Da Afghanistan Bank

Economic & Statistical Bulletin

Annual Bulletin FY1394

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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 describes developments in the fiscal year 1394, which covers December 21, 2014 to December 20, 2015.

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ABBREVIATIONS

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

Senior Management

H.E. Khalil Sediq

Governor

Khan Afzal Hadawal

First Deputy Governor

Alhaj Essa Khan Turab

Second 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 2015 annual statistical bulletin provides a comprehensive account of the Afghan economy in 2015. In this bulletin you will find thorough analysis of the developments that has been taken place in all sectors of the economy in 2015 as well as succinct examination of the challenges faced by all sectors.

Over the fiscal year 2015 Afghanistan continued to struggle with an array of constraints and formidable challenges on economic front emanating from mass immigration, considerable capital flight, deteriorating security and most importantly from economic and political uncertainty. As a result Afghan economy plunged into recession and registered a negative growth of 2.2 percent in fiscal year 2015. All three sector of the economy failed to deliver anticipated performance with agriculture sector being the main driver of meltdown of Afghan economy in 2015, registering a growth of -16.9 percent in 2015 compared to a growth of 3.7 percent in 2014. Industry and services sector, however, had positive growth of 1 percent and 1.3 percent respectively. Meanwhile, in core measures of inflation, there is a decrease recorded in 30% trimmed mean. Inflation by this measure reached to 2.2 percent (y-over-y) compared to 4.3 percent in the previous year.

DAB achieved all quantitative targets under Staff Monitored Program (SMP) of IMF as well as completed actions for structural benchmarks. In the fiscal year 2015 reserve money (Da Afghanistan Bank's operational target) grew at 3.16 percent, standing at AF 232,323.5 million at the end of the year. The actual reserve money growth remained well below from the end year revised target of 7 percent. Currency in Circulation; the indicative target of DAB; increased by 2.63 percent, reaching AF 202, 169.3 million.

Turbulent economic and political environment of the country also left its imprints on external sector. Available data shows that the deficit in the current account increased to USD 4,809.97 million against of USD 4,020.25 million recorded in the previous year. Similarly, the capital account of the balance of payments illustrated a decline of 51 percent in the FY 1394 when compared to the FY 1393, as a result of lower inward capital transfers

On the fiscal front, implementation of new taxation measures and institutional reforms resulted in pick-up of domestic revenue (both tax and non-tax revenue). The total revenue collection in 2015 exceeded the target level of AF 114.2 billion by 23 percent reaching AF 123.4 billion.

Banking sector earned net profits amounting to AF 522 million for the year 2015 or fiscal year 1394, against AF2.02 billion net profit in the previous year. Private Banks and Branches of Foreign banks ended up with profits, while State-Owned Banks ended with losses during the fiscal year 2015. It is worth mentioning that the asset base of the banking strengthened in the FY 2015 by 5.48 percent or AF 13.99 billion.

1

GLOBAL ECONOMIC ENVIRONMENT

1

GLOBAL ECONOMIC ENVIRONMENT

Global growth remained moderate during 2015, with uneven performance across the major countries and regions. Global growth was estimated around 3.1 percent in 2015, slightly lower than 3.4 percent in 2014. Relative to 2014, the growth rate improved for advanced economies during 2015, while growth in emerging market and developing economies seemed to be lower, primarily reflecting weaker performance of some large emerging market economies and oil-exporting countries. However, global economic growth in 2016 is expected to increase to 3.6 percent in light of the modest recovery in advanced economies and higher growth prospects for emerging markets and developing economies unless there is substantial spill-over of Chinese slowdown on these economies. The growth rate of advanced economies was 2 percent in 2015 and expected to increase to 2.2 percent in 2016. However, the growth rate of emerging economies was estimated about 4 percent in 2015, 0.6 percentage point lower than 2014 and expected to increase to 4.5 percent in 2016. Growth rate of the United States was estimated around 2.6 percent in 2015 and is expected to increase to 2.8 percent in 2016. The economic recovery in the euro area seems broadly on track with a generally robust recovery in domestic demand and rising inflation. The economic recovery has been reasonable in the euro area, domestic demand increased and the growth was estimated to be about 1.5 percent in 2015.

Growth projections have been revised upward for many euro area economies, but in Greece, unfolding developments are likely to take a much heavier toll on economic activities relative to earlier expectations. In Japan, growth in the first quarter of 2015 was stronger than expected reaching 0.6 percent mainly supported by a pickup in capital investment. However, consumption remains sluggish and more than half of quarterly growth stemmed from changes in inventories.

The growth in emerging market and developing economies in 2015 declined as a result of lower commodity prices, slower capital inflows, embargoes and conflicts in a number of countries and the gradual fall in growth in China. The slowdown reflects the dampening impact of lower commodity prices and tighter external financial conditions—particularly in Latin America and oil exporting countries, the rebalancing in China, and structural bottlenecks, as well as economic distress related to geopolitical factors, particularly in the Commonwealth of Independent States and some countries in the Middle East and North Africa. Growth rate of China decreased to 6.8 percent in 2015 from a growth rate of 7.3 percent in 2014. India's economic growth remained almost unchanged in 2015 and projected to be 7.5 percent in 2016 taking advantage of the recent policy reforms and gradual increase in investment.

Consumer prices in advanced economies decreased to about 0.3 percent in 2015 from 1.4 percent in 2014. In contrast, consumer prices in emerging markets and developing economies increased to about 5.6 percent in 2015 from 5.1 percent in 2014. However, it is expected that declining oil and other commodities prices will reduce the overall consumer prices by 0.5 percentage points restoring it to 5.1 percent again in 2016.

The world trade growth decreased from 3.3 percent in 2014 to 3.2 percent in 2015. The balance of trade in advanced economies deteriorated in 2015, since export growth was weaker than import growth during the period. The growth rate of imports for advanced economies increased from 3.4 percent in 2014 to 4 percent in 2015. In emerging markets and developing economies, growth rate of imports declined from 3.6 percent in 2014 to 1.3 percent in 2015. Exports of advanced economies grew by 3.1 percent in 2015, while the same in emerging markets and developing economies grew by 3.9 percent to 4.8 percent during the same years.

2

MONETARY AND CAPITAL MARKET DEVELOPMENTS

2

MONETARY AND CAPITAL MARKET DEVELOPMENTS

Monetary and capital market developments provides a relatively detailed account of monetary program, monetary aggregates, foreign exchange rates, net international reserves, as well as the open market operations.

In the fiscal year 2015 (22 Dec. 2014 to 21 Dec. 2015) reserve money -Da Afghanistan Bank's operational target- grew at 3.16 percent, standing at AF 232,323.5 million at the end of the year. The actual reserve money growth remained well below from the end year revised target of 7 percent. Currency in circulation which is an indicative target of DAB has increased by 2.63 percent in the year under review, reaching AF 202,169.3 million. DAB also experienced a considerable drop of 3.26 percent on its net international reserve (NIR) level which is equivalent to USD 219.76 million.

Narrow money (M1), stood at AF 389,916 million at the end of the year under review, registering an annual growth of 1.5 percent (Y-o-Y). Broad money (M2) demonstrated similar behavior, representing a growth rate of 3.30 percent (Y-o-Y) standing at AF 414,819 million at the end of the fiscal year 2015.

In order to control the reserve money growth, DAB utilizes monetary instruments of FX auction and selling of capital notes under the open market operations.

In the fiscal year 2015, DAB has auctioned a total amount of USD 2,797.3 million to manage the liquidity in the market as well as to mitigate the unnecessary fluctuations in the exchange rate of Afghani against the foreign currencies. The total outstanding amount of CNs stood at AF 32.678 billion at the end of year under review.

Meanwhile, in the fiscal year 2015 Afghani depreciated against the US dollar by 17.166 percent.

I – MONETARY PROGRAM

According to the monetary policy framework (MPF), of DAB's monetary policy department, reserve money remained the key operational target (performance criterion) in the period under review or FY 2015, while currency in circulation was set as the indicative target.

To determine the amount of reserve money (RM) for purpose of supporting domestic price stability, which is DAB's primary objective, DAB uses quantitative theory of money. Hence, the assigned targets for RM and CIC are based on expected economic growth and expected inflation during the concerned period. For the fiscal year 2015 the ceilings for reserve money and currency in circulation growth were set at 11% but during the course of the year the growth rate were revised downward to 7% because of low level economic activities and decline in demand for Afghani during the FY 2015. Actual RM growth was figured out to 3.16 percent and actual CIC growth was 2.63 percent which are well below from the revised target of the FY2015. The low actual RM and CIC growth signal a sluggish economic activity driven mainly by over all security concerns and increasing level of migration from the country. In addition to this higher revenue collection by ministry of finance also played its role in limiting the growth of RM and CIC during fiscal year 2015. Meanwhile, DAB continued to conduct a tight monetary policy in the reporting period in order to absorb excess liquidity as well as to prevent volatility in the nominal exchange rate of Afghani against foreign currencies. The Figure 2.1 and 2.2 present the ceiling and the actual reserve money and currency in circulation for the year under review.

Figure 2.1: Reserve Money for the FY 1394 (Dec.14 to Dec15)

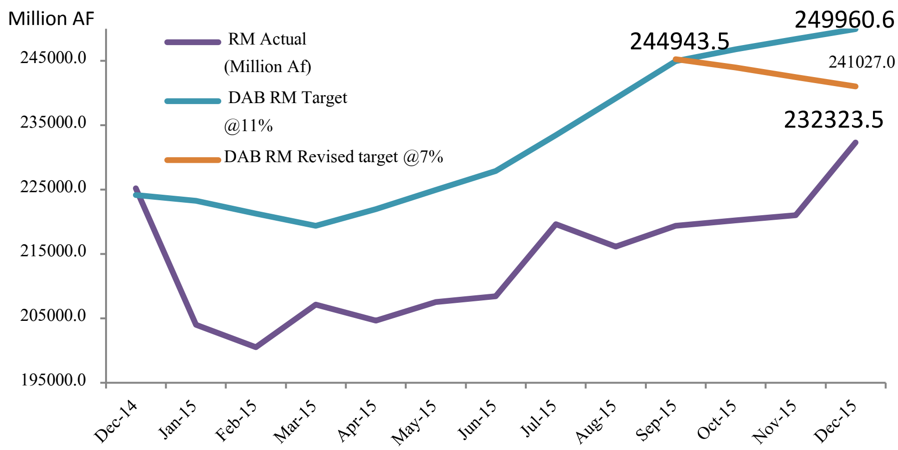
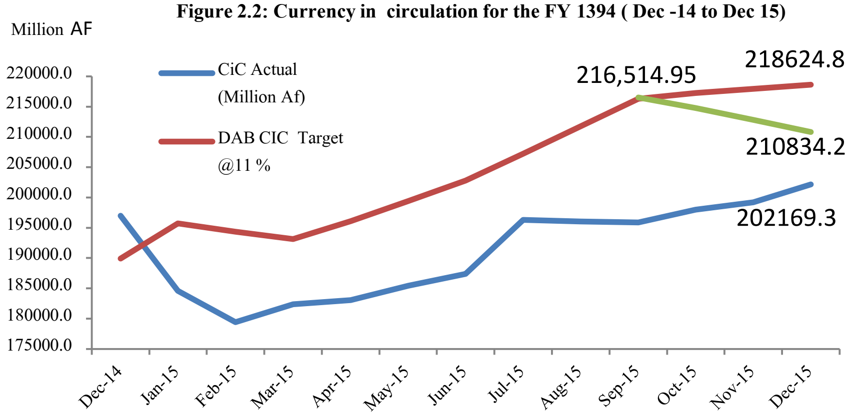


Figure 2.2: Currency in circulation for the FY 1394 (Dec -14 to Dec 15)



Source: *Monetary Policy Department/DAB*

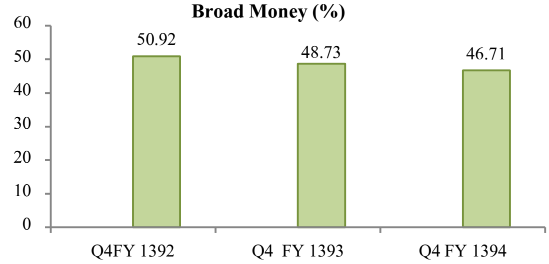
II. MONETARY AGGREGATES

The Monetary Section of the Monetary Policy Department compiles monetary aggregates - narrow money (M1), and broad money (M2) in accordance to the Monetary and Financial Statistics (MFS) methodology and definition.

Narrow money, includes all banknotes, coins, demand deposits, and other liquid assets of the commercial banks with the central bank, while broad money includes narrow money components and other less liquid assets or quasi money.

As shown in Table 2.1 narrow money (M1) grew by 1.5 percent in FY2015 compared to 9.5 percent in FY2014, showing a difference of AF 5,764 million. Currency outside depository corporations or CIC, a major component of M1 (50.3%), grew by 4.08 percent in 2015 compared to 16.4 percent in the previous year. The difference in currency outside depository corporations in 2015 compared to 2014 is AF 7,683 millions. Demand deposits which are the other component of M1 experienced a negative growth of (- 0.98) percent at the end of FY2015 while Its growth was 3.7 percent in previous year which was AF1, 919 million higher than current year.

Figure 2.3: Demand Deposits as Share of Broad Money (%)



Source: *Monetary Policy Department/DAB*

The supply of broad money (M2) expanded by AF 414,819 million in the year under review from AF 401,583 million in the previous year showing a difference of AF 13,237 million. This shows an increase of 3.3 percent in 2015 down from 8.3 percent in the previous year. The current period figures show that M1 remained as the main contributing component of M2 (94%).

Quasi money or time deposits of commercial banks, which is the other component of M2, grew by 42.87 percent (y-o-y) at the end of 2015. Quasi money constitutes only 6 percent of broad money during the period under review, although higher than 4.34 percent in FY 2014 but still the impact of changes in quasi money on the M2 is negligible. The year-on-year difference of Afghani denominated time deposits stood at AF 2,397 million, while the foreign currency denominated time deposits recorded AF 5,076 Million AF45.98 and 41.55 percents higher than previous year. Afghani-denominated time deposits constitute 1.83 percent of broad money. While, the share of foreign currency denominated time deposits stood at 4.17 percent of M2.

Demand deposits as a share of broad money decreased to 46.71 percent (Y-o-Y) in the year under review, down from 48.73 percent in the previous year (Figure 2.3).

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

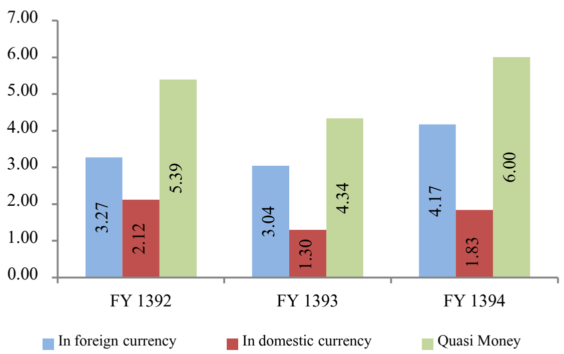
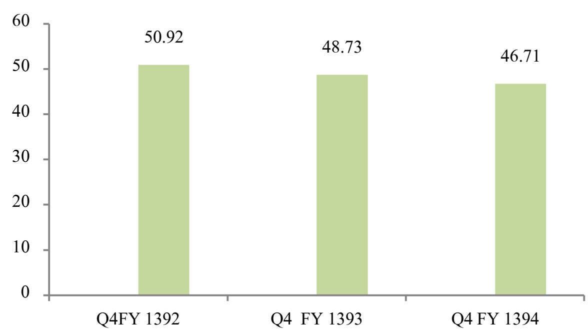


Figure 2.3: Demand Deposits as Share of Broad Money (%)



Source: *Monetary Policy Department/DAB*

Table 2.1: Monetary Aggregate for the FY 2015 (Dec 14 - Dec 15)

Figures in million AF, unless otherwise indicated

In Million AF	Q4 2013 Amount	Q4 2014 Amount	Δ Y-o-Y	Difference	Q4 2015 Amount	Δ Y-o-Y	Difference
1-Net Foreign Assets	483,924	487,005	0.6%	3,081	532,494	9.34%	45,489
(a) Foreign Assets	513,630	514,730	0.2%	1,100	563,699	9.51%	48,969
DAB Foreign exchange reserves	421,774	427,621	1.4%	5,847	467,588	9.35%	39,967
Gold	60,424	47,509	-21.4%	0.000	51,513	8.43%	0.000
Other	361,350	380,112	5.2%	18,762	416,075	9.46%	35,962
Other foreign assets	91,856	87,109	-5.2%	-4,747	96,111	10.33%	9,002
(b) Foreign liabilities	29,706	27,725	-6.7%	-1,981	31,205	12.55%	3,480

2. Net Domestic Assets	-113,243	-85,422	-24.6%	27,821	-117,552	37.61%	-32,130
(a) Net Domestic Credit	-45,675	-28,672	-37.2%	17,003	2,013	-107.02%	30,685
Net Credit to Nonfinancial Public Sector	-91,139	-71,216	-21.9%	19,923	-43,155	-39.40%	28,061
Net Credit to Central Government	-90,929	-71,099	-21.8%	19,830	-43,249	-39.17%	27,850
Credit to Central Government	33,709	32,899	-2.4%	-810	61,206	86.04%	28,306
Liabilities to Central Government	124,638	103,999	-16.6%	-20,639	104,455	0.44%	457
Net Credit to State & Local Government	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Net Credit to Public Nonfinancial Corporations	-210.020	-116.324	0.000	94	94.346	0.000	211
Credit to Private Sector	46,813.544	43,943.424	0.000	-2,870	46,646.260	0.000	2,703
Net Credit to Other financial Corporations	-1,349	-1,400	3.7%	-50	-1,478.30	5.62%	-79
(b) Capital Accounts	110,484	100,220	-9.3%	-10,263	151,120	50.79%	50,899
(c) Other Items Net	42,916	43,471	1.3%	554	31,555	-27.41%	-11,915
3- Broad Money (M2)	370,684	401,583	8.3%	30,899	414,819	3.30%	13,237
Narrow Money (M1)	350,696	384,152	9.5%	33,456	389,916	1.50%	5,764
CiC (Currency outside depository corporations)	161,944	188,451	16.4%	26,507	196,134	4.08%	7,683
Demand Deposits	188,751	195,701	3.7%	6,950	193,782	-0.98%	-1,919
Other Deposits (Quasi Money)	19,988	17,431	-12.8%	-2,557	24,904	42.87%	7,473
In Afghani	7,867	5,214	-33.7%	-2,653	7,611	45.98%	2,397
In Foreign currency	12,121	12,217	0.8%	96	17,293	41.55%	5,076
Securities Other Than Shares		0.000	0.000	0.000	0.000	0.000	0.000

***Source:** Monetary Survey, Monetary Policy Department/ DAB*

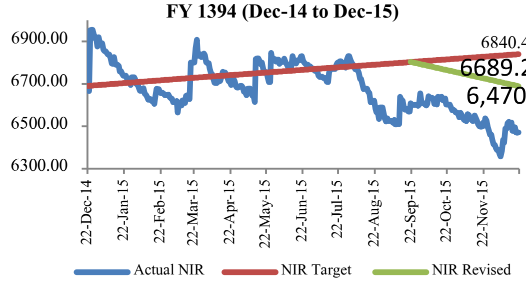
2.1 Net International Reserve

Da Afghanistan Bank holds international reserves which 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 dollars is defined as reserve assets minus reserve liabilities.

