Nepal Rastra Bank

Research Department

Current Macroeconomic Situation of Nepal

(Based on the First Month's Data of 2015/16)

Growth Outlook

1. The real GDP at basic price is projected to grow 6 percent in 2015/16 compared to a growth of 3 percent in the previous year. Of the gross value added output, the agricultural sector, which contributes around one third of GDP is projected to grow 1.7 percent while non-agriculture sector is projected to show a growth of 7.7 percent. Stepped up works relating to post-earthquake reconstruction and rehabilitation and a pick up in mega projects of national priority where expected to underpin the growth outlook of 6 percent for 2015/16 as enshrined in the government budget and monetary policy of 2015/16.

2. Generally, monsoon remains active in Nepal during June 10 to September 23 every year. According to the monsoon report based on information gathered from 21 different centers of the country by the Department of Hydrology and Meteorology, the average rainfall during Jun 10 to August 15 this year has been 74.2 percent of 30 years' average rainfall. This is likely to dampen the agricultural output further.

3. During the first few weeks starting from mid-July, eastern and mid-terai region witnessed low rain fall. As a result, paddy plantation could not take place on time in one fourth of paddy land. However, the paddy plantation has improved with the reactivation of monsoon since the second week of August.

4. As a result of continuous strike in terai starting from the third week of August, agriculture sector has suffered on account of disturbances in the supply of fertilizers and market access of agricultural products. Similarly, non-agriculture sector including manufacturing, construction, trade, hotel and tourism sectors are also affected adversely.

5. The post earthquake reconstructions and other developmental activities did not get momentum in the first month of the current fiscal year. Likewise, construction works on projects of national importance relating to roads, irrigation and hydroelectricity could not take due course. Maintenance and construction of strategically important Araniko Highway, access roads of mega hydro projects, Melamchi Drinking Water Project remained sluggish. The construction work of Upper Tamakoshi obstructed by earthquake has not yet resumed.

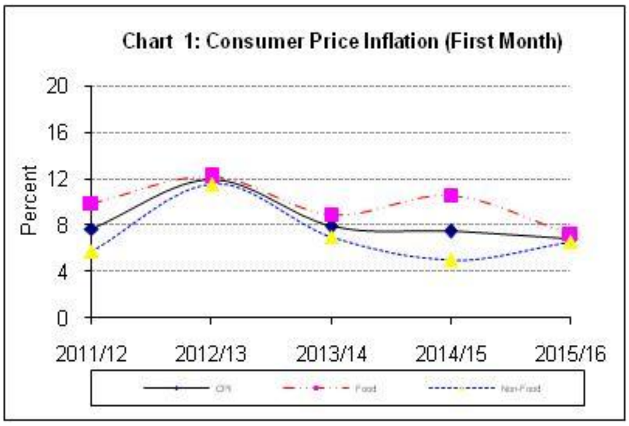
6. Among two major customs points of foreign trade of Nepal with China, Rasuwa-Kerung customs remained closed and Tapotani customs point has not yet been fully operational.

7. All these developments relating to economic activity of the first month do not portend well, and rather cast a shadow on growth outlook for 2015/16.

Inflation, Salary and Wage Rate

Consumer Price Inflation

8. Based on the revised basket of goods and services as per the results of the fifth Household Budget Survey, the y-o-y inflation as measured by the consumer price index (CPI) increased by 6.9 percent in mid-August 2015 compared to 7.5 percent in the corresponding period of the previous year. The indices of food and beverage group and non-food and services group increased by 7.3 percent and 6.6 percent respectively during the review period. Such indices had increased by 10.6 percent and 5 percent respectively in the corresponding period of the previous year.



9. Under food and beverage group, price index of pulses and legumes sub-group increased by the higher rate of 26.4 percent during the review period compared to an increase of 7.8 percent in the corresponding period of the previous year. The price indices of spices sub-group and milk products and eggs sub-group, which had increased by 2.6 percent and 9.5 percent in the corresponding period of the previous year, increased by 9.8 percent and 9.3 percent respectively during the

Box 1: Consumer Price Index Based on the Results of Fifth Household Budget Survey

Nepal Rastra Bank conducted the Fifth Household Budget Survey to update the basket of goods and services and their weights for constructing national consumer price index. The survey collected information on household income and expenses from 8028 households selected from 207 wards of 84 market centers that covered 55 districts of the country.

From the survey results, the weight for food and beverage group found to be 43.91 percent whereas the weight for non-food and service group found to be 56.09 percent. The base year for the new series of CPI is 2014/15.

In the new series of CPI, 496 goods and services have been included in the commodity basket among which 402 are goods and 94 are services. For price collection, 60 market centers have been selected out of which 23 market centers are from Terai Region, 32 centers from Hills and 5 centers from Mountain Region. Among the selected market centers, 29 are rural market centers while 31 are urban market centers.

review period. The price indices of cereal grains and their products sub-group and alcoholic drinks sub-group increased by 9.1 percent and 8.4 percent respectively during the review period compared to an increase of 10.9 percent and 19.4 percent respectively in the corresponding period of the previous year. The price index of sugar and sweets sub-group, which had decreased by 0.6 percent in the corresponding period of the previous year, decreased by 0.3 percent in the review period.

10. Under non-food and services, the price index of education sub-group increased by 12.1 percent during the review period compared to an increase of 5.5 percent in the corresponding period of the previous year. The price indices of clothing and footwear sub-group and housing and utilities sub-group, which had increased by 8.1 percent and 2.7 percent in the corresponding period of the previous year, increased by 9.7 percent and 9.6 percent respectively. During the review period, the price indices of furnishing and household equipment sub-group and communication sub-group increased by 4.1 percent and 3.5 percent respectively. The price index of furnishing and household equipment sub-group had increased by 5.4 percent whereas the price index of communication sub-group had decreased by 0.5 percent in the corresponding period of the previous year. The price index of transport sub-group decreased by 4 percent in the review period compared to an increase of 3.7 percent in the corresponding period of the previous year.

