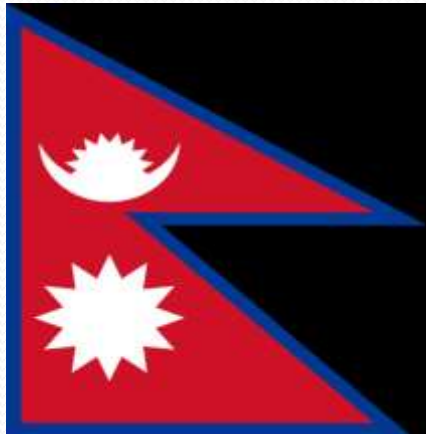


Nepal

Recent Economic Developments and Outlook

International Development Partner Group
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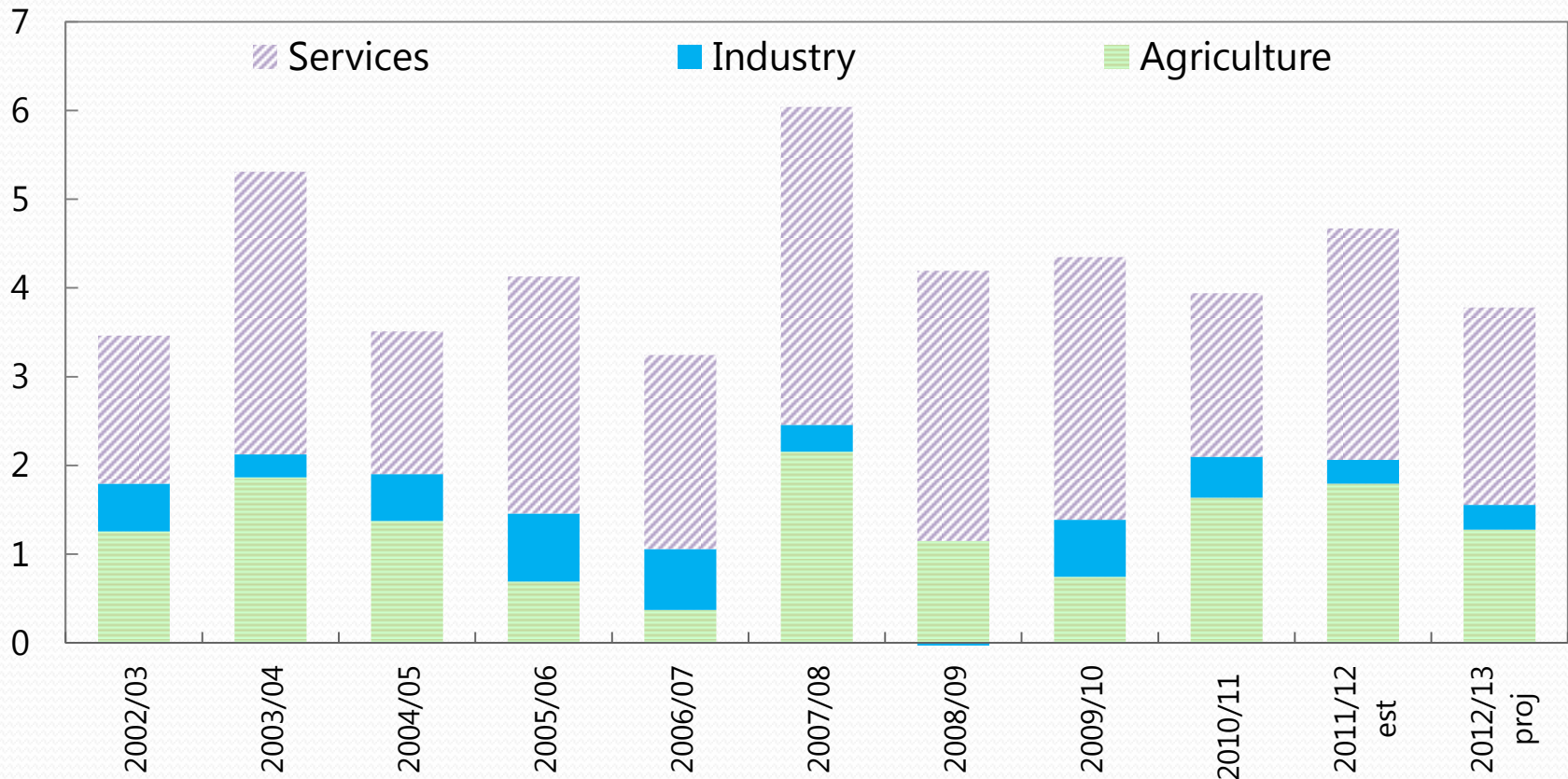
Outline

