MACROECONOMIC ANALYSIS OF NEPAL

Mangsir 2080 (Based on Five months' data published by NRB)

Machhapuchpuchhre Capital

Research, Strategy & Product Development

TABLE OF CONTENTS

1. MONTHLY MACROECONOMIC OVERVIEW

As per South Asian Development Update and Nepal Development Update 2023, Nepal's economic growth is estimated to rebound to 3.9% in the year 2024, and projects Nepal's economy to grow by 5% in 2025. Nepal's gross domestic growth rate was estimated to be 1.9% last year. The economy is expected to rebound due to the lagged impact of the lifting of import restrictions, the rebound in the tourism sector, and the gradual loosening of monetary policy.

The macroeconomic situation in the fifth month of the fiscal year 2080/81 (Mangsir 2080) presents a modestly improving economic outlook overall. The balance of payments (BOP) surplus in Mangsir 2080 is 210.59 Billion. The sustained surplus figure as of the fifth month of the fiscal year provides an optimistic view that the BOP Surplus will continue in the rest of the months in the present fiscal year as well. The BOP Surplus can be attributed majorly to the rising inflow of remittance into the country and declining imports. The inflation rate of Nepal stands at 4.95% as of Kartik 2080 and is below the targeted limit of 6.5% set by NRB.

The price of crude oil has decreased by 6.70% on a Y-o-Y basis from USD 82.34 per barrel to USD 76.84 per barrel. Such decrease was influenced by factors such as fears of global recession, hesitation on follow through on oil output cuts by OPEC+, and the US's oil production achieving record levels. The decrease in price per barrel also leads to a decrease in the import figure of the country as petroleum products fall into the topmost import of the country (Market share =18.12%). The GoN's policy to promote electric vehicles within the country is expected to lead to a gradual decrease in the import of petroleum products. On the one hand, the reduced reliance on imported petroleum products will result in reduced expenditure on imports. On the other hand, the increased usage of domestically produced electricity for powering electric vehicles can contribute to the economic development of Nepal.

The export figure is still in a decreasing trend nonetheless, a positive development is the rising electricity exports, which can be viewed as a silver lining in the present difficult circumstances. As per the fifth meeting of the Joint Steering Committee held in Bangladesh, Bangladesh has agreed to purchase 40 MW of electricity from Nepal through India's transmission lines. A meeting of the Economic Affairs Committee of the Council of Ministers held on Dec 6 gave in-principle approval to the proposal to import electricity from Nepal. Additionally, Nepal has signed a long-term power purchase agreement with India for the export of 10,000 MW within 10 years. According to the latest reports, Nepal has exported 12.5 Billion units of electricity to India as of mid-Oct 2023. If Nepal succeeds in harnessing its extensive hydropower potential, it will contribute to an increase in exports, leading to a decrease in the trade deficit.

With the improving economic outlook, there are foreign investment commitments, signaling a promising economic shift. The most recent data from the Department of Industry (DoI) reveals a remarkable 28.93% surge in foreign investment within just one month, from Kartik to Mangsir in 2080. This surge, totaling Rs 2.26 billion, not only highlights renewed foreign investor confidence but also presents a potential opportunity for the government to capitalize on this momentum.

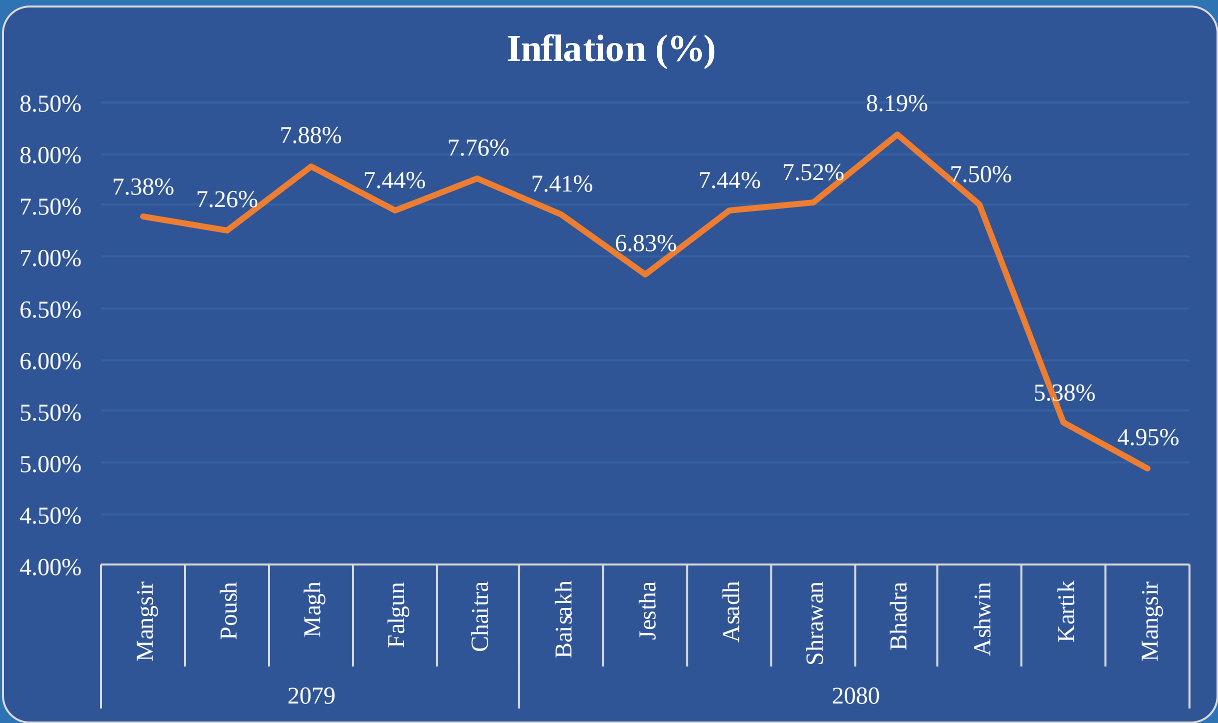
In the previous fiscal year, NRB's attempt to preserve gross foreign reserves through the implementation of import controls led to the loss of government revenue in the form of import and excise duties. This measure led to a budget deficit of 397.87 Billion in the FY 2079/80. To manage the budget deficit, the government has resorted to raising funds from internal borrowing. The government has set a target of acquiring internal loans worth Rs 240 billion in the current fiscal year 2080/81. According to the Public Debt Management Office (PDMO), the government raised as much as Rs97.31 billion in domestic debt during the first quarter of the current fiscal. This accounts for 40.5 percent of the total domestic loans planned to be raised in the current fiscal.

