



Da Afghanistan Bank

Economic & Statistical Bulletin

Annual Bulletin - FY 1395



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Economic & Statistical Bulletin

Annual Bulletin - 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 Annual Bulletin analyzes developments in fiscal year 1395 (2016).

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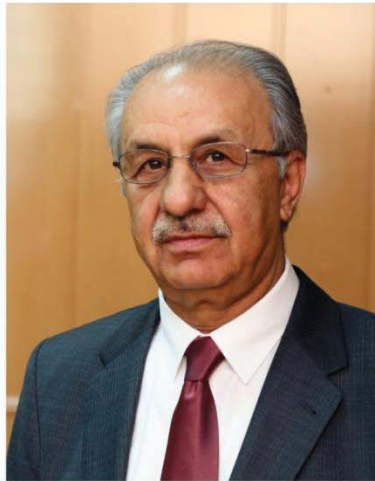
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ABBREVIATIONS

DAB	Da Afghanistan Bank
GOA	Government of Afghanistan
EMDEs	Emerging Markets and Development Economies
LICs	Least Income Countries
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
ARTF	Afghanistan Reconstruction Trust Fund
LOTFA	Law and Order Trust Fund for Afghanistan
MPD	Monetary Policy Department
GDP	Gross Domestic Product
CSO	Central Statistics Organization
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



Khalil Sediq

Governor



Muhammad Qaseem Rahimi

Second Deputy Governor



Wahidullah Nosher

First Deputy 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

Da Afghanistan Bank's annual economic and statistical bulletin for the FY 2016 provides a comprehensive account of developments in the Afghan Economy during in FY 2016. In this bulletin, you will find a summary report of the global economy as well as thorough analysis of the developments that have taken place in all sectors of the Afghanistan's economy in 2016 and succinct examination of the challenges faced by these sectors.

Global economy experienced a slower growth during the FY 2016 as compared with the previous year. According to the World Bank, the estimated global economic growth was 2.3 percent from 2.7 percent in the FY 2015 showing the weakest performance since the global financial crisis in 2007-08, mainly attributed to lower investment, stagnant global trade and higher level of policy uncertainty.

GDP growth of low income countries remained lower registering 4.7 percent. The reasons behind low growth are lower prices of commodities, bad weather conditions, and political and security challenges.

In the fiscal year 2016, Afghanistan's economy recorded a stronger growth comparing to the previous year despite persistent constraints and formidable economic challenges originating mainly from uncertain political environment and deteriorating security. Afghanistan's economy registered a positive GDP growth of 3.6 percent in 2016, up from a negative growth of 2.2

percent in the fiscal year 2015. The growth is mainly attributed to the two sectors of the economy, agriculture and services sectors. Agriculture sector performed exceptionally well compared to previous year. Services sector also experienced improvements, while industry sector marked weakness over the review period.

Agriculture sector witnessed a high growth rate of 12 percent as a result of government's support and favourable weather condition from a significant negative figure of 16.9 percent in the FY 2015. It is worth to mention that robust recovery in the production of narcotics in the FY 2016 (which grew by 45.5 percent from -48.4 percent) contributed significantly to agriculture growth.

By the end of 2016, global commodity prices recorded a higher rate for energy and non-energy commodities. Energy price rose by 11 percent due to higher prices of coal, while non-energy prices recorded a slower increase of just one percent mainly driven by higher prices of metals. Since the economy is Afghanistan is heavy reliant on import the increase in international commodity prices left its imprint on domestic prices in Afghanistan.

Headline CPI inflation during the fourth quarter of FY 2016 shows an upward trend. The year over year measure of changes in CPI index shows an inflation rate of 4.5 percent in the fourth quarter of FY 2016 from 0.1 percent observed in the same period of the previous year.

Inflation when measured on quarter to quarter basis also rose to 2.0 percent which is slightly higher from 1.6 percent recorded in the corresponding period of last year.

Da Afghanistan Bank maintains monetary targeting regime and targets reserve money to contain inflation. In the fiscal year 2016, reserve money (Da Afghanistan Bank's operational target) grew by 10.97 percent, exceeding the targeted level of 10 percent by a slight margin.

DAB has auctioned total amount of USD 1,926.25 million during the FY 2016 in order to manage liquidity in the market and to mitigate the sharp fluctuations in the exchange rate of Afghani against foreign currencies especially US dollar. In the review period, the value of Afghani appreciated against US dollar by 1.78 percent.

Da Afghanistan Bank's net international reserve (NIR) consists of monetary gold, reserve position and holdings with the IMF and special drawing rights (SDR) as well as major foreign exchange such as US dollar, Euro, Great Britain Pound and others. NIR increased by 6.31 percent or USD 404.89 million standing at USD 6,824.69 million in the FY 2016, while it recorded a decrease of USD 394 million in the previous year.

During the FY 2016, external sector improved benefiting from modest growth in exports of goods, sustained decline in imports of goods and enhanced inflows in the current transfers (grants). A substantial increase in the current transfers and earnings from exports of goods

helped offset expenditure on imports to a sizable extent. These developments, together with an increase of workers' remittances and income inflows helped to reduce the external current account deficit by 20 percent to USD 3,771.83 million in the FY 1395 compared to a deficit of USD 4,720.68 million in the FY 1394.

Inflow to the capital account decreased on account of inflows (capital transfers) to the government sector.

Net portfolio investment increased during the year 2016, while Foreign Direct Investment (FDI), net inflows declined while net Portfolio Investment increased during the year under review.

Banking sector earned net profits amounting to AF 4.29 billion for the year 2016, against AF net profit of 522 million in the previous year. State owned banks and branches of foreign banks ended up with profits, while private banks ended up with losses during the fiscal year 2016. It is worth mentioning that the asset base of the banking weakened in the FY 2016 depicting 10.56 percent growth reaching AF 2.83 billion, while this figure was reported at 12.18 percent.

1

GLOBAL ECONOMIC ENVIRONMENT

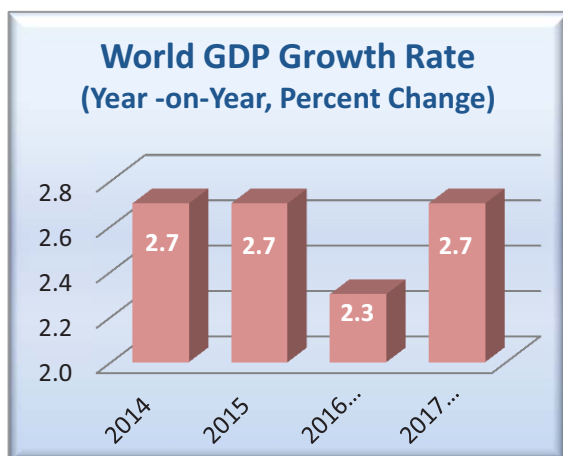


1

GLOBAL ECONOMIC ENVIRONMENT

According to the World Bank, the annual global growth is estimated to have decreased to 2.3 percent in 2016 from 2.7 percent increase recorded in the previous year indicating the weakest performance since the global financial crisis while the annual global growth is expected to increase to 2.7 percent in the coming year. Lower investment, stagnant global trade, and higher level of policy uncertainty are the main factors that affected the world economy negatively.

Figure 1.1: Global GDP growth rate



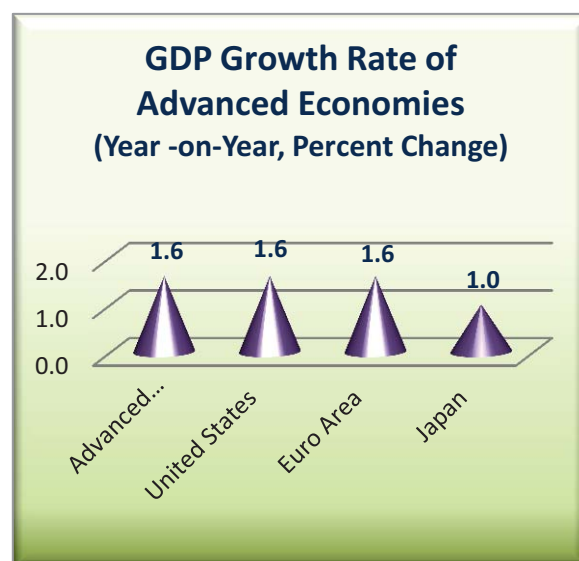
Source: World Bank

I. ADVANCED ECONOMIES

In 2016, advanced economies experienced subdued growth and low inflation amid

increasing policy uncertainty, tepid investment and sluggish productivity growth. Therefore the annual growth of the advanced economies has been estimated to have declined to 1.6 percent from 2.1 percent in 2015. Economic activity is expected to increase in 2017, but uncertainty regarding the policies of the new U.S. administration and United Kingdom's decision to leave the European Union (Brexit) could significantly influence the economic growth of these countries.

Figure 1.2: GDP growth rate of Advanced Economies



Source: World Bank

1.1.1 Economy of the United States:

The growth of the United States' economy slowed significantly from 2.6 percent in 2015 to an estimated 1.6 percent in 2016. The main reasons behind lower growth of the U.S. economy were lower exports, continuing decrease in the inventories and a deceleration in private investment. The economic activity had increased again in the period before the U.S. elections in November and the labor markets further tightened resulting in increased wage growth in a slowly manner. This supported continued gains in real disposable income which could help further reduce the poverty rates. Despite subdued growth, the economy of the U.S. continued to move closer to the Federal Reserve's full employment and inflation objectives. The unemployment rate was below 5 percent in the most of the second half of 2016.

1.1.2 Economy of the Euro Zone:

The economic growth of the Euro Area decreased from 2 percent in 2015 to 1.6 percent in 2016. The main reason behind the decline in the growth was lower domestic demand and a decline in exports. Confidence in the Euro Area has been resilient after the United Kingdom's vote to leave the European Union in June, 2016. Uncertainty about the Brexit is expected to lower UK's economic growth and to some extent the Euro Area in the coming year. The oil prices, which indicated a decline in the early 2016, increased indicating reduced support to real income and private consumption growth relative to 2014-15

periods. The labor market and credit conditions continued to improve in 2016. Employment reached its pre-crisis levels while the unemployment rate declined from higher levels with cross-country variations. Negative policy interest rates, combined with large-scale asset purchase programs by the European Central Bank, led to a noticeable easing of borrowing costs and had an overall positive effect on lending flows.

1.1.3 Economy of Japan:

The Japan's economic growth is estimated at 1.0 percent for the year 2016 after the release of new and revised national accounts data. Investment and exports were generally weak, while private consumption indicated some signs of improvement after two years of contraction. A modest increase in wage growth was noted due to labor shortages; however, the benefits were reduced by low inflation expectations and increasing share of part-time employment. In September 2016, the central bank of Japan changed its policy focus from a quantitative target for government bond purchases to a more flexible approach aimed at stabilizing long-term interest rates around zero. This decision could help alleviate constraints associated with the increased scarcity of bonds eligible for purchase by the central bank, and at the same time mitigate the adverse effects of negative long term yields on financial institutions. Despite the policy shift, the yen appreciated in the earlier part of 2016. Since the exports of Japan are often denominated in destination currencies, this

dampened profits and investments in 2016. However, the yen depreciated rapidly towards the end of the year.

II. EMERGING MARKET AND DEVELOPING ECONOMIES

The emerging markets and developing economies (EMDEs) grew at an estimated rate of 3.4 percent in 2016. These economies would experience higher growth in the coming year which is expected to be 4.2 percent. In 2016, the EMDEs experienced a slight increase in the domestic demand that offset a decline in the global trade. Generally, the financing conditions in the EMDEs were good through most of 2016, but the financing conditions narrowed latter in the year and as a result, the U.S. dollar appreciated causing the global bond yields to rise.

Lower global trade and decreased commodity prices created challenging conditions for the commodity exporting EMDEs. After a decline in the economic growth of these countries in 2015, economic growth was supported by some stabilization in the domestic demand in 2016. Brazil and Russia noted a decline in their private consumption in a slower manner in 2016. The investment level also indicated a decline in 2016, particularly in Brazil, Colombia and Russia while the investment growth in other exporters in East Asia and Pacific, Eastern Europe and Central Asia, and Latin America and the Caribbean, indicated an increase. Despite comprising two-fifth of the output of exporting EMDE, Russia and Brazil

experienced recession for last two years (2015 and 2016).

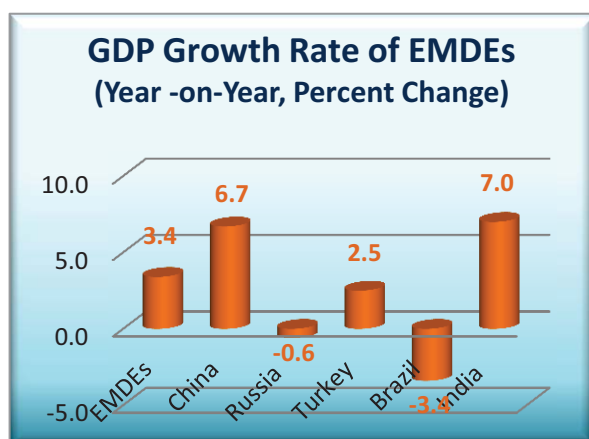
Several large oil exporting countries such as Azerbaijan, Angola, Kazakhstan, and Nigeria which have strictly managed exchange rates, allowed their exchange rates to increase in 2015-16 period after significant decline in their reserves. Despite soft economic activity, Azerbaijan, Angola, Nigeria, Mozambique, and Mongolia, had to pursue policy tightening in the second half of 2016 due to balance of payment pressures, depreciation in their domestic currencies, and higher inflation rates.

The economic growth of the commodity importing EMDEs has been estimated at 5.6 percent for 2016. The growth of the commodity importing EMDEs excluding China, which is a group of countries that produce one-third of the EMDE output, has been estimated to have decreased to 4.3 percent in 2016. This decline in economic growth partly reflects a downgrade to the India's fast pace of expansion.

Commodity importing EMDEs continued to take advantage from improvements in the past terms-of-trade and sound macro-economic policies. Taking the advantage of low inflation and low energy costs, Croatia, Thailand, Tunisia, and the Philippines, were able to maintain accommodative macro-economic policies. Thailand benefitted from improved confidence, the Philippines benefitted from higher implementation of public investment projects while Bangladesh and Pakistan benefitted from large cross-border infrastructure investments.

In the commodity importing EMDEs, the domestic demand remained strong which was supported by low commodity prices and accommodative monetary and fiscal policies. In many commodity importers, particularly, in Eastern Europe and South Asia, the private consumption was strong while investment growth has recovered in many commodity importers, especially in Eastern Europe (Croatia, Romania, Serbia), East Asia and Pacific (Cambodia, the Philippines), and South Asia (Pakistan). The exports of many commodity importers decreased due to lower demand in the major markets except for the trading partners of Germany that benefited from the excellent performance of Germany; some Asian countries with improving competitiveness (Cambodia, India), and countries with strong exports of services (Croatia, India, Lebanon, the Philippines, Sri Lanka, Thailand).

Figure 1.3: The GDP growth rate of the emerging markets and developing economies (EMDEs)



Source: World Bank

1.2.1 The Economy of China

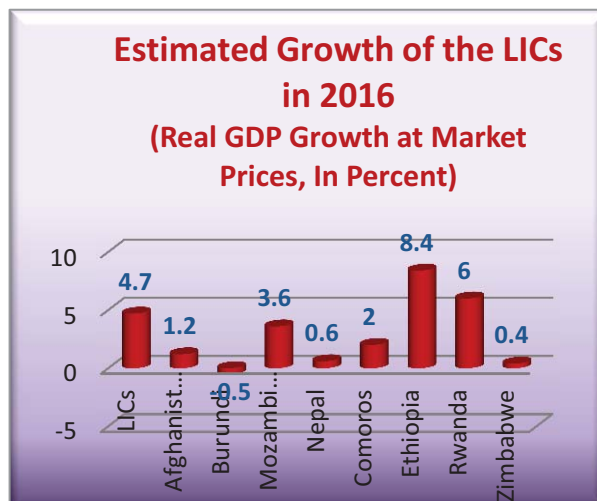
The economic growth of China indicated a slight decrease in 2016 and has been estimated at 6.7 percent. Growth was noted mainly in services sector while the industrial production stabilized at a moderate level. The growth in domestic consumption was strong and the growth in investment continued to moderate. The decrease in the investment growth was mainly in the private sector while investment by the non-private sector indicated an upward trend in 2016. However, the economic growth of China has been projected to moderate to 6.5 percent in 2017.

III. THE Low-Income Countries (LICs)

The growth of the low-income countries (LICs) remained subdued in 2016 and has been estimated to 4.7 percent. Lower prices of commodities, bad weather conditions, and political and security problems were the main factors which causing a decrease in the output of various countries. The economic growth indicated a decline among commodity exporting LICs while the economic growth showed no change for commodity-importing LICs compared to the last year. The overall growth of the LICs is expected to improve in the upcoming year and has been forecasted to 5.6 percent. The main challenges that these countries will face in the way of economic growth are considered to be bad weather conditions particularly, worsening drought

conditions as well as bad political and security conditions.

Figure 1.4: The real GDP growth of least income countries (LICs) in 2016



Source: World Bank

The average inflation in LICs in 2016 indicated almost no change from the previous year with a slight decrease in the inflation in commodity-importing LICs. In some cases, the prices were stabilized by moderate currency movements and an increase in agricultural output. The inflation rate indicated an increase in metal exporting LICs because of depreciation in the currency and an increase in the food prices due to drought. Meanwhile, the inflation among oil exporting LICs remained low indicating lower level of domestic demand.

The external current account deficits narrowed among LICs in 2016 but the deficits were large. The narrowing of the deficits in the external current account mainly shows a decline in the imports by the metal exporting LICs. Conversely, the deficits in the oil exporting LICs indicated an increase. The current

account deficits among the importing LICs only slightly narrowed since the strong demand for importing capital goods offset benefits from lower prices of oil. Meanwhile, a decline in the capital inflows was noted among LICs.

A narrowing in the current account deficits with reduced capital inflows among LICs put pressure on the exchange rates and international reserves in these countries in 2016. Generally, the currencies of the LICs, except for the commodity exporting LICs, indicated a depreciation against the U.S. dollar, however; the depreciation was lower compared to the last year. The currencies of Mozambique and Congo showed a significant depreciation against the U.S. dollar. The currencies of commodity-importing LICs such as Rwanda, and Uganda depreciated slightly since low oil prices put positive impacts on the current account balance. During the month of importing goods and services, the international reserves of Burundi, the Comoros and Mozambique declined by over 30 percent.

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The World Bank Group Flagship Report, "Global Economic Prospects" January 2017



2

MONETARY AND CAPITAL MARKET
DEVELOPMENT

2

MONETARY AND CAPITAL MARKET
DEVELOPMENT

Developments in monetary sector were upward in 2016 as different indicators represented positive trends. Observing the data, reserve money (RM) increased by 10.97 percent in 2016 higher than 3.16 percent in 2015. At the time, commercial Banks' deposits with the central bank, which are components of reserve money increased by 10.62 percent from their previous values.

Reserve money growth, which is Da Afghanistan Bank's operational target, remained well below the assigned target during first and second quarters, but surpassed for a short period of time during the second half of the year. Currency in circulation (set as indicative target) increased by 11 percent in the year under review, reaching AF 223,599.46 million. Da Afghanistan Bank also experienced accumulation of 6.3 percent (USD 404.89 million) in net international reserve (NIR).

Narrow money (M1) stood at AF 423,306 million at the end of the year under review, registering an annual growth of 8.65 percent. Broad money

(M2) demonstrated similar behavior, and grew by 9.7 percent standing at AF 455,217 million.

In order to monitor and manage reserve money growth, DAB utilizes monetary instruments such as FX auction and capital notes under the open market operations.

In the fiscal year 2016, DAB has auctioned a total amount of USD 1,926.25 million to manage the liquidity in the market as well as to mitigate the sharp fluctuations in the exchange rate of Afghani against foreign currencies. At the end of the year, the total outstanding amount of CNs stood at AF 43.619 billion.

Meanwhile, Afghani appreciated against the US dollar by 1.78 percent in the year 2016.

I. MONETARY PROGRAM

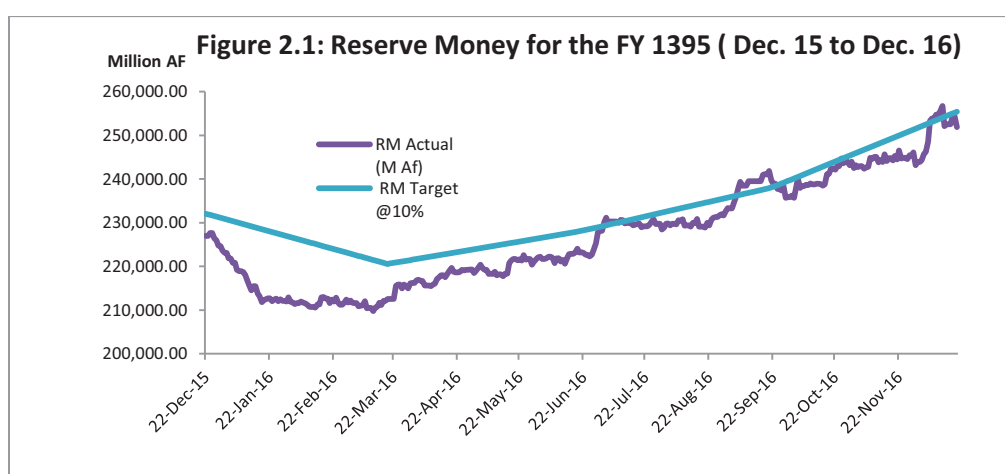
Reserve Money remained the key operational target (performance criterion) of monetary policy department during FY 2016, while currency in circulation was set as the indicative target.

To support domestic price stability, Da Afghanistan Bank determines the amount of

reserve many based on quantitative theory of money. Hence, the assigned targets for RM and CIC are based on expected economic growth and inflation during the concerned period. For the fiscal year 2016, the ceiling for reserve money and currency in circulation growth was set 10% due to higher expected economic growth and low inflation rate. By the end of the period under review, actual RM grew by 10.97

percent and actual CIC growth was 11 percent, which are slightly above the target. However, they were well managed according to the assigned target. Central bank continued its sterilization policy, but in smaller amount than the previous periods.

The Figure 2.1 and 2.1 illustrate the ceiling and the actual reserve money and currency in circulation for the year under review.



Source: Monetary Policy Department/DAB

II. MONETARY AGGREGATES

Monetary Policy Department compiles monetary aggregates - narrow money (M1) and broad money (M2) in accordance with Monetary and Financial Statistics (MFS) methodology.

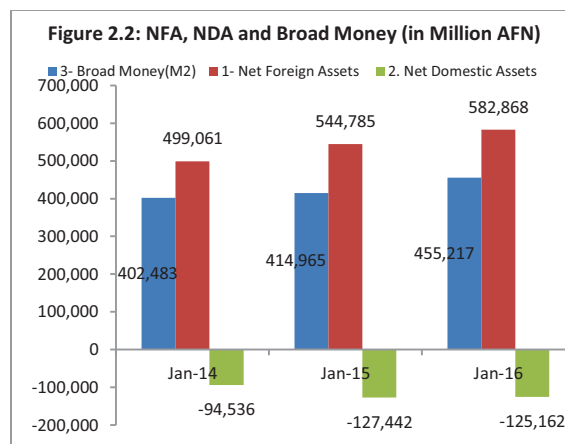
Narrow money, includes currency outside depository corporations and demand deposits, while broad money includes narrow money components and other less liquid assets or quasi money.

As shown in Table 2.1, narrow money grew by 8.65 percent in FY2016 compared to 1.2 percent recorded in FY2015, showing a difference of AF 33,715 million. Currency outside depository corporations or CIC, which accounts for 48 percent of M1, grew by 10.29 percent in 2016 compared to 4.1 percent in the previous year. Demand deposits, which are other components of M1, experienced a growth rate of 7 percent at the end of FY2016, significantly higher from -1.5 percent observed in the previous year. Demand deposit in

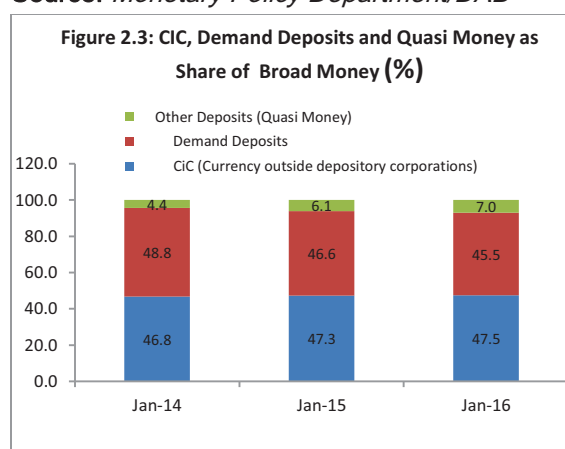
comparison to the previous year is AF 13,540 million higher.

The supply of broad money (M2) expanded by AF 455,217 million in the year under review from AF 414,965 million in the previous year, showing an increase of 9.7 percent. The data shows that M1, with 93 percent share, remained the main contributing component of M2.

Quasi money or time deposits of commercial banks, which are the other component of M2, grew by 25.76 percent (y-o-y) at the end of 2016. Quasi money constitutes 7 percent of broad money during the period under review, which is higher than 6.1 percent in FY 2015. Therefore, the impact of changes in quasi money on M2 is negligible. The year-on-year change of Afghani denominated time deposits increased by 50 percent standing at AF 3,792 million, and foreign currency denominated time deposits rose by 15 percent reaching to AF 2,745 million. Afghani-denominated time deposits constituted 2.5 percent and foreign currency denominated time deposits stood at 4.5 percent of M2 respectively. Demand deposits as a share of broad money decreased to 45.5 percent (Y-o-Y) at the end of the year under review, while it was shown 46.6 percent in the previous year (Figure 2.1 and 2.2).



