



Da Afghanistan Bank

Economic & Statistical Bulletin

Quarterly Bulletin, Q1 - FY 1395



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Quarterly Bulletin, Q1 - FY 1395

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Note:

Afghanistan's Fiscal year has been changed effective from 1391 (2012). The new fiscal year begins on December 21 each year. This Quarterly Bulletin describes developments in the first quarter of fiscal year 1395, which covers December 20, 2015 to March 20, 2016.

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ABBREVIATIONS

DAB	Da Afghanistan Bank
GOA	Government of Afghanistan
FEMA	Foreign Exchange Market in Afghanistan
CPI	Consumer Price Index
NCPI	National Consumer Price Index
KCPI	Kabul Consumer Price Index
TM	Trimmed Mean
MOF	Ministry of Finance
CMEA	Ex-Soviet Trading Block
ARTF	Afghanistan Reconstruction Trust Fund
LOTFA	Law and Order Trust Fund for Afghanistan
MPD	Monetary Policy Department
GDP	Gross Domestic Product
WGP	World Gross Product
CSO	Central Statistics Office
CIS	Commonwealth of Independent States
IMF	International Monetary Fund
IDB	Islamic Development Bank
SDR	Special Drawing Rights
RM	Reserve Money
CiC	Currency in circulation
NIR	Net International Reserves
GIA	Gross International Asset
FX Auction	Foreign Exchange Auction
CNs	Capital Notes
ONDF	Overnight Deposit Facility
ONCF	Overnight Credit Facility
CA	Current Account
FA	Financial Account
FDI	Foreign Direct Investment
FSD	Financial Supervision Department
LCs	Letters of Credit
ODCs	Other Depository Corporations
ROA	Return on Assets
ROE	Return on Equity
NPL	Non-performing Loan

Senior Management



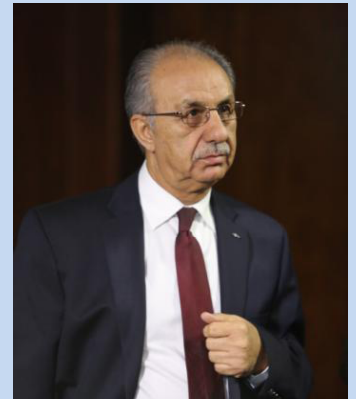
Alhaj Essa Khan Turab

Second Deputy Governor



Khan Afzal Hadawal

First Deputy Governor



H.E. Khalil Sediq

Governor



Message

From the Governor

‘Da Afghanistan Bank (DAB) policies/efforts are geared towards protecting the most vulnerable segments of society by focusing on price stability -DAB’s primary mission- through implementing a sound and effective monetary policy’

EXECUTIVE SUMMARY

During the first quarter of the fiscal year 2016 economic activities remained subdued in almost every sector of the Afghan economy. Turbulent economic and political environment of the country continued to weaken economic growth and private and public investment. Meanwhile, undertaken reforms such as expanding electricity supply, increasing domestic revenue and efforts to encourage private investment demonstrate Afghan Unity Government commitment to restore economic stability in the country. It is worth mentioning that such reforms also helped guard Afghan economy against global slowdown.

The first quarter of 2016 saw a surge in consumer price in Afghanistan. Headline inflation rose to 3.8 percent from a deflation rate of 0.6 percent (Y-over-Y). High inflation during the review period is underpinned by both external -higher price of commodity in South Asia- and internal factors. However, at the end of the first quarter of 2016, depreciation of Afghani against the U.S dollar remained the main source of inflationary pressures on the CPI.

Meanwhile on the fiscal front the overall performance in the public sector was sluggish due to deferment in budget approval by the parliament that also caused donors to lower their contribution. Furthermore, Afghanistan's public expenditure remained unbalanced during FY 2016, owing to continued deterioration in

security conditions which undermined private investment, delayed budget execution, and capital flight.

Balance of payment figures demonstrates weak performance of the external sector. The current account deficit in the first quarter of the FY 1395 increased significantly when compared with the same quarter of last year. The deficit was attributed largely to the decline in inflows in services and income account as well as decline in inward transfers especially home remittances. Trade deficit (trade in goods) rose slightly by 1 percent to USD 1,482.51 million in the first quarter of the FY 1395 in comparison to USD 1,500.51 million in the first quarter of the FY 1394. Similarly, capital account of the balance of payments illustrated a decline of 44 percent in the first quarter of the FY 1395 when compared to the same quarter of the FY 1394 as a result of lower inward capital transfers.



1

GLOBAL ECONOMIC ENVIRONMENT

1

GLOBAL ECONOMIC ENVIRONMENT

The global economy expanded by almost 0.9 percent in Q1 2016, slightly higher than 0.78 percent in Q4 2015. The growth was in the light of 0.6 percent growth in advanced economies in the first quarter of 2016 and 1.1 percent expansion in the emerging and developing economies.

I. Advanced Economies

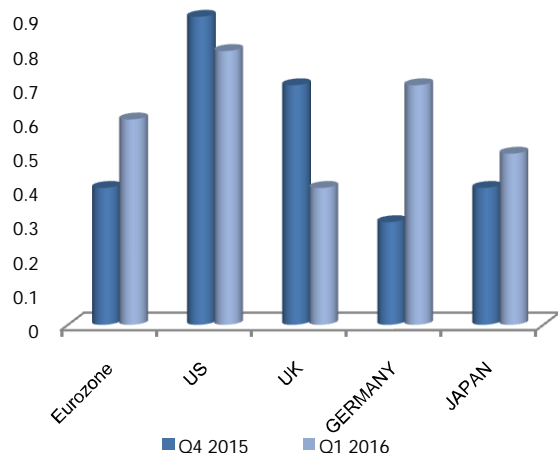
Advanced Economies experienced relatively slower growth in the first quarter of the fiscal year 2016 as compared to the previous quarter. The US economy expanded by 0.8 percent, slightly lower than 0.9 percent expansion recorded in Q4 2015. The Q1 2016 figure presented the slowest growth pace since 2014 due to fall in consumer spending, worsening investment and business inventories. The same as US economy, Euro-zone economy advanced by 0.6 percent in the first three months of 2016 (Q1 2016), higher than an upwardly revised 0.4 percent expansion in the previous quarter, mainly driven by households spending and increase in

the volume of private investment, which recorded the strongest performance in the last year.

Meanwhile, UK's economy expanded 0.4 percent in Q1 2016, lower than 0.7 percent in Q4 2015. The sluggish growth in UK's economy related mainly to fall in business investment and decline in exports.

The Japanese economy expanded 0.5 percent in first quarter of 2016, compared to an initial estimate of a 0.4 percent growth. Private consumption grew faster than expected while business spending fell much lower than anticipated while government spending and exports were in line with expectations.

The German economy grew a seasonally-adjusted 0.7 percent in the first quarter of 2016, accelerating from a 0.3 percent expansion in the preceding quarter. It is the strongest expansion since the first quarter of 2015, mainly driven by household spending and a rapid increase in investment, although foreign trade had a slight downward effect on growth.

Figure 1.1: GDP Growth

Consumer prices in the Euro-zone edged up 0.3 percent in March of 2016, higher than 0.2 percent in the previous quarter, it was almost in line with advanced economies but much lower than emerging economies such as Russia, India and China. The US inflation rate was 1.1 percent in Q1 2016, higher than 0.46 percent in Q4 2015, the rise in inflation was mainly due to increase in prices of shelter and health care.

Consumer prices in the United Kingdom accelerated to 0.5 percent in March 2016 from 0.2 percent in December 2016. Cost of housing and utilities increased for the first time in three months and recreation and culture recorded the biggest gain since October of 2014.

Consumer prices in Japan dropped to zero percent in March of 2016, from 0.2 percent in Q4 2015. It was the third straight month of decline as prices of food eased while cost of housing and transport declined.

Consumer prices in Germany rose 0.3 percent in March of 2016, remaining unchanged from December 2015. While cost of energy fell at a slower pace, cost of services rose further.

The seasonally adjusted unemployment rate in the Euro Area remained at 10.4 percent at the end of the first quarter of fiscal year 2016.

The labor market in the United States improved noticeably, unemployment dropped to 4.9 percent in Q1 2016, lower than 5.8 percent rise in Q4 2015 while unemployment rate in the United Kingdom remained 5.1 percent in Q4 2015 and Q1 2016. It was the lowest rate since 2005 in this country.

The seasonally adjusted unemployment rate in Japan was recorded at 3.2 percent in March of 2016, 0.1 percent higher than the previous two months and in line with market expectations. This rate was rather higher in Germany. The unemployment seasonally adjusted rate was 4.3 percent in March of 2016, compared to an upwardly revised 4.4 percent in the previous quarter. The jobless rate remained at its lowest level in 35 years in Germany.

The Euro-zone trade surplus recorded at USD 33.13 billion in Q1 of 2016 compared to USD 29.32 billion in Q4 2015. Considering the first five months of the year, the trade surplus increased to USD 119.83 billion, compared to USD 97.75 billion in the same period of 2015. Meanwhile, trade gap in the United States narrowed in March 2016 to USD 35536 billion compared to USD 41487 billion deficits in December 2015.

Trade deficit in the United Kingdom went up by USD 1.7 billion to USD 5.75 billion in Q1 2016 from USD 2.75 billion in Q4 2015. Imports comparing to exports, declined for the first time this year.

Japan recorded a USD 6.63 billion deficit in March of 2016, compared to a USD 1.23 billion surplus in previous quarter. It was the first deficit since January. Exports dropped by 11.3 percent and imports decreased by 13.8 percent and matching market consensus

The trade surplus in Germany increased to USD 29.76 billion in March of 2016 as exports went up while imports recorded the third month of no growth. The trade surplus in Germany recorded at USD 21.26 billion surplus in Q4 2015.

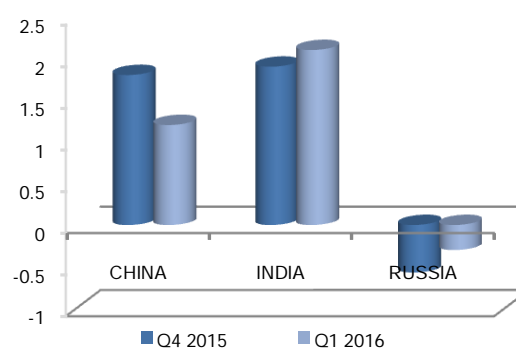
II. Emerging Economies

Growth in emerging market economies was very modest as most of these economies experienced slower growth rate and were considerably impacted by Chinese economic slowdown.

Chinese economy expanded 1.2 percent in Q1 2016, lower than 1.8 percent growth in the previous quarter and weakest since July 2013. Meanwhile, Russia's GDP growth rate contracted to -0.3 percent in Q1 2016, improved as compared to negative 0.57 percent growth in Q4 2015. It is believed that fall in exports and consumers spending were the main drivers of negative growth in Russia. The Gross Domestic Product (GDP) in India

expanded by 2.10 percent in the first quarter of 2016 over the previous quarter. It is worth mentioning that GDP Growth Rate in India averaged 1.67 percent from 1996 until 2016, reaching an all-time high of 5.80 percent in the second quarter of 2009 and a record low of -1.80 percent in the first quarter of 2009.

Figure 1.2: Economic Growth



Consumer prices in Russia dropped to 7.3 percent in March of 2016 from 12.9 percent in the previous month. It was below the market expectations of 7.4 percent. Food, housing and transport prices growth decelerated while recreation and culture prices rose at a slower pace. On the contrary, the inflation rate recorded at 2.3 percent at the end of Q1 2016 which was higher than 1.6 percent registered in Q4 2015. The inflation rate still remained below the government's 3 percent target for 2016.

The consumer prices in India went up to 4.83 percent in March of 2016 from 5.56 percent recorded in the previous quarter.

More than any advanced or emerging economy, Russia recorded the highest unemployment rate at 6 percent in March of

2016, up from 5.8 percent in the previous quarter (December of 2016).

Despite structural transformation of Chinese economy, the unemployment Rate remained almost unchanged in Q1 2016, just over 4 percent. Unemployment Rate in China averaged 4.13 percent from 2002 until 2016.

Russia's trade surplus decreased sharply to USD 7.96 billion in March 2016 from a USD 11.3 billion surplus in the previous quarter. Exports dropped 28.3 percent and imports went down at a slower 5.5 percent in Russia.

In the first quarter of fiscal year 2016 Chinese trade surplus was lower than expected. China's trade surplus shrank significantly from USD 59.63 billion in Q4 2015 to USD 28.7 billion in Q1 2016, resulting from rapid decline exports and rise in imports.

The trade deficit in India declined to USD 5.07 billion in Q1 of 2016 from USD 11.644 billion in Q4 2015. India's balance of trade improved due to unprecedented rise in its exports and decline in oil prices.



2

**MONETARY AND CAPITAL MARKET
DEVELOPMENTS**

2

MONETARY AND CAPITAL MARKET DEVELOPMENTS

Monetary and capital market developments chapter provides a brief report on monetary program, monetary aggregates, net international reserves foreign exchange rates, as well as the open market operation and liquidity condition.

In the first quarter of fiscal year 1395 (22 Dec. 2015 to 19 March. 2016) , reserve money -Da Afghanistan Bank's operational target- experienced a negative growth of 6.35 percent, standing at Af 212,548.02 million at the end of Q1FY 2016. Currency in circulation which is indicative target of DAB has also decreased by 5.86 percent in the period under review, Af 189,617.60 million.

Narrow money (M1) stood at Af 366,679 million at the end of the quarter under review, registering a growth of 3.58 percent (Q-o-Q). Broad money (M2) demonstrated similar behavior; stood at Af 394,290 million at the end of the first quarter of FY 2016, expanding by 5.48 percent

During the Q1, FY 2016 DAB's net international reserve (NIR) recorded an increase of 1.91 percent, reaching USD 6,546.83 million.

At the end of Q1 FY 2016, Afghani depreciated against the US dollar by 18.29 percent in comparison with the first quarter of FY 2015.

During the first quarter of FY 2016, DAB auctioned a total amount of USD 479.24 million to manage the liquidity in the market as well as to mitigate the severe fluctuations in the exchange rate of Afghani against the foreign currencies. The total outstanding amount of CNs stood at Af 32.12 billion at the end of period under review.

I – MONETARY PROGRAM

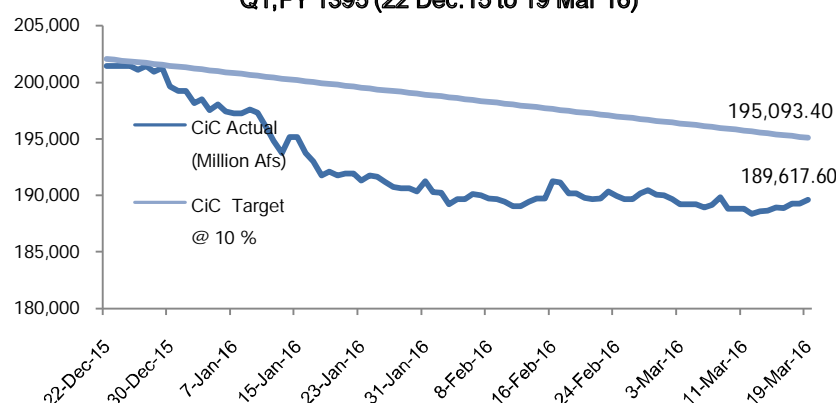
To determine the amount of reserve money (RM) for purpose of supporting domestic price stability, which is DAB's primary objective, DAB uses quantitative theory of money. Hence, the assigned targets for RM and currency in circulation (CIC) are based on expected economic growth and expected inflation during the concerned period.

Considering DAB's past experiences and low level of demand for Afghani in domestic market, DAB set ceilings for reserve money and currency in circulation growth at - 4.95 and - 3.46 percent respectively for the Q1 of FY2016. With hindsight, actual RM and CIC remained well below to the target with negative growth of 6.35 and 5.86 percent.

DAB continued to conduct a tight monetary policy in the reporting period in order to absorb excess liquidity as well as to prevent volatility in the nominal exchange rate of Afghani against foreign currencies.