NIR decreased by 3.28 percent, USD 219.76 million, in FY2015, while it had an increase of USD 394 million in the FY2014. For the fiscal year 2015, the NIR accumulation floor was set at USD 150 million and later in the course of the year it was revised and set at minus USD1.25 million, but in real ground we experienced a larger de-accumulation of actual NIR, at the end of the fiscal year 2015 NIR stood at USD 6470.7 at the end of fiscal year 2015 while at the start of the year the amount was USD 6690.47 millions.

Figure 2.5 explains the trend of NIR actual and target during FY2015.

Figure 2.5: NIR Actual and target in million USD for the FY 1394 (Dec-14 to Dec-15)



***Source:** Monetary Survey, Monetary Policy Department/ DAB*

III. FROEIGN EXCHANGE MARKET

3.1 Foreign Exchange Rates

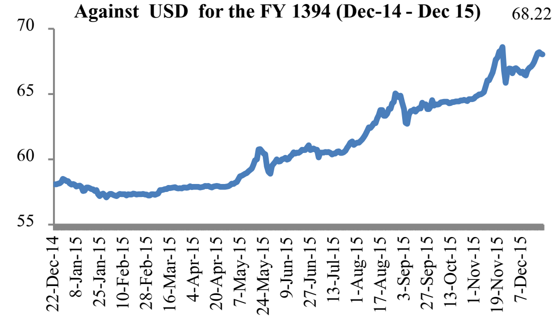
Da Afghanistan Bank (DAB's) ultimate goal is to maintain price stability but besides of its primary goal the DAB also consider the fluctuations of foreign exchanges at foreign exchange market. In order to achieve and maintain its primary goal, DAB tries to utilizes its monetary instruments effectively with sound policy implementation.

During FY 2015 the Afghani depreciated against the dollar and euro and many other currencies. Pressure on the weakening Afghani was mainly triggered by the persistently high current account deficit, USD global appreciation due to United States economic growth and monetary easing policy, as well as domestic factors emanating from national political and security situations.

The daily historic review of the average exchange rate of AF against the U.S. dollars for the fiscal year 2015 is shown in figures below.

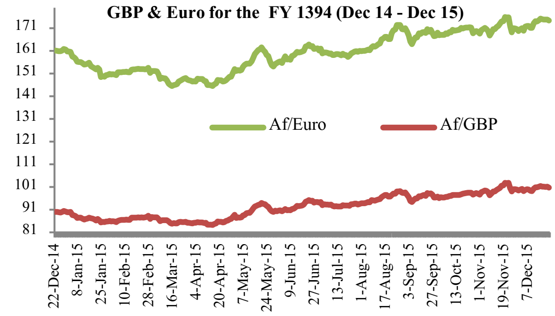
Afghani depreciated against the U.S dollar by 17.17 percent, traded at AF 68.05 per U.S. dollar at the end of the year under review. In addition, Afghani depreciated against the INR and PKR by 9.57 and 10.5 percents respectively. Meanwhile, Afghani deprecation recorded against the Euro, GBP and IRR by 3.61 percent, 11.86 percent and 12.05 percent respectively.

Figure 2.6: Daily Average Ex- Rate of Afghani Against USD for the FY 1394 (Dec-14 - Dec 15)



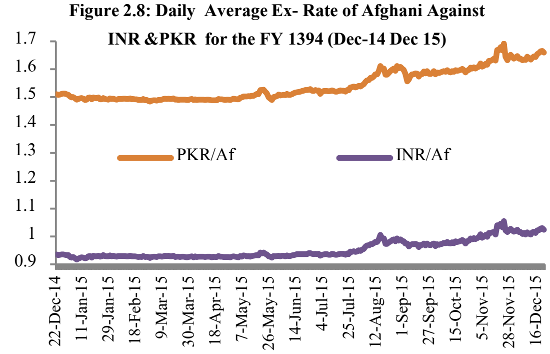
Source: *Monetary Survey, Monetary Policy Department/ DAB*

Figure 2.7: **Daily Average Ex-Rate of Afghani against GBP & Euro for the FY 1394 (Dec 14 - Dec 15)**



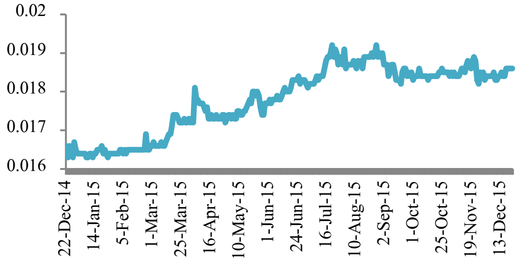
Source: *Monetary Survey Section, M PD/ DAB*

Figure 2.8: Daily Average Ex- Rate of Afghani Against INR &PKR for the FY 1394 (Dec-14 Dec 15)



Source: *Monetary Survey Section, M PD/ DAB*

Figure 2.9: Daily Average Ex- Rate of Afghani Against IRR for the FY 1394 (Dec-14 Dec 15)



Source: *Monetary Survey, Monetary Policy Department/ DAB*

3.2 Foreign Exchange Auction

In order to control the money supply, DAB anchors reserve money by conducting bi-weekly foreign exchange auctions (DAB recently auctioning USD three times each week), and a weekly capital notes auction, which are the primary monetary instruments used by DAB. DAB 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 2015 DAB auctioned a total of USD 2.793 billion; when the total demand was USD 3.924 billion. On average, 38 bidders participated in each auction and 32 bids were the winning bids with the average amount of USD 27.7 million; while the data for FY 2014, recorded total awarded amount at USD 3.341 billion, with a total demand of USD 4.698 billion. On average, 37 bidders participated in each auction and 32 bids were awarded with an average amount of USD 34.81 millions.

Table 2.2: Foreign Exchange Auction's Summery for FY 2015 (million USD)

Auction Date	No of Bidders	Highest Price	Lowest Price	Market Ex Rate	Cut off Price	Amount Announced	Amount Awarded	Total Demand
23-Dec-14	38.0	58.1	57.9	58.1	58.1	40.0	40.2	65.5
27-Dec-14	38.0	58.3	58.0	58.3	58.3	40.0	40.8	65.6
30-Dec-14	37.0	58.3	58.1	58.3	58.3	50.0	52.4	63.5
4-Jan-15	33.0	58.1	57.8	58.1	58.0	50.0	44.4	47.8
6-Jan-15	35.0	58.0	57.5	58.1	57.9	50.0	50.2	61.8
10-Jan-15	35.0	58.0	57.8	58.0	58.0	45.0	45.2	56.3
13-Jan-15	34.0	57.6	57.3	57.6	57.6	40.0	34.6	48.2
17-Jan-15	38.0	57.8	57.6	57.8	57.8	40.0	42.6	47.7
20-Jan-15	34.0	57.5	57.4	57.7	57.5	40.0	35.2	44.0
24-Jan-15	33.0	57.2	56.8	57.3	57.1	40.0	27.8	38.4
27-Jan-15	33.0	57.3	56.8	57.3	57.2	35.0	31.5	41.3
31-Jan-15	30.0	57.3	57.0	57.3	57.3	30.0	28.0	35.8
3-Feb-15	31.0	57.2	57.1	57.2	57.2	30.0	30.5	39.2
7-Feb-15	36.0	57.4	57.0	57.4	57.4	25.0	26.9	39.6

10-Feb-15	32.0	57.3	57.1	57.3	57.2	30.0	29.7	37.3
14-Feb-15	34.0	57.3	57.1	57.3	57.3	30.0	23.4	35.6
17-Feb-15	36.0	57.4	57.1	57.3	57.4	25.0	24.5	37.8
21-Feb-15	33.0	57.3	57.0	57.3	57.3	25.0	22.6	30.3
24-Feb-15	33.0	57.4	57.3	57.4	57.3	20.0	18.0	24.0
28-Feb-15	38.0	57.3	57.1	57.2	57.2	20.0	13.8	21.4
3-Mar-15	38.0	57.3	57.0	57.3	57.3	15.0	13.2	24.6
7-Mar-15	31.0	57.5	57.4	57.4	57.4	10.0	10.0	15.5
10-Mar15	34.0	57.7	57.5	57.7	57.7	15.0	14.8	25.0
14-Mar15	34.0	57.8	57.4	57.8	57.8	20.0	25.3	30.4
17-Mar15	36.0	57.8	57.6	57.8	57.8	25.0	25.2	31.0
24-Mar15	34.0	57.8	57.3	57.8	57.7	35.0	33.0	42.3
28-Mar15	35.0	57.8	57.5	57.9	57.8	25.0	25.4	32.8
31-Mar15	36.0	57.9	57.4	57.9	57.9	25.0	35.1	41.1
4-Apr-15	30.0	57.8	57.5	57.9	57.8	35.0	32.9	45.7
7-Apr-15	33.0	57.9	57.3	57.9	57.8	35.0	35.0	42.7
11-Apr-15	32.0	57.9	57.8	58.0	57.9	35.0	35.1	38.3
14-Apr-15	33.0	57.9	57.5	57.9	57.8	35.0	35.2	43.5
18-Apr-15	34.0	57.9	57.7	57.9	57.9	30.0	30.5	40.5
21-Apr-15	36.0	57.9	54.8	57.9	57.8	30.0	30.7	41.2
25-Apr-15	33.0	57.9	57.8	57.9	57.9	30.0	30.1	42.1
2-May-15	33.0	58.1	56.5	58.1	58.1	30.0	22.3	40.4
5-May-15	35.0	58.6	58.3	58.5	58.5	20.0	20.1	32.1
9-May-15	36.0	58.8	58.1	58.8	58.8	25.0	25.0	35.8
12-May15	39.0	59.1	58.0	59.1	59.1	35.0	33.4	52.1
16-May15	38.0	59.6	58.6	59.6	59.6	30.0	29.8	46.7
19-May15	38.0	60.9	59.5	60.8	60.8	30.0	35.5	47.9
23-May15	41.0	60.5	59.8	60.4	60.4	33.0	33.3	48.2
26-May15	39.0	59.1	58.1	59.5	59.1	30.0	29.8	43.3
30-May15	40.0	59.8	59.3	59.7	59.7	25.0	24.7	38.8
2-Jun-15	40.0	59.9	58.8	59.8	59.8	28.0	26.2	38.1
6-Jun-15	36.0	60.1	59.6	60.0	60.0	26.0	24.1	34.1
9-Jun-15	36.0	60.0	59.6	60.0	60.0	24.0	18.1	33.7
13-Jun-15	39.0	60.6	60.2	60.5	60.6	18.0	18.7	31.7
16-Jun-15	39.0	60.6	60.0	60.5	60.5	18.0	18.4	27.7
22-Jun-15	36.0	60.7	60.4	60.7	60.7	35.0	32.0	44.8
27-Jun-15	37.0	60.8	60.7	60.8	60.8	25.0	26.3	40.2
30-Jun-15	36.0	60.7	60.1	60.7	60.7	25.0	20.7	35.0
4-Jul-15	35.0	60.5	60.2	60.5	60.5	20.0	19.7	28.6
7-Jul-15	33.0	60.6	60.0	60.5	60.5	20.0	17.8	27.9
11-Jul-15	32.0	60.4	59.1	60.4	60.3	20.0	18.1	25.7
14-Jul-15	34.0	60.6	60.3	60.6	60.6	18.0	18.1	27.2
25-Jul-15	36.0	61.1	60.5	61.1	61.1	18.0	18.4	28.7
28-Jul-15	35.0	61.1	60.1	61.1	61.1	30.0	30.1	42.0
1-Aug-15	39.0	61.4	61.3	61.3	61.3	30.0	30.7	46.8

4-Aug-15	40.0	61.8	61.0	61.7	61.7	30.0	29.5	45.2
8-Aug-15	42.0	62.7	62.1	62.5	62.1	30.0	38.9	38.9
11-Aug-15	48.0	62.8	62.1	62.8	62.6	30.0	38.2	53.9
15-Aug-15	41.0	63.3	62.1	63.4	63.0	35.0	35.7	58.2
18-Aug-15	52.0	63.3	62.8	63.3	63.1	40.0	40.8	66.4
22-Aug-15	40.0	63.5	63.0	63.5	63.4	40.0	40.5	75.9
25-Aug-15	42.0	64.4	63.1	64.3	64.3	40.0	50.1	72.4
29-Aug-15	51.0	64.9	63.1	64.4	64.7	40.0	40.2	61.8
1-Sep-15	47.0	64.4	63.1	64.4	64.1	40.0	38.2	48.8
7-Sep-15	50.0	63.5	63.0	63.4	63.4	35.0	35.7	57.8
12-Sep-15	34.0	63.7	62.0	63.8	63.5	35.0	26.7	38.0
15-Sep-15	42.0	63.9	63.4	63.9	63.9	30.0	32.4	46.7
19-Sep-15	44.0	64.2	63.2	64.2	64.1	30.0	30.4	41.5
22-Sep-15	34.0	63.9	63.1	63.9	63.8	20.0	20.0	29.3
29-Sep-15	37.0	64.6	64.1	64.5	64.5	25.0	30.6	34.5
3-Oct-15	37.0	64.2	63.3	64.1	64.1	25.0	21.6	28.8
6-Oct-15	30.0	64.4	64.1	64.4	64.3	25.0	20.35	28.5
10-Oct-15	29.0	64.4	64.0	64.4	64.4	25.0	20.8	29.0
13-Oct-15	32.0	64.4	64.0	64.4	64.4	20.0	17.8	26.0
17-Oct-15	27.0	64.5	64.1	64.5	64.4	20.0	16.3	22.3
20-Oct-15	28.0	64.5	64.2	64.5	64.5	20.0	16.5	23.5
25-Oct-15	29.0	64.5	64.3	64.5	64.4	20.0	15.5	22.6
27-Oct-15	37.0	64.6	64.5	64.6	64.6	22.0	20.2	29.4
31-Oct-15	39.0	64.7	64.3	64.7	64.7	22.0	20.8	31.5
3-Nov-15	39.0	65.0	64.8	65.0	65.0	25.0	24.7	36.2
7-Nov-15	34.0	65.2	65.0	65.2	65.1	25.0	22.0	30.4
10-Nov-15	33.0	66.2	65.1	65.4	66.1	25.0	27.9	43.7
14-Nov-15	42.0	66.7	65.7	66.6	66.6	30.0	27.2	38.9
17-Nov-15	46.0	67.7	66.6	67.6	67.6	40.0	38.1	57.5
21-Nov-15	46.0	68.4	67.1	68.3	68.3	40.0	37.2	47.5
23-Nov-15	30.0	67.0	65.0	66.8	66.3	30.0	30.5	32.7
25-Nov-15	42.0	65.8	62.2	65.9	65.6	30.0	30.8	40.4
28-Nov-15	45.0	67.1	66.1	67.0	67.0	25.0	25.5	42.2
30-Nov-15	46.0	67.0	65.0	66.6	66.5	25.0	26.8	37.0
2-Dec-15	47.0	66.9	66.5	67.0	66.8	25.0	26.2	33.3
5-Dec-15	36.0	66.7	66.1	66.8	66.5	18.0	23.9	24.5
7-Dec-15	42.0	66.7	66.4	66.7	66.6	15.0	18.1	24.2
9-Dec-15	50.0	66.4	66.2	66.4	66.3	16.0	16.1	23.4
12-Dec-15	51.0	67.1	66.8	67.0	67.0	12.0	11.3	18.1
14-Dec-15	55.0	67.3	67.1	67.2	67.2	14.0	14.3	23.1
16-Dec-15	57.0	67.8	67.1	67.8	67.8	15.0	16.5	24.0
19-Dec-15	56.0	68.3	67.3	68.2	68.3	15.0	16.1	23.2
Total						**2,842**	**2793.6**	**3924.1**

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

IV. CAPITAL MARKET & LIQUIDITY CONDITIONS

4.1 Capital Note Auctions

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.

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

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

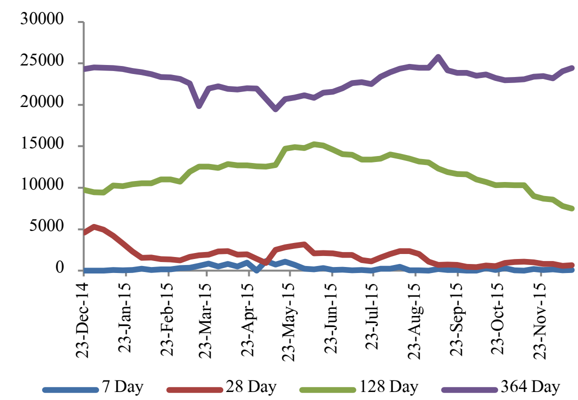
Total outstanding stock of capital notes reached AF 32.7 billion at the end of the fiscal year 2015, which shows a decrease of 13.5 percent compared to AF37.8 billion the end of fiscal year 2014, . The decrease in the level of securities shows the decrease of Afghani demand by banking sector and gives the signal for increase of FX auction level which may cause the decrease of DAB reserve position.

The outstanding stock of 7 day notes which was recently to CN by DAB, stood at AF 100 million, experiencing higher volume during the first half of the year and lower amount in second half of the year under review. 28 day CN outstanding amount stood at 650 million with lower amount of demand and awarded amount during the second half of the fiscal year 2015. The stock outstanding for 182 day notes stood at AF 7.496 billion at the end of FY2015. The amount of outstanding of 364 days capital notes was figured out to 24.43 recorded a volatile figure of demand and awarded amount during the fiscal year under review.

Figure 2.10 exhibits breakdown of the total outstanding stock for all maturities during the fiscal year 2015.

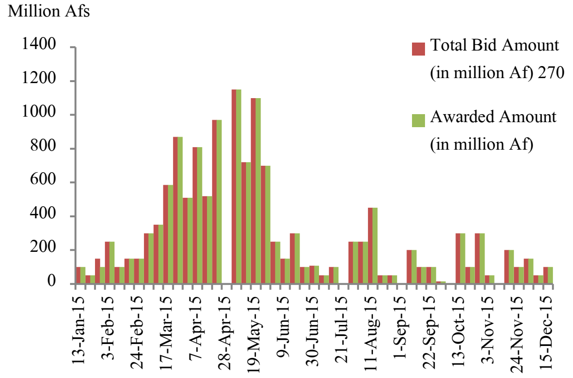
In addition the weighted average interest rate for 7 day capital note was 1.8 percent and for 28 day security it is recorded 3.544 percent, while for 182 day security, it ended at 5.172 percent and for 364 days capital notes it recorded 6.70 in the FY 2015.