- IMF 2012 Article IV Consultation just concluded
 - ➔ See www.imf.org/nepal [shortly]
- Snapshot of recent economic developments
- Outlook for 2012/13 and policy messages
- Longer term horizon
- Fund engagement beyond Article IV

Snapshot of recent developments

- Growth in 2011/12 was 4.6%

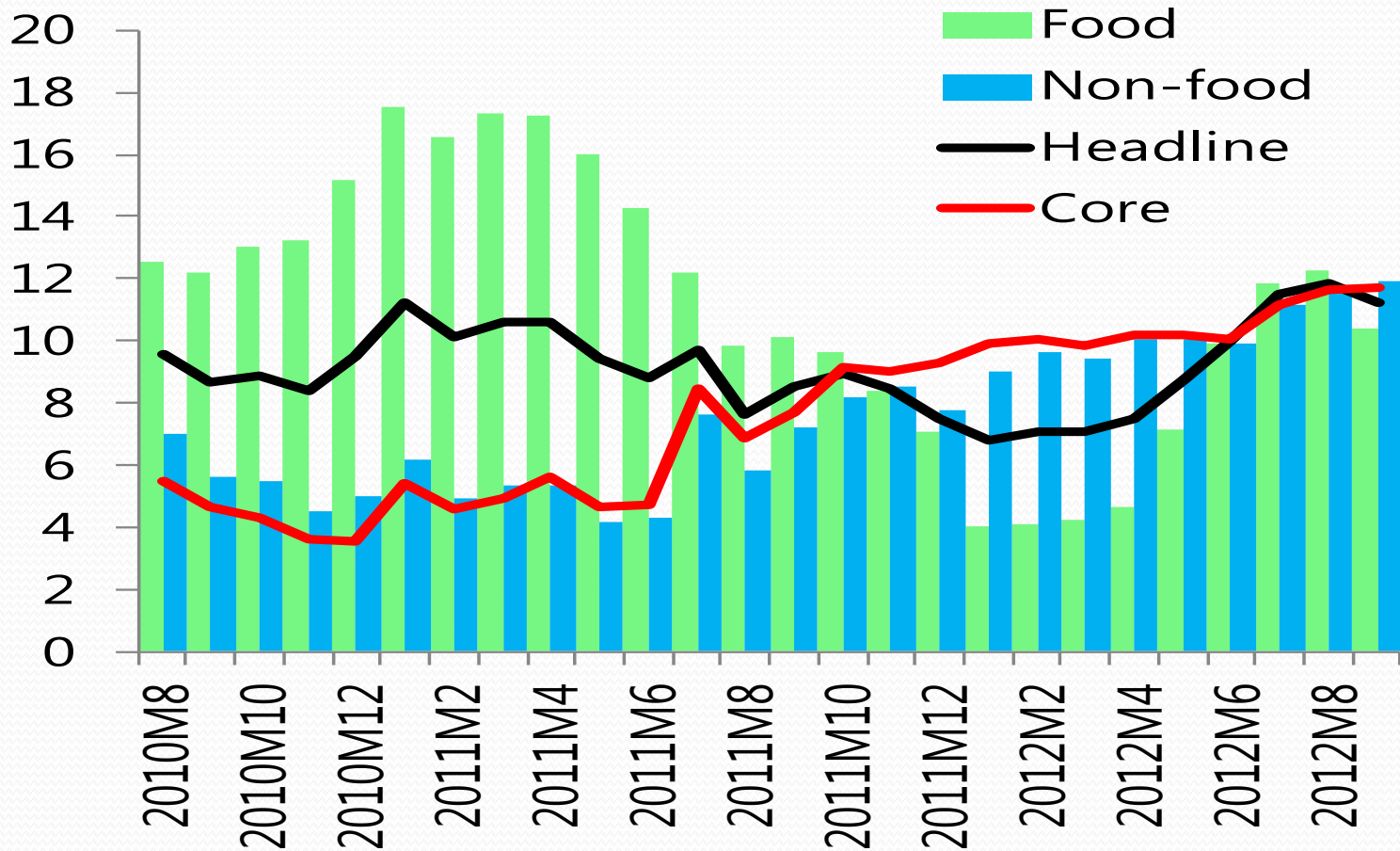
Sectoral Contribution to Growth (in percent)



