultural commodities, imported commodities and domestic manufactured commodities increased by 18.8 percent, 11.8 percent and 11.2 percent respectively in the review period as compared to 1.7 percent, 6.9 percent and 6.6 percent a year ago.
30. Among the agricultural commodities, primarily the price index of fruits and vegetables, livestock production and pulses increased by 42.0 percent, 24.0 percent and 19.0 percent respectively in the review period. In the previous year, while the price index of fruits and vegetables had declined by 19.6 percent, the price indices of live stock production and pulses had risen by 5.6 percent and 9.5 percent, respectively. Within the group of domestic manufactured commodities, the price indices of food-related products as well as beverages and tobacco both increased by 11.8 percent in mid-February 2009 compared to a rise of 8.0 percent and 5.3 percent respectively a year ago.
31. Of imported commodities, the price index of transport vehicles and machinery goods increased by 21.9 percent in mid-February 2009 compared to an increase of 3.3 percent a year ago. Likewise, the price indices of textile related products also increased by 20.6 percent in the review period compared to a decline of 4.3 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 17.6 percent in mid-February 2009 compared to a rise of 8.8 percent a year ago. Of the salary and wage rate indices, the salary index increased by 20.8 percent in the review period compared to a rise of 10.9 percent in the corresponding period of the previous year. The wage rate index increased by 16.4 percent in the review period compared to an increase of 8.2 percent in the same period of the previous year. Such an increase was on account of increase in the salary of civil servants and a rise in the wages of laborers because of the supply constraints due mainly to the migration of youths from rural areas along with the increasing trend of Nepalese youths seeking employment abroad. Wages of agricultural, industrial and construction laborers increased by 23.0 percent, 7.0 percent and 15.3 percent respectively in the review period. Last year, these wage rates had increased by 6.3 percent, 10.2 percent and 11.1 percent respectively.

### **Fiscal Situation**

#### **Budget Deficit / Surplus**

33. In the first seven months of 2008/09, the government budget remained at a surplus of Rs.8.8 billion in contrast to a deficit of Rs 6.2 billion in the corresponding period of the previous year. An increase in revenue and foreign cash grants accounted for such a budget surplus in the review period.

#### **Government Expenditure**

34. In the first seven months of 2008/09, the total government expenditure increased by 15.1 percent to Rs.78.4 billion compared to an increase of 31.1 percent in the corresponding period of the

previous year. The deceleration of such spending was due to a decline in the growth rate of recurrent as well as capital expenditure.

35. In the first seven months of 2008/09, recurrent expenditure increased by 17.5 percent to Rs.52.0 billion. In the corresponding period of the previous year, recurrent expenditure had increased by 20.6 percent. The effective implementation of government directions 2008 with regard to economizing the expenditure led to such deceleration in recurrent expenditure in the review period.
36. In the review period, capital expenditure declined by 20.1 percent to Rs 11.1 billion in contrast to an increase of 79.1 percent in the corresponding period of the previous year. Delay in presenting budget, lack of representatives in local bodies, delay in the formulation of programmes and directives regarding the projects under New Nepal movement, delay in contracts and procurement procedures as well as uncertain and irregular power supply and conflict accounted for such a decline in capital expenditure in the review period.

### **Government Revenue**

37. In the first seven months of 2008/09, revenue mobilization of the government grew by 32.5 percent to Rs.72.3 billion compared to an increase of 29.0 percent in the corresponding period of the previous year. Government's strong commitment in revenue leakage control, revenue administration reforms and voluntary declaration of income tax programme (VDIS) contributed to such an impressive growth of revenue mobilization in the review period.
38. Of the total revenue mobilization, VAT revenue grew by 18.4 percent to Rs 20.5 billion in mid-February 2009. It had increased by 24.2 percent in the corresponding period of the previous year. The increase in VAT revenue was on account of growing imports and consumption induced by the rise in remittances and reforms in VAT administration.
39. In the review period, customs revenue rose by 18.6 percent to Rs 13.4 billion compared to an increase of 28.3 percent in the same period of the previous year. Reforms in customs administration and the increase in imports of high tax yielding vehicles and spare parts contributed to such an increase in customs revenue. However the frequent conflict in border area and the reduction of the custom rates to zero of 131 goods by the budget led to the low growth rate of customs revenue in the review period.
40. In the review period, excise revenue increased by 38.7 percent to Rs 7.7 billion compared to an increase of 28.7 percent in the same period of the previous year. Reforms in excise administration and increase in the imports of high tax yielding vehicles accounted for such a growth of excise revenue in the review period.
41. Income tax revenue increased by 37.7 percent to Rs 13.3 billion in the first seven months of 2008/09. Receipt of Rs 1.0 billion under VDIS program due to the strong government administrative and political commitment contributed to such an increase in income tax collection. Last year, such revenue had risen by 40.6 percent.
42. In the review period, non-tax revenue grew by 61.3 percent to Rs 13.1 billion compared to an increase of 22.8 percent in the same period of the preceding year. Such an increase in non-tax revenue was on account of the increase in dividend paid by some public enterprises to the government.