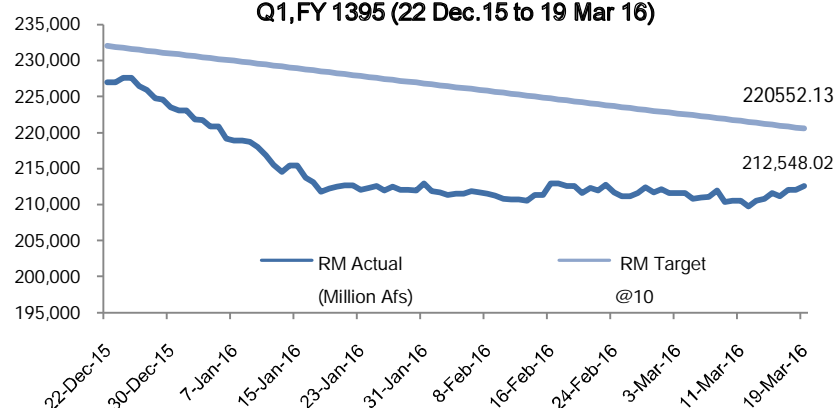
The Figure 2.1 and 2.2 present the ceiling and the actual currency in circulation and reserve money for the period under review.

Figure 2.1: Currency in Circulation for the Q1, FY 1395 (22 Dec. 15 to 19 Mar 16)



Source: Monetary Policy Department/DAB

Figure 2.2: Reserve Money for the Q1, FY 1395 (22 Dec. 15 to 19 Mar 16)



Source: Monetary Policy Department/DAB

II. MONETARY AGGREGATES

As shown in Table 2.1 narrow money (M1) grew by 3.58 percent in Q1, FY2015 compared to 4.4 percent in Q1, FY2015, showing a difference of Af 12,680 million. Currency outside depository corporations or CIC -a major component of M1 (50%)- grew by 5.55 percent in Q1, 2016 compared to 7.3 percent recorded in the first quarter of the previous year. The difference in currency outside depository corporations in Q1, 2016 compared to Q1, 2015 is Af 9,674 millions. Demand deposits –other major component of M1- experienced a growth of 1.67 percent during a Q1, FY2015 while its quarterly growth was 1.8 percent.

The supply of broad money (M2) expanded to Af 394,290 million in the Q1, FY 2016 from Af 373, 5795 million in the same quarter of previous year, up by 5.48 percent. The current period figures show that M1 remained the main contributing component of M2 (93%).

Quasi money or time deposits of commercial banks, which is the other component of M2, grew by 39.47 percent (y-o-y) in the Q1 of FY 2016. Quasi money constituted only 7 percent of broad money during the period under review, although higher than 5 percent in Q1 FY 2015 but still the impact of changes in quasi money on the M2 is negligible. The year-on-year difference of Afghani denominated time deposits stood at Af 1,909 million, while the foreign currency denominated time deposits recorded Af 18,784 million which is 45.86 percents higher than previous year. Afghani-denominated time deposits constitute 2 percent of broad money. While, the share of foreign currency denominated time deposits was 5 percent of M2 in the quarter under review.

Demand deposits as a share of broad money decreased to 46 percent (Y-o-Y) in the quarter under review, down by 8 percent compared to the same quarter of previous year. The figures 2.3 and 2.4 indicate some facts about money aggregates and its components.

Figure 2.3: Demand Deposits as Share of Broad Money in %

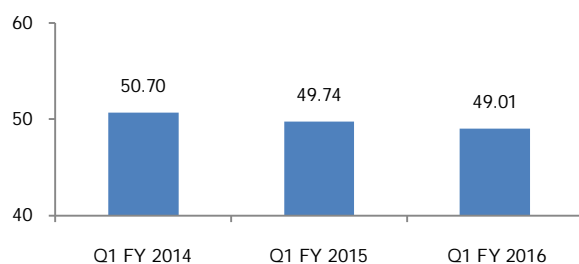
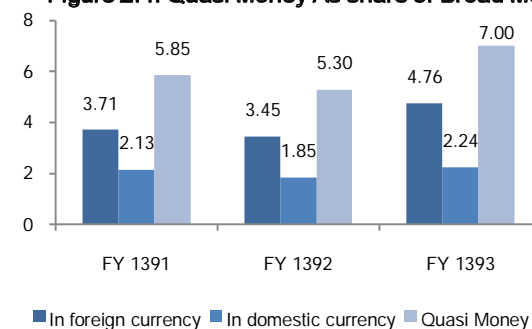


Figure 2.4: Quasi Money As share of Broad Money (%)



Source: Monetary Policy Department/DAB

Table 2.1: Monetary Aggregate for the FY 1395 (Dec 15 - March 16)

Figures in million AF, unless otherwise indicated

In Million Af	Q1,2014	Q1, 2015	Y-o-Y Δ	Difference	Q1 2016	Y-o-Y Δ	Difference
	Amount	Amount			Amount		
1- Net Foreign Assets	468,329	483,627	3.3%	15,298	548,969	13.51%	65,342
(a) Foreign Assets	497,107	509,667	2.5%	12,560	581,123	14.02%	71,455
DAB Foreign exchange reserves	409,184	425,334	3.9%	16,149	477,665	12.30%	52,332
Gold	47,509	47,509	0.0%	0	51,513	8.43%	4,004
Other	361,676	377,825	4.5%	16,149	426,152	12.79%	48,328
Other foreign assets	87,923	84,334	-4.1%	-3,589	103,457	22.68%	19,124
(b) Foreign Liabilities	28,778	26,040	-9.5%	-2,738	32,153	23.48%	6,113
2. Net Domestic Assets	-108,324	-109,808	1.4%	-1,483	-154,485	40.69%	-44,677
(a) Net Domestic Credit	-52,962	-31,895	-39.8%	21,067	-24,097	-24.45%	7,799
Net Credit to Nonfinancial Public Sector	-97,933	-71,840	-26.6%	26,093	-72,640	1.11%	-800
Net Credit to Central Government	-97,874	-71,754	-26.7%	26,120	-72,735	1.37%	-980
Credit to Central Government	34,473	59,088	71.4%	24,615	61,164	3.51%	2,076
Liabilities to Central Government	132,347	130,842	-1.1%	-1,505	133,898	2.34%	3,057
Net Credit to State & Local Government	0.000	0.000	0.0%	0	0.000	0.000	0
Net Credit to Public Nonfinancial Corporations	-59	-86	44.9%	-27	94	-210.15%	180
Credit to Private Sector	46,320	41,588	-10.2%	-4,732	49,974.50	20.16%	8,386
Net Credit to Other Financial Corporations	-1,349	-1,644	21.8%	-295	-1,430.80	-12.96%	213
(b) Capital Accounts	104,187	95,499	-8.3%	-8,688	142,589	49.31%	47,090
(c) Other Items Net	48,825	17,586	-64.0%	-31,238	12,200	-30.63%	-5,386
3- Broad Money(M2)	359,990	373,795	3.8%	13,804	394,290	5.48%	20,495
Narrow Money(M1)	338,934	353,998	4.4%	15,065	366,679	3.58%	12,680
CiC (Currency outside depository corporations)	162,368	174,174	7.3%	11,806	183,848	5.55%	9,674
Demand Deposits	176,566	179,824	1.8%	3,259	182,830	1.67%	3,006
Other Deposits (Quasi Money)	21,057	19,796	-6.0%	-1,260	27,611	39.47%	7,815
In Afghani	7,685	6,919	-10.0%	-767	8,827	27.59%	1,909
In Foreign currency	13,372	12,878	-3.7%	-494	18,784	45.86%	5,906
Securities Other Than Shares	0.000	0.000	0.000	0.000	0.000	0.000	0.000

Source: Monetary Survey, Monetary Policy Department/ DAB

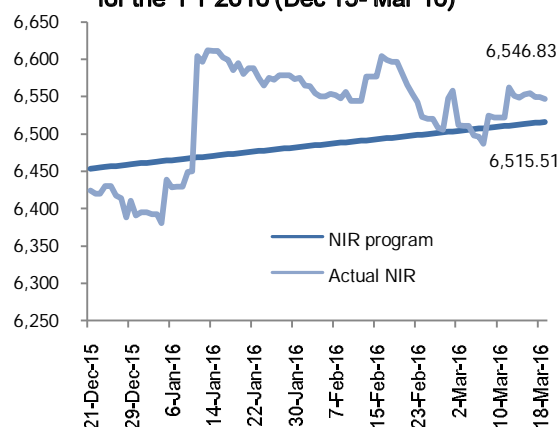
2.1 NET INTERNATIONAL RESERVE

NIR increased by 3.88 percent, USD 254.08 million, during the first quarter of the fiscal year 2016. The target of NIR for the first quarter of fiscal year 2016 was set at USD 6515.15 million

while the actual figure of NIR recorded the amount of USD 6549.52 million which is well above the targeted amount.

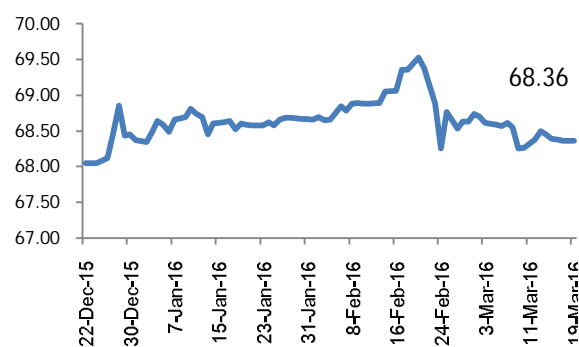
Figure 2.5 explains the trend of NIR actual and target during Q1, FY2016.

**Figure 2.5: Net International Reserve
for the FY 2016 (Dec 15- Mar 16)**



Source: Monetary Survey, Monetary Policy Department/ DAB

**Figure 2.6 : Daily Average Ex-Rate of Afghani
against USD for the FY 2016 (Dec 15- Mar 16)**



Source: Monetary Survey, Monetary Policy Department/ DAB

III. FOREIGN EXCHANGE MARKET

Afghani depreciated against the U.S dollar by 18.29 percent from the same quarter, traded at Af 68.36 per U.S. dollar at the end of Q1, FY2016.

The devaluation of Afghani was mainly triggered by the persistently high current account deficit, as well as domestic factors emanating from national political and security situations.

The daily historic review of the average exchange rate of Af against the U.S. dollar for the Q1 of fiscal year 2016 is shown in figures below.

IV. OPEN MARKET OPERATION & LIQUIDITY CONDITIONS

4.1 Foreign Exchange Auction

During the first quarter of fiscal year 2016 DAB auctioned a total amount of USD 479.24 million and the total demand was USD 647.72 million. On average, 47 bidders participated in each auction and 35 winning bidders were awarded with the average amount of USD 13.31 million. Whereas, in the same period of FY 2015 total awarded amount was USD 750.20 million, with a total demand of USD 1007.10 million.

4.2 Capital Note Auction

Total outstanding stock of capital notes reached Af 32.12 billion at the end of the Q1 FY 2016, which shows a decrease of 8.5 percent

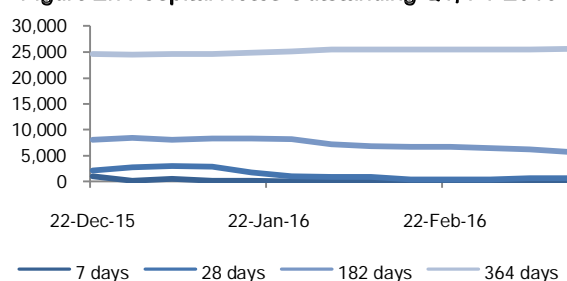
compared to Af 34.86 billion at the end of Q1 FY 2015.

Meanwhile, the outstanding stock of 7 day note stood at Af 30 million, 28 days CN outstanding amount stood at 530 million, outstanding stock for 182 day notes stood at Af 6.120 billion and the amount of outstanding of 364 days capital notes was stood at 23.9 billion at the period under review.

Figure 2.07 exhibits breakdown of the total outstanding stock for all maturities during the Q1, FY2016.

In addition the weighted average interest rate for 7 day capital note was 1.8 percent, for 28 day security was 3.53 percent, meanwhile interest rate for 182 day was 5.15 percent and for 364 days capital notes interest rate was set at 6.73 percent at the end of this reporting period.

Figure 2.7: Capital Notes Outstanding Q1, FY 2016



Source: Market Operations Department/DAB

5.3 Required and Excess Reserves

Commercial banks are required to hold 8 percent of their total deposits as obligatory reserves with the DAB, in recent development

from 28 June 2015 onward DAB has stopped paying interest rate for required reserve.

In order to provide commercial banks with facilities to better manage their liquidity and to provide them with a proper opportunity to invest their excess reserves apart from capital notes, DAB introduced the **overnight standing facilities** in 1385 (2006-2007). However, DAB stopped issuing Overnight Security Facilities from it has been temporarily. After assessment of OSF effectiveness as monetary policy tool DAB uphold overnight standing facilities. During Q1 FY 2016 the payment of interest rate to the mentioned facility reached to Afs 6.426 million.

Overnight Credit Facility: This facility allows commercial banks to borrow local currency from Da Afghanistan Bank on an overnight basis, whenever they face a shortfall in their short term liquidity position. The rate that banks are charged for this facility is 350 basis points above the last 28 day CNs auction rate. This borrowing is collateralized with the outstanding of capital notes. The reason behind such high rate of interest is to encourage the inter-bank lending among the commercial banks.



3

THE INFLATION TREND AND OUTLOOK

3

INFLATION TREND AND OUTLOOK

At the start of 2016, global economy witnessed low commodity price consistent with weaker price of energy and agricultural products, and devaluation of US dollar. Based on the most recent reports, energy price lowered 21 percent from its level in December 2015. During the first quarter of 2016, crude oil price fell by 22 percent, which resulted in lower price of energy. Negative effects on oil price came partly from demand side, but most importantly from supply side surging from disruptions in Iraq and Nigeria. With benign contribution of weather conditions, agricultural prices continued its broad based declining trend, as the overall index dropped by 1.4 percent (Q-to-Q), and almost 9 percent (Y-over-Y). The decline in agriculture price was driven primarily by falling price of beverage price index (7.5 percent), and agricultural raw material price index (1.8 percent).

In South Asia, inflation increased, while oil price remained cheap. Pakistan showed an inflation rate of 3.9 percent, higher than 3.2 percent observed in the previous quarter. However, inflationary pressures in the regions

are somehow downplayed by low inflation in India.

I. CONSUMER PRICE IN AFGHANISTAN

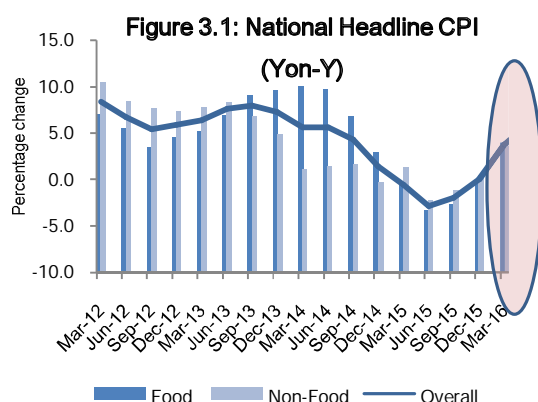
In the first quarter of 2016, consumer price in Afghanistan increased. Headline inflation rose to 3.8 percent from a deflation rate of 0.6 percent (Y-over-Y).

High inflation during the review period is partly because of higher price of commodity in South Asia, but more primarily due to internal factors. By the end of the first quarter of 2016, depreciation of Afghani against the U.S dollar remained the main source of inflationary pressures on the CPI.

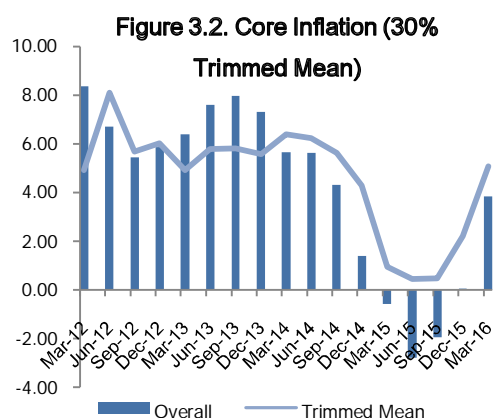
Unlikely, when measured on quarter-to-quarter basis, overall inflation decreased to 0.8 percent in the first quarter of 2016 from 3.4 percent recorded in the last quarter of 2015.