Inflation remains a concern

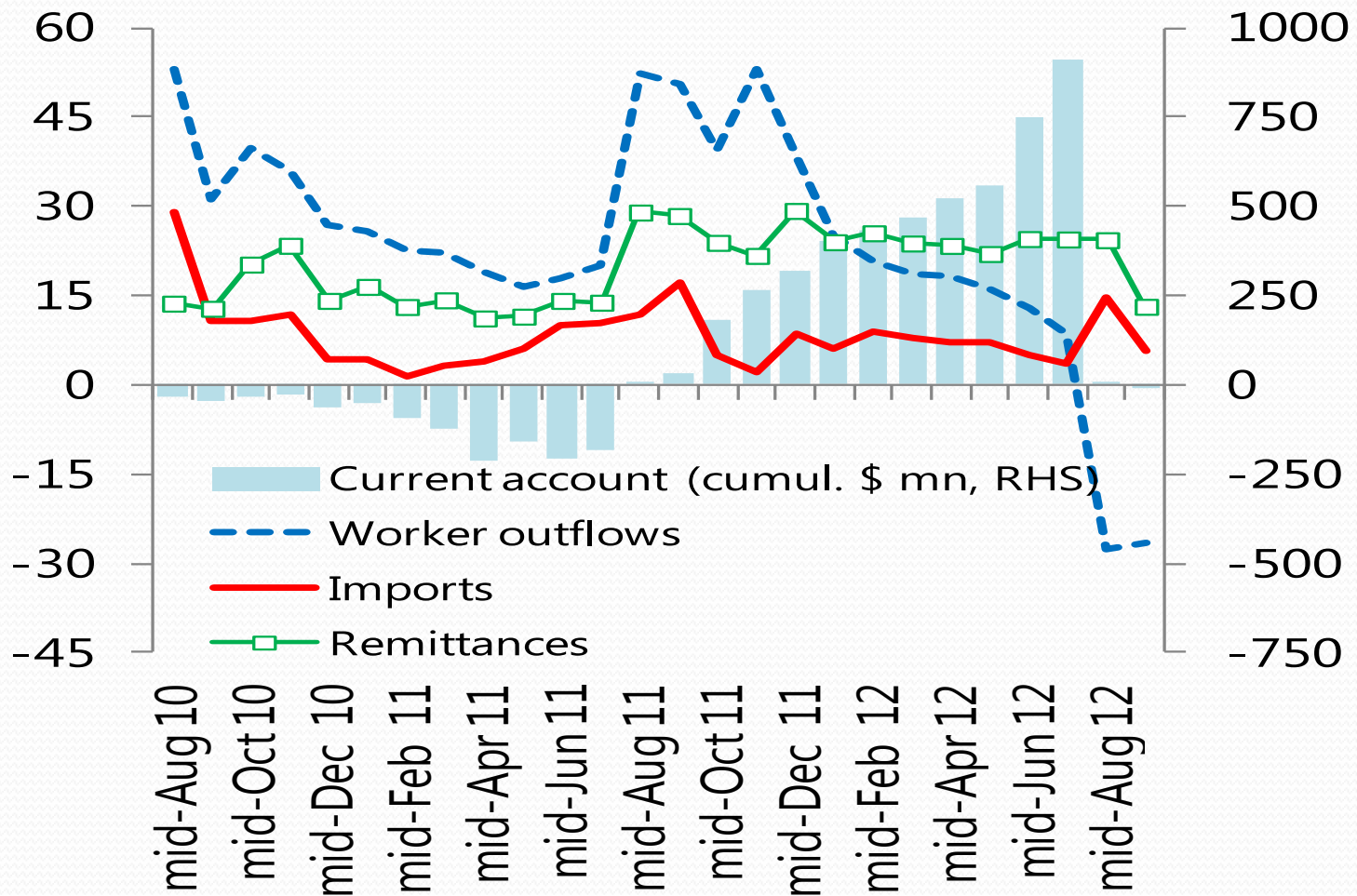
Inflation

(Year-on-year percent change)



