Nepal Rastra Bank

Research Department

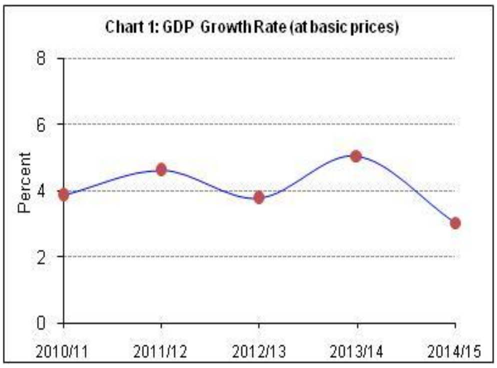
Current Macroeconomic Situation of Nepal

(Based on the Annual Data of 2014/15)

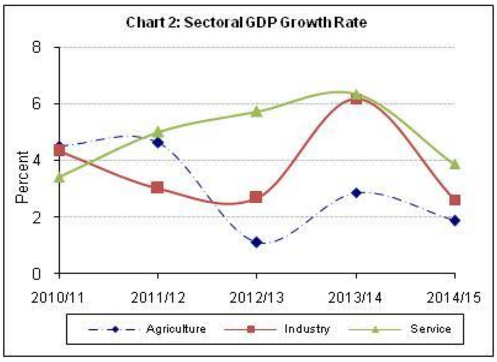
Real Sector

Gross Domestic Product

1. According to the Central Bureau of Statistics (CBS), the real GDP at basic price is estimated to grow by 3.0 percent in 2014/15 compared to a 5.1 percent growth in the previous year. Similarly, the real GDP at producers' price is estimated to grow by 3.4 percent in the review year compared to a 5.4 percent growth in the previous year. Delay in monsoon, the devastating earthquake of 25 April 2015 and the subsequent aftershocks have significant negative impact on all sectors of the economy resulting into a lower output growth in the review year.



2. According to the Post Disaster Needs Assessment (PDNA) report published by the National Planning Commission (NPC), the earthquake caused a total loss of Rs. 706 billion in the economy. The damage of the earthquake is estimated at 57.8 percent in the social sector, 25.2 percent in the productive sector, 9.5 percent in the infrastructure sector and 7.5 percent in the cross cutting issues. The loss from the earthquake is estimated at about one-third GDP of 2014/15. The destruction resulted in a loss of Rs. 36.0 billion in the GDP leading to around 1.6 percentage points shrinkage in the overall economic growth rate (Box 2).



3. In the review year, the agriculture sector, which contributes about a one-third to real GDP is expected to grow by 1.9 percent and the non-agriculture sector by 3.6 percent. These sectors had grown by 2.9 percent and 6.3 percent respectively in the previous year.

Box 1 : Gross National Disposable Income (At Current Prices)

Description	Rs in Billion			Percent Change	
	2012/13	**2013/14**	**2014/15**	**2013/14**	**2014/15**
GDP at Producers' Price	1695.0	1941.6	2124.7	14.6	9.4
Factor Income, Net *	13.1	32.8	34.2	150.4	4.6
Current Transfers, Net *	497.7	631.5	710.0	26.9	12.4
Gross National Disposable Income	2205.8	2605.9	2868.9	18.1	10.1

* Extracted from annual BOP statement, 2014/15.
Source: Central Bureau of Statistics

4. In the review year, the agricultural sector saw a lower rate of growth on account of the decline in the production of principal cereal crops - paddy and maize owing to late monsoon, and losses in livestock and some agro-products from the earthquake. A total loss of Rs. 28.4 billion in the

agriculture, bee-keeping, fishery, poultry and irrigation is estimated due to the earthquake. The earthquake damage has resulted in 0.4 percent contraction in agricultural growth.

5. In the review year, the industrial sector is estimated to grow by 2.6 percent compared to a growth of 6.2 percent in the previous year. The lower growth in industrial sector is attributed to labor shortage, physical damages caused by the earthquake and sluggish demand for industrial production. The industrial sector witnessed a sluggish progress due to the damage in fixed assets and production of around Rs. 19.0 billion as well as the negative effect on 20.0 percent strategically important road networks and about 25.0 percent reduction in the power production on account of the earthquake. The obstruction in Araniko Highway to the nearby Nepal-China border is still not fully resumed and Pasang Lhamu highway, the alternative highway that links Nepal to China, is still blocked due to the earthquake. The construction process of Upper Tamakoshi Hydropower Project has not been resumed yet.

Box 2 : 2015 April Earthquake – Damage and Effect on Economic Growth

1. **Human and physical damage:** Around 8 million population including the death toll of around 9 thousand and injury of 22 thousand people suffered from the earthquake. While a total of around 0.5 million houses were damaged fully, 0.3 million houses were partially damaged due to the tremor. Likewise, 20 percent of road network, 23 percent of schools and 25 percent of electricity production have been affected by the earthquake.
2. **Effect on economic growth:** The estimate of GDP growth rate has been downgraded to 3.0 percent from the estimate of 4.6 percent before the earthquake.

Sector	Pre earthquake estimate	Post earthquake estimate
Agricultural Sector	2.3	1.9
Non-agricultureSsector	5.7	3.6
Gross Domestic Product (at basic price)	4.6	3.0
Gross Domestic Product (at market price)	5.0	3.4

3. **Effect on poverty:** Poverty is estimated to increase by at least 2.5 percent to 3 percent in 2014/15. As a result, around 0.7 million additional people are pushed below the poverty line.

Source: Post Disaster Needs Assessment Report, NPC, 2015.

6. In the review year, the service sector is estimated to grow by 3.9 percent compared to a growth of 6.3 percent in the previous year. Despite the improvement in labor relation, security situation and other structural bottlenecks, adverse impact of the devastating earthquake of April 25, 2015, especially on hotel and restaurants, real estate, renting and business activities and wholesale and retail trade have impeded the growth rate of service sector in the review year.