Source: Monetary Policy Department/DAB



Source: Monetary Policy Department/DAB

**Table 2.1: Depository Corporations:
Analytical Balance Sheet and Monetary Aggregate FY 1395**

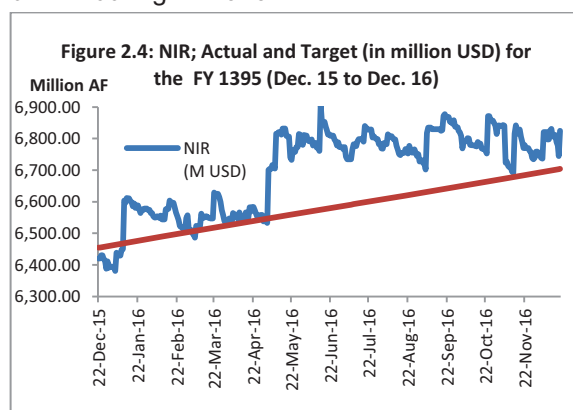
<i>In Million AF</i>	Dec -2014	Dec - 2015	Dec -2016				
	Amount	Amount	Y-o-Y Δ	Difference	Amount	Y-o-Y Δ	Difference
1- Net Foreign Assets	499,061	544,785	9.2%	45,724	582,868	6.99%	38,083
(a) Gross Foreign Assets	507,289	555,610	9.5%	48,321	594,017	6.91%	38,407
Foreign Exchange Reserves	57,762	110,946	92.1%	53,184	100,349	-9.55%	-10,597
Gold	48,988	51,948	6.0%	2,960	53,391	2.78%	1,442
Other	308,933	291,825	-5.5%	-17,108	331,171	13.48%	39,346
Other Foreign Assets	91,605	100,890	10.1%	9,285	109,106	8.14%	8,216
(b) Foreign Liabilities	8,228	10,825	31.6%	2,597	11,148	2.99%	323
2. Net Domestic Assets	-94,536	-127,442	34.8%	-32,906	-125,162	-1.79%	2,280
(a) Net Domestic Credit	-9,409	-7,103	-24.5%	2,306	-18,107	154.91%	-11,004
Net Credit to Nonfinancial Public Sector	-54,320	-54,387	0.1%	-67	-63,850	17.40%	-9,463
Net Credit to Central Government	-54,204	-54,482	0.5%	-278	-63,945	17.37%	-9,463
Credit to Central Government	27,754	28,316	2.0%	562	23,021	-18.70%	-5,295
Liabilities to Central Government	81,958	82,798	1.0%	840	86,965	5.03%	4,168
Net Credit to State & Local Government	0.000	0.000	0.0%	0	0.000	0.000	0
Net Credit to Public Nonfinancial Corporations	-116	95	-181.7%	211	94	-0.48%	0
Credit to Private Sector	46,394	48,872	5.3%	2,477	47,111.83	-3.60%	-1,760
Net Credit to Other Financial Corporations	-1,484	-1,588	7.0%	-104	-1,368.71	-13.80%	219
(b) Capital Accounts	103,889	141,214	35.9%	37,325	127,336	-9.83%	-13,878
(c) Other Items Net	18,763	20,876	11.3%	2,113	20,282	-2.84%	-594
3- Broad Money(M2)	402,483	414,965	3.1%	12,482	455,217	9.70%	40,252
Narrow Money(M1)	384,795	389,591	1.2%	4,796	423,306	8.65%	33,715
CiC (Currency outside depository corporations)	188,451	196,134	4.1%	7,683	216,308	10.29%	20,175
Demand Deposits	196,344	193,458	-1.5%	-2,887	206,998	7.00%	13,540
Other Deposits (Quasi Money)	17,688	25,374	43.5%	7,686	31,911	25.76%	6,537
In Afghani	5,135	7,631	48.6%	2,496	11,423	49.68%	3,792
In Foreign currency	12,553	17,743	41.3%	5,190	20,488	15.47%	2,745
Non liquid Liabilities	2,042	2,378	16.4%	336	2,490	4.71%	112

2.1 NET INTERNATIONAL RESERVE

Da Afghanistan Bank's international reserves consist of monetary gold, reserve position and holdings with the IMF and Special Drawing Rights (SDR) as well as major foreign exchange such as US dollars, Euro, Great British Pound and others. The Net International Reserves (NIR) of Afghanistan expressed in terms of US dollar is defined as reserve assets minus reserve liabilities.

NIR increased by 6.31 percent which is equivalent to USD 404.89 million in FY2016, while it had a decrease of USD 394 million in the FY2015. For the end of fiscal year 2016, the NIR accumulation floor was set USD 283.91 million, but in real ground, the total accumulation of NIR reached to USD 6,824.69 million. This figure at the beginning of the year, it was recorded USD 6,419.80 million.

Figure 2.4 illustrates the target and actual trend of NIR during FY2016.



Source: Monetary Survey, Monetary Policy Department/ DAB

III. FOREIGN EXCHANGE MARKET

3.1 Foreign Exchange Rates

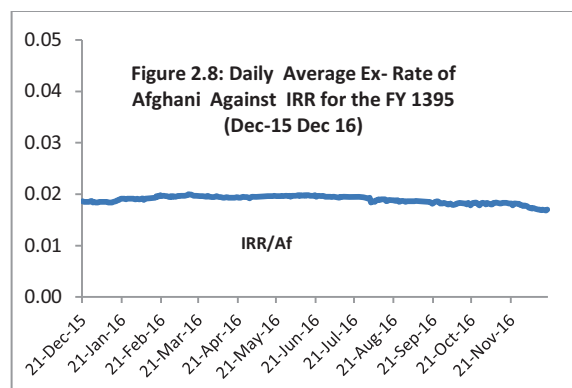
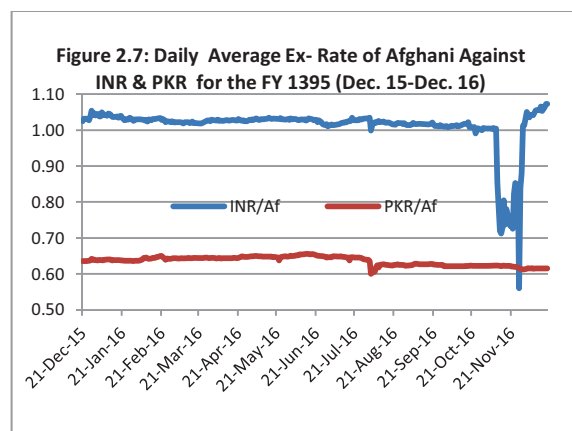
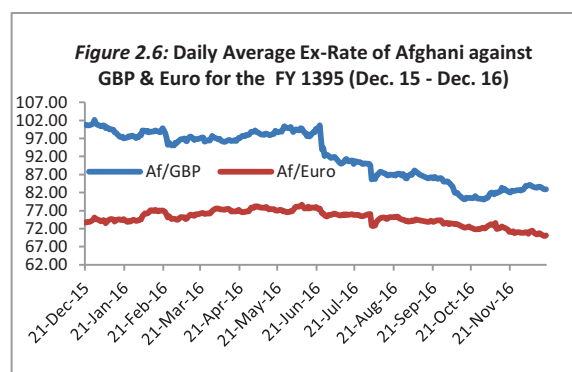
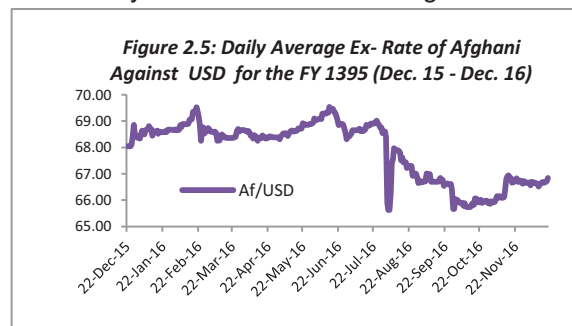
T Da Afghanistan Bank's ultimate goal is to maintain price stability. In order to achieve and maintain this goal, DAB puts its focus to utilize its monetary instruments, basically the open market operations, effectively with sound policy implementation.

During the first half of FY 2016, Afghani remained stable against the US dollar and many other currencies, while during the second half of the year, it appreciated significantly. The main factors supporting the Afghani value are the usage campaign, mostly in south and south east regions of the country, and repatriation of Afghan refugees from Iran and Pakistan.

Afghani appreciated by 1.978 percent against the U.S dollar, traded at AF 66.70 per US dollar at the end of the review period. At the time, it depreciated by 4.75 percent against the INR, but improved by 3.15 against PKR. In addition, the Afghani exchange rate against Euro, GBP and IRR increased by 4.81 percent, 17.74 percent, and 8.6 percent respectively.

The daily historic review of the average exchange rate of AF against the U.S. dollars for

the fiscal year 2016 is shown in figures below.



Source: Monetary Survey, Monetary Policy Department/ DAB

3.2 Foreign Exchange Auction

In order to control the money supply, Da Afghanistan Bank anchors reserve money by conducting foreign exchange auctions three times each week, and a weekly capital notes auction, which are its primary monetary instruments. Central bank continued the FX auction to mop up excess liquidity from the market and to avoid extra volatilities in the exchange rate of Afghani against the foreign currencies, especially the U.S. dollar.

During the fiscal year 2016, DAB auctioned a total amount of USD 1.926 billion; when the total demand was USD 2.669 billion. On average, 48 bidders participated in each auction and 34 bids were the winning bids with the average amount of USD 13.285 million. The data for FY 2015 recorded a total awarded amount of USD 2.793 billion, with a total demand of USD 3.924 billion. On average, 38 bidders participated in each auction and 32 bids were awarded with an average amount of USD 27.7 million.

Table 2.2: Foreign Exchange Auction's Summary for FY 2016 (million USD)

Auction Date	No. of Bidders	Highest Price	Lowest Price	Market Ex-Rate	Cut off Price	Amount Announced	Amount Awarded	Total Demand
22-Dec-15	55	68.06	67.40	68.05	68.00	25.00	25.10	44
26-Dec-15	51	68.155	67.91	68.12	68.09	15.00	15.40	42
28-Dec-15	56	68.87	68.30	68.86	68.81	15.00	20.18	49
30-Dec-15	54	68.48	68.10	68.45	68.43	18.00	18.02	40
2-Jan-16	43	68.35	68.00	68.34	68.22	18.00	17.73	48
4-Jan-16	51	68.69	68.20	68.64	68.58	16.00	16.39	47
6-Jan-16	50	68.46	68.30	68.49	68.43	15.00	15.25	40
9-Jan-16	56	68.73	68.50	68.69	68.70	13.00	14.02	40
11-Jan-16	55	68.76	68.32	68.74	68.72	15.00	15.30	42
13-Jan-16	51	68.47	67.41	68.45	68.43	15.00	14.57	37
16-Jan-16	52	68.64	68.55	68.62	68.61	15.00	14.35	37
18-Jan-16	49	68.52	68.21	68.52	68.48	15.00	14.80	36
20-Jan-16	53	68.60	68.52	68.59	68.58	15.00	14.85	34
23-Jan-16	48	68.62	68.01	68.58	68.58	15.00	14.70	34
25-Jan-16	40	68.57	68.44	68.58	68.54	15.00	9.90	25
27-Jan-16	41	68.69	68.60	68.68	68.66	12.00	9.27	28
30-Jan-16	41	68.67	68.58	68.67	68.63	12.00	11.95	37
1-Feb-16	39	68.65	68.40	68.66	68.63	12.00	9.37	27
3-Feb-16	40	68.65	68.58	68.65	68.62	12.00	9.58	27
6-Feb-16	5	68.75	68.70	68.85	68.70	12.00	1.80	5
8-Feb-16	53	68.92	68.76	68.88	68.86	10.00	10.70	37
10-Feb-16	42	68.88	68.67	68.88	68.87	12.00	10.20	29
13-Feb-16	47	68.90	68.85	68.89	68.88	12.00	12.21	35
17-Feb-16	41	69.38	69.10	69.36	69.10	12.00	13.16	40
20-Feb-16	51	69.50	68.39	69.53	69.16	12.00	16.59	47
22-Feb-16	49	69.19	68.70	69.14	69.00	14.00	14.18	35
24-Feb-16	52	68.11	67.40	68.25	68.01	14.00	13.76	35
27-Feb-16	46	68.53	68.31	68.53	68.48	14.00	13.55	33
29-Feb-16	53	68.64	68.57	68.63	68.61	14.00	12.60	30
2-Mar-16	49	68.71	68.51	68.70	68.67	14.00	13.93	34
5-Mar-16	43	68.58	68.48	68.59	68.53	14.00	12.32	32

7-Mar-16	47	68.61	68.55	68.61	68.58	12.00	11.41	32
9-Mar-16	46	68.22	68.04	68.25	68.17	12.00	10.01	28
12-Mar-16	49	68.43	68.37	68.38	68.40	10.00	10.15	34
14-Mar-16	48	68.45	68.37	68.45	68.41	12.00	11.08	32
16-Mar-16	43	68.42	68.25	68.38	68.37	12.00	10.86	43
23-Mar-16	21	68.29	68.02	68.36	68.15	20.00	8.95	20
26-Mar-16	44	68.68	68.36	68.63	68.61	12.00	11.82	33
28-Mar-16	47	68.69	68.55	68.61	68.59	15.00	14.50	33
30-Mar-16	51	68.67	68.51	68.64	68.64	14.00	14.09	35
2-Apr-16	45	68.64	68.40	68.64	68.55	14.00	11.33	33
4-Apr-16	50	68.72	68.50	68.59	68.56	13.00	12.30	33
6-Apr-16	49	68.75	68.51	68.56	68.54	13.00	12.33	33
9-Apr-16	48	68.34	68.18	68.34	68.28	13.00	11.72	32
11-Apr-16	53	68.42	68.31	68.43	68.39	13.00	12.38	33
13-Apr-16	47	68.23	68.10	68.25	68.22	13.00	10.28	27
16-Apr-16	52	68.37	68.30	68.35	68.35	13.00	12.64	33
18-Apr-16	57	68.40	68.35	68.39	68.38	13.00	12.08	33
20-Apr-16	53	68.47	68.25	68.34	68.32	13.00	11.43	31
23-Apr-16	51	68.47	68.35	68.42	68.40	13.00	11.63	31
25-Apr-16	50	68.41	68.33	68.41	68.39	13.00	13.65	38
30-Apr-16	44	68.37	68.21	68.37	68.36	13.00	10.56	30
2-May-16	43	68.32	68.25	68.31	68.31	12.00	10.08	28
4-May-16	47	68.48	58.46	68.47	68.46	12.00	10.43	30
7-May-16	52	68.57	68.42	68.54	68.55	12.00	12.19	35
9-May-16	50	68.46	68.37	68.43	68.44	12.00	10.05	29
11-May-16	44	68.60	68.45	68.59	68.57	12.00	10.04	29
14-May-16	51	68.61	68.45	68.61	68.59	12.00	11.09	32
18-May-16	52	68.73	68.63	68.72	68.71	14.00	13.98	35
21-May-16	52	68.72	68.65	68.71	68.71	14.00	13.81	34
23-May-16	53	68.96	68.57	68.86	68.85	15.00	14.80	35
25-May-16	51	68.87	68.80	68.86	68.85	15.00	14.00	35
28-May-16	45	68.91	68.82	68.90	68.89	15.00	13.35	32
30-May-16	47	68.93	68.82	68.91	68.91	12.00	10.62	31
1-Jun-16	44	69.13	68.09	69.10	69.05	12.00	12.70	37

4-Jun-16	52	69.08	68.05	69.07	69.06	15.00	15.00	35
8-Jun-16	50	69.29	69.10	69.28	69.25	15.00	15.37	39
11-Jun-16	47	69.27	68.23	69.28	69.25	16.00	15.39	38
13-Jun-16	52	69.33	69.28	69.32	69.31	16.00	16.09	36
15-Jun-16	53	69.46	69.39	69.46	69.44	18.00	18.89	38
18-Jun-16	48	69.38	69.25	69.34	69.31	18.00	17.69	38
20-Jun-16	51	69.19	69.10	69.19	69.17	18.00	16.94	35
22-Jun-16	49	68.87	68.25	68.85	68.84	17.00	14.65	31
25-Jun-16	43	68.91	68.75	68.89	68.88	16.00	14.32	36
27-Jun-16	45	68.73	68.58	68.71	68.69	16.00	14.18	35
29-Jun-16	45	68.36	68.18	68.31	68.29	15.00	12.13	31
2-Jul-16	44	68.50	68.40	68.46	68.44	14.00	11.85	30
4-Jul-16	47	68.68	68.35	68.65	68.66	14.00	13.01	33
9-Jul-16	37	68.70	68.25	68.66	68.50	14.00	9.77	27
11-Jul-16	35	68.62	68.50	68.62	68.58	15.00	11.60	27
13-Jul-16	55	68.65	68.59	68.62	68.61	15.00	13.00	31
16-Jul-16	52	68.89	68.67	68.86	68.86	15.00	13.70	33
18-Jul-16	51	68.83	68.62	68.82	68.81	15.00	12.20	30
20-Jul-16	49	68.92	68.85	68.90	68.91	15.00	14.00	35
25-Jul-16	53	69.07	68.80	69.02	68.99	18.00	16.12	36
27-Jul-16	46	68.87	68.70	68.86	68.85	15.00	12.77	32
30-Jul-16	49	68.64	68.40	68.55	68.53	15.00	13.40	33
1-Aug-16	35	68.49	68.20	68.61	68.44	15.00	7.50	19
3-Aug-16	45	67.42	66.00	65.91	66.85	15.00	9.33	29
6-Aug-16	50	66.26	65.00	66.30	66.18	12.00	8.93	28
8-Aug-16	56	68.50	67.30	67.57	67.50	14.00	14.59	18
10-Aug-16	50	67.94	67.40	67.93	67.86	14.00	12.84	35
13-Aug-16	52	67.91	67.75	67.87	67.87	14.00	12.63	35
15-Aug-16	42	67.52	67.15	67.51	67.45	14.00	10.69	30
17-Aug-16	43	67.42	67.10	67.44	67.38	14.00	9.96	28
20-Aug-16	47	67.21	67.01	67.22	67.14	14.00	10.10	29
22-Aug-16	49	67.26	67.21	67.24	67.24	12.00	10.20	29
24-Aug-16	47	67.26	67.01	67.30	67.21	12.00	10.28	31
27-Aug-16	48	67.90	66.91	67.01	67.01	12.00	10.15	30

29-Aug-16	42	66.84	66.61	66.84	66.81	12.00	9.27	29
31-Aug-16	47	66.71	66.52	66.74	66.68	12.00	9.03	28
3-Sep-16	50	66.71	66.60	66.71	66.69	10.00	8.70	30
3-Sep-16	50	66.71	66.60	66.71	66.69	10.00	8.70	30
5-Sep-16	49	66.73	66.20	66.71	66.71	10.00	9.57	33
7-Sep-16	48	67.02	66.84	66.99	66.96	12.00	11.57	34
10-Sep-16	45	66.74	66.62	66.70	66.70	12.00	10.08	29
17-Sep-16	44	66.78	66.68	66.77	66.75	12.00	11.65	35
19-Sep-16	48	66.72	66.60	66.73	66.67	14.00	11.77	32
21-Sep-16	50	66.56	66.00	66.54	66.54	14.00	12.50	33
24-Sep-16	46	66.63	66.54	66.64	66.62	14.00	11.95	32
26-Sep-16	48	66.61	66.56	66.60	66.60	12.00	10.19	31
28-Sep-16	40	66.37	66.20	66.40	66.31	12.00	8.58	29
1-Oct-16	40	66.40	65.85	66.04	66.00	12.00	10.62	32
3-Oct-16	37	65.92	65.70	66.00	65.89	12.00	8.51	26
5-Oct-16	46	65.88	65.70	65.90	65.86	12.00	10.53	31
8-Oct-16	42	65.75	65.62	65.79	65.71	12.00	9.76	29
10-Oct-16	43	65.78	65.66	65.76	65.76	12.00	8.82	25
15-Oct-16	48	65.87	65.50	65.85	65.85	14.00	10.31	27
17-Oct-16	42	65.84	65.71	65.83	65.80	12.00	9.44	31
19-Oct-16	49	66.05	65.96	66.06	66.00	14.00	14.01	37
22-Oct-16	48	66.90	65.80	65.91	65.91	14.00	12.58	32
24-Oct-16	38	65.90	65.80	65.90	65.86	14.00	11.55	32
26-Oct-16	49	65.93	65.85	65.94	65.90	14.00	14.45	36
29-Oct-16	44	65.95	65.70	65.90	65.84	15.00	14.67	35
31-Oct-16	46	65.83	65.75	65.86	65.82	15.00	14.22	33
2-Nov-16	49	65.91	65.65	65.91	65.88	15.00	14.90	35
5-Nov-16	51	66.05	65.96	66.03	66.00	15.00	15.50	37
7-Nov-16	51	66.07	66.02	66.08	66.05	17.00	17.22	36
9-Nov-16	48	66.12	66.08	66.14	66.11	17.00	17.34	37
12-Nov-16	48	66.12	66.05	66.12	66.10	17.00	17.24	37
14-Nov-16	50	66.82	65.79	66.81	66.68	18.00	18.22	40
16-Nov-16	57	66.97	66.80	66.94	66.87	18.00	18.60	41
19-Nov-16	51	66.63	66.46	66.66	66.56	20.00	20.10	42

21-Nov-16	53	66.69	66.55	66.70	66.66	20.00	19.80	35
23-Nov-16	54	66.84	66.75	66.83	66.81	18.00	18.12	38
26-Nov-16	53	66.72	66.66	66.74	66.69	20.00	19.67	38
28-Nov-16	51	66.60	66.35	66.62	66.57	20.00	18.85	38
30-Nov-16	54	66.71	66.62	66.71	66.68	18.00	18.04	41
3-Dec-16	55	66.67	66.50	66.63	66.64	19.00	17.50	38
5-Dec-16	52	66.56	66.41	66.57	66.52	18.00	16.05	38
7-Dec-16	57	66.71	66.61	66.69	66.68	18.00	17.04	36
10-Dec-16	53	66.62	66.48	66.62	66.57	20.00	20.60	42
12-Dec-16	55	66.58	66.35	66.51	66.48	20.00	19.85	40
14-Dec-16	53	66.62	66.54	66.62	66.60	20.00	20.00	38
17-Dec-16	53	66.66	66.55	66.66	66.64	20.00	20.20	41
19-Dec-16	51	66.71	66.67	66.70	66.70	20.00	19.75	37
26-Oct-16	49	65.93	65.85	65.94	65.90	14.00	14.45	36
29-Oct-16	44	65.95	65.70	65.90	65.84	15.00	14.67	35
31-Oct-16	46	65.83	65.75	65.86	65.82	15.00	14.22	33
2-Nov-16	49	65.91	65.65	65.91	65.88	15.00	14.90	35
5-Nov-16	51	66.05	65.96	66.03	66.00	15.00	15.50	37
7-Nov-16	51	66.07	66.02	66.08	66.05	17.00	17.22	36
9-Nov-16	48	66.12	66.08	66.14	66.11	17.00	17.34	37
12-Nov-16	48	66.12	66.05	66.12	66.10	17.00	17.24	37
14-Nov-16	50	66.82	65.79	66.81	66.68	18.00	18.22	40
16-Nov-16	57	66.97	66.80	66.94	66.87	18.00	18.60	41
19-Nov-16	51	66.63	66.46	66.66	66.56	20.00	20.10	42
21-Nov-16	53	66.69	66.55	66.70	66.66	20.00	19.80	35
23-Nov-16	54	66.84	66.75	66.83	66.81	18.00	18.12	38
26-Nov-16	53	66.72	66.66	66.74	66.69	20.00	19.67	38
28-Nov-16	51	66.60	66.35	66.62	66.57	20.00	18.85	38
30-Nov-16	54	66.71	66.62	66.71	66.68	18.00	18.04	41
3-Dec-16	55	66.67	66.50	66.63	66.64	19.00	17.50	38
5-Dec-16	52	66.56	66.41	66.57	66.52	18.00	16.05	38
7-Dec-16	57	66.71	66.61	66.69	66.68	18.00	17.04	36
10-Dec-16	53	66.62	66.48	66.62	66.57	20.00	20.60	42
12-Dec-16	55	66.58	66.35	66.51	66.48	20.00	19.85	40

14-Dec-16	53	66.62	66.54	66.62	66.60	20.00	20.00	38
17-Dec-16	53	66.66	66.55	66.66	66.64	20.00	20.20	41
19-Dec-16	51	66.71	66.67	66.67	66.67	20.00	19.75	26.65
Total						2100	1926.25	2669.46

***Source:** Market Operations Department and Monetary Policy Department staff calculations*

IV. CAPITAL MARKET & LIQUIDITY CONDITIONS

4.1 Capital Notes Auction

Capital notes are Afghani denominated short-term securities offered by the central bank to the primary market customers, mostly licensed commercial banks on weekly basis.

Da Afghanistan Bank uses Capital Notes (CNs) as the second monetary tool to manage the money supply growth. Capital notes are used to absorb the excess liquidity of the commercial banks.

Currently, DAB offers capital notes with maturity of one week, one month, three months, six months, and one year. The one week security has recently been introduced to the market in order to expand the use of capital notes as monetary policy tool.

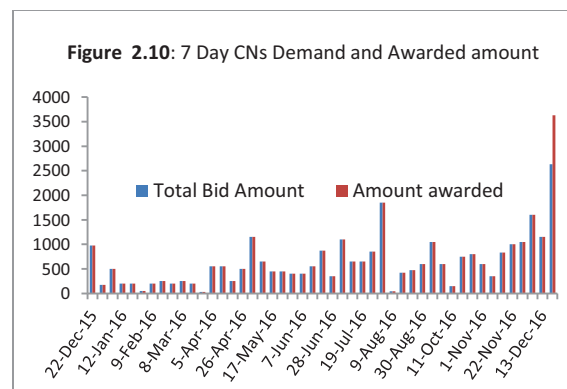
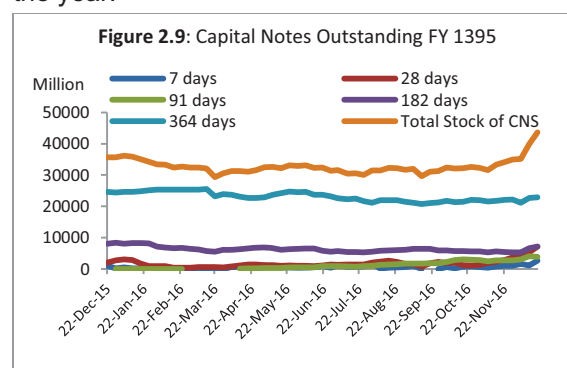
The total outstanding stock of capital notes reached AF 43.6 billion at the end of the fiscal year 2016, which shows an increase of 33.5 percent compared to AF32.7 billion at the end of the previous year. The increase in the level of securities shows the increase of Afghani demand by banking sector and gives the signal for lower amount of FX auction level which may have caused the higher NIR accumulation during the reporting period.

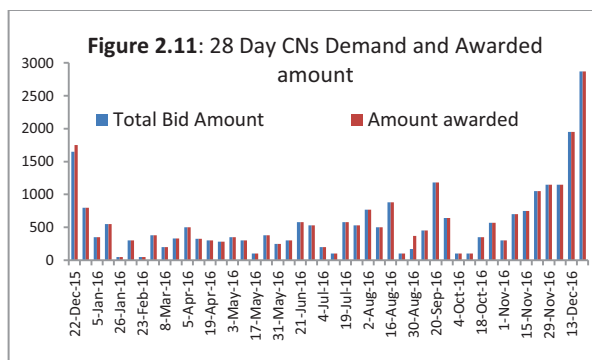
The outstanding stock of 7 day capital notes stood at AF2631 million, representing higher volume than the stock of FY2015. 28 days CNs outstanding amount stood at AF7, 120 million, while newly created 91 days outstanding stock

of CNs recorded the amount of AF 3,850 million. The stock outstanding for 182 and 364 day notes stood at AF 7,088 million and AF 22,930 million respectively showing higher amounts in FY2016 in comparison with the previous year's amounts.

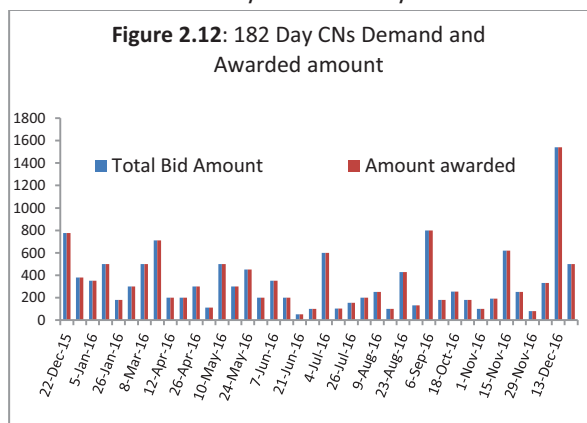
Figure 4.1 exhibits breakdown of the total outstanding stock for all maturities during the fiscal year 2016.