The public debt has reached Rs.2.36 trillion by mid-November out of which 1.18 trillion is domestic debt and 1.17 trillion is external debt.

As for the situation of liquidity in the economy, there is sufficient liquidity in the market owing to the inclusion of 60% of government funds in the deposits of BFIs. Due to subdued loan demand, the CD ratio is in a comfortable position at around 80% The policy rate, bank rate, and deposit collection rate have also been reduced to 5.5%, 7%, and 3% respectively as per the 1st quarterly review of monetary policy 2080, and the banks have also gradually started reducing interest rates.

2. MACROECONOMIC INDICATORS

2.1 Inflation

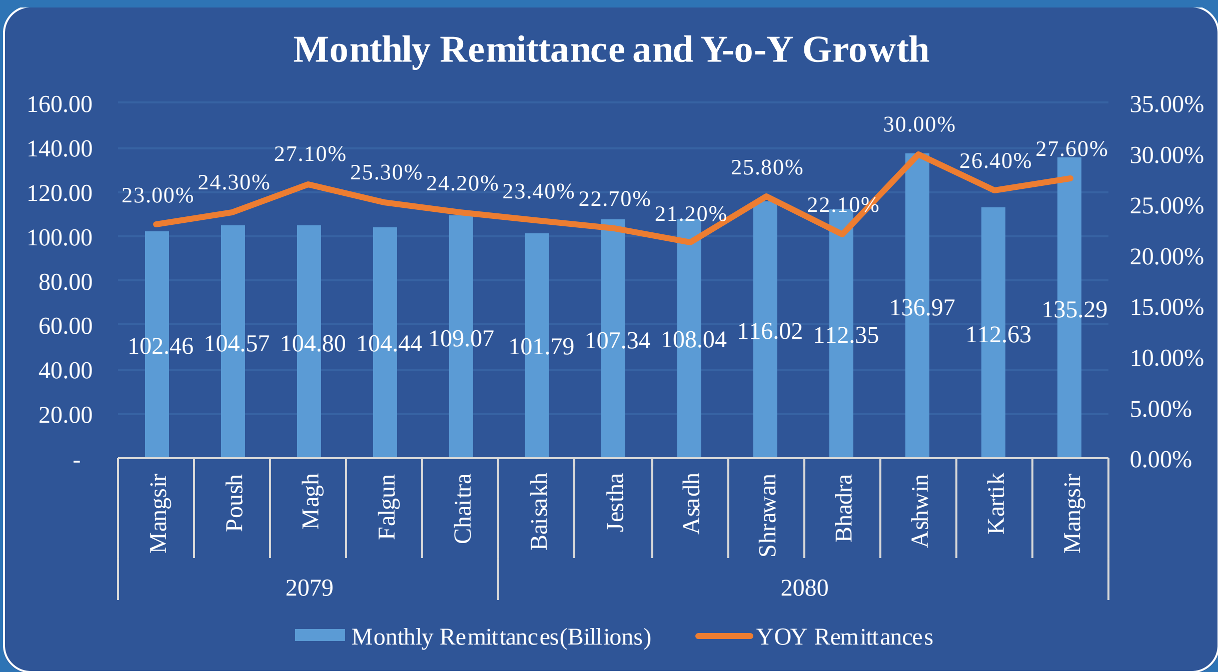


The inflation as of Mangsir 2080 has decreased as compared to the previous month and also compared to the inflation level in the same period of the previous year. The inflation rate as of Mangsir 2080 is at the lowest level in 24 months. The rate is below the targeted rate of 6.5%

set by NRB in Monetary Policy 2080/81. The decrease in inflation from the previous month can be associated with the decrease in oil prices from the previous month by 6.70%. Food and Beverage inflation stood at 5.85% whereas non-food and service inflation stood at 8.59%.

India's retail inflation hit a 4-month high of 5.69% in December 2023. Changes in India's CPI inflation hold direct implications for Nepal's economy, given the close economic ties between the two nations. Recently, India which is a major market for onion import for Nepal has banned the export of onions. Hence, to counter that, Nepal has started importing onions from China instead. This measure could lessen the impact of onion shortage on CPI (Consumer Price Inflation) and help maintain the existing inflation rate.

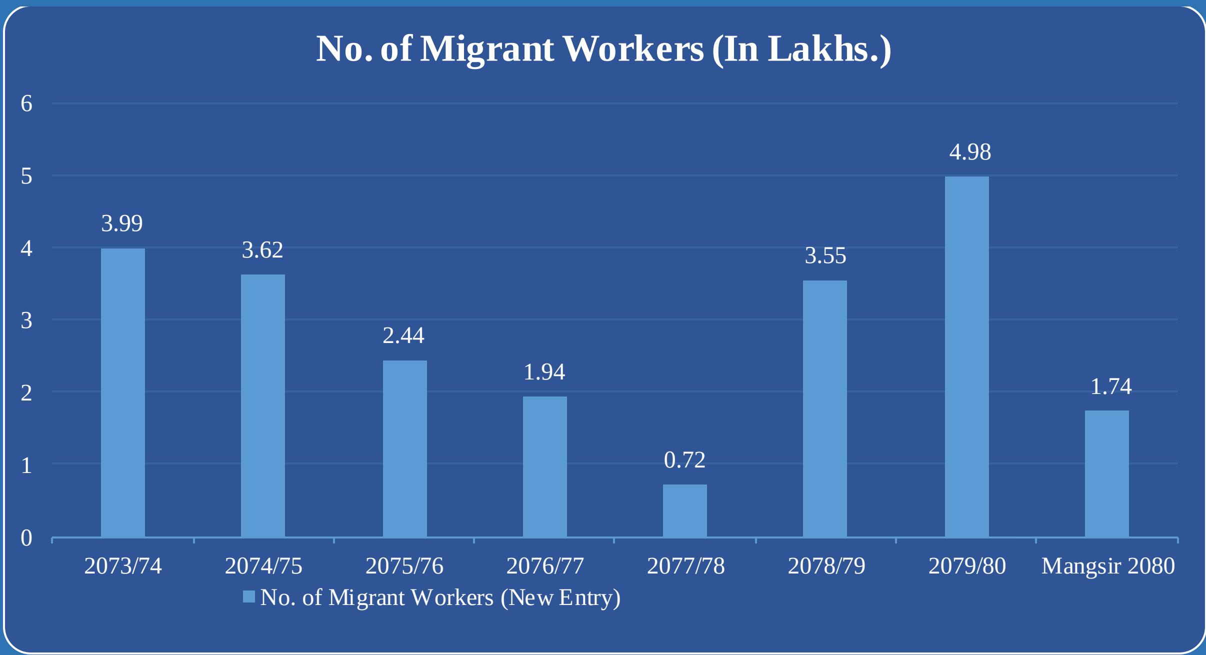
2.2 Remittance



Nepal's economy is highly dependent on remittance so the growth of remittance can be considered positive for the economy. The remittance increased by 27.60% on a Y-o-Y basis and reached 613.25 Billion as of Mangsir 2080. The remittance figure in the corresponding period of the previous year stood at 664.75 Billion.