7. The PDNA report reveals that poverty is estimated to increase by at least 2.5 percent to 3.0 percent due to the earthquake in 2014/15. This resulted into an additional 0.7 million people falling below the poverty line. Of these additional people pushed into the poverty, 50.0 percent to 60.0 percent are believed to live in the central hills and mountains. In addition, the poverty situation is likely to aggravate

Box 3 : Summary of Disaster Effects

	Disaster Effects (Rs. in Million)		
	Damages	**Losses**	**Total**
Social Sectors	**355028**	**53597**	**408625**
Housing and Human Settlements	303632	46908	350540
Health	6422	1122	7544
Education	28064	3254	31318
Cultural Heritage	16910	2313	19223
Productive Sectors	**58074**	**120046**	**178121**
Agriculture	16405	11962	28366
Irrigation	383	0	383
Commerce	9015	7938	16953
Industry	8394	10877	19271
Tourism	18863	62379	81242
Finance	5015	26890	31905
Infrastructure Sectors	**52460**	**14323**	**66783**
Electricity	17807	3435	21242
Communications	3610	5085	8695
Community Infrastructure	3349	0	3349
Transport	17188	4930	22118
Water and Sanitation	10506	873	11379
Cross-Cutting Issues	**51872**	**1061**	**52933**
Governance	18757	0	18757
Disaster Risk Reduction	155	0	155
Environment and Forestry	32960	1061	34021
Total	**517,434**	**189,027**	**706,462**

Source : Post Disaster Needs Assessment Report, NPC, 2015.

further due to the disruption in water supply, sanitation, health services and schools and increase in food shortage on account of the devastating earthquake.

8. The Government of Nepal (GoN) organized the International Donor Conference on Nepal's Reconstruction on 25 June 2015. Bilateral and multilateral development partners such as India, China, Japan, USA, UK, Asian Development Bank, World Bank, among others, participated in the conference. The GON presented details of Rs. 706 billion loss caused by the earthquake to the participating donors. The donors made commitments of aid worth over Rs. 440 billion to support the reconstruction effort of Nepal. Out of the total committed aid, both grants and soft loan are approximately in equal amount (Box 3).

Foreign Employment

9. In 2014/15, the GoN, Department of Foreign Employment granted final approval to 0.51 million workers for foreign employment, registering a decline of 2.8 percent from the previous year. The number of people going abroad for foreign employment has been declining in recent months due to the impact of earthquake and strike of the manpower agencies against the governmental decision of free airfare and free visa for the workers.

10. Countries including Malaysia, Qatar, Saudi Arabia, UAE, Kuwait and South Korea were the major destinations for Nepalese workers in 2014/15. Among the total workers granted final approval for foreign employment in the review year, 39.5 percent received approval for Malaysia followed by 24.2 percent for Qatar, 19.2 percent for Saudi Arabia, 10.5 percent for UAE, 1.9 percent for Kuwait and 1.0 percent for South Korea (Box 4). In the review year, the number of work permission has decreased in all countries except Saudi Arab compared to the previous year.

Box 4 : Number of Workers Approved for Foreign Employment

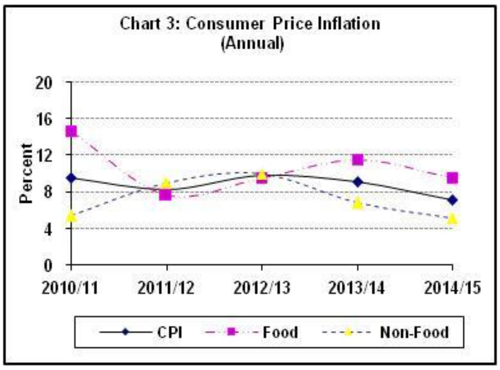
Destination Countries	Total Approval for Foreign Employment			Percent Change		Share (in percent)
	2012/13	2013/14	2014/15	2013/14	2014/15	2014/15
Malaysia	156770	214270	202828	36.7	-5.3	39.5
Qatar	90935	125170	124368	37.6	-0.6	24.2
Saudi Arabia	86276	86653	98246	0.4	13.4	19.2
UAE	52295	54625	53699	4.5	-1.7	10.5
Kuwait	14401	19861	9668	37.9	-51.3	1.9
South Korea	4299	5811	5158	35.2	-11.2	1.0
Others	48567	21424	18920	--55.9	-11.7	3.6
Total	453543	527814	512887	16.4	-2.8	100.0

Source: GoN, Department of Foreign Employment.

Inflation, Salary and Wage Rate

Consumer Price Inflation

11. The annual average consumer price inflation increased by 7.2 percent in 2014/15 compared to an increase of 9.1 percent in 2013/14. Inflation remained lower than the projected 8.0 percent in the monetary policy of 2014/15. This is mainly due to the decline in the price of petroleum products, the control of monetary aggregates at the desired level through effective liquidity management and the lower level of inflation in neighboring countries.



12. The annual average indices of food and beverages group and non-food and services group increased by 9.6 percent and 5.2 percent respectively during the review year. Such indices had increased by 11.6 percent and 6.8 percent respectively in 2013/14.

13. Under the food and beverages group, the annual average price index of tobacco products sub-group increased by the highest rate of 25.6 percent in the review year whereas it had increased by 18.8

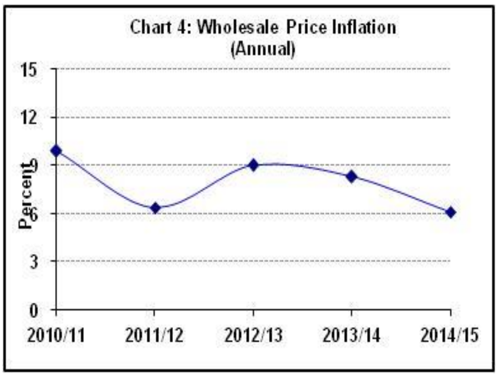
percent in the previous year. Similarly, the annual average price indices of hard drinks sub-group and legume varities sub-group increased by 20.1 percent and 17.6 percent respectively compared to the increment of 16.9 percent and 4.9 percent respectively in the previous year. Likewise, the annual average price indices of fruits sub-group and milk products and egg sub-group which had witnessed a growth of 13.7 percent and 7.2 percent in the previous year went up by 13.7 percent and 12.8 percent respectively in the review year.

14. Under the non-food and services group, the annual average index of clothing and footwear sub-group increased by the highest rate of 9.9 percent in the review year whereas it had increased by 11.1 percent in the previous year. Similarly, the annual average price indices of furnishing and household equipment sub-group and miscellaneous goods and services sub-group went up by 8.2 percent and 8.0 percent respectively in the review year compared to the rise of 9.2 percent and 7.3 percent respectively in the previous year. Likewise, the annual average price indices of recreation and culture sub-group and education sub-group increased by 6.2 percent and 5.6 percent respectively in the review year. These indices had increased by 6.7 percent and 7.6 percent respectively in the previous year.