11. In terms of ecological regions, the price index in the Kathmandu Valley increased by 8.3 percent followed by 7.5 percent in Mountain region, 7.2 percent in Hills and 5.8 percent in Terai region during the review period. Such indices had increased by 7.8 percent in the Kathmandu Valley, 6.7 percent in Hills and 7.7 percent in Terai region in the corresponding period of the previous year.

Wholesale Price Inflation

12. The y-o-y wholesale price index increased by 5.4 percent during the review period compared to a rise of 7.4 percent in the corresponding period of the previous year. The wholesale price indices of agricultural commodities and domestic manufactured commodities increased by 9.4 percent and 5 percent respectively, whereas such index of imported commodities decreased by 2.9 percent in the review period. The increments in agricultural commodities, domestic manufactured commodities and imported commodities were 8.3 percent, 8.2 percent and 5.1 percent respectively in the corresponding period of the previous year.

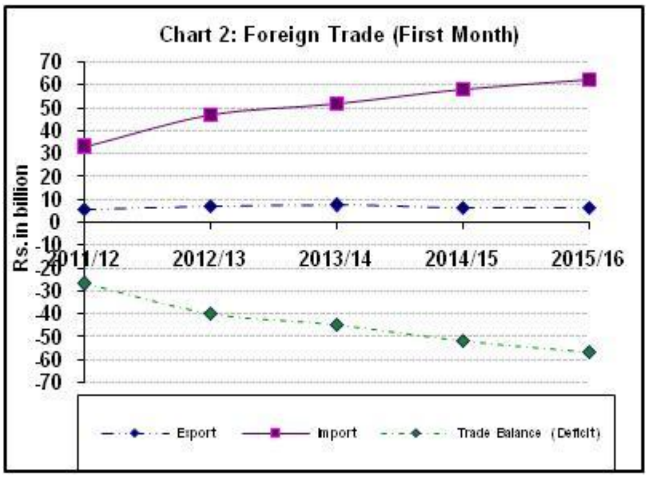
National Salary and Wage Rate

13. The y-o-y salary and wage rate index increased by 6.1 percent during the review period compared to an increase of 12.6 percent in the corresponding period of the previous year. Within the salary and wage rate index, the salary index increased by 1 percent and the wage rate index increased by 7.4 percent compared to an increase of 19.5 percent and 11 percent respectively in the corresponding period of the previous year.

14. The salary indices of bank and financial institutions, public corporations and education sub-group increased by 6 percent, 2.5 percent and 1.5 percent respectively during the review period. Likewise, wage rate indices of agricultural labourer, construction labourer and industrial labourer witnessed a growth of 10.7 percent, 4.6 percent and 1.6 percent respectively in the review period.

External Sector Situation

Foreign Trade



15. Merchandise exports fell further 3.9 percent to Rs. 6.46 billion in the first month of 2015/16. Such exports had dropped by 11.5 percent to Rs. 6.72 billion in the same period of the previous year. The total exports decreased due to the fall in exports to India, China and other countries.

16. Exports to India decreased by 6.2 percent during the review period compared to a decrease of 15.4 percent in the same period of the previous year. Exports to India decreased mainly due to the fall in the exports of zinc sheet, GI pipe, wire, textiles, among others. Similarly, exports to China marginally decreased by 0.5 percent in the review period compared to a decrease of 56.7 percent in the same period of the previous year. This decrease is mainly attributed to the decrease in the exports of tanned skin, rudraksha among others. Similarly, exports to other countries dropped slightly by 0.3 percent in the review period compared to the decrease of 0.8 percent in the same period of the previous year. Exports to other countries decreased due to a drop in the exports of pulses, tea, handicrafts, among others. In US dollar terms, exports to China decreased by 5.8 percent to USD 0.9 million during the review period compared to a sharp fall of 57 percent in the same period of the previous year. Similarly, exports to other countries decreased by 5.5 percent to USD 25.2 million in the review period compared to the decrease of 1.5 percent in the same period of the previous year.

17. During the review period, merchandise imports increased by 7.2 percent to Rs. 62.58 billion. Such imports had gone up by 12.5 percent to Rs. 58.36 billion in the same period of the previous year. The growth of imports remained low mainly due to the decrease in the price of petroleum products and also fall in the imports of silver, video television and parts, telecommunication equipment and parts, among others.

18. Imports from India rose by 6 percent in the review period compared to a growth of 16.8 percent in the same period of the previous year. Imports of vehicle and spare parts, cold rolled sheet in coil, MS billet, MS wire rod, among others increased while the import of petroleum products, cement, and electrical equipment, among other decreased in the review period. Likewise, imports from China increased sharply by 38.6 percent in the review period compared to a growth of 23.9 percent in the same

period of the previous year. Imports from China rose due to the increase in the imports of chemical fertilizer, readymade garment, shoes/sandle, vehicle and spare parts, among others. Similarly, imports from other countries decreased by 3.7 percent in the review period compared to a decrease of 2.7 percent in the same period of the previous year. Imports from other countries decreased mainly due to a fall in the imports of silver, chemical fertilizer, telecommunication equipment and parts, copper wire among others. In US dollar terms, imports from China increased by 31.2 percent to USD 82.8 million in the review period compared to an increase of 23 percent in the same period of the previous year. Similarly, imports from other countries decreased by 8.8 percent to USD 122.2 million in the review period compared to the decrease of 3.4 percent in the previous year.