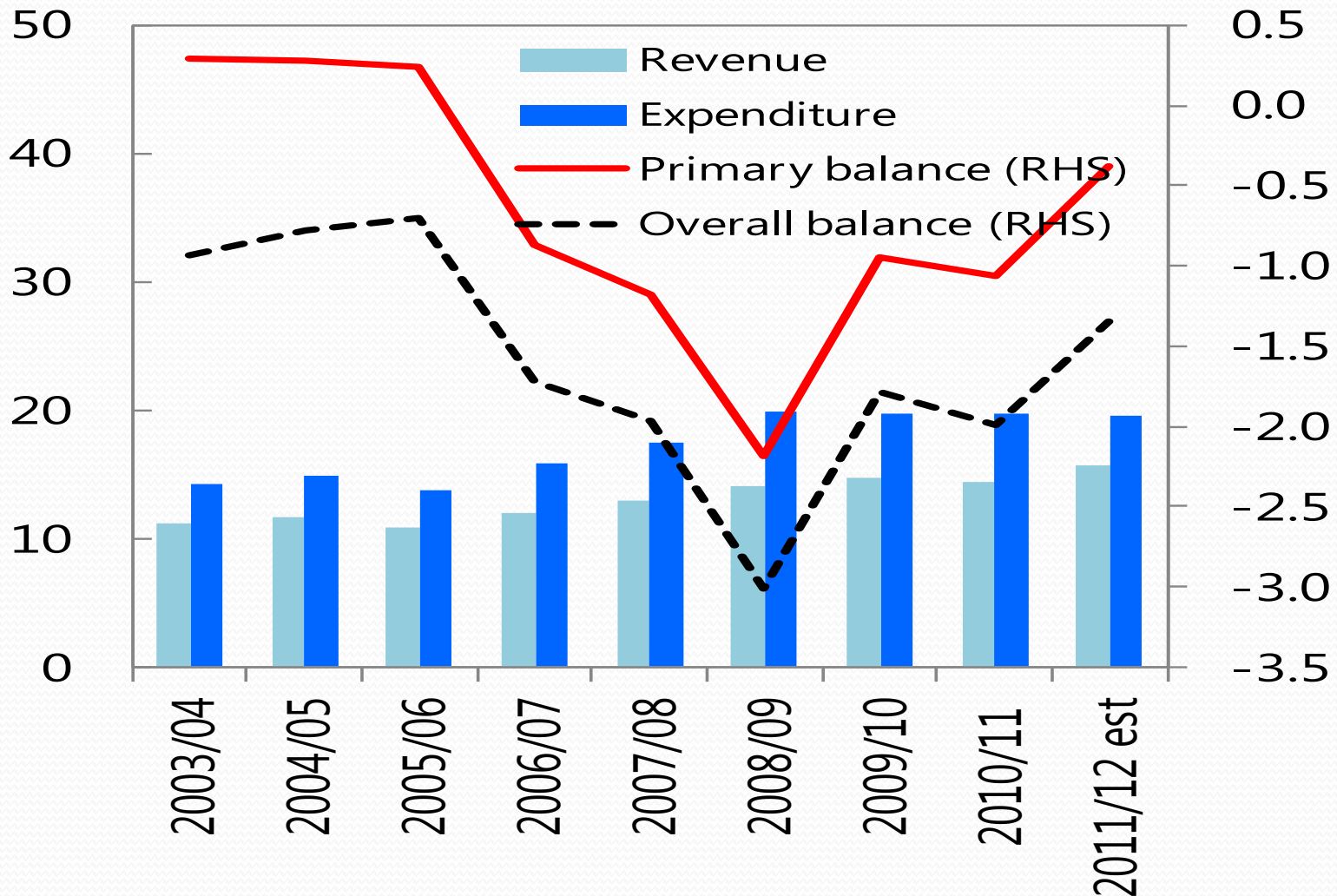
Current account improved, but risks have grown