Looking ahead, the profile of Kabul headline CPI was similar to that of nationwide. Overall inflation in the capital of the country rose to

4.4 percent compared to -1.8 percent recorded in corresponding quarter of the previous year, while it declined on quarter-to-quarter basis (0.0 percent from 3.6 percent).



Source: Central Statistics Organization/DAB staff calculation



Source: Monetary Policy Department/DAB

3.1 Developments in National Headline CPI

1.1.1 Annual Developments

The year-over-year measure of inflation represented a significant increase in price level. During the first quarter of 2016, headline inflation when measured on year-

over-year basis rose to an inflation rate of 3.8 percent compared to a deflation rate of 0.6 percent recorded in first quarter of the previous year.

During the reporting period, both, food and non-food items of the CPI showed higher inflation rate. Given that inflation in most important sub-components of food item increased, this index rose to 4.0 percent, which is well higher than the deflation rate of 0.6 percent recorded in the same quarter of the previous year. In non-food category, inflation rose to 3.7 percent compared to a deflation rate of 0.5 percent (Y-over-Y).

In food sub-index, upward pressures came mainly from higher price of bread and cereals, meat, milk, cheese and eggs, oils and fats, and vegetables. However, the highest increase was seen in vegetable's price index standing at 1.9 percent from -11.7 percent.

Turning on non-food item, increase in price of housing, electricity, water and gas, furnishing and household goods, health, and transportation significantly contributed to higher inflation. In this item, price of transportation rose by 2.0 percent from -6.9 percent, which is the highest annual increase in non-food sub-index.

Core measures of inflation also showed upward movement compared to the same period of the previous year. Trimmed Mean, the most common measure of core inflation rose to 5.1 percent from 0.9 percent (year over year). In addition, CPI excluding bread and cereals, oil and fats and transportation

turned around to an inflation rate of 3.8 over-Y).
percent from a deflation rate of 0.4 percent(Y-

Table 3.1: Breakdown of National Headline CPI

(Percent changes year on year)

(March 2011=100)

	Weight	1393				1394				1395
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Overall Index	100.0	5.6	5.6	4.2	1.3	-0.6	-2.8	-1.9	0.1	3.8
Food and beverages	52.0	10.0	9.7	6.8	2.9	-0.6	-3.3	-2.6	-0.3	4.0
Bread and Cereals	17.7	9.5	11.4	11.0	8.0	2.1	-3.4	-2.3	0.5	5.0
Meat	7.2	2.6	3.4	3.7	3.4	2.4	-0.2	-1.5	0.8	3.2
Milk, cheese and eggs	4.8	6.5	6.1	2.1	3.4	1.4	1.0	1.5	1.3	2.4
Oils and fats	4.0	1.8	1.7	0.9	-1.7	-6.2	-7.2	-6.5	-6.6	-1.9
Fresh and dried fruits	4.8	8.5	9.9	9.2	11.5	6.6	7.9	2.0	0.5	3.6
Vegetables	7.9	30.3	24.3	7.1	-9.6	-11.7	-	-	-6.3	1.9
Sugar and sweets	2.9	2.5	-1.6	-0.2	-1.0	-1.1	0.5	0.4	6.0	11.1
Spices	0.9	10.5	9.4	12.0	5.9	1.0	-1.0	0.3	6.6	13.3
Non-alcoholic beverages	1.8	7.4	3.7	4.0	2.1	1.3	3.1	4.6	5.3	7.9
Non-Food	48.0	1.1	1.4	1.4	-0.5	-0.5	-2.2	-1.2	0.5	3.7
Tobacco	0.4	8.4	3.0	0.6	6.7	7.2	12.8	25.0	22.4	21.8
Clothing	7.0	8.3	8.1	6.9	4.2	2.9	2.0	6.6	8.6	9.9
Housing,	20.7	-8.5	-9.1	-8.8	-9.7	-4.6	-7.0	-7.4	-6.6	-2.7
Furnishing and household goods	7.0	8.5	10.4	10.3	8.4	4.9	2.1	3.3	5.7	9.7
Health	3.3	8.8	9.0	10.3	8.5	7.7	7.4	6.9	9.4	9.4
Transportation	4.7	16.6	20.1	19.5	11.3	-6.9	-	-7.8	-3.4	2.0
Communication	1.1	-1.5	-1.4	-2.0	-3.4	-4.7	-3.3	-2.2	-1.3	-0.1
Education	0.7	1.9	5.0	4.0	2.8	2.0	-2.7	-3.7	-5.1	-7.6
Information and Culture	0.1	6.5	5.4	7.1	7.0	1.2	3.8	5.2	6.3	6.5
Restaurants and Hotels	1.0	2.6	2.4	4.6	3.2	2.2	4.2	-0.8	-0.3	0.7
Miscellaneous	1.8	7.6	10.2	8.2	7.6	7.3	7.2	10.6	9.5	9.1
core inflation (30% TM)		6.4	6.3	5.6	4.3	0.9	0.5	0.5	2.2	5.1
Core inflation (Headline excl. B&C, O&F and T)		4.3	3.6	1.7	-0.8	-0.4	-1.9	-1.2	-1.0	3.8

Source: Central Statistics Office/Monetary Policy Department, DAB staff calculation.

1.1.2 Quarterly Developments in national CPI

The short-term measure of inflation represented a different trend to annual measure. Nationwide inflation when calculated on quarter-to-quarter basis fell to 0.8 percent from 3.4 percent recorded in the previous quarter. This decline is in line with low inflation in both, food and non-food items of the CPI.

Food inflation dropped to 1.6 percent from 4.5 percent. Price of bread and cereals, and vegetables sharply declined, which put significant downward effects on food sub-index. However, the largest quarterly decrease in this category was seen in vegetables', its price shrunk by 5.8 percent in the first quarter of 2016 from 17.4 percent observed in the previous quarter.

Non-food inflation also fell reaching to a deflation rate of 0.2 percent from an inflation rate of 2.2 percent. Although, deflationary pressures came from low prices of clothing, housing, electricity, water and gas, and transportation, the largest change happened in price of transportation declining by -3.6 percent from 1.1 percent

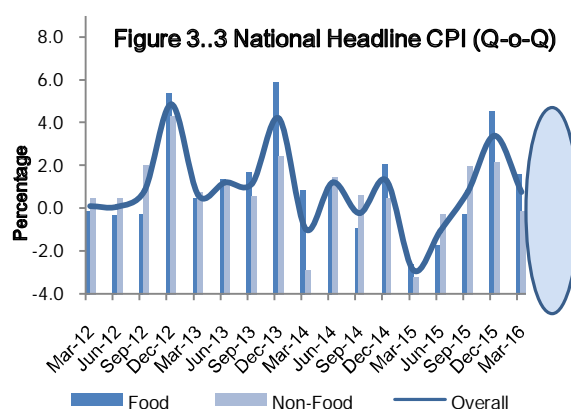


Table 3.2: Breakdown of National Headline CPI

(Percent changes quarter-on-quarter)

(March 2011 = 100)

	FY1393			FY 1394				FY1395
	Q1	Q2	Q3	Q1	Q2	Q3	Q4	Q1
Overall Index	-1.0	1.2	-0.2	1.3	-2.9	-1.1	0.8	3.4
Food and beverages	0.8	1.0	-1.0	2.0	-2.6	-1.7	-0.3	4.5
Bread and Cereals	0.6	4.1	2.7	0.4	-5.0	-1.4	4.0	3.2
Meat	0.3	0.7	2.1	0.3	-0.7	-1.9	0.8	2.7
Milk, cheese and eggs	1.9	-1.8	0.8	2.5	-0.1	-2.1	1.2	2.4
Oils and fats	-0.9	-0.2	-0.1	-0.5	-5.4	-1.3	0.6	-0.5
Fresh and dried fruits	6.5	3.4	-1.7	3.1	1.8	4.6	-7.1	1.5
Vegetables	-0.3	-3.0	-14.7	9.7	-2.7	-7.6	-11.2	17.4
Sugar and sweets	-2.1	-2.8	3.3	0.7	-2.3	-1.2	3.3	6.3
Spices	3.3	2.7	0.3	-0.5	-1.5	0.7	1.7	5.7
Non-alcoholic beverages	0.5	-0.6	1.9	0.3	-0.3	1.1	3.4	1.0
Non-Food	-2.9	1.4	0.6	0.5	-3.2	-0.3	1.9	2.2
Tobacco	-0.2	2.2	-2.8	7.6	0.3	7.5	7.8	5.4
Clothing	1.2	1.9	-0.2	1.3	-0.1	1.1	4.3	3.2
Housing,	-10.3	-0.3	-0.1	1.1	-5.7	-2.8	0.0	1.9
Furnishing and household goods	1.8	4.6	1.1	0.7	-1.5	1.7	2.4	3.0
Health	4.2	2.0	2.5	-0.4	3.4	1.8	2.0	1.9
Transportation	9.1	3.2	2.4	-3.5	-8.7	-0.2	4.9	1.1
Communication	-0.1	-1.3	-1.3	-0.7	-1.4	0.1	-0.3	0.3
Education	1.8	2.4	-0.2	-1.2	1.0	-2.2	-1.3	-2.6
Information and Culture	5.5	-1.0	1.6	0.8	-0.2	1.5	2.9	1.9
Restaurants and Hotels	0.9	0.4	3.3	-1.5	0.0	2.3	-1.6	-1.0
Miscellaneous	1.2	2.8	0.1	3.3	1.0	2.6	3.3	2.2

Source: Central Statistics Office/Monetary Policy Department, DAB staff calculation.

1.2 Developments in Kabul CPI

1.2.1 Annual Developments

In the first quarter of 2016, Kabul headline inflation increased (Y-over-Y), which is the second consecutive quarter of rising inflation.

Higher inflation in Kabul is driven by higher inflation in both, food and non-food categories of the index, as the headline CPI turned around to an inflation rate of 4.4 percent compared to a deflation rate of 1.8

percent recorded in the first quarter of the previous year.

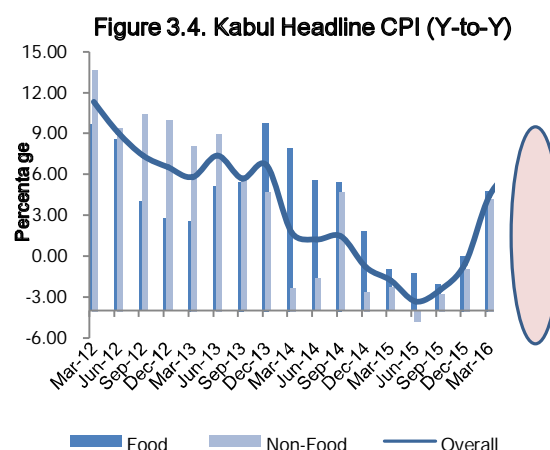
Food item, which accounts for around 52 percent of the whole CPI, exhibited higher inflation over a one year horizon. In the category, inflationary effects came from higher prices of bread and cereals, meat, milk, cheese and eggs, oils and fats, fresh and dried fruits, and sugar and sweets. As a result, food inflation increased to 4.8 percent from a deflation rate of 1.0 percent.

Non-food item which comprises around 48 percent of the whole index increased to 4.2

percent, while it was calculated -2.3 percent in the same quarter of the previous year. This increase is mainly resulted from higher price of clothing, housing, electricity, water and gas, furnishing and household goods, and transportation. In this item, the highest increase was seen in price of transportation rising by 8.2 percent in the first quarter of 2016 from -14.7 percent calculated a year ago.

Inflation when calculated based on core measures also increased. The 30% trimmed mean showed an inflation rate of 8.4 percent in March 2016, which is well higher the rate of 0.7 percent recorded in first quarter of 2015. Meanwhile, CPI excluding bread and cereals, oils and fats, and transportation

increased to an inflation rate of 6.2 percent from a deflation rate of 1.0 percent (Y-over-Y).



Source: Central Statistics Office/DAB staff calculation.

Table 3.3: Breakdown of Kabul Headline CPI

(Percent changes year-on-year)

(March 2011=100)

	Weight	1393				1394				1395
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Overall Index	100.0	1.8	1.2	1.2	-1.1	-1.8	-3.6	-2.5	-0.6	4.4
Food and beverages	52.0	7.9	5.5	5.4	1.8	-1.0	-1.3	-2.1	0.0	4.8
Bread and Cereals	17.7	7.7	4.8	6.6	3.0	-1.9	-2.9	-3.2	-0.7	1.1
Meat	7.2	-1.4	-1.4	3.8	2.6	0.5	1.1	0.7	4.3	8.7
Milk, cheese and eggs	4.8	6.1	9.9	8.7	5.9	2.7	6.1	8.5	7.1	8.1
Oils and fats	4.0	-0.9	-3.1	-5.1	-5.5	-12.6	-7.7	-7.5	-5.5	-3.1
Fresh and dried fruits	4.8	6.5	8.8	7.4	12.9	5.1	8.3	3.0	3.1	9.7
Vegetables	7.9	24.7	15.8	8.9	-5.6	-2.3	-10.2	-12.6	-11.5	-3.0
Sugar and sweets	2.9	-0.5	-6.9	-3.5	-5.1	-2.8	1.4	2.6	13.9	26.9
Spices	0.9	8.3	7.0	9.2	7.2	1.4	3.6	9.3	19.8	30.0
Non-alcoholic beverages	1.8	7.8	2.1	2.6	3.2	-0.8	3.0	5.3	9.5	11.6
Non-Food	48.0	-2.4	-1.7	-1.6	-3.1	-2.3	-5.2	-2.8	-0.9	4.2

Tobacco	0.4	11.2	13.3	11.5	15.5	12.9	9.1	22.6	20.1	20.8
Clothing	7.0	7.8	11.5	11.3	10.3	5.6	0.8	9.8	13.8	17.8
Housing, electricity, water and gas	20.7	-12.2	-13.2	-13.1	-13.4	-5.5	-9.7	-10.0	-9.6	-4.7
Furnishing and household goods	7.0	6.2	13.4	13.2	12.5	7.2	3.9	8.5	14.0	19.8
Health	3.3	7.8	7.3	8.7	4.1	4.1	3.5	0.2	0.3	1.7
Transportation	4.7	33.3	33.2	32.1	19.4	-14.7	-15.4	-7.4	-3.4	8.2
Communication	1.1	-0.8	-2.2	-4.0	-5.0	-5.7	-3.6	-1.6	-0.2	0.3
Education	0.7	-0.1	2.8	1.9	2.1	1.6	-3.8	-5.8	-7.3	-9.7
Information and Culture	0.1	14.0	14.6	19.1	18.3	1.8	5.6	6.8	9.8	11.7
Restaurants and Hotels	1.0	1.5	2.3	5.2	3.1	1.7	5.5	-0.6	0.0	2.2
Miscellaneous	1.8	4.3	7.9	3.8	5.0	4.5	8.3	17.8	17.9	19.1
Core inflation (28% TM)		5.3	5.7	6.2	4.4	0.7	1.2	1.9	4.7	8.4
Core inflation (Headline excl. B&C, O&F and T)		-1.3	-1.3	-3.8	-3.1	-1.0	-2.6	-1.7	-1.4	6.2

Source: Central Statistics Office/Monetary Policy Department, DAB staff calculation.

1.2.2 Quarterly Developments, Kabul CPI

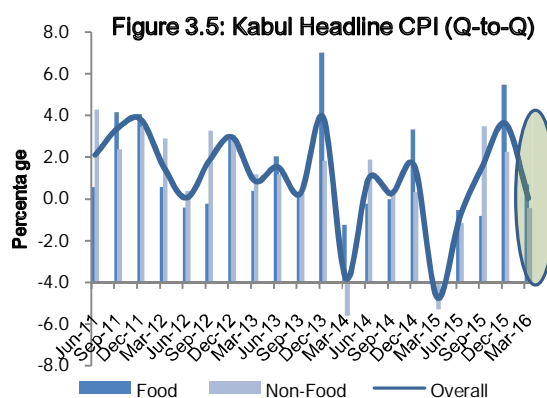
During the first quarter of 2016, the quarter-to-quarter measure of inflation in Kabul moved downward, which reflects lower inflation in both food and non-food items of the CPI. In March 2016, headline inflation lessened to 0.0 percent from 3.6 percent recorded in December 2015.