15. Region-wise, the annual average price indices increased by 7.3 percent in Hills followed by 7.2 percent in Kathmandu Valley and 7.1 percent in Terai in the review year. Such indices had risen by 8.1 percent in Hills, 9.1 percent in Kathmandu Valley and 9.6 percent in Terai in the previous year.

Wholesale Price Inflation

16. The annual average wholesale price inflation increased by 6.1 percent in 2014/15 compared to a growth of 8.3 percent in the previous year. The annual average price indices of agricultural commodities, domestic manufactured commodities and imported commodities increased by 8.8 percent, 5.6 percent and 0.7 percent respectively in the review year compared to a growth of 11.3 percent, 6.0 percent and 4.2 percent in the previous year.



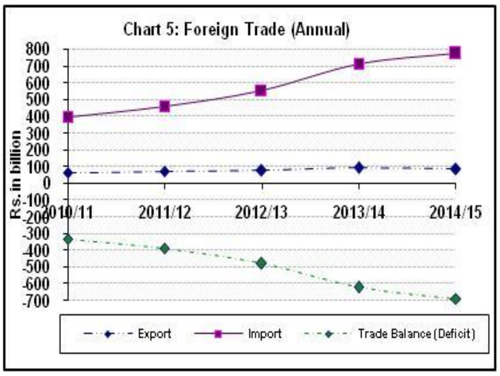
National Salary and Wage Rate Index

17. The annual average salary and wage rate index increased by 8.4 percent in 2014/15 whereas it had risen by 13.7 percent in the previous year. In the review year, both the annual average salary index and the annual average wage rate index rose by the same rate of 8.4 percent compared to an increase of 25.4 percent and 11.1 percent respectively in the previous year. In the review year, the wage rate index of construction laborers, industrial laborers and agricultural laborers increased by 12.9 percent, 8.3 percent and 7.7 percent respectively.

External Sector Situation

Foreign Trade

18. The trade deficit widened in 2014/15 on account of the increase in imports and the fall in exports. The trade deficit widened at a lower pace due to slow down in the import growth caused by devastating earthquake in the last quarter of the review year.



19. Merchandise exports decreased by 7.3 percent to Rs. 85.32 billion in 2014/15. Such exports had increased by 19.6 percent to Rs. 91.99 billion in the previous year. A fall in exports to India, China and other countries resulted in a decrease in overall exports.

20. Exports to India dropped by 6.3 percent during the review year in contrast to an increase of 16.9 percent in the previous year. Exports to India decreased mainly due to the decrease in exports of

zinc sheet, textiles, cardamom, copper wire rod, among others. Similarly, exports to China decreased by 21.5 percent in the review year in contrast to an increase of 36.2 percent in the previous year. This decrease is mainly attributed to the decrease in the exports of wheat flour, handicraft goods, agarbatti, pashmina, among others. Similarly, exports to other countries decreased by 7.8 percent in the review year in contrast to an increase of 23.9 percent in the previous year. Exports to other countries dropped due to the decrease in the exports of pulses, pashmina, woolen carpet, readymade garments, among others. In US dollar terms, exports to China decreased by 22.4 percent to USD 22.6 million during the review year in contrast to an increase of 22.6 percent in the previous year. Similarly, exports to other countries decreased by 9.0 percent to USD 274.1 million in the review year in contrast to an increase of 11.3 percent in the previous year.

21. During the review year, merchandise imports increased by 8.4 percent to Rs. 774.68 billion. Such imports had gone up by 28.3 percent to Rs. 714.37 billion in the previous year. The growth of imports remained low mainly due to the decrease in the price of petroleum products and the decline in imports of gold, betelnut, coal, crude soyabean oil, among others. On a monthly basis, merchandise imports increased by 34.2 percent in the twelfth month of the current fiscal year compared to that of the previous month due to the increase in imports of aircraft spare parts, medicine, vehicle and spare parts and petroleum product, among others.

22. Imports from India went up by 2.9 percent in the review year compared to a growth of 30.2 percent in the previous year. Imports from India increased primarily due to an increase in the imports of vehicle and spare parts, rice/paddy, electrical equipment, machinery and parts, among others. Likewise, imports from China increased sharply by 36.6 percent in the review year compared to a growth of 17.4 percent in the previous year. Imports from China increased due to the increase in imports of telecommunication equipments and parts, machinery and parts, chemical fertilizer, electrical equipments, among others. Similarly, imports from other countries increased by 12.1 percent in the review year compared to a growth of 28.2 percent in the previous year. Imports from other countries rose mainly due to an increase in imports of helicopter/aircraft and spare parts, silver, medicine, crude palm oil, among others. In US dollar terms, imports from China increased by 34.9 percent to USD 1.01 billion in the review year compared to an increase of 5.2 percent during the previous year. Similarly, imports from other countries increased by 10.5 percent to USD 1.84 billion in the review year compared to an increase of 15.0 percent in the previous year.

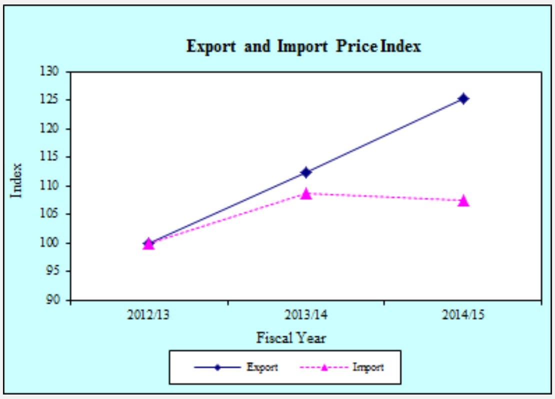
23. Total trade deficit during the review year grew by 10.8 percent to Rs. 689.37 billion compared to an increase of 29.7 percent in the previous year. Trade deficit with India, China and other countries increased by 4.2 percent, 39.0 percent and 16.5 percent respectively. Such deficits had increased by 32.4 percent, 16.8 percent and 29.1 percent respectively in the previous year. The FOB based trade deficit increased by 11.4 percent to Rs. 663.50 billion in the review year compared to a growth of 29.1 percent in the previous year.

24. Exports-imports ratio declined to 11.0 percent in the review year as a result of decrease in exports and increase in imports. Such a ratio was 12.9 percent in the previous year.

Export and Import Price Index

25. Nepal Rastra Bank (NRB) has prepared and made public for the first time the export and import price index from this edition of Current Macroeconomic Situation. The annual average unit value export price index based on customs data increased by 11.5 percent in 2014/15 compared to 12.4 percent rise in the previous year. Increase in price of major export items such as red lentils, big cardamom, p.p. woven fabrics, jute sacking bags caused the export price index to increase in the review year.