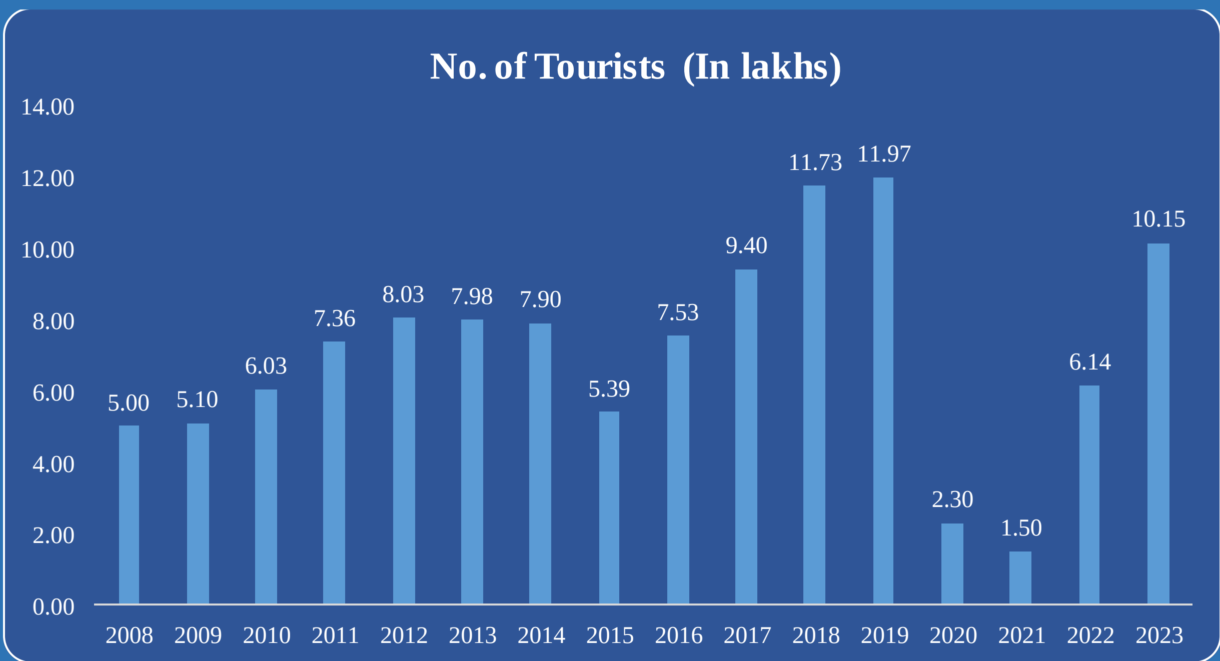
The remittance has been more than Rs 100 billion for a year now. As of Mangsir 2080, the monthly remittance to GDP ratio has increased to 2.51% from 2.11% during the corresponding period last year. Nepal has the largest remittance inflow as a share of GDP in the South Asian region. According to the World Bank's 2021 data, the Remittance to GDP ratio of Nepal is 22.7% whereas other South Asian Nations' figures are below 10%.

2.3 No. of Migrant Workers



The above chart presents the yearly data of no. of migrant workers from the FY 2073/74 to the recent FY 2079/80. As of Mangsir 2080, the number of migrant workers (new entry) has reached 1.74 Lakhs in the five months of FY 2080/81 which is a 26.7% decrease from the same period of the previous year. The number of migrant workers (renewed entry) decreased by 10.3% as of Mangsir 2080 on a Y-o-Y basis. Currently, UAE is the number one destination nation for Nepali migrant workers with a share of 25.7% followed by Malaysia, Saudi Arabia, and Qatar.

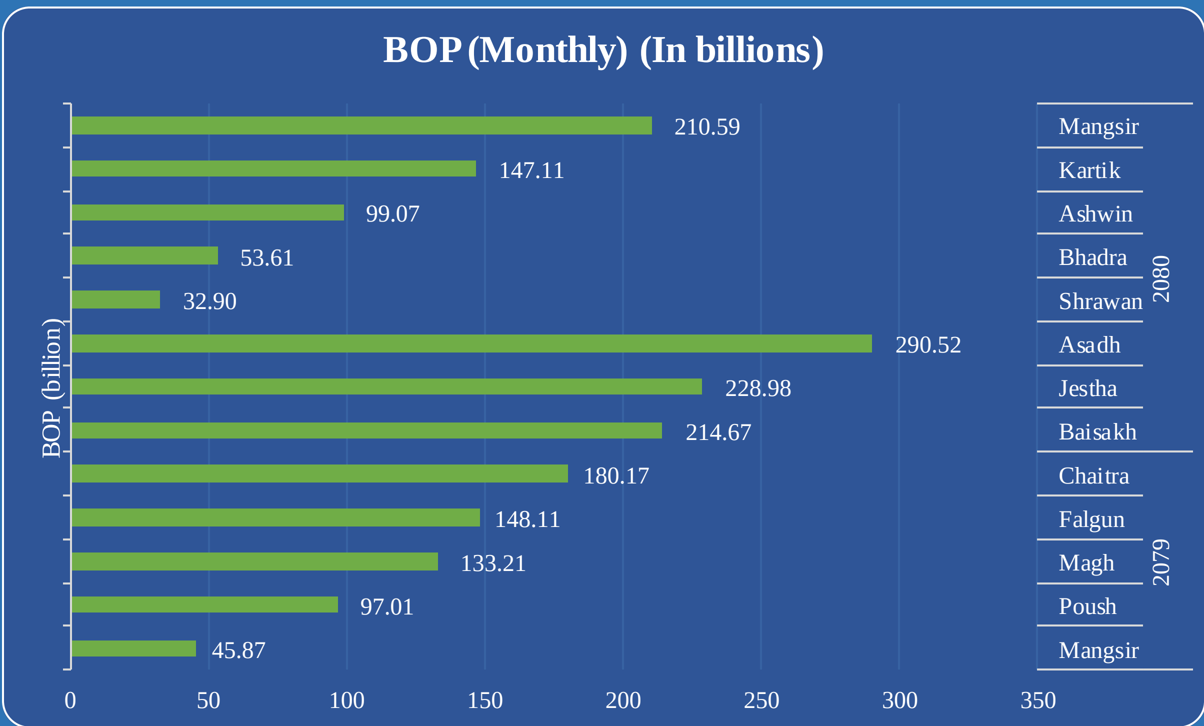
2.4 No. of Tourist Arrival



The number of tourist arrivals, which had significantly decreased in the year 2020 due to the pandemic, is slowly increasing. The number of tourist arrivals increased from 1.5 lakh to 6.14 lakhs in the year 2022. At the end of 2023, the number of tourist arrivals stood at 10.15 lakhs which was around 6.14 lakhs only in the same period of the previous year. In 2023, the no of tourist arrivals increased significantly as compared to the total no of tourist arrivals in recent years. The gradual increased number of tourists coming to the nation is expected to have a positive impact on the hospitality sector of the nation.