The trend of movement of food sub-index was descending as the rate of inflation in this category declined to 0.7 percent compared to 5.5 percent observed in the previous quarter. In this item, prices of bread and cereals, meat, milk, cheese and eggs, oils and fats,

vegetables, and sugar and sweets decreased, which had led to lower food inflation. However, vegetables price exhibited the largest decline of 5.9 percent from 19.8 percent. On the other hand, price of fresh and dried fruits increased by 8.9 percent compared to 2.4 percent.

Non-food category of the CPI also contributed to low inflation during the first quarter of 2016. Inflation in this item eased to -0.4 percent compared to 2.3 percent recorded in the previous quarter. The decline of non-food inflation is mainly driven by low prices of clothing, housing, electricity, water and gas, furnishing and household goods, and transportation among which the largest

decrease is seen in clothing. Price of this component declined by 1.2 percent from 6.4 percent (Q-to-Q). Unlikely, health price rose by 3.1 percent during May 2016, from -2.0 percent observed in December 2015.



Source: Central Statistics Organization/ DAB staff calculation.

Table 3.4: Quarter-on-Quarter Changes in Kabul Headline CPI

(Percent changes quarter-on-quarter)

(March 2001=100)

	1393				1394				1395
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Overall Index	-3.8	1.0	0.3	1.6	-4.7	-0.9	1.6	3.6	0.0
Food and beverages	-1.2	-0.2	0.0	3.3	-3.9	-0.5	-0.8	5.5	0.7
Bread and Cereals	-2.8	2.0	5.1	-1.1	-7.4	1.0	4.8	1.4	-5.8
Meat	-0.5	-2.5	4.4	1.3	-2.6	-1.9	3.9	4.9	1.5
Milk, cheese and eggs	2.0	-1.5	2.5	3.0	-1.1	1.7	4.7	1.6	-0.1
Oils and fats	-2.6	-1.6	-0.8	-0.6	-9.9	3.9	-0.5	1.5	-7.7
Fresh and dried fruits	9.9	5.1	-4.5	2.3	2.3	8.3	-9.2	2.4	8.9
Vegetables	-6.6	-3.9	-11.0	18.2	-3.4	-11.7	-13.4	19.8	5.9
Sugar and sweets	-5.2	-5.6	6.0	0.0	-3.0	-1.5	7.3	11.1	8.1
Spices	3.1	0.9	1.8	1.1	-2.4	3.2	7.4	10.8	5.8
Non-alcoholic beverages	2.0	-2.6	2.3	1.5	-2.0	1.2	4.6	5.5	-0.1
Non-Food	-5.6	1.9	0.5	0.3	-5.3	-1.1	3.5	2.3	-0.4
Tobacco	1.9	7.4	0.5	5.0	-0.4	3.8	12.9	2.8	0.2
Clothing	2.2	5.2	-0.1	2.6	-2.2	0.5	8.8	6.4	1.2
Housing	-14.0	0.1	-0.1	0.6	-6.9	-4.3	0.5	1.0	-1.9
Furnishing and household goods	1.4	8.2	1.3	1.3	-3.3	4.8	5.8	6.4	1.6
Health	1.6	0.8	3.7	-2.0	1.7	0.2	0.4	-2.0	3.1
Transportation	21.9	0.5	1.7	-4.1	-12.9	-0.4	11.4	0.0	-2.4
Communication	-0.1	-2.1	-1.9	-1.0	-0.8	0.1	0.1	0.4	-0.3
Education	1.0	2.0	0.1	-1.1	0.5	-3.3	-1.9	-2.8	-2.0
Information and Culture	14.0	-0.3	3.6	0.5	-1.9	3.4	4.8	3.2	-0.2
Restaurants and Hotels	1.5	0.8	2.9	-2.0	0.0	4.6	-3.1	-1.3	2.2
Miscellaneous	0.4	3.2	-1.9	3.3	-0.1	7.0	6.8	3.4	0.9

Source: Central Statistics Office/Monetary Policy Department, DAB staff calculations

II. NEAR TERM INFLATION OUTLOOK

The near-term outlook of inflation is likely to be upward. The central bank forecasts the inflation rate at around 4 percent by the end of June 2016, but it will be subject to a course of factors.

First, there are positive prospects about the future of oil price. Based on forecasts of the organization of petroleum exporting countries (OPEC), total demand for oil may increase in the second quarter of 2016, while the total supply may decline over the period. Higher global price of oil will not only increase the imports price in Afghanistan, but may also cause to higher price of domestically produced goods. Second; inflation in Afghanistan may receive intensive effects from low exchange rate. As the Afghani is not expected to appreciate against the U.S dollar, it may cause the inflation to continue its upward movement.

3.1 Risks

Forecasting inflation in Afghanistan depends on some medium and long-term risks. The most important is the risk to economic growth. Although, GDP growth projection is inclined toward upside, still there are some concerns about security situation, which give negative outlook for domestic consumption. In addition, negative shocks may come from inflation rate of neighboring countries. A continuous decline in the rate of inflation in this region may shade the national inflation in Afghanistan.



4

EXTERNAL SECTOR DEVELOPMENTS

4

EXTERNAL SECTOR DEVELOPMENTS

This chapter presents a brief analysis of the performance of the external sector of the Afghan economy for the first quarter of FY 1395. Also, this chapter highlights major developments in the external sector and compares them with developments recorded in preceding and corresponding quarters of previous year.

4.1: Balance of Payments

4.1.1 Current Account Balance

As shown in figure 4.1 the country's current account deficit in the first quarter of the FY 1395 increased significantly when compared with the same quarter of last year.

This was attributed largely to the decline in inflows in services and income account as well as decline in inward transfers especially home remittances.

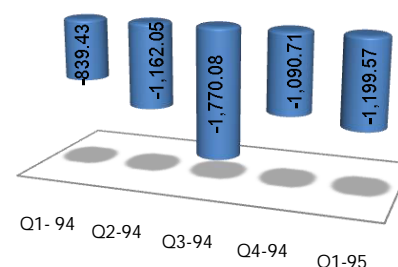
Trade deficit (trade in goods) rose slightly by 1 percent to USD 1,482.51 million in the first quarter of the FY 1395 in comparison to USD 1,500.51 million in the first quarter of the FY 1394.

Likewise; the deficit in the services account significantly increased by 87 percent to USD 191.42 million in the first quarter of the FY 1395 from USD 102.87 million in the corresponding quarter of previous year.

Similarly; in the income account turned from a surplus of USD 72.71 million in the first quarter of the FY 1394 to a deficit of USD 4.55 million in the period under review.

Also, current transfers' surplus which was largely influenced by grants and worker personal home remittances from foreign countries narrowed by 31 percent to USD 479.42 million in the first quarter of the FY 1395 from USD 691.16 million when compared with the similar quarter of the FY 1394 (Table 4.1 and figure 4.1).

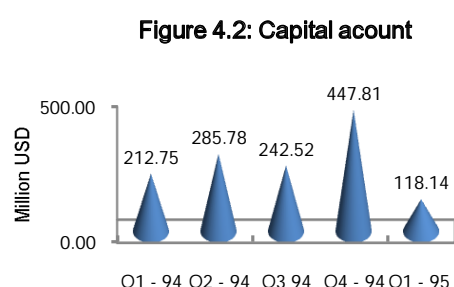
Figure 4.1: Balance of Payments Current Account (million USD)



Source: CSO/DAB staff calculations

4.1.2 Capital Account

The capital account of the balance of payments illustrated a decline of 44 percent in the first quarter of the FY 1395 when compared to the same quarter of the FY 1394 (Table 4.1, Figure 4.2) as a result of lower inward capital transfers. Net inflows in the capital account dropped to USD 118.14 million in the first quarter of the FY 1395 from USD 212.75 million recorded in the comparable quarter of the last year. This was mainly due to net capital transfers received by the government, corporations and households which reduced to USD 121.05 million in the first quarter of the FY 1395 from USD 219.37 million recorded in the preceding and corresponding quarter of the FY 1394.



Source: CSO/DAB staff calculations

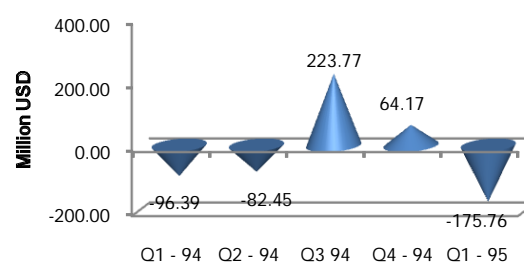
4.1.3 Financial Account

Financial account of the BOP recorded a net inflow of USD 175.76 million in the first quarter of the FY 1395 higher from a net inflow of USD 98.39 million recorded in the FY 1394 (Table 4.1 Figure 4.3). Further analysis reveals that

the country's aggregate financial assets abroad increased to USD 107.65 million in the first quarter of the FY1395 from USD 39.33 million recorded in the corresponding quarter of the FY 1394.

Similarly, aggregate financial liabilities decreased to USD 12.42 million in the first quarter of the FY 1395 from USD -10.13 million recorded in the same quarter of the previous year as a result of lower financial inflows occasioned by the insecurity challenges which affected both FDI and portfolio investments.

Figure 4.3: Financial account

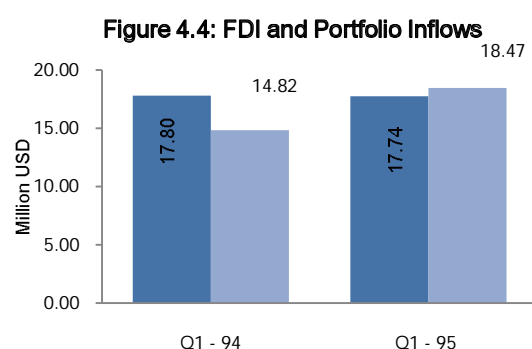


Source: CSO/DAB staff calculations

4.1.3 Foreign Direct Investment (FDI) and Portfolio Inflow

According to the available data, Portfolio Investment recorded an increase while Foreign Direct Investment (FDI) related inflows remained the same (USD 17.47) in the period under review. As shown in table (4.1 and figure 4.4) portfolio investment inflows increased to

USD 18.47 million in the first quarter of the FY 1395 from USD 14.82 million recorded in the first quarter of the FY 1394. The observed increase in portfolio investment in the quarter under review could be ascribed to the growing confidence in the economy during the period under review.



Source: CSO/DAB staff calculations

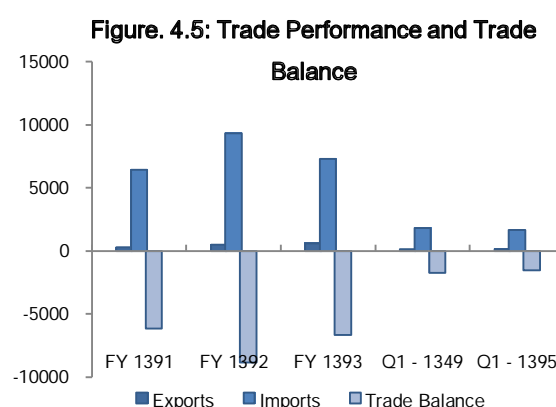
4.2 Merchandise Trade

Base on quarter on quarter comparison, available data revealed that Afghanistan trade balance improved in the first quarter of the FY 1395 (Table 4.2, Figure 4.5) following by a mild expansion in merchandise exports and a slight expansion in the merchandise imports.

Earnings from exports increased by 13 percent to USD 132.83 million in the first quarter of the FY 1395 from USD 117.24 million in the first quarter of the FY 1394 as a result of increasing food item such as fresh and dry fruits and medical seeds.

While, expenditure on total imports declined by 9 percent to USD 1,656.21 million in the first quarter of the FY 1395 from USD 1,828.16 million recorded in the first quarter of the FY 1394. This decline was mainly driven by lower imports of fuel and lubricants, industrial supply, and consumer goods.

As the growth of imports withered and export grew faster, consequently trade deficit declined to USD 1,523.38 million in the first quarter of the FY 1395 from USD 1,710.92 million recorded in the same quarter of the previous, down by almost 11 percent.

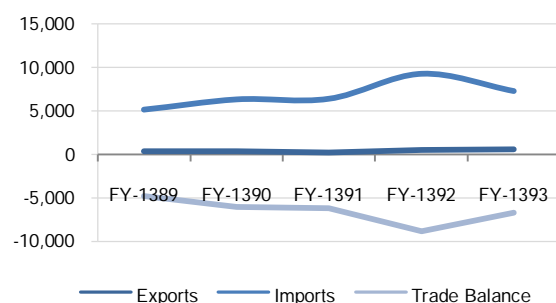


Source: CSO/DAB staff calculations

Table 4.1: Breakdown of Merchandise Trade (in million USD)

	Total 1390		Share (%)		Total 1391		Share (%)		Total 1392	
	Total 1390	Share (%)	Total 1391	Share (%)	Total 1392	Share (%)	Total 1393	Share (%)	Total 1394	Share (%)
Imports	6,388.37	100%	6,419.67	100%	9,339.60	100%	7,294.63	100%	7,679.09	100%
Industrial supplies	614.77	9.6%	969.88	15.1%	1272.14	13.6%	863.19	11.8%	709.19	9.2%
Fuel and Lubricants	2,184.59	34.2%	1,083.65	16.9%	2167.37	23.2%	1155.94	15.8%	1688.58	22.0%
Consumer goods	857.38	13.4%	1,255.48	19.6%	1942.85	20.8%	2345.86	32.2%	1715.25	22.3%
Capital goods and other	2,731.63	42.8%	3,110.66	48.5%	3,957	42.4%	2929.64	40.2%	3566.07	46.4%
Exports	375.03	100%	261.63	100.0%	499.81	100%	620.88	100%	555.71	100%
Carpets & Rugs	46.60	12%	8.43	3.2%	85.5	17.1%	87.04	14.0%	108.31	19.5%
Food Items	133.39	36%	104.23	39.8%	175.92	35.2%	272.13	43.8%	210.17	37.8%
Leather & Wool	28.07	7%	26.82	10.3%	59.54	11.9%	49.35	7.9%	28.47	5.1%
Medical seeds & others	166.97	45%	122.15	46.7%	178.86	35.8%	212.36	34.2%	208.76	37.6%
Trade Balance	-6,013.34		-6,158.04		-8,839.79		-6,673.75		-7,123.38	
Trade Balance as % of GDP	-33%		-31%		-43%		-31%		-33%	

Source: Central Statistics Organization and DAB staff calculations

Figure 4.6: Trade Performance & Trade Balance (million USD)

Source: Central Statistics Organization and DAB staff calculations

4.3 Direction of Trade

The main export destinations for Afghanistan are Pakistan, Iran, India, China, and Commonwealth of Independent States (CIS).

According to the merchandise trade statistics, during the first quarter of the FY 1395 Afghanistan's largest exports partner has been Pakistan. The share of Afghanistan's exports to Pakistan slightly declined to 32.64 percent from 34 percent.

In terms of value, exports to Pakistan grew by 9 percent to USD 43.35 million in the first quarter of the FY 1395 from USD 39.95 million in the first quarter of the FY 1394.

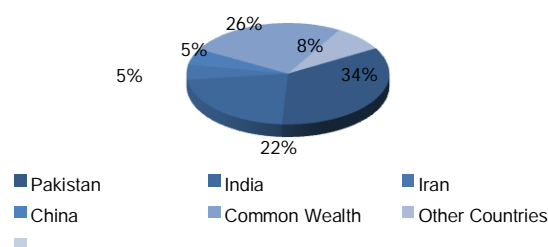
Commonwealth of Independent State (CIS) countries ranked the second largest buyer of Afghanistan's exports. The share of Afghanistan's exports to CIS countries rose to 24.21 percent in the first quarter of the FY 1395 from 16 percent that was recorded in the corresponding quarter of the last year.