Figure 2.10: Cspital Notes Outstanding FY 1394



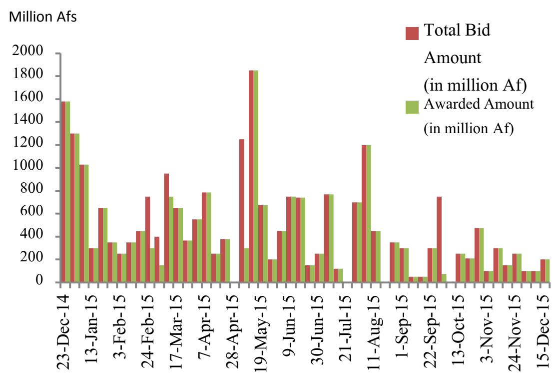
Source: *Market Operations Department/DAB*

Figure 2.11: 7 Day CNs Demand and Awarded amount



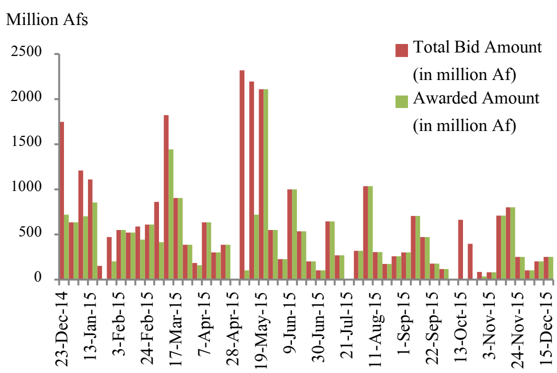
Source: *Market Operations Department/DAB*

Figure 2.12: 28 Day CNs Demand and Awarded amount



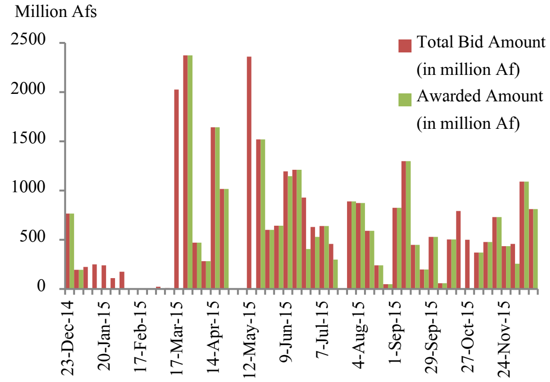
Source: *Market Operations Department/DAB*

Figure 2.13: 182 Day CNs Demand and Awarded amount



Source: *Market Operations Department/DAB*

Figure 2.14: 364 Day CNs Demand and Awarded amount



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 the DAB, which remunerated at one basis point below the cut-off rate of the last 28 day capital notes auction, or equal to the deposit facility rate. During the FY 2015 DAB has paid an amount of Afs 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.

In order to provide commercial banks with facilities to better manage their liquidity and to provide them with a proper opportunity to invest their excess reserves apart from capital notes, DAB introduced the **overnight standing facilities** in 1385 (2006-2007). However it has been temporarily called off for a short time in order to monitor its effectiveness as a monetary policy instrument which may lead to better monetary formulation. After assessment of OSF effectiveness as monetary policy tool DAB uphold the overnight standing facilities and during FY 2015 the payment of interest rate to the mentioned facility figured out to Afs 10.122 million.

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

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. (%)
23-Dec-14									
30-Dec-14									
6-Jan-15	2000	270					3		
13-Jan-15	2000	100	100	1	1	1.8	1.8	1.8	1.8
20-Jan-15	1500	50	50	2	1	1.8	1.85	1.8	1.8
27-Jan-15	1000	150	100	2	1	1.8	1.83	1.8	1.8
3-Feb-15	1000	250	250	3	3	1.8	1.8	1.8	1.8
10-Feb-15	1000	100	100	1	1	1.8	1.8	1.8	1.8
17-Feb-15	500	150	150	2	2	1.8	1.8	1.8	1.8
24-Feb-15	300	150	150	2	2	1.8	1.8	1.8	1.8
3-Mar-15	300	300	300	2	2	1.8	1.8	1.8	1.8
10-Mar-15	500	350	350	2	2	1.8	1.8	1.8	1.8
17-Mar-15	1000	585	585	4	4	1.8	1.8	1.8	1.8
24-Mar-15	500	870	870	5	5	1.8	1.8	1.8	1.8
31-Mar-15	1500	510	510	3	3	1.8	1.8	1.8	1.8
7-Apr-15	1000	810	810	5	5	1.8	1.8	1.8	1.8
14-Apr-15	1000	520	520	3	3	1.8	1.8	1.8	1.8
21-Apr-15	1000	970	970	6	6	1.8	1.8	1.8	1.8
5-May-15	1000	1150	1150	6	6	1.8	1.8	1.8	1.8
12-May-15	1500	720	720	4	4	1.8	1.8	1.8	1.8
19-May-15	1500	1100	1100	5	5	1.799	1.8	1.8	1.8
26-May-15	2000	700	700	3	3	1.797	1.8	1.8	1.798
2-Jun-15	1500	250	250	1	1	1.8	1.8	1.8	1.8
9-Jun-15	250	150	150	1	1	1.8	1.8	1.8	1.8
16-Jun-15	500	300	300	1	1	1.8	1.8	1.8	1.8
23-Jun-15	750	100	100	1	1	1.8	1.8	1.8	1.8
30-Jun-15	500	108	108	1	1	1.8	1.8	1.8	1.8
7-Jul-15	250	50	50	1	1	1.8	1.8	1.8	1.8
14-Jul-15	500	100	100	1	1	1.8	1.8	1.8	1.8
28-Jul-15	500	250	250	2	2	1.8	1.8	1.8	1.8
4-Aug-15	500	250	250	2	2	1.8	1.8	1.8	1.8
11-Aug-15	500	450	450	3	3	1.8	1.8	1.8	1.8
18-Aug-15	1000	50	50	1	1	1.8	1.8	1.8	1.8
25-Aug-15	200	50	50	1	1	1.8	1.8	1.8	1.8
1-Sep-15	1000	0	0	0	0	0	0	0	0
8-Sep-15	250	200	200	1	1	1.8	1.8	1.8	1.8
15-Sep-15	200	100	100	1	1	1.8	1.8	1.8	1.8
22-Sep-15	100	100	100	1	1	1.8	1.8	1.8	1.8
29-Sep-15	500	15	15	1	1	1.8	1.8	1.8	1.8
6-Oct-15	250	0	0	0	0	0	0	0	0
13-Oct-15	100	300	300	2	2	1.8	1.8	1.8	1.8
20-Oct-15	500	100	100	1	1	1.8	1.8	1.8	1.8
27-Oct-15	250	300	300	1	1	1.8	1.8	1.8	1.8
3-Nov-15	500	50	50	1	1	1.8	1.8	1.8	1.8
10-Nov-15	500	0	0	0	0	0	0	0	
17-Nov-15	500	200	200	1	1	1.8	1.8	1.8	1.8
24-Nov-15	500	100	100	1	1	1.8	1.8	1.8	1.8
1-Dec-15	500	150	150	1	1	1.8	1.8	1.8	1.8
8-Dec-15	650	50	50	1	1	1.8	1.8	1.8	1.8
15-Dec-15	500	100	100	1	1	1.8	1.8	1.8	1.8
Total	**35,850**	**13,678**	**13,358**						

Source: *Market Operation 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 Win Bids	Cut off Rate (%)	Low Bid (%)	Highest Bid (%)	Weighted Avg. (%)
23-Dec-14	2000	1580	1580	7	7	3.558	3.56	3.56	3.56
30-Dec-14	2000	1300	1300	5	5	3.556	3.56	3.56	3.559
6-Jan-15	2000	1030	1030	6	6	3.55	3.56	3.56	3.56
13-Jan-15	2000	300	300	2	2	3.56	3.56	3.56	3.56
20-Jan-15	2000	650	650	2	2	3.56	3.56	3.56	3.56
27-Jan-15	1500	350	350	3	3	3.559	3.56	3.56	3.56
3-Feb-15	1500	250	250	2	2	3.559	3.56	3.56	3.559
10-Feb-15	1000	350	350	2	2	3.56	3.56	3.56	3.56
17-Feb-15	1000	450	450	2	2	3.56	3.56	3.56	3.56
24-Feb-15	500	750	300	5	1	3.559	3.56	3.559	3.559
3-Mar-15	500	400	150	3	1	3.55	3.559	3.55	3.55
10-Mar-15	1000	950	750	5	4	3.545	3.57	3.55	3.548
17-Mar-15	1000	650	650	4	4	3.54	3.55	3.55	3.549
24-Mar-15	1000	365	365	4	4	3.55	3.55	3.55	3.549
31-Mar-15	1000	550	550	4	4	3.49	3.55	3.55	3.546
7-Apr-15	1500	785	785	6	6	3.546	3.55	3.55	3.549
14-Apr-15	1000	250	250	2	2	3.55	3.55	3.55	3.55
21-Apr-15	1000	380	380	5	5	3.55	3.55	3.55	3.55
5-May-15	1500	1250	300	8	1	3.549	3.55	3.549	3.549
12-May15	1250	1850	1850	7	7	3.5	3.549	3.549	3.529
19-May15	1500	675	675	5	5	3.53	3.549	3.549	3.541
26-May15	1000	200	200	1	1	3.549	3.549	3.549	3.549
2-Jun-15	1500	450	450	2	2	3.54	3.548	3.548	3.545
9-Jun-15	2000	750	750	4	4	3.546	3.549	3.549	3.547
16-Jun-15	1500	740	740	6	6	3.53	3.549	3.549	3.543
23-Jun-15	750	150	150	1	1	3.549	3.549	3.549	3.549
30-Jun-15	500	250	250	2	2	3.542	3.549	3.549	3.543
7-Jul-15	1000	770	770	4	4	3.545	3.549	3.549	3.548
14-Jul-15	1000	120	120	2	2	3.549	3.549	3.549	3.549
28-Jul-15	1000	700	700	4	4	3.547	3.549	3.549	3.548
4-Aug-15	1000	1200	1200	5	5	3.53		3.549	3.49
11-Aug-15	500	450	450	2	2	3.53	3.549	3.549	3.538
18-Aug-15	500	0	0	0	0	0	0	0	0
25-Aug-15	1000	350	350	3	3	3.547	3.548	3.548	3.548
1-Sep-15	1500	300	300	2	2	3.547	3.548	3.548	3.547
8-Sep-15	500	50	50	1	1	3.548	3.548	3.548	3.548
15-Sep-15	500	50	50	1	1	3.547	3.548	3.48	3.48
22-Sep-15	500	300	300	2	2	3.54	3.548	3.548	3.546
29-Sep-15	750	750	75	1	1	3.54	3.54	3.54	3.54
6-Oct-15	250	0	0	0	0	0	0	0	0
13-Oct-15	250	250	250	2	2	3.54	3.54	3.54	3.54
20-Oct-15	750	210	210	2	2	3.54	3.54	3.54	3.54
27-Oct-15	500	475	475	4	4	3.53	3.54	3.54	3.54
3-Nov-15	500	100	100	1	1	3.54	3.54	3.54	3.54
10-Nov-15	500	300	300	3	3	3.52	3.54	3.54	3.533
17-Nov-15	1000	150	150	2	2	3.52	3.54	3.54	3.527
24-Nov-15	1250	250	250	2	2	3.53	3.535	3.535	3.534
1-Dec-15	500	100	100	1	1	3.535	3.535	3.535	3.535
8-Dec-15	800	100	100	1	1	3.535	3.535	3.535	3.535
15-Dec-15	500	200	200	2	2	3.535	3.535	3.535	3.535
Total	**51,550**	**24,830**	**22,305**						

Source: *Market Operation Department/ DAB*

Table 2.5: Auction of 182 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 (%)
23-Dec-14	1500	1747.338	718.338	7	6	5.226	7.1	0.05227	5.227
30-Dec-14	1500	635.496	635.496	4	4	5.22	5.227	0.05227	5.223
6-Jan-15	1500	1208.456	700	3	3	5.227	5.23	0.05227	5.227
13-Jan-15	1000	1110	852.705	4	4	5.227	5.228	0.05227	5.227
20-Jan-15	1000	150	0	2	0	0	5.227	0.05227	0
27-Jan-15	1000	470	200	3	1	5.2	5.227	0.052	5.2
3-Feb-15	1000	550	550	3	3	5.16	5.2	0.052	5.185
10-Feb-15	1500	519.131	519.131	3	3	5.19	5.2	0.052	5.19
17-Feb-15	1000	587.904	443.952	5	5	5.198	5.21	0.052	5.198
24-Feb-15	1000	607.64	607.64	4	4	5.19	5.2	0.052	5.2
3-Mar-15	1000	862.295	415	5	3	5.18	5.21	0.0519	5.184
10-Mar-15	1000	1822.295	1442.295	8	6	5.18	5.2	0.0519	5.189
17-Mar-15	1000	903.382	903.382	5	5	5.18	5.195	0.0518	5.195
24-Mar-15	1000	385.202	385.202	4	4	5.19	5.195	0.0519	5.19
31-Mar-15	1000	185	160	4	3	5.194	5.2	0.05195	5.194
7-Apr-15	1000	635	635	3	3	5.19	5.195	0.05195	5.195
14-Apr-15	500	300	300	3	3	5.195	5.195	0.0595	5.195
21-Apr-15	500	385	385	3	3	5.195	5.195	0.05195	5.195
5-May-15	500	2320	100	5	1	5.18	5.195	0.0518	5.18
12-May-15	750	2195	720	6	4	5.15	5.18	0.05179	5.174
19-May-15	1000	2110	2110	6	6	5.17	5.179	0.05179	5.177
26-May-15	1500	550	550	4	4	5.174	5.179	0.05179	5.177
2-Jun-15	1000	225	225	2	2	5.178	5.179	0.05179	5.177
9-Jun-15	500	1000	1000	4	4	5.175	5.179	0.05179	5.178
16-Jun-15	1500	535	535	4	4	5.178	5.179	0.05179	5.179
23-Jun-15	1000	200	200	2	2	5.178	5.179	0.05179	5.179
30-Jun-15	1500	100	100	1	1	5.175	5.175	0.05175	5.175
7-Jul-15	1000	645	645	3	3	5.174	5.175	0.05175	5.175
14-Jul-15	500	270	270	2	2	5.174	5.175	0.05175	5.175
28-Jul-15	1000	316.502	316.502	2	2	5.175	5.175	0.05175	5.175
4-Aug-15	1000	1034.245	1034.245	6	6	5.174	5.175	0.05175	5.175
11-Aug-15	1000	305.207	305.207	2	2	5.175	5.175	0.05175	5.175
18-Aug-15	1000	171.813	171.813	1	1	5.175	5.175	5.175	5.18
25-Aug-15	1000	258.333	258.333	2	2	5.175	5.175	5.175	5.18
1-Sep-15	1000	301.422	301.422	2	2	5.175	5.175	5.175	5.175
8-Sep-15	1500	704.238	704.238	3	3	5.175	5.175	5.175	5.175
15-Sep-15	1000	470.412	470.412	3	3	5.174	5.175	5.175	5.175
22-Sep-15	500	177.727	177.727	3	3	5.174	5.175	5.175	5.175
29-Sep-15	750	115.648	115.648	2	2	5.17	5.175	5.175	5.175
6-Oct-15	1000	0.399	0	1	0	0	5.175	0	0
13-Oct-15	500	662.752	0	4	4	5.18		0	5.18
20-Oct-15	500	395	0	2	0	0	0	0	0
27-Oct-15	500	85	35	2	1	5.15	5.175	5.15	5.15
3-Nov-15	750	80	80	1	1	5.15	5.15	5.15	5.15
10-Nov-15	750	710	710	3	3	5.13	5.15	5.15	5.147
17-Nov-15	1500	800	800	3	3	5.15	5.15	5.15	5.15
24-Nov-15	1250	250	250	2	2	5.149	5.15	5.15	5.15
1-Dec-15	1000	100	100	1	1	5.15	5.15	5.15	5.15
8-Dec-15	1500	200	200	1	1	5.15	5.15	5.15	5.15
15-Dec-15	1000	250	250	2	2	5.149	5.15	5.15	5.15
Total	**49,750**	**30,602**	**22,588**						

Source: *Market Operation Department/ DAB*

Table 2.6: Auction of 364 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. (%)
23-Dec-14	1500	765	765	6	6	7.09	7.1	7.1	7.1
30-Dec-14	1000	195	195	3	3	7.099	7.1	7.1	7.099
6-Jan-15	500	225	0	4	0	0	7.1	0	0
13-Jan-15	500	250	0	2	0	0	7.1	7.08	0
20-Jan-15	500	241.57	0	2	0	7.05	7.1	0	0
27-Jan-15	500	110	0	2	0	7	7.04	0	0
3-Feb-15	500	176.57	0	2	0	0	6.9	6.9	0
10-Feb-15	500	5	0	1	0	0	6.8	6.8	0
17-Feb-15	500	0	0	0	0	0	0	0	0
24-Feb-15	500		0	1	0	6.75	6.75		0
3-Mar-15	500	25	0	0	0	6.75	6.75	0	0
10-Mar-15	1000	10	0	0	0	6.75	6.75	0	0
17-Mar-15	1000	2025	0	1	0	6.73	6.75	0	0
24-Mar-15	500	2374	2374	2	2	6.69	6.7	6.69	6.7
31-Mar-15	500	470	470	4	4	6.69	6.7	6.7	6.699
7-Apr-15	500	283	283	3	3	6.7	6.7	6.7	6.7
14-Apr-15	1000	1643	1643.5	4	4	6.7	6.7	6.7	6.7
21-Apr-15	1000	1016	1016	4	4	6.7	6.699	6.7	6.7
5-May-15									
12-May-15	250	2360		5	0	0	6.7	6.68	0
19-May-15	500	1520	1520	3	3	6.6	6.68	6.68	6.663
26-May-15	1500	600	600	3	3	6.65	6.68	6.68	6.664
2-Jun-15	1500	642.471	642.471	3	3	6.67	6.68	6.68	6.674
9-Jun-15	1500	1195.217	1145.217	7	6	6.675	6.685	6.68	6.68
16-Jun-15	1000	1210	1210	7	6	6.675	6.68	6.68	6.68
23-Jun-15	500	927.894	405	3	1	6.679	6.68	6.679	6.679
30-Jun-15	500	631.232	531.232	2	2	6.675	6.68	6.679	6.676
7-Jul-15	500	638.798	638.798	4	4	6.678	6.679	6.679	6.679
14-Jul-15	500	457.199	300.199	2	2	6.679	6.68	6.679	6.679
28-Jul-15	500	890	890	4	4	6.67	6.679	6.679	6.676
4-Aug-15	500	875	875	3	3	6.679	6.679	6.679	6.676
11-Aug-15	500	590	590	3	3	6.676	6.679	6.679	6.676
18-Aug-15	500	240	240	2	2	6.679	6.679	6.679	6.676
25-Aug-15	500	50	50	1	1	6.679	6.679	6.679	6.689
1-Sep-15	1000	825	825	3	3	6.679	6.679	6.679	6.679
8-Sep-15	1500	1300	1300	4	4	6.679	6.679	6.679	6.679
15-Sep-15	700	450	450	2	2	6.679	6.679	6.679	6.679
22-Sep-15	500	200	200	2	2	6.679	6.679	6.679	6.679

29-Sep-15	1000	530	530	3	3	6.678	6.679	6.679	6.679
6-Oct-15	1000	60	60	1	1	6.679	6.679	6.679	6.679
13-Oct-15	500	505	505	4	4	6.678	6.679	6.679	6.679
20-Oct-15	1000	790.994	0	4	0	0	6.679	0	0
27-Oct-15	500	500		1	0	0	6.679	0	0
3-Nov-15	1000	369.19	369.19	3	3	6.654	6.679	6.679	6.674
10-Nov-15	1000	478.916	478.916	4	4	6.675	6.679	6.679	6.677
17-Nov-15	1500	731.196	731.196	4	4	6.675	6.679	6.679	6.679
24-Nov-15	1000	435	435	4	4	6.678	6.679	6.679	6.679
1-Dec-15	1500	458.712	258.712	3	3	6.678	6.679	6.679	6.679
8-Dec-15	800	1092.319	1092.319	5	5	6.677	6.679	6.679	6.678
15-Dec-15	1000	813.172	813.172	5	5	6.678	6.68	6.68	6.679
Total	**38,50**	**32,181**	**24,432**						

Source: *Market Operation Department/ DAB*

3

THE INFLATION TREND AND OUTLOOK

3

THE INFLATION TREND AND OUTLOOK

Global economic growth remained modest surrounded by infirm aggregate demand, falling commodity price, and increasing volatility in financial markets across major economies. For the end of 2015, world economic growth is estimated around 2.4 percent, which marks a lower revision from previous estimation of 2.8 percent. After remarkable slowdown in China, and other large developing and transition economies such as Brazil and Russian federation, advanced economies are expected to contribute more to global growth through mitigation of deflationary risks and stimulating investment and aggregate demand. In 2015, developed economies performed well, while economic performance in emerging economies was poor.