External Sector (Year on year change in cumulative)



Fiscal deficit “over-performed” (and it’s a problem)

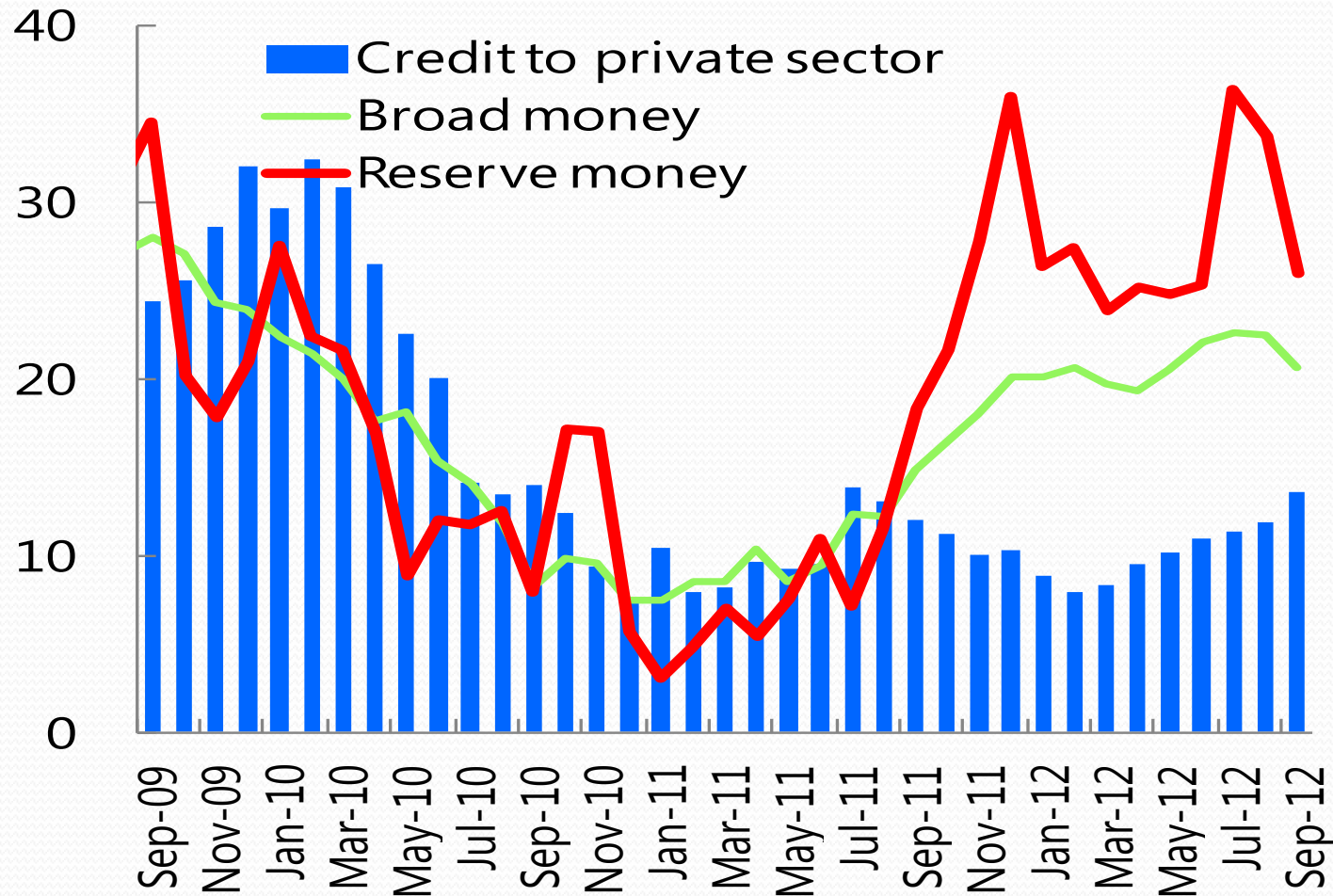
Revenue and Expenditure (In percent of GDP)