In terms of value Afghanistan's total exports to CIS countries increased by 73 percent to a value of USD 32.16 million in the first quarter of the FY 1395 compared to a value of USD 18.54 million in the first quarter of the FY 1394.

India was the third largest buyer of Afghanistan's exports in the first quarter of the FY 1395. The share of exports to India declined to 21.06 percent from 33.29 percent recorded in the first quarter of the FY 1394.

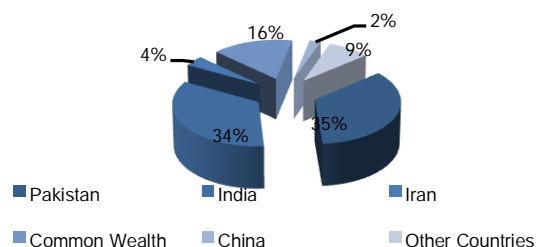
In terms of value, exports to India decreased by 28 percent from USD 39.03 million in the first quarter of the FY 1394 to USD 27.97 million in the

**Figure 4.7: Direction of Exports
(% share) in the Q1 - FY 1395**



Source: Central Statistics Organization and DAB staff calculations

**Figure. 4.8: Direction of Exports
(% share) in the Q1 - FY 1394**



Source: Central Statistics Organization and DAB staff calculations

CIS countries were the largest source of imports for Afghanistan during the first quarter

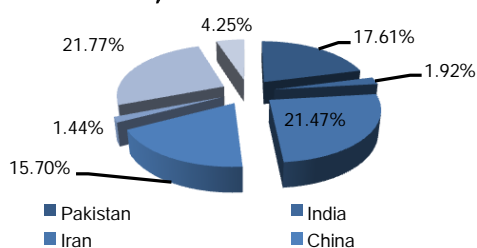
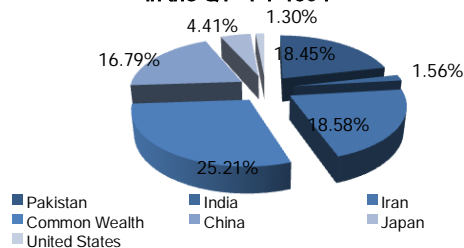
of the FY 1395. Total Imports from CIS countries decreased by 22 percent from USD 460.80 million with share of 25.21 percent in the first quarter of the FY 1394 to USD 360.50 million with share of 21.77 percent in the reporting period.

Iran was the second largest origin of imports for Afghanistan in the first quarter of the FY 1395. Total Imports from Iran increased to USD 355.53 from USD 339.75 million, its share in total imports also increased from 18.58 percent to 21.47 percent.

Pakistan was the third largest import sourcing country to Afghanistan in the first quarter of the FY 1395. The share of imports from Pakistan in total imports declined from 18.45 percent in the first quarter of the FY 1394 to 17.61 percent in the reviewed quarter. In terms of value, the total imports from Pakistan also decline to USD 291.68 million in the first quarter of the FY 1395 from USD 337.30 million in the similar quarter of preceding year, registering 14 percent reduction.

China was the fourth largest import origin to Afghanistan in the first quarter of the FY 1395. Total Imports from China decreased to USD 259.96 million with share of 14.70 percent from USD 306.98 million with share of 16.79 percent, registered 15 percent reduction in the first quarter of the FY 1395.

Japan, India and USA were the fifth, sixth and seventh largest import sourcing countries for Afghanistan, accountable for 4.25 percent, 1.92 percent and 1.44 percent of total imports respectively.

Figure 4.9: Direction of Imports (% share) in the Q1 - FY 1395**Figure 4.10: Direction of Imports (%share) in the Q1 - FY 1394**

Source: CSO and DAB staff calculations Source: Central Statistics

Organization and DAB staff calculations

Table 4.2: Direction of External Trade: FY1394 (in million USD)

	Exports	% Shares	Imports	% Share	Trade Balance
Pakistan	223.36	40.19%	1391.99	18.13%	-1168.63
India	169.08	30.43%	127.25	1.66%	41.83
Iran	29.57	5.32%	1742.18	22.69%	-1712.61
Germany	6.87	1.24%	33.09	0.43%	-26.22
China	11.66	2.10%	1,090.92	14.21%	-1079.26
England		0.00%	5.41	0.07%	-5.41
Saudi Arabia	0.25	0.04%		0.00%	0.25
USA		0.00%	244.54	3.18%	-244.54
Common Wealth of Independence States (CIS)	44.13	7.94%	1581.00	20.59%	-1536.87
Japan		0.00%	302.27	3.94%	-302.27
Other Countries	70.79	12.74%	1160.47	15.11%	-1089.68
Total	555.71	100%	7,679.12	100%	(7,123.41)

Source: CSO and DAB staff calculations

Table 4.3: Direction of External Trade: FY1393 (In million USD)

Country Name	Exports	% Shares	Imports	% Share	Trade Balance
Pakistan	212.61	34.24%	1360.89	18.66%	-1148.28
India	153.05	24.65%	117.32	1.61%	35.73
Iran	40.89	6.59%	1424.21	19.52%	-1383.32
Germany	18.56	2.99%	76.47	1.05%	-57.91
Common Wealth	30.22	4.87%	1739.20	23.84%	-1708.98
China	31.32	5.04%	824.13	11.30%	-792.81
Saudi Arabia	0.43	0.07%		0.00%	0.43
Japan		0.00%	216.27	2.96%	-216.27
England		0.00%	5.73	0.08%	-5.73
United States		0.00%	78.13	1.07%	-78.13
Other Countries	133.80	21.55%	1452.31	19.91%	-1318.51
Total	620.88	100.00%	7294.66	100.00%	-6673.78

Source: Central Statistics Organization and DAB staff calculations

4.4 Composition of Trade

The composition of imports in the first quarter of the FY 1395 indicates that;

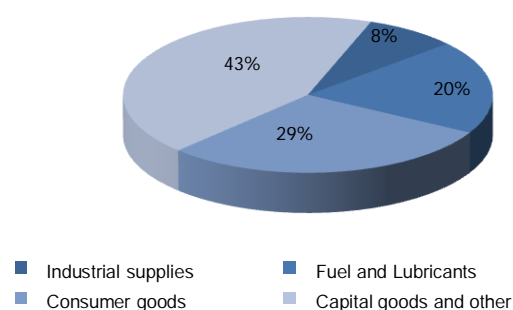
- ✓ Imports of Capital goods had the largest share of 47.2 percent in the basket of imports. But in terms of value imports of such goods slightly declined by 1 percent to USD 781.56 million in the first quarter of the FY 1395 from USD 789.85 million recorded in the same quarter of the previous year.
- ✓ The second largest share recorded for consumer goods in the basket of imports during the first quarter of the FY 1395, although its share dropped from 29.3 to 28.1 percent in the reporting quarter. In terms of value imports of such goods also declined by 13 percent to USD 465.54 million in the first quarter of the FY 1395 from USD 535.45 million recorded in the first quarter of the FY 1394.
- ✓ Fuel and lubricants (petroleum oil) imports had the third largest share in the basket of Afghanistan's imports which is slightly declined from 19.5 to 17 percent in the reporting quarter. In terms of value, imports of such goods in total imports significantly decreased by 20 percent to USD 284.96 million in the first quarter of the FY 1395 from USD 356.15 million in the first quarter of the FY 1394.
- ✓ Industrial supplies had the smallest share in the basket of Afghanistan's imports during

the reporting quarter, its share in total imports, however, declined to 7.5 percent in the first quarter of the FY 1395 from 8 percent recorded in the first quarter of the FY 1394.

In terms of value imports of such goods also declined by 15 percent, to USD 124.42 million in the first quarter of the FY 1395 from USD 146.71 million in the first quarter of the FY 1394.

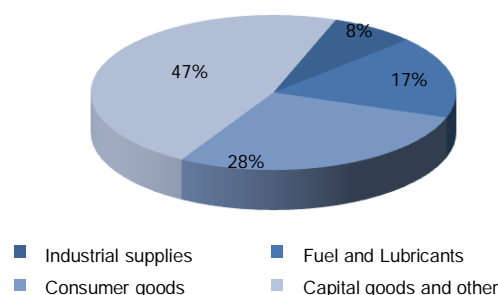
Industrial supplies, which comprised metals, fertilizer, chemical, and cement, posted a decline due to the reduction in the number of development projects all over the country as a result of political and security uncertainties (Table 4.3- 4.4 and Figure 4.9 - 4.10).

Figure 4.11: Composition of Imports (share%) in the first quarter of FY 1394



Source: Central Statistics Office and DAB staff calculations

**Figure 4.12: Composition of Imports
(share%) in the first quarter of FY 1395**



Source: Central Statistics Office and DAB staff calculations

3.2: Composition of exports

The composition of exports in the first quarter of the FY 1394 reveals that;

- ✓ Exports of food item had the largest share in the basket of Afghanistan's exports. In the first quarter of fiscal year 1395 the share of food items increased to 51.4 percent from 30.9 percent recorded in the corresponding quarter of the FY 1394.

Earnings from exports of food items (oil seeds, fresh and dry fruits) significantly increased by 89 percent to USD 68.27 million in the first quarter of the FY 1395 from USD 36.17 million in the same quarter of the previous year.

- ✓ The second largest share in total exports was recorded for medical seeds, even though, its shares decreased to 30.9 percent in the first quarter of the FY 1395 from 32.3 percent recorded in the corresponding quarter of last the year. However, in term of value exports of medical seeds increased by

8 percent to USD 41.09 million in the first quarter of the FY 1395 from USD 37.92 million which recorded in the preceding and corresponding of the FY 1394.

- ✓ Carpets and rugs, which are considered the main exports of Afghanistan in the past decade, had the third largest share in total exports. Its share, however, declined to 2.2 percent in the first quarter of the FY 1395 from 4.5 percent in the first quarter of FY 1394.

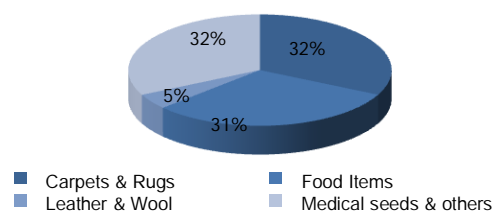
Earnings from exports of carpet and rugs also declined by 46 percent (USD 20.55 million) during the quarter under review.

- ✓ The share of leather and wool was smallest in the basket of Afghanistan's exports, which declined from 4.5 percent to 2.2 percent during the quarter under review.

Earnings from exports of leather and wool dropped to USD 2.92 million in the first quarter of the FY 1395 from USD 5.28 million recorded in the similar quarter of the last year.

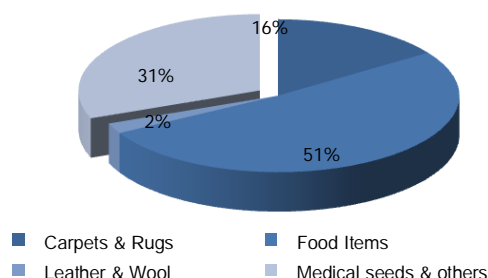
(Figure 4.11 and 4.12) indicated composition of exports in the Q1 FY 1394 with Q1 FY 1395.

**Figure 4.13: Composition of Exports
(share%) in the first quarter of FY 1395**



Source: Central Statistics Organization/DAB staff calculation

Figure 4.14: Composition of Exports (share%) in the first quarter of FY 1394



Source: Central Statistics Organization/DAB staff calculation

4.5 External Debt

As shown in table 4.5 and figure 4.13 Afghanistan's total external debt slightly decreased by almost 2.2 percent to USD 2,136.95 million in the first quarter of the FY 1395 from USD 2,184.24 million similar quarter of the FY 1394, which shows about USD 47.28 million declines. The decline in total external debt could be attributed to long-term components, like the external commercial loan payment, narrowing NIR deposits and Special Drawing Rights (SDR) allocated by the International Monetary Fund (IMF).

During the period under review, loan principal repayments made to the Asian Development Bank, and International Monetary Fund (IMF),

while service charges were paid to the World Bank and OPEC Fund.

Meanwhile, World Bank, major multilateral creditor to Afghanistan, made some debt forgiveness on principle and services charge during the quarter under review.

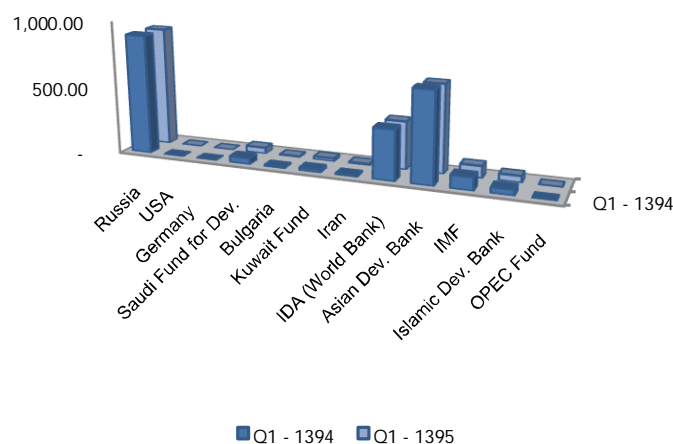
The total loan amounts payable to the Paris Club creditors in the first quarter of the FY 1395 stood at USD 898.31 million which is payable to Russian federation.

In other words, Afghanistan's total debt from the Paris club members stands at about 42 percent of total current external debt. It is worth mentioning that Afghanistan's total loan has decreased slightly by about 1 percent compared to the preceding year.

Furthermore, total debt from Non-Paris Club members which include, (Saudi Fund for Development, Bulgaria, Kuwait fund and Iran) decreased by 3 percent to USD 84.85 million in the first quarter of the FY 139 in comparison with USD 87.86 million recorded in the first quarter of the FY 1394.

On the other hand, total debt from multilateral creditors to Afghanistan decreased to USD 1,152.03 million from USD 1,197.82 million which shows USD 44.3 million reduction in the total debt during the reporting quarter.

**Figure 4.15: External Debt Comparisons;
Q3 -1393 & Q3-1394**



Source: Debt Asset Management Unit, Ministry of Finance

Table 4.4: Breakdown of External Debt for the FY 2014 (in units indicated)

	In million USD	Percent of total
Total external debt	2,139.77	100.00
Bilateral	983.63	45.97
Paris Club	898.84	42.01
Russian Federation	898.84	42.01
United States	-	0.00
Germany	-	0.00
Non-Paris Club	84.79	3.96
Multilateral	1,156.14	54.03
of which: IDA (World Bank)	357.99	16.73
Asian Development Bank	655.33	30.63
International Monetary Fund	92.41	4.32
Islamic Development Bank	48.62	2.27
OPEC Fund	1.79	0.08

Source: Debt, Asset Management Unit, Ministry of Finance, Afghanistan

4.6 Net International Reserves

According to the latest available data the Net International Reserves (NIR), decreased by 3.72 percent, standing at USD 6,548.43 million in the first quarter of the FY 1395, down from

USD 6801.45 million in the corresponding quarter of the previous year (Table 4.7 and Figure 4.14).

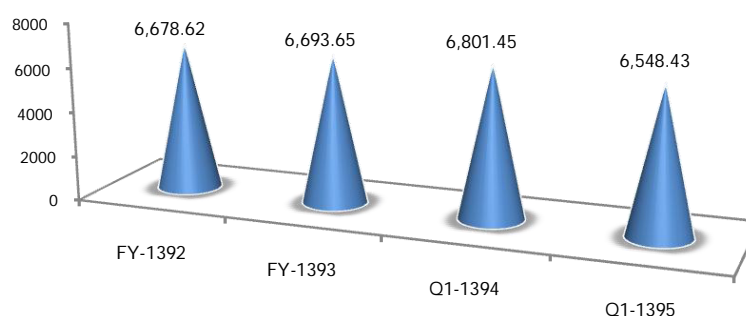
The decrease in the level of NIR was mainly due to the decline in the reserve assets which narrowed by 3.56 percent to USD 7,082.60 million in the first quarter of the FY 1395 from USD 7,343.73 million in the corresponding quarter of last year.