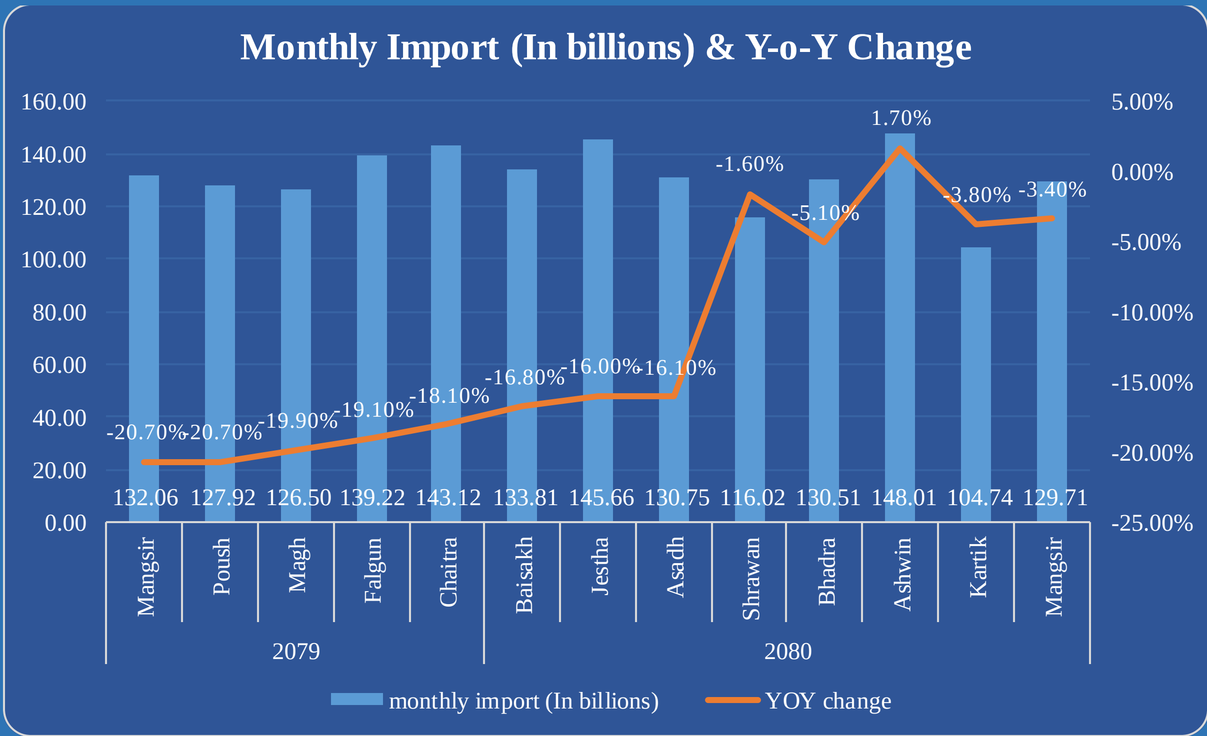
The government of Nepal has decided to mark the period from 2023 to 2033 as the Visit Nepal Decade (VND) to revitalize the nation's tourism sector, which suffered significant setbacks due to the Covid-19 pandemic over the past two years and with the longer-term goal of establishing Nepal as a leading destination in the global tourism market. The Ministry of Culture, Tourism, and Civil Aviation has already prepared a Strategic Action Plan to make the VND 2023-32 successful. It plans to increase the number of tourist arrivals to 3.5 million (excluding Indian nationals) and to generate 1 million additional jobs in the tourism industry. Likewise, the government aims to increase per tourist per day spending from the present 48 US dollars to 125 US dollars. This is expected to boost tourism's contribution to the country's gross domestic product.

2.5 Balance of Payment (BOP)



As of Mangsir 2080, the BOP remained at a surplus of Rs.210.59 billion. In the same period last year, it was at a surplus of 45.87 billion. It has been over a year since the BOP had continued to be the surplus figure. The reduced imports caused by the economic slowdown and increase in remittance have reduced the pressure on BOP and the trade deficit which has significantly contributed to BOP Surplus. It is crucial to closely monitor import figures to keep a close eye on the liquidity position of the economy as the import restrictions have been completely lifted.

2.6 Imports



The import has decreased by 3.40% as of Mangsir 2080 to 642.21 billion on a Y-o-Y basis. In the same period of the previous year, the import figure stood at 664.75 billion.

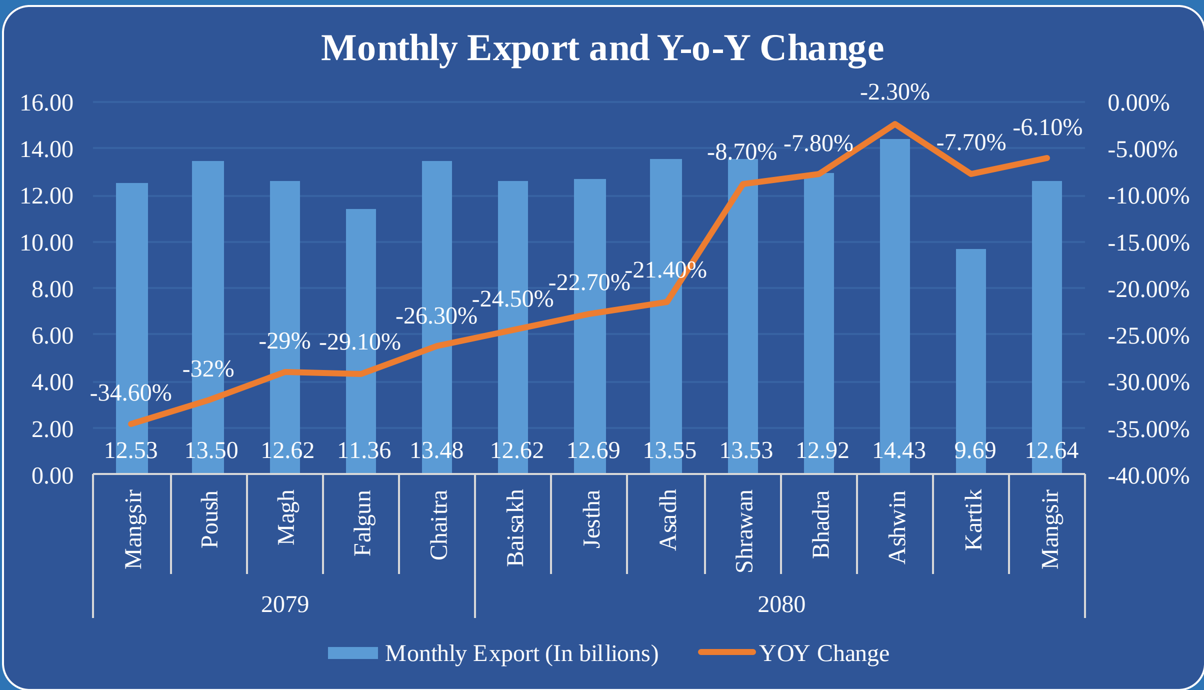
The monthly imports have increased to 129.71 billion in Mangsir 2080 from 104.74 billion in the previous month. Destination-wise, imports from India have decreased by 1.3% percent, and imports from China have increased by 32.8 % percent respectively, and it has decreased by 28.4% for other countries. The reduction in imports in the current month can be attributed to the decline in the import of Petroleum products with a share of 18.12% in total imports by 4%.