Box 5 : Export and Import Price Index



Note:- *Export and Import Price Index (XMPI) are published for the first time by constructing the index applying unit value approach based on customs data. Index has been prepared by selecting 72 export items and 117 import items on the basis of their share on total foreign trade. Laspeyre's Index Formula has been used to construct XMPI.*

26. The annual average unit value import price index based on customs data decreased by 1.0 percent in the review year in contrast to 8.6 percent rise in the previous year. The fall in price of major import items such as diesel, L.P. gas, petrol caused import price index to decrease in the review year.

27. The ratio of export to import price index (Terms of Trade- TOT) improved by 12.6 percent compared to 3.4 percent increase in 2013/14 (Box 5). This ratio reflects that international trade is in Nepal's favor. Despite the improvement in this ratio, Nepal has not benefited from the improved TOT in terms of production and employment because of fall in exports.

Service Account

28. The services income in the review year increased by 19.4 percent to Rs. 149.29 billion, which had increased by 31.4 percent in the previous year. Of the total services income, the travel income, government income and other income increased by 15.2 percent, 33.4 percent and 16.6 percent respectively.

29. The total service expenses increased by 16.8 percent in the review year compared to 18.9 percent increase in the previous year. The transportation expenses, travel expenses, government service expenses and other service expenses increased by 10.5 percent, 26.1 percent, 21.5 percent and 9.5 percent respectively.

30. The net service income recorded Rs. 27.62 billion surplus in the review year compared to Rs. 20.88 billion in the previous year. This is due to a higher growth of income relative to expenses.

Transfers and Remittances

31. The net transfer receipt increased by 12.4 percent to Rs. 709.96 in the review year compared to 26.9 percent in the previous year. The total foreign grants of Rs. 52.86 billion is received in the review year compared to Rs. 48.52 billion in the previous year.

32. The inflow of workers' remittances increased by 13.6 percent to Rs. 617.28 billion in the review year compared to 25.0 percent growth of previous year. In US dollar terms, remittances increased by 11.9 percent to US dollar 6.19 billion compared to a growth of 12.3 percent in the previous year.

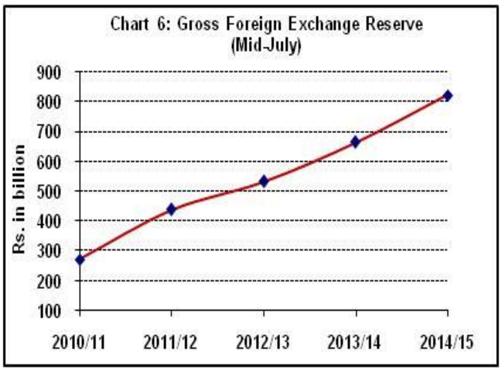
33. The pension income increased by 2.5 percent to Rs. 42.39 billion in the review year from the level of Rs. 41.37 billion in the previous year.

Current Account

34. The current account registered a surplus of Rs. 108.32 billion during the review year compared to a surplus of Rs. 89.72 billion in the previous year. The higher level of surplus in current account is mainly attributed to the low growth of good imports, increase in remittance inflows and grants, among others. The current account surplus in US dollar terms stood at USD 1.07 billion compared to USD 909.2 million of the previous year.

BOP Situation

35. The overall BOP registered a record high surplus of Rs. 144.85 billion in 2014/15 compared to a surplus of Rs. 127.13 billion in the previous year. In US dollar terms, the BOP recorded a surplus of USD 1.43 billion compared to USD 1.29 billion in the previous year.



Foreign Exchange Reserves

36. The foreign exchange reserve held by NRB increased by 22.8 percent to Rs. 702.88 billion at mid-July 2015 compared to Rs. 572.40 billion as of mid-July 2014.

37. The foreign exchange reserve of banks and financial institutions (except NRB) increased by 30.1 percent at mid-July 2015 to Rs. 121.00 billion compared to Rs. 93.01 billion as of mid-July 2014.

38. The gross foreign exchange reserves increased by 23.8 percent to Rs. 823.87 billion in mid-July 2015 from Rs. 665.41 billion as of mid-July 2014. Such reserves had increased by 24.8 percent in the previous year. The gross foreign exchange reserves in US dollar terms increased by 17.4 percent to USD 8.15 billion in mid-July 2015. Such reserves had increased by 23.6 percent in the previous year.

39. During the review year, the Indian currency reserve increased by 26.7 percent to IRs 120.28 billion. Such reserves had increased by 27.4 percent in the previous year. Likewise, convertible foreign exchange increased by 16.6 percent to USD 6.24 billion in the review year which had increased by 22.9 percent in the previous year.

Reserve Adequacy Indicators

40. Based on the total imports of the current fiscal year, the current level of foreign exchange reserves is sufficient for financing merchandise imports of 13.0 months, and merchandise and services imports of 11.2 months.

41. The reserve adequacy ratios remained satisfactory in the review year. The ratio of reserve to GDP, reserve to imports and reserve to broad money (M2) remained at 38.8 percent, 93.2 percent and 43.9 percent respectively in the review year (Box 6). Such ratios were 34.3 percent, 83.1 percent and 42.5 percent in the previous year.

Box 6 : Reserve Adequacy Ratios (In Percent)

	2012/13	2013/14	2014/15
Reserve/GDP	31.5	34.3	38.8
Reserve/Imports*	84.0	83.1	93.2
Reserve/M2	40.5	42.5	43.9

* Goods and services imports

International Investment Position (IIP)

42. NRB has prepared and made public for the first time the International Investment Position (IIP) from this edition of Current Macroeconomic Situation. The IIP shows that foreign assets and liabilities of Nepal were Rs. 847.66 billion and Rs. 487.32 billion respectively in mid-July 2015 (Box 7). Accordingly, the net IIP remained in surplus by Rs. 360.35 billon as at mid-July 2015. Such surplus was Rs. 204.03 billion in mid-July 2014.

Box 7 : International Investment Position

The International Investment Position (IIP) is one of the indicators reflecting the performance of external sector. The IIP shows the economy's external financial assets and liabilities position at a particular point of time. The IIP includes foreign direct investment, portfolio investment, financial derivatives, other investment, and reserves. Net IIP is positive, if assets (claims) are more than foreign liabilities (obligations) and negative, if the foreign assets (claims) are less than foreign liabilities (obligations). The IIP shows the position of the country whether it is net debtor or lender. The favorable position of IIP shows comfortable position of external sector. The IIP has been prepared and published for the first time on the basis of information of NRB, BFIs, FCGO and data obtained from various surveys.