Liquidity conditions eased in the financial sector

Monetary Aggregates

(Year-on-year percent change)



Financial sector improved, but risks remain

Nepal: Commercial Banks' FSIs 1/			
	2010	2011	2012 1/
Capital adequacy			
Capital fund to risk weighted assets	9.6	10.6	11.5
Tier 1 capital to risk weighted assets	7.9	9.1	10.0
Asset quality			
NPLs to total loans	2.5	3.2	2.6
Loan loss provision to total loans	4.6	4.0	3.6
Earnings and profitability			
Return on equity (ROE) 2/	33.9	25.3	22.5
Return on assets (ROA) 2/	1.9	1.7	1.5
Liquidity			
Liquid assets to total assets	13.1	11.2	13.0
Liquid assets to demand and savings deposits	31.7	31.6	36.6
Liquid assets to total deposits	16.0	14.3	16.3
Exposure to real estate			
Share of real estate and housing loans	20.7	18.5	16.9
Share of loans collateralized by land and buildings	58.4	68.4	55.9

1/ Capital adequacy, NPLs, loan loss provisioning, ROE, ROA, and exposure to real estate indicators as of July 2012; liquidity indicators as of June 2012; and

2/ Excluding state-owned banks.

Outlook for 2012/13

- **GDP growth is likely to decline—IMF: 3.8%**
 - Agriculture (poor monsoon)
 - Fiscal policy uncertainty
- **Inflation to remain elevated—IMF: 8.3%**
 - Some spillover from India
- **Current account to weaken—still in surplus**
 - Outflow of workers is slowing, so remittances could fall
 - Imports seem to be recovering

