

NEPAL

Economy Update

June 1, 2021 | Economics

An update on the economy of Nepal for nine months of the financial year 2020/21 (July 15th – June 14th) has been presented here where the domestic economic situation, external sector scenario, fiscal position, banking and monetary policy stance have been analysed.

Snapshot of the economy

Table 1: Annual data

| Indicators | 2017/18 | 2018/19 | 2019/20 | 2020/21 (E) |
|--|---------|---------|---------|-------------|
| Real GDP growth at basic price (%) | 7.6 | 6.7 | -2.1 | 4.0 |
| Nominal GDP growth at producers' price | 12.3 | 11.7 | 1.4 | 9.0 |
| GDP (current prices : Rs bn) | 3,455 | 3,858 | 3,914 | 4,266 |
| GFCF/ GDP (%) | 32.4 | 33.8 | 28.4 | 27.3 |

Source: Nepal Rastra Bank

Table 2: Monthly data

| Indicators | April 2020 | Feb 2021 | March 2021 | April 2021 |
|------------------------------------|------------|----------|------------|------------|
| Consumer price inflation (y-o-y%) | 6.7 | 2.7 | 3.0 | 3.1 |
| Wholesale price inflation (y-o-y%) | 7.8 | 6.1 | 6.3 | 6.1 |
| Export growth (y-o-y%) | -54 | 18.5 | 9.3 | 257 |
| Import growth (y-o-y%) | -48 | 30.7 | 16.3 | 187 |
| Trade deficit growth (y-o-y%) | -48 | 31.7 | 17.0 | 182 |
| Trade deficit(Rs bn) | 54.3 | 133.3 | 129.5 | 153.4 |
| Worker's remittances (\$ mn) | 286 | 620 | 638 | 742 |
| Foreign exchange reserves (\$ bn) | 9.8 | 12.6 | 12.4 | 12.4 |
| Domestic credit (YoY%) | 16.8 | 21.8 | 21.9 | 21.1 |
| Deposits (YoY%) | 9.7 | 22.4 | 21.9 | 13.7 |
| Bank rate (%) | 6.0 | 5.0 | 5.0 | 5.0 |
| Weighted average deposit rate (%) | 6.74 | 4.86 | 4.76 | 4.79 |
| Weighted average lending rates (%) | 11.77 | 8.89 | 8.73 | 8.61 |

Source: Nepal Rastra Bank

Positive Economic Outlook for 2020/21 by the Central Bureau of Statistics, Nepal

- The Central Bureau of Statistics has estimated Nepal's economy to grow by around 4% in 2020/21 after a decline of 2.1% in 2019/20.
 - This is likely to be driven by notable growth in accommodative and food services (11.2% v/s -37% last year), power (7.7% over 26% last year), financial and insurance activities (5.8% v/s 4.8% last year) and healthcare (6.5% over 5.2% last year).
 - Agriculture, which has share of 1/5th in total output, is estimated to grow by 2.6% in 2020/21 compared with 2.2% in 2019/20.
 - Manufacturing sector, which accounts for 12.5% in total output is estimated to grow by 3.9% in 2020/21 as against 8.6% de-growth last year.
 - Wholesale and retail trade, transportation and storage and accommodation and food services, which are estimated to have witnessed double digit contraction in 2019/20, are expected to grow in 2020/21.
 - The savings rate in the economy (GNP to GDP) is estimated to marginally decline to 31.4% in 2020/21 compared with 32.6% in 2019/20.
 - The investment rate in the economy (GFCF to GDP) is estimated to fall further to a 3-year low of 27.3% in 2020/21 compared with 28.4% in 2019/20.
- **Positive Economic Outlook:** The World Bank has projected the economy to grow by 2.7% in 2020/21, 3.9% in 2021/22 and 5.1% in 2022/23 and these projections are based on assumptions of successful domestic and global vaccine rollout and gradual resumption of international tourism. The IMF has projected the Nepal economy to grow by 2.9% in 2020/21.