SN	Items	As of Mid-July (Rs. in Million)		
		2012/13	2013/14	2014/15
A	**Assets**	**559141.8**	**681315.1**	**847663.1**
1	Direct Investment	0.0	0.0	0.0
2	Portfolio Investment	0.0	0.0	0.0
3	Other Investments	85350.7	87562.1	121163.5
	Other Equity	2495.8	2502.8	5476.1
	Currency and Deposits	22025.6	29912.6	44169.5
	Loans	52.6	1228.9	10122.6
	Trade Credit and Advances	5147.4	1620.0	2234.3
	Other Account Receivables	55629.4	52297.8	59161.0
4	Official Reserve Assets*	473791.1	593752.9	726499.6
B	**Liabilities**	**480095.8**	**477283.1**	**487315.8**
1	Direct Investment	52113.3	57264.0	63426.7
2	Portfolio Investment	0.0	0.0	0.0
3	Other Investments	427982.5	420019.1	423889.1
	Other Equity	0.0	0.0.	0.0
	Currency and Deposits	56115.3	29370.5	39870.3
	Loans	347624.7	356787.1	351400.2
	Trade Credit and Advances	14434.6	23686.1	22912.3
	Other Account Payables	20.2	41.7	38.2
	Special Drawing Rights	9787.8	10133.8	9668.1
	Net IIP	79046.0	204031.9	360347.3

* based on resident and non-resident flows.

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

43. The price of oil (Crude Oil Brent) in the international market decreased sharply by 45.3 percent to USD 57.31 per barrel in mid-July 2015

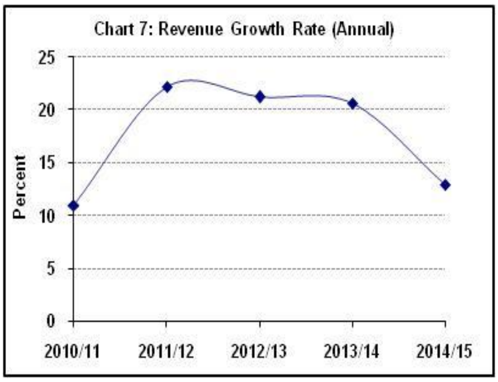
from USD 104.73 per barrel a year ago. The decrease in the price of petroleum product is attributed to the decrease in demand of petroleum products in Japan, China and Euro area coupled with constant production by the OPEC and increase in production by the USA. Similarly, the price of gold declined by 12.6 percent to USD 1144.40 per ounce from USD 1310.00 per ounce a year ago.

44. Nepalese currency vis-à-vis the US dollar depreciated by 5.2 percent in mid-July 2015 from the level of mid-July 2014. It had depreciated by 0.9 percent in the previous year. The exchange rate per US dollar remained Rs. 101.14 in mid-July 2015 compared to Rs. 95.90 in mid-July 2014.

Fiscal Situation *

Government Revenue

45. In 2014/15, the government revenue increased by 13.8 percent to Rs. 405.85 billion, showing the actual revenue collection at 96.0 percent of annual target of Rs. 422.90 billion. The revenue had risen by 20.5 percent to Rs. 356.62 billion in 2013/14. Despite the slowdown in economic activities after April earthquake and the deceleration of imports, revenue-to-GDP ratio stood at 19.1 percent in the review year (Box 8). Such ratio was 18.4 percent in 2013/14.



46. Of the total revenue mobilization, VAT revenue grew by 11.3 percent to Rs. 112.52 billion in 2014/15. Such revenue had increased by 21.2 percent to Rs 101.11 billion in 2013/14.

47. Income tax revenue increased by 14.1 percent to Rs. 89.11 billion in 2014/15 compared to an increase of 18.2 percent to Rs. 78.09 billion in 2013/14.

48. In 2014/15, customs revenue rose by 10.1 percent to Rs. 74.84 billion compared to an increase of 19.4 percent to Rs. 67.98 billion in 2013/14. The low growth rate of revenue can be mainly attributed to the decline in growth rate of imports in the review year.

49. During the review year, excise revenue increased by 17.9 percent to Rs. 53.54 billion compared to an increase of 25.3 percent to Rs. 45.41 billion in 2013/14.

50. Among the components of revenue in 2014/15, VAT revenue registered a share of 27.7 percent followed by income tax revenue (22.0 percent), customs revenue (18.4 percent), and excise revenue (13.2 percent). In the previous year, such compositions were 28.4 percent, 21.9 percent, 19.1 percent and 12.7 percent respectively.

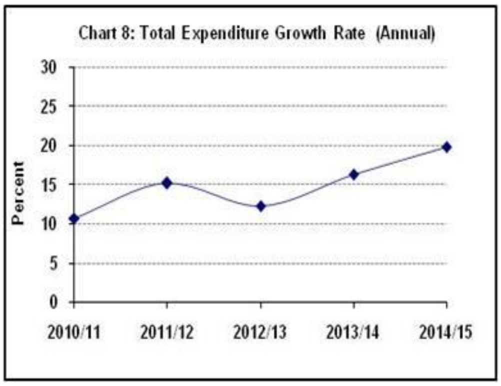
51. In the review year, non-tax revenue increased by 13.0 percent to Rs. 49.90 billion compared to an increase of 20.1 percent to Rs. 44.18 billion in 2013/14.

52. Of the total revenue, the share of tax revenue and non-tax revenue stood at 87.7 percent and 12.3 percent respectively in the review year. Likewise, the share of direct and indirect tax revenue in total tax revenue remained at 32.3 percent and 67.7 percent respectively. In the previous year, the shares of tax and non-tax revenue in the total revenue were 87.6 percent and 12.4 percent respectively while the shares of direct and indirect tax revenue in the total tax revenue were 31.4 percent and 68.6 percent respectively.

* Based on the data reported by 8 NRB offices, 66 branches of Rastriya Banijya Bank Limited, 44 branches of Nepal Bank Limited, 9 branches of Everest Bank Limited, 4 branches of Global IME Bank Limited and 1-1 branch each of Nepal Bangladesh Bank Limited, NMB Bank Limited and Bank of Kathmandu Limited conducting government transactions and release report from 79 DTCOs and payment centers.