2.6.1 Top Five Imports

S.N	Top 5 Imports	Five Months (Mid-Dec 2023) (In Mn.)	Share in Total imports (%)	Percentage Change
1	Petroleum Products	116,339.87	18.12%	-4.0
2	Other Machinery and Parts	28,744.43	4.48%	-1.7
3	Transport Equip, Vehicle and other Vehicle Spare Parts	28,445.70	4.43%	0.8
4	Medicine	18,142.07	2.82%	-10.7
5	Telecommunication Equipment and Parts	17,365.53	2.70%	4.8

The Top 5 Imports in the month of Mangsir 2080 have been presented in the above table. The data shows that the import of petroleum products has decreased by 4% as compared to the same period of the previous year while the import of transport equipment, vehicles, and other vehicle spare parts increased by around 0.8%. The import of other machinery and parts has slightly decreased by 1.7% as compared to the same period of the previous year. Telecommunication equipment and parts have also occupied a share in the top 5 imports this month with an increase of 4.8%.

2.7 Exports



The exports have decreased by 6.10% to 63.21 billion as of Mangsir 2080 on a Y-o-Y basis. In the same period of the previous year, the exports stood at 67.3 billion.
Destination-wise, exports to India decreased by 11.3 percent while exports to China increased massively by 322.3 percent and 2.3 percent to other countries (Y-o-Y Change). A reduction in the exports could be due to a substantial decline in palm oil exports by 77.2%. Whereas the export of Zinc sheets, Particle Board, and Ginger has significantly increased. Similarly, Nepal has exported electricity worth 12.38 billion in the five months of the current fiscal year 2080/81 which has increased from 8.23 billion in the same period of the previous year.

According to statistics from the Trade and Export Promotion Centre, Nepal's export of high-value products increased by 18 percent in the first quarter of the current fiscal year, largely due to a rise in the shipment of iron and steel products, cardamom, dog chew, ginger, cement, and lentils.

The total trade deficit has decreased by 3.10 percent to Rs.579 billion during the five months of the current fiscal year. Such a deficit had decreased by 18.80 percent in the corresponding period of the previous year. The export-import ratio decreased to 9.8 percent in the review period from 10.1 percent in the corresponding period of the previous year.

2.7.1 Top Five Exports

S.N	Top 5 Exports	Five Months (Mid-Dec 2023) (In Mn.)	Share in Total Exports (%)	Percentage Change
1	Zinc sheet	4,974.12	7.87%	96.9
2	Polyester Yarn & Thread	4,670.92	7.39%	13.6
3	Woolen Carpet	4,530.03	7.17%	-5.3
4	Juice	3,398.40	5.38%	50.0
5	Cardamom	3,098.61	4.90%	13.8

The top five exports from our country have been presented in the above table. While the overall export figure has decreased as a result of a decrease in the export of palm oil following the increase in import duty of oils imported from Nepal by India, it has also encouraged the export of domestically produced/available goods. The exports of Zinc sheets, Polyester Yarn, thread, juice, ginger, and cardamom have impressively increased in FY 2080/81 compared to the previous year. According to recent reports, Cardamom is now being sold at the highest price in the past four years. The price was Rs 28,000 last year but good quality of cardamom is now being sold at Rs 85,000 per quintal. This may be the reason behind the increase in cardamom exports in recent months.

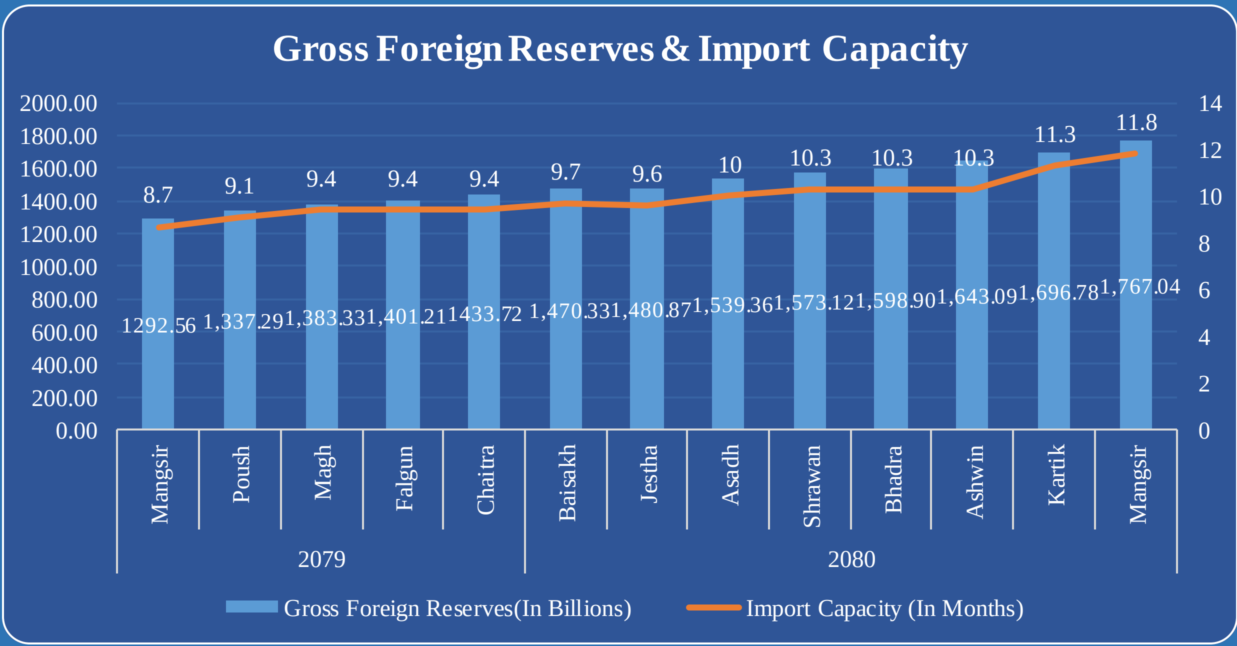
Electricity Exports (In Mn.)				
S.N.	Export	2022/23	2023/24	Percentage Change
		Five months	Five months	
1	Electricity	8,217.19	12,375.56	50.61%