19. Total trade deficit during the review period grew 8.7 percent to Rs. 56.12 billion compared to an increase of 16.6 percent in the same period of the previous year. Trade deficit with India and China increased by 7.4 percent and 39.1 percent respectively. Such deficits had gone up by 22.2 percent and 27.3 percent respectively in the same period of the previous year. On the other hand, trade deficit with other countries decreased by 4.6 percent in the review period compared to the decline of 3.2 percent in the same period of the previous year. The FOB based trade deficit increased by 8.5 percent to Rs. 53.73 billion in the review period. Such deficit had gone up by 15.8 percent in the same period of the previous year.

20. Exports-imports ratio declined to 10.3 percent in the review period as a result of decrease in exports and increase in imports. Such a ratio had remained at 11.5 percent in the same period of the previous year.

Services

21. The gross services receipts in the review period decreased by 16 percent to Rs. 9.70 billion which had increased by 29.8 percent in the same period of the previous year. The travel receipts and other services receipts decreased by 9.9 percent and 44.8 percent respectively in the review period. On the other hand, government services receipts increased by 57 percent in the review period. The services receipts fell on account of the devastating earthquake of April 25, 2015, which caused massive loss in tourism including other service sectors.

22. The total service expenses increased by 16 percent in the review period compared to the 24.4 percent increase in the same period of the previous year. The transportation expenses, travel expenses and other service expenses increased by 11.3 percent, 24 percent and 0.4 percent respectively in the review period.

23. The net services receipts remained in deficit by Rs. 1.43 billion on account of a decrease in services receipts and increase in service expenses in the review period compared to Rs. 1.96 billion surplus in the same period of the previous year.

Transfers

24. The net transfer receipt increased by 29.7 percent to Rs. 61.32 billion in the review period due to an upsurge in foreign grants, remittance inflows and pension. It had decreased by 1.5 percent in the same period of the previous year.

25. The gross transfer receipt increased by 29.5 percent to Rs. 61.48 billion in the review period against a decrease of 1.7 percent in the same period of the previous year. The total foreign grants of Rs. 4.46 billion was received in the review period. Such grant was Rs. 2.26 billion in the same period of the previous year.

26. The remittances increased by 26.3 percent to Rs. 53.27 billion in the review period compared to a growth of 0.8 percent in the same period of the previous year. In US dollar terms, the remittances increased by 19.6 percent to USD 520.1 million compared to a growth of 0.1 percent in the same period of the previous year.

Box 2: The Number of Nepalese Workers going abroad for Foreign Employment *

Month/Year	2013/14	2014/15	2015/16
Sawan	45937	42309	38081
Bhadra	24214	51551	-
Ashoj	31959	35550	-
Kartik	31949	43213	-
Mangsir	41634	53354	-
Paush	50032	45362	-
Magh	37285	48941	-
Fagun	48552	44460	-
Chaitra	45854	52210	-
Baishak	54173	31375	-
Jestha	54926	37962	-
Asad	61717	26600	-
Total	**528232**	**512887**	**38081**
Percentage Change	16.5	-2.9	-10.0**

* Based on final approval for foreign employment.
** July/August 2014-July/August 2015
Source:- Foreign Employment Department

27. The number of workers going abroad for foreign employment, which directly affects remittances inflow, has decreased to some extent in recent months. The number of Nepalese workers seeking foreign employment, based on final approval for foreign employment, decreased by 10 percent in the first month of 2015/16 than the level a year ago. It had decreased by 7.9 percent in the same period of the previous year. On the monthly basis, it increased by 43.2 percent in the review month compared to that of the previous month.

28. The pension income increased by 24.5 percent to Rs. 3.75 billion in the review period. Such income was Rs. 3.01 billion in the same period a year ago.

Current Account

29. The current account registered a surplus of Rs. 8.15 billion during the review period compared to a surplus of Rs. 1.25 billion in the same period of the previous year. The surplus of current account is mainly attributed to the low growth of merchandise import, increase in remittances and grants, among others. The current account surplus in US dollar terms was USD 79.5 million in the review period compared to USD 12.8 million of the same period of the previous year.

Capital and Financial Account

30. The capital transfer under the capital account amounted to Rs. 754.6 million in the review period compared to Rs. 542.1 million in the same period of the previous year.

31. Foreign Direct Investment (FDI) inflow under the financial account amounted to Rs. 44.3 million in the review period compared to Rs. 2 million in the same period of the previous year.

32. In 2014/15, dividend payment to FDI companies, based on approval, stood at Rs. 7.21 billion. No dividend was paid in the first month of current fiscal year 2015/16.

Box 3: Dividend Payment to FDI Companies*

(Rs. in million)

SN	Sectors	2014/15 Annual
1	Financial Sector	1794.43
2	Communication Sector	4.00
3	Hydro Power Sector	2874.48
4	Industry Sector	2299.19
5	Service Sector	238.61
	Total	**7210.71**

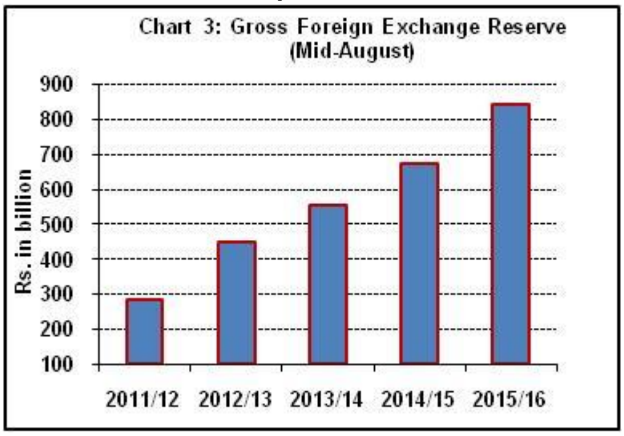
**Based on approval from NRB*

BOP Situation

33. The overall BOP showed a surplus of Rs. 4.95 billion in the review period compared to a surplus of Rs. 2.77 billion in the same period of the previous year. In US dollar terms, the BOP recorded a surplus of USD 48.4 million compared to USD 28.6 million in the same period of the previous year.