In addition, the weighted average interest rate for 7 day capital note was 1.8 percent, for 28 days security recorded at 3.55 percent, for 91 day notes were 4.33 percent, for 182 days security ending at 5.15 percent, and for 364 days capital notes, it recorded 6.67 percent in the FY 2016 with some small fluctuation during the year.

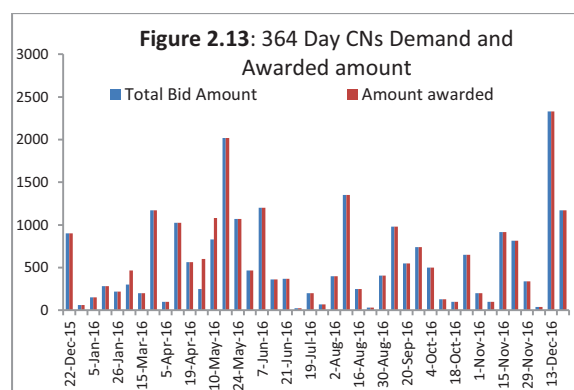




Source: Market Operations Department/DAB



Source: Market Operations Department/DAB



Source: Market Operations Department/DAB

4.2 Required and Excess Reserves

Commercial banks are required to hold 8 percent of their total deposits as obligatory reserves with DAB, which remunerated at one basis point below the cut-off rate of the last 28

days capital notes auction, or equal to the deposit facility rate. During the FY 2015, DAB has paid an amount of AF 193.745 million as required reserve interest rate to banking system. In recent development from 28 June 2015 onward, DAB has stopped paying interest rate for required reserve and no interest have been paid for commercial banks required reserves since then.

Overnight Deposit Facility which is available to all commercial banks to gain interest on their excess balances and provides a floor for rates on capital notes, is not counted towards required reserves. The interest rate on the overnight deposit facility is now 100 basis points below 28 day notes auction cut-off rate (based on a circular to all banks approved by DAB Executive Board on June 09, 2010).

The outstanding amount of deposit facility balances fluctuated between AF one to eight billion during the reporting period. During FY 2016, the payment of interest rate to the mentioned facility reached to AF 23.07 million.

Overnight Credit Facility: This facility is used by banks for short term cash needs. The facility allows banks to borrow Afghani from Central Bank on an overnight basis when they face a short fall in cash flow. The rate that the banks are charged for this facility is 350 basis points above the last 28 day CNs auction. This borrowing is collateralized with outstanding capital notes only (according to the circular of Feb 27, 2007).

During the year under review, one bank benefited from credit facility. The amount of interest received from this window reached AF 570.160 million during the period under review.

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 bank. During the period under review no bank faced shortfalls to their liquidity positions.

Table 2.3: Auction of 7 Day Capital Notes (million AF)

Start Date	Auction Amount	Amount awarded	Total Bid Amount	No. of total bids	No. of Win Bids	Cut off Rate (%)	Low Bid (%)	Highest Bid (%)	Weighted Avg. (%)
22-Dec-15	250	975	975	3	3	1.80	1.80	1.80	1.80
29-Dec-15	2000	175	175	1	1	1.80	1.80	1.80	1.80
5-Jan-16	750	500	500	2	2	1.80	1.83	1.80	1.80
12-Jan-16	750	200	200	1	1	1.80	1.80	1.80	1.80
19-Jan-16	500	200	200	1	1	1.80	1.80	1.80	1.80
2-Feb-16	500	50	50	1	1	1.80	1.80	1.80	1.80
9-Feb-16	500	200	200	1	1				

						1.80	1.80	1.80	1.80
23-Feb-16	750	250	250	2	2	1.80	1.80	1.80	1.80
1-Mar-16	750	200	200	3	3	1.80	1.80	1.80	1.80
8-Mar-16	750	250	250	3	3	1.80	1.80	1.80	1.80
15-Mar-16	500	200	200	3	3	1.80	1.80	1.80	1.80
29-Mar-16	500	30	30	1	1	1.80	1.80	1.80	1.80
5-Apr-16	500	550	550	2	2	1.80	1.80	1.80	1.80
12-Apr-16	750	550	550	3	3	1.80	1.80	1.80	1.80
19-Apr-16	750	250	250	1	1	1.80	1.80	1.80	1.80
26-Apr-16	500	500	500	3	3	1.80	1.80	1.80	1.80
3-May-16	750	1150	1150	6	6	1.80	1.80	1.80	1.80
10-May-16	1500	650	650	4	4	1.80	1.80	1.80	1.80
17-May-16	1000	450	450	3	3	1.80	1.80	1.80	1.80
24-May-16	750	450	450	4	4	1.80	1.80	1.80	1.80
31-May-16	750	400	400	2	2	1.8	1.8	1.8	1.8
7-Jun-16	750	400	400	2	2	1.8	1.8	1.8	1.8
14-Jun-16	750	550	550	3	3	1.8	1.8	1.8	1.8
21-Jun-16	1000	870	870	5	5	1.8	1.8	1.8	1.8
28-Jun-16	1500	350	350	2	2	1.8	1.8	1.8	1.8
4-Jul-16	1000	1100	1100	5	5	1.8	1.8	1.8	1.8
12-Jul-16	1500	650	650	5	5	1.8	1.8	1.8	1.8
19-Jul-16	1000	650	650	5	5	1.8	1.8	1.8	1.8
26-Jul-16	1000	850	850	3	3	1.8	1.8	1.8	1.8
2-Aug-16	1250	1850	1850	6	6	1.8	1.8	1.8	1.8
9-Aug-16	1250	42	42	1	1	1.8	1.8	1.8	1.8

16-Aug-16	500	425	425	4	4	1.8	1.8	1.8	1.8
23-Aug-16	750	475	475	4	4	1.79	1.8	180	1.796
30-Aug-16	750	600	600	4	4	1.79	1.8	1.8	1.797
6-Sep-16	800	1050	1050	4	4	1.8	1.8	1.8	1.8
4-Oct-16	500	600	600	2	2	1.8	1.8	1.8	1.8
11-Oct-16	1000	150	150	2	2	1.8	1.8	1.8	1.8
18-Oct-16	750	750	750	3	3	1.8	1.8	1.8	1.8
25-Oct-16	1000	800	800	3	3	1.78	1.8	1.8	1.8
1-Nov-16	1300	600	600	4	4	1.79	1.8	1.8	1.8
8-Nov-16	1000	350	350	3	3	1.79	1.8	1.8	1.796
15-Nov-16	700	830	830	5	5	1.79	1.8	1.8	1.798
22-Nov-16	1000	1000	1000	5	5	1.79	1.8	1.8	1.8
29-Nov-16	1000	1050	1050	5	5	1.79	1.8	1.8	1.8
6-Dec-16	1500	1600	1600	7	7	1.79	1.8	1.8	1.8
13-Dec-16	2000	1150	1150	4	4	1.79	1.8	1.8	1.8
20-Dec-16	2500	3631	2631	8	8	1.79	1.82	1.82	1.82

Total **43,800** **30,553** **29,553**

Source: Market Operations Department/DAB

Table 2.4: Auction of 28 Day Capital Notes (million AF)

Start Date	Auction Amount	Amount awarded	Total Bid Amount	No. of total bids	No. of Wing Bids	Cut off Rate (%)	Low Bid %	Highest Bid (%)	Weighted Avg. Rate (%)
22-Dec-15	750	1750	1650	4	3	3.53	3.54	3.54	3.54
29-Dec-15	1000	800	800	3	3	3.53	3.54	3.54	3.53
5-Jan-16	750	350	350	3	3	3.53	3.54	3.54	3.54
19-Jan-16	2000	550	550	2	2	3.53	3.54	3.54	3.54
26-Jan-16	100	50	50	1	1	3.54	3.54	3.54	3.54
2-Feb-16	500	300	300	2	2	3.54	3.54	3.54	3.53

23-Feb-16	500	50	50	1	1	3.54	3.54	3.54	3.54
1-Mar-16	500	380	380	3	3	3.52	3.54	3.54	3.53
8-Mar-16	500	200	200	2	2	3.54	3.54	3.54	3.54
29-Mar-16	750	330	330	3	3	3.53	3.54	3.54	3.53
5-Apr-16	500	500	500	3	3	3.54	3.54	3.54	3.54
12-Apr-16	500	325	325	4	4	3.53	3.54	3.54	3.53
19-Apr-16	500	300	300	4	4	3.53	3.54	3.54	3.54
26-Apr-16	500	280	280	4	4	3.53	3.54	3.54	3.53
3-May-16	750	350	350	3	3	3.54	3.54	3.54	3.54
10-May-16	750	300	300	2	2	3.54	3.54	3.54	3.54
17-May-16	750	100	100	1	1	3.53	3.53	3.53	3.53
24-May-16	750	380	380	4	4	3.53	3.53	3.53	3.53
31-May-16	750	250	250	2	2	3.53	3.535	3.535	3.535
7-Jun-16	750	300	300	2	2	3.535	3.535	3.535	3.535
21-Jun-16	750	580	580	5	5	3.53	3.535	3.535	3.533
28-Jun-16	750	530	530	1	1	3.53	3.53	3.53	3.53
4-Jul-16	750	200	200	1	1	3.535	3.535	3.535	3.535
12-Jul-16	750	100	100	1	1	3.534	3.534	3.534	3.534
19-Jul-16	1000	580	580	4	4	3.53	3.534	3.534	3.532
26-Jul-16	1000	530	530	1	1	3.533	3.533	3.533	3.533
2-Aug-16	750	770	770	3	3	3.53	3.533	3.533	3.532
9-Aug-16	750	500	500	3	3	3.53	3.533	3.533	3.531
16-Aug-16	750	880	880	5	5	3.53	3.533	3.533	3.533
23-Aug-16	750	100	100	1	1	3.45	3.45	3.45	3.45
30-Aug-16	1000	370	170	3	2	3.45	3.533	3.45	3.45
6-Sep-16	700	450	450	1	1	3.53	3.53	3.53	3.53
20-Sep-16	300	1180	1180	7	7	3.45	3.533	3.533	3.533

27-Sep-16	300	640	640	5	5	3.45	3.533	3.533	3.533
4-Oct-16	100	100	100	1	1	3.533	3.533	3.533	3.533
11-Oct-16	1000	100	100	1	1	3.533	3.533	3.533	3.533
18-Oct-16	1500	350	350	3	3	3.45	3.533	3.497	3.533
25-Oct-16	1500	570	570	5	5	3.45	3.533	3.533	3.511
1-Nov-16	200	300	300	2	2	3.53	3.533	3.53	3.53
8-Nov-16	500	700	700	4	4	3.5	3.533	3.533	3.526
15-Nov-16	500	750	750	5	5	3.5	3.533	3.533	3.526
22-Nov-16	750	1050	1050	4	4	3.533	3.533	3.533	3.533
29-Nov-16	750	1150	1150	5	5	3.53	3.533	3.533	3.533
6-Dec-16	1000	1150	1150	4	4	3.49	3.533	3.533	3.533
13-Dec-16	3000	1950	1950	4	4	3.49	3.533	3.533	3.533
20-Dec-16	2500	2870	2870	8	8	3.5	3.55	3.55	3.55
Total	37,450	26,295	25,995						

Source: Market Operations Department/DAB

Table 2.5: Auction of 91 Day Capital Notes (million AF)

Start Date	Auction Amount	Amount awarded	Total Bid Amount	No. of total bids	No. of Win Bids	Cut off Rate (%)	Low Bid (%)	Highest Bid (%)	Weighted Avg. (%)
12-Apr-16	250	100	100	1	1	4.33	4.33	4.33	4.33
19-Apr-16	250	300	100	2	1	4.33	4.34	4.33	4.33
3-May-16	500	120	120	3	3	4.33	4.33	4.33	4.33
10-May-16	500	20	20	1	1	4.33	4.33	4.33	4.33
24-May-16	500	130	130	4	4	4.33	4.33	4.33	4.33
31-May-16	500	30	30	1	1	4.29	4.33	4.33	4.329
14-Jun-16	500	40	40	1	1	4.329	4.33	4.33	4.329
21-Jun-16	500	322.7	322.7	3	3	4.329	4.33	4.33	4.33
4-Jul-16	750	20	20	1	1	4.329	4.33	4.33	4.329
12-Jul-16	750	30	30	1	1	4.33	4.33	4.33	4.33
26-Jul-16	500	150	150	2	2	4.329	4.33	4.33	4.33

2-Aug-16	500	250	250	2	2	4.33	4.33	4.33	4.33
9-Aug-16	750	350	350	2	2	4.33	4.33	4.33	4.33
16-Aug-16	750	100	100	1	1	4.33	4.33	4.33	4.33
23-Aug-16	500	200	200	1	1	4.33	4.33	4.33	4.33
30-Aug-16	750	300	300	1	1	4.33	4.33	4.33	4.33
20-Sep-16	800	400	400	2	2	4.33	4.33	4.33	4.33
4-Oct-16	250	450	450	3	3	4.33	4.33	4.33	4.33
11-Oct-16	500	630	630	3	3	4.33	4.33	4.33	4.33
18-Oct-16	500	200	200	2	2	4.33	4.33	4.3	4.33
25-Oct-16	500	100	100	1	1	4.33	4.33	4.33	4.33
1-Nov-16	400	100	100	1	1	4.33	4.33	4.33	4.33
15-Nov-16	300	380	380	4	4	4.329	4.33	4.33	4.33
22-Nov-16	750	230	230	2	2	4.33	4.33	4.33	4.33
29-Nov-16	750	230	230	3	3	4.329	4.33	4.33	4.33
6-Dec-16	500	330	330	2	2	4.33	4.33	4.33	4.33
13-Dec-16	1000	1050	1050	2	2	4.29	4.33	4.33	4.33
20-Dec-16	1000	150	150	2	2	4.33	4.33	4.33	4.33
Total	16,000	6,712.7	6,512.7						

Source: Market Operations Department/DAB

Table 2.6: Auction of 182 Day Capital Notes (million AF)

Start Date	Auction Amount	Amount awarded	Total Bid Amount	No. of total bids	No. of Win Bids	Cut off Rate (%)	Low Bid (%)	Highest Bid (%)	Weighted Avg. (%)
22-Dec-15	750	775	775	4	4	5.12	5.15	5.15	5.14
29-Dec-15	500	380	380	4	4	5.15	5.15	5.15	5.14
5-Jan-16	1000	350	350	3	3	5.14	5.15	5.15	5.15
12-Jan-16	1000	500	500	2	2	5.15	5.15	5.15	5.15
26-Jan-16	500	180	180	2	2	5.15	5.15	5.15	5.15
23-Feb-16	500	300	300	1	1	5.15	5.15	5.15	5.15
8-Mar-16	1000	500	500	2	2				5.15

						5.15	5.15	5.15	
29-Mar-16	500	710	710	3	3	5.15	5.15	5.15	5.15
12-Apr-16	250	200	200	1	1	5.15	5.15	5.15	5.15
19-Apr-16	250	200	200	1	1	5.15	5.15	5.15	5.15
26-Apr-16	250	300	300	2	2	5.15	5.15	5.15	5.15
3-May-16	250	110	110	2	2	5.15	5.15	5.15	5.15
10-May-16	750	500	500	4	4	5.14	5.15	5.15	5.15
17-May-16	750	300	300	3	3	5.15	5.15	5.15	5.15
24-May-16	500	450	450	3	3	5.15	5.15	5.15	5.15
31-May-16	500	200	200	1	1	5.15	5.15	5.15	5.15
7-Jun-16	500	350	350	2	2	5.15	5.15	5.15	5.15
14-Jun-16	750	200	200	1	1	5.15	5.15	5.15	5.15
21-Jun-16	1000	50	50	1	1	5.15	5.15	5.15	5.15
28-Jun-16	750	100	100	1	1	5.15	5.15	5.15	5.15
4-Jul-16	500	600	600	2	2	5.15	5.15	5.15	5.15
12-Jul-16	500	103.4	103.4	1	1	5.15	5.15	5.15	5.15
26-Jul-16	500	153	153	2	2	5.149	5.15	5.15	5.15
2-Aug-16	500	200	200	1	1	5.15	5.15	5.15	5.15
9-Aug-16	750	250	250	2	2	5.15	5.15	5.15	5.15
16-Aug-16	750	100	100	1	1	5.15	5.15	5.15	5.15
23-Aug-16	500	428	428	2	2	5.15	5.15	5.15	5.15
30-Aug-16	500	130	130	1	1	5.15	5.15	5.15	5.15
6-Sep-16	700	800	800	2	2	5.145	5.15	5.15	5.15
27-Sep-16	1200	180	180	1	1	5.15	5.15	5.15	5.15
18-Oct-16	750	254	254	2	2	5.15	5.15	5.15	5.15
25-Oct-16	500	180	180	2	2	5.149	5.15	5.15	5.15
1-Nov-16	200	100	100	1	1	5.15	5.15	5.15	5.15
8-Nov-16	500	190	190	2	2	5.15	5.15	5.15	5.15
15-Nov-16	500	620	620	5	5	5.149	5.15	5.15	5.15

22-Nov-16	720	250	250	3	3	5.15	5.15	5.15	5.15
29-Nov-16	500	80	80	2	2	5.149	5.15	5.15	5.15
6-Dec-16	750	330	330	2	2	5.15	5.15	5.15	5.15
13-Dec-16	1000	1540	1540	2	2	5.13	5.15	5.15	5.15
20-Dec-16	1000	500	500	4	4	5.15	5.15	5.15	5.15
Total	25,070	13,643.4	13,643.4						

Source: Market Operations Department/DAB

Table 2.7: Auction of 364 Day Capital Notes (million AF)

Start Date	Auction Amount	Amount awarded	Total Bid Amount	No. of total bids	No. of Win Bids	Cut off Rate (%)	Low Bid (%)	Highest Bid (%)	Weighted Avg. (%)
22-Dec-15	1000	900	900	4	4	6.68	6.68	6.68	6.68
29-Dec-15	500	59.564	59.564	2	1	6.68	6.68	6.68	6.68
5-Jan-16	500	150	150	2	2	6.68	6.68	6.68	6.68
19-Jan-16	200	282	282	1	1	6.68	6.68	6.68	6.68
26-Jan-16	500	220	220	1	1	6.68	6.68	6.68	6.68
2-Feb-16	250	467.107	300	2	1	6.68	6.68	6.68	6.68
15-Mar-16	250	200	200	1	1	6.68	6.75	6.68	6.68
29-Mar-16	750	1170.8	1170.8	5	5	6.67	6.68	6.68	6.68
5-Apr-16	500	100	100	1	1	6.67	6.67	6.67	6.67
12-Apr-16	1750	1025	1025	2	2	6.67	6.67	6.67	6.67
19-Apr-16	1500	565	565	2	2	6.67	6.70	6.67	6.67
3-May-16	250	600	250	2	1	6.65	6.67	6.65	6.65
10-May-16	250	1080	830	5	5	6.60	6.66	6.65	6.64
17-May-16	1000	2020	2020	2	2	6.65	6.65	6.65	6.65

24-May-16	1000	1070	1070	4	4	6.64	6.65	6.65	6.65
31-May-16	1000	465	465	2	2	6.65	6.65	6.65	6.65
7-Jun-16	1500	1200	1200	3	3	6.65	6.65	6.65	6.65
14-Jun-16	1500	360	360	2	2	6.649	6.65	6.65	6.65
21-Jun-16	750	370	370	2	2	6.62	6.65	6.65	6.65
28-Jun-16	750	25	25	1	1	6.65	6.65	6.65	6.65
19-Jul-16	500	200	200	1	1	6.665	6.665	6.665	6.665
26-Jul-16	1000	70	70	1	1	6.664	6.665	6.664	6.665
2-Aug-16	1000	400	400	2	2	6.665	6.665	6.665	6.665
9-Aug-16	500	1350	1350	3	3	6.64	6.665	6.665	6.665
16-Aug-16	750	250	250	2	2	6.664	6.665	6.665	6.665
23-Aug-16	500	32.5	32.5	1	1	6.665	6.665	6.665	6.665
30-Aug-16	500	405	405	3	3	6.659	6.665	6.665	6.665
6-Sep-16	1700	980	980	2	2	6.664	6.665	6.665	6.665
20-Sep-16	500	550	550	2	2	6.664	6.665	6.665	6.665
27-Sep-16	900	740	740	3	3	6.664	6.665	6.665	6.665
4-Oct-16	500	500	500	1	1	6.65	6.665	6.65	6.66
11-Oct-16	500	130	130	2	2	6.65	6.665	6.665	6.665
18-Oct-16	500	100	100	1	1	6.665	6.665	6.665	6.665
25-Oct-16	500	650	650	2	2	6.662	6.665	6.65	6.663
1-Nov-16	600	200	200	1	1	6.665	6.665	6.665	6.665
8-Nov-16	500	100	100	1	1	6.66	6.66	6.66	6.66
15-Nov-16	750	915	915	5	5	6.66	6.665	6.665	6.665
22-Nov-16	750	815	815	4	4	6.664	6.665	6.665	6.664
29-Nov-16	1000	340	340	3	3	6.664	6.665	6.665	6.665
6-Dec-16	750	40	40	2	2	6.664	6.664	6.665	6.665
13-Dec-16	1000	2330	2330	3	3	6.57	6.665	6.665	6.665
20-Dec-16	1000	1170	1170	4	4	6.6	6.665	6.665	6.665
22-Dec-15	1000	900	900	4	4	6.68	6.68	6.68	6.68
29-Dec-15	500	59.564	59.564	2	1	6.68	6.68	6.68	6.68

5-Jan-16	500	150	150	2	2	6.68	6.68	6.68	6.68
19-Jan-16	200	282	282	1	1	6.68	6.68	6.68	6.68
26-Jan-16	500	220	220	1	1	6.68	6.68	6.68	6.68
2-Feb-16	250	467	300	2	1	6.68	6.68	6.68	6.68
15-Mar-16	250	200	200	1	1	6.68	6.75	6.68	6.68
29-Mar-16	750	1170.8	1170.8	5	5	6.67	6.68	6.68	6.68
Total	31,900	24,596.97	23,829.86						

Source: Market Operations Department/DAB



3

INFLATION TREND AND OUTLOOK

3

INFLATION TREND AND OUTLOOK



By the end of 2016, global commodity market reported higher prices for almost all items. This increase is consistent with higher prices of both, energy and non-energy commodities. With strong gains in all types of fuel, energy price rose by 11 percent compared to the previous quarter. The trend of movement in price of coal was also upward and recorded an increase of 38 percent due to strong demand and weak supply in China as the government decided to decrease its coal capacity. Similarly, Natural gas prices soared 8 percent mainly because of higher demand and outages in production of liquefied natural gas.

Non-energy commodities prices also increased but at a slower pace compared to energy commodities. During the review period, non-energy prices recorded 1 percent increase, which was mainly driven by higher prices of metals. The rate of increase in price of metals is shown 10 percent due mainly to contraction in the supply of zinc and lead in China. However, in non-energy index, grains prices recorded largest decline (4 percent) mainly led by ample production of rice, maize and wheat.¹

¹ World Bank commodity market outlook, January 2017.

In the light of higher prices of commodities in global markets, domestic prices in Afghanistan also increased in the last quarter of the FY 2016.

I. CONSUMER PRICE IN AFGHANISTAN

Consumer Price Index (CPI) in Afghanistan which was previously calculated based on prices of March 2011 is now being compiled on the base prices of April 2015. In this revision, the CPI components are aligned with new weights too.

Afghanistan's headline CPI inflation increased in the fourth quarter of 2016. The year-over-year measure of changes in consumer price index showed an inflation rate of 4.5 percent higher from 0.1 percent observed in the same quarter of the previous year. This increase is in line with higher price of commodities in global markets. Based on the reports, almost all items of the global commodity price index exhibited higher prices over the last quarter of 2016.

Similar to the year-over-year measure, inflation when measured on quarter-to-quarter basis also rose over the period under review. Observing the data, inflation by this measure stood at 2.0 percent slightly higher from 1.6 percent.

Kabul CPI also represented higher inflation rate during the fourth quarter of 2016. Observing the

profile of Kabul headline CPI, inflation turned around to 5.2 percent from -0.6 percent recorded in corresponding quarter of the previous year. On quarter-to-quarter basis, this index slightly increased to 1.7 percent from 1.3 percent.

3.1 Developments in National Headline CPI

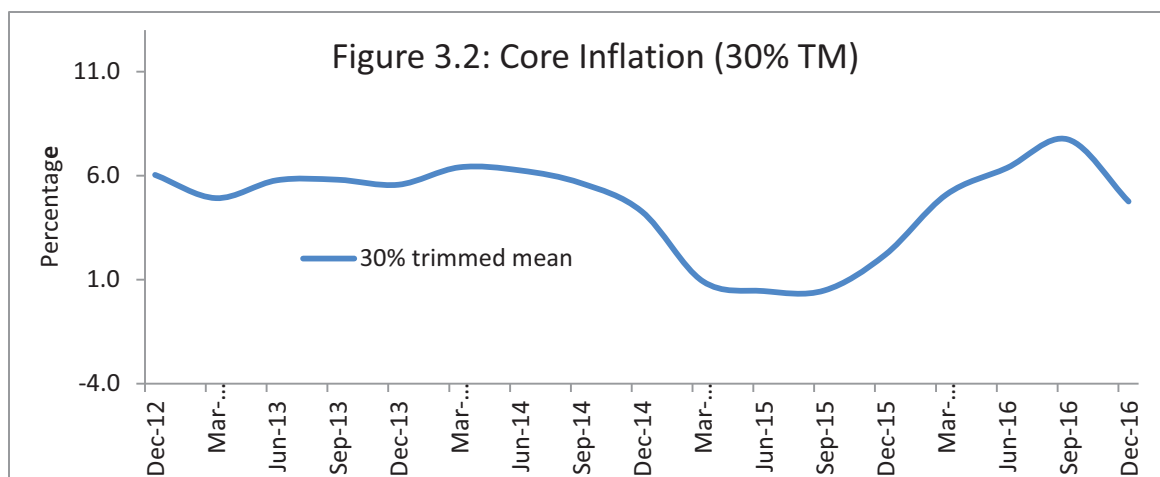
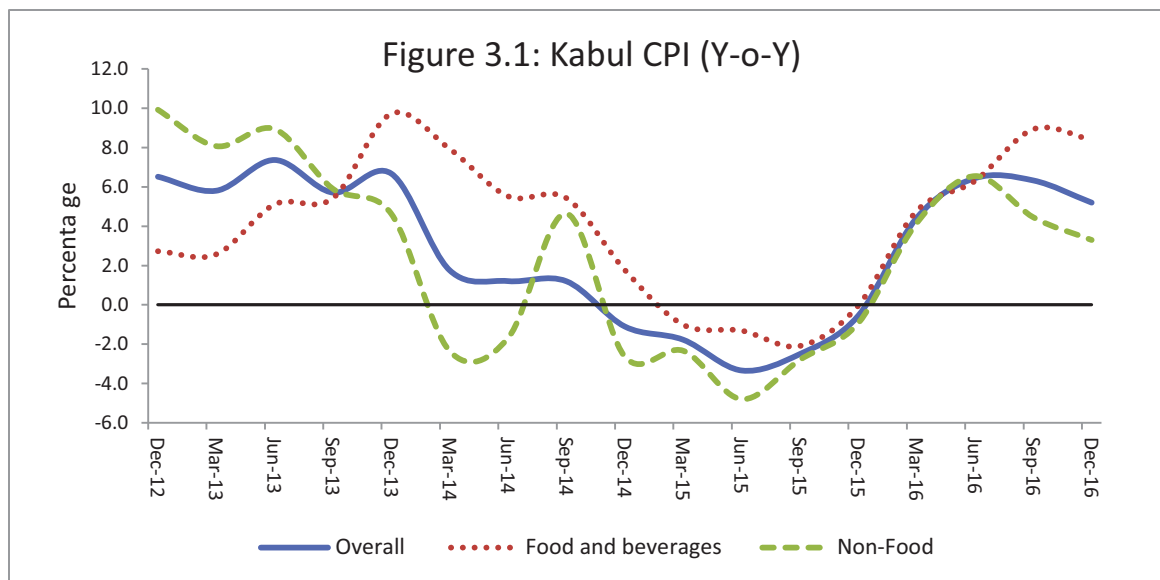
3.1.1 Annual Developments

Consumer price index in the fourth quarter of 2016 represented a significant year-over-year increase. As per the available data, headline inflation by this measure surged up to 4.5 percent from 0.1 percent recorded in the same quarter of the previous year. This increase is on the back of higher inflation in both, food and non-food items. Given that inflation in most sub-components of food item increased, this index jumped up to an inflation rate of 5.8 percent from a deflation rate of 0.3 percent. In the food index, inflationary pressures came from high prices of meat, milk, cheese and eggs; oils and fats; fresh and dried fruits; vegetables; sugar and sweets;

and spices. The highest increase in this item is recorded in price of vegetables index which soared to 11.9 percent from -6.3 percent. On the other hand, during the review period, price index of bread and cereals stood at -0.5 percent lower from 0.5 percent.