Global commodity price fell in 2015. Oil price dropped by almost 48 percent, owing to continuous oversupply, slowdown in Chinese economy, appreciation of U.S dollar, and fall in equity markets. Less-than expected demand also contributed to lower oil price over the year.

In response to lower commodity price, global inflation continued to decline. In 2015, consumer price is estimated to be 2.6 percent, which is the lowest level since 2009.

Downward trend in global inflation had implications on domestic prices in Afghanistan as well. Headline CPI inflation decreased to 0.1 percent from 1.3 percent (y-over-y). When measured on quarter-to-quarter basis, headline inflation increased significantly to 3.4 percent during the fourth quarter of 2015 compared to 0.8 percent recorded in previous quarter.

I. CONSUMER PRICE IN AFGHANISTAN

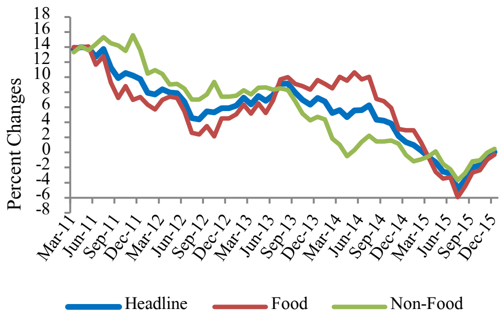
Since the withdrawal of international security forces in 2014, the economy of Afghanistan has been suffering from political and security uncertainties, resulting in significant downturn in economic growth. These challenges have confronted the delivery of public services, private investment, personal safety and business confidence to critical threats. As a result, the aggregate consumption declined notably, which led to lower price level.

By the end of the fourth quarter of 2015, headline CPI inflation declined to 0.1 percent from 1.3

percent in the fourth quarter of the previous year. During the review period, food inflation declined, which put deflationary pressures on the overall CPI, while non-food component recorded higher inflation compared to corresponding period of the previous year.

Unlike to the national CPI, overall price level increased in Kabul. Headline inflation increased to -0.6 percent compared to -1.1 percent recorded in the previous year. During the fourth quarter of 2015, inflation declined in food item, while it increased in non-food category, which could push up the overall inflation rate.

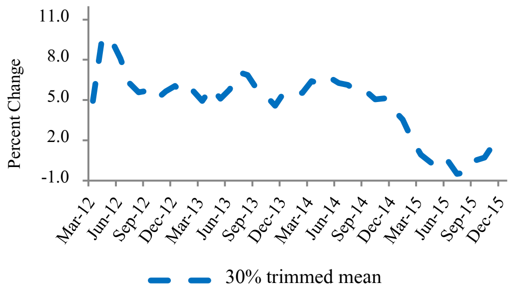
Figure 3.1: National Headline CPI Inflation



Source: *Central Statistics Organization/DAB staff calculation*

In core measures of inflation, there is a decrease recorded in 30% trimmed mean. Inflation by this measure reached to 2.2 percent (y-over-y) compared to 4.3 percent in the previous year.

Figure 3.3: Core Inflation (30% Trimmed Mean)



Source: *Monetary Policy Department/DAB*

3.1 Developments in National Headline CPI

1.1.1 Annual Developments

Lower global commodity price for the second consecutive year weighed on the overall price level in Afghanistan. The headline inflation dropped to 0.1 percent (Y-on-Y) from 1.3 percent over the previous fiscal year. The fall in headline inflation over fiscal year 2015 is in line with lower price of food items, while non-food sub-index experienced higher prices compared to the previous period.

Towards the end of the year, food inflation decreased to -0.3 percent from 2.9 percent (Y-on-Y). During this reporting period, average price of bread and cereals declined reaching at an inflation rate of 0.5 percent from 8.0 percent. Moreover, inflation in fresh and dried fruits dropped to 0.5 percent from 11.5 percent, which resulted in lower inflation in food sub-index. However, these impacts are somehow offset by higher price of vegetables (standing at a deflation rate of 6.3 percent from a deflation rate of 9.6 percent). The pace of change in other food sub-components does not seem to have any significant contribution to the overall index.

In non-food subcomponent of CPI, inflation increased by 0.5 percent compared to -0.5 percent in the previous year. The highest annual increase is seen in inflation rate of clothing (8.6 percent from 4.2 percent), followed by housing, electricity, water and gas (-6.6 percent from -9.7 percent). On the other hand, average price of transportation declined sharply and turned around to a deflation rate of 3.4 percent from an inflation rate of 11.3 percent (year-over-year). In addition, average price of furnishing and household goods dropped to 5.7 percent inflation from 8.4 percent.

Table 3.1: Breakdown of National Headline CPI

(Percent changes year on year)

(March 2011=100)

	Weight	1392				1393				1394			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Overall Index	100.0	6.4	7.6	8.0	7.3	5.6	5.6	4.2	1.3	-0.7	-2.8	-1.9	0.1
Food and beverages	52.0	5.2	6.9	9.1	9.6	10.0	9.7	6.8	2.9	-0.6	-3.3	-2.6	-0.3
Bread and Cereals	17.7	12.8	13.7	14.6	9.1	9.5	11.4	11.0	8.0	1.9	-3.4	-2.3	0.5
Meat	7.2	6.0	5.3	6.6	5.0	2.6	3.4	3.7	3.4	2.4	-0.2	-1.5	0.8
Milk, cheese and eggs	4.8	4.9	4.1	7.8	5.0	6.5	6.1	2.1	3.4	1.4	1.0	1.5	1.3
Oils and fats	4.0	-0.5	-2.3	-0.4	0.3	1.8	1.7	0.9	-1.7	-6.2	-7.2	-6.5	-6.6
Fresh and dried fruits	4.8	-3.2	-2.0	-0.1	4.7	8.5	9.9	9.2	11.5	6.6	7.9	2.0	0.5
Vegetables	7.9	-3.3	6.6	15.3	30.7	30.3	24.3	7.1	-9.6	-11.7	-15.9	-12.4	-6.3
Sugar and sweets	2.9	3.4	4.7	2.8	2.4	2.5	-1.6	-0.2	-1.0	-1.1	0.5	0.4	6.0
Spices	0.9	8.8	10.2	5.6	8.1	10.5	9.4	12.0	5.9	1.0	-1.0	0.3	6.6
Non-alcoholic beverages	1.8	7.6	8.5	6.8	6.6	7.4	3.7	4.0	2.1	1.3	3.1	4.6	5.3
Non-Food	48.0	7.7	8.4	6.8	4.9	1.1	1.4	1.4	-0.5	-0.8	-2.2	-1.2	0.5
Tobacco	0.4	11.5	19.5	21.2	10.9	8.4	3.0	0.6	6.7	2.8	12.8	25.0	22.4
Clothing	7.0	8.0	10.3	8.9	8.8	8.3	8.1	6.9	4.2	2.9	2.0	6.6	8.6
Housing,	20.7	11.8	11.1	6.8	2.1	-8.5	-9.1	-8.8	-9.7	-5.1	-7.0	-7.4	-6.6
Furnishing and household goods	7.0	3.9	6.0	6.5	8.7	8.5	10.4	10.3	8.4	4.9	2.1	3.3	5.7
Health	3.3	11.3	13.0	11.2	8.0	8.8	9.0	10.3	8.5	7.7	7.4	6.9	9.4
Transportation	4.7	-2.5	-1.5	3.6	5.8	16.6	20.1	19.5	11.3	-6.9	-10.0	-7.8	-3.4
Communication	1.1	-6.7	-6.4	-4.5	-2.5	-1.5	-1.4	-2.0	-3.4	-4.7	-3.3	-2.2	-1.3
Education	0.7	7.1	1.7	1.8	1.8	1.9	5.0	4.0	2.8	2.0	-2.7	-3.7	-5.1
Information and Culture	0.1	3.2	3.5	2.6	2.3	6.5	5.4	7.1	7.0	1.2	3.8	5.2	6.3
Restaurants and Hotels	1.0	2.4	2.8	3.7	1.8	2.6	2.4	4.6	3.2	2.2	4.2	-0.8	-0.3
Miscellaneous	1.8	5.5	5.2	6.6	8.0	7.6	10.2	8.2	7.6	7.3	7.2	10.6	9.5
core inflation (30% TM)		4.9	5.8	5.8	5.6	6.4	6.3	5.6	4.3	-0.1	0.5	0.5	2.2
Core inflation (Headline excl. B&C, O&F and T)		5.9	7.4	7.2	7.2	4.3	3.6	1.7	-0.8	-0.7	-1.9	-1.2	-1.0

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

1.1.2 Quarterly Developments in national CPI

Since the first quarter of FY2015, headline CPI inflation when measured on quarter-to-quarter basis has been increasing. During the fourth quarter, inflation recorded its two year peak, standing at 3.4 percent from 0.8 percent in the previous quarter.

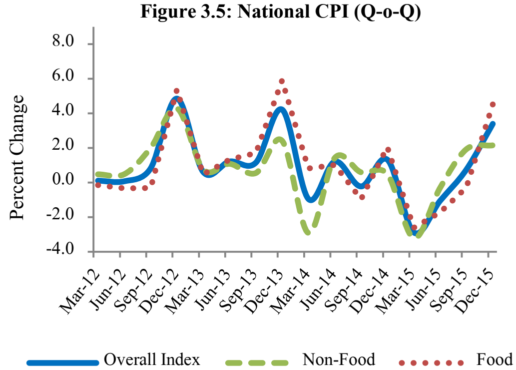
Higher inflation occurred due mainly to capital outflows, causing the national currency to depreciate by around 6.6 percent against US dollar from the previous quarter. In addition, higher price of food (especially flour) in Pakistan also shaded on the food price in Afghanistan.

Inflation increased in both main items of the CPI, but price of food component rose by a greater pace compared to that of non-food category.

Food component of CPI, which accounts for around 52 percent of the index, turned around to an inflation rate of 4.5 percent from a deflation rate of 0.3 percent. Upward pressures on this item came basically from higher price of fresh and dried fruits, and vegetables. Fresh and dried fruits, after recording a deflation rate of 7.1 percent in the previous quarter, turned around to 1.5 percent inflation over the fourth quarter of the year 2015. Meanwhile, inflation rate in vegetables increased to 17.4 percent compared to -11.2 percent over the previous quarter. Unlikely; average price of bread and cereals declined by 0.8 percentage point. This sub-component of food item comprises around 17 percent of the whole index; therefore, a small change in this component can affect the overall index.

Non-food category also had a similar trend to the overall index. Inflation in this item increased to 2.2 percent compared to 1.9 percent in previous quarter. The highest increase in non-food sub-index inflation is recorded in housing, electricity, water and gas (1.9 percent from 0.0 percent), followed by furnishing and household goods (3.0 percent from 2.4 percent). However, inflationary pressures of these components are somehow offset by lower inflation in transportation (1.1 percent from 4.9 percent).

Figure 3.5: National CPI (Q-o-Q)



Source: *Central Statistics Organization/ DAB staff calculation.*

Table 3.2: Breakdown of National Headline CPI

(Percent changes quarter-on-quarter)

(March 2011 = 100)

	FY1392			FY1393				FY1394			
	Q1	**Q2**	**Q3**	**Q1**	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**	**Q3**	**Q4**
Overall Index	0.6	1.2	1.1	4.2	-1.0	1.2	-0.2	1.3	-2.9	-0.9	0.8
Food and beverages	0.5	1.3	1.7	5.9	0.8	1.0	-1.0	2.0	-2.7	-1.7	-0.3
Bread and Cereals	0.2	2.4	3.0	3.2	0.6	4.1	2.7	0.4	-5.1	-1.3	4.0
Meat	2.6	0.0	1.8	0.6	0.3	0.7	2.1	0.3	-0.7	-1.9	0.8
Milk, cheese and eggs	0.4	-1.4	4.8	1.2	1.9	-1.8	0.8	2.5	-0.1	-2.1	1.2
Oils and fats	-2.3	-0.2	0.7	2.1	-0.9	-0.2	-0.1	-0.5	-5.4	-1.3	0.6
Fresh and dried fruits	2.7	2.0	-1.0	0.9	6.5	3.4	-1.7	3.1	1.8	4.6	-7.1
Vegetables	0.0	1.7	-1.0	29.9	-0.3	-3.0	-14.7	9.7	-2.7	-7.6	-11.2
Sugar and sweets	-2.3	1.3	1.9	1.5	-2.1	-2.8	3.3	0.7	-2.3	-1.2	3.3
Spices	1.0	3.8	-2.1	5.3	3.3	2.7	0.3	-0.5	-1.5	0.7	1.7
Non-alcoholic beverages	-0.2	3.0	1.6	2.1	0.5	-0.6	1.9	0.3	-0.3	1.1	3.4
Non-Food	0.8	1.1	0.6	2.4	-2.9	1.4	0.6	0.5	-3.3	0.0	1.9
Tobacco	2.1	7.5	-0.5	1.5	-0.2	2.2	-2.8	7.6	-3.8	12.1	7.8
Clothing	1.7	2.1	0.9	3.8	1.2	1.9	-0.2	1.3	-0.1	1.1	4.3
Housing,	0.1	0.4	-0.4	2.0	-10.3	-0.3	-0.1	1.1	-5.7	-2.2	0.0
Furnishing and household goods	1.9	2.8	1.2	2.5	1.8	4.6	1.1	0.7	-1.5	1.7	2.4
Health	3.4	1.8	1.3	1.2	4.2	2.0	2.5	-0.4	3.4	1.8	2.0
Transportation	-1.0	0.2	2.9	3.6	9.1	3.2	2.4	-3.5	-8.7	-0.2	4.9
Communication	-1.1	-1.4	-0.7	0.7	-0.1	-1.3	-1.3	-0.7	-1.4	0.1	-0.3
Education	1.7	-0.6	0.8	0.0	1.8	2.4	-0.2	-1.2	1.0	-2.2	-1.3
Information and Culture	1.3	0.1	0.0	0.9	5.5	-1.0	1.6	0.8	-0.2	1.5	2.9
Restaurants and Hotels	0.2	0.6	1.1	-0.1	0.9	0.4	3.3	-1.5	0.0	2.3	-1.6
Miscellaneous	1.6	0.3	2.0	4.0	1.2	2.8	0.1	3.3	1.0	2.6	3.3

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

* Afghanistan has changed its fiscal year effective from 1391. The new fiscal year begins on December 21 and ends on December 20 each Gregorian year. New fiscal year 1391 contains 9 months due to this change.

1.2 Developments in Kabul CPI

1.2.1 Annual Developments

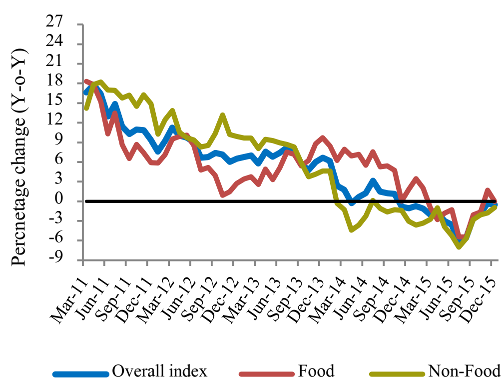
Overall inflation in Kabul exhibited a slight increase over a one year horizon, but remained in a negative territory. During the fourth quarter of 2015, Headline CPI inflation in Kabul increased to -0.6 percent compared to -1.1 percent recorded in corresponding quarter of previous year. These improvements were attributed to increasing non-food price, while price of food category decreased compared to the previous period.

Amid the lower price of bread and cereals, fresh and dried fruits, and vegetables, food item of the CPI declined to a zero inflation rate from 1.8 percent (Y-over-Y). Price of bread and cereals, which makes the largest weight in food item averaged lower to a deflation rate of 0.7 percent from an inflation rate of 3.0 percent. Meanwhile, inflation in fresh and dried fruits dropped to 3.1 percent from 12.9 percent, and vegetables eased to -11.5 percent from -5.6 percent. Other sub-components of food item recorded higher inflation, among which the highest increase was seen in meat (4.3 percent from 2.6 percent). However, these improvements are not as significant to have remarkable contribution to the overall price level.

Owing to higher price of clothing, housing, electricity, water and gas, and furnishing and household goods, non-food inflation increased to -0.9 percent from -3.1 percent. The highest annual increase in this item is seen in housing, electricity, water and gas (-9.6 percent from -13.4 percent). This component alone comprises around 21 percent of the whole index; therefore, any change in its prices contributes the changes in the overall inflation significantly. Moreover, average inflation in clothing increased to 13.8 percent from 10.3 percent, and furnishing and household goods rose to 14.0 percent from 12.5 percent. At the time, owing to lower price of oil in global markets, inflation in transportation declined to -3.4 percent from 19.4 percent.

Trimmed mean (30%), which is the most useful core measure of inflation in Afghanistan, increased slightly to 4.7 percent compared to 4.4 percent recorded in corresponding quarter of the previous year. In addition, CPI excluding B&C, O&F, and T rose to -1.4 percent from -3.1 percent (y-over-y).