- **The downside risks to the economic outlook include:**
 - Delays in vaccinations and new outbreak of COVID-19 both domestically and globally which could dampen prospects of economic recovery
 - International travel restrictions could weigh on the tourism sector
 - Political uncertainty
- **COVID-19 status:** There has been a second spike in COVID-19 cases from mid-April 2021 and had touched almost 9,000 daily cases in mid-May 2021 and has marginally moderated to around 8,000 cases by May 26, 2021. The active cases as of May 27, 2021 is around 116 ('000) people. Nepal had announced a stringent lockdown from the end of April 2021 to contain the spread of the virus and this has been extended till June 3. The Oxford's stringency index, which measures the degree of lockdown stringency on a scale of 100, rose from 30 by the end of April to 94 since the first week of May.
- **Vaccination status:** As of 26, May, 2021, 628 ('000) people have been completely vaccinated in Nepal, which means only 2.1% of the total population (29.1 million) have been completed vaccinated. 2.1 mn people have been vaccinated at least once which is 7.2% of the total population.

Steady inflation levels like previous month at retail and wholesale level

- Retail inflation remained broadly stable at 3.1% in April 2021 compared with 3% in March 2021 but is significantly lower than 6.7% in April 2020. Both food and non-food inflation has fallen sharply compared with April 2020.
 - Food inflation has declined from 9.7% in April 2020 to 3.5% in April 2021 primarily on account of deflation in vegetables segment of 11.7% as against double-digit growth of 32.3%. There has been a deflation of 2% in case of Fruits compared with double-digit.
 - Pulses and legumes have registered an inflation of 8.8% in April 2021 compared with 14.4% in April 2020.
 - Non-food and services inflation was at 2.8% in April 2021 compared with 4.5% in April 2020 with the moderation chiefly owing to housing and utilities. There has been deflation of 0.5% in case of Education during April 2021 as against 5.8% in April 2020.
- Wholesale inflation remained elevated at 6.1% in April 2021, 0.2% lower than the previous month and 1.6% lower than April 2020. The easing of wholesale inflation from last year has been on account of fall in food inflation, which accounts for almost 1/3rd of the WPI basket. However, there has been a notable jump in the inflation of the manufacturing segment driven by chemicals and basic metals.
 - The highest spike was observed in case of chemicals (16.9%), basic metals (12.7%) and paper products (12.4%) in April 2021 compared with benign wholesale inflation in April 2020. This can be chiefly attributed to the notable pick-up in commodity prices.
 - Wholesale food inflation has fallen to 2.3% in April 2021 compared with 17% in April 2020.
 - Wholesale fuel inflation was at 3.6% in April 2021 as against a deflation of 0.5% in April 2020 and this reflects the pick-up in global crude oil prices.

External Sector – Trade deficit widens while workers' remittances and forex reserves increase

Sharp rise in imports have led to widening of deficits in April 2021

- Trade deficit rose to Rs 153 bn in April 2021, three times more than the corresponding month previous year (Rs 54 bn) on account of spike in imports. Trade deficit during these 9-months stood at Rs 1016 bn, 12.5% more than the corresponding period last year.
 - Imports at Rs 167 bn in April 2021 are almost triple than that of April 2020. Exports at Rs 13.9 bn during the month are 3.5 times more than the corresponding month last year.
 - Total imports at Rs 1,111 bn during the period August-April 2021 grew by 13.1% more than the corresponding period last year. Total exports at Rs 94.7 bn during the same period grew at a much faster pace of 20%.

Improvement in worker's remittances for 9-month period

- Worker's remittances rose sharply in April 2021 to \$742 mn, 2.5 times more than April 2020. Total worker's remittances during August to April 2021 have been \$6.2 bn, 13% more than the corresponding period last year.
- The flow of remittances has increased with individuals sending more money owing to the concerns surrounding the pandemic. However, a number of workers are still not able to go back to their destinations and that has had a bearing on overall remittances.