In the non-food category, inflation is supported by higher prices of housing, transportation, education, information and culture; and restaurants, while price indices of clothing, furnishing and household goods, health, communication, and miscellaneous declined over the review period. In this item, education price index exhibited the highest increase which rose to 22.8 percent from -5.1 percent.

Core measures of inflation also showed upward movement compared to a year ago. Trimmed Mean, the most common measure of core inflation rose to 4.8 percent from 2.2 percent. In addition, CPI excluding bread and cereals, oil and fats; and transportation strengthened and reached 5.6 percent from 0.5 percent (Y-o-Y).



Source: Central Statistics Organization/Monetary Policy Department staff calculation

Table 3.1: Breakdown of National Headline CPI

(Percent changes year on year)

(March 2011=100)

	Weights	1393				1394				1395			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Overall Index	100.0	5.6	5.6	4.2	1.3	-0.6	-2.8	-1.9	0.1	3.8	5.96	6.9	4.5
Food and beverages	47.8	10.0	9.7	6.8	2.9	-0.6	-3.3	-2.6	-0.3	4.0	6.8	8.3	5.8
Bread and Cereals	14.6	9.5	11.4	11.0	8.0	2.1	-3.4	-2.3	0.5	5.0	7.6	4.0	-0.5
Meat	7.5	2.6	3.4	3.7	3.4	2.4	-0.2	-1.5	0.8	3.2	6.7	11.3	6.1
Milk, cheese and Eggs	4.7	6.5	6.1	2.1	3.4	1.4	1.0	1.5	1.3	2.4	3.1	2.2	2.0
Oils and fats	4.6	1.8	1.7	0.9	-1.7	-6.2	-7.2	-6.5	-6.6	-1.9	3.9	9.8	6.7
Fresh and dried Fruits	5.0	8.5	9.9	9.2	11.5	6.6	7.9	2.0	0.5	3.6	4.9	10.0	4.7
Vegetables	6.0	30.3	24.3	7.1	-9.6	11.7	-15.9	12.4	-6.3	1.9	4.2	13.3	11.9
Sugar and sweets	2.7	2.5	-1.6	-0.2	-1.0	-1.1	0.5	0.4	6.0	11.1	19.9	24.1	20.0
Spices	1.3	10.5	9.4	12.0	5.9	1.0	-1.0	0.3	6.6	13.3	16.9	20.0	33.5
Non-alcoholic beverages	1.4	7.4	3.7	4.0	2.1	1.3	3.1	4.6	5.3	7.9	7.3	6.1	3.7
Non-Food	52.2	1.1	1.4	1.4	-0.5	-0.5	-2.2	-1.2	0.5	3.7	5.0	5.2	3.4
Tobacco	0.3	8.4	3.0	0.6	6.7	7.2	12.8	25.0	22.4	21.8	12.8	13.3	7.9
Clothing	4.6	8.3	8.1	6.9	4.2	2.9	2.0	6.6	8.6	9.9	9.1	7.8	3.2
Housing, Furnishing and Household goods	19.1	-8.5	-9.1	-8.8	-9.7	-4.6	-7.0	-7.4	-6.6	-2.7	1.6	3.4	5.0
Health	11.9	8.5	10.4	10.3	8.4	4.9	2.1	3.3	5.7	9.7	8.9	8.6	1.8
Transportation	6.2	8.8	9.0	10.3	8.5	7.7	7.4	6.9	9.4	9.4	8.7	9.3	4.0
Communication	4.3	16.6	20.1	19.5	11.3	-6.9	-10.0	-7.8	-3.4	2.0	3.0	-0.5	1.2
Information and Culture	1.7	-1.5	-1.4	-2.0	-3.4	-4.7	-3.3	-2.2	-1.3	-0.1	1.5	-0.4	-1.9
Education	1.1	6.5	5.4	7.1	7.0	1.2	3.8	5.2	6.3	6.5	5.2	1.6	-2.4
Restaurants and Hotels	0.4	1.9	5.0	4.0	2.8	2.0	-2.7	-3.7	-5.1	-7.6	9.2	23.2	22.8
Miscellaneous	1.1	2.6	2.4	4.6	3.2	2.2	4.2	-0.8	-0.3	0.7	-3.6	2.0	3.4
core inflation (30% TM)		6.4	6.3	5.6	4.3	0.9	0.5	0.5	2.2	5.1	6.4	7.8	4.8
Core inflation (Headline excl. B&C, O&F and T)		4.3	3.6	1.7	-0.8	-0.4	-1.9	-1.2	0.5	3.9	5.8	8.0	5.6

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

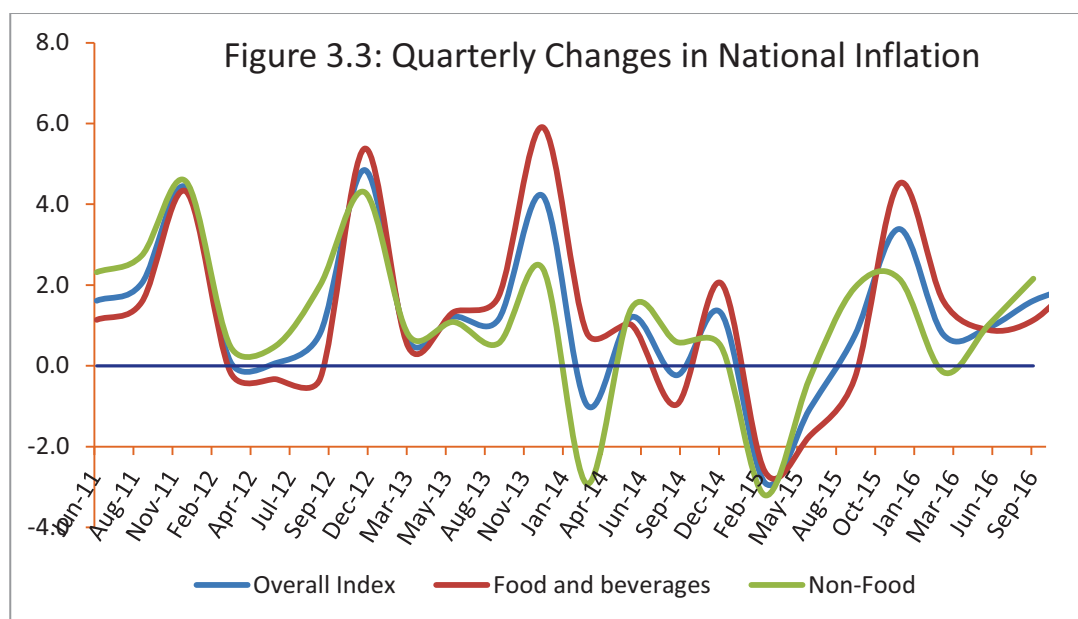
3.1.2 Quarterly Developments in National CPI

The short-term measure of inflation represented a similar trend to annual measure. Nationwide inflation when calculated on quarter-to-quarter basis soared to 2.0 percent from 1.6 percent recorded in the previous quarter. This increase is in line with high inflation in food items, while non-food category showed a lower rate in comparison with the previous quarter.

Over a one quarter period, food inflation picked up to 2.2 percent from 1.1 percent. In this item, price indices of bread and cereals; milk, cheese and eggs; fresh and dried fruits; vegetables; and spices increased while price

indices of meat, sugar and sweets, and non-alcoholic beverages weakened. However, the largest quarterly increase in this category was recorded in vegetables price index, which stood at 11.2 percent significantly higher from -3.4 percent.

Non-food inflation, on the other hand, fell and stood at 1.8 percent from 2.2 percent. All important components of this index recorded lower prices, but the largest decrease is observed in price index of education turning around to -0.4 percent from 11.3 percent.



Source: Central Statistics Organization/Monetary Policy Department staff calculation.

Table 3.2: National Headline CPI (Percent Changes quarter-on-quarter)

March 2011 = 100

	1393				1394				1395			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Overall Index	-1.0	1.2	-0.2	1.3	-2.9	-1.1	0.8	3.4	0.8	0.9	1.6	2.0
Food and beverages	0.8	1.0	-1.0	2.0	-2.6	-1.7	-0.3	4.5	1.6	0.9	1.1	2.2
Bread and Cereals	0.6	4.1	2.7	0.4	-5.0	-1.4	4.0	3.2	-0.7	1.0	0.5	0.8
Meat	0.3	0.7	2.1	0.3	-0.7	-1.9	0.8	2.7	1.7	1.4	5.1	-0.4
Milk, cheese and eggs	1.9	-1.8	0.8	2.5	-0.1	-2.1	1.2	2.4	0.9	-1.4	0.3	3.0
Oils and fats	-0.9	-0.2	-0.1	-0.5	-5.4	-1.3	0.6	-0.5	-0.7	4.6	6.3	1.3
Fresh and dried fruits	6.5	3.4	-1.7	3.1	1.8	4.6	-7.1	1.5	4.9	5.9	-2.5	-1.6
Vegetables	-0.3	-3.0	-	9.7	-2.7	-7.6	-11.2	17.4	5.8	-5.5	-3.4	11.2
			14.7									
Sugar and sweets	-2.1	-2.8	3.3	0.7	-2.3	-1.2	3.3	6.3	2.4	6.7	6.8	0.7
Spices	3.3	2.7	0.3	-0.5	-1.5	0.7	1.7	5.7	4.7	3.9	4.3	10.9
Non-alcoholic beverages	0.5	-0.6	1.9	0.3	-0.3	1.1	3.4	1.0	2.1	0.6	2.3	0.2
Non-Food	-2.9	1.4	0.6	0.5	-3.2	-0.3	1.9	2.2	-0.2	1.0	2.2	1.8
Tobacco	-0.2	2.2	-2.8	7.6	0.3	7.5	7.8	5.4	-0.2	-0.4	8.2	3.6
Clothing	1.2	1.9	-0.2	1.3	-0.1	1.1	4.3	3.2	1.1	0.3	3.0	-0.7
Housing,	-10.3	-0.3	-0.1	1.1	-5.7	-2.8	0.0	1.9	-1.7	1.5	1.7	3.5
Furnishing and household												
Goods	1.8	4.6	1.1	0.7	-1.5	1.7	2.4	3.0	2.3	1.0	2.1	0.0
Health	4.2	2.0	2.5	-0.4	3.4	1.8	2.0	1.9	3.4	1.1	2.5	0.1
Transportation	9.1	3.2	2.4	-3.5	-8.7	-0.2	4.9	1.1	-3.6	0.8	1.2	7.3
Communication	-0.1	-1.3	-1.3	-0.7	-1.4	0.1	-0.3	0.3	-0.3	1.7	-2.1	-0.1
Information and Culture	5.5	-1.0	1.6	0.8	-0.2	1.5	2.9	1.9	0.1	0.2	-0.6	-0.7
Education	1.8	2.4	-0.2	-1.2	1.0	-2.2	-1.3	-2.6	-1.7	15.6	11.3	-0.4
Restaurants and Hotels	0.9	0.4	3.3	-1.5	0.0	2.3	-1.6	-1.0	1.0	-2.1	4.2	0.0
Miscellaneous	1.2	2.8	0.1	3.3	1.0	2.6	3.3	2.2	0.6	1.0	3.4	-0.2

Source: Central Statistics Organization/Monetary Policy Department staff calculation.

3.2 Developments in Kabul CPI

3.2.1 Annual Developments

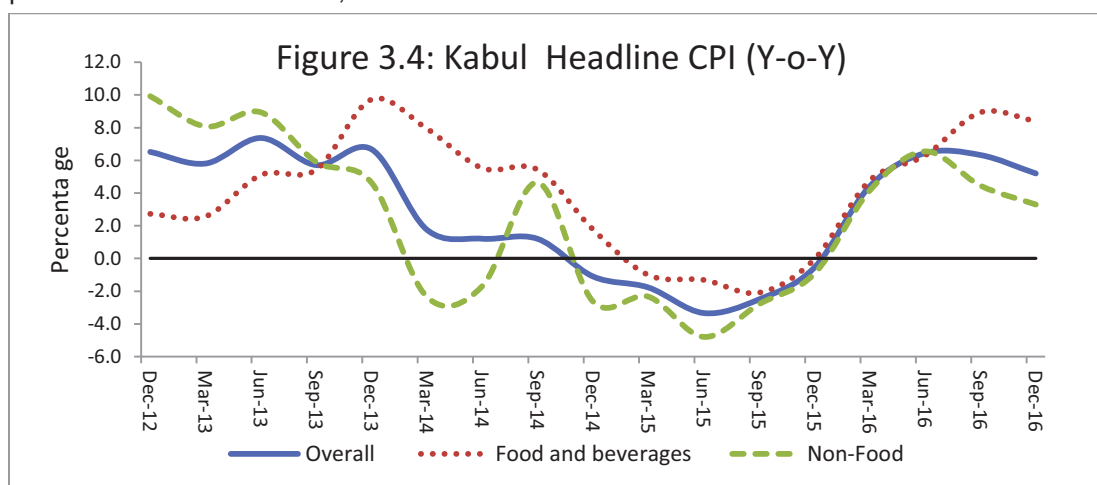
In the last quarter of 2016, Kabul headline inflation increased (Y-o-Y). This increase is driven by higher inflation in both, food and non-food categories of the index. Headline CPI inflation turned around to an inflation rate of 5.2 percent from a deflation rate of 0.6 percent recorded in corresponding quarter of the previous year.

Food items, which account for around 37 percent of the whole CPI, exhibited higher inflation over a one year horizon. In this category, inflationary effects came from higher prices of meat, oils and fats, fresh and dried fruits, vegetables, sugar and sweets, and spices. As a result, food inflation increased to 4.8 percent from 1.0 percent.

Non-food items, comprising around 63 percent of the whole index, increased to 3.3

percent. This figure was calculated at -0.9 percent in the same quarter of the previous year. This increase is mainly attributed to higher prices of housing, electricity, water and gas; health; transportation; education; and restaurants and hotels. In this item, price index of transportation increased most significantly standing at 8.2 percent in the fourth quarter of 2016 from -14.7 percent calculated a year ago.

Inflation when calculated based on core measures also increased. The 30% trimmed mean represented an inflation rate of 8.3 percent in December 2016, which is well higher the rate of 4.7 percent recorded in last quarter of 2015. Meanwhile, CPI excluding bread and cereals, oils and fats, and transportation increased to an inflation rate of 6.3 percent from a deflation rate of 0.1 percent (Y-o-Y).



Source: Central Statistics Organization/ DAB staff calculation.

Table 3.3: Breakdown of Kabul Headline CPI

(Percent changes year on year)

(March 2011=100)

	Weights	1393				1394				1395			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Overall Index	100.0	1.8	1.2	1.2	-1.1	-1.8	-3.3	-2.5	-0.6	4.4	6.4	6.3	5.2
Food and beverages	37.2	7.9	5.5	5.4	1.8	-1.0	-1.3	-2.1	0.0	4.8	6.3	8.9	8.4
Bread and Cereals	9.8	7.7	4.8	6.6	3.0	-1.9	-2.9	-3.2	-0.7	1.1	-0.2	-2.9	-3.1
Meat	6.4	-1.4	-1.4	3.8	2.6	0.5	1.1	0.7	4.3	8.7	12.1	16.6	10.0
Milk, cheese and Eggs	3.2	6.1	9.9	8.7	5.9	2.7	6.1	8.5	7.1	8.1	4.4	3.1	2.8
Oils and fats	3.6	-0.9	-3.1	-5.1	-5.5	-	-7.7	-7.5	-5.5	-3.1	-4.7	4.7	5.4
Fresh and dried Fruits	5.2	6.5	8.8	7.4	12.9	5.1	8.3	3.0	3.1	9.7	9.1	13.7	8.4
Vegetables	4.2	24.7	15.8	8.9	-5.6	-2.3	-	-	-	-3.0	3.2	14.8	18.6
Sugar and Sweets	2.8	-0.5	-6.9	-3.5	-5.1	-2.8	1.4	2.6	13.9	26.9	39.3	40.4	31.8
Spices	1.0	8.3	7.0	9.2	7.2	1.4	3.6	9.3	19.8	30.0	35.1	33.3	25.3
Non-alcoholic Beverages	0.9	7.8	2.1	2.6	3.2	-0.8	3.0	5.3	9.5	11.6	13.6	12.0	5.2
Non-Food	62.8	-2.4	-1.7	-1.6	-3.1	-2.3	-4.8	-2.8	-0.9	4.2	6.5	4.5	3.3
Tobacco	0.3	11.2	13.3	11.5	15.5	12.9	9.1	22.6	20.1	20.8	17.1	9.1	10.4
Clothing	4.8	7.8	11.5	11.3	10.3	5.6	0.8	9.8	13.8	17.8	16.7	11.4	3.4
Housing, Electricity, water and gas	23.5	-	-	-	-	-5.5	-8.8	-9.9	-9.6	-4.7	1.7	1.0	4.7
Furnishing and Household goods	17.6	6.2	13.4	13.2	12.5	7.2	3.9	8.5	14.0	19.8	15.4	9.9	1.2
Health	5.3	7.8	7.3	8.7	4.1	4.1	3.5	0.2	0.3	1.7	0.9	1.4	3.2
Transportation	4.6	33.3	33.2	32.1	19.4	-	-	-7.4	-3.4	8.2	9.2	-0.5	2.4
Communication	2.0	-0.8	-2.2	-4.0	-5.0	-5.7	-3.6	-1.6	-0.2	0.3	0.0	0.1	-0.8
Information and Culture	0.7	14.0	14.6	19.1	18.3	1.8	5.6	6.8	9.8	11.7	8.1	1.9	-3.2
Education	1.7	-0.1	2.8	1.9	2.1	1.6	-3.8	-5.8	-7.3	-9.7	11.4	29.7	31.6
Restaurants and	1.0	1.5	2.3	5.2	3.1	1.7	5.5	-0.6	0.0	2.2	-7.4	0.8	1.5

Hotels													
Miscellaneous	1.3	4.3	7.9	3.8	5.0	4.5	8.3	17.8	17.9	19.1	12.5	14.9	11.4
Core inflation (30% TM)		5.3	5.7	6.2	4.4	0.7	1.2	1.9	4.7	8.4	8.5	8.2	8.3
Core inflation (Headline excl. B&C, O&F and T)		-1.3	-1.3	-3.8	-3.1	-1.0	-2.3	-1.6	-0.1	5.4	8.5	9.4	6.3

Source: Central Statistics Organization/Monetary Policy Department staff calculation.

*Afghanistan's financial year (Dec to January) began from 1391, therefore includes 3 quarters.

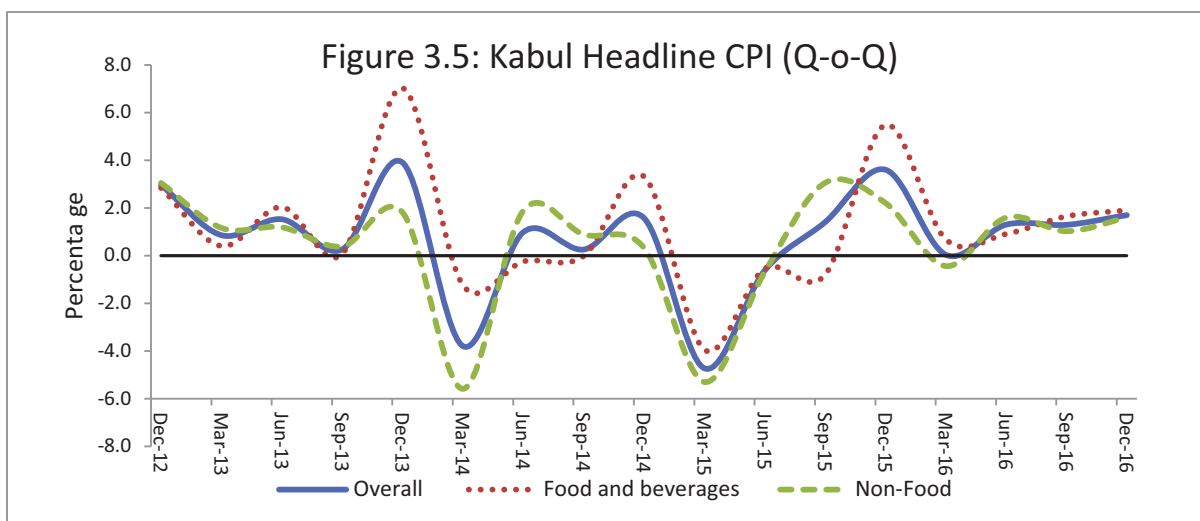
3.2.2 Quarterly Developments, Kabul CPI

By the end of 2016, the quarter-to-quarter measure of inflation in Kabul moved upward, which reflects higher inflation in both, food and non-food items of the CPI. Headline inflation soared to 1.7 percent from 1.3 percent.

The trend of movement in food sub-index was increasing as it rose to 1.9 percent compared to 1.6 percent observed in the previous quarter. In this item, prices of fresh and dried fruits, vegetables, and spices increased, which led to higher food inflation. The highest increase in this item is seen in price index of vegetables which turned around to 15.3 percent from -3.6 percent. On the other hand, price indices of bread and cereals; meat; milk, cheese and eggs; oils

and fats; sugar and sweets; and non-alcoholic beverages decreased (quarter-to-quarter).

Non-food category of the CPI also contributed to high inflation during the fourth quarter of 2016. Inflation in this item strengthened and reached 1.6 percent compared to 1.0 percent recorded in the previous quarter. The increase in non-food inflation is mainly driven by high prices of housing, transportation, and information and culture, among which the largest increase is observed in transportation price index. This item rose to 6.2 percent from 1.5 percent (Q-to-Q). In contrast, price indices of clothing, furnishing and household goods, health, communication, education, restaurants and hotels, and miscellaneous lowered during the review period.



Source: Central Statistics Organization/ DAB staff calculation.

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

(Percent changes quarter-on-quarter)

(March 2011=100)

	1393				1394				1395			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Overall Index	-3.8	1.0	0.3	1.6	-4.7	-0.6	1.4	3.6	0.0	1.3	1.3	1.7
Food and beverages	-1.2	-0.2	0.0	3.3	-3.9	-0.5	-0.8	5.5	0.7	0.9	1.6	1.9
Bread and Cereals	-2.8	2.0	5.1	-1.1	-7.4	1.0	4.8	1.4	-5.8	-0.3	1.9	0.9
Meat	-0.5	-2.5	4.4	1.3	-2.6	-1.9	3.9	4.9	1.5	1.2	8.1	0.7
Milk, cheese and eggs	2.0	-1.5	2.5	3.0	-1.1	1.7	4.7	1.6	-0.1	-1.8	3.4	1.2
Oils and fats	-2.6	-1.6	-0.8	-0.6	-9.9	3.9	-0.5	1.5	-7.7	2.2	9.3	1.8
Fresh and dried fruits	9.9	5.1	-4.5	2.3	2.3	8.3	-9.2	2.4	8.9	7.7	-5.3	-4.3
Vegetables	-6.6	-3.9	11.0	18.2	-3.4	11.7	13.4	19.8	5.9	-6.0	-3.6	15.3
Sugar and sweets	-5.2	-5.6	6.0	0.0	-3.0	-1.5	7.3	11.1	8.1	8.1	8.1	1.5
Spices	3.1	0.9	1.8	1.1	-2.4	3.2	7.4	10.8	5.8	7.2	6.0	6.8
Non-alcoholic beverages	2.0	-2.6	2.3	1.5	-2.0	1.2	4.6	5.5	-0.1	3.0	3.2	-1.2
Non-Food	-5.6	1.9	0.5	0.3	-5.3	-0.7	3.1	2.2	-0.4	1.6	1.0	1.6
Tobacco	1.9	7.4	0.5	5.0	-0.4	3.8	12.9	2.8	0.2	0.7	5.1	5.3
Clothing	2.2	5.2	-0.1	2.6	-2.2	0.5	8.8	6.4	1.2	-0.4	3.9	-1.4
Housing	-	0.1	-0.1	0.6	-6.9	-3.4	-0.4	0.9	-1.9	3.1	-1.1	3.9
Furnishing and household goods	14.0	1.4	8.2	1.3	1.3	-3.3	4.8	5.8	6.4	1.6	0.9	0.8
Health	1.6	0.8	3.7	-2.0	1.7	0.2	0.4	-2.0	3.1	-0.6	0.9	-1.2
Transportation	21.9	0.5	1.7	-4.1	-	-0.4	11.4	0.0	-2.4	0.5	1.5	6.2
Communication	-0.1	-2.1	-1.9	-1.0	-0.8	0.1	0.1	0.4	-0.3	-0.2	0.2	0.0

Information and Culture	14.0	-0.3	3.6	0.5	-1.9	3.4	4.8	3.2	-0.2	0.1	-1.2	-0.5
Education	1.0	2.0	0.1	-1.1	0.5	-3.3	-1.9	-2.8	-2.0	19.2	14.2	-0.5
Restaurants and Hotels	1.5	0.8	2.9	-2.0	0.0	4.6	-3.1	-1.3	2.2	-5.2	5.4	-0.6
Miscellaneous	0.4	3.2	-1.9	3.3	-0.1	7.0	6.8	3.4	0.9	1.0	9.0	-1.4

Source: Central Statistics Organization/Monetary Policy Department staff calculations

*Afghanistan's financial year (Dec to January) began form 1391, therefore includes 3 quarters

II. NEAR TERM INFLATION OUTLOOK

The near-term outlook of inflation is likely to be upward. The central bank forecasts inflation rate to increase in the first half of 2017. The prospects will be subject to a course of factors. First, inflation in Afghanistan will get intensive effects from increasing prices of commodities in global markets. Energy prices are projected to increase by around 26 percent in 2017. In the meantime, these projections for non-energy prices show a 3 percent increase in 2017².