Figure 3.6: Kabul Headline CPI Inflation



Source: *Central Statistics Office/DAB staff calculation.*

Table 3.3: Breakdown of Kabul Headline CPI

(Percent changes year-on-year)

(March 2011=100)

	Weight	1393				1394			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Overall Index	100.0	1.2	1.2	-1.1	-2.0	-3.6	-2.5	-0.6	1.2
Food and beverages	52.0	5.5	5.4	1.8	-1.0	-1.3	-2.1	0.0	5.5
Bread and Cereals	17.7	4.8	6.6	3.0	-1.9	-2.9	-3.2	-0.7	4.8
Meat	7.2	-1.4	3.8	2.6	0.5	1.1	0.7	4.3	-1.4
Milk, cheese and eggs	4.8	9.9	8.7	5.9	2.7	6.1	8.5	7.1	9.9
Oils and fats	4.0	-3.1	-5.1	-5.5	-12.6	-7.7	-7.5	-5.5	-3.1
Fresh and dried fruits	4.8	8.8	7.4	12.9	5.1	8.3	3.0	3.1	8.8
Vegetables	7.9	15.8	8.9	-5.6	-2.3	-10.2	-12.6	-11.5	15.8
Sugar and sweets	2.9	-6.9	-3.5	-5.1	-2.8	1.4	2.6	13.9	-6.9
Spices	0.9	7.0	9.2	7.2	1.4	3.6	9.3	19.8	7.0
Non-alcoholic beverages	1.8	2.1	2.6	3.2	-0.8	3.0	5.3	9.5	2.1
Non-Food	48.0	-1.7	-1.6	-3.1	-2.8	-5.2	-2.8	-0.9	-1.7
Tobacco	0.4	13.3	11.5	15.5	12.9	9.1	22.6	20.1	13.3
Clothing	7.0	11.5	11.3	10.3	5.6	0.8	9.8	13.8	11.5
Housing, electricity, water and gas	20.7	-13.2	-13.1	-13.4	-6.4	-9.7	-10.0	-9.6	-13.2
Furnishing and household goods	7.0	13.4	13.2	12.5	7.2	3.9	8.5	14.0	13.4
Health	3.3	7.3	8.7	4.1	4.1	3.5	0.2	0.3	7.3
Transportation	4.7	33.2	32.1	19.4	-14.7	-15.4	-7.4	-3.4	33.2
Communication	1.1	-2.2	-4.0	-5.0	-5.7	-3.6	-1.6	-0.2	-2.2
Education	0.7	2.8	1.9	2.1	1.6	-3.8	-5.8	-7.3	2.8
Information and Culture	0.1	14.6	19.1	18.3	1.8	5.6	6.8	9.8	14.6
Restaurants and Hotels	1.0	2.3	5.2	3.1	1.7	5.5	-0.6	0.0	2.3
Miscellaneous	1.8	7.9	3.8	5.0	4.5	8.3	17.8	17.9	7.9
Core inflation (28% TM)		5.7	6.2	4.4	0.7	1.2	1.9	4.7	5.7
Core inflation (Headline excl. B&C, O&F and T)		-1.3	-3.8	-3.1	-0.5	-2.6	-1.7	-1.4	-1.3

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

1.2.2 Quarterly Developments, Kabul CPI

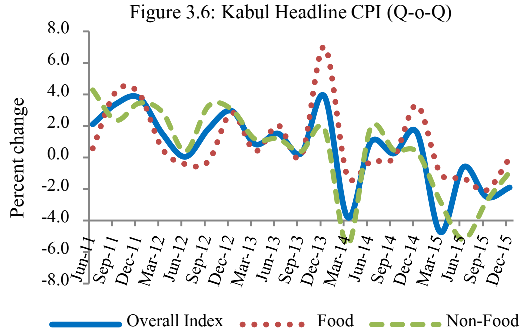
In December 2015, due to a dramatic increase in food price, the scale of quarterly price increase in Kabul CPI was ascending. Meanwhile, the price of non-food component of CPI decreased. Overall inflation reached its two year peak, standing at 3.6 percent from 1.6 percent one year earlier.

Reflecting large-scale increments in average price of fresh and dried fruits, and vegetables, food inflation picked up to 5.5 percent from -0.8 percent in

previous quarter. During the reporting period, inflation rate of vegetables averaged higher to 19.8 percent from -13.4 percent in the previous quarter. Similarly, fresh and dried fruits turned around to 2.4 percent from -9.2 percent. In addition, inflation increased for meat (4.9 percent from 3.9 percent). On the other hand, bread and cereals, and milk, cheese and eggs recorded lower inflation.

Non-food price averaged 2.3 percent compared to 3.5 percent in the previous quarter. Lower inflation in non-food component was caused mainly by decreasing inflation rate of clothing (6.4 percent from 8.8 percent), health (-2.0 percent from 0.4 percent), and transportation (0.0 percent from 11.4 percent). In contrast, housing inflation increased to 1.0 percent from 0.5 percent, and furnishing and household goods to 6.4 percent from 5.8 percent.

Figure 3.6: Kabul Headline CPI (Q-o-Q)



Source: *Central Statistics Organization/ DAB staff calculation.*

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

(Percent changes quarter-on-quarter)

(March 2001=100)

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

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

II. REGIONAL INFLATION TREND

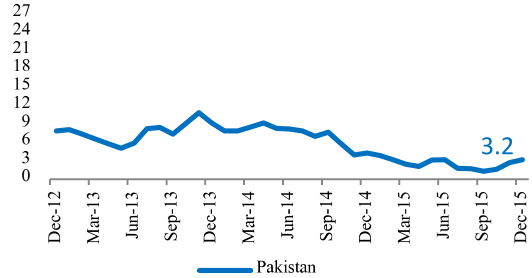
In this section, we discuss the recent developments in inflation in South Asian countries. During the fourth quarter, inflation recorded its lowest level. As a result of low commodity and food price, and declining administered price (in India and Sri Lanka), inflation fell remarkably across the region. In this way, South Asia became one of the regions with lowest inflation in the world.

1.1 Inflation in Pakistan

Headline CPI inflation in Pakistan continued its downward trend. During December 2015, 12 month period average inflation stood at 4.5 percent, its 11 year lowest level. In addition, core inflation (trimmed mean) dropped to 2.7 percent, while it was recorded 5.2 percent in 2014. Giving low level of inflation, the central bank of Pakistan is on its way to successfully meet its policy target.

Deflationary pressures have come indirectly from lower global price of oil and food. Therefore, on the back of low inflation the central bank decreased its policy rate five times during the year to control price stability.

Figure 3.7: Pakistan Headline CPI (Y-o-Y)



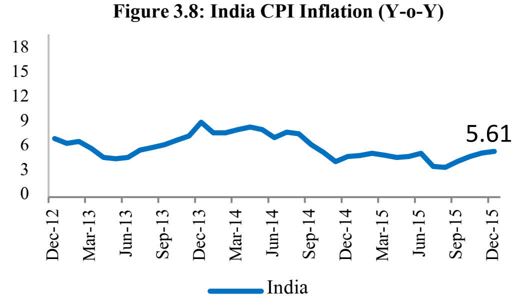
Source: *Monetary Policy Department, DAB staff calculations*

1.2 Inflation in India

In India consumer price index subdued, as headline inflation fell to 5.9 percent in 2015 from an average of 10.1 percent in preceding two years. However, inflation has leveled higher in December standing at 5.61 percent compared to 4.28 percent recorded in corresponding month of last year. Lower inflation has led the central bank to loose monetary policy in 2015.

Disinflation in India owes much to international developments, including cheaper oil and food price.

Figure 3.8: India CPI Inflation (Y-o-Y)



Source: *Monetary Policy Department, DAB staff calculations*

III. NEAR TERM INFLATION OUTLOOK

In the medium-term, inflation is expected to get momentum. Based on Da Afghanistan Bank forecast, inflation will increase by around 2.5 percent in the first six half of 2016. However, this will depend on spillover effects from economic development, exchange rate behavior, and international price of oil and food.

Economic growth is expected to increase, mainly because of registration of new businesses, and good performance expected in agriculture sector. Along with this, overall consumption may increase, which leads to higher inflation.

Inflationary pressures may come from lower exchange rate as well. Given the import oriented economy of Afghanistan, devaluation of Afghani mostly translates to higher consumer price in the country. However, as global price of oil and food is expected to remain subdued, it may turn down the effects of low exchange rate on the overall price level.

3.1 Risks

For the near-term outlook, risks to inflation are thought to be on the upside, albeit global price prospects have weakened. During the fourth quarter of 2015, the largest contribution to the inflation came from exchange rate. Afghanistan has a huge deficit in its trade balance, and is therefore not immune from exchange rate decline. Thus, this factor may remain an important stimulus to inflation in the near future.

4

EXTERNAL SECTOR DEVELOPMENTS

4

EXTERNAL SECTOR DEVELOPMENTS

Major developments in the external sector of the Afghan economy for the FY 1394 relative to the FY 1393 are presented in this chapter. The available data reveals that performance of the external sector was weak in the FY 1394. The sluggish performance was tied mainly to deteriorating security environment and persisting political uncertainty, continuing to spirally undermine private sector's confidence and poor growth in economic activities.

This reflected a negative outcome (deficit) of USD 3511.60 million in Balance of payment which is equal to 16 percent of the Gross Domestic Product (GDP). This development could be attributed to the decline in inflow of investment income, lower foreign investment flows, and unpredictable political environment during the FY 1394.

Also, the stock of external reserve assets depleted by 4 percent to USD 6,965.81 million but could finance almost 11 months of current import commitments in the FY 1394.

The stock of external debt declined marginally by 5.3 percent to USD 2,139.77 million during the reporting year.

The weak performance of the external sector and its vulnerability to external shocks owed to the subdued contributions of the agriculture sector and low production in the economy.

4.1: Balance of Payments

4.1.1 Current Account Balance

Available data showed that the deficit in the current account was USD 4,809.97 million which is equivalent to 22 percent of total GDP in the FY 1394, higher than a deficit of USD 4,020.25 million recorded in the previous year. This development was attributed to lower exports of goods and services as well as lower current transfers (grants) to the country and increased out-payments of imports of goods and services in the FY 1394.

According to available data, the deficit in the current account increased by 20 percent in the FY 1394.

Trade deficit (trade in goods) rose by 10 percent to USD 6,457.22 million in the FY 1394 in comparison to USD 5,871.53 million in the previous year.

Likewise, the deficit in the services account rose by 20 percent to USD 676.92 million in the FY 1394 from USD 564.10 million in the preceding year. This could be attributed to addition in out-payments in respect of transportation services. As well as current transfers' surplus which was largely influenced by grants and worker personal home remittances from foreign countries narrowed by 11 percent to USD 2,144.21 million in the FY 1394 from USD 2,417.75 million when compared with previous year.

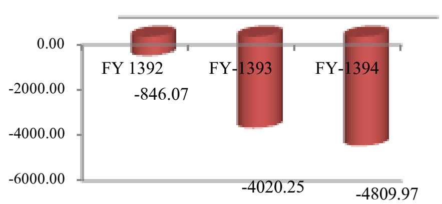
Conversely; in the income account we turned from a deficit of USD 2.37 million in the FY 1393 to a surplus of USD 197.96 million in the FY 1394 (Table 4.1).

Table 4.1: Current Account Balance

	FY1392	FY1393	FY1394
Current account balance	**-846.07**	**-4020.25**	**-4809.97**
Trade balance	-1236.78	-5871.53	-6457.22
Exports	177.55	658.29	579.99
Imports	-1414.33	-6529.83	-7037.21
Services A/c	-76.00	-564.10	-676.92
Income A/c	7.79	-2.37	179.96
Current Transfers	458.92	2417.75	2144.21

Source: *Central Statistics Organization/DAB staff calculations*

Figure 4.1: Afghanistan Balance Of Payments Current Account Goods, Services ,Income , Current transfers in million USD



Source: *Central Statistics Organization/DAB staff calculations*

4.1.2 Capital and Financial Accounts

The capital account of the balance of payments illustrated a decline of 51 percent in the FY 1394 when compared to the FY 1393, as a result of lower inward capital transfers.

Net inflows to the capital account dropped from USD 2,429.93 million in the FY 1393 to USD 1,188.86 million in the FY 1394. This was mainly due to net capital transfers received by the government, corporations and households reduced to USD 1,215.45 million in the FY 1394 compared to USD 2,463.32 million recorded in the previous year.

Financial account of the BOP recorded a net outflow of USD 109.50 million in the FY 1394 while in the previous year it showed a net inflow of USD 1017.85 million. Further analysis reveals that the country's aggregate financial assets abroad increased to USD 152.31 million in the FY1394 from USD 21.59 million that was recorded in the FY 1393.

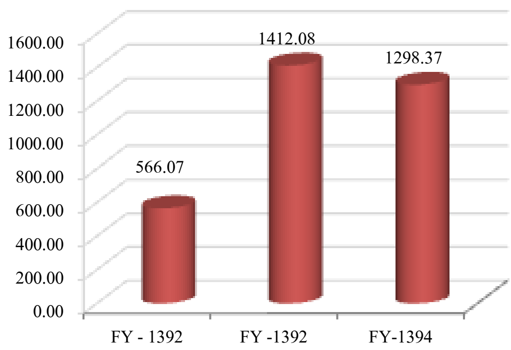
likewise, the aggregate financial liabilities decreased to USD 24.66 million in the FY 1394 from USD -162.70 million recorded in the FY 1393, as a result of lower financial inflows occasioned by the insecurity challenges, that affected both FDI and portfolio investments.

Table 4.2: Capital and Financial Account

	FY 1392	FY1393	FY1394
Capital and financial account	566.07	1412.08	1298.37
Capital account	545.53	2429.93	1188.86
Capital transfers	552.90	2463.32	1215.45
Financial account	20.54	-1017.85	109.50
Reserve Assets	35.61	-876.53	117.33

Source: *Central Statistics Organization/DAB staff calculations*

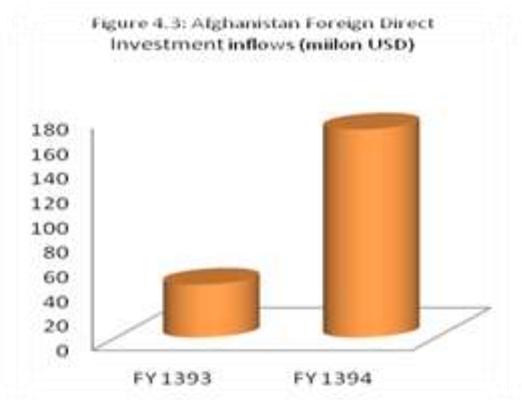
Figure 4.2: Capital and Financial Account



Source: *Central Statistics Organization/DAB staff calculations*

4.1.3 Foreign Direct Investment (FDI)

According to available data, the total foreign direct investment (FDI) related inflows amounted to USD 169.15 million in the FY 1394 in comparison with USD 42.98 million recorded in the FY 1393. While, portfolio investment inflows decreased to USD 81.51 million in the FY 1394 from USD 148.67 million which was recorded in the FY 1393.

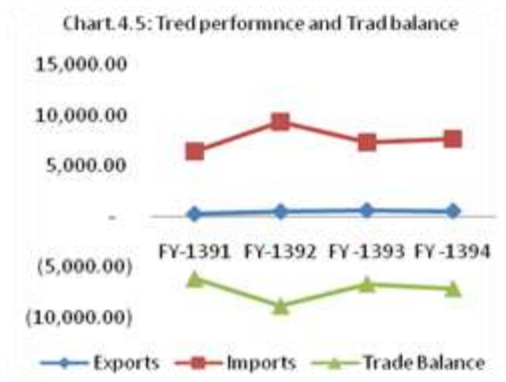


Source: External Sector/Monetary Policy Department/DAB

4.2 Merchandise Trade

The Merchandise trade deficit which contracted in FY 1393, was reversed in FY 1394, resulting to an expansion in trade deficit. Earnings from exports narrowed by 10 percent at the same time the expenditure on imports grew by almost 5 percent; consequently expanding the trade deficit by 7 percent over the FY 1394. However, as imports grew faster and export growth decelerate in the FY 1394, overall trade deficit expanded to a value of USD 7,123.38 million.

However, as a percentage of GDP, the trade deficit increased to 33 percent in FY 1394 from 31 percent that was recorded in FY 1393.



4.2.1 Exports

Accordingly, earnings from exports decreased to a value of USD 555.71 million in the FY 1394 from a value of USD 620.88 million that was recorded in the last year, with contribution from all major exporting categories.

Trade statistics indicated that export of leather & wool, food items and medical seeds shows downward trend, while carpet & rugs shows upward trend in the FY 1394.

Earnings from leather and wool exports declined by 42 percent to a value of USD 28.47 million in the FY 1394 compared to a value of USD 49.35 million in the FY 1393.

In the fiscal year 1394 earnings from food items such as fresh & dry fruit and medical seeds exports decreased by almost 23 and 2 percent respectively. Similarly the value of earnings from food items and medical seeds plunged to USD 210.17 and 208.76 million from USD 272.13 and 212.36 million respectively in the FY 1394 review.

While, earnings from carpet and rugs exports increased by 24 percent to a value of USD 108.31 million in the FY 1394 compared from value of USD 87.04 million recorded in the FY1393.

4.2.2 Imports

In the same time, expenditure on imports increased to USD 7,679.09 million in the FY 1394 compared to a value of USD 7,294.63 million recorded in the previous year.

The major contribution was made by fuel and lubricants and capital goods. Imports of fuel and lubricants which accounted for approximately 22 percent of total imports reported USD 1,688.58 million, reflecting 46 percent increase in the FY 1394. In the meantime, expenditure on imports of capital goods which accounted for 46.4 percent of the total imports increased by 22 percent to a value of USD 3,566.07 million in the FY 1394 from a value of USD 2929.64 million in the previous year.

Conversely, expenditure on imports of consumer goods which accounted for about 22.3 percent of total imports declined by 27 percent to a value of USD 1,715.25 million in the FY 1394 from a value of USD 2345.86 million, in the FY 1393. Expenditure on industrial supply accounted for about 9.2 percent of total imports, declined to a value of USD 709.19 million in the FY 1394 from a value of USD 863.19 million reflecting by about 18 percent decrease over the last year.

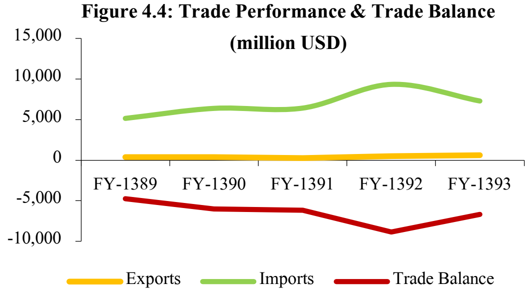
Table (3) below gives a detailed break-down of the merchandise trade statistics from FY 1390 up to the end of the FY 1394.

Table 4.3: Breakdown of Merchandise Trade (in million USD)

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

Source: *Central Statistics Organization and DAB staff calculations*

Figure 4.4: Trade Performance & Trade Balance (million USD)



Source: *Central Statistics Organization and DAB staff calculations*

4.3 Direction of Trade

The main export destinations for Afghanistan are Pakistan, Iran, India, China, and Common Wealth of Independence States (CIS).