Foreign Exchange Reserves

34. The gross foreign exchange reserves increased by 2.3 percent to Rs. 842.53 billion as at mid-August 2015 from Rs. 823.87 billion as of mid-July 2015. Such reserves had increased by 1.3 percent in the same period of the previous year. The gross foreign exchange reserves in US dollar terms decreased by 0.3 percent to USD 8.12 billion in mid-August 2015. Such reserves had increased by 0.2 percent in the same period of the previous year.



35. The foreign exchange reserves held by NRB increased by 2.6 percent to Rs. 721.09 billion as at mid-August 2015 compared to Rs. 702.88 billion as of mid-July 2015. Such reserves had increased by 1.2 percent in the same period of the previous year. The share of NRB in total reserves stood at 85.6 percent as at mid-August 2015.

36. The foreign exchange reserves of banks and financial institutions (except NRB) increased by 0.4 percent to Rs. 121.44 billion as at mid-August 2015 compared to

Rs. 121 billion as of mid-July 2015. Such reserves had increased by 1.5 percent in the same period of the previous year.

37. During the review period, the inconvertible foreign exchange reserves increased by 2.5 percent to IRs 122.72 billion. Such reserves had decreased by 3.6 percent in the same period of the previous year. The share of inconvertible foreign exchange reserves in total reserves stood at 23.3 percent as at mid-August 2015.

Foreign Exchange Adequacy Indicators

38. The reserve adequacy indicators remained satisfactory in the review period. Based on the imports of the first month of current fiscal year, the foreign exchange holding of the banking sector is sufficient for financing merchandise imports of 13.8 months, and merchandise and services imports of 11.7 months. The ratio of reserve to GDP, reserve to imports and reserve to M2 remained 39.7 percent, 97.3 percent and 45.1 percent respectively in the review period. Such ratios were 38.8 percent, 93.2 percent and 43.9 percent as at mid-July 2015.

Box 4 : Reserve Adequacy Ratio (Percent)

Description	Mid-July		Mid-August	
	2014	2015	2014	2015
Reserve/GDP	34.3	38.8	34.7[a]	39.7[a]
Reserve/Imports*	83.1	93.2	84.2	97.3
Reserve/M2	42.5	43.9	43.4	45.1

* Goods and services import
a, GDP data of the previous year is used.

Export-Import Price Index

39. The y-o-y unit value export price index based on customs data increased by 11.4 percent in the first month of 2015/16 compared to 6.5 percent rise in the same period of the previous year. Increase in price of major export items such as big cardamom, jute, plastic utensil, lentil caused the export price index to rise in review period.

40. The y-o-y unit value import price index based on customs data decreased by 8.5 percent in the review period. It had increased by 9.1 percent in the corresponding period of the previous year. Price of major import items such as diesel, L.P. gas, petrol caused import price index to decrease in review period.

41. Terms of Trade (TOT) index increased by 21.8 percent on y-o-y basis in the first month of 2015/16 compared to a decrease of 2.4 percent in the corresponding period of the previous year.

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

42. The price of oil (Crude Oil Brent) in the international market decreased sharply by 52.8 percent to USD 47.77 per barrel in mid-August 2015 from USD 101.13 per barrel a year ago. The decrease in the price of petroleum product during this period is attributed due to the decrease of demand for petroleum products in Japan, China

and Euro area accompanied with no decrease in production by the OPEC, and USA. Similarly, the price of gold declined by 13.7 percent to USD 1118.80 per ounce in the mid-August 2015 from USD 1296 per ounce a year ago.

43. Nepalese currency vis-à-vis the US dollar depreciated by 2.5 percent in mid-August 2015 from mid-July 2015. It had depreciated by 1.1 percent in the same period of the previous year. The exchange rate per US dollar stood at Rs. 103.71 in mid-August 2015. It was Rs. 101.14 in mid-July 2015.

Policy Measures for Narrowing Down Trade Deficit

44. Nepal has undertaken some policy initiatives to promote export and facilitate international transactions. Some of the developments in this area are discussed below.

Export Cash Subsidy

45. With a view to promoting export, the GoN has made a provision of providing cash incentive of 2 percent for export of specified 10 industrial goods, 1 percent for export of specified 15 industrial and 7 agricultural goods. Under this provision, a reimbursement of Rs 250.3 million was made for exporters as cash subsidy in 2014/15. In the first month of the current fiscal year, Rs 8.83 million has been reimbursed as cash subsidy for export of four products including leather products, pulses, pashmina and carpet.

Export Refinance

46. The NRB has been providing export refinance at 1 percent to help promote export. Under this facility, banks and financial institutions are not allowed to charge borrowers more than 4.5 percent interest rate on such refinance. The utilization of export refinance has been increasing in the recent years. Under this, Rs 2.92 billion was utilized in 2014/15 and Rs 20 million in the first month of 2015/16.

Gold Imports

47. The NRB on August 11, 2015 amended the "Gold import and selling procedure, 2068" which increased the daily import quota on gold to 20 kilogram from 15 kilogram until mid-October 2015. This provision is expected to help improve export of jewelries.

