

## Nepal economy update: May 2020

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An update on the economy of Nepal for the first nine months of new financial year 2019/20 has been presented here wherein 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	2016/17	2017/18	2018/19	2019/20
Real GDP at producers' price (%)	8.2	6.7	7.0	2.3

Source: Nepal Rastra Bank

Table 2: Monthly data

Indicators	Apr 2019	Feb 2020	Mar 2020	Apr 2020
Consumer price inflation (y-o-y%)	4.5	6.9	6.7	6.7
Wholesale price inflation (y-o-y%)	4.4	7.1	6.6	7.8
Export growth (y-o-y%)	36.1	0.3	22.0	-54.5
Import growth (y-o-y%)	3.3	-0.4	4.2	-48.2
Trade deficit growth (y-o-y%)	1.3	-0.4	2.8	-47.7
Trade deficit (Rs bn)	103.9	101.2	110.7	54.4
Foreign exchange reserves (\$ bn)	9.5	9.6	9.6	9.5
Bank credit growth (y-o-y%)	27.2	13.2	12.6	16.8
Bank deposit growth (y-o-y%)	19.8	15.6	16.1	16.9

Source: Nepal Rastra Bank

**Table 3: Cumulative data (First 9 months of the fiscal)**

Indicators	Apr 2019	Apr 2020
Export growth (y-o-y%)	17.7	12.9
Import growth (y-o-y%)	21.3	-7.5
Trade deficit growth (y-o-y%)	21.5	-8.9
Trade deficit (Rs bn)	992	903
Incremental bank deposit growth (%)	10.6	9.7
Incremental Bank credit growth (%)	13.2	8.9

Source: Nepal Rastra Bank

**Notable decline in GDP growth estimated in 2019/20**

- The economy is estimated to grow by 2.3% in 2019/20 as per the estimates of the Central Bureau of Statistics compared with 7% grow recorded in 2018/19. The notable decline in growth can be attributed to the outbreak of COVID-19 and its impact on various sectors in the economy.
- In order to combat the rising number of cases in Nepal (at around 400 cases on May 19, 2020), the country had announced a nation-wide lockdown since March 24 and the restrictions are likely to be lifted on June 2. The 2-month lockdown has had adverse impact on the economy of Nepal.
- The COVID effect has been translated into negative growth in mining and quarrying, manufacturing, construction, hotel and restaurant and transportation sub-sectors.
- Agriculture, industry and services sectors are estimated to grow by 2.6%, 3.2% and 2% in 2019/20, notably lower than a year ago.

**Build-up in retail prices and wholesale prices**

- Retail inflation was at 6.74% in April 2020 higher than 4.4% witnessed during the corresponding month a year ago. Retail inflation during the month has been largely driven by elevated food price inflation (9.7% in April 19/20 v/s 2.8% in April 18/19). Non-food and services inflation recorded moderation in inflation from 5.8% in April 18/19 to 4.5% in April 19/20.
  - Within food components, double digit inflation was recorded in vegetables (32%), fruits (25%), pulses, spices (14.4%) and alcohol and tobacco products (10%). These 5 commodities account for 12% in the total CPI basket.
  - However, moderation in the inflation of cereals (share of 11% in CPI basket) from 6% in April 18/19 to 4% in April 19/20 limited the rise in CPI inflation.

- Within non-food components, housing (4.6%), clothes (5.2%) and furnishing (4.6%) recorded a moderation in April'20 compared with corresponding period a year ago. These 3 components account for 32% of the total CPI basket.
- Wholesale inflation rose to 3-months high of 7.8% in April'20 compared with 6.6% in March'20 and 4.4% in April'19. The increase in April'20 (y-o-y) can be ascribed to significant increase in the food prices (having a weight of 31%). However, deflation in fuel and power component limited the increase.
  - Wholesale inflation in primary components continues to remain at elevated levels at 16% in April'20 (2.4% in April'19) while inflation in manufacturing components (highest weightage of 57%) remained stable at the same level as last year at 4.5%. Deflation in fuel and power component was -0.5% in April'20 compared with 11.6% growth a year ago.
  - Within manufacturing commodities, contraction in case of basic metals (1.6%), electronic products (1.6%), and non-metallic minerals (1%) has dragged the overall wholesale inflation lower. At the same time, inflation in food, beverages and tobacco under manufacturing component grew at double digit pace of 12.5% in April'20.