Current account deficit widens by 61% during August-April 2021 (YoY)

- During August-April 2021, Nepal has recorded a current account deficit of \$1.77 bn compared with a current account deficit of \$1.1 bn in the corresponding period last year. The deficit during this period has been primarily on account of higher trade deficit in merchandise goods.
- As per World Bank's outlook, current account deficit is expected to widen over the medium term as import growth accelerates with increased consumption while service exports remain subdued (tourism is expected to recover fully in 2022/23). The current account deficit is expected to widen to 3.2% of GDP by 2021/22, financed primarily by long term concessional loans.

Increase in foreign exchange reserves

- The foreign exchange reserves were US \$12.4 bn as on mid-April 2021, 3.2% higher than mid-Jul 2020.
- Based on the imports of nine months of 2020/21, the foreign exchange reserves of the banking sector is sufficient to cover the prospective merchandise imports of 11.9 months, and merchandise and services imports of 10.8 months.

Appreciation of domestic currency

- The domestic currency (month average) has strengthened by 3.1% from Rs 120.8/\$ in July 2020 to 117.03/\$ in April 2021 and has marginally depreciated by 0.36% compared with the previous month. There has been a broad weakness in the US dollar amidst US fiscal stimulus and sustained accommodative monetary policy.

Low base drives crude oil prices higher in April 2021 (YoY) while gold prices register a modest increase

- The price of Brent crude oil (\$/ barrel) was \$62.8/barrel in mid-April 2021, more than triple of the corresponding period of the previous year (\$20.2 in April 2020). The sharp rise in crude oil prices is primarily because of a low base effect coupled with prospects of improved demand outlook amidst better economic recovery and better than expected vaccination drives. However, increase in supply following negotiations between US and Iran has dampened prices to some extent.
- The price of Gold (\$/ounce) has increased to \$1,748/ounce as at mid-April 2021, 4% higher than corresponding period last year. However, the prices have reduced compared with the prices observed during the start of the financial year (mid-July 2020 - \$1,804/ounce). The y-o-y pickup has largely been on account of safe-haven demand amidst the coronavirus pandemic, which has led to investors shifting away from riskier assets. The recent rally in gold prices can be ascribed to inflationary concerns at the global level emanating from the boom in the commodity cycle.

Government finances falls into deficit

- The government balance (difference between total revenue and expenditure) has recorded a small deficit of Rs 12.6 bn during August-April 2021 compared with a surplus of 62 bn in the corresponding period last year. Total revenue resources have fallen by 5.5% during the period while total expenditure has grown by 5.6%.
 - Key revenue heads which have registered a robust growth during the 9 months include VAT(17.5%), Customs (37.3%), Excise (18.9%) with these 3 heads accounting for 3/5th of the total revenue.
- The fiscal deficit is projected to remain elevated over the medium term with revenue performances remaining weak and additional spending on economic relief measures, vaccinations and project implementation weighing on finances. The fiscal deficit as per World Bank is projected to widen to close to 8% of GDP in 2021/22. Thereafter, the World Bank projects, fiscal deficit to narrow to 6.5% of GDP as revenues recover.

Bank Credit and Deposits

- Incremental domestic credit expanded by 16.4% during August-April 2021 compared with growth of 9.1% in the corresponding period last year. On y-o-y basis, domestic credit growth has moderated to 21.1% as on April 2021 compared with 16.8% growth last year.
- Deposits at Banks and Financial Institutions (BFIs) rose sharply by 13.7% during August-April 2021 over 9.7% growth in the corresponding period of the previous year. On y-o-y basis, deposits at BFIs expanded 23% as on April 2021 compared with 16.9% growth last year.

Key interest rates

- The bank rate (key policy rate) was stable at 5% in March 2021.
- The weighted average deposit rate at 4.79% in April 2021 was 2 bps higher than last month and almost 2% lower than corresponding month last year.
- The weighted average lending rate for commercial banks at 8.61% in April 2021 was 11 bps lower than last month and 3.15% lower than corresponding month last year.

Capital Markets

- The NSE index at 2714.8 points as on mid-April 2021 was 116% higher than corresponding period last year.
- The stock market capitalization at 3,759 bn as of mid-April 2021 is 134% higher than last year.

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