Trade Facilitation

48. The payment ceiling through TT/Draft for import from other countries (except India) has been increased to USD 40,000 from USD 35,000 effective from August 3, 2015. This provision is expected to improve the import of industrial raw materials and thereby expansion of Nepalese export.

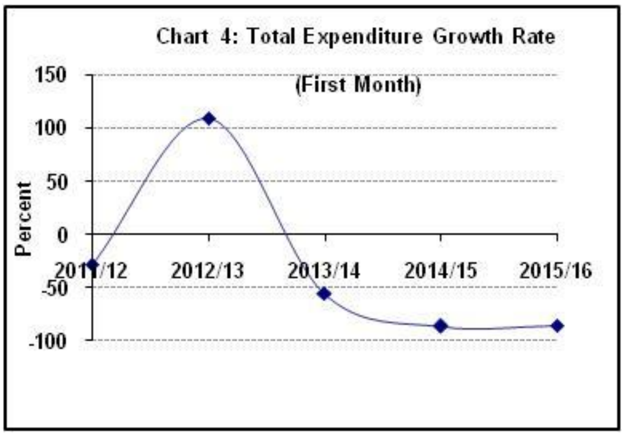
Provisions on INR Exchange Facility

49. The NRB on August 3, 2015, has further eased the exchange facility of Indian Currency (IC) for the various government agencies, governmental and semi-governmental organizations, NGOs, INGOs and general public. In addition, a provision is introduced whereby the NRB can provide necessary IC for one week to bank and financial institutions. Similarly, banks and financial institutions are allowed to carry out interbank transaction and borrowing in IC.

Fiscal Situation *

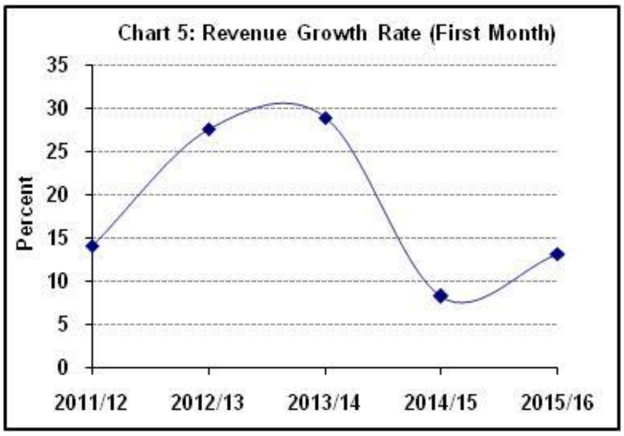
Budget Deficit / Surplus

50. In the first month of 2015/16, government budget on cash basis remained at a surplus of Rs. 31.97 billion. Such budget surplus was Rs. 28.26 billion in the corresponding period of the previous year. The higher surplus in government budget in the review month is attributed to a decline in government expenditure coupled with an increase in revenue collection and foreign grants.



Government Expenditure

51. During the review period, total government expenditure on cash basis dropped by 85.4 percent to Rs. 133 million compared to a decrease of 86.2 percent to Rs. 910 million in the corresponding period of the previous year. Total government expenditure fell on account of the decline in both recurrent and capital expenditure.



Government Revenue

52. During the review period, the government revenue mobilization increased by 13.1 percent to Rs. 30.20 billion. Such revenue had risen by 8.2 percent to Rs. 26.70

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* Based on the data reported by 8 NRB offices, 67 branches of Rastriya Banijya Bank Limited, 44 out of 47 branches of Nepal Bank limited, 9 branches of Everest Bank Limited, 4 branches each of Global IME Bank Limited and Agriculture Development Bank limited, 1/1 branch each of NMB Bank Limited and Bank of Kathmandhu Limited conducting government transactions and release report from 79 DTCOs and payment centres.

billion in the corresponding period of the previous year.

Domestic Debt

53. During the review period, total outstanding domestic debt of the government has remained same as of mid-July 2015 at Rs.196.79 billion. The Budget 2015/16 has made provision to mobilize domestic debt of Rs. 88 billion and domestic debt payment of Rs. 41.10 billion during the current fiscal year.

Budgetary measures for boosting government revenue and increasing government expenditure

54. The budget of 2015/16 has laid out a number of measures aimed at boosting the government revenue and increase government expenditure.

55. On the revenue side, measures introduced are:

a. Mandatory provision to submit income tax return by natural person with annual income exceeding Rs. 4 million.

b. Increase in threshold for the registration of Value Added Tax to Rs. 5 million from Rs. 2 million.

c. Increase in excise duty on cigarette, beer and alcohol.

d. Exemption in dividend tax to special and tourism industries in case of capitalization of their accumulated profit for the expansion of the industry's capacity.

e. Exemption in income tax, excise license fee and house rent tax on the certification of complete loss of business by the District Disaster Relief Committee of the earthquake affected district for those taxpayers who are eligible to submit presumptive tax return in the current fiscal year.

f. Exemption of additional thirty percent income tax to special and tourism industries generating more than hundred employment for Nepalese citizens.

g. Exemption of excise duty and the road maintenance fee on import of vehicle having capacity of 40 or more seats by registered cooperatives and public transport service companies.

h. Exemption of social security tax on payments of pension from the government treasury.

i. Deduction facility while calculating taxable income for the amount deposited in the National Reconstruction Fund and Prime Minister Disaster Relief Fund.