### External Sector – mixed

#### Trade deficit contracts

- Trade deficit at Rs 54.8 bn in April'20 was almost half of the trade deficit recorded in March'20. Imports at Rs 58.3 bn were almost half that of the previous month while exports at Rs 3.9 bn were 1/3<sup>rd</sup> of the previous month.
- Trade deficit for the first 9 months of the year stood at Rs 903 bn, 8.9% lower than corresponding period a year ago. This contraction has been on account of export growth of 13% and negative growth in imports of 7.5% during July-April'20.

#### Lower workers' remittances

- The workers' remittances witnessed a y-o-y contraction of 51.5% in April 2020 as against significant positive growth of 3.6% in April 2019.
  - The worker's remittances, which are an important source of receipt which limit the current account deficit, could be lower in 2019/20 on account of coronavirus outbreak.
- The aggregate workers remittances stood at Rs 626.9 bn during July-April'20, 4% lower than corresponding period a year ago.

#### Current account deficit falls

- The current account deficit for the first 9 months of the current fiscal (2019/20) contracted by 34% to \$1.18 bn compared with \$1.8 bn seen in the corresponding period a year ago. The contraction was on account of decline in the trade deficit, lower workers' remittances and higher foreign direct investment in Nepal.

#### Steady foreign exchange reserves

- The foreign exchange reserves were US \$9.5 bn as on mid-April 2020, at almost the same levels witnessed in mid-July'19.

- Based on the imports of the nine months of the current fiscal year 2019/20, the foreign exchange reserves of the banking sector is sufficient to cover the prospective merchandise imports of 10.7 months, and merchandise and services imports of 9.5 months

### Depreciation of domestic currency

- The domestic currency (month average) for April 2020 stood at Rs.120.59/US\$ and has depreciated by 9.2% from the start of the fiscal.
- The depreciation on a month on month basis in April'20 is 4.1%.

### Deterioration in the Government's fiscal position

- The government balance (difference between total revenue and expenditure) recorded a deficit of Rs.56.3 bn during the first 9 months of the fiscal as against a surplus of Rs 17.3 bn during the corresponding period a year ago. Total revenues contracted by 5.2% for the 9 months under review while total expenditure grew by 7% which cumulatively pressured government finances.
  - The negative growth in revenues was seen in case of customs (-5.5%) and excise (-4.5%), both of which account for 30% of total revenues of the government. However, the revenues under income tax grew by 15% during the 9 months compared with corresponding period a year ago.

### Fall in incremental deposit and credit growth

- Incremental credit grew by 8.9% during July-April'20 compared with 13.2% growth recorded in corresponding period a year ago. On y-o-y basis, domestic credit growth moderated from 27.2% in April'19 to 16.8% in April'20.
- Incremental deposits at Banks and Financial Institutions (BFIs) during the first 9 months of the fiscal increased by 9.7%, lower than 10.6% deposit growth recorded in the corresponding period a year ago. On y-o-y basis, deposits grew by 16.9% as of mid-April 2020.

### Key interest rates

- The bank rate (key policy rate) has remained unchanged at 6%.
- The weighted average deposit rate at 6.74% in April 2020 was 3 bps lower than a month ago.
- The weighted average lending rate for commercial banks at 11.77% in April 2020 was 3 bps lower than a month ago.

### Capital Markets

- The NEPSE index grew by almost 5.7% on a y-o-y basis to 1,251 as of mid-April 2020. From the start of the fiscal year, the fall has been marginal at 0.6%.
- The stock market capitalization at 1600 bn as of mid-April 2020 which is 9.4% on a year on year basis and 2.1% higher from the start of the fiscal.