Government Expenditure

53. Government expenditure, on cash basis, increased by 19.8 percent to Rs. 499.96 billion in 2014/15 compared to an increase of 16.3 percent to Rs. 417.47 billion in 2013/14. An increase in recurrent and capital expenditure contributed to such a growth of total expenditure during the review year.



54. During the review year, recurrent expenditure increased by 10.9 percent to Rs. 328.98 billion compared to a growth of 21.7 percent in the preceding year. Such expenditure stood at 82.5 percent of annual budget estimate for 2014/15. The review year witnessed normal growth in recurrent expenditure as against the higher growth induced primarily by Constitution Assembly election in the previous year.

55. In the review year, capital expenditure increased by 26.6 percent to Rs. 77.67 billion, 66.5 percent of annual budget estimate, compared to its growth of 19.8 percent in the previous year.

Box 8 : Major Fiscal Indicators
(As Percent of GDP)

Heads	2012/13	2013/14	2014/15
Total Expenditure	21.2	21.5	23.5
Recurrent expenditure	14.4	15.3	15.5
Capital expenditure	3.0	3.2	3.7
Revenue	17.5	18.4	19.1
Tax Revenue	15.3	16.1	16.8
Fiscal Deficit	-1.8	-0.7	-1.8

56. During the review year, financial expenditure increased by 57.0 percent to Rs. 93.30 billion, 91.1 percent of annual budget estimate, compared to its growth of 14.1 percent in the previous year. Increase in share and loan investment in hydropower projects and substantial repayment of domestic debt by the GoN contributed to the higher growth of financial expenditure in the review year.

Budget Deficit

57. In the review year, government budget on cash basis remained at a deficit of Rs. 38.62 billion. Such budget deficit was Rs. 13.75 billion in 2013/14. Low growth in resource mobilization relative to government expenditure accounted for such a budget deficit during the review year. The ratio of budget deficit-to-GDP remained at 1.8 percent in the review year.

Sources of Deficit Financing

58. Domestic borrowings of Rs. 42.42 billion was mobilized in 2014/15. This accounted for 2.0 percent of GDP. Domestic borrowing of Rs. 19.98 billion was mobilized in the previous year.

59. The GoN repaid principal of domestic borrowings of Rs. 47.45 billion in 2014/15. Moreover, the GoN had cash balance of Rs. 41.08 billion (including the previous year's balance of Rs. 23.50 billion) at NRB at the end of 2014/15.

Government Debt

60. The outstanding foreign loan of the GoN stood at Rs. 342.96 billion in mid-July 2015. The outstanding domestic debt of the GoN declined from Rs. 201.82 billion at mid-July 2014 to Rs. 196.79 billion in mid-July 2015.

Box 9 : Public Debt Situation

	Public Debt Indicators	2012/13	2013/14	2014/15
1	Total Debt/ GDP	31.9	28.3	25.4
2	External Debt/ GDP	19.7	17.9	16.1
3	Domestic Debt/ GDP	12.2	10.4	9.3
4	External Debt/ Exports	184.0	153.4	138.5
5	External Debt Servicing/ Exports	9.5	8.9	8.1
6	Total Debt Servicing/ Revenue	16.5	14.6	18.7
7	Domestic Debt Servicing/ Revenue	10.7	9.2	13.6
8	External Debt Servicing/ Revenue	5.8	5.4	5.1

Note: IMF Promissory Note and overdraft amount are not included in Domestic Debt.
Source: FCGO and NRB

61. Both external debt/GDP and domestic debt/ GDP ratios of the GoN has been declining in the last few years. Consequently, the total debt of the GoN to GDP ratio stood at 25.4 percent in

2014/15. Total debt servicing/revenue ratio, however, increased to 18.7 percent in the review year (Box 9).

Government Budget for 2015/16

62. The GoN announced the budget for 2015/16 on 14 July 2015. The budget, which is focused on reconstruction works, has announced the establishment of "National Reconstruction Fund" and issuance of reconstruction bonds for raising funds. Besides, the budget has made several important provisions related to the financial sector (Box 10).

Box 10: Provisions Related to Banking Sector in 2015/16 Budget

Development and consolidation of the financial sector: Implementing Financial Sector Development Strategy, legal and policy arrangements for regulating and supervising saving and credit cooperatives as well as micro credit institutions; continuing policy of merger and acquisition of the bank and financial institutions; making institutional arrangements and policy provision aimed at avoiding duplication in the micro credit; implementing cooperatives and poverty management information system.

Expanding access to finance: Expanding branchless and mobile banking facilities, and campaigning for opening at least one bank account for each household.

Increasing credit flows to productive and infrastructure sector: Provisioning of concessional loan and capital grant for the cooperative societies, farmers associated with cooperatives and groups of entrepreneurs engaged in activities related to agriculture small and medium industries; accomplishing the primary task to establish infrastructure development bank in participation with private sector, and restructuring NIDC Development Bank and Hydropower Investment and Development Company so as to make them capable to invest in infrastructure.

Minimizing negative economic effects of the earthquake: Issuing the “Reconstruction Bond” to mobilize resources for "National Reconstruction Fund", provisioning special housing loan for earthquake affected households up to Rs. 2.5 million within the Kathmandu Valley and Rs. 1.5 million outside the Valley for wishing to reconstruct their houses at a 2 percent concessional interest rate; setting up Economic Rehabilitation Fund under NRB for providing refinancing facility and interest subsidy for the sectors including earthquake affected residential home, agriculture, business and tourism.

Reform in payment process: Making arrangement to disburse the cash transfer provided by the state through bank account; determining the ceiling of amount for cash transaction; introducing compulsory provision to deposit revenue above Rs. 500,000 only through cheque.

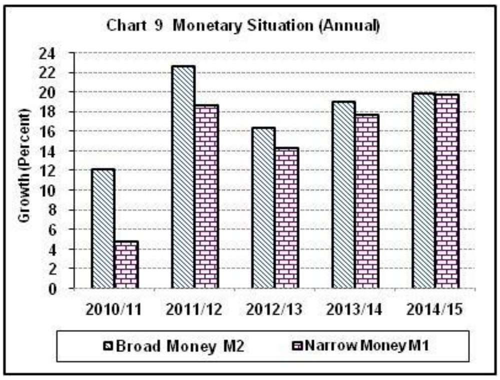
Capital account convertibility: Amending the Foreign Exchange Regulation Act and Foreign Investment Prohibition Act.

Source: FY 2015/16 Budget, Ministry of Finance.