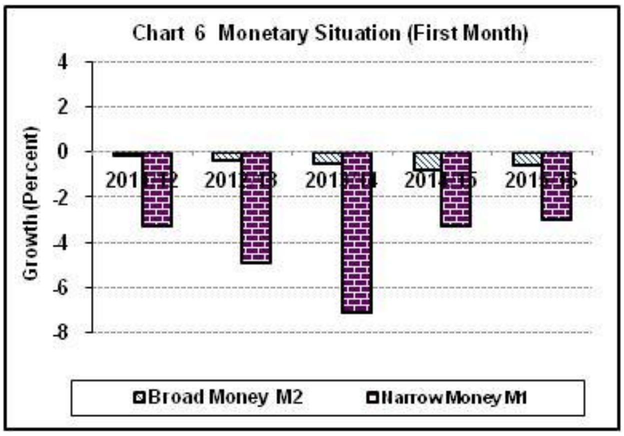
56. On the government expenditure side, measures introduced are:

a. Declaration of fiscal year 2015/16 as 'Budget Implementation Year'.
b. Simplification in procurement process through improvement in the public procurement laws.
c. Initiation of annual program approval and authorization from the very beginning of the fiscal year.
d. Establishment of neutral mechanism that can take decision swiftly for land acquisition and compensation distribution in mega projects.
e. No transfer policy for project directors, chief account and other key project staff working in prioritized projects throughout the project period if their performance level is more than 80 percent.

Monetary Situation

Money Supply

57. Broad money supply (M2) decreased by 0.6 percent in the first month of 2015/16 compared to a decrease of 0.8 percent in the corresponding period of the previous year. Likewise, narrow money supply (M1) declined by 3 percent in the review period compared to a decrease of 3.3 percent in the same period of the previous year. On y-o-y basis, M2 expanded by 20.1 percent and M1 expanded by 20 percent in mid-August 2015.



58. Net foreign assets (after adjusting foreign exchange valuation gain/loss) increased by Rs. 4.95 billion (0.7 percent) during the review period compared to an increase of Rs. 2.77 billion (0.5 percent) in the corresponding period of the previous year. Increase in remittances as well as a lower growth of imports resulted in a higher growth of net foreign assets.

Domestic Credit

59. Domestic credit decreased by 2.2 percent in the review period compared to a decrease of 1.3 percent in the same period of the previous year. On y-o-y basis, domestic credit increased by 14.5 percent in mid-August 2015. A rise in cash balances of GoN with the NRB resulted in a decelerated growth rate of domestic credit in the review period. Likewise, claims on the private sector increased marginally in the review period compared to a growth of 0.8 percent in the corresponding period of the previous year. On y-o-y basis, claims on the private sector increased by 18.5 percent in mid-August 2015 compared to a growth of 19.1 percent a year ago.

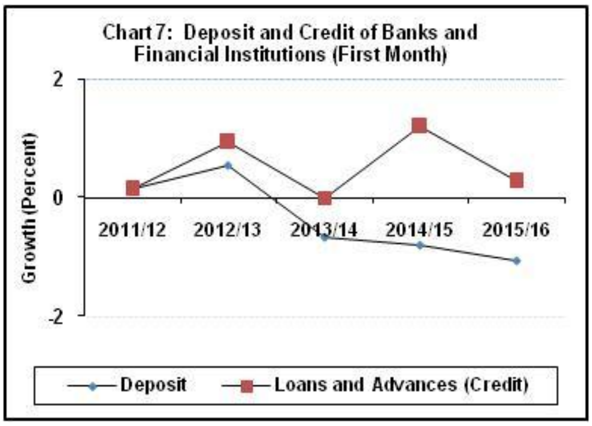
Reserve Money

60. Reserve money decreased by 12.6 percent in the review period compared to a decrease of 4.4 percent in the corresponding period of the previous year. On y-o-y basis, reserve money increased by 4.5 percent in mid-August 2015. The liquidity absorption through deposit collection auction accounted for a lower growth of reserve money.

Deposit Mobilization

61. Deposits at banks and financial institutions (BFIs) decreased by 0.8 percent (Rs. 13.26 billion) in the review period compared to a decrease of 0.6 percent (Rs. 7.87 billion) in the corresponding period of the previous year. Deposits at commercial banks decreased by 0.7 percent while that of development banks and finance companies increased by 0.05 percent, and 0.5 percent respectively in the review period. In the same period of the previous year, deposits at commercial banks and development banks had decreased by 0.1 percent and 2.3 percent respectively. However, such deposits at finance companies had increased by 1.5 percent. On y-o-y basis, deposits at BFIs expanded by 19.8 percent in mid-August 2015.

Credit Disbursement



62. Loans and advances of BFIs increased by 0. 2 percent (Rs. 3.13 billion) in the review period compared to a growth of 0.9 percent (Rs. 12.02 billion) in the corresponding period of the previous year. In the review period, loans and advances of commercial banks, development banks and finance companies increased by 0.5 percent, 0.7 percent and 1.5 percent respectively. Likewise, credit to the private sector from BFIs decreased by 0.4 percent (Rs. 5.39 billion) in the review period compared to an increase of 0.3 percent (Rs. 3.50 billion) in the same period of the previous year. Private sector credit from commercial banks and development banks decreased by 0.1 percent and 2.4 percent respectively, while that of finance companies increased

by 0.5 percent. On y-o-y basis, credit to the private sector from BFIs increased by 19 percent in mid-August 2015.

63. Credit to the industrial production sector increased by Rs. 1.08 billion (0.4 percent) in the review period compared to an increase of Rs. 3.55 billion (1.6 percent) in the same period of the previous year. In the review period, credit to the wholesale and retail trade sector decreased by Rs. 2.04 billion (0.7 percent) while that of construction sector and the transport, communication and public sector increased by Rs. 0.22 billion (0.1 percent) and Rs. 2.31 billion (3.9 percent) respectively. The credit to the wholesale and retail trade sector, construction sector and transportation, communication and public service sector had increased by Rs. 2.92 billion (1.2 percent), Rs. 0.82 billion (0.7 percent) and Rs. 0.68 billion (1.4 percent) respectively in the same period of the previous year. In the review period, credit to the agriculture sector decreased by Rs. 0.67 billion (1.0 percent) compared to a decrease of Rs. 0.35 billion (0.7 percent) in the corresponding period of the previous year.