Second, repatriation of refugees also remains an important factor in determining inflation in 2017. During the previous year, an approximate number of 1.5 million Afghans returned to Afghanistan. It is expected that a similar number may return in 2017 too³, which forms around 5 percent of the total population. This will definitely increase the aggregate demand in the market and lead to higher inflation.

² World Bank commodity market outlook, January 2017.

³ UNAMA- Population movement outlook, January 2017.



4

EXTERNAL SECTOR DEVELOPMENT

4

EXTERNAL SECTOR DEVELOPMENTS

The highlights of some major developments in the external sector of the Afghanistan economy for the FY 1395 in comparison with the previous year are captured in this report. The available data reveals that the external sector improved further benefiting from modest growth in exports of goods, sustained decline in imports of goods and enhanced inflows in the current transfers (grants). A substantial increase in the current transfers and earnings from exports of goods helped offset expenditure on imports to a sizable extent. These developments, together with an increase of workers' remittances and income inflows helped to reduce the external current account deficit by 20 percent to USD 3,771.83 million in the FY 1395 compared to a deficit of USD 4,720.68 million in the FY 1394.

Inflow to the capital account decreased on account of inflows (capital transfers) to the government sector.

Foreign Direct Investment (FDI), net inflows declined while net Portfolio Investment increased during the year under review.

In the same vein, BOP recorded a deficit of USD 3,022.23 million in the FY 1395 compared

to the deficit of USD 2,908.20 million in the FY 1394.

The official reserve assets rose to USD 641.28 million in the FY 1395 compared to USD 258.45 million in the FY 1394.

I. BALANCE OF PAYMENTS

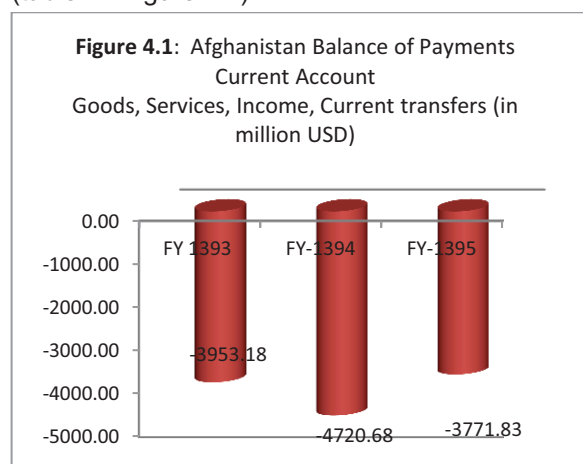
4.1.1 Current Account Balance

Current account deficit (CAD) of the balance of payments narrowed by 20 percent due to lower trade deficit in the FY 1395 which was mainly driven by a significantly decline in merchandise imports relative to exports and increased inflows from current transfers (grants). Based on available data, current account posted a deficit of USD 3,771.83 million in the FY 1395, compared with a deficit of USD 4,720.68 million recorded in the FY 1394. Further analysis reveals that imports of goods declined by 13 percent to USD 6,149.31 million in the FY 1395 from USD 7,033.71 million in the FY 1394. On the other hand, earnings from exports of goods grew by 7 percent to USD 619.12 million in the FY 1395 from USD 579.99 million in the FY 1394. The

export earnings were largely driven by food items (fresh and dry fruit) which accounted for 44 percent of total exports and medical seeds which accounted for 39 percent of the total exports.

The deficit in the services account rose by 8 percent to USD 790.76 million in the FY 1395 from USD 733.06 million in the previous year. This could be attributed to addition in out-payments in respect of transportation services. The surplus in the income account declined by 71 percent to USD 51.72 million in the FY 1395 from USD 179.96 million recorded in the FY 1394.

Also, current transfers' surplus which was largely influenced by grants and worker personal home remittances from foreign countries grew by 9 percent to USD 2,497.40 million in the FY 1395 from USD 2,286.13 million when compared with previous year (table 4.1 figure 4.1).



Source: CSO/DAB staff calculations

4.1.2 Capital Account

The capital account of the balance of payments illustrated a decline of 6 percent in the FY 1395 when compared to the FY 1394, as a result of lower inward capital transfers.

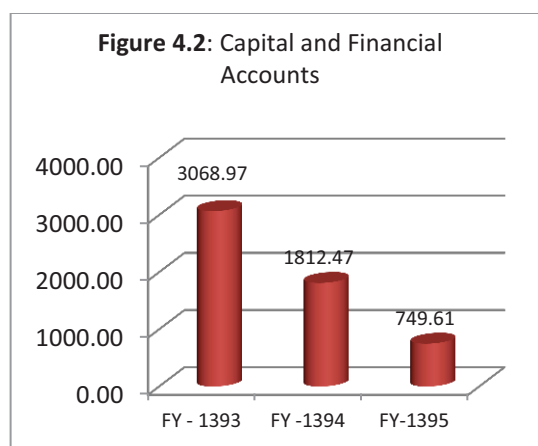
Net inflows to the capital account dropped from USD 1,507.48 million in the FY 1394 to USD 1,418.13 million in the FY 1395. This was mainly due to net capital transfers received by the government, corporations and households which reduced to USD 1,425.82 million in the FY 1395 from USD 1,534.07 million recorded in the previous year.

Financial Account

Financial account of the BOP recorded a net inflow of USD 668.53 million in the FY 1395 while in the previous year it indicated a net outflow of USD 304.99 million (figure 4.2 table 4.2).

Further analysis reveals that the country's aggregate financial assets abroad increased to USD 36.73 million in the FY1395 compared to USD 27.12 million recorded in the FY 1394.

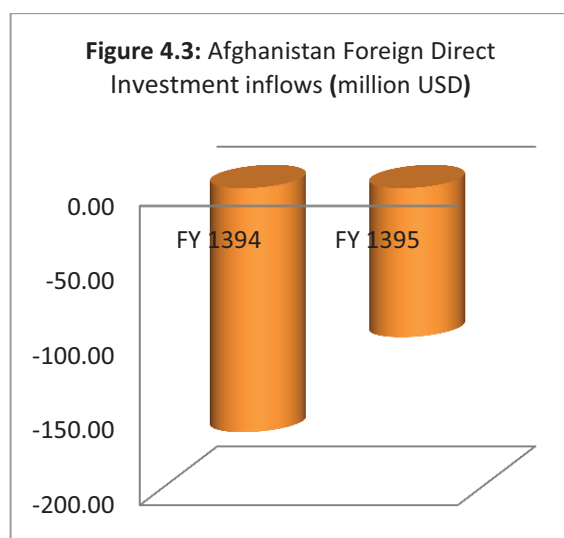
Likewise, the aggregate financial liabilities, decreased to USD 1 million in the FY 1395 from USD 7.89 million recorded in the FY 1394, as a result of lower financial inflows occasioned by the insecurity challenges, that affected both FDI and portfolio investments.



Source: CSO/DAB staff calculations

4.1.3: FDI and Portfolio Inflow

Based on the available data, the total foreign direct investment (FDI) related inflows amounted to USD 99.61 million in the FY 1395 in comparison with USD 163.06 million recorded in the FY 1394. At the same time, portfolio investment inflows increased to USD 90.85 million in the FY 1395 from USD 81.51 million which was recorded in the FY 1394.



Source: CSO/DAB staff calculations

4.1.4 Merchandise Trade

Merchandise This part of the report presents an analysis of the Afghanistan's merchandise trade performance in the FY 1395 and compares them with trade performance in the FY 1394.

In the year under review, the external trade deficit was recorded at USD 5,805.51 million, showed a decline of 19 percent in comparison with USD 7,123.38 million recorded in the FY 1394 (Figure 4.4, Table 4.3).

Aggregate exports increased by 10 percent to USD 613.80 million in the FY 1395, higher than USD 555.71 million recorded in the FY 1394. Leather and wool, food items and medical seeds exports showed an upward trend, while carpet and rugs exports declined in the FY 1395. Exports of leather and wool which accounted for about 9 percent of total exports (USD 55 million) reflected 93 percent increase in the FY 1395. Export of food items (fresh and dry fruit) which accounted for about 44 percent of the total exports increased by 28 percent to USD 269.91 million in the FY 1395 from USD 210.17 million in the FY 1394. Similarly exports of medical seeds which accounted for about 38 percent of the total exports increased by 13 percent to USD 236.38 million in the FY 1395 from USD 208.76 million in the FY 1394. Meanwhile, exports of carpet and rugs which constitute 8.6 percent of the total exports declined significantly by 52 percent to USD 52.51 million in the FY 1395 from USD 108.31 million in the FY 1394.

At the same time, aggregate imports declined by 16 percent to USD 6,419.31 million in the FY 1395 compared to a value of USD 7,679 million recorded in the previous year.

The major contribution of decline in total imports came from lower imports of fuel and lubricants, industrial supplies and capital goods. Imports of fuel and lubricants, declined largely on account of lower volumes imported in the FY 1395. Imports of fuel and lubricants which accounted for approximately 16.8 percent of total imports reported USD 1,078.73 million, reflecting 36 percent decrease in the FY 1395. Imports of Industrial supply which accounted for about 8 percent of the total imports decreased by 24 percent to USD 536.74 million in the FY 1395 from USD 709.19 million in the last year. Similarly, imports of capital goods which accounted for about 45 percent of the total imports declined by 18 percent to USD 2,936.75 million in the FY 1395 from USD 3,566.07 million in the FY 1394.

II. DIRECTION OF TRADE

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

According to the available merchandise statistics, **Pakistan continued to be the largest buyer of Afghanistan's exports.** The share of Afghanistan's total exports to Pakistan increased to 47.54 percent in the FY 1395 from 40.19 percent in the FY 1394. The value of total

export to Pakistan increased to USD 291.77 million in the FY 1395 from USD 223.37 million in the FY 1394, registering 31 percent increase in exports over the year 1395. Export of leather and wool, food items such as (fresh and dry fruit and oil seeds) and medical seeds to Pakistan increased by 173%, 107% and 42% respectively in the FY 1395 while exports of carpet and rugs to Pakistan declined by 48 percent in the reporting year.

India ranked the second largest buyer of Afghanistan's exports. The share of exports to India increased to 32.19 percent in the FY 1395 from 30.43 percent recorded in the FY 1394. The value of total exports to India increased to USD 197.60 million in the FY 1395 from USD 169.08 million in the FY 1394, escalating by 17 percent.

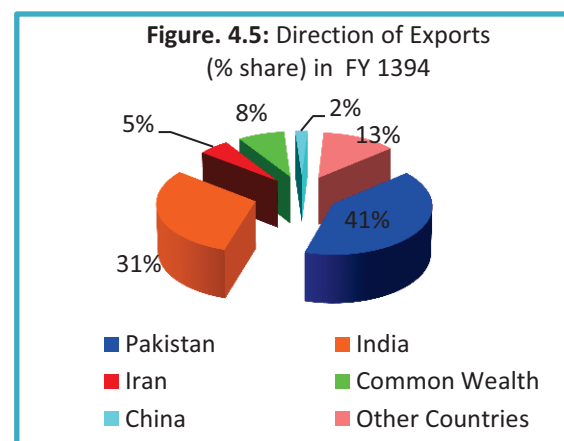
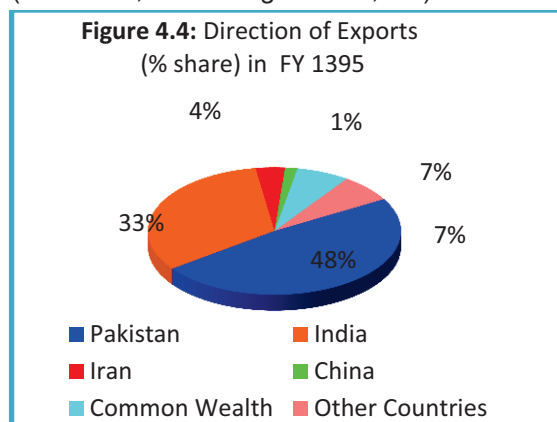
Export of food items and medical seeds to India increased by 18 and 17 percent respectively in the FY 1395. While exports of leather and wool showed 78 percent decreases in the FY 1395.

The third largest buyer of Afghanistan's exports is Commonwealth of Independent State (CIS) countries. The share of Afghanistan's exports to CIS countries dropped to 6.67 percent in the FY 1394 from 7.94 percent recorded last year.

The Earnings from exports from CIS countries dropped by 7 percent to USD 40.95 million in the FY 1395 from USD 44.31 million in the previous year.

The major exporting items to CIS countries were fresh fruits which accounted for about 6

percent of total exports in the year under review (tables 4.4, 4.5 and figures 4.5, 4.6).



CIS countries were the largest import origin of Afghanistan in the FY 1395. Total Imports from CIS countries decreased to USD 1,320.70 million with share of 20.57 percent from USD 1,581 million with share of 20.59 percent, registered 16 percent reduction in total imports. The main imports from CIS countries were consumer goods which accounted for 8 percent, capital goods accounted for 5 percent, petroleum oil accounted for 5 percent and industrial supplies such as metal products and

fertilizer which accounted for 3 percent of total imports in the FY 1395.

Iran was the second largest source of imports for Afghanistan during the FY 1395.

The share of imports from Iran decreased to 20.19 percent in the FY 1395, from 22.69 percent recorded in the last year.

The value of total imports from Iran also declined to USD 1,296.26 million from USD 1,742.18 million, registered 26 percent reduction in the FY 1395. The major importing products from Iran were petroleum oil, capital goods and industrial supplies which accounted for about 10%, 7% and 3% of total imports in the FY 1395.

Pakistan is the third largest import sourcing country to Afghanistan in the FY 1394. The shares of imports from Pakistan in the total imports increased from 18.13 to 20 percent in the FY 1395. But in terms of value, total imports from Pakistan declined to USD 1,285.26 million from USD 1,391.99 million, registered a reduction of 8 percent in the FY 1395.

Main import components from Pakistan include consumer goods, industrial supplies, capital goods products and petroleum oil.

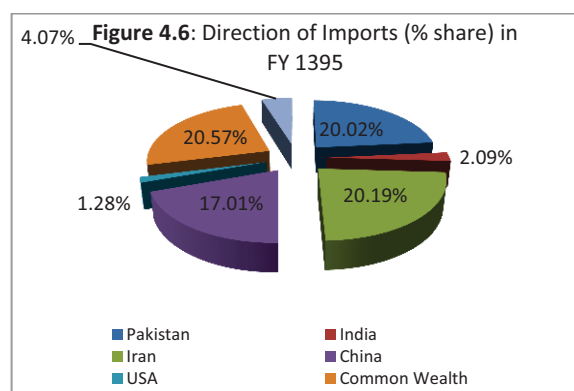
China is the fourth largest import origin to Afghanistan in the FY 1395. The share of imports from China increased to about 17 percent in the FY 1395 from 14.21 percent in the FY1394. But in terms of value, the total imports from China remain unchanged (USD

1091.85 million). The main imports from China were capital goods (spare parts) and consumer goods which accounted for 10 and 7 percent of total imports respectively.

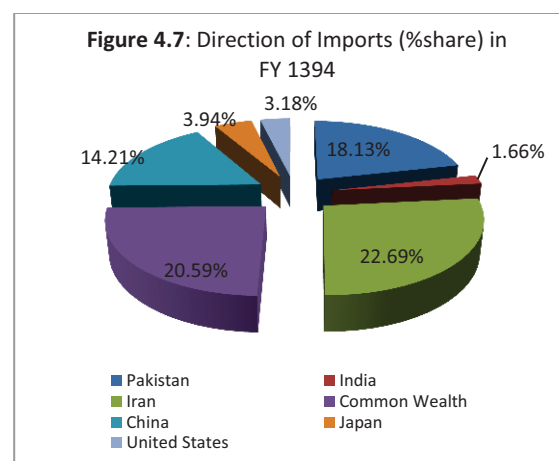
Japan, India, and USA were the fifth, sixth and seventh largest import sources for Afghanistan, accountable for 4 percent, 2 percent and 1 percent of total imports respectively. However, total imports from Japan dropped by 14 percent to USD 261.33 million in the FY 1395 from USD 203.27 million in the FY 1394, due to lower imports of capital goods and consumer goods in the FY 1395.

Imports from India grew by 5 percent to USD 134.16 million from USD 127.25 million. The major imports from India were sugar, fabrics, medicines, cigarettes and threads.

Imports from USA declined significantly by 66 percent to USD 81.93 million in the FY 1395 from USD 244.54 million due to lower imports of capital goods (spare parts), medicines and threads in the FY 1395 (tables 4.4, 4.5 and figures 4.6, 4.7).



Source: CSO and DAB staff calculations



Source: CSO/DAB staff calculations

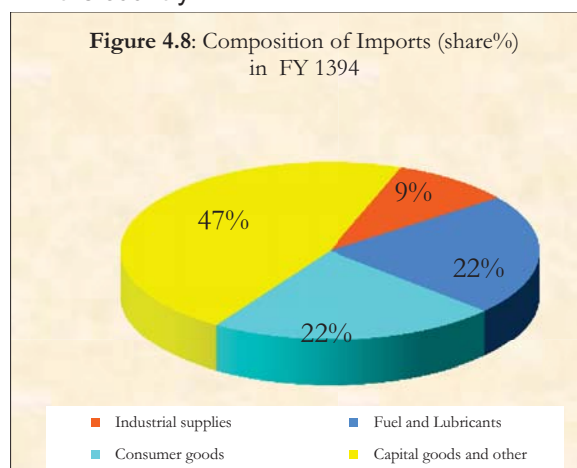
III. COMPOSITION OF TRADE

4.3.1. Composition of Imports

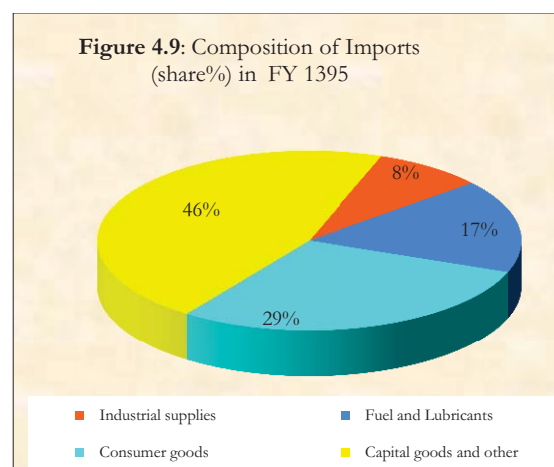
The composition of imports in the FY 1395 indicates that;

- ✓ Imports of Capital goods had the largest share of 45.7 percent in the basket of imports despite its value declined by 18 percent to USD 2,936.75 million in the FY 1395 from USD 3,566.07 million recorded in the previous year.
- ✓ The second largest share recorded for consumer goods in the basket of imports during the FY 1395. Share of consumer goods increased to 29.1 percent from 22.3 percent. In terms of value, imports of such goods in total imports increased to USD 1,867.36 million in the FY 1395 from USD 1,715.25 million in the FY 1394.

- ✓ Imports of fuel and lubricants (petroleum oil) had the third largest share in the basket of Afghanistan's imports which is decreased from 22 percent in the FY 1394 to 16.8 percent in the reporting year. In terms of value, imports of such item in total imports significantly dropped by 36 percent to USD 1,078.73 million in the FY 1395 from USD 1,688.58 million in the FY 1394.
- ✓ Industrial supplies had the smallest share in the basket of Afghanistan's imports during the year under review. The share of industrial supplies in total imports dropped to 8.4 percent in the FY 1395 from 9.2 percent in the FY 1394. The value of imports of industrial supplies also declined by 24 percent, to USD 536.47 million in the FY 1395 from USD 709.19 million in 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.



Source: CSO and DAB staff calculations



Source: CSO and DAB staff calculations

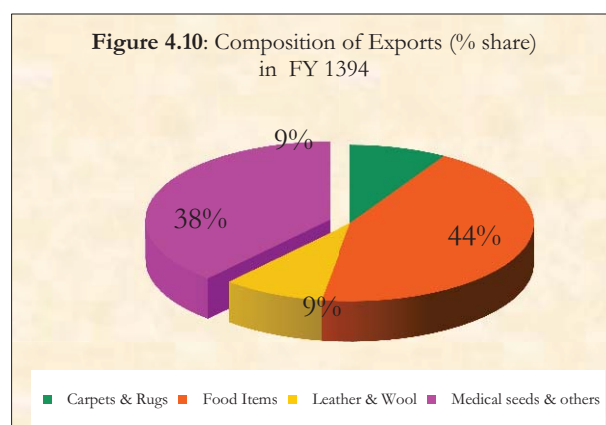
4.3.2. Composition of exports

The Composition of exports in the FY 1395 reveals that;

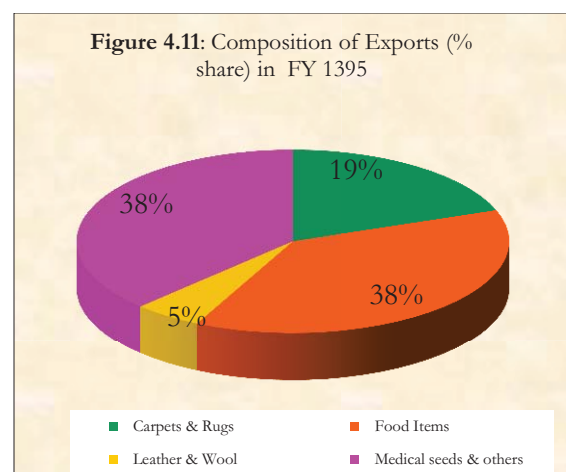
- ✓ Exports of food item had the largest share in the basket of Afghanistan's exports. The share of food item in the total exports recorded 44 percent increase in the FY 1395 from 37.8 percent recorded in the FY 1394.
- In term of value, exports of food items (oil seeds, fresh and dry fruits) increased by 28 percent to USD 269.91 million in the FY 1395 from USD 210.17 million in the previous year.
- ✓ The second largest share in total exports was recorded for medical seeds which increased to 38.5 percent in the FY 1395 from 37.6 percent recorded in the FY 1394. In term of value, exports of medical seeds in total exports increased by 13 percent to USD 236.38 million in the FY 1395 from USD 508.76 million in the FY 1394.

- ✓ Leather and wool had the third largest share in total exports which increased to 9 percent in the FY 1395 from 5 percent recorded in the FY 1394. The value of such goods increased significantly by 93 percent to USD 55 million in the FY 1395 from USD 28.47 million in the FY 1394.
- ✓ Carpet and rugs, which are considered the main component of Afghanistan's exports in the past decades, had the smallest share in basket of Afghanistan's exports. Furthermore, the share of carpet and rugs declined from 19.5 percent in the FY 1394 to 8.6 percent in the FY 1395.

Earnings from export of carpet and rugs also declined by 52 percent to USD 52.51 million in the FY 1395 from USD 108.31 million that recorded in the last year.



Source: CSO and DAB staff calculations



Source: CSO and DAB staff calculations

IV. EXTERNAL DEBT

Afghanistan's total external debt slightly decreased by almost 2 percent to USD 2,081.28 million in the FY 1395 from USD 2,130.06 million in the FY 1394, indicating a reduction of USD 48.79 million. 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 were made to the World Bank, Asian Development Bank, Islamic Development Bank, International Monetary Fund (IMF), and Bulgaria. On the other hand, service charges were paid to the World Bank, Asian Development Bank and Islamic Development Bank.

Meanwhile, the World Bank, a major multilateral creditor to Afghanistan, made some debt

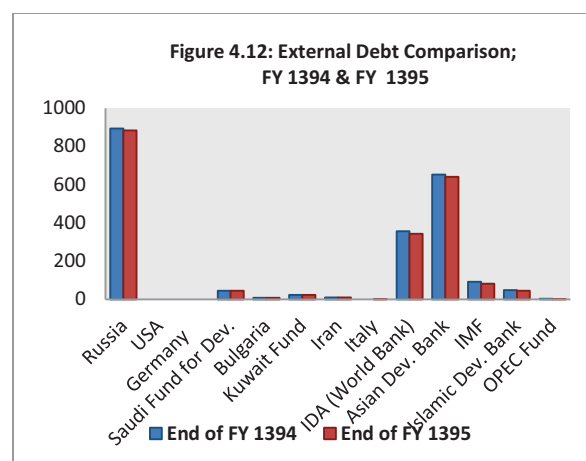
forgiveness on principal and services, and Asian Development Bank made some debt release only on service charges during the year under review.

The total loan amounts payable to the Paris Club creditors in the FY 1395 stood at USD 884.70 million which is payable to Russian federation.

In other words, Afghanistan's total debt from the Paris club members stands at about 42.51 percent of total current external debt which has decreased slightly by about 1 percent compared to the preceding year.

Furthermore, total debt from Non-Paris Club members including Saudi Fund for Development, Bulgaria, Kuwait fund and Iran remained unchanged at USD 84.21 million during the year under review.

On the other hand, total debt from multilateral creditors to Afghanistan decreased to USD 1,112.36 million from USD 1,150.89 million which shows USD 38.53 million reduction in the total debt from multilateral creditors during the reporting year.



Source: CSO and DAB staff calculations

V. NET INTERNATIONAL RESERVES

According to the latest available data, the Net International Reserves (NIR) increased by 5.88 percent standing at USD 6,821.90 million in the FY 1395, up from USD 6,443 million recorded in the last year. The increase in the level of NIR was mainly due to the increase in reserve assets which extended by 8 percent to USD 7,541.02 million in the FY 1395 from USD 6,965.81 million in the FY 1394.

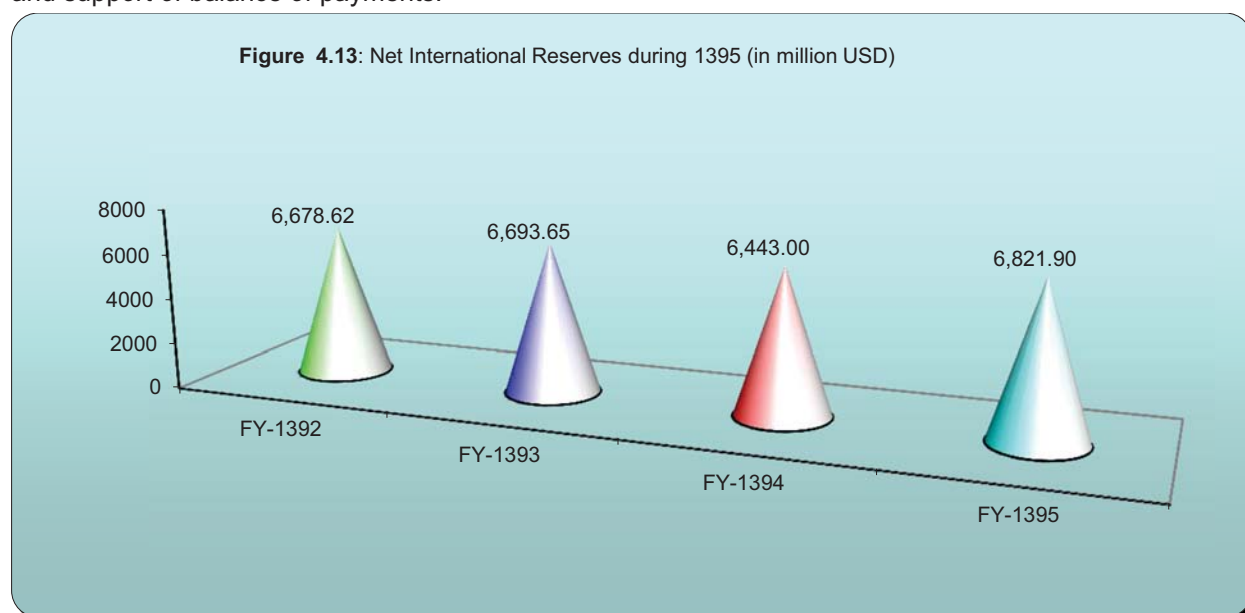
Likewise, reserve liabilities increased by 37.55 percent to USD 719.13 million in the FY 1395 from USD 522.80 million that was recorded in the FY 1394; this demonstrates that the reserve assets are higher than the reserve liabilities. The incensement in reserve liabilities is mainly attributed to the commercial banks deposits in foreign currency which boosted up by 49 percent to USD 647.68 million from USD 433.57 million in the reporting year.