Looking into the exports of electricity from Nepal, the data shows that the exports of electricity have increased on a Y-o-Y basis in the current fiscal year 2080/81. Thus, there is the prospect of electricity exports due to various reasons. A recent study has identified that Nepal has the potential to harness over 72,000 MW of hydropower, but as of date, Nepal's installed capacity is around 2800 MW till date. The Ministry of Energy, Water Resources and Irrigation is preparing a 12-year plan to boost energy production and expand the market, with the target of producing over 28,000MW of electricity by 2035.

The "Upper Tamakoshi Hydropower Project" has increased the production capacity to 2,190 MW. Further, with the announcement of a restructuring of NEA and HIDCL in the financial budget of 2080/81, electricity production shall increase creating further prospects for electricity exports. Additionally, Nepal and Bangladesh have agreed to the power trading of around 40-50MW of electricity from Nepal. If Nepal succeeds in selling electricity to Bangladesh, it will become the country's first power export outside India. It can become a catalyst for increasing exports in the upcoming months.

However, with the onset of the dry season, there has been increased demand for electricity in Nepal, to meet the domestic demand, NEA is currently importing electricity from India to meet the increased electricity demand. Previously Nepal was exporting electricity to India in the wet season but has again resorted to importing electricity instead. Hence, the electricity export figure is expected to be affected for the entirety of the dry season.

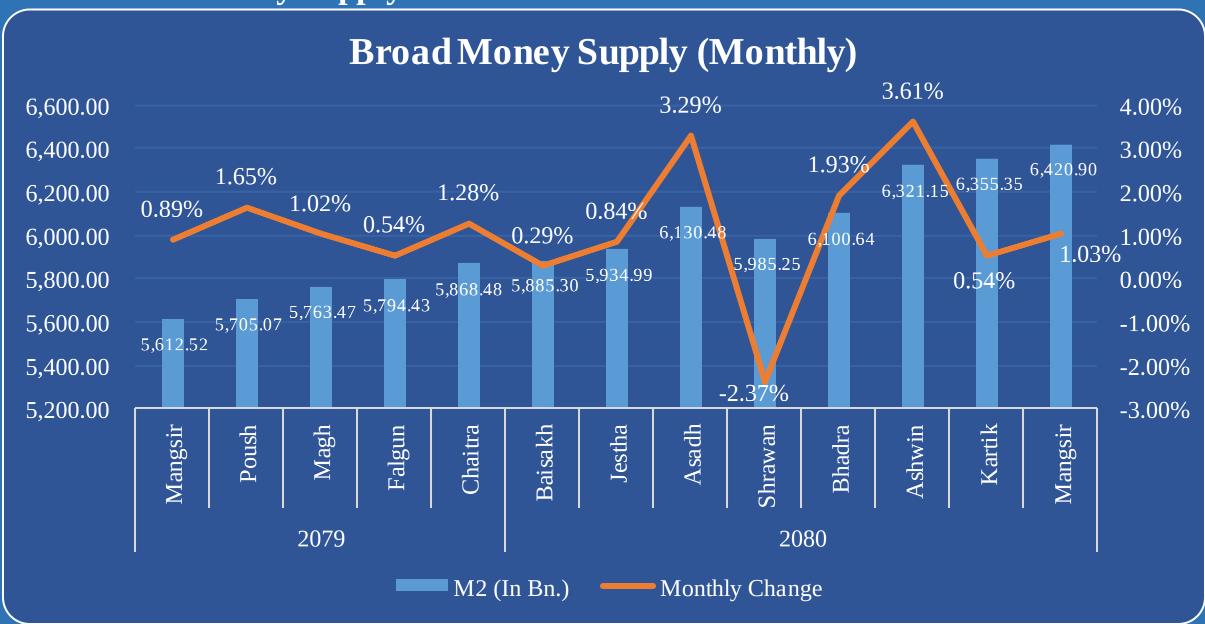
2.8 Gross Foreign Reserves & Import Capacity



The Gross Foreign Reserves and import capacity is on an increasing trend in FY 2080/81 as well. As of Mangsir 2080, gross foreign reserves stood at 1767.04 billion which was 1292.56 billion in the same period of the previous year. The gross foreign reserves increased to 1767.04 billion from 1573.12 billion in Shrawan 2080 which is an increase of 12.33%. Likewise, the import capacity for merchandise and service imports increased to 11.8 months as of Mangsir 2080.

Currently, Nepal's import capacity and gross foreign exchange reserves are in a favorable position, alleviating concerns of the nation experiencing a situation similar to Sri Lanka, which underwent an economic crisis due to a shortage of gross foreign exchange.