Liquidity Management

64. In the first month of 2015/16, the NRB mopped up Rs. 57.25 billion liquidity through deposit auctions, Rs. 13 billion through reverse repo auction and Rs. 5.90 billion through outright sale auction on cumulative basis. However, the outstanding deposit collection auction amounted to Rs. 107.25 billion as at mid-August 2015. In the corresponding period of the previous year, Rs. 99.50 billion was mopped up through reverse repo.

65. In the review period, the NRB injected net liquidity of Rs. 34.04 billion through the net purchase of USD 332.50 million from foreign exchange market(commercial banks). Net liquidity of Rs. 26.79 billion was injected through the net purchase of USD 275.65 million in the corresponding period of the previous year.

66. The NRB purchased Indian currency (INR) equivalent to Rs. 32.80 billion through the sale of USD 320 million in the review period. INR equivalent to Rs. 19.39 billion was purchased through the sale of USD 200 million in the corresponding period of the previous year.

Refinance and Productive Sector Lending

67. The NRB has been providing refinance facility to enhance productive sector lending and contribute to export promotion. Utilization of this facility has increased.

Box 5: Status of Refinance
(Rs. in billion)

Particulars	2014/15 (First Month)	2014/15 (Annual)	2015/16 (First Month)
General Refinance	0.06	5.99	0.58
Export Refinance	0.39	2.92	0.02
Total	**0.45**	**8.91**	**0.60**

68. There is a policy-provision for BFIs to disburse credit in the productive sector. Such credit of commercial banks out of their total loans and advance remained 16.4 percent in mid-August 2015.

Inter-bank Transaction and Standing Liquidity Facility

69. In the review period, inter-bank transactions of commercial banks stood at Rs. 54.16 billion and those of other financial institutions (excluding transactions among commercial banks) amounted to Rs. 10.39 billion. These were Rs. 4.18 billion and Rs. 13.11 billion respectively in the corresponding period of the previous year. The BFIs did not use standing liquidity facility (SLF) in the review period like in the same period of the previous year.

Interest Rates

70. Both the weighted average of 91-day Treasury Bill rate and inter-bank transaction rates increased in the first month of 2015/16 compared to a year ago. The weighted average 91-day Treasury Bill rate increased to 0.9478 percent in the review month from 0.0044 percent a year ago. The weighted average inter-bank transaction rate among commercial banks that was 0.15 percent a year ago reached 0.74 percent in the review month. Likewise, the weighted average inter-bank rate among other financial institutions increased to 3.09 percent from 2.50 percent a year ago.

71. Weighted average interest rate spread between deposit and lending rate of commercial banks inched down to 4.55 percent from 4.82 percent a year ago and the average base rate came down to 7.18 percent from 7.68 percent a year ago.

Loans to SMEs and Secured Transactions Registry

72. The nature of collateral accepted for lending is one of the major factors influencing extension of financial access. Studies have shown that higher preference to immovable properties (such as real estate and fixed assets) over the movable ones (such as machinery, instruments, cattle and agriculture products) is major constraints in expanding financial services in the developing countries. The small and medium scale enterprises (SMEs) have been affected due to lack of sufficient fixed assets to be pledged as collateral. In context of SMEs dominance in Nepal, the credit expansion in this sector has not been as expected due to high priority given to the fixed assets as collateral in credit disbursement. Last three-year average data show that banks and financial institutions have extended 59.4 percent of their total credit against the collateral of house and land and 13.6 percent against the collateral of current assets (such as agricultural and non-agricultural products). Likewise, the three-year average of SMEs lending by commercial banks is only 2.3 percent. Thus, insufficient collateral is one of the major constraints for SME finance in Nepal. It is expected that the implementation of secured transaction registry will address this problem. Although the Secured Transaction Act, 2006 is already in place; the delay in establishment of secured transaction registry office has affected the registration process. However, it is recently planned that the registration process is to be undertaken by the Credit Information Center Limited.

Reinstating the Bank Branches Closed during the Conflict

73. Expansion of branch network and new financial products such as mobile banking, branchless banking has contributed to widen the access to finance. The branch network of BFIs reached 3,838 in mid-July 2015 from 3,430 a year ago. The ongoing process of reinstating the commercial bank branches closed during the conflict will be helpful in expanding access to finance. Up to mid-July 2015, 54 branches of Agriculture Development Bank Limited have been re-established while 13 branches are in the process of re-establishment. Likewise, 47 branches of Rastriya Banijya Bank Limited and 26 branches of Nepal Bank Limited have been re-established and 50 and 94 of their branches respectively are in the process of reestablishment. Thus, of the total 284 public sector bank branches closed during the conflict period, 127 branches have been re-established and 157 branches are still in the process of re-establishment.

Box 6: Reinstatement of Bank Branches Closed during the Conflict Period

Particulars	Total	Nepal Bank Ltd.	Rastriya Banijya Bank Ltd.	Agriculture Development Bank Ltd.
Total closed branches	284	120	97	67
Reinstated branches	127	26	47	54
In the process of reinstatement	157	94	50	13

Progress on Zero Interest Refinance Facility for Branch Expansion

74. With an objective of extending financial services in the specified 14 districts including Bhojpur, Okhaldhunga and others having low access to finance; the NRB has made provision to provide interest free loans up to Rs. 5 million and Rs. 10 million to establish branches in and outside the district headquarters respectively for the period of 6 months. However, no such facility was requested by the BFIs in 2014/15. Likewise, there is also a provision to provide interest free loans up to Rs. 3 million to microfinance institutions, if they wish to establish a branch in the specified 22 districts. Under this scheme, the NRB provided Rs. 30 million refinance in 2014/15.