### **Foreign Cash Loans and Grants**

43. The government received foreign cash loans of Rs 2.8 billion and foreign cash grants of Rs 12.9 billion in the first seven months of 2008/09. The government had received foreign cash loans of Rs 2.5 billion and foreign cash grants of Rs 5.4 billion in the corresponding period of the previous year.
44. The government mobilized domestic borrowing of Rs 8.7 billion in the review period. It had received domestic borrowing of Rs 9.2 billion in the corresponding period of the previous year.

### **Foreign Trade**

45. Exports rose by 19.5 percent in the first seven months of 2008/09 in contrast to a decline by 3.3 percent in the corresponding period of the previous year. While exports to India rose by 2.3 percent in 2008/09 as against a decline by 5.5 percent in the corresponding period of the previous year, exports to other countries soared by 58.4 percent in comparison to an increase of 1.9 percent in the same period of the previous year.
46. The rise in the exports of readymade garments, G.I. pipe, shoes & sandles, tooth paste and catechue was, to a large degree, attributed to the increase in exports to India. Likewise, the rapid increase in the exports to other countries can be ascribed to the rise in the exports of pulses, woolen carpets, pashmina, readymade garments and herbs.
47. In the first seven months of 2008/09, total imports went up by 25.5 percent as compared to an increase of 18.5 percent in the corresponding period of the previous year. While imports from India increased by 12.5 percent in the review period in comparison to a growth of 24.5 percent in the corresponding period of 2007/08, imports from other countries surged by 47.9 percent in comparison to a growth of 9.5 percent a year earlier.
48. An increase in the import of petroleum products, vehicles & spare parts, cold rolled sheet in coil, other machinery & parts and medicine, among others, from India and gold, electrical goods, MS billet, other machinery & parts and computer & parts, among others, from other countries were largely responsible for the rise in total imports in the first seven months of 2008/09.

### **Balance of Payments**

49. In the first seven months of 2008/09, the overall BOP recorded a significant surplus of Rs. 25.68 billion in comparison to a surplus of Rs. 251.1 million in the corresponding period of the previous year. The current account also posted a surplus of Rs. 20.32 billion in the first seven months of 2008/09 in comparison to a deficit of Rs. 7.62 billion in the corresponding period of the previous year. Such current account surplus was primarily attributed to the surge in net transfers by 55.1 percent in the first seven months of 2008/09. Under transfers, workers' remittances soared by 58.6 percent in the first seven months of 2008/09 in comparison to the growth of 23.2 percent in the corresponding period of the previous year.

### **Foreign Exchange Reserves**

50. In mid-February 2009, the gross foreign exchange reserves aggregated Rs. 251.79 billion, an upsurge by 18.4 percent compared to the level as at mid-July 2008. In the corresponding period of the previous year, such reserves had increased by 1.2 percent. On the basis of US dollar, gross foreign exchange reserves rose by 4.4 percent to US\$ 3.24 billion in mid-February 2009. Such

reserves had increased by 3.6 percent in the same period in the previous year. The current level of reserves is sufficient for financing merchandise imports of 11.3 months and merchandise and service imports of 9.1 months.

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

51. In the international market, the price of oil (Crude Oil Brent) plummeted by 54.7 percent to US\$ 43.38 per barrel in mid-February, 2009 from US\$ 95.80 per barrel in mid-February 2008. Similarly, the price of gold rose by 2.0 percent to US\$ 935.50 per ounce in mid-February, 2009 from US\$ 917.00 per ounce a year earlier.
52. In comparison to mid-July 2008, the Nepalese currency *vis-à-vis* the US dollar depreciated by 11.84 percent in mid-February 2009. It had appreciated by 2.37 percent in the corresponding period of the previous year. The exchange rate of one US dollar stood at Rs. 77.70 in mid-February 2009 compared to Rs. 68.50 in mid-July 2008.