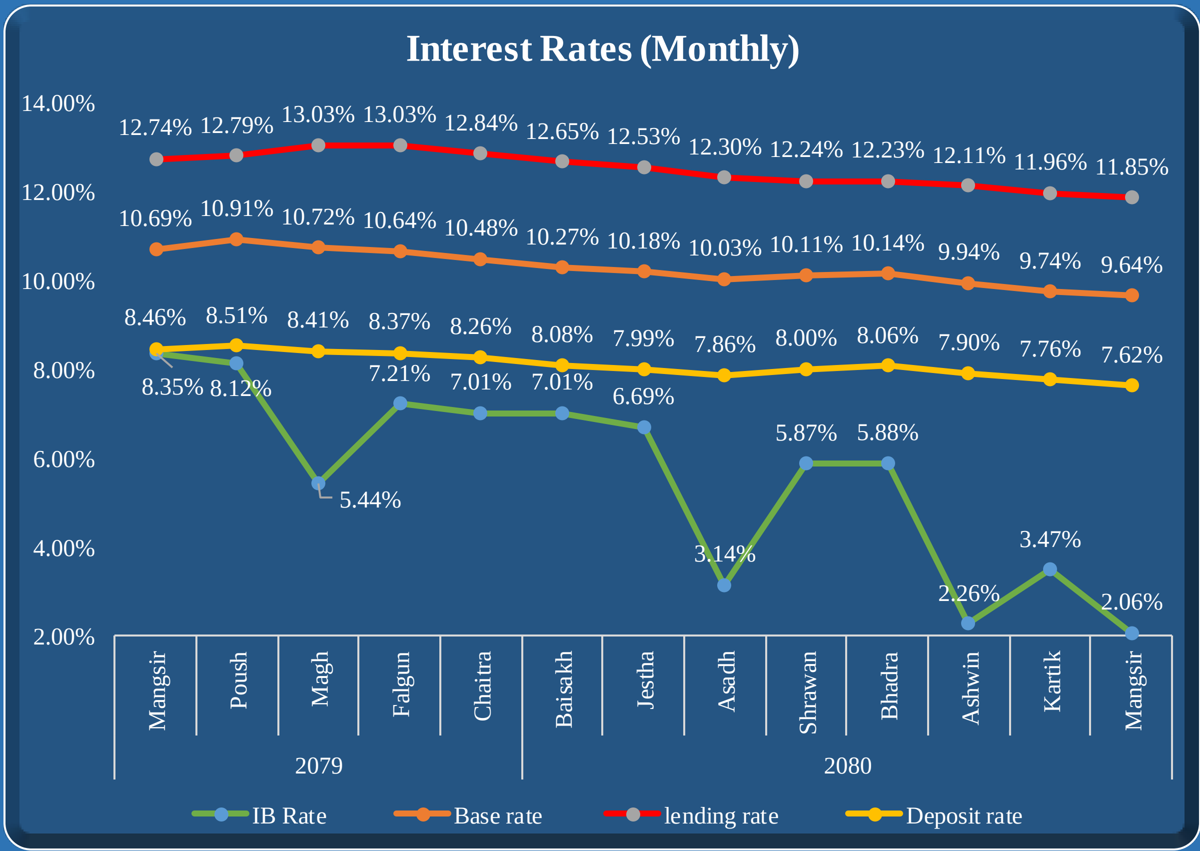
2.9 Broad Money Supply



Broad money supply is a measure of the total amount of money in an economy that is readily available for spending. It includes all physical currency, such as banknotes and coins, as well as money held in various types of accounts, such as demand deposits, time deposits, and savings deposits. The broad money supply figure had been in an increasing trend in the previous fiscal year and has slightly increased by 1.03% in the fifth month of the new fiscal year.

2.10 Interest Rates

Weighted Average Monthly Interest Rates (Line Chart)



In FY 2079/80, to control rising inflation and excessive lending in unproductive sectors, NRB implemented several measures to reduce market liquidity, resulting in a rise in the market interest rate. Hence, for most months of FY 2079/80, the interbank rate was at a high level signifying tightness of liquidity. However, the liquidity persevered towards the end of the FY with the interbank rate coming down to as low as 3.14%.

In Bhadra 2080/81, the government permitted the BFIs to count 60% of government funds as deposits to aid liquidity in the hopes of the interest rate decrease. It was a major factor in increasing liquidity in the current fiscal year. The interbank rate as of Mangsir 2080/81 is 2.06%. According to the first quarterly review of monetary policy, the interbank interest limit has been set to 3% for this fiscal year.

As per the latest interest rates published by commercial banks for the month of Magh 2080, 18 commercial banks have decreased their deposit interest rates, no bank has increased their interest rates and 2 have kept them constant following the previous month’s interest rate. The average FD rate for individuals in Magh is 8.167%, down from the previous month's 8.991% in the commercial bank industry.

2.11 Government Revenue and Expenditure

Date	Government Revenue		Government Expenditure	
	Amt. in billions	% of Target Budget	Amt. in billions	% of Target Budget
Mangsir 2079	357.83	24.53%	435.21	24.26%
Mangsir 2080	383.92	26.07%	453.00	25.87%

The government revenue and expenditure as of Mangsir 2080 are 383.92 billion and 453 billion respectively. The government revenue and expenditure have reached 26.07% and 25.87% of the target budget respectively as of Mangsir 2080/81.

However, the government expenditure disbursed is slightly higher than the previous year's. The money in circulation also depends on the disbursement of government expenditure. Higher government expenditure aids in easing the liquidity situation in the economy.

Date	Capital Expenditure	Budget Deficit/Surplus (Billions)
Mangsir 2079	8.94%	-77.38
Mangsir 2080	11.94%	-69.07

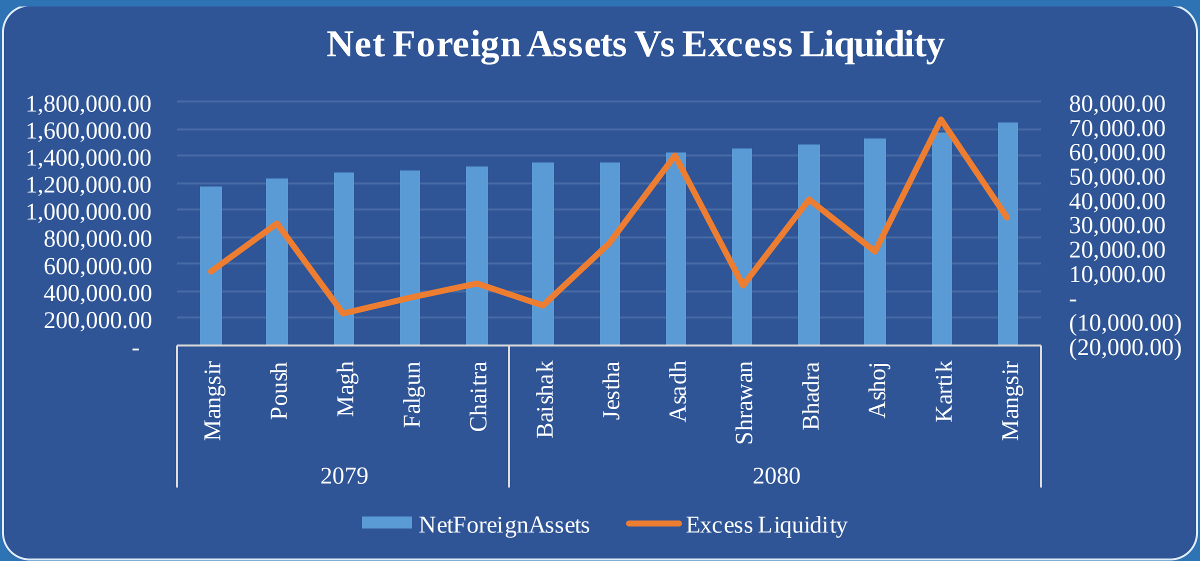
Source: FCGO

Capital expenditure is the most important component of government expenditure as it helps to accelerate the economy through development projects. The capital expenditure utilized by the government as of Mangsir's end stood at 11.94%. While it is at a higher rate than the capital expenditure utilized the year before.