Likewise, reserve liabilities recorded a mild contraction of 1.50 percent, standing at USD 534.17 million in the first quarter of the FY 1395, up from USD 542.29 million recorded in the first quarter of the FY 1394.. The reduction in reserve liabilities is mainly attributed to the use of fund resources which declined by almost 10 percent to USD 81.43 million in the first quarter of the FY 1395 from USD 10169 million recorded in the same quarter of the previous year. This reduction in reserve liabilities is also

attributed to the commercial banks deposits in foreign currency which declined by 2.30 percent to USD 433.57 million in the first quarter of the FY 1395 from USD 443.80 million in the same quarter of the previous year.

Currently, Net International Reserves (NIR) on average supports almost 12 months of imports which is considered to be a very comfortable reserve position. The decline in the Net International Reserves (NIR) could be attributed to significant outflows of foreign exchange in the form of foreign and personal remittances. The current position of Afghanistan Net International Reserves (NIR) is providing a good cushion of the capacity of monetary policy and support of balance of payments.

Figure 4.16: Net International Reserves during the past period (In Million USD)



Source: Monetary Policy Department/DAB

Table 4.5: Merchandise Trade in (Million USD)

Years	FY 1391		FY 1392		FY 1393		Q1 - 1349		Q1 - 1395	
	Total	Share (%)	Total	Share (%)	Total	Share (%)	Total	Share (%)	Total	Share (%)
Imports	6,419.67	100%	9,339.60	100%	7,294.63	100%	1,828.16	100%	1,656.21	100%
Industrial supplies	969.88	15.1%	1,272.14	13.6%	863.19	11.8%	146.71	8.0%	124.42	7.5%
Fuel and Lubricants	1,083.65	16.9%	2,167.37	23.2%	1155.94	15.8%	356.15	19.5%	284.69	17.2%
Consumer goods	1,255.48	19.6%	1,942.85	20.8%	2345.86	32.2%	535.45	29.3%	465.54	28.1%
Capital goods and other	3,110.66	48.5%	3,957.24	42.4%	2,930	40.2%	789.85	43.2%	781.56	47.2%
Exports	261.63	100%	499.81	100.0%	620.88	100%	117.24	100%	132.83	100%
Carpets & Rugs	8.43	3%	85.49	17.1%	87.0	14.0%	37.87	32.3%	20.55	15.5%
Food Items	104.23	40%	175.92	35.2%	272.13	43.8%	36.17	30.9%	68.27	51.4%
Leather & Wool	26.82	10%	59.54	11.9%	49.35	7.9%	5.28	4.5%	2.92	2.2%
Medical seeds & others	122.15	47%	178.86	35.8%	212.36	34.2%	37.92	32.3%	41.09	30.9%
Trade Balance	-6,158.04		-8,839.79		-6,673.75		-1,710.92		-1,523.38	
Trade Balance as % of GDP	-31%		-43%		-31%		-8%		-7%	

Source: Monetary Policy Department/DAB

Table 4.6: Afghanistan Balance of Payments in (Million USD)

Items / Years	Q1- 1394	Q2-1394	Q3-1394	Q4-1394	Q1-1395
Current Account	-839.43	-1162.05	-1770.08	-1090.71	-1199.57
Credit	1218.61	1032.72	968.10	788.23	779.77
Debit	-2058.04	-2194.78	-2738.18	-1878.95	-1979.35
Goods Account	-1500.51	-1625.15	-2042.63	-1288.93	-1482.51
Credit	128.89	121.96	162.90	166.24	133.63
Debit	-1629.41	-1747.10	-2205.53	-1455.17	-1616.14
Services Account	-102.78	-202.17	-200.43	-223.85	-191.94
Credit	263.84	190.36	278.96	133.28	121.31
Debit	-366.62	-392.54	-479.38	-357.13	-313.26
Income Account	72.71	48.19	37.34	21.72	-4.55
Credit	107.12	68.88	63.58	47.40	15.07
Debit	-34.41	-20.69	-26.24	-25.68	-19.62
Current transfers	691.16	617.08	435.63	400.34	479.42
Credit	718.76	651.52	462.66	441.30	509.76
Debit	-27.60	-34.45	-27.03	-40.96	-30.34
Capital and financial account	116.36	203.33	466.29	511.98	-57.62
Capital account	212.75	285.78	242.52	447.81	118.14
Credit	220.30	299.31	252.90	448.21	121.05
Debit	-7.56	-13.52	-10.38	-0.41	-2.91
Capital transfers	219.37	296.42	251.85	447.81	121.05
Credit	220.30	298.98	252.85	448.21	121.05
Debit	-0.93	-2.55	-0.99	-0.41	0.00
Financial account	-96.39	-82.45	223.77	64.17	-175.76
Direct investment	17.80	33.18	77.98	40.20	17.74
Portfolio investment	-14.82	-36.55	-15.83	-14.31	-18.47
Assets	-14.82	-36.55	-15.83	-14.31	-18.47
Liabilities	0.00	0.00	0.00	0.00	0.00
Other investment	44.01	-33.11	-80.40	-26.37	-76.76
Assets	54.15	-20.13	-96.84	-8.38	-89.19
Liabilities	-10.13	-12.98	16.44	-17.99	12.42
Reserve Assets	-143.37	-45.97	242.02	64.65	-98.27
Net errors and omissions	-723.07	-958.72	-1303.79	-578.74	-1257.20
Overall Balance					

Table 4.7: Direction of External Trade : for the first quarter of the FY 1394 in (Million USD)

Country Name	Exports	% Shares	Imports	% Share	Trade Balance
Pakistan	39.95	34.08%	337.30	18.45%	-297.35
India	39.03	33.29%	28.47	1.56%	10.56
Iran	4.53	3.86%	339.75	18.58%	-335.22
Germany	2.83	2.41%	9.94	0.54%	-7.11
Common Wealth	18.54	15.81%	460.80	25.21%	-442.26
China	2.57	2.19%	306.98	16.79%	-304.41
Saudi Arabia	0.12	0.10%		0.00%	0.12
Japan		0.00%	80.66	4.41%	-80.66
England		0.00%	1.60	0.09%	-1.60
United States		0.00%	23.85	1.30%	-23.85
Other Countries	9.67	8.25%	238.83	13.06%	-229.16
Total	117.24	100.00%	1828.18	100.00%	-1710.94

*Source: Monetary Policy Department/DAB***Table 4.8: Direction of External Trade: for the first quarter of the FY 1395 in (Million USD)**

Country Name	Exports	% Shares	Imports	% Share	Trade Balance
Pakistan	43.35	32.64%	291.68	17.61%	-248.33
India	27.97	21.06%	31.76	1.92%	-3.79
Iran	6.08	4.58%	355.53	21.47%	-349.45
Germany	1.56	1.17%	7.80	0.47%	-6.24
China	6.49	4.89%	259.96	15.70%	-253.47
England		0.00%	3.93	0.24%	-3.93
Saudi Arabia	4.83	3.64%		0.00%	4.83
USA		0.00%	23.93	1.44%	-23.93
Common Wealth	32.16	24.21%	360.50	21.77%	-328.34
Japan		0.00%	70.37	4.25%	-70.37
Other Countries	10.39	7.82%	250.78	15.14%	
Total	132.83	100%	1,656.24	100%	(1,523.41)

Source: Monetary Policy Department/DAB

Table 4.9: Net International Reserves, for the FY 1394 (million of USD)

Changes in the previous quarter	FY 1391	% change	FY 1392	% change	FY 1393	% change	FY 1394	% change
Net International Reserves (million USD)	6,471.94	23.22	6,678.62	3.19	6,693.65	0.22	6,443.00	-3.74
Reserve Assets	6,866.79	22.71	7,183.33	4.61	7,247.76	0.90	6,965.81	-3.89
Reserve Liabilities	394.85	10.91	504.71	27.82	554.12	9.79	522.80	-5.65
Commercial bank deposits in foreign currency	245.00	4.00	367.65	50.06	443.80	20.71	433.57	-2.30
Non-resident deposits in foreign currency	0.11	-89.57	0.14	23.87	0.14	-0.02	0.14	0.00
Use of Fund resources	149.73	17.53	136.92	-8.56	110.18	-19.53	89.10	-19.14
Gross Intl. Reserves (in months of import)	12.84		9.23		11.92289856		10.88536	
Net Intl. Reserves (in months of import)	12.10		9		11		10	

Source: Monetary Policy Department/DAB



FISCAL SECTOR DEVELOPMENTS

5

FISCAL DEVELOPMENTS

During the first quarter of FY 2016, the overall performance in the public sector was sluggish due to deferment in budget approval by the parliament that also caused donors to lower their contribution. Furthermore, Afghanistan's public expenditure remained unbalanced during FY 2016, owing to continued deterioration in security conditions which undermined private investment, delayed budget execution, and capital flight. These factors coupled with pick-ups in operating expenditure posed serious challenges for the government to achieve fiscal sustainability.

5.1 Budget Execution Rate

During the first three months of FY 2016, from the allocated budget the government's total execution rate was only 10.59 percent, compared to 10 percent in the previous year. The execution rate of current budget was 15 percent comparing to 13 percent in FY 2015. Meanwhile, execution rate of development expenditure was only 3.50 percent, compared to 3 percent of execution rate the same quarter

last year. Comparing to the first quarter FY 2015, execution is presenting a slight increase. The lower execution rate of the core budget was attributed to several factors, and most importantly due to suspension of budget approval and deterioration in security condition in provinces and reduction in donors' funds.

5.2 Budget Deficit

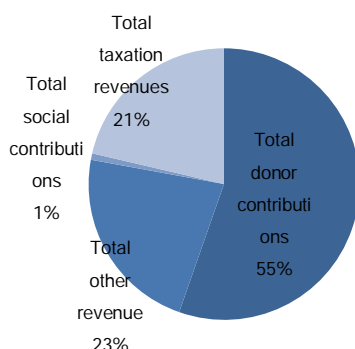
The overall budget prior to donor's contribution had a deficit in the first quarter of FY 2016 increased to AF 16.45 billion. However, budget presented surplus including donor grants standing at AF 23.74 billion.

5.3 Revenue Collection

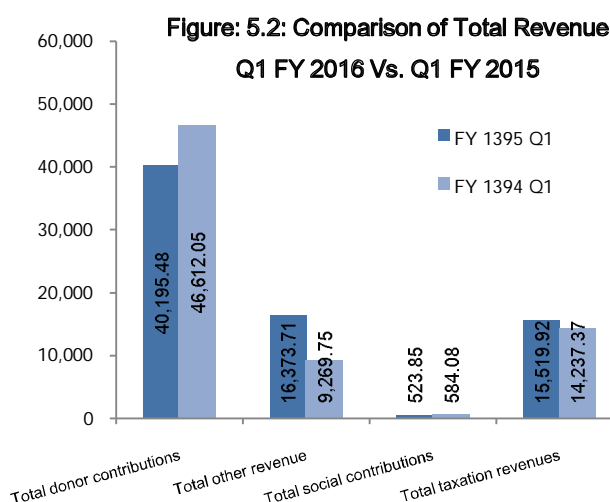
Domestic revenue collected in the first quarter of FY 2016 indicates a significant increase of 35 percent catapulting the total collection to AF32.42 billion, compared to AF 24.09 billion FY 2015.

The positive momentum gained in the first quarter was result of reforms undertaken in the revenue collection system and in customs and revenue administration.

Figure 5.1: Composition of Total Revenue FY 1395 First Quarter



Source: Ministry of Finance/MPD calculation



Source: Ministry of Finance/MPD calculation

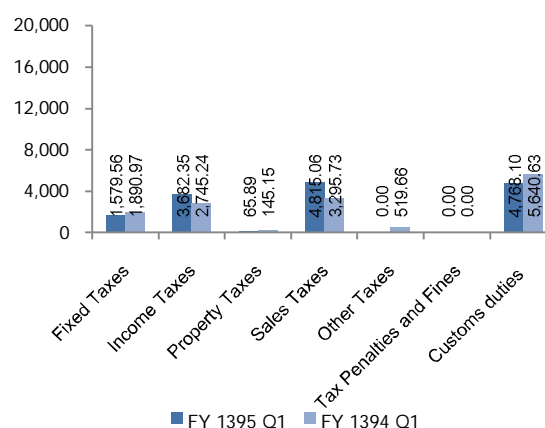
5.3.1 Tax Revenue

Total tax collections showed growth for the quarter under review, in accordance to receipts, overall tax revenue increased from AF 14.24 billion to AF 15.52, compared to the same

quarter of the FY 2015, which represents an increment of 9 percent or AF 1.28 billion.

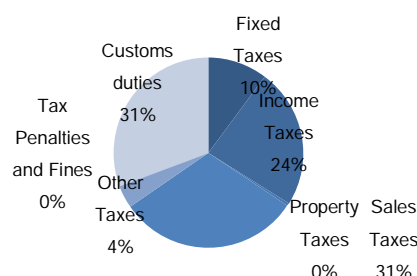
On the contrary total tax collection from the custom duties presented 15 percent decline, plummeting from a total of AF 5.64 billion to AF 4.77 billion in FY 2015.

Figure 5.3: Comparison of Tax Revenue



Source: Ministry of Finance/MPD calculation

Figure 5.4: Composition of Tax Revenue



Source: Ministry of Finance/MPD calculation

5.3.2 Non-tax Revenues

The main contributor in domestic revenues was non-tax revenues which presented a significant increase of 77 percent reaching AF 16.37 billion, compared to AF 9.27 billion same quarter of the previous year. The momentous increase was mainly due to high performance in administrative fee and miscellaneous revenues. On the other hand, Extractive industry, a major component of the non-tax revenue, underperformed compared to the first quarter FY 2015, and was ended at AF 0.03 billion, down from AF 0.14 billion same quarter FY 2015, demonstrating 79 percent of decline.

Social contribution that constitutes only 2 percent of the total domestic revenue presented a decline of 10 percent. The total amount collected were AF 0.52 billion, down from AF 0.58 billion in FY 2015.

5.4 Grants

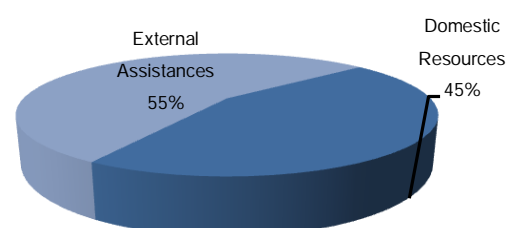
Afghan government receives grants from various donors, trusts and international committees to finance varieties of programs in both operating and development expenditures. Integrated grants presented a slight decline in FY 2016, compared to FY 2015.

Total development and operating grants in the first quarter of FY 2016 amounted to AF 40.20 billion down from AF 46.61 billion in FY 2015, screening 14 percent decrease. Nonetheless, grants received under the ARTF program over the FY 2016 was AF 7.64 billion that represents

83 percent increase over the same period of the previous FY 2015. On the contrary, grants received from LOTFA scheme decreased to AF 6.87 billion in the quarter under review compared to AF 7.14 billion in the same quarter FY 2015, witnessing a slight decrease of 4 percent.

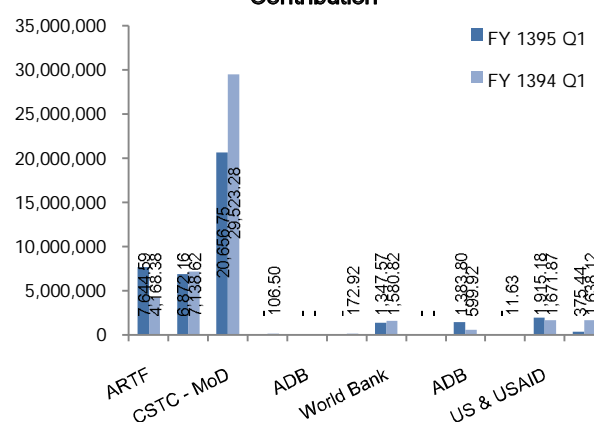
Domestic revenue could finance 45 percent of the total core budget and 55 percent is financed through external grants.

Figure 5.5: Financing Sources of National Budget Quarter 1, FY 1395



Source: Ministry of Finance/MPD calculation

Figure 5.6: Comparison of Donors Contribution



Source: Ministry of Finance/MPD calculation

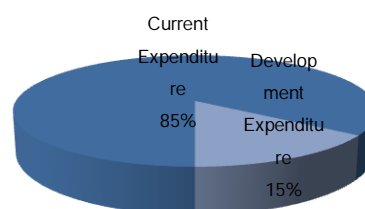
5.5 Expenditure

Total expenditure for the quarter under review were AF 48.88 billion that indicates the augmentation of 10 percent over the total spending of AF 44.26 billion in the same period previous year.