The use of fund resources decreased to USD 71.31 million in the FY 1395 from USD 89.10 million in the FY 1394 recording 20 percent decline. The reserve liability of nonresident deposits in foreign currency almost remained unchanged in the reporting year.

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.

Currently, Net International Reserves (NIR) on average supports almost 13 months of imports while countries with 6 months coverage of imports enjoy a relatively comfortable reserve position.

Table 4.7 and Figure 4.14 represent the Net International Reserves (NIR) of Afghanistan for the past few periods.



Source: CSO and DAB staff calculations

Table 4.1: Current Account Balance (in million USD)

Item/ period	FY - 1393	FY -1394	FY-1395
Capital and financial A/c	3068.97	1812.47	749.61
Capital account	2541.15	1507.48	1418.13
Capital transfers	2574.54	1534.07	1425.82
Financial account	527.82	-304.99	668.53
Reserve Assets	352.47	-258.45	641.28

Source: CSO/DAB staff calculations

Table 4.2: Merchandise Trade (in million USD)

Years	FY 1391		FY 1392		FY 1393		FY 1394		FY - 1395	
	<i>Total</i>	<i>Share (%)</i>	<i>Total</i>	<i>Share (%)</i>	<i>Total</i>	<i>Share (%)</i>	<i>Total</i>	<i>Share (%)</i>	<i>Total</i>	<i>Share (%)</i>
Imports	6,419.67	100%	9,339.60	100%	7,294.63	100%	7,679.09	100%	6,419.31	100%
Industrial supplies	969.88	15.1%	1,272.14	13.6%	863.19	11.8%	709.19	9.2%	536.47	8.4%
Fuel and Lubricants	1,083.65	16.9%	2,167.37	23.2%	1,155.94	15.8%	1,688.58	22.0%	1,078.73	16.8%
Consumer goods	1,255.48	19.6%	1,942.85	20.8%	2,345.86	32.2%	1,715.25	22.3%	1,867.36	29.1%
Capital goods and other	3,110.66	48.5%	3,957.24	42.4%	2,930	40.2%	3,566.07	46.4%	2,936.75	45.7%
Exports	261.63	100%	499.81	100.0%	620.88	100%	555.71	100%	613.80	100%
Carpets & Rugs	8.43	3%	85.49	17.1%	87.0	14.0%	108.31	19.5%	52.51	8.6%
Food Items	104.23	40%	175.92	35.2%	272.13	43.8%	210.17	37.8%	269.91	44.0%
Leather & Wool	26.82	10%	59.54	11.9%	49.35	7.9%	28.47	5.1%	55.00	9.0%
Medical seeds & others	122.15	47%	178.86	35.8%	212.36	34.2%	208.76	37.6%	236.38	38.5%
Trade Balance	-		-8,839.79		-		-		-	
	6,158.04				6,673.75		7,123.38		5,805.51	
Trade Balance as % of GDP	-31%		-43%		-31%		-33%			

Source: CSO/DAB staff calculations

Table 4.3: Direction of External Trade FY 1395 (in million USD)

<i>Country Name</i>	<i>Exports</i>	<i>% Shares</i>	<i>Imports</i>	<i>% Share</i>	<i>Trade Balance</i>
Pakistan	291.77	47.54%	1285.26	20.02%	-993.49
India	197.60	32.19%	134.16	2.09%	63.44
Iran	22.60	3.68%	1296.26	20.19%	-1273.66
Germany	3.57	0.58%	28.19	0.44%	-24.62
China	9.51	1.55%	1,091.85	17.01%	-1082.34
England		0.00%	9.18	0.14%	-9.18
Saudi Arabia	5.59	0.91%		0.00%	5.59
USA		0.00%	81.93	1.28%	-81.93
Common Wealth	40.95	6.67%	1320.70	20.57%	-1279.75
Japan		0.00%	261.33	4.07%	-261.33
Other Countries	42.21	6.88%	910.40	14.18%	-868.19
Total	613.80	100%	6,419.26	100%	(5,805.46)

Source: CSO and DAB staff calculations

Table 4.4: Direction of External Trade FY 1394 (in million USD)

<i>Country Name</i>	<i>Exports</i>	<i>% Shares</i>	<i>Imports</i>	<i>% Share</i>	<i>Trade Balance</i>
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
Common Wealth	44.13	7.94%	1581.00	20.59%	-1536.87
China	11.66	2.10%	1090.92	14.21%	-1079.26
Saudi Arabia	0.25	0.04%		0.00%	0.25
Japan		0.00%	302.27	3.94%	-302.27

England		0.00%	5.41	0.07%	-5.41
United States		0.00%	244.54	3.18%	-244.54
Other Countries	70.79	12.74%	1160.47	15.11%	-1089.68
Total	555.71	100.00%	7679.12	100.00%	-7123.41

Source: CSO and DAB staff calculations

Table 4.5: External Debt FY 1395

	In million USD	Percent of total
Total external debt	2,081.28	100.00
Bilateral	968.91	46.55
Paris Club	884.70	42.51
Russian Federation	884.70	42.51
United States	-	0.00
Germany	-	0.00
Non-Paris Club	84.21	4.05
Multilateral	1,112.36	53.45
of which: IDA (World Bank)	342.14	16.44
Asian Development Bank	641.18	30.81
International Monetary Fund	82.16	3.95
Islamic Development Bank	45.16	2.17
OPEC Fund	1.72	0.08

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

Table 4.6: Net International Reserves FY 1395 (in million USD)

Changes on the previous quarter	FY-1392	% change	FY-1393	% change	FY-1394	% change	FY-1395	% change
Net international Reserves (million US Dollar)	6,678.62	23.22	6,693.65	0.22	6,443.00	-3.74	6,821.90	5.88
Reserve Assets	7,183.33	22.71	7,247.76	0.90	6,965.81	-3.89	7,541.02	8.26
Reserve Liabilities	504.71	10.91	554.12	9.79	522.80	-5.65	719.13	37.55
Commercial bank deposits in foreign currency	367.65	4.00	443.80	20.71	433.57	-2.30	647.68	49.38
Nonresident deposits in foreign currency	0.14	-89.57	0.14	-0.02	0.14	0.00	0.14	-0.03
Use of Fund resources	136.92	17.53	110.18	-19.53	89.10	-19.14	71.31	-19.96
Gross Intl. Reserves (in months of import)	9.23		11.92		10.89		14.10	
Net Intl. Reserves (in months of import)	8.58		11		10		13	

Source: Monetary Policy Department, DAB



5

THE REAL SECTOR DEVELOPMENT

5

THE REAL SECTOR DEVELOPMENTS

Economic growth of Afghanistan in 2016 firmed broadly as expected and the total GDP represented an estimated growth rate of 3.6 percent from the previous year. There was great recovery in agriculture coincided with improvements in services, but a marked weakness in industries sector.

Agriculture sector benefited from the government's supports and favorable weather condition, which resulted in a high growth rate of 12 percent after a diminishing year. This figure in the previous year was calculated -16.9 percent. In addition, agriculture growth has also been bolstered by a robust recovery in production of narcotics as it grew by 45.5 percent from -48.4 percent.

Industries sector experienced significant slowdown in 2016. Owing to poor performance in wood production and construction related activities, growth in industries sector dropping to -1.9 percent from 4.5 percent. However, production of basic metals was exceptionally well.

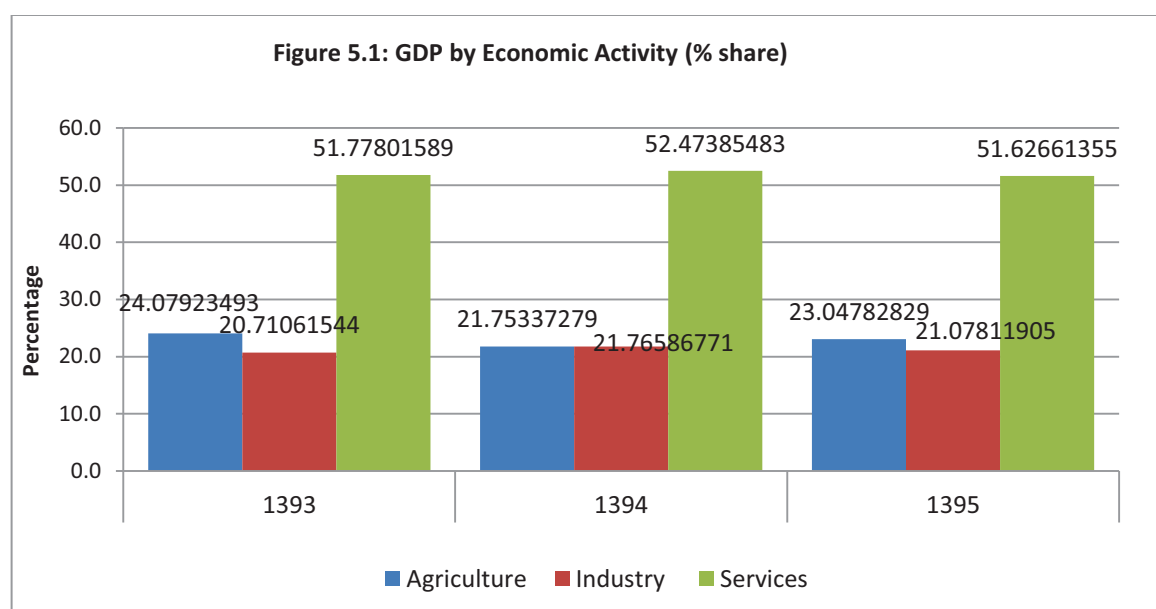
Services sector grew by an annualized rate of 2.4 percent in 2016 with much greater extent

than 1.4 percent recorded in 2015. Majority of indicators in this sector such as: finance, insurance, real estate and business; ownership of dwellings; community, social and personal services; government services; and other services helped the enhanced performance in services sector.

I. GROSS DOMESTIC PRODUCT BY ECONOMIC ACTIVITY

Economic growth in Afghanistan recovered by a rate of 3.6 percent in 2016 from -1.8 percent, albeit the country witnessed substantial uncertainties. Agriculture picked up benefiting from government's supports, favorable monsoon and strong contribution by narcotics; services improved by receiving contribution from robust growth of finance, insurance, real estate and business; but industries weakened due to poor performance in wood production and construction related activities.

While the spike in GDP growth was due largely to rise in opium production, it delivered much less resilience without contribution of narcotics representing a growth rate of 2.1 percent from 1.3 percent.



Source: Central Statistics Organization

As a whole, growth in agriculture, which has employed most of the country's population, was expectedly robust as it significantly rose to 12.4 percent above the pace set in the previous year (-16.9 percent). In explaining this better than expected pattern of expansion, the role of narcotics was considerable. Based on the reports, the total production of opium soared by 45 percent over the reporting period turning around from -48 percent recorded in the previous year. Except livestock, other components of agriculture sector delivered vigorous performance in 2016. Cereals recorded a growth rate of -4.7 percent from -14.2 percent, and fruits increased by 32.1 percent from 7.2 percent. The "other" component of agriculture also rose turning around to 6.3 percent from -2.2 percent. However, excluding opium, agriculture sector

grew by 6 percent compared to -5.7 percent observed in the preceding year.

Growth in industries sector declined by -1.9 percent in 2016, the worst since 2002. Within the total, construction sector dropped by -4.7 percent over the year from 8.1 percent recorded one year back. However, other components either showed upward movement, or remained unchanged. Movement of mining and quarrying was upward representing a growth rate of 10.4 percent from -7.9 percent. Electricity, gas and water also trended upward by 4 percent from -1.5 percent. Manufacturing sub-sector remained unchanged at 1 percent, albeit the condition in its components was mixed with a significant decline in wood and wood production including furniture, but increasing pattern in textile, wearing apparel and leather; non-metallic minerals except petroleum and coal; and basic metal more importantly. The

performance of construction, on the other hand, was unfavorable putting negative contribution to growth in industry's sector. This component declined to -4.7 percent from 8.3 percent.

Growth in services sector was fractionally above the rate set in the previous year. With contribution by finance, insurance, real estate and business; transport, storage, and communication; ownership of dwellings; community, social and personal services, government services; and other services; this sector grew by 2.4 percent from 1.4 percent.

Finance, insurance, real estate and business increased by 20 percent from -2.3 percent, the strongest outturn in services sector. At the margin, wholesale and retail trade, and restaurants and hotels exhibited a huge decline standing at -7.2 percent from 3.8 percent.

Finally saying, tax on imports stood at 7.8 percent significantly low from 16.1 percent observed one year back.

Table 5.1: Real GDP Growth by Sectors of Production (in percent)

**Real GDP at Market Prices
(Annual % change)**

***Including Opium**

Solar year	1393	1394	1395
Calendar year	2014/15	2015/16	2016/17
Agriculture	3.7	-16.9	12.4
Cereals	3.7	-14.2	-4.7
Fresh Fruits	18.9	7.2	32.1
Livestock	0.1	0.4	0.2
Opium (Poppy)		-48.4	45.5
Others**	-57.9	-2.2	6.3
Industry	2.4	4.5	-1.9
Mining and quarrying	-2.2	-7.9	10.4
Manufacturing	-2.5	1.0	1.0
Food, beverage, & tobacco	0.7	1.5	1.1
Textile, wearing apparel & leather	-35.7	-15.7	-14.8
Wood & wood prod. incl. furniture	-25.2	-21.2	-84.2
Paper, paper production printing, publishing	8.9	0.1	0.1
Chemicals & Chemical petroleum, coal, rubber, plastic	-16.2	1.1	1.8
Non-metallic mineral except petroleum & coal	-26.1	9.3	21.3
Metal basic	-76.9	-41.0	10.7

Electricity, gas, and water	2.7	-1.5	4.0
Construction	7.0	8.1	-4.7
Services	4.0	1.4	2.4
Wholesale & retail trade, restaurants & hotels	-1.0	3.8	-7.2
Wholesale & retail trade	-2.7	2.9	-9.3
Restaurants & hotels	9.2	8.9	3.6
Transport, storage and communication	1.8	4.2	4.9
Transport & storage	-1.7	0.7	0.5
Post and telecommunications	7.8	9.8	11.1
Finance, insurance, real estate and business	109.0	-2.3	20.0
Banking Finance	113.3	-2.3	19.6
Insurance	2.3	3.8	54.2
Real estate and business services	-4.5	-6.3	-3.1
Ownership of dwellings	-2.4	-4.6	2.0
Community, social and personal service	-1.2	-2.2	-0.6
Producers of Government Services	8.0	-2.3	0.5
Other services	-0.6	-10.1	6.7
Total	3.6	-2.4	3.4
Less: Imputed bank service charge			
Taxes on imports	-10.8	16.1	7.8
GDP at Market Prices	3.1	-1.8	3.6

Source: Central Statistics Organization

***Preliminary data*

II. GROSS DOMESTIC PRODUCTS BY EXPENDITURE APPROACH

GDP, under expenditure method, is calculated in nominal terms only. On balance, during 2016, nominal growth rate of GDP rose to 9 percent from 3.2 percent recorded in the preceding year. This increase was resulted from positive contributions by total final consumption and change in inventories. However, the expansion was partly offset by downturn in gross domestic fixed investment and increased gap between exports and imports.

The most dominant component in Afghanistan's GDP is the total final consumption expenditure, which is broken down into private consumption and government consumption.

Taking support from both sub-divisions total final consumption expenditure at current market price increased by 7.5 percent from 6.4 percent in the previous year.

Nominal growth of gross fixed investment, on the other hand, was bottomed-out at -1.5 percent relative to 11.9 percent observed in the previous year. Although durable capital goods

considerably increased, lower performance in construction which accounts for vast majority of gross domestic fixed investment led to negative growth in alluded component. During the reporting period, growth of “change in inventories and data” (investment in consumer goods) supported GDP growth by turning around to 18.8 percent significantly higher from -0.1 percent in the previous period.

Total value of exports of goods and non-factor services increased to AF 91,983 million from AF 86,704 million recording a growth rate of 6.1 percent lower from 11.2 percent. At the time, imports of goods and non-factor services reached AF 653,902 million from AF 610,686 million, which shows a growth rate of 7.1 percent from 12.3 percent. As a result, resource balance (the gap between exports and imports) rose to AF -561,919 million from AF -523,981 million, but the rate of increase was slower at 7.2 percent compared to 12.5 percent seen in the previous year.

According to the data released by the Central Statistics Organization (CSO) in 2016, total population increased by 2.1 percent from 1.8 percent increase in 2015, the Afghani exchange rate against US dollar depreciated by 5.6 percent lower from 11.2 percent decline in the previous year, GDP per capita increased by 6.7 percent from 1.4 percent, GDP deflator showed a rate of 5.3 percent slightly higher from the previous rate of 5.1 percent, domestic absorption increased by 8.5 percent from 5.8

percent, and gross domestic savings surged up by 37.6 percent from -34.4 percent.

Table 5.2: Gross Domestic Product by Expenditure-Categories in Current Price (%Δ Year-on-Year)

Category	1395	1394	1393
	2016-17	2015-16	2014-15
Total final consumption expenditure	7.5	6.4	1.8
Private consumption	7.4	7.2	1.0
Government consumption	8.0	1.5	7.6
Gross Domestic Fixed Investment	-1.5	11.9	7.1
Gross fixed capital formation	-1.5	11.9	7.1
Construction	-2.4	14.0	12.8
Durable capital goods	23.2	-27.9	-44.9
Resource balance	7.2	12.5	-7.8
Exports of goods and NFS	6.1	11.2	6.4
Exports of goods	5.7	11.2	7.4
Non-factor Services	8.1	11.2	2.1
Less: Imports of goods and NFS	7.1	12.3	-6.0
Imports of goods	5.9	11.2	-6.8
Non-factor Services	16.0	22.1	2.0
*Change in Inventories and data	18.8	-0.1	-12.4
GDP at market price	9.0	3.2	2.0

Source: Central Statistics Organization

*Preliminary data

III. GDP OUTLOOK FOR 2017

The trend in Afghanistan's GDP growth is expected to gain momentum in 2017. On balance, the economy is expected to grow by 3.0% in 2017 and reach a growth rate of 4-5% till 2019. In the year 2016, growth was largely driven by agriculture and we expect this sector to remain the main driver of growth in the upcoming 2018 and 2019 years. It is worth to mention that agriculture sector is heavily dependent on the seasonal rainfalls and is expected to record desirable changes due to favorable rainfalls showered this year. The fragile security environment has been the single most binding constraint to private-sector investment and private-sector-led growth.

Continued violence and economic uncertainties are expected to undermine the growth of Afghanistan's economy. Despite the political and security challenges, the government of Afghanistan and international community are striving hard to develop and sustain stable economic system in the country. Regardless of domestic insurgency, the government of Afghanistan has been working on core long term projects and programs.

The ministry of agriculture has been working on agribusinesses programs to nourish and add value to the agriculture sector. The government of Afghanistan in collaboration with foreign donors is committed to provide technical

assistance to agriculture sector to enhance the capacity and output. Thus, this sector is expected to grow by a significant rate in 2017. Industry and services sectors are also expected to deliver greater performance in 2017. Despite the political and security challenges, the government of Afghanistan and international community are striving hard to develop and sustain stable economic system in the country. Regardless of domestic insurgency, they have been working on core long term projects and programs. Also, the government has been making tremendous efforts to support and strengthen textile and manufacturing sectors to open gateway to industrialization in the country. Furthermore, government and private sector are keen to invest in Afghanistan and these sectors are bringing about more positive changes in near future.



6

FISCAL SECTOR DEVELOPMENT

6

FISCAL DEVELOPMENTS

The key objectives in the fiscal area are to achieve sustained increase in revenue collection in order to permit the gradual takeover of externally financed operating & development expenditure and to ensure expenditure allocation consistent with Afghanistan National Development Strategy (ANDS). Furthermore, other goals include improvements in public expenditure management, fiscal policy formulation, efficiency in public enterprises, tax and customs administration.

Moreover, like other emerging and under developed economies around the world, Afghanistan also faces a budget imbalance (Budget Deficit) as the total core expenditure exceeded total domestic revenue (excluding grants) in FY 1395 leading to AF 198.48 billion budget deficit where including grants, a budget surplus of AF 5.30 billion is observed comparably.

Beside the total domestic revenue is increased from 123.38 billion to AF 154.48 billion in FY 1395, an increase of AF 31.10 billion or 25.20 % growth in domestic revenue collection is

observed compared to same period of previous year.

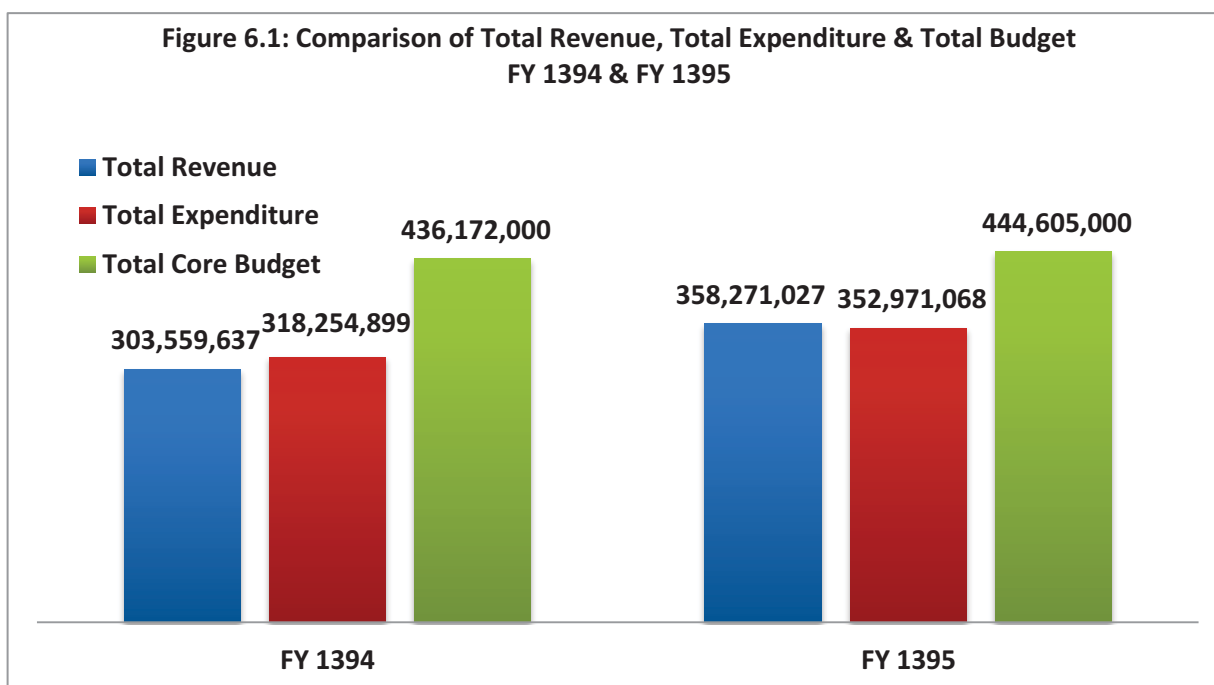
Meanwhile, total core expenditure increased from AF 318.25 billion of FY 1394 to AF 353.73 billion of FY 1395 an increase of AF 35.48 billion leading to 11.15 % increase in expenditure as compared to same period of last year.

On the other hand, donor contributions are used to finance both operating and development expenditures. The total donor contribution (grants) allocated to operating and development expenditures are increased from AF 180.17 billion of FY 1394 to AF 203.78 billion of FY 1395 indicating AF 23.61 billion illustrating 13.11% increase in the level of grants compared with last year. The main donor contributors to operating and development expenditures are ARTF, LOTFA, (CSTC-A, MoD, MoI & NATO), ADB, WB, EC, US & USAID.

Furthermore, comparably total core budget increased from AF 436.17 billion of FY 1394 to AF 444.61 billion during FY 1395 with an increase of AF 8.43 billion or 1.93% in total core budget on annual basis. On the other hand,

operating budget execution rate depicts a significant increase of 7% from 83% to 90% during FY 1395 while development budget

execution rate has decreased from 55.44% of FY 1394 to 55.01 of FY 1395 showing a diminutive decrease of 0.43% comparably.



Source: Ministry of Finance

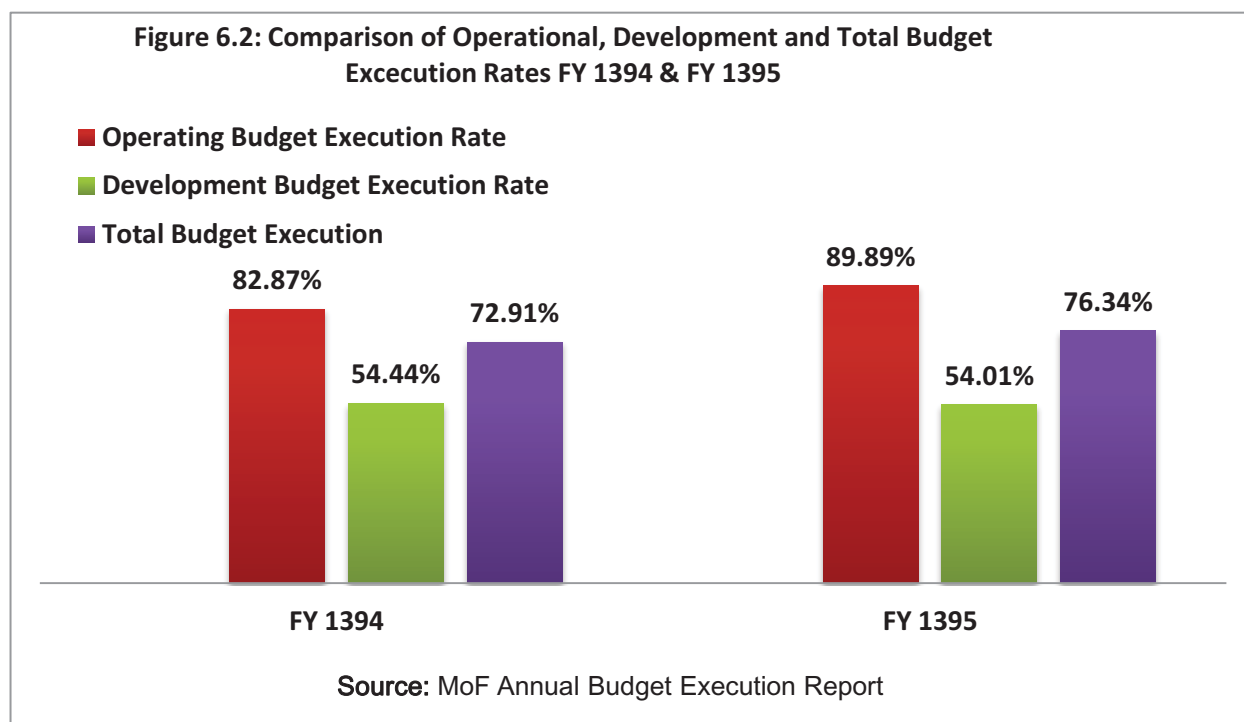
I. BUDGET EXECUTION RATE

During the reference period of FY 1395, government successfully managed to spend only 76.34 percent of the total of AF 445 billion allocated budget, while 72.91 percent of the total allocated budget of AF 436 billion in the FY 1394 represents 3.43 percent increase in overall budget execution rate of FY 1395 compared to same period of FY 1394. Moreover, operating budget execution rate obviously indicates 7.02 percent increase from 82.87 percent of FY 1394 to 89.89 percent of FY 1395 out of total allocated budget of AF 276.05 billion in FY 1395. In addition,

development budget execution rate evidently represents 0.43 percent decrease from 54.44 percent of FY 1394 to 54.01 percent during FY 1395 out of total allocated budget of AF 168.55 billion set in FY1395.