As of Mangsir 2080, there is a budget deficit of 69.07 billion which is only slightly lower than the budget deficit in the same period of the previous year. The persisting budget deficit is a matter of concern for the currently thriving economy.

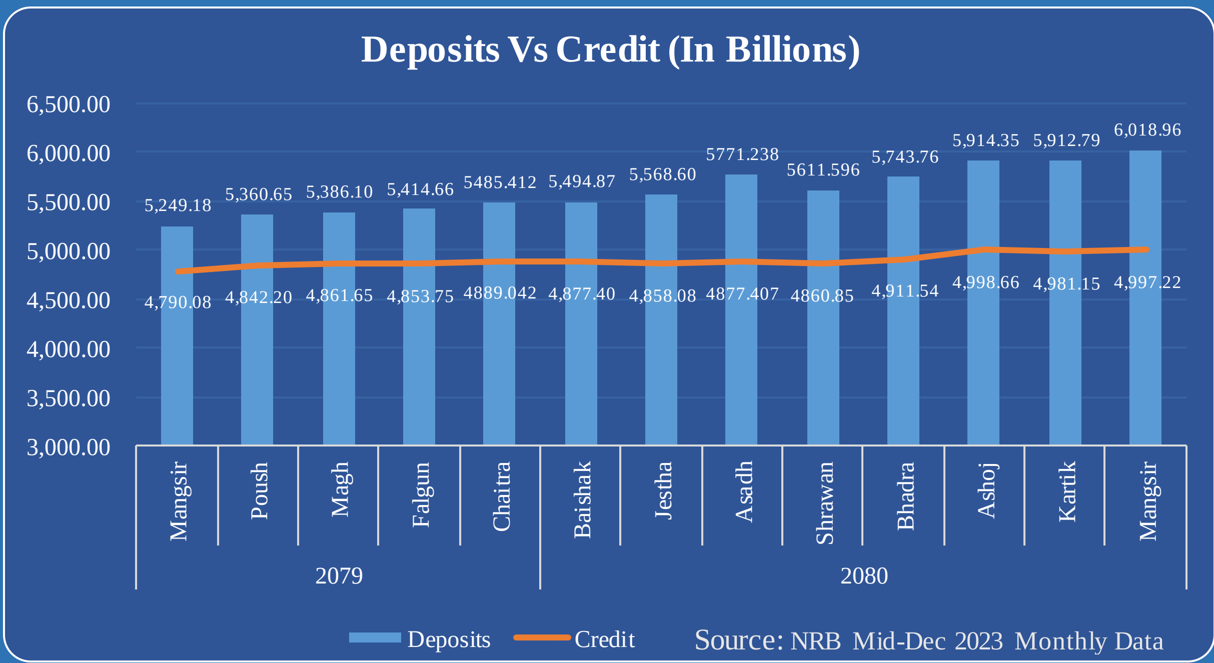
2.6 Market Liquidity

In Millions.



The position of excess liquidity stood at around 32.25 Billion (As of Mangsir 2080). The excess liquidity has decreased compared to the previous month which stood at around 72.49 Billion. This may have been due to the constant efforts of NRB to withdraw liquidity from the market in recent months. The position of excess liquidity had been in an extremely vulnerable state after the persisting credit crisis in the Nepalese economy which arose as a result of excessive lending during the post-COVID period and the rising import figure. The liquidity has improved greatly which may be attributed to the import restrictions placed, the discouragement of loans flowing into unproductive sectors, and the allowance to count local funds as deposits. At the end of Bhadra 2080, the decision was made on the allowance of counting 60% of local funds as deposits, which has contributed to increased liquidity in recent months. The decreased import figure and increased remittance have positively affected the net foreign assets of the country with a growth of 3.37% and has reached 1.58 Trillion in the current month.

2.7 Total Deposits and Credit



The total deposits have slightly increased by 1.80% and the lending has increased by 0.32% as of Mangsir 2080 compared to the previous month. The total deposits are 6018.96 billion, and the total credit is 49971.22 billion as of Mangsir 2080.

3. Conclusion

In conclusion, the current economic outlook in Nepal appears positive and reflects an improving outlook supported by sustained imports, growth in remittances, and a surplus in the balance of payments. However, it's important to note that the reduction in imports, initially due to restrictive policies and more recently because of economic slowdown, may not be a sustainable, long-term solution, especially without corresponding growth in domestic production. While the increase in remittances is a boost to the economy, it also signals a significant outflow of active manpower from the nation, which can pose challenges to the country's long-term economic growth prospects. There is a comfortable liquidity position compared to the previous year and the interest rates have decreased as well, however, there is limited credit expansion and subdued market demand. The government's ineffectiveness in allocating and spending funds for capital expenditure presents challenges in sustaining a favorable liquidity position in the economy throughout the year. The inflation has also come down to a lower level but might potentially be affected by the geopolitical rifts, and tight financial conditions in the global world. However, The World Bank (WB) has predicted that the expansion of the Nepali economy will be satisfactory, compared to the average growth of the world economy. According to the WB, the average economic growth rate of the world in 2024 will be 2.4 percent and Nepal's economic growth rate will be 3.9 percent in the current fiscal year (FY) 2023/24. In the last fiscal year 2022/23, Nepal's economic expansion was only 1.9 percent.

The possibility of positively contributing to the economy through the opportunity to export electricity exists. With the Credit to Deposit Ratio staying within the 81% range, there is an excess of loanable funds exceeding 400 billion within the banking industry. Through the first quarterly revision of monetary policy, restrictions on real estate and share loans have been slightly loosened which might increase the loan demand gradually. If the government and central bank implement appropriate policies and strategies, improving liquidity could be utilized for credit expansion at a lower interest rate. This, in turn, would stimulate demand in the market, boosting economic activity in the country. The reduction in market interest rates, coupled with increased liquidity, could catalyze enhancing economic activities and mitigating the impact of the economic slowdown.

References

https://kathmandupost.com/national/2023/11/26/can-nepal-harness-its-huge-hydropower-potential

https://myrepublica.nagariknetwork.com/news/price-of-cardamom-increases-threefold/

https://myrepublica.nagariknetwork.com/news/rising-domestic-demand-spurs-nepal-to-halt-electricity-exports-amid-dropping-temperatures/

You Can Find Us at:

Scan to Join our MCL Viber Community

https://www.facebook.com/machhapuchchhrecapital/

https://instagram.com/machhapuchchhrecapital?igshid=OGQ5ZDc2ODk2ZA==