The current expenditure increased to AF 41.42 billion during the first quarter of FY 2016, rose from AF 36.98 billion showing 12 percent supplement.

Similarly, development expenditure enlarged to AF 7.46 billion from sum of AF 7.28 billion indicating a slight raise of 2 percent.

Figure 5.7: Composition of Total Government Expenditure Quarter 1, FY 1395



Source: Ministry of Finance/MPD calculation



6

BANKING SYSTEM PERFORMANCE

6

BANKING SYSTEM PERFORMANCE

Asset base of the banking sector decreased by 0.57 percent or AF 1.55 billion during the first quarter of 2016

as compared to 3.45 percent increase in the previous quarter ending Dec, 2015. The decrease in banking system assets over the quarter under review is mainly due to a decrease in deposit base.

Gross loans portfolio of the banking sector witnessed a decrease of 0.63 percent or AF 289 million over the last quarter against 4.55 percent increase in the quarter ending Dec, 2015. The decrease in the loan portfolio over the quarter is mainly attributed to less customer utilization of OD loans.

Deposits, the main funding source in the banking sector which comprises 95.66 percent of the total liabilities of the sector, stood at AF 231.05 billion, indicating a decrease of 2.51 percent against 8.46 percent increase in the previous quarter (ending Dec, 2015). The decrease in total deposit base of the banking sector is attributed to withdrawals from the Afghani denominated demand deposits. AF-denominated deposits indicated decrease of 9.28 percent compared to 0.96 percent

increase in the previous quarter while USD denominated deposits was down by 0.43 percent against 11.44 percent increase in Dec, 2015.

The capital base of the banking sector, increased by 12.85 percent standing at AF 27.84 billion over the period under review. The increase in total financial capital over the last quarter is attributed to profits made during the quarter.

Capital adequacy ratio (CAR) of the banking sector stands at 21.14 percent. Most of the banking institutions are above the set limits for CAR, but two banking institutions are very close to the limit and one bank ratio is negative.

Banking sector earned a net profit amounting to AF 2.93 billion over the quarter under review, against AF 817 million of net profit in the previous quarters having a significant increase in Return on Assets (ROA) and return on equity (ROE) of the banking sector over the first quarter of 2016. Return on Assets (ROA) increased to 4.35 percent showing an increase of around 4 percentage points compared to 0.31 percent in Dec, 2015 and return on equity (ROE)

ratio improved significantly, compared to 2.55 percent in December, 2015, reaching to 43.74 percent.

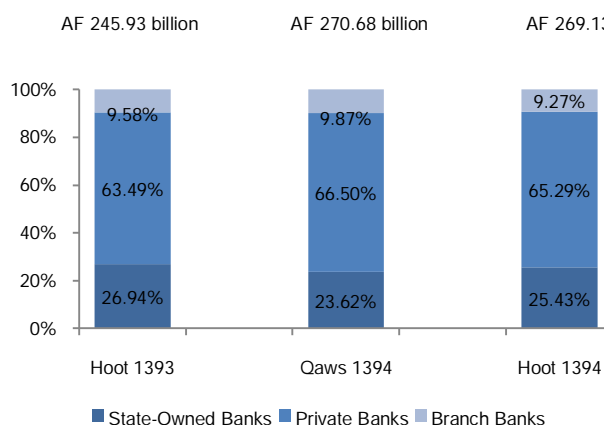
I. Assets of the Banking System

The assets size of the banking sector declined by 0.57 percent in the quarter under analysis against 3.45 percent increase in Dec, 2015. See figure 6.1.

The breakup of total assets reveals that the most obvious increase was registered in all other assets category of total assets increasing by AF 5.12 billion (56.37 percent) followed by interbank claims increased by AF 4.58 billion (5.85 percent) and investments increased by AF 966 million (5.13 percent), while cash in vault and claims on DAB, net-loans and fixed assets showed decrease of AF 11.01 billion (9.49 percent), AF 760 million (1.84 percent) and AF 4456 million (6.20 percent) respectively during the reviewed quarter.

The most important components of the system's total asset portfolio were cash in vault/claims on DAB (39.00 percent), interbank claims (30.78 percent), net loans (15.02 percent), investments (7.35 Percent), "other assets" (5.26 percent) and fixed assets make 2.56 percent of the total assets. See table 6.1.

**Figure 6.1: Share of Banking Sector
(Total assets)**



Source: Financial Supervision Department, DAB

Table 6.1: Composition of Assets and Liabilities

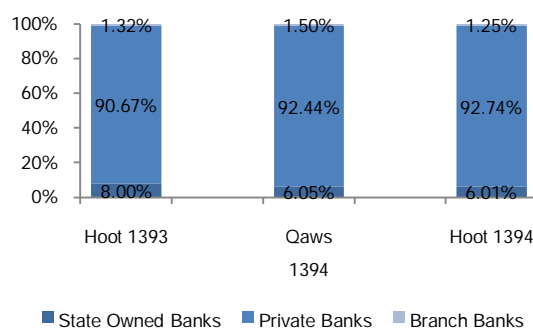
Amount in million AF	Qaws, 1394 Dec, 2015		Hoot, 1394 Mar, 2016	% of Total Assets/Liability	Q-o-Q Growth
Assets					
Cash in vault and claims on DAB	115,984	104,970	39.00	-9.49	115,984
Interbank claims	78,262	82,846	30.78	5.85	78,262
Investments	18,815	19,781	7.35	5.13	18,815
Loans (Net)	41,186	40,426	15.02	-1.84	41,186
Fixed Assets	7,352	6,896	2.56	-6.2	7,352
Others	9,090	14,214	5.28	56.37	9,090
Total	270,689	269,133		-0.57	270,689
Liabilities					
Deposits	237,002	231,054	95.66	-2.51	237,002
Borrowings	4,452	3,694	1.53	-17.02	4,452
Other	4,561	6,798	2.81	49.04	4,561
Total	246,015	241,546		-1.81	246,015
Financial Capital	24,673	27,845		12.85	24,673

Source: Financial Supervision Department, DAB

1.1 Gross Loans

Total gross loans indicated AF289 billion or 0.63 percent decreasesince last year, constituting 16.76 percent of the total assets. Thedecrease in total loan portfolio is mainly attributed to less utilization of OD by customers (Overdraft loans). Out of fourteen banking institution, six banks experienced some Increases in their loan portfolio whereas the remaining eight banksobserved a decrease intheir loan portfolio. While the remaining one bank (NKB) did not participate in lending;

Figure 6.2: Share of the Gross Loans Portfolio among banking group



Source: Financial Supervision Department, DAB

Gross loan portfolio showed a decrease across the banking groups. Private Banks with 92.74percent share in total portfolio posted 0.31 percent or AF 131million of reduction, State-owned banks with 6.01 percent share depicted 1.34 percent or AF 37million decrease and Branches of foreign banks holding 1.24 percent of the portfolio was downby17.59 percent or AF 120 million during the quarter under review By the end of Dec.2015 (Qaws 1394), total provision cover of the system was 9.29percent of total gross loans in comparison with 7.21 percent in the previous year ending Dec. 2014.

7.1.1 Loan Loss Reserves

By the end of Mar, 2016 (Hoot 1394), total provision cover of the system was 10.40percent of total gross loans as opposed to9.29 percent recorded in the previous year ending Dec, 2015.

7.1.2 Distribution of Credit

In order to broaden the base of the loan portfolio and to improve the risk diversification and financial access, besides new avenues of earning, DAB has diversified the sector wide distribution of Other Commercial Loans to thirty sectors¹. The analysis of deployment of credit in different sectors indicates that the major portion of the loan portfolio is classified as

“other commercial loans” (92.83 percent against 92.78percent in Dec, 2015), mainly in “Petroleum and lubricants” (10.46 percent), “Construction and building” (8.86percent), “Wholesale” (8.48percent), “all other services” (7.78 percent) and “Cement and Construction” (7.63 percent)sectors. Significant Increases were observed in retail trading, and in construction and building sectors both in absolute amount and percentage of total gross loans, while wholesale and spare parts were among top decreasing sectors. Loans designated to SME and Micro Credit sectors posted an increase of AF 193million

¹ Accounting Circular No. 93/01 dated 26/06/1393

Table 6.2: Sectoral Distribution of Credit

	Hoot, 1388 (Mar, 2010)	Hoot, 1389 (Mar, 2011)	Hoot, 1390 (Mar, 2012)	Qaws, 1391 (Dec, 2012)	Qaws, 1392 (Dec, 2013)	Qaws, 1393 (Dec, 2014)	Qaws, 1394 (Dec, 2015)	Hoot, 1394 (Mar, 2016)
Commercial Real Estate and Construction Loans	19.92	25.98	2.85	2.29	2.02%	1.80%	1.90%	1.69%
Other Commercial Loans	-	-	-	-	-			
Mining	-	0.02	0.72	0.11	0.07%			
Manufacturing	1.22	2.72	13.32	11.88	9.36%			
Trade	32.29	34.16	27.84	28.3	29.81%			
Communication	1.04	1.23	0.94	2.35	3.70%			
Service	4.84	6.72	11.95	15.94	22.11%			
Utilities	2.47	0.03	0.3	0.07	0.05%			
<i>Agricultural Loans</i>						0.27%	0.33%	0.22%
<i>Livestock and Farms</i>						0%	0.03%	0.03%
<i>Manufacturing and Industry(product of metal, wood, plastic, rubber)</i>						2%	4.42%	4.49%
<i>Manufacturing, Handmade and Machine products</i>						4%	4.24%	4.15%
<i>Cement and Construction Materials</i>						3%	1.96%	1.72%
<i>Textile</i>						2.59%	0.52%	0.59%
<i>Power</i>						0.35%	0.22%	0.44%
<i>Construction and Building</i>						12.52%	7.54%	8.86%
<i>Services</i>						4.79%	3.80%	3.40%
<i>Hotel and Restaurant</i>						1.20%	1.46%	0.78%
<i>Telecommunication</i>						2.92%	5.70%	5.70%
<i>Ground Transportation</i>						4.87%	5.31%	5.74%
<i>Air Transportation</i>						4.18%	2.66%	2.82%
<i>Health and Hygienic</i>						0.71%	1.16%	1.69%
<i>Median, Advertisements and Printer</i>						0.04%	0.04%	0.03%
<i>All Other Services</i>						1.41%	7.56%	7.78%
<i>Wholesales</i>						4.93%	9.89%	8.48%
<i>Machineries</i>						0.12%	0.25%	0.37%
<i>Petroleum and Lubricants</i>						8.74%	9.80%	10.46%
<i>Spare Parts</i>						0.24%	1.42%	0.20%
<i>Electronics</i>						1.40%	1.58%	1.45%
<i>Cement and other Construction Materials</i>						1.87%	2.73%	2.01%
<i>Food Items</i>						4.52%	8.24%	7.63%
<i>All Other Items</i>						5.72%	3.47%	4.08%
<i>Retail Trading</i>						3.92%	3.28%	5.06%
<i>Road and Railway</i>						2.41%	1.17%	1.09%
<i>Dams</i>						0.61%	0.09%	0.00%
<i>Mines</i>						0.08%	1.48%	0.46%
<i>Other infrastructure Projects</i>						1.81%	2.44%	3.10%
<i>Financial and Lending Institutions</i>						0.00%	0.00%	0.00%
Agricultural Loans	0.88	0.75	2.06	2.66	2.38%	2.34%	2.35%	2.48%
Consumer Loans	1.33	1.01	0.82	0.74	0.24%	0.26%	0.30%	0.31%
Residential Mortgage Loans to Individuals	7.3	8.95	15.65	14.46	10.84%	7.14%	2.68%	2.68%
All Other Loans	3.69	10	12.65	10.71	9.41%	6.68%	0.00%	0.00%

Source: Financial Supervision Department/DAB

7.1.3 Classification of Loans

7.1.3.1 Non-performing loans

Non-performing loans (NPLs) constitute 15.48 percent of total gross loans or 28.90 percent of regulatory capital, which is not a favorable situation. Moreover, it can be seen that trend of credit risk is increasing. Observing this trend, It can be inferred that quality of risk management in banks with poor credit performance is weakening. It is essential that banks with poor loan quality evaluate credit applications carefully.

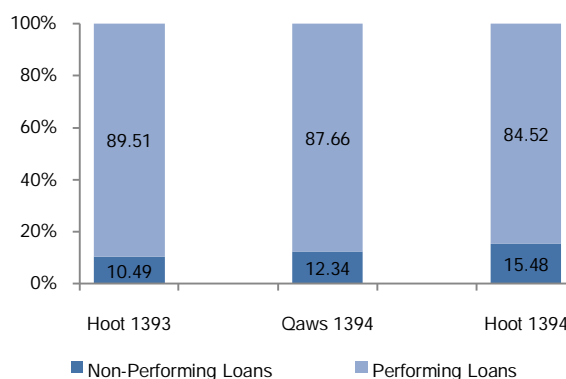
In monetary terms, by the end of Mar, 2016, growth in non-performing loans increased by AF1.38 billion reaching to are cord high level of AF6.99 billion or 15.48 percent of total gross loans and 28.90 percent of the system's regulatory capital against AF 5.60 billion or 12.34 percent of the total gross loans in the preceding quarter. The deterioration is mainly due to weaker loan quality. More than 79percent of the NPLs relates to three Private commercial banks holding 63.34 percent of total gross loans of the banking sector.

This situation requires regulatory oversight and prompt remedial action to be taken to improve governance of credit risk and to avoid negative impact on the profitability and capital adequacy of the banks with poor credit quality.

The sector wide distribution of NPL reveals that a major portion of NPLs originated from

commercial loans mostly related to trade, services and manufacturing sectors.

Figure 6.3: Quality of Loan Portfolio



Source: Financial Supervision Department/DAB

7.1.3.2 Adversely-classified loans

Adversely classified loans (substandard, doubtful) depicted AF 755million increase over the last quarter reaching to AF 9.45 billion, constitutes 20.95 percent of the total gross loans or 39.12 percent of regulatory capital. This development requires strong board oversight and remedial actions by management to reduce the level of Adversely Classified loans to an acceptable level. In addition, more emphasis should be focused on strengthening corporate governance in banks with poor credit quality, enhancing effectiveness and efficiency of

internal controls, and adequately managing inherent and unsystematic risk.

7.1.3.3 Loans classified Watch

Loans classified in the “watch”² category are AF 3.52billion, which makes 7.82 percent of total gross loans, decreased by 27.32 percent since the previous quarter (Dec, 2015). The decrease is mostly attributed to one private commercial bank in the system. This category of loans requires close monitoring as it may lead to more adversely classified loans (Substandard, Doubtful) and losses in the future.

7.1.3.4 Loans classified loss³

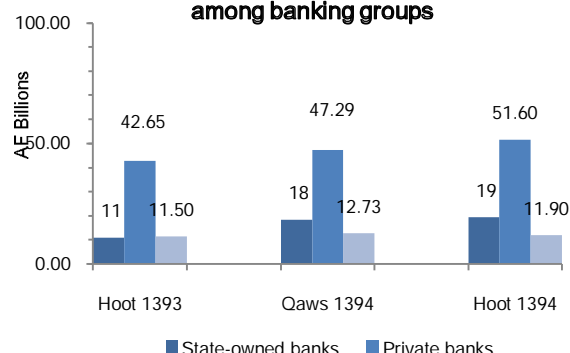
Loans classified as loss amounts to AF 134 million or 0.29 percent of total gross loans showing a rise by AF 471million since previous quarter, which is attributable to three banks.

1.2 Interbank Claims

Interbank Claims are the second largest among the asset categories, currently comprising 30.78 percent of total assets registered an increase of AF4.58 billions in previous quarter (Dec, 2015). The rise in this

category of assets is mostly attributable to two banking institutions, indicating that the banking sector has channeled a portion of its attracted funds as deposits in other financial institutions inside and outside of the country. See figure 6.4.