On the other hand, total budget execution rate is presenting a slight increase of only 3.43 percent in the period under review. Overall lower execution rate of the core budget below the target was attributed to several factors in particular to the time consuming procurement process and approval of expenses by the National Procurement Authority (NPA), suspension of budget approval, deteriorating

security condition in provinces and underperformances by the budgetary units.



II. CORE BUDGET (DEFICIT & SURPLUS)

The overall budget prior to donor's contribution had a deficit of AFN 198.48 billion in FY 1395. However, external source of finance plus domestic revenues' total budget presents a surplus of AFN 5.30 billion in FY 1395.

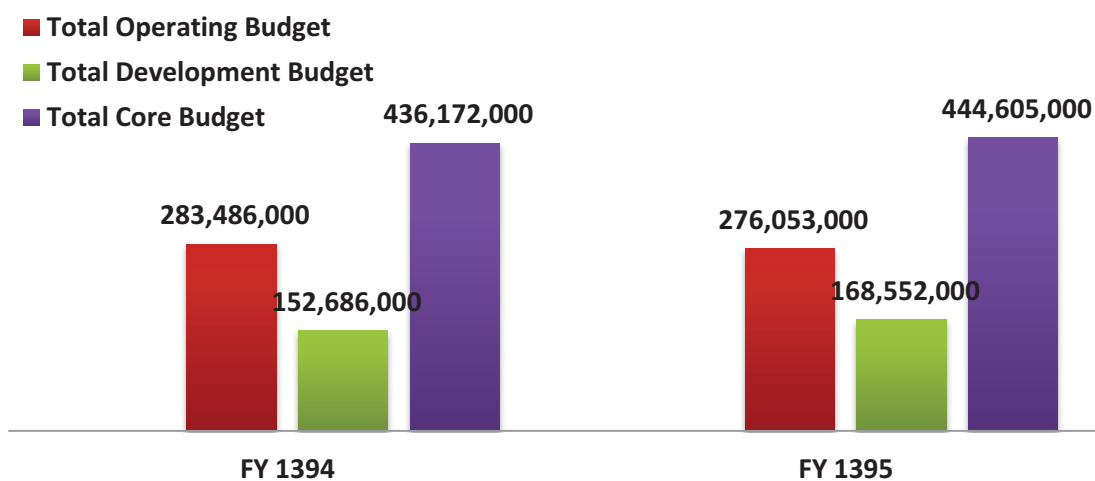
Meanwhile, total budget of FY 1395 plainly represents an increase of AF 8.43 billion from AF 436.17 billion to AF 444.61 billion in FY 1395 indicating 1.93 percent increase in annual budget compared to the same period of FY 1394. Moreover, total operating budget of FY 1395 manifestly shows a decrease of AF 7.44 billion indicating 2.6 percent decrease from

AF 283.49 billion in FY 1394 to AF 276.05 billion during the FY 1395. On the other hand, total development budget distinctly shows an increase of 15.87 billion representing 10.39 percent increase from 152.69 billion of FY 1394 to 168.55 billion in FY 1395.

Figure 6.3: Comparison of Total Core Budget FY 1394 & FY 1395



Figure 6.4: Comparison of Total Budget FY 1394 & FY 1395

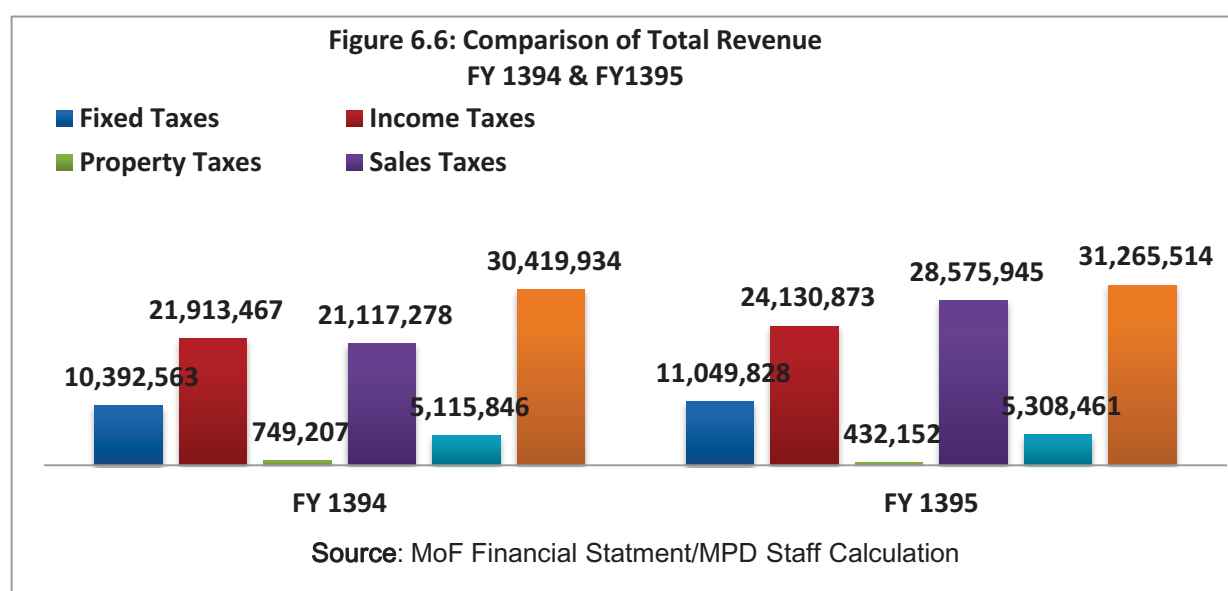
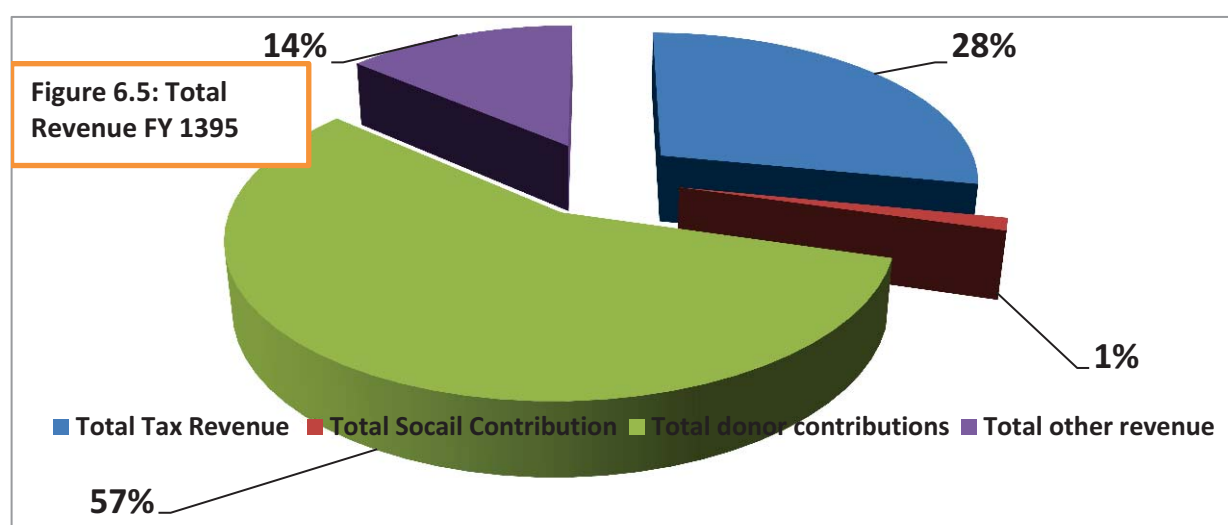


Source: MoF Annual Budget Manual & Annual Cash Plan

III. TOTAL REVENUE

During Total revenues including grants increased significantly with the total collection of AFN 358.27 billion in the period under review as compared to AFN 303.56 billion of FY 1394, presenting a significant increase of AFN 54.71 billion or 18.02 percent. Furthermore, in order to meet current budget deficit of FY 1395, total donor contribution plays a vital role in total

revenue collection that steers to annual budget surplus. Moreover, the positive momentum gained in revenue collection of FY 1395 was mainly as a result of reforms in the customs & revenue collection system, administration fee, the implementation of new tax measures, increase in telecommunication fee and increase in BRT (Business Receipt Tax) from 2 to 4 percent. Figure 6.5 shows comparison of Total Revenue of FY 1395.

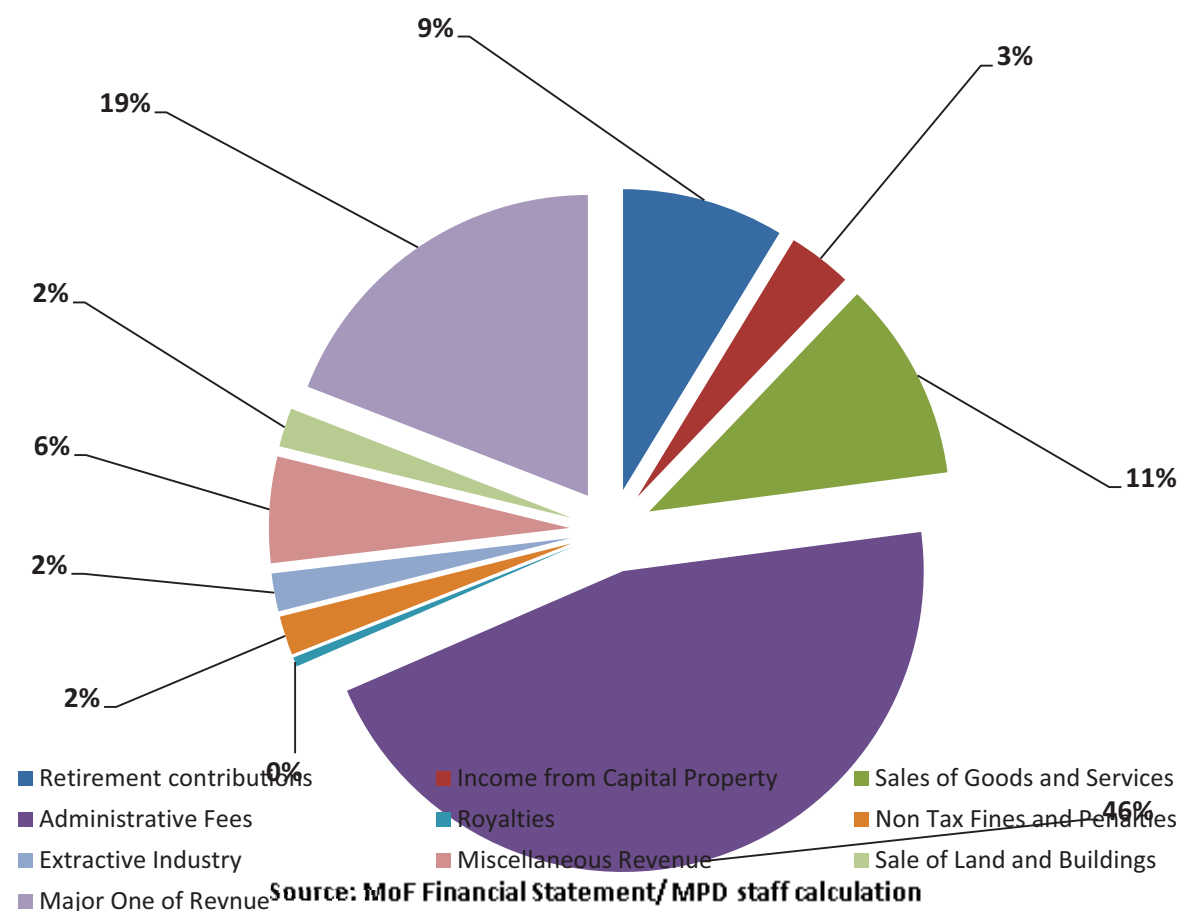


6.3.1 Non-tax Revenues

Non-tax revenue is one of the core contributors of domestic revenue representing a significant increase of 58.46 percent from AFN 33.68 billion in the FY 1394 to AFN 53.37 billion during the FY 1395 showing a momentous boost of AFN 19.69 billion in the period under review. On the other hand, the vital acceleration in non-tax revenue is mainly attributed to increase in high performance of administration fee which represents 60.74 percent increase,

royalties 70.97 percent increase, miscellaneous revenues represent 33.49 percent and Extractive Industry represents 79.43 percent increase compared to the same period of FY 1394. Ministry of communication, Ministry of Transport and Ministry of Interior Affairs are agencies which mainly collect non-tax revenues such as telecommunication and stamp fees.

Figure 6.7: Components of Total Non-Tax Revenue FY 1395



IV. GRANTS

The Afghan government receives grants and occasional loans from various donors, trusts and international committees to finance variety of programs. The donor contribution comprises an important part of the national budget financing major expenditure items in both operating and development budgets. Fiscal sustainability is defined as total domestic expenditure being financed by the total domestic revenue. Afghanistan's domestic expenditure is being financed by; foreign grants and foreign loans as well as domestic revenue. On the other hand, total development and operating grants manifestly represent significant increase of 13.11 percent from AFN 180.17 billion of FY 1394 to AFN 203.78 billion in the period under review showing AFN 23.61 billion acceleration in grants and loans as compared to the same period of previous year mainly due to funds released for Capacity Building of Community Development Councils (CDCs). Basic Package of Health Services and Essential Package of Hospital Services, constituted the largest portion of the total development grants.

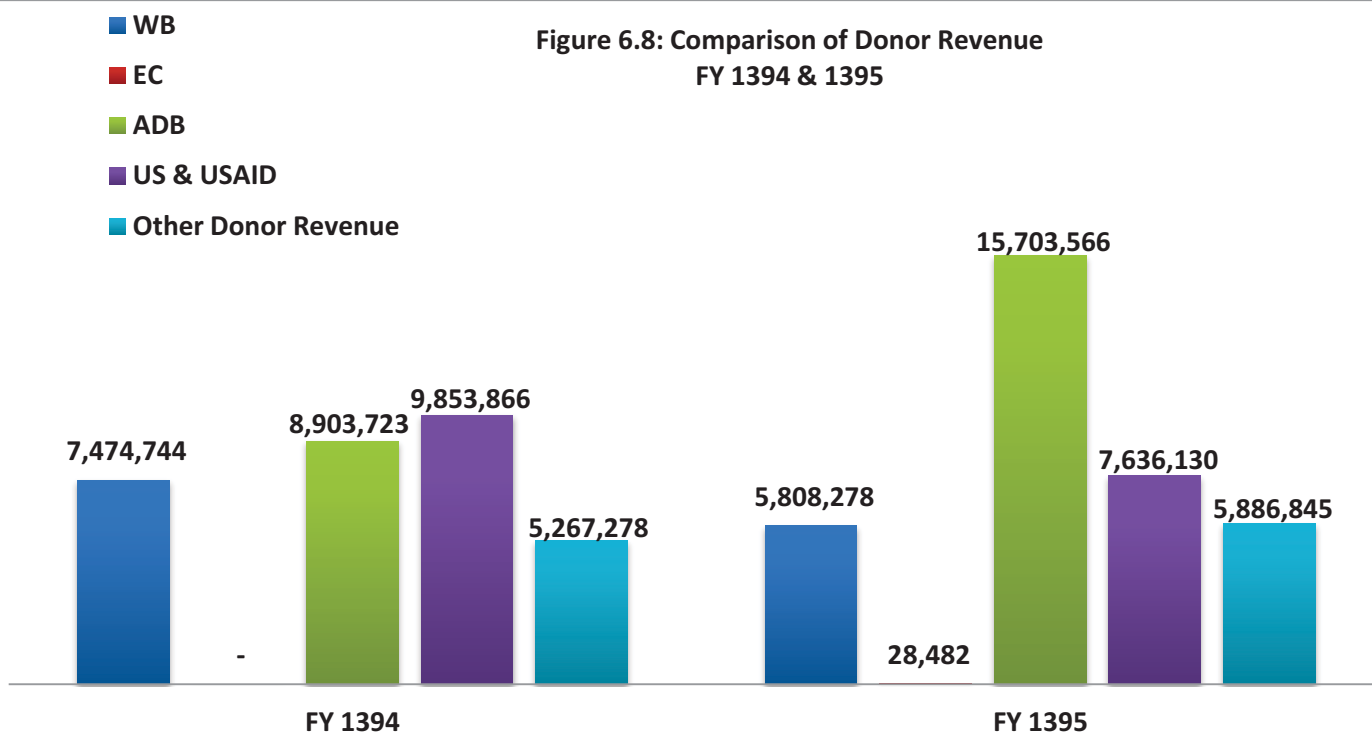
The main donor contributors to the development and operating expenditures are ARTF, LOTFA, (CSTC-A, MoD, MoI & NATO), ADB, WB, EC, US & USAID.

V. EXPENDITURE

During The core expenditures are classified into development and operating expenditures which are allocated to eight different sectors such as security, governance, education, health, agriculture, social protection, infrastructure, and economic governance. In addition, the sector-wise expenditure is provided for both operating and development budgets, while increased expenditure on infrastructure, economic governance, and agriculture sectors are in line with the ANDS priority. Furthermore, total core expenditure manifestly presents 10.91 percent increase from AFN 318.25 billion of FY 1394 to AFN 352.97 billion of FY 1395 perceptibly indicating AFN 34.72 billion acceleration in overall development and operating expenditures compared to the same period of the previous year.

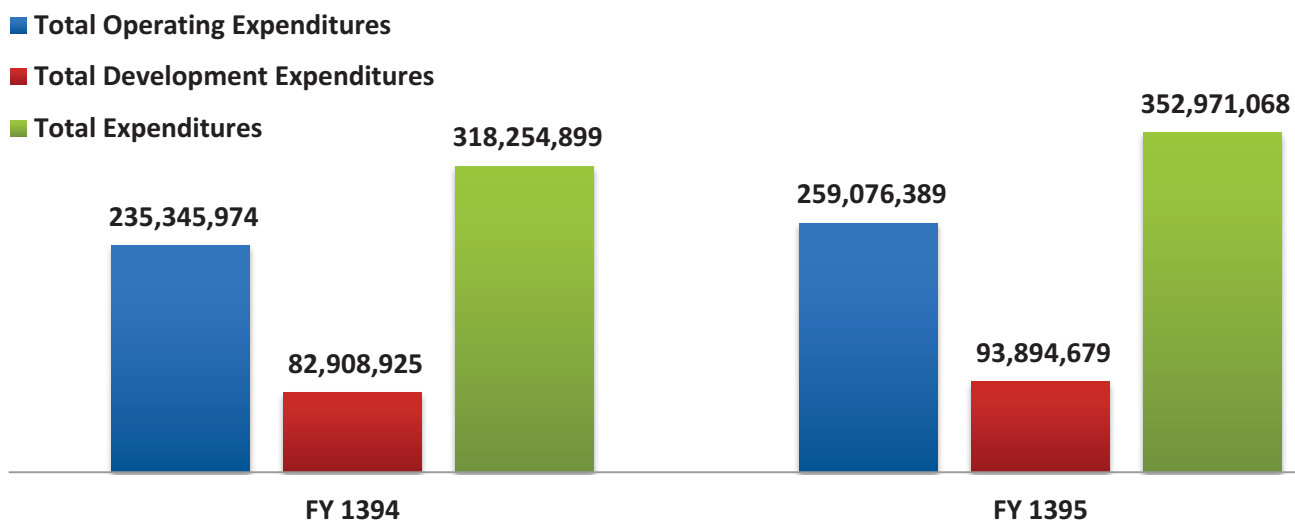
In addition, operating expenditure plainly indicates 10.14 percent increase from AFN 235.35 billion of FY 1394 to AFN 259.21 billion of FY 1395 which represents AFN 23.86 billion comparing to the same period of last year mainly attributed to interest payment, compensation of employees and social transfers irrespective of other components. Meanwhile, development expenditure shows a significant increase of 14.01 percent from AFN 82.91 billion in FY 1394 to AFN 94.52 billion during the FY 1395 indicating AFN 11.61 billion speeding up in development expenditure compared with the same period of last year.

Figure 6.8: Comparison of Donor Revenue
FY 1394 & 1395



Source: MoF Financial Statment/MPD staff calculation

Figure 6.9: Comparison of Total Expenditure
FY 1394 & FY 1395



Source: MoF Financial Statment/MPD staff calculation



7

BANKING SYSTEM PERFORMANCE

7

BANKING SYSTEM PERFORMANCE

A sset base of the banking sector grew at a slower pace than the previous year, depicting 10.56 percent growth (AF 2.83 billion) during the review year compared to 12.18 percent increase in the year ending December 2016. The increase in banking system assets was mainly due to increase in cash in vault and claims on DAB, investments and other assets.

Gross loans portfolio of the banking sector declined by 9.14 percent (AF 4.15 billion) over the last year against 5.03 percent growth in December 2015. The decrease in the loan portfolio over the year was mainly attributed to repossession of assets, settlement of loans and less customer utilization of OD (Overdraft loans).

Deposits, the main funding source of banking sector stood at AF 254.92 billion, comprising 96.18 percent of the total liabilities of the sector increased by 7.57 percent against 8.29 percent increase in the previous year (December 2015). The major increase in deposit base of the banking sector is attributed to saving deposits and occurred in AFN currency. Deposits were

largely denominated in USD (63.44 percent) with Afghani denominated deposits lagging at 30.93 percent. AF-denominated deposits indicated 19.42 percent increase against 11.46 percent decrease in Dec. 2015, while USD denominated deposits were up by 0.50 percent against 17.45 percent increase in Dec. 2015.

The capital base of the banking sector remained strong and increased by 37.43 percent standing at AF 33.91 billion. Capital adequacy ratio (CAR) of the banking sector is recorded at 27.68 percent in the period under review. Disaggregated analysis shows that all banking institutions except one bank in the system registered capital adequacy ratio above the minimum threshold (12 percent of risk-weighted assets). The Basel benchmark for capital to risk weighted is 8 percent.

Banking sector earned net profit amounting to AF 4.29 billion in the review year, against AF 522 million net profits in the previous year. Return on Assets (ROA) stood at 1.55 percent annualized against 0.20 percent annualized in December 2015 and Return on Equity (ROE) registered at 15.38 percent

annualized against 1.69 percent annualized in December 2015. The increase in profitability of the banking sector is mostly ascribed to significant increase in non-interest income. Another contributing factor was decrease in credit provision and interest expense, while operating expenses showed increase in the year under analysis. State-Owned Banks (SOB) and branches of foreign banks (BFB) ended up with profits, while Private Banks (PB) suffered from loss.

I. ASSETS OF THE BANKING SYSTEM

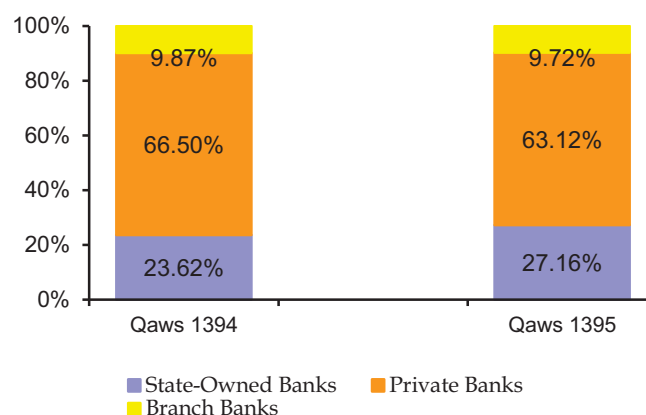
The assets size of the banking sector increased by 10.45 percent in the year under analysis against 12.18 percent increase in the last year December 2015. (Figure 7.1)

The breakup of total assets reveals that the most obvious increase was registered in cash in vault and claims On DAB which increased by AF 25.38 billion (21.88 percent) followed by investments increased by AF 6.42 billion (34.11 percent) and repossessed assets increased by AF 1.53 billion, while interbank claims and gross loans showed decrease of AF 5.51 billion (7.04 percent) and AF 4.15billion (9.14 percent) respectively during the current year.

The most important components of the system's total asset portfolio were cash in

vault/claims on DAB (47.28 percent), interbank claims (24.33 percent), net loans (12.18 percent), investments (8.44 Percent), "other assets" (4.64 percent) and fixed assets comprising 2.35 percent of the total assets. See table 7.1.

Figure 7.1: Share of Total assets of the banking sector



Source: Financial Supervision Department/
DAB

Table 7.1: Assets of the banking sector

Amount in million AF	Qaws, 1394 Dec. 2015	Qaws, 1395 Dec. 2016	% of Total Assets/Liability	Y-o-Y Growth
Assets				
Cash in vault and claims on DAB	115,984	141,367	47.28%	21.88%
Interbank claims(Net)	78,261	72,748	24.33%	-7.04%
Investments	18,815	25,232	8.44%	34.11%
Loans (Net)	41,186	36,428	12.18%	-11.55%
Intangible assets	594.6039	784.76521	0.26%	31.98%
Reposessed Assets	0	1,534	0.51%	
Fixed Assets	7,352	7,012	2.35%	-4.62%
Others	8,495	13,873	4.64%	63.30%
Total	270,689	298,979		10.45%
Liabilities				
Deposits	237,002	254,952	96.18%	7.57%
Borrowings	4,452	3,597	1.36%	-19.20%
Subordinated Debt	43	21	0.01%	-50.00%
Other	4,520	6,502	2.45%	43.85%
Total	246,017	265,072		7.75%
Financial Capital	24,671	33,906		37.43%

Source: Financial Supervision Department, DAB

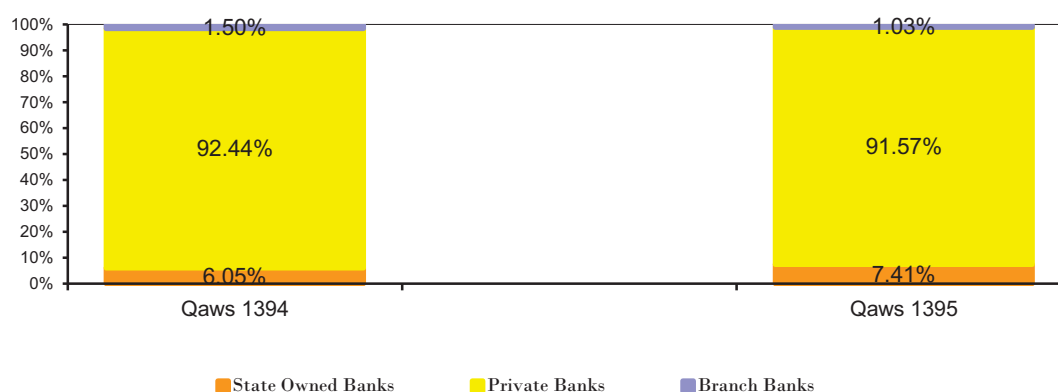
7.1.1 Gross Loans

Total gross loans indicated AF 4.15 billion or 9.14 percent decline since last year, constituting 13.80 percent of the total assets. The decrease in total loan portfolio is

mainly attributed to repossession of assets amounted AF 1.53 billion, settlement of loans and less customer utilization of OD (Overdraft loans).