Monetary Situation

Money Supply

63. Broad money supply (M2) increased by 19.9 percent in 2014/15 compared to an increase of 19.1 percent in the previous year. Likewise, narrow money supply (M1) grew by 19.7 percent in the review year compared to a growth of 17.7 percent in the previous year.



64. Net foreign assets (after adjusting foreign exchange valuation gain/loss) increased by Rs. 144.85 billion (24.2 percent) during the review year compared to an increase of Rs. 127.13 billion (27.2 percent) in the previous year. A higher inflow of remittances along with a decelerated growth of imports resulted in an expansion of net foreign assets in the review year.

Domestic Credit

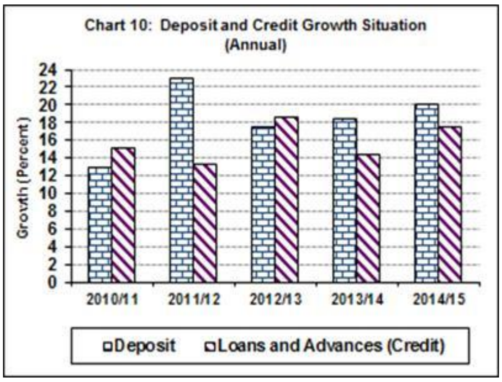
65. Domestic credit increased by 14.9 percent in the review year compared to a growth of 12.7 percent in the previous year. Increase in claims on the private sector as well as financial institutions resulted in a higher growth of domestic credit in the review year. Likewise, claims on the private sector increased by 19.4 percent in the review year compared to a growth of 18.3 percent in the previous year.

Reserve Money

66. Reserve money increased by 14.3 percent in the review year compared to an increase of 23.3 percent in the previous year. The absorption of liquidity through deposit collection auction accounted for a slower growth of reserve money.

Deposit Mobilization

67. Deposits at banks and financial institutions (BFIs) increased by 20.1 percent (Rs. 282.06 billion) in the review year compared to an increase of 18.4 percent (Rs. 218.68 billion) in the previous year. Deposits at commercial banks and development banks increased by 21.4 percent and 15.2 percent respectively while that of finance companies decreased by 0.6 percent in the review year compared to the respective increase of 17.8 percent, 29.1 percent and 5.7 percent in the previous year.



Credit Disbursement

68. Loans and advances of BFIs increased by 17.5 percent (Rs. 229.30 billion) in the review year compared to a growth of 14.4 percent (Rs. 165.48 billion) in the previous year. In the review period, loans and advances of commercial banks, development banks and finance companies increased by 18.8 percent, 13.5 percent and 0.3 percent respectively. Likewise, credit to the private sector from BFIs increased by 19.8 percent (Rs. 221.61 billion) in the review year compared to an increase of 18.7 percent (Rs. 176.14 billion) in the previous year. In the review year, private sector credit from commercial banks, development banks and finance companies increased by 22.0 percent, 16.0 percent and 0.4 percent respectively.

69. BFIs' credit exposure to the production, construction, wholesale and retail trade sectors shows a remarkable growth in the review year. Credit to production sector increased by Rs. 32.89 billion (14.8 percent) in the review year compared to an increase of Rs. 32.10 billion (16.8 percent) in the previous year. Likewise, credit to the construction sector increased by Rs. 33.31 billion (27.9 percent), the wholesale and retail trade sector by Rs. 53.23 billion (21.8 percent) and the transportation, communication and public service sector by Rs. 12.75 billion (27.0 percent) during the review year. The credit to the construction sector, wholesale and retail trade sector and transportation, communication and public service sector had increased by Rs. 23.49 billion (24.5 percent), Rs. 45.94 billion (23.2 percent) and Rs. 3.45 billion (7.9 percent) respectively in the previous year. In the review year, credit to the agriculture sector increased by Rs. 14.25 billion (28.0 percent) compared to an increase of Rs. 11.13 billion (28.0 percent) in the previous year.

70. Financial deepening increased in 2014/15. Indicators reflecting financial deepening such as ratios of total deposit, loans and advances and claims on private sector to GDP increased significantly compared to the previous year (Box 11).

Box 11 : Major Monetary and Financial Indicators (in percent)

Indicators	2012/13	2013/14	2014/15
M2/GDP	77.6	80.7	88.4
Total Deposits/GDP	70.1	72.5	79.5
Loans and Advances/GDP	67.7	67.6	72.6
Claims on Private Sector/GDP	57.4	59.3	64.7
Broad Money (M2) Multiplier	3.7	3.6	3.8

Liquidity Management

71. In 2014/15, the NRB mopped up liquidity of Rs. 155.0 billion through deposit auctions, Rs. 315.80 billion through reverse repo auction and Rs. 6.0 billion through outright sale auction on cumulative basis. In the previous year, Rs. 602.50 billion was mopped up through reverse repo and Rs. 8.50 billion through outright sale auction.

72. In the review year, the NRB injected net liquidity of Rs. 396.72 billion through the net purchase of USD 4.03 billion from foreign exchange market (commercial banks). Net liquidity of Rs. 343.46 billion was injected through the net purchase of USD 3.52 billion in the previous year.

73. The NRB purchased Indian currency (INR) equivalent to Rs. 348.09 billion through the sale of USD 3.50 billion in the review year. INR equivalent to Rs. 307.98 billion was purchased through the sale of USD 3.14 billion in the previous year.

Inter-bank Transaction and Standing Liquidity Facility

74. In the review year, inter-bank transactions of commercial banks stood at Rs. 374.70 billion and those of other financial institutions (excluding transactions among commercial banks) amounted to Rs. 226.91 billion. These were Rs. 200.76 billion and Rs. 171.06 billion respectively in the previous year. The BFIs used standing liquidity facility (SLF) of Rs. 10.31 billion in the review year.

Interest Rates

75. Both the weighted average of 91-days Treasury Bill rate and inter-bank transaction rates increased in the last month of 2014/15 compared to a year ago. The weighted average 91-days Treasury Bill rate increased to 0.1739 percent in the review month from 0.02 percent a year ago. The weighted average inter-bank transaction rate among commercial banks that was 0.16 percent a year ago reached 1.01 percent in the review month. Likewise, the weighted average inter-bank rate among other financial institutions increased to 3.89 percent from 2.40 percent a year ago.

76. Weighted average interest rate spread of commercial banks inched down to 4.61 percent in the review month from 5.21 percent a year ago and the average base rate came down to 7.88 percent from 8.36 percent a year ago.