According to the merchandize trade statistics, **Pakistan continued to be the largest buyer of Afghanistan's exports.** The share of Afghanistan's total exports to Pakistan increased to 40.19 percent in the FY 1394 from 34.24 percent in FY 1393, registering a 5 percent increase in export earnings over the last year.

Based on year on year comparison; exports of carpet and rugs to Pakistan increase by 44 percent in the FY 1394. In the same time exports of leather and wool and food items such as fresh and dry fruits, to Pakistan declined by 22 and 20 percent respectively.

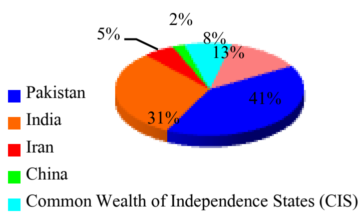
India ranked the second largest buyer of Afghanistan's exports. The share of exports to India increased to almost 30 percent in the FY 1394 from 25 percent recorded in the FY 1393.

Exports of medical seeds to India shows 71 percent growth during FY2015, but the other exporting categories such as leather and wool, carpets, rugs and food items declined 82 percent, 25 percent and 19 percent respectively. Afghanistan's total exports to India grew by almost 10% to a value of USD 169 million in the FY 1394 compared to USD 153 million in the previous year.

The third largest buyer of Afghanistan's exports is Commonwealth of Independent States (CIS) countries. The share of Afghanistan's exports to CIS countries rose to almost 8 percent in the FY 1394 from that of 5 percent in the previous year.

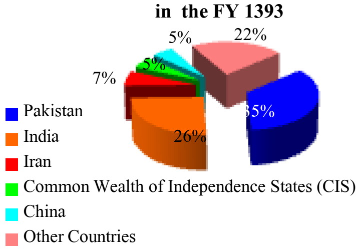
In terms of value Afghanistan's total exports to CIS countries increased by 46 percent to a value of USD 44.13 million in the FY 1394 compared to a value of USD 30.22 million in the FY 1393. The major exporting items to CIS countries were fresh fruits which accounted for about 5 percent of total exports in the year under review.

Figure 4.5: Direction of Exports (% share) in the FY 1394



Source: *Central Statistics Organization and DAB staff calculations*

Figure. 4.6: Direction of Exports (% share) in the FY 1393



Source: *Central Statistics Organization and DAB staff calculations*

Iran was the single largest source of imports for Afghanistan during the FY 1394.

The share of Imports from Iran increased to 22.69 percent in FY 1394 from 19.52 percent recorded in the last year.

In terms of value, the total imports from Iran also increased to USD 1,742.18 million from USD 1,424.21 million, registered 22 percent growth in FY 1394. In the FY 1394 the major importing products from Iran were petroleum oil and industrial supplies which accounted for about 18 and 41 percent of total imports respectively. .

CIS countries were the second largest import origin of Afghanistan in the FY 1394. Total Imports from CIS countries decreased to USD 1,581 million with share of 20.59 percent from USD 1,739.20 million with share of 23.84 percent, registered 9 percent reduction in total imports. The main imports from CIS countries were petroleum oil which accounted 50 percent, consumer goods accounted 20 percent and industrial supplies such as (metal products and fertilizer) accounted 10 percent of total imports in the FY 1394.

Pakistan is the third largest import sourcing country to Afghanistan in the FY 1394. The shares of imports from Pakistan in the total imports remained nearly unchanged in FY 1394, but in terms of value, total imports from Pakistan increased to USD 1,391.99 million from USD 1,360.89 million, registered a slightly growth of 2 percent in the FY 1394.

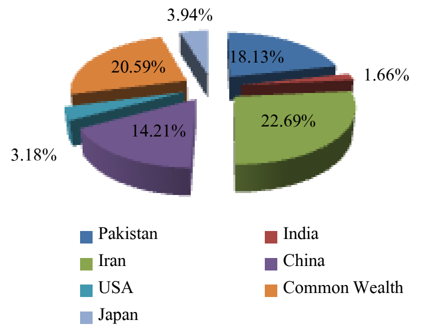
Consumer goods, industrial supplies, capital goods products and petroleum oil were the main imports categories from Pakistan.

China is the fourth largest import origin to Afghanistan in the FY 1394. Total Imports from China increased to USD 1,090.92 million with share of 14.21 percent from USD 824.13 million with share of 11.30 percent, registered 32 percent growth in the FY 1394. The main imports from China were capital goods (spare parts) and consumer goods which accounted for 66 percent and 32 percent of total imports respectively. .

Japan, USA and India were the fifth, sixth and seventh largest import sourcing countries for Afghanistan, accountable for 3.94 percent, 3.18 percent and 1.66 percent of total imports respectively. However, total imports from Japan grew by 40 percent to USD 302.27 million from USD 216.27 million, due to higher imports of capital goods in the FY 1394. Likewise imports from USA grew by 213 percent to USD 244.54 million from USD 78.13 million due to higher imports of capital goods and medicines in the FY 1394. The major imports from Japan and USA comprised of spare parts, machinery, and motor cars.

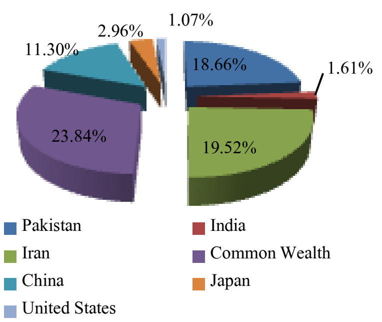
Similarly, imports from India grew by 8 percent to USD 127.25 million from USD 117.32 million in 1393. The major imports from India were capital goods, sugar and fabrics.

Figure 4.7: Direction of Imports (% share) in the FY 1394



Source: *Central Statistics Organization and DAB staff calculations*

Figure 4.8: Direction of Imports (%share) in the FY 1393



Source: *Central Statistics Organization and DAB staff calculations*

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

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

Source: *CSO and DAB staff calculations*

Table 4.5: Direction of External Trade: FY1393 (In million USD)

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

Source: *Central Statistics Organization and DAB staff calculations*

4.4 Composition of Trade

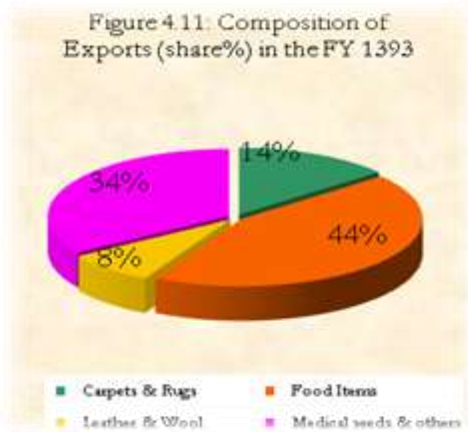
The composition of imports in the FY 1394 indicates that;

Imports of Capital goods had the largest share of 46.4 percent in the basket of imports. In terms of value the imports of Capital goods increased by 22 percent, up from USD 2,929.64 million in the FY 1393 to USD 3,566.07 million in the reporting year. The second largest share recorded for consumer goods in the basket of imports during the FY 1394, although its share dropped to 22.3 percent in the FY 1394 from 32.2 percent in the previous year. Likewise the expenditure on imports of such goods also declined by 27 percent to USD 1,715.25 million in the FY 1394 from USD 2645.86 million in the FY 1393.

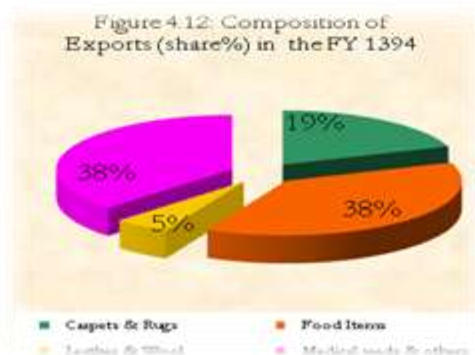
Imports of fuel and lubricants (petroleum oil) had the third largest share in the basket of Afghanistan's imports which is slightly increased from 15.8 percent in the FY 1393 to 22 percent in the reporting year. In terms of value, imports of such item in total imports significantly increased by 46 percent to USD 1,688.58 million in the FY 1394 from USD 1,155.94 million in the FY 1393.

Industrial supplies had the smallest share in the basket of Afghanistan's imports. The imports of industrial supplies plunged 9.2 percent in the FY 1394 from 11.8 percent recorded in the FY 1393. In terms of value the imports of industrial supplies also declined by 18 percent to USD 709.19 million in the FY 1394 from USD 863.19 million in the FY 1393.

This decline was primarily due to the reduction in the number of development projects all over the country as a result of political and security uncertainties.



Source: *Central Statistics Office and DAB staff calculations*



Source: *Central Statistics Office and DAB staff calculations*

The composition of exports in the FY 1394 reveals that exports of food item had the largest share in the basket of Afghanistan's exports even though its share declined to 37.8 percent in the reporting year, from 43.8 percent recorded in the FY 1393.

Earnings from exports of food items (oil seeds, fresh and dry fruits) also decreased by 23 percent to USD 210.17 million in the FY 1394 from USD 272.13 million in the previous year.

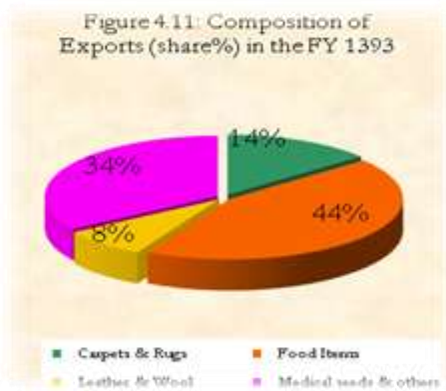
The second largest share in total exports was recorded for medical seeds, in the current fiscal year the share of medical seeds increased to 37.6 percent in the FY 1394 from 34.2 percent in the FY 1393. But in terms of value, exports of medical seeds declined slightly by 2 percent to USD 208.76 million in the FY 1394 from USD 212.36 million that was recorded in the FY 1393.

Carpets and rugs which are considered the main components of Afghanistan's exports in the past decades had the third largest share, 19.5 percent, in total exports, witnessing an increase of 5.5 percent in its share in total exports.

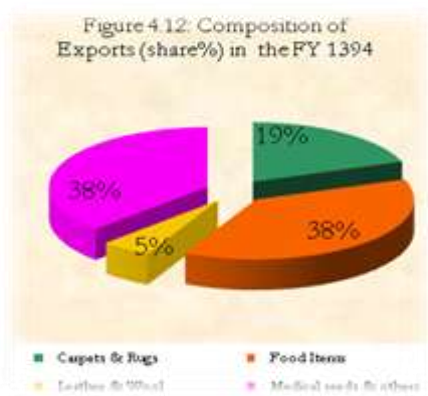
Earnings from exports of carpet and rugs also increased by 24 percent to USD 108.31 million during the year under review from USD 87.04 million that was recorded in the last year.

The share of leather and wool was smallest in the basket of Afghanistan's exports, which declined from 7.9 percent to 5.1 percent during the year under review.

Also, earnings from exports of leather and wool dropped to USD 28.47 million in FY1394 from USD 49.35 million recorded in the FY 1393, down by almost 42 percent.



Source: *Central Statistics Organization/DAB staff calculation*



Source: *Central Statistics Organization/DAB staff calculation*

4.5 External Debt

Afghanistan's total external debt slightly decreased by almost 5 percent to USD 2,139.77 million in the FY 1394 from USD 2,260.04 million in the FY 1393, which shows about USD 120.27 million declines. The decline in total external debt could be attributed to long-term components, like the external commercial loan payment, narrowing NIR deposits and Special Drawing Rights (SDR) allocated by the International Monetary Fund (IMF).

During the period under review, loan principal repayments were made to the World Bank, Asian Development Bank, Saudi Fund for Development, International Monetary Fund (IMF), and Bulgaria. Meanwhile, service charges were paid to the World Bank, Asian Development Bank and Kuwait Fund.

Meanwhile, World Bank, major multilateral creditor to Afghanistan, made some debt forgiveness only on principle during the year under review.

The total loan amounts payable to the Paris Club creditors in the FY 1394 stood at USD 898.84 million which is payable to Russian federation.

In other words, Afghanistan's total debt from the Paris club members stands at about 42 percent of total current external debt which decreased by about 3 percent in 2015 compared to FY2014.

Table 4.6: Breakdown of External Debt for the FY 2014 (in units indicated)

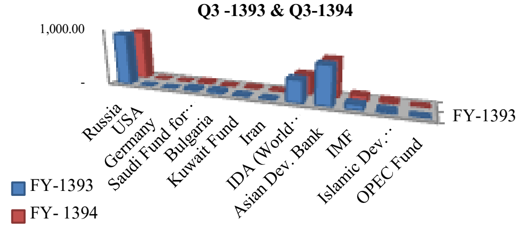
	In million USD	Percent of total
Total external debt	2,139.77	100.00
Bilateral	983.63	45.97
Paris Club	898.84	42.01
Russian Federation	898.84	42.01
United States	-	0.00
Germany	-	0.00
Non-Paris Club	84.79	3.96
Multilateral	1,156.14	54.03
of which: IDA (World Bank)	357.99	16.73
Asian Development Bank	655.33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

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

Furthermore, total debt from Non-Paris Club members which include Saudi Fund for Development, Bulgaria, Kuwait fund and Iran significantly decreased by 34 percent to USD 84.79 million in the FY 1394 in comparison with USD 128.90 million in the FY 1393.

On the other hand, total debt from multilateral creditors to Afghanistan decreased to USD 1,156.14 million from USD 1,206.92 million which shows USD 50.78 million reduction in the total debt from multilateral creditors during the reporting year.

Figure 4.13: External Debt Comparisons; Q3 -1393 & Q3-1394



***Source:** Treasury Department/MoF/DAB staff calculation*

4.6 Net International Reserves

According to the latest available data the Net International Reserves (NIR), decreased slightly by 3.74 percent, standing at USD 6,443 million in the FY 1394, down from USD 6,693.65 million that was recorded last year. The decrease in the level of NIR was mainly due to the decline in the reserve assets which narrowed by 3.89 percent to USD 6,965.81 million in the FY 1394 from USD 7247.76 million in the FY 1393.

Likewise, reserve liabilities contracted by 5.65 percent to USD 522.80 million in the FY 1394 from USD 554.12 million that was recorded in the FY 1393; this demonstrates that the reserve assets are higher than the reserve liabilities. The reduction in reserve liabilities is mainly attributed to the commercial banks deposits in foreign currency which declined by 2.30 percent to USD 433.57 million from USD 443.80 million in the reporting year.

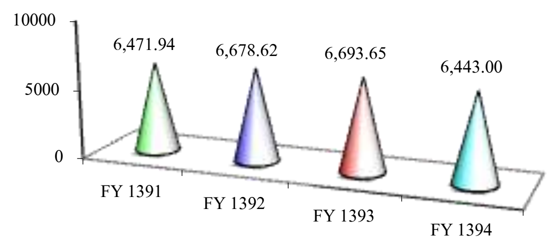
Use of fund resource decrease to USD 89.10 million in the FY 1394 from USD 110.18 million in the FY 1393, declining by 19.14 percent . The reserve liability of nonresident deposits in foreign currency remained almost unchanged in the reporting year.

The decline in the Net International Reserves (NIR) could be attributed to significant outflows of foreign exchange, particularly in the form of foreign and Personal remittances. The current position of Afghanistan Net International Reserves (NIR) is providing a good tool for monetary policy.

Currently, Net International Reserves (NIR) on average supports almost 10 months of imports, it is generally believed that 6 months coverage of imports is a comfortable reserve position.

Figure 4.14: represents the Net International Reserves (NIR) of Afghanistan for the past few periods.

Figure 4.14: Net International Reserves during the past period (In Million USD)



Source: *Monetary Policy Department/DAB*

Table 4.7: Net International Reserves, for the FY 1394 (million of USD)

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

5

THE REAL SECTOR DEVELOPMENTS

5

THE REAL SECTOR DEVELOPMENTS

After several years of broad-based economic growth, Afghanistan is now experiencing troublesome economic conditions. Since the start of 2015, the economic developments have been slow and the vulnerabilities remained high. The reason behind the slowness was mainly the political and security situation in the country as it caused investments to slow down and lowered the consumer confidence. However, in the last quarter of FY2015 political conditions relatively improved which positively impacted the economy as a whole.

Political and economic uncertainties significantly impeded the economic activities in the country, as a result of which the economy plunged into recession and registered a negative growth of 2.4 percent in 2015 compared to 2.2 percent in 2014.

Growth in agriculture, one of the important components of Afghanistan's GDP, significantly declined and reached to -16.9 percent in 2015 compared to a growth of 3.7 percent in 2014. The reason behind this slowdown was the problems in harvesting agricultural crops in north east zone of the country. During 2015, industry performed well at a rate of 4.5 percent compared to 2.4 percent, while growth in services sector fell to 1.3 percent from 2.2 percent.

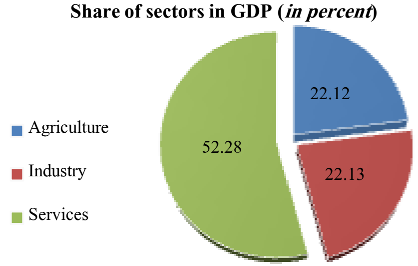
I. GROSS DOMESTIC PRODUCT (GDP) BY SECTORS PRODUCTION

Traditionally the afghan economy is more dependent on agriculture, although its share in the overall GDP has been declining over the years. Nevertheless, the agriculture sector has never produced at full capacity in Afghanistan. Services, on the other hand, have been increasing as a share of GDP over the past years.

Overall real GDP growth of -2.4 percent, was driven by -16.9 percent in real income from agriculture compare to a 2.2 percent increase in 2014. Agriculture which comprises a 22.1 percent of the overall GDP grew by -16.9 percent in 2015 compare to 3.7 percent growth in 2014. Services which comprise a massive 52.2 percent of the overall GDP, showed a slight decline in the growth compared to previous year, grew by only 1.3 percent in 2015 compared to 2.2 percent growth recorded in 2014. On the other hand, the share of Industry in the total

GDP has almost remained the same over the years with only slight changes (at 22.1 percent), as it grew by 4.5 percent in 2015 compare to 2.4 percent increase recorded in 2014.

Share of sectors in GDP (*in percent*)



Source:

Growth in agriculture sector was estimated to get momentum in 2015, but unexpected tensions in north east of the country laid unfavorable effects on agriculture sector. In most parts, the formers faced different obstacles in harvesting their agriculture crops. It is worth mentioning that this region supplies the largest portion of the country's cereals, the recent political turmoil in the area led to lower agriculture performance.. The available data reveals that in the fiscal year 2015 significant declines in the production of cereal and opium were the main drivers of meltdown of agricultural sector. T he total potential production of opium was estimated around 3300 tons in 2015, representing a 48 percent decrease from its previous year's level. The decline in production level is partly because of less area under cultivation, but more importantly due to reduction in yields/hectare.