Ratio of Population in Access to Financial Services

75. Nepal FinScope Consumer Survey, 2014 shows that 40 percent of adults in Nepal have access to financial services from NRB licensed BFIs and 21 percent have access to such services from non-bank financial institutions such as cooperatives, insurance companies and remittance companies. This shows that 61 percent of adults in Nepal have access to formal financial services.

Macro prudential Regulation

76. There is a provision to limit credit in real estate sector at 25 percent of total credit disbursement. Such credit flow of BFIs was Rs. 205.96 billion (including Rs. 119.64

million residential home loans less than Rs. 10 million each) in mid-August, 2015. This is 15.16 percent of total credit exposure of BFIs.

77. There are provisions to maintain Loan-to-Value (LTV) ratio at 60 percent while lending in real estate sector, single obligor limit not to exceed 40 percent of the total loans and advances, Statutory Liquidity Ratio (SLR) at 12 percent of total deposits for commercial banks and 9 percent and 8 percent for development banks and finance companies, which collect current and call deposits respectively.

78. BFIs can provide margin lending against share collateral on the basis of average of final price of 180 days or prevailing market price, whichever is less. Such loan remained 1.8 percent of total credit exposure in mid-August 2015.

79. There is a provision of not exceeding 80 percent credit-deposit (local currency deposit and including core capital) ratio. Such ratios of commercial banks, development banks and finance companies stood at 72.53 percent, 70.03 percent and 75.14 percent respectively in mid-August 2015. This shows that BFIs have additional room for credit disbursement.

80. To manage the risk that occurs because of higher institutional deposits in the deposit structure of BFIs, there is a provision for commercial banks to limit institutional deposit at 60 percent of their total deposit. Share of such deposits at BFIs remained at 48.4 percent in mid-August, 2015.

81. Commercial banks are required to maintain 10 percent capital fund ratio of the risk weighted assets and development banks and finance companies are required 11 percent each. Such ratios of commercial banks, development banks and finance companies were 11.94 percent, 16.14 percent and 21.51 percent respectively in mid-August 2015. BFIs are required to maintain capital buffer of 1 percent or more in addition to capital adequacy ratio (CAR) before they distribute dividend.

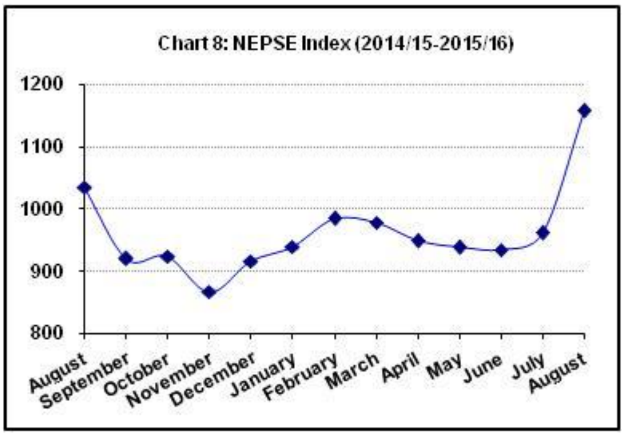
82. There is no limit for commercial banks to collect deposits, while development banks and finance companies can collect financial resources up to 20 times and 15 times of their core capital respectively. Accordingly, development banks' and finance companies' resources collection are 6.7 times and 4.9 times of their core capital respectively in mid-August 2015.

Status of Micro-credit

83. Total Assets/Liabilities of "D" class microfinance institutions increased by 35.8 percent to Rs. 68.68 billion in mid-July 2015. Likewise, total deposits at these institutions reached Rs. 16 billion and total loans and investment Rs. 55.07 billion and Rs. 2.47 billion respectively.

Securities Market

84. The NEPSE index increased by 11.9 percent to 1157.6 points in mid-August 2015 on y-o-y basis. This index had increased by 92.8 percent to 1034.4 points a year ago. The index started to surge with rise in investors' confidence which was attributed to the provision of the hike in paid-up capital of BFIs in the 2015/16 monetary policy.



85. The stock market capitalization on y-o-y point basis increased by 12.9 percent to Rs. 1192.47 billion in mid-August 2015. The ratio of market capitalization to the GDP of 2014/15 stood at 56.1 percent in mid-August 2015 compared to such ratio of 54.4 percent a year ago.

86. Of the total market capitalization in mid-August 2015, the share of banks and financial institutions (including insurance companies) stood at 80.9 percent, hydropower 5.6 percent, manufacturing and processing companies 2.8 percent, hotels 2.1 percent, trading 0.1 percent and others 8.6 percent respectively.

87. Total number of companies listed at the NEPSE decreased from 234 in mid-August 2014 to 231 in mid-August 2015 due to the merger of some BFIs. Of the total listed companies, the number of BFIs (including insurance companies) stood at 197 followed by manufacturing and processing industries (18), hydropower (6), hotels and trading (4 each) and other companies (2).

88. On y-o-y basis, total paid-up capital of the listed companies increased by 24.7 percent to Rs. 212.99 billion in mid-August 2015. In the first month of 2015/16, the total securities worth of Rs. 788 million was listed in the NEPSE, in which the value of bonus shares was Rs. 188 million and the debenture was Rs. 600 million.