Figure 6.4: Share of Inter bank Claims among banking groups



Source: Financial Supervision Department/DAB

1.3 Investment

The investment portfolio of the banking sector, comprising bonds, Gov. Securities, and investment in associated companies, grew by 5.13 percent (AF 966 million) over the previous quarter, standing at AF19.78 billion or 7.35percent of total assets. Major part of the sector's investment took place outside Afghanistan.

1.4 Cash in Vault and Claims on DAB

Cash in vault and claims on DAB remains the largest category, both in absolute as well as percentage terms, making 39.00 percent of the total assets, showed a decrease of AF

² Assets and advances for which the principal and/or interest remains outstanding for 1-30 days (Watch)-new Assets Classification and provision regulation

³ Assets on which the payment of principal or interest is due and remains unpaid for 540 days or more (Loss) as per Accounting Letter No. 03/92 dated 16/09/1392

11.01billion, since the previous quarter ending Dec, 2015.

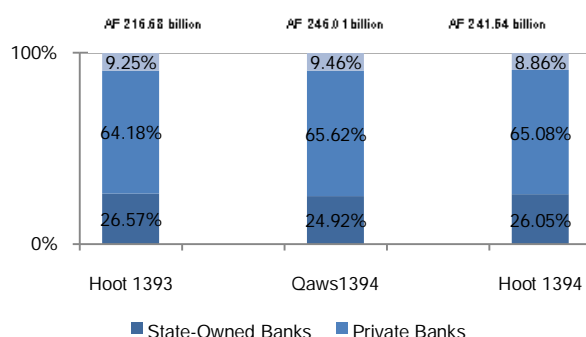
The banking sector is fully compliant with required reserves regulations and is deploying slowly and prudently the attracted funds into other types of assets

II. LIABILITIES

Total liabilities of the banking sector decreased by AF4.46 billion or 1.81 percent standing at AF241.54 billion against AF246.01 billion in the preceding quarter FY (Dec, 2015). All components of total liabilities except all other liabilities have shown decrease over the last quarter.

The majority of liabilities are made up of deposits (95.66 percent), with “other liabilities” at second and borrowings in third place. See table 6.

Figure 6.5: Liabilities decreased by AF 4.46 billion or 1.81 percent



Source: Financial Supervision Department, DAB

2.1 Deposits

Deposits being the main funding source, amounted to AF 231.05 billion for the

quarter under review, decreased by AF 5.94 billion or 2.51percent, compared to 8.46 percent increase in Dec, 2015. The decrease in deposit base of the banking sector is attributed to withdrawals from the demand deposits and occurred in AF currency. Currency wise analysis shows that Afghani denominated deposits indicated 9.28 percent decrease (against 0.96percent increase in Dec, 2015) accounting for 25.93 percent of total deposits, while US dollar denominated deposits were down by 0.43percent (11.44 percent increase in Dec, 2015) making 69.34 percent of the total deposits of the system.

Private Banks attracted AF151.04 billion deposits, showing a reduction of 3.73 percentage points against 14.15percent increase in previous quarter, making up 65.37 percent of the system's deposits.

The share of state-owned banks amounted to AF60.12billion, increased by 2.73 percent (3.77 percent decrease in Dec, 2015) since preceding quarter (Sep, 2015) accounted for 26.02percent of the system's deposits.

The share of branches of foreign banks stands at AF19.88 billion decreased by 7.81percent (7.02percent increase in Dec, 2015) making up 8.61 percent of total deposits of the system.

In terms of types of deposits, demand deposits accounted for 75.18percent of the total deposit base, down by 5.11 percent, saving deposits with 19.06 percent of total deposits was in the second place, and

depicted 5.55 percent increase while time deposits making up to 5.76 percent of the

total deposit portfolio, was up by 8.87 percent since Dec, 2015.

Figure 6.6: Currency Composition of Deposits

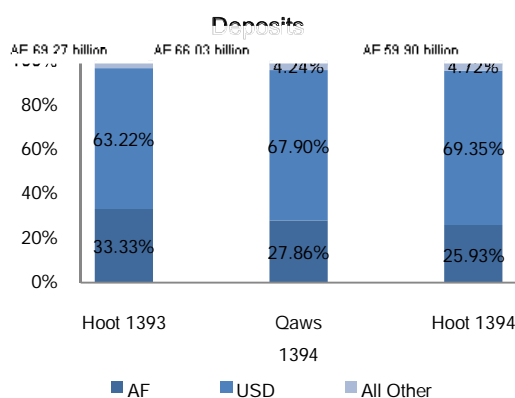
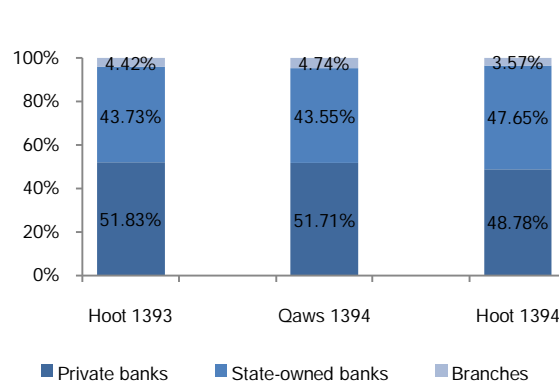


Figure 6.7: Afghani Denominated Deposits



Source: Financial Supervision Department, DAB

Figure 6.8: Deposits decreased by 2.51 percent or AF 5.94 billion

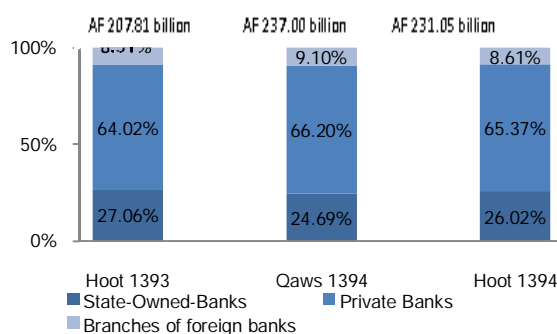
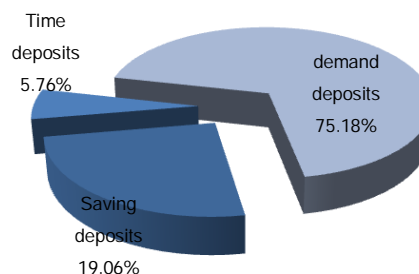


Figure 6.9: Breakdown of Deposits



Source: Financial Supervision Department, DAB

2.2 Borrowings

The share of borrowings in total funding structure of the system decreased by 17.02 percent standing at AF 3.69 billion at the end of Mar, 2016, making 1.53 percent of

total liabilities in comparison with 0.13 percent decrease in the preceding quarter. The current borrowing position is attributed to three banking institutions.

III. LIQUIDITY

Liquidity risk can be defined as the risk of not having sufficient liquid assets to meet the demand of borrowers and depositors. To avoid liquidity risk, banks should maintain an asset liability committee (ALCO); one of its

tasks are the liquidity management of the bank through gap analysis, stress testing, scenario analysis, cash flow analysis, etc. according to policies of the bank.

Table 6.3: Key Financial Soundness Indicators of the banking Sector

Ratio in %	(Mar, 2010)	(Mar, 2011)	(Mar, 2011)*	(Mar, 2011)	(Dec, 2012)	(Dec, 2013)	(Dec, 2014)	(Dec, 2015)	(Mar, 2016)
Total Capital Adequacy Ratio	25.81	-14.46	30.39	23.06	21.84	26.34	26.46	19.94	21.14
Tier 1 Capital Adequacy Ratio	24.19	-14.51	30.29	23.98	19.97	24.65	26.09	19.66	19.63
Non-Performing Loans to Total Gross Loans	0.5	48.4	3.75	5.15	5.31	5.1	8.09	12.34	15.48
Return on Assets (ROA)	1.41	-20.08	0.24	-1.21	-0.54	0.74	0.90	0.20	4.35
Return on Equity (ROE)	10.35	-520.66	1.9	-17.9	-7.17	10.03	7.35	1.69	43.74
liquidity Ratio (Broad Measure Median)	59.19	63.32	63.83	57.37	72.13	67.93	73.6	68.22	68.89
liquidity Assets to Total Assets	0.38	40.58	47.01	55.82	63.75	73.18	73.28	75.05	74.40

*Excluding Kabul Bank

Source: Financial Supervision Department/ DAB

IV. Capital

The system is well capitalized. The capital fund of the banking sector stands at AF 27.84 billion; increased by 12.85 percentage points or AF 3.17 billion over the last quarter. The increase in total financial capital is attributed to profits and capital injection.

On an aggregate basis the Capital Adequacy ratio of the banking sector stands at 21.14 percent. See table 6.5.

Disaggregated analysis shows that all banks except one bank in the system registered capital adequacy ratio above the minimum

threshold, (12 percent of risk-weighted assets.)

3.1 Liquidity Ratio (broad measure)

Banks are required to maintain a liquid asset ratio not less than 15 percent.

This should provide a comfortable safeguard against any liquidity shortfall.

Generally, a surplus liquidity position was observed in the banking sector during this period (69 percent of the sector's total assets are comprised of liquid assets). Ratio

of the broad liquidity as a median for the whole system stood at 68.89percent. All banking institutions were well above the minimum required level. See table 6.5.

V. Profitability

On a cumulative basis, the profitability of the banking sector for the first quarter of 2016 was AF2.93billion of net profit which compared to AF 817 million of net profits in Dec, 2015, shows a significant increase.

The increase in profitability of the banking sector as evident from the table 6.5 is mostly ascribable to a significant increase in non-interest income attributed to one of the state-owned banks came from the revaluation of investment properties, and other contributing factors such as a decrease in operating cost. This is while credit provision showed increase and net-interest income decreased in the quarter under analysis.

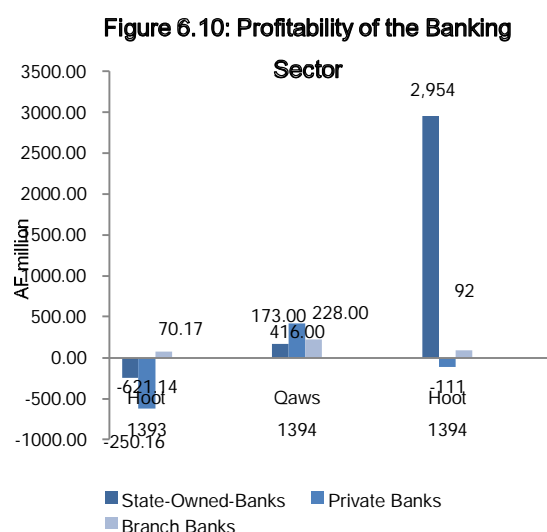
As a result, the returns on assets (ROA) improved to 4.35 from 0.31 percent and return on equity (ROE) became 43.74 percent from 2.55 percent in the previous quarter. See table 6.5.

On a cumulative basis six banking institutions have incurred AF 329million losses in the quarter under analysis against AF 193 million losses posted by four banks in the quarter ending Dec, 2015.

On core income basis three banks ended with losses, against the two banks in the previous quarter.

Group wise analysis reveals State-Owned Banks (SOB) and branches of foreign banks (BFB) ended up with profits, while Private Banks (PB) ended up with losses for the quarter under review. See figure 6.10.

Major portion of the profitability of the banking sector is attributed to state-owned banks standing AF 2.95 billion, increased by 2.78billion or 1607.5 percent, Branches of foreign banks are at second place with AF 92million profit, registering AF 136 million decrease over the quarter, while private banks are at loss standing at AF 111 million decreased mainly due to increase in credit provisions.

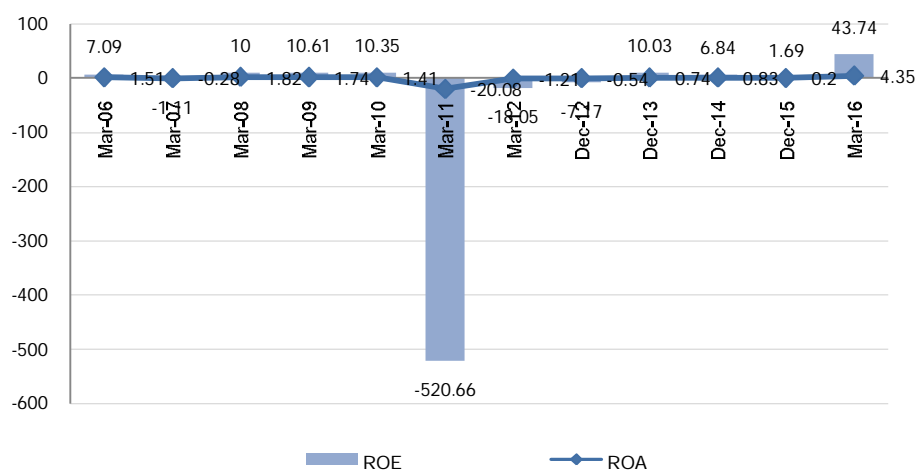


Source: Financial Supervision Department, DAB

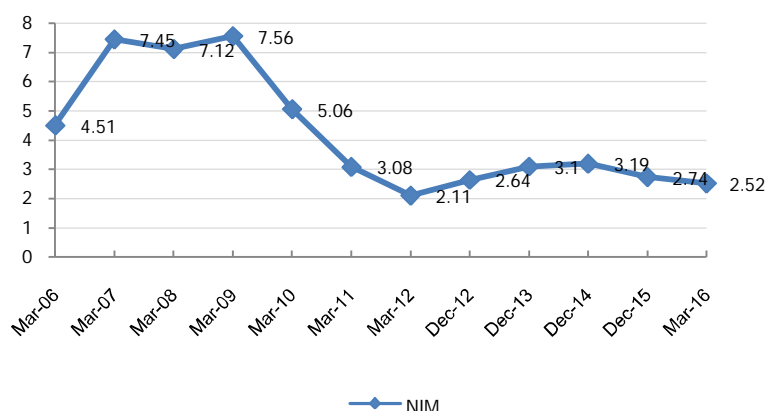
Table 6.4: P/L Schedule

	1393 (Mar, 2015)	1394 (Dec, 2015)	1394 (Mar, 2016)	%change Q-o-Q
interest income	2,131	2,266	2,198	-3.00
interest expense	519	501	500	-0.19
Net interest income	1,612	1,765	1,699	-3.74
Non-interest income	926	2,104	4,067	93.29
Non-interest expenses	1,354	1,832	1,327	-27.56
Salary cost	896	926	909	-1.83
Credit provisions	1,011	284	515	81.33
P/L before tax	-723	827	3,015	264.57
P/L after tax	-801	817	2,935	259.24

Source: Financial Supervision Department, DAB

Figure 6.11: Return on Assets and Return of Equity

Source: Financial Supervision Department/ DAB

Figure 6.16: Net Interest Margin

Source: Financial Supervision Department/DA

VI. FOREIGN EXCHANGE RISK

The level of overall open FX position risk being taken by banks is largely within the levels set by DAB. In general, all the banking institutions were within the limits set for the overall open FX position, except for three banking institutions holding open FX positions on overall and on an individual currency (USD long and short position) basis violated the limits.

The impact of change in exchange rate upon regulatory capital of the system reveals that a 20 percent appreciation in exchange rate would increase the regulatory capital of the system by AF 8.81 billion and vice versa. Similarly, a 4 percent appreciation would correspond to AF 1.76 billion increase and vice versa.

VII. INTEREST RATE RISK

Overall the banking system is in an interest-rate sensitive position. However, calculations made from the Interest Rate Sensitivity Schedules of all banks reveal that, the net-interest income of the system over the next 12 months may increase by AF1.79 billion in the event of increase in the market interstate (upward interest rate shock) by 3 percentage points. Conversely, if the interest rate decreases by 3 percentage points (downward interest rate shock) interest income will decline by AF1.79 billion. For two banking institution, if the interest-rate increases by 3 percentage points, it will decrease their net interest income over the next 12 months.

The major reason for the overwhelming asset-sensitivity of the banks is the large excess of interest earning assets over interest bearing liabilities. Although it may improve the net interest margin and overall profitability of banks, this situation makes the banks more vulnerable to a sudden decrease in the market rates.

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