Cereals, fresh and dried fruits, and livestock recorded a lower growth in comparison to the last year among which the most significant fall was seen in cereals, -14.2 percent in 2015 compared to 3.7 growth observed in 2014. There was a decline in the growth of fruits in 2015 as it grew by 7.2 percent compare to 18.9 percent recorded in 2014. The other component of agriculture declined sharply to -29.1 percent from 0.9 percent in the last year. Incomes from livestock, recovered very slightly from a 0.1 percent in 2014 to an increase of 0.4 percent in 2015. Similarly, , activities in industry and services sectors were also estimated to record a higher growth rate, but raising political tensions desponded the investors and declined the consumer confidence. According to available data the service sector grew by only 1.3 percent, which was lower than the 2.2 percent last year. This decline in the growth of the service sector was primarily driven by a sharp decline in incomes from finance, insurance and real estate business.. Ownership of dwellings contracted by 4.6 percent in 2015 compared to contraction of 2.4 in 2014. Producers of government services tightened by 2.3 percent in 2015 compare to 8.0 percent in 2014. Transport, storage and communication, showed a slight increase compare to last year's growth, increasing by 4.2 percent in 2015 compared to 1.8 percent in 2014.

Meanwhile, industrial sector displayed a stronger performance than agricultural sector, Manufacturing, the largest subsector, grew by 1.0 percent, which was slightly higher than the -2.5 percent last year. There were few impressive increases found in the industrial sectors relative to total GDP. For example, incomes from construction (10.03 percent of the total GDP) increased by 8.1 percent from 7.0 percent. Also there were some industrial subsectors that declined in 2015 such as the decline in the electricity, gas and water to -1.5 percent from 2.7 percent last year, since it has a very low contribution to GDP so it will not affect the overall result by much.

Table 5.1: Gross Domestic Production (GDP) by Sectors (in percent)

	1392 (2013-14)	1393 (2014-15)	1394 (2015-16)
Agriculture	24.7	24.3	22.1
Industries	19.6	20.9	22.1
Services	51.7	51.3	52.3

Source: *Central Statistics Organization (CSO)*

Table 5.2: Real GDP Growth by Sectors of Production (in percent)

	1392	1393	1394
	2013-14	2014-15	2015-16
Agriculture	8.3	3.7	-16.9
Cereals	2.3	3.7	-14.2
Fruits	2.8	18.9	7.2
Livestock	-0.2	0.1	0.4
Others	16.7	0.9	-29.1
Industry	4.5	2.4	4.5
Mining and quarrying	-1.8	-2.2	-7.9
Manufacturing	1.3	-2.5	1.0
Food, beverage, & tobacco	1.2	0.7	1.5
Textile, wearing apparel & leather	0.4	-35.7	-15.7
Wood & wood prod. incl. furniture	3.7	-25.2	-21.2
Paper, papers prod. printing, publishing	7.7	8.9	0.1
Chemicals & petroleum, coal, rubber, plastic	0.7	-16.2	1.1
Non-metallic mineral except petroleum & coal	4.6	-26.1	9.3
Metal basic	5.9	-76.9	-41.0
Electricity, gas, and water	15.6	2.7	-1.5
Construction	8.0	7.0	8.1
Services	6.4	2.2	1.3
Wholesale & retail trade, restaurants & hotels	0.4	-1.0	3.8
Wholesale & retail trade	-1.5	-2.7	2.9
Restaurants & hotels	13.6	9.2	8.9
Transport, storage and communication	11.9	1.8	4.2
Transport & storage	9.1	-1.7	0.7

Post and telecommunications	17.0	7.8	9.8
Finance, insurance, real estate and business	-10.9	-8.2	-15.3
Banking	-11.3	-8.5	-16.0
Insurance	2.3	2.3	3.8
Real estate and business services	-8.3	-4.5	-6.3
Ownership of dwellings	-6.3	-2.4	-4.6
Community, social and personal service	12.9	-1.2	-2.2
Producers of Government Services	4.2	8.0	-2.3
Other services	4.8	-0.6	-10.1

Source: *Central Statistics Organization *Preliminary data*

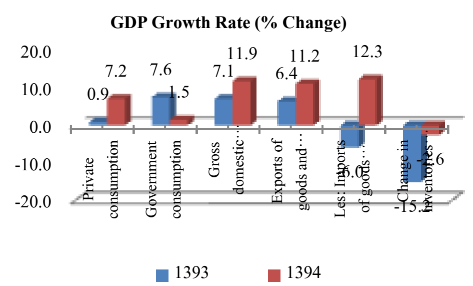
1.1 Gross Domestic Production by Expenditure Categories

Gross domestic production by expenditure categories consists of total final consumption expenditure, gross domestic investment, net export, and change in inventories. In Afghanistan, GDP by this method is measured in nominal term. During 2015, total GDP at market price grew by 2.5 percent, mainly driven by increase in total consumption, and domestic investment. However, larger trade deficit laid downward pressures on economic development.

Higher GDP in 2015 is supported by total consumption expenditure increasing by 6.4 percent from 1.8 percent. Private consumption recorded higher growth rate, 7.2 percent from 0.9 percent, as well as larger share of 84 percent compared to 80 percent in the previous year's total GDP. On the other hand, growth in government consumption declined to 1.5 percent from 7.6 percent.

In 2015, construction grew by 14.1 percent from 12.8 percent. In durable capital goods, growth continued to be negative at -27.9 percent, albeit it is higher than -44.8 recorded in the previous year. Developments in these areas resulted in higher growth rate of 11.9 percent from 7.1 percent in total gross domestic investment.

Total exports of goods and non-factor services increased by 11.2 percent from 6.4 percent, which is mainly supported by non-factor services (11.2 percent compared to 2.1 percent), and partly by exports of goods (11.2 percent from 7.4 percent). Imports of goods and non-factor services also rose, which could offset the increase in exports. In 2015, growth in total imports increased to 12.3 percent from -6 percent in 2014. The increase in imports reflects higher imports for both, goods (11.2 percent from -6.8 percent), and non-factor services (22.1 percent from 2.0 percent).



Source: *Central Statistics Organization*

Table 5.3: Nominal Gross Domestic Product by Expenditure Categories (%Δ Year-on-Year)

Category	2014	2015
Total final consumption expenditure	1.8	6.4
Private consumption	0.9	7.2
Government consumption	7.6	1.5
Gross Domestic Fixed Investment	7.1	11.9
Gross fixed capital formation	7.1	11.9
Construction	12.8	14.0
Durable capital goods	-44.9	-27.9
Resource balance	-7.8	12.5
Exports of goods and NFS	6.4	11.2
Exports of goods	7.4	11.2
Non-factor Services	2.1	11.2
Less: Imports of goods and NFS	-6.0	12.3
Imports of goods	-6.8	11.2
Non-factor Services	2.0	22.1
Change in Inventories and data discrepancies	-15.2	-2.6
GDP at Market Price	1.0	2.5

*Preliminary data Source: Central Statistic Office

II. OUTLOOK FOR 1394

Afghanistan's economic activities are expected to grow at greater pace in 2016, mainly because of government's commitments to provide proper business environment and to enhance economic infrastructure.

In agriculture sector, the government will continue its technical and counseling assistances to the formers, which are funded by foreign donors. These supports will concentrate mostly in improving the productivity of agriculture sector. There are special remarks on wheat, rice and vegetables, as the government has announced new projects especially in Northeast zone, Nangarhar, Heart, and Kandahar provinces to boost and enhance the cultivation and harvesting processes of these components.

In 2016, we also expect the industries and services sector to perform better compared to 2015. The reason substantiating the claim is that the government is committed to provide proper environment for national and international investors to start/expand their businesses in Afghanistan. One of the government's priorities in 2016 is establishing/improving domestic electricity dams, which can have significant positive impacts on economic performances. In addition, there are large projects planned in housing sector such as: the Chinese projects which will start in 2016, and the housing project for security personal, which will be implemented by the government. The TAPI and CASA-1000 are also seen to contribute to GDP growth.

6

FISCAL SECTOR DEVELOPMENTS

6

FISCAL DEVELOPMENTS

The fiscal sector developments chapter aims to assess and scrutinize performance of government in terms of revenue collection, government expenditures, grants and loans . The FY 2015 marked a substantial improvement in revenue collection. The impressive performance in revenue collection was mainly attributed to reforms to the revenue collection system, significant improvements in the tax code, in confluence with successful efforts to modernize customs and revenue administration.

However, Afghanistan's public expenditure remained unbalanced during FY 2015, owing to deterioration in security conditions which undermined private investment, delayed budget execution, and , capital flight. These factors coupled with pick-ups in operating expenditure posed serious challenges for the government to achieve fiscal sustainability.

In spite of high performance in revenue collection, domestic revenue is still significantly lower than government expenditure, both current and development expenditures. However, in order to reconcile the government spending with revenues and fill the financing gap, the government adopted the austerity measures which include cuts on discretionary item spending.

The government overall balance obtained a budget deficit of AF 14.70 billion for the FY2015.

6.1 BUDGET EXCECUTION RATE

Fiscal year 2015 saw a modest improvement in government's budget execution rate. Afghan Government managed executed only 73 percent of the core budget, compared to 67 percent in the previous year. The execution rate of current budget was 83 percent comparing to 79 percent in FY 2014. Meanwhile, execution rate of development expenditure was only 54 percent, compared to 46 percent of execution rate the same period last year.

The lower execution rate of the core budget was attributed to several factors and most importantly due to deterioration in security condition in provinces, low capacity at ministries and government agencies in planning and executing projects, delays in budget approvals and procurements and reduction in donors' funds.

6.2 BUDGET DEFICIT

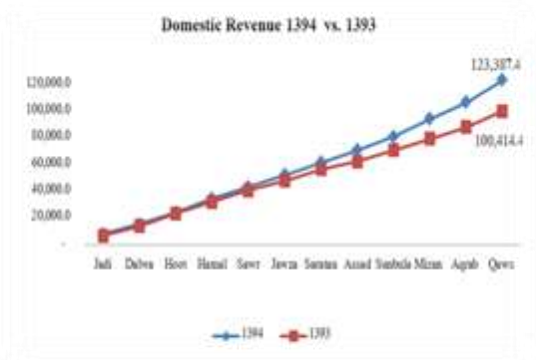
The overall budget had a deficit in 2015 decreased to AF 14.70 billion from AF 18.13 in 2014. It is believed that the decrease in budget deficit was primarily due to higher revenue collection, which was also higher than it was projected.

6.3 REVENUE COLLECTION

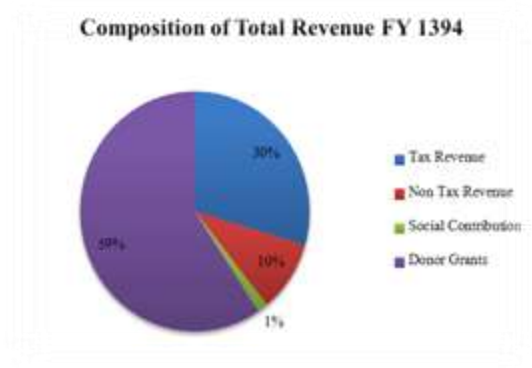
During FY 2015, reforms to the revenue collection system gained momentum with the implementation of new tax measures and important institutional reforms in customs and revenue administration.

Domestic revenue collection both tax and non-tax picked up and exceeded targeted amount of AF 114.2 billion reaching AF 123.4 billion in the FY 2015, recording an increase of 23 percent compared to the AF 100.4 billion collections in FY 2014.

However, the domestic revenue is still significantly lower than the government needs to cover its current and development expenditure.



Source: *Ministry of Finance/MPD calculation*

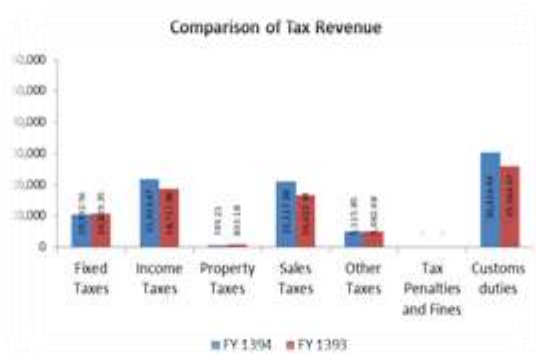


Source: *Ministry of Finance/MPD calculation*

6.3.1 Tax Revenue

Revenue collected from taxes (including customs revenue) constitutes the largest portion, around 73 percent of the total domestic revenues. Total tax revenue at the end of the FY 2015 presented considerable incline of 15 percent compared to the same period of the previous year. Total tax revenue collected (excluding custom duties) was AF 59.3 billion, up from AF 52.1 billion recorded at the end of FY 2014.

Customs duties, a major contributor to the total tax revenues, demonstrated a 17 percent of increment in FY 2015, total collections from custom duties reached 30.42 billion, compared to the AF 25.96 billion in the previous year.



Source: *Ministry of Finance/MPD calculation*

Figure 5.4: Composition of Domestic Revenue: YTD FY 1394 (actuals)

Source: *Ministry of Finance/MPD calculation*

6.3.2 Non-tax Revenues

Non-tax revenue continued to perform significantly above the estimates during the period under review and the actual revenue collection in this category was AF 29.2 billion, up from AF 17.9 billion in the previous year, presenting a significant increase of 63 percent.

Extractive industry, major component of the non-tax revenue under-performed and ended up total collection of AF 0.61 billion, lower than 0.70 billion in the FY 2014, demonstrating 13 percent decline.

In addition, a significant decline of 29 percent in sales of land and buildings were also observed in the fiscal year 2015.

The other main contributors to the non-tax revenue included income from capital and properties, sales of goods and services, administrative fees, royalties, and non-tax fines and penalties.

Social contribution that constitutes only 4 percent of the total domestic revenue presented a slight increase of only 2 percent. The total amount collected were AF 4.44 billion, up from AF 4.37 billion in FY 2014.

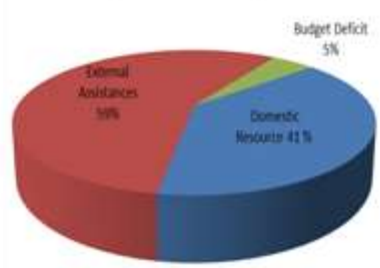
6.4 GRANTS

Afghan government receives grants from various donors, trusts and international committees to finance varieties of programs in both operating and development expenditures. Integrated grants presented a slight decline in FY 2015, compared to FY 2014.

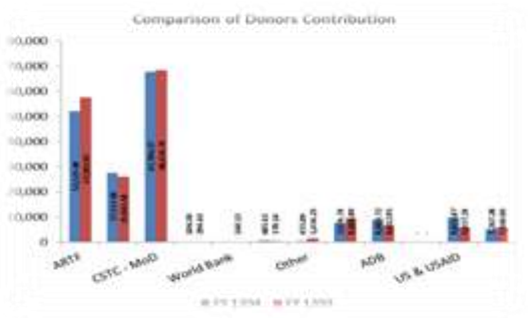
Total development and operating grants in FY 2015 amounted to AF 180.17 billion down from AF 181.98 billion in FY 2014, screening 24 percent decrease. Nevertheless, grants received under the ARTF program over the FY 2015 was AF 52.13 billion that represents a 9 percent decrease over the same period of the previous FY 2014. On the contrary, grants received from LOTFA scheme increased to AF 27.51 billion in the year under review compared to AF 25.94 billion in FY 2014, witnessing a slight increase of 6 percent.

Domestic revenue could only finance 29 percent of the total core budget and 71 percent is financed through external grants.

Financing Sources of National Budget: FY2015



Source: *Ministry of Finance/MPD calculation*



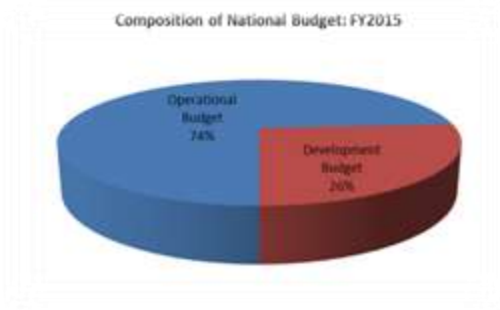
Source: *Ministry of Finance/MPD calculation*

6.5 EXPENDITURES

Total allotted budget for 2015 were AF 438.54 billion which indicates a decrement of 3.3 percent over the total allocated budget of AF 453.59billion in the year FY 2014.

Overall pay out expenditure amounted AF 318.25 billion during FY 2015 up from AF 300.52 billion FY 2014, showing 6 percent increase. On the other hand, expenditure constituted only 26 percent of GDP. The current or operating expenditure increased to AF 235.35 billion during FY 2015, up from AF 227.87 billion showing 3 percent incline and was accounted 19 percent of GDP.

Similarly, development expenditure enlarged to AF 82.91 billion from sum of AF 72.65 billion indicating 14 percent or AF 10.26 billion of increment. However, Development expenditures accounted for 7 percent of GDP.



Source: *Ministry of Finance/MPD calculation*

7

BANKING SYSTEM PERFORMANCE

7

BANKING SYSTEM PERFORMANCE

Asset sset base of the banking sector grewby5.48percent or AF 13.99 billion during the year under analysis compared to4.42 percent increase in Dec.2014.The increase in banking system assets was mainly due to increase in deposit base and FX rates.

Gross loans portfolio of the banking sector witnessed an increase of 5.03 percent or AF 2.17 billion over the last year against 7.89 percent decrease in previous year. The increase in the loan portfolio over the year is mainly accounted for exchange rate, disbursements of new loans and customer utilization of OD loans.

Deposits, the main funding source in the banking sector, stood at AF237.00 billion, comprising 96.34 percent of the total liabilities of the sector increased by 8.29 percent against 5.30percentincreasein the previous year (Dec. 2014), owing to increase demand deposits and FX rates. Deposits were largely denominated in USD (67.90 percent) with Afghani denominated deposits lagging at 27.86 percent. AF-denominated deposits indicated decrease of 11.46 points against 12.64percentincrease inDec.2014, while USD denominated deposits was up by 17.45 points against 1.15 percent increase in Dec.2014.

The capital base of the banking sector remained strong, although decreased by 17.61 percent stands at AF 24.67 billion. The decrease in total financial capital is attributed to adjustment of amount [1]AF 11 billion (this figure was reported as FX translation adjustment under capital) with claims on Ministry of Finance in the month of Dec. 2015 as a result of external audit report in one of the banks.

Capital adequacy ratio (CAR) of the banking sector recorded at19.94 percent. It shows that all the banking institutions are above the set limits for CAR, but two banking institutions are very close to the limit and one bank ratio is negative[2].

Banking sector earned net profits amounting to AF 522million for the year 2015 or fiscal year 1394, against AF2.02billion net profit in the previous year, resulting in 0.20 percent Return on Assets (ROA) against 0.83 percent in Dec. 2014 and 1.69 percent Return on Equity (ROE) against

[1] The mentioned amount was the FX revaluation gain, NKB as per the external audit report adjusted the figure with claims on MoF on the assets side.

[2] NKB's capital is negative due to huge losses.

6.84 percent in Dec.2014.Private Banks and Branches of Foreign banks ended up with profits, while State-Owned Banks ended with losses during the year under analysis.