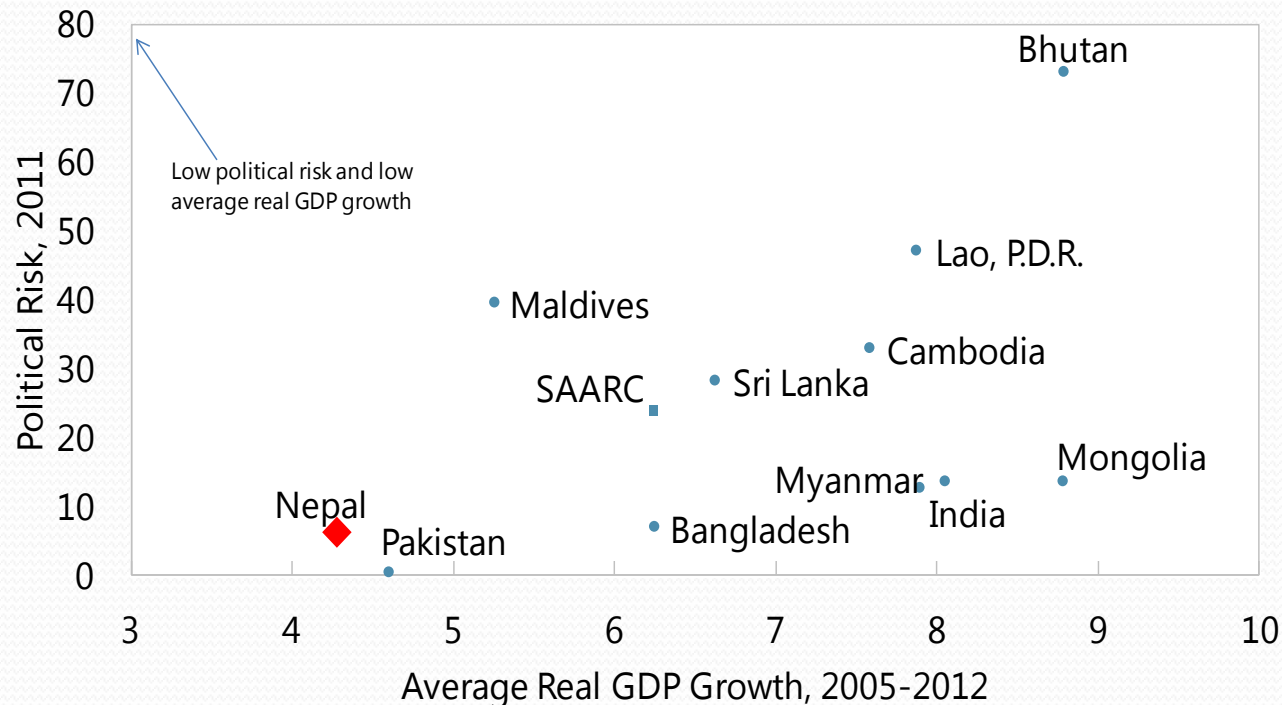
Policy Messages

- Welcome issuance of the last 2/3 budget (avoids “fiscal cliff”)
- At the same time, there are limits to fiscal space:
 - mounting quasi-fiscal liabilities (NOC)
 - weak capital spending (will need to catch up)
 - interest rate differential with India and rising inflation limit monetary policy
- Addressing financial sector vulnerability with accelerated and well-sequenced reform is crucial, but may also impinge on the fisc

Longer Term Perspective

Political stalemate hampers long-term growth potential

Political Risk and Average Growth 1/



Sources: IMF, *World Economic Outlook*; and World Bank, *Worldwide Governance Indicators*.
1/ Political risk represents the political stability and absence of violence/terrorism ranking from the Worldwide Governance Indicators database. SAARC is calculated as a simple average of data in South Asian Association for Regional Cooperation member countries.

Structural reforms needed

Nepal: Governance and Doing Business Indicators

Governance Indicators (percentile rank; a higher value indicates better performance)

	2007	2008	2009	2010	2011	2012	
Governance Indicators							
Political Stability / Absence of Violence	5.8	5.7	6.6	5.7	6.1	...	→
Voice and Accountability	30.3	30.8	31.3	31.3	31.5	...	→
Government Effectiveness	29.1	23.8	21.5	25.8	22.7	...	↓
Regulatory Quality	33.3	30.1	29.1	26.3	24.9	...	↓
Rule of Law	30.1	26.0	19.4	16.6	17.4	...	↓
Control of Corruption	25.7	26.2	28.2	28.7	23.7	...	↓

Doing Business Indicators (out of 183 rated countries -- a lower rank is a better performance)

Doing Business (overall rating)	100	111	121	123	116	107	↑
Starting a Business	49	60	73	87	96	100	↓
Dealing with Licenses / Construction Permits	127	125	129	131	130	140	↓
Registering Property	25	25	28	26	25	24	→
Getting Credit	101	97	109	113	89	67	↑
Protecting Investors	60	64	70	73	74	79	→
Trading Across Borders	136	151	157	161	164	162	→
Enforcing Contracts	105	123	121	122	123	137	↓

Source: Worldwide Governance Indicators, World Bank; Doing Business 2012, World Bank.

IMF Engagement beyond Article IV

1. IMF program—menu of options:
 - ECF, PSI, SMP
2. Technical assistance (mainly funded by donors):
 - Resident advisor on financial sector issues
 - Resident advisor on tax administration
 - Resident advisor on PFM (TSA, MTEF)
 - Ongoing and forthcoming TA missions:
 - Revenue administration and tax policy review
 - National accounts and BoP statistics
 - AML/CFT regime
 - PFM, GFS and fiscal reporting

**Thank
you**

*Want to
know more?
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nepal](http://www.imf.org/nepal)*