Figure 7.2:

Figure 7.2: Share of Gross Loans Portfolio among banking group



Source: Financial Supervision Department, DAB

Decline in loan portfolio were observed at nine banking institutions, whereas five banking institutions observed an increase in their loan portfolio and the remaining one bank (New Kabul Bank) did not participate in lending.

Gross loan portfolio declined in Private Banks and Branches of foreign banks but increased in State-owned banks. Private Banks with 91.57 percent share in total portfolio posted 10 percent or AF 4.20 billion decrease, branches of foreign banks with 1.03 percent share depicted 37 percent or AF 258 million decrease while State-owned banks holding 7.41 percent share of the portfolio increased by 11 percent or AF 307 million during the current year.

While assessing the level of credit risk, banks must give due attention to credit risk mitigation tools within their risk mitigation framework. Banks are required to make both general reserves (on standard assets) and specific provisions (on non-standard assets) in order to mitigate their credit risk and according to revised Asset classification and provisioning regulation, from September 2016 banks are required to set at least 1 percent reserve for their standard assets.

By the end of December 2016 (Qaws 1395), total provision cover of the system was 11.71 percent of total gross loans as opposed to 9.30 percent recorded in the last year December 2015.

7.1.2 Loan Loss Reserves

7.1.3 Distribution of Credit

In order to broad-based the loan portfolio and broaden the risk diversification and financial access besides new avenues of earning, DAB has diversified the sector wide distribution of Other Commercial Loans to thirty sectors⁴. The analysis of deployment of credit in different sectors indicate that the major portion of the loan portfolio is classified as “other commercial loans” (90.13 percent against 92.78 percent in Dec. 2015) mainly in “Petroleum and lubricants” (11.08 percent), “all other services” (9.90 percent), “Construction and building” (8.20 percent), “Food items” (7.80 percent) and “Retail trading” sectors (7.31 percent). Significant decreases were observed in Wholesales, Manufacturing and Industry, and Spare parts sectors both in absolute amount and percentage of total gross loans, while retail trading and “all other services” were among top increasing sectors. Loans designated to Micro Credit sector posted an increase of AF 709 million amounting to AF 4.08 billion provided by one bank and SME sector increased by AF 536 million amounting to AF 2.59 billion provided by five banking institutions. Concentration of loans to a few sectors of the economy would expose banks to credit risk in the event of crises situation associated to that sector inversely affecting the overall banking

sectors and therefore, banks should closely monitor the potential risk associated with key sectors given the high NPL ratio. About 74.01 percent of the loans were designated in Kabul while Herat and Balkh provinces lie in the second and third places and Nangarhar and Badghis provinces are at fourth and fifth places respectively. The proportion of loans in other provinces was negligible. The designation of loans by sector, geography and institution is not adequately diversified, but it is expected that with time, the distribution of loans will improve. It is desirable that all banks take active part in lending so as to diversify lending services and properly perform their role in financial intermediation.

⁴ Accounting Circular No. 93/01 dated 26/06/1393

Table 7.2: Sectorial 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)	Qaws, 1395 (Dec. 2016)
Commercial Real Estate and Construction Loans	19.92	25.98	2.85	2.29	2.02%	1.80%	1.90%	2.92%
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%			
Agricultural Loans						0.27%	0.33%	0.12%
Livestock and Farms						0%	0.03%	0.06%
Manufacturing and Industry(product of metal, wood, plastic, rubber)						2%	4.42%	3.47%
Manufacturing, Handmade and Machine products						4%	4.24%	3.74%
Cement and Construction Materials						3%	1.96%	1.27%
Textile						2.59%	0.52%	0.72%
Power						0.35%	0.22%	0.38%
Construction and Building						12.52%	7.54%	8.20%
Services						4.79%	3.80%	3.32%
Hotel and Restaurant						1.20%	1.46%	1.33%
Telecommunication						2.92%	5.70%	5.96%
Ground Transportation						4.87%	5.31%	4.86%
Air Transportation						4.18%	2.66%	2.35%
Health and Hygienic						0.71%	1.16%	1.42%

Median, Advertisements and Printer						0.04%	0.04%	0.05%
All Other Services						1.41%	7.56%	9.90%
Wholesales						4.93%	9.89%	4.34%
Machineries						0.12%	0.25%	0.13%
Petroleum and Lubricants						8.74%	9.80%	11.08%
Spare Parts						0.24%	1.42%	0.26%
Electronics						1.40%	1.58%	1.91%
Cement and other Construction Materials						1.87%	2.73%	2.35%
Food Items						4.52%	8.24%	7.80%
All Other Items						5.72%	3.47%	4.17%
Retail Trading						3.92%	3.28%	7.31%
Road and Railway						2.41%	1.17%	0.64%
Dams						0.61%	0.09%	0.04%
Mines						0.08%	1.48%	0.52%
Other infrastructure Projects						1.81%	2.44%	2.44%
Financial and Lending Institutions						0.00%	0.00%	0.00%
Agricultural Loans	0.88	0.75	2.06	2.66	2.38%	2.34%	2.35%	3.08%
Consumer Loans	1.33	1.01	0.82	0.74	0.24%	0.26%	0.30%	0.65%
Residential Mortgage Loans to Individuals	7.3	8.95	15.65	14.46	10.84%	7.14%	2.68%	2.78%
All Other Loans	3.69	10	12.65	10.71	9.41%	6.68%	0.00%	0.43%

Source: Financial Supervision Department/DAB

II. CLASSIFICATION OF LOANS

7.2.1 Non-performing loans

Banks should strengthen credit risk management measures to significantly reduce the high level of NPLs, Which is not a favourable situation. Moreover, it can be inferred that banks with poor credit performance suffer from inefficient risk management. It is essential that banks with poor loan quality evaluate credit applications carefully, comply with all applicable laws, regulations, circulars, internal policies and procedures, and closely monitor financial condition of their borrowers to ensure that credit expansion will not pose a threat to the stability of the financial system.

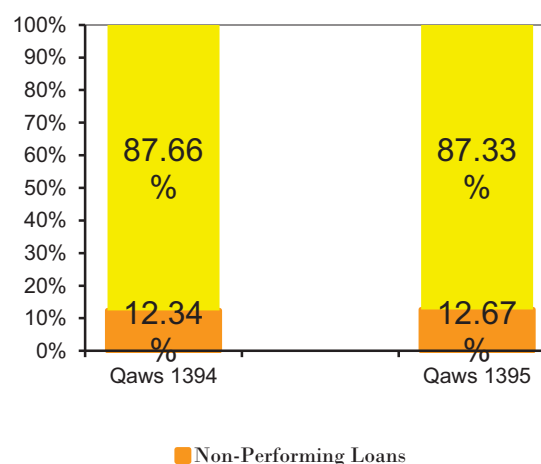
In monetary terms, by the end of December 2016, non-performing loans stood at AF 5.23 billion or 12.67 percent of total gross loans and 17.44 percent of the system's regulatory capital against AF 5.60 billion or 12.34 percent of the total gross loans in the preceding year. The decrease in non-performing loan is mainly due to repossession of loans and charge offs. More than 75 percent of the NPLs belong to three Private commercial banks holding 57.68 percent of total gross loans of the banking sector.

Source: Financial Supervision
Department/DAB

Financial Supervision Department (FSD) is closely working with the financial institutions with poor loan performance to design and implement plans to improve their asset quality. This situation requires regulatory oversight and prompt remedial action to improve governance of credit risk to avoid negative impact over the profitability and capital adequacy of the banks with poor credit quality.

The sector wide distribution of NPL reveals that major part of NPL originates from Trade sector making 38.68 percent of the sector's NPL, with services and manufacturing sectors at the second and third place, though the NPL showed decrease in these sectors over the year, the NPL increased in "other sectors".

Figure 7.3: Quality of Loan Portfolio



7.2.2 Adversely-classified loans

Adversely classified loans (substandard, doubtful)⁵ depicted AF 2.40 billion increase over the last year to AF 11.10 billion, constituting 26.91 percent of the total gross loans or 37.07 percent of regulatory capital and therefore, require 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. Management should take appropriate measures to address issues and weaknesses that have resulted in poor credit performance as per prudential regulations. Though systematic risk and economic downturn may have affected weak and systematically important bank's asset quality especially loans; however, management of banks should develop mechanisms to predict such risks, hedge their potential risk and take proper precautionary measures as per prudential regulations.

⁵Assets and advances for which the principal and/or interest remains outstanding for 31-90 days (Substandard). Default assets and advances for which the principal and/or interest remains outstanding for 91-360 days (Doubtful)- as per new Assets Classification and provision Regulation

7.2.3 Loans classified Watch

Loans classified in the "watch"⁶ category are AF 3.89 billion, which makes 9.45 percent of total gross loans decreased by 19.70 percent since last year (December 2015). The decrease is mostly attributed to three private commercial banks and one state owned bank in the system. This category of loans require close monitoring as it may lead to more adversely classified loans (Substandard, Doubtful) and losses in the future.

7.2.4 Loans classified loss⁷

Loans classified under this category amount to AF 556 million or 1.35 percent of total gross loans are up by AF 210 million since last year, attributed to seven banks. Banks are required to maintain enough capital at all times to cover losses resulting from loans classified in this category as it prompts charge-off from balance sheet.

⁶Assets and advances for which the principal and/or interest remains outstanding for 1-30 days (Watch)-new Assets Classification and provision regulation

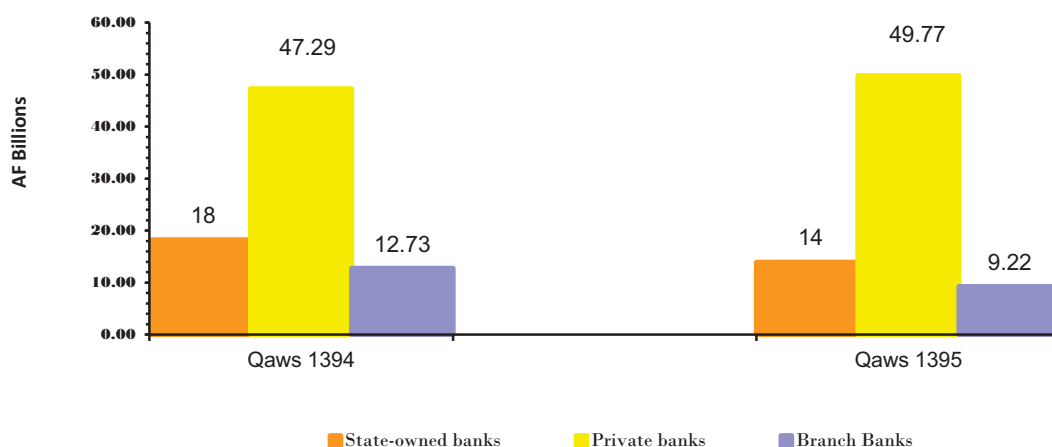
⁷ Assets on which the payment of principal or interest is due and remains unpaid for 540 days or more (Loss) as per Accounting Letter No. 03/92 dated 16/09/1392

6.2.5 Interbank Claims

Interbank Claims are the second largest among various asset categories, currently comprising AF 72.93 billion 24.39 percent of total assets registered AF 5.33 billion 6.81 percent decrease since last year (December 2015) which are mostly attributed to nine banking institutions and indicate that the banking sector has transferred a portion of its interbank claims to its cash in vault and DAB capital notes accounts, may be to decrease the risk level of the assets and strengthen its liquidity position while all banks broad liquidity ratios are above the minimum threshold.

Later on, by improving security and economic situation of the country banking sector can substitute these assets to higher income earning assets. Banks must not only appropriately measure risks associated with individual bank's but also country or countries in which they have placed funds. See figure 7.4.

Figure 7.4: Share of Inter bank Claims among banking groups



Source: Financial Supervision Department, DAB

7.2.6 Investment

The investment⁸ portfolio of the banking sector comprises of bonds, Government Securities and investment in associated companies which grew by 34.11 percent or AF 6.42 billion over the last year, standing at AF 25.23 billion which constitutes 8.44 percent of total assets. The increase in investment came from eleven banking institutions. Major part of the sector's investment took place outside Afghanistan. The investment portfolio is attributed to two state owned banks, six commercial banks and three branches of foreign banks.

7.2.7 Cash in Vault and Claims on DAB

Cash in vault and claims on DAB remains the largest category making 47.28 percent of the total assets, showed an increase of AF 25.38 billion, both in absolute as well as in

percentage of total assets since last year ending December 2015.

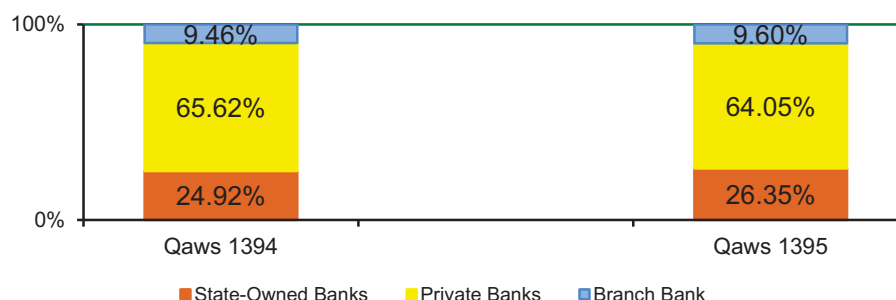
The banking sector is fully compliant with required reserves regulations and is deploying slowly and prudently the attracted funds into other types of assets.

III. LIABILITIES

Total liabilities of the banking sector increased by AF 19.05 million or 7.75 percent standing at AF 265.07 billion against AF 246.02 billion in the preceding year (December 2015). All components of total liabilities except suspense accounts, borrowings, subordinated debt and hedging derivatives have shown increase over the last year.

The majority of liabilities are made up of deposits (96.18 percent), with "other liabilities" at second and "borrowings" in third place. See table 7.3.

Figure 7.5: Increase in the Liabilities among the banking group



⁸Investments include investment in bonds, securities, associated companies, in a subsidiary and in a bank

7.3.1 Deposits

In terms of types of deposits, demand deposits accounted for 74.79 percent of the total deposit base, increased by 4.17 percent, saving deposits with 19.82 percent of total deposits was in the second place and depicted 21.13 percent increase, while time deposit making up 5.39 percent of the total deposit portfolio was up by 12.27 percent since December 2015.

Deposits being the main funding source, amounted to AF 254.95 billion for the current year under review showing an increase of AF 17.95 billion or 7.57 percent, compared to last year December 2015. The major increase in deposit base of the banking sector is attributed to saving deposits and occurred in AFN currency. Currency wise analysis shows that Afghani denominated deposits indicated 19.42 percent increase (against 11.46 percent decrease in December 2015) accounting for 30.93 percent of total deposits, while US dollar denominated deposits increased only by 0.50 percent (17.45 percent increase in Dec. 2015) making 63.44 percent of the total deposits of the system.

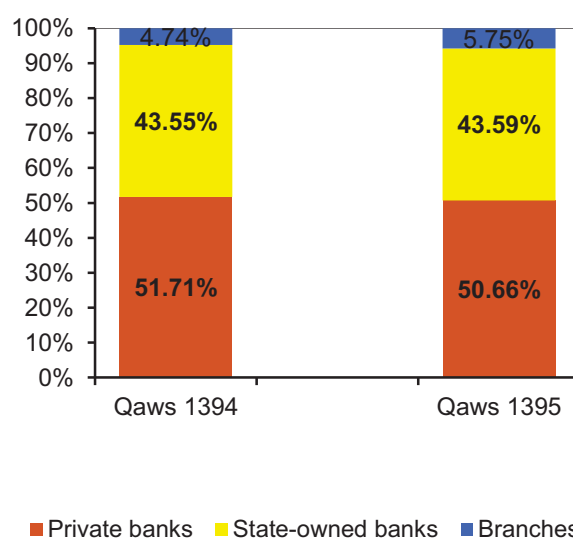
Private Banks attracted AF 165.14 billion deposits, increased by 5.25 percent against 11.52 percent increase in last year, making up 64.77 percent of the system's deposits. The share of state-owned banks amounted to AF 65.78 billion, increased by 12.39

percent (1.91 percent increase in December 2015) since preceding year, accounted for 25.80 percent of the system's deposits.

The share of branches of foreign banks stands at AF 24.04 billion increased by 11.43 percent (4.09 percent increase in December 2015) making up 9.43 percent of total deposits of the system.

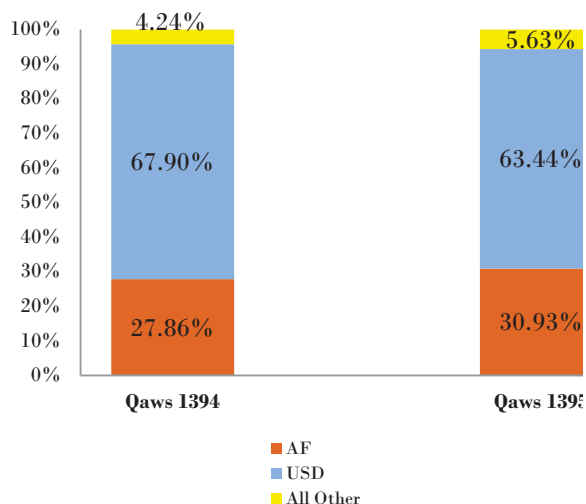
Source: Financial Supervision

Figure 7.6: Afghani Denominated Deposits



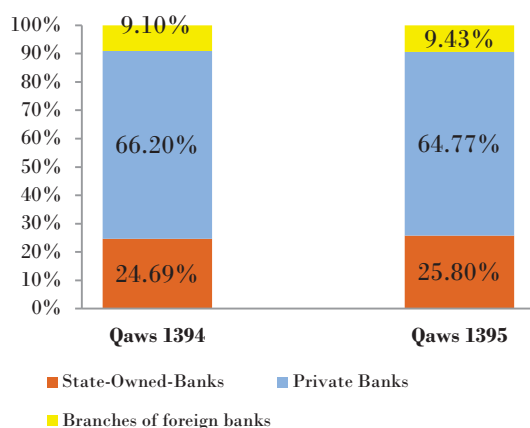
Department/DAB

Figure 7.7: Currency Composition of Deposits



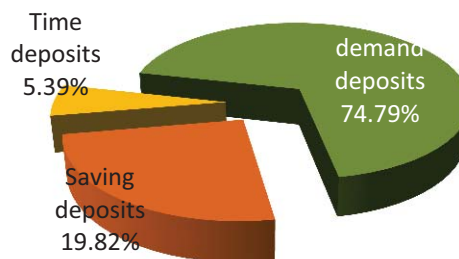
Source: Financial Supervision Department/DAB

Figure 7.8: Increase in Deposits among the banking group



Source: Financial Supervision Department/ DAB

Figure 7.9: Breakdown of Deposits



Source: Financial Supervision Department/DAB

6.3.2 Borrowings

The share of borrowings in total funding structure of the system decreased by 19.20 percent standing at AF 3.59 billion at the end of December 2016, making 1.36 percent of total liabilities in comparison with 11.83 percent increase in the preceding year. The current borrowing position is attributed to three banking institutions.

IV. LIQUIDITY

Liquidity risk can be defined as the risk of not having sufficient liquid assets to meet the demand of borrowers and depositors. All banks are required to maintain a reasonable level in order to avoid any liquidity problem. For this reason, banks should maintain an asset liability committee (ALCO); one of its tasks is the liquidity management of the bank through gap analysis, stress testing,

scenario analysis, cash flow analysis, etc.
according to policies of the bank.

Table 7.3: 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)	(Dec. 2016)
Total Capital Adequacy Ratio	25.81	-14.46	30.39	23.06	21.84	26.34	26.46	19.94	27.68
Tier 1 Capital Adequacy Ratio	24.19	-14.51	30.29	23.98	19.97	24.65	26.09	19.66	22.93
Non-Performing Loans to Total Gross Loans	0.5	48.4	3.75	5.15	5.31	5.1	8.09	12.34	12.67
Return on Assets (ROA)	1.41	-20.08	0.24	-1.21	-0.54	0.74	0.90	0.20	1.55
Return on Equity (ROE)	10.35	-520.66	1.9	-17.9	-7.17	10.03	7.35	1.69	15.38
liquidity Ratio (Broad Measure Median)	59.19	63.32	63.83	57.37	72.13	67.93	73.6	68.22	67.74
liquidity Assets to Total Assets	0.38	40.58	47.01	55.82	63.75	73.18	73.28	75.05	71.98

*Excluding New Kabul Bank

Source: Financial Supervision Department/ DAB

7.4.1 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. 71.98 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 67.74 percent. All

banking institutions were well above the minimum required level. See table 7.4.

V. CAPITAL

The system is well capitalized. The capital fund of the banking sector stands at AF 33.91 billion; increased by 37.43percentage points or AF 9.23billion over the last year. The increase in total financial capital is mainly attributed to profits and capital injection.

On an aggregate basis, the Capital Adequacy Ratio of the banking sector stands at 27.68 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). The Basel benchmark for capital to risk weighted is 8 percent.

VI. PROFITABILITY

On a cumulative basis for the year ending December 2016, the banking sector earned AF 4.29 billion net profit as compared to AF

522 million net profits in December 2015, showing huge increase over the year.

The increase in profitability of the banking sector as evident from the table 6.5 P/L is mostly ascribed to significant increase in non-interest income, other contributing factor was decrease in credit provision and interest expense, while operating cost showed increase in the year under analysis. (Table 7.4)

The returns on assets (ROA) stand at 1.55 percent annualized from 0.20 percent annualized and return on equity (ROE) became 15.38 percent annualized from 1.69 percent annualized in last year.

Table 7.4: P/L Schedule

Items	1394 (Dec. 2015)	1395 (Dec. 2016)	%change Y-o-Y
Interest income	9,076	9,054	-0.25
Interest expense	2,044	1,813	-11.29
Net interest income	7,032	7,240	2.96
Non-interest income	5,243	10,005	90.83
Non-interest expenses	5,607	5,846	4.26
Salary cost	3,687	3,751	1.72
Credit provisions	2,952	2,354	-20.26
P/L before tax	762	5,271	591.89
P/L after tax	522	4,293	721.92

Source: Financial Supervision Department, DAB

On a cumulative basis, three banking institutions have incurred AF 1.19 billion losses in the year under analysis against AF 1.28 billion losses posted by four banks in the last year December 2016.

On core income basis, three banks ended with losses, against two banks in the last year.

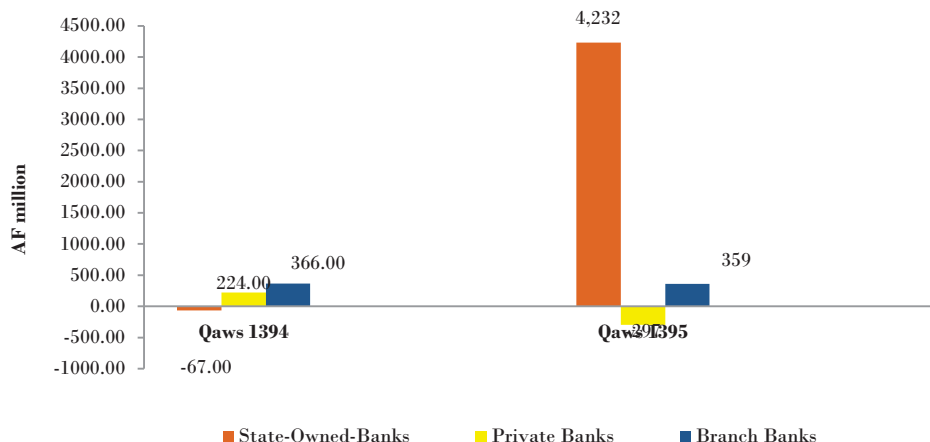
Group wise analysis reveals that State-Owned Banks (SOB) and branches of foreign banks (BFB) ended up with profits in

the year under analysis while Private Banks (PB) occur loss in December 2016.

(Figure 7.10)

Major portion of the profitability of the banking sector is attributed to State-Owned Banks standing at AF 4.23 billion and branches of foreign banks at AF 359 million profits in December 2016, while Private Banks ended up with loss of AF 297 million in December 2016.

Figure 7.10: Profitability of the Banking Sector



Source: Financial Supervision Department, DAB

Figure 7.11: ROE & ROA of the banking sector

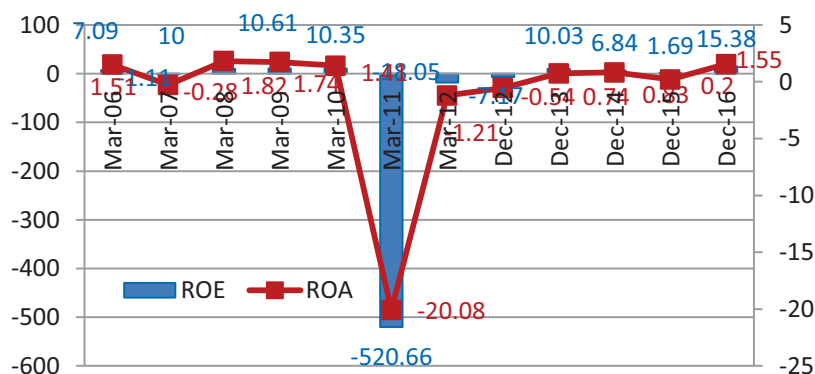
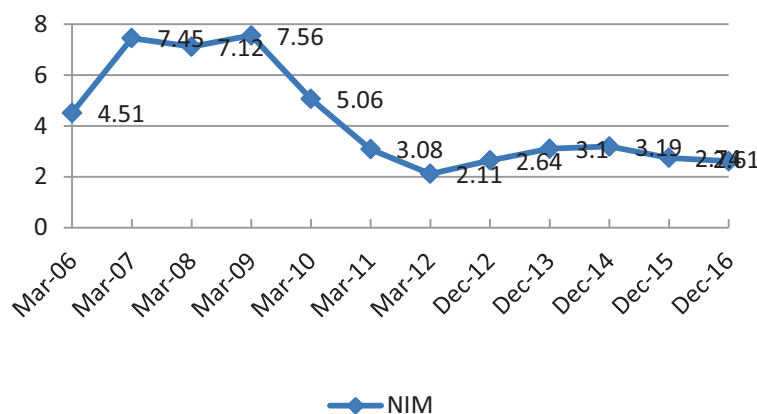


Figure 7.12: Net Interest Margin



Source: Financial Supervision Department, DAB

IV. 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 seven banking institutions that are holding open FX positions on overall and on an individual currency (USD long and short position, EURO long position) basis and violated the limits. Those banks need to bring their FX positions under the set limit otherwise; depreciation (decrease in the value) of US dollar can lead the banks to more losses.

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 1.61 billion and vice versa.

Similarly, a 4 percent change would correspond to AF 323 million 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 AF 1.41 billion in the event of increase in the market interest rate (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 AF 1.41 billion. For three 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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