Presence of Banks and Financial Institutions

77. The total number of banks and financial institutions licensed by NRB came down to 193 in mid-July 2015 from 200 a year ago (Box 12). The total number of commercial banks stood 30 while the number of development banks, finance companies and microfinance development banks stood at 76, 48 and 39 respectively as of mid-July 2015. Despite the decline in the number of BFIs due to merger and acquisition, financial access has widened because of expansion in number of BFIs branches from 3430 at mid-July 2014 to 3838 at mid-July 2015 together with the expansion of some products such as mobile banking and branchless banking.

Box 12 : Number of Banks and Financial Institutions

Bank and Financial Institutions	Number of BFIs		Branches of BFIs	
	2014 (Mid-July)	2015 (Mid-July)	2014 (Mid-July)	2015 (Mid-July)
Commercial Banks	30	30	1547	1672
Development Banks	84	76	818	808
Finance Companies	53	48	239	242
Microfinance Development Banks	33	39	826	1116
Total	**200**	**193**	**3430**	**3838**

Non-Performing Loans of Banks and Financial Institutions

78. The ratio of non-performing loan (NPL) to total loans of BFIs dropped to 3.33 percent in mid-July 2015 compared to 3.76 percent a year ago.

Box 13 : Non-performing Loans of Banks and Financial Institutions

(In percent)

Institutions	2014 (Mid-July)	2015 (Mid-July)
Commercial Banks	2.92	2.63
Development Banks	4.16	3.58
Finance Companies	14.33	14.58
Overall	3.76	3.33

Securities Market

79. NEPSE index decreased by 7.2 percent to 961.2 points in mid-July 2015 on y-o-y basis. This index had increased by 99.9 percent to 1036.1 points a year ago.

80. The y-o-y stock market capitalization decreased by 6.4 percent to Rs. 989.40 billion in mid-July 2015. The ratio of market capitalization to GDP stood at 46.6 percent in mid-July 2015 compared to 54.4 percent a year ago.

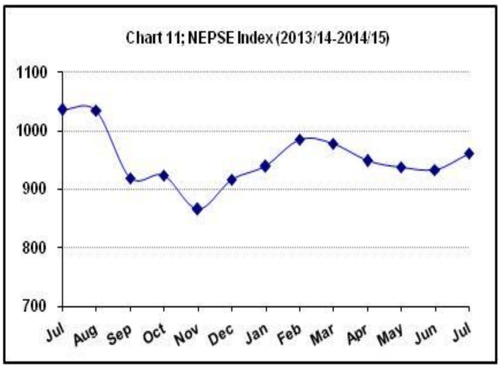


Chart 11; NEPSE Index (2013/14-2014/15)

81. Of the total market capitalization as of mid-July 2015, the share of banks and financial institutions (including insurance companies) stood at 77.7 percent. Hydropower, manufacturing and processing companies, hotels, trading and others recorded a share of 7.0 percent, 3.0 percent, 2.5 percent, 0.1 percent and 9.6 percent respectively.

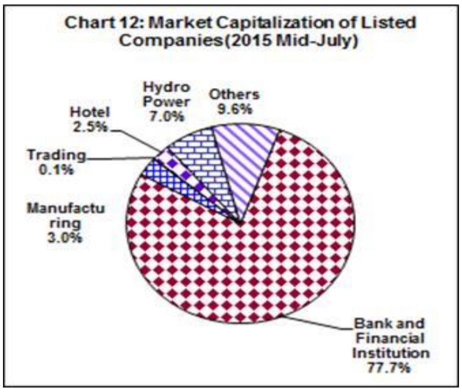


Chart 12: Market Capitalization of Listed Companies(2015 Mid-July)

82. The total number of companies listed at the NEPSE decreased from 237 in mid-July 2014 to 232 in mid-July 2015. Merger of some banks and financial institutions during this period resulted in a decline in the number of listed companies. Of the total listed companies, the number of banks and financial institutions (including insurance companies) stood at 198 followed by production and processing industries (18), hotels (4), business entities (4), hydropower (6) and other companies (2).

83. On y-o-y basis, total paid-up capital of the listed companies increased by 22.6 percent to Rs. 179.69 billion in mid-July 2015. Securities worth Rs. 24.45 billion comprising ordinary shares of Rs. 9.94 billion, right shares of Rs. 1.54 billion and bonus shares of Rs. 12.97 billion were listed in the NEPSE during 2014/15.

Summary of Current Macroeconomic Situation

84. The analysis of the overall macroeconomic situation of 2014/15 shows that there are some structural problems in the economy despite the sound macroeconomic fundamentals. The significant surplus in BoP, comfortable reserve position and single digit inflation; all indicate a stable macroeconomic situation. However, the slump in economic activities is the matter of concern. The devastating earthquake that struck in the fourth quarter of the review year has severely affected the economic development of the country.

85. The decline in export, the mirror image of economic activities, is another matter of concern. Though export price index is on increasing trend, the main reasons behind the failure to reap its benefits are the capacity constraints in the productive sectors and inadequate development of infrastructures.

86. On fiscal front, resource mobilization of the government is satisfactory as reflected in the rising revenue-to-GDP ratio. However, capital expenditure has not increased relative to resource mobilization. The accumulation of cash balance of the government at NRB due to low expenditure relative to resource mobilization implies the existence of entrenched structural problems in the public spending system.

87. The public debt-to-GDP ratio, which has been continuously falling in the last few years, declined further to 25.4 percent in mid-July 2015. This shows the improvement in the debt sustainability of the nation and an ample fiscal space for building necessary infrastructure for economic development. The utilization of such fiscal space for nation building, however, stands as a challenge.

88. The balance of payment recorded a huge surplus of Rs. 144.85 billion in the review year. The country needs to utilize foreign exchange reserves generated from such BoP surplus for the development of infrastructures. Due consideration needs to be given to utilize such surplus in support of nation building process.

89. Monetary aggregates were kept at the desired level in 2014/15. Despite high growth in net foreign assets, this was possible mainly due to liquidity absorption through open market operations such as the deposit collection auction. This has also helped to contain inflation within the targeted level.

90. A number of banks and financial institutions merged with each other as a result of NRB's initiative to consolidate the financial system. The merger/acquisition process is expected to further accelerate in the coming days. Together with merger and acquisition of financial institutions, NRB has been licensing new microfinance institutions and encouraging expansion of bank branch network in areas of low financial access. This has resulted in widening the financial access together with the consolidation of financial institutions. The challenge before the nation is to prioritize the task of financial sector development along with the financial sector stability set in a dynamic mode through the promotion of financial access and consolidation of the financial sector.