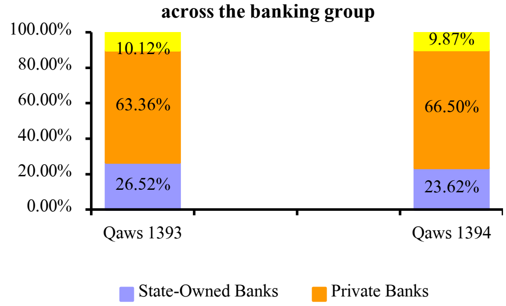
I. Assets of the Banking System

The assets size of the banking sector grew by 5.48 percentage points in the year under analysis against 4.42 percent increase in previous year. Figure 6.1

The breakup of total assets reveals that FY2015 registered an increase of AF 3.77 billion (25.12) i in investments. Meanwhile, interbank claims increased by AF 10.23 billion (15.05 percent), fixed assets increased by AF 758million (11.50 percent), cash in vault and claims on DAB showed an increase of AF 3.16billion (2.80 percent) and net loans increased by AF 1.07billion (2.67 percent).Other assets, however, decreased by AF 4.94 billion (35.23 percent) during the year under analysis.

The most important components of the system's total asset portfolio were cash in vault/claims on DAB (42.85percent), interbank claims (28.91 percent), net loans (15.22 percent),investments (6.95Percent), "other assets" (3.36percent) and fixed assets make 2.72 percent of the total assets. Table 6.1

Figure 6.1: Share of Banking Sector (Total assets) across the banking group



Source: *Financial Supervision Department, DAB*

Table 6.1: Composition of Assets and Liabilities

	Qaws 1392 Dec. 2013	Qaws 1393 Dec. 2014	% of Total Assets/Liabilities	Y-o-Y growth
Assets				
Cash in vault and claims on DAB	101,374	112,820	43.93%	11.29%
Interbank claims	68,809	68,025	26.49%	-1.14%
Investments	11,430	15,038	5.85%	31.56%
Loans (Net)	44,834	40,281	15.69%	-10.15%
Fixed Assets	6,797	6,594	2.57%	-2.98%
Others	12,507	14,037	5.46	12.23%
Total	245,751	256,795		4.50%
Liabilities				
Deposits	207,822	218,847	96.57%	5.31%
Borrowings	5,620	3,981	1.76%	-29.16%
Other	4,000	3,790	1.67%	-5.25%
Total	217,442	226,618		4.21%

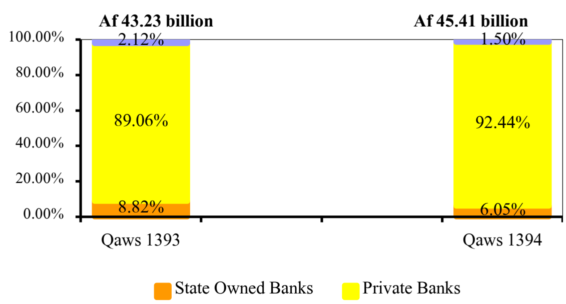
***Source:** Financial Supervision Department, DAB*

1.1 Gross Loans

Total gross loans indicated AF2.17 billion or 5.03 percent increase since last year, constituting 16.78 percent of the total assets. The increase in loan portfolio is mainly attributed to exchange rate, disbursement of new loans and customer utilization of OD[3] loans.

In addition, increases in loan portfolio were observed in nine banking institutions, whereas five banking institutions observed a decrease in their loan portfolio. While the remaining one bank (NKB) did not participate in lending; Gross loan portfolio showed an increase across the banking groups. Private Banks with 92.44percent share in total portfolio posted 9.02 percent or AF 3.47billion increases, State-owned banks with 6.05 percent share depicted 27.88 percent or AF 1.06billion decrease and Branches of foreign banks holding 1.50 percent share of the portfolio recorded a decrease of 25.71 percent or AF 236 million during the year under analysis.

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



***Source:** Financial Supervision Department, DAB*

[3] OD: Over draft

7.1.1 Loan Loss Reserves

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.

By the end ofDec.2015 (Qaws 1394), total provision cover of the system was 9.29percent of total gross loans in comparison with7.21 percent in the previous year ending Dec. 2014.

7.1.2 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 have diversified the sector wide distribution of Other Commercial Loans to thirty sectors[4]. The analysis of deployment of credit in different sectors indicates that the major portion of the loan portfolio is classified as "other commercial loans" (92.78 percent against 81.77 percent in Dec.2014), mainly in "wholesale" (9.89 percent), "petroleum and lubricants" (9.80percent), "food item" (8.24percent) and "all other services" (7.56 percent) sectors. About 74.84 percent of the loans were designated in Kabul with Herat and Balkh provinces in the second and third 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 6.2: Sectorial Distribution of Credit

	Hoot 1388 (Mar 2010)	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)
Commercial Real Estate and Construction Loans	0.19	19.92	25.98	2.85	2.29	2.02%	1.80%	1.90%
Other Commercial Loans	-	-	-	-	-	-		
Mining	-	-	0.02	0.72	0.11	0.07%		
Manufacturing	0.01	1.22	2.72	13.32	11.88	9.36%		
Trade	0.51	32.29	34.16	27.84	28.3	29.81%		
Communication	0	1.04	1.23	0.94	2.35	3.70%		
Service	0.09	4.84	6.72	11.95	15.94	22.11%		
Utilities	0.01	2.47	0.03	0.3	0.07	0.05%		
Agricultural Loans							0.27%	0.33%
Livestock and Farms							0%	0.03%
Manufacturing and Industry(product of metal, wood, plastic, rubber)							2%	4.42%
Manufacturing, Handmade and Machine products							4%	4.24%
Cement and Construction Materials							3%	1.96%
Textile							2.59%	0.52%
Power							0.35%	0.22%
Construction and Building							12.52%	7.54%
Services							4.79%	3.80%
Hotel and Restaurant							1.20%	1.46%
Telecommunication							2.92%	5.70%
Ground Transportation							4.87%	5.31%
Air Transportation							4.18%	2.66%
Health and Hygienic							0.71%	1.16%
Median, Advertisements and Printer							0.04%	0.04%
All Other Services							1.41%	7.56%
Wholesales							4.93%	9.89%
Machineries							0.12%	0.25%
Petroleum and Lubricants							8.74%	9.80%
Spare Parts							0.24%	1.42%
Electronics							1.40%	1.58%
Cement and other Construction Materials							1.87%	2.73%
Food Items							4.52%	8.24%
All Other Items							5.72%	3.47%
Retail Trading							3.92%	3.28%
Road and Railway							2.41%	1.17%
Dames							0.61%	0.09%
Mines							0.08%	1.48%
Other infrastructure Projects							1.81%	2.44%
Financial and Lending Institutions							0.00%	0.00%
Agricultural Loans	0	0.88	0.75	2.06	2.66	2.38%	2.34%	2.35%
Consumer Loans	0.02	1.33	1.01	0.82	0.74	0.24%	0.26%	0.30%
Residential Mortgage Loans to Individuals	0.01	7.3	8.95	15.65	14.46	10.84%	7.14%	2.68%
All Other Loans	0.05	3.69	10	12.65	10.71	9.41%	6.68%	0.00%

Source: *Financial Supervision Department/DAB*

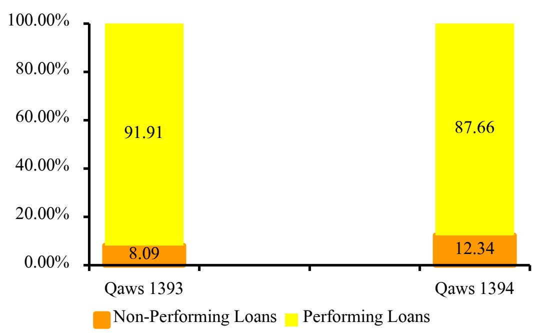
7.1.3 Classification of Loans

7.1.3.1 Non-performing loans

By the end of Dec.2015the growth in non-performing loans accelerated by AF2.10 billion standingatAF5.60 billion, 12.34 percent of total gross loans and 26.32 percent of the system's regulatory capital against AF 3.49 billion or 8.09 percent of the total gross loans in the preceding year. The deterioration is mainly due to weaker loan quality. More than 60percent of the NPLs relates to two Private commercial banks holding 47.93 percent of total gross loans of the banking sector.

The sector wide distribution of NPL reveals that a major portion of NPLs originated from commercial loans mostly related to trade, manufacturing and services sectors. Increases were posted in manufacturing, trade, utilities and residential mortgage loans to individuals sectors, while services sector posted decrease.

Figure 6.3: Quality of Loan Portfolio



Source: *Financial Supervision Department/DAB*

7.1.3.2 Adversely-classified loans

Adversely classified loans (sub-standard, doubtful) [5]depicted AF 2.14billion increase over the last year amounting to AF 8.69 billion, constituting 19.16 percent of the total gross loans.

7.1.3.3 Loans classified Watch

Loans classified in the "watch"[6] category are AF 4.85billion, which makes 10.69 percent of total gross loans, increased by 57.59 percent since the previous year (Dec.2014) attributed mainly to two private commercial banks.

7.1.3.4 Loans classified loss7

Loans classified loss, amounts to AF 408 million or 0.89 percent of total gross loans, were up by AF 240 million since previous year, mostly attributed to two banks.

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[5]Assets 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

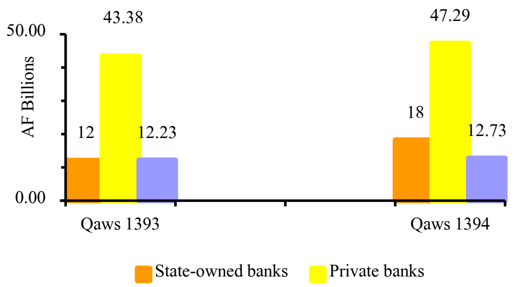
[6] Assets and advances for which the principal and/or interest remains outstanding for 1-30 days (Watch)-new Assets Classification and provision regulation

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

1.2 Interbank Claims

Interbank Claims are the second largest among various asset categories, currently comprising AF78.26 billion–28.91 percent of total assets registered AF10.23 billion increases since previous year (Dec.2014), mostly attributed to four banking institutions, indicating that the banking sector has channeled a portion of its attracted funds as deposits in other financial institutions. These institutions are both inside and outside the country. Later on, if needed for liquidity purposes or after receiving applications from low-risk borrowers, these assets can be substituted to higher income earning assets. Figure 6.4

Figure 6.4: Share of Inter bank Claims among banking groups



Source: *Financial Supervision Department/DAB*

1.3 Investment

The investment[8] portfolio of the banking sector comprising of bonds, Gov. Securities and investment in associated companies. Banking sector investment portfolio grew by 25.12 percent or AF 3.77 billion standing at AF18.81 billion, 6.95 percent of total assets, in the FY2015. Major part of the sector's investment took place outside Afghanistan. The investment portfolio is attributed to five commercial banks and two branches of foreign banks.

1.4 Cash in Vault and Claims on DAB

Cash in vault and claims on DAB remains the largest category making 42.85 percent of the total assets, showed an increase of AF 3.16billion, both in absolute as well as in percentage of total assets since previous year ending Dec.2014.

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

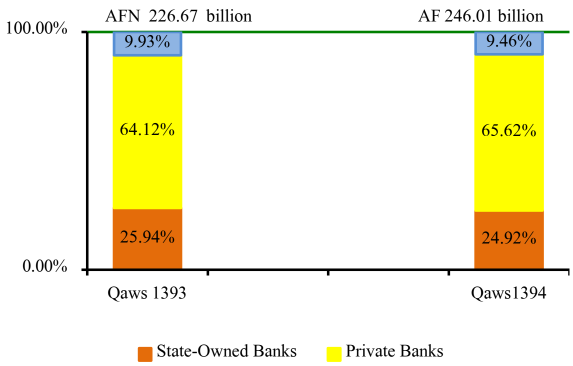
II. LIABILITIES

Total liabilities of the banking sector increased by AF19.33 billion, 8.53 percent, standing at AF246.01 billion against AF226.67 billion in the preceding year (Dec. 2014). All components of total liabilities have shown increase over the fiscal year 2015.

The majority of liabilities are made up of deposits (96.34 percent). This is an indication of public confidence, and good public relations and marketing policies of the banking sector, with "other liabilities "at second and borrowings in third place. Table 6.5

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

Figure 6.5: Liabilities increased by AF 19.33 billion or 8.53 percent



Source: *Financial Supervision Department, DAB*

2.1 Deposits

Deposits being the main funding source, amounted to AF 237.00 billion for the year under analysis, increased by AF 18.15 billion or 8.29 percent, compared to 5.31 percent increase in Dec. 2014.The increase in Deposit base of the banking sector attributed to increase in FX rates. Currency wise analysis shows that the USD and Other currency increased by AF 26.70 billion, of which almost 6 percent was due to inflow of funds and the remaining 93 percent was due to increase in FX rates. The USD rate showed almost 9percent increase over the last year.

Afghani denominated deposits indicated 11.46 percent decrease against 12.64 percent increase in FY 2014, accounting for 27.86 percent of total deposits, while US dollar denominated deposits were up by 17.45 percent, making 67.90 percent of the total deposits of the system.

Private Banks attracted AF 156.91 billion deposits, up by 11.52 percent against 8.99 percent increase in previous year, making up 66.20 percent of the system's deposits.

The share of state-owned banks increased to AF 58.52 billion or 1.91 percent)in the period under review). Deposits in state owned banks accounted for 24.69 percent of the system's deposits.

The share of branches of foreign banks stands at AF 21.57 billion making up 9.10 percent of total deposits in the system, increased by 4.09 percent compared to9.04 percent decrease in 2014..

In terms of types of deposits, demand deposits accounted for 77.24 percent of the total deposit base, up by 6.90 percent, saving deposits constituting 17.60 percent of total deposits depicted 3.92 percent. Meanwhile, time deposits, making up 5.16 percent of the total deposits, portfolio was up by 63.67 percent since in 2015.

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Figure 6.7: Afghani Denominated Deposits

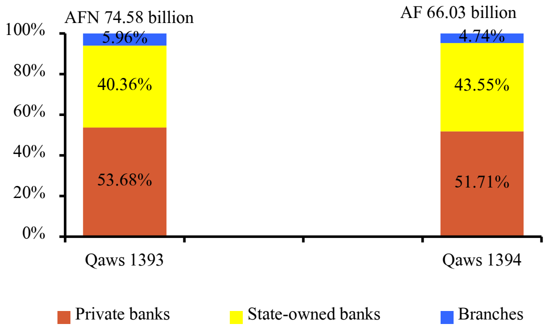
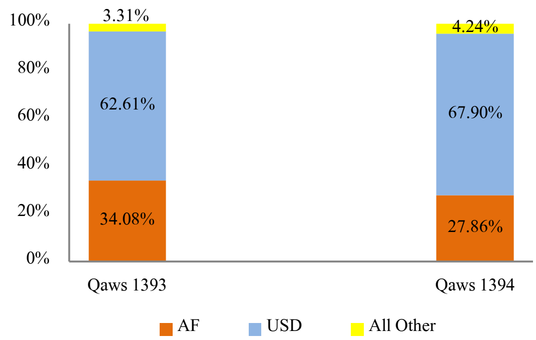


Figure 6.6: Currency Composition of Deposits



Source: *Financial Supervision Department, DAB*

Figure 6.8: Deposits Increased by 8.29 percent
or
AF 18.15 billion

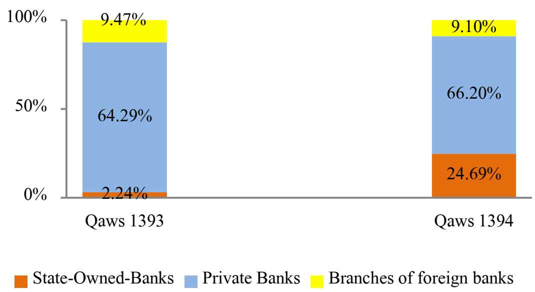
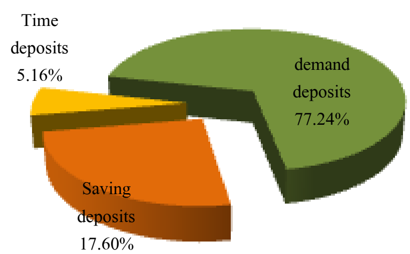


Figure 6.9: Breakdown of Deposits



Source: *Financial Supervision Department, DAB*

2.2 Borrowings

The share of borrowings in total funding structure of the system increased by 11.83 percent standing at AF 4.45 billion at the end of Dec.2015, making 1.81percent of total liabilities in comparison with 29.16 percent decrease in the preceding year. The current borrowing position is attributed to four banking institutions.

III. LIQUIDITY

Liquidity risk can be defined as the risk of not having sufficient liquid assets to meet the demand of borrowers and depositors. 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.

IV. CAPITAL

The system is well capitalized. The capital fund of the banking sector stands at AF24.67billion; decreased by 17.61 percentage points or AF 5.27 billion over the last year. The decrease in total financial capital is attributed to adjustment of amount AF 11 billion (this figure was reported as FX translation adjustment under capital) with claims on Ministry of Finance in the month of Dec. 2015 as a result of the external audit report in one of the banks.

On an aggregate basis the Capital Adequacy ratio of the banking sector stands at 19.94 percent. Table 6.5

Disaggregated analysis shows that all banks in the system registered capital adequacy ratio above the minimum threshold (12 percent of risk-weighted assets), but two banking institutions are very close to the limit and one bank ration is negative. The Basel benchmark for capital to risk weighted is 8 percent.

3.1 Liquidity Ratio (broad measure)

Banks are required to maintain a liquid asset ratio not less than 15 percent. This should provide a comfortable safeguard against any liquidity shortfall.

Generally, a surplus liquidity position was observed in the banking sector during this period. 69 percent of the sector's total assets are comprised of liquid assets. Ratio of the broad liquidity as a median for the whole system stood at 68.22 percent. All banking institutions were well above the minimum required level. Table 6.5

Table 6.5: Key Financial Soundness Indicators of the banking Sector

	1388 (Mar 10)	1390 (Mar 11)	1390 (Mar 11)	1390 (Mar 12)	1391 (Dec 12)	1392 (Dec. 13)	1393 (Dec. 14)	1394 (Dec. 15)
Total Capital Adequacy Ratio	25.81	-14.46	30.39	23.06	21.84	26.34	26.46	19.94
Tier 1 Capital Adequacy Ratio	24.19	-14.51	30.29	23.98	19.97	24.65	26.09	19.66
Non-Performing Loans to Total Gross Loans	0.5	48.4	3.75	5.15	5.31	5.10	8.09	12.34
Return on Assets (ROA)	1.41	-20.08	0.24	-1.21	-0.54	0.74	0.90	0.20
Return on Equity (ROE)	10.35	-520.66	1.9	-17.9	-7.17	10.03	7.35	1.69
liquidity Ratio (Broad Measure Median)	59.19	63.32	63.83	57.37	72.13	67.93	73.60	68.22
liquidity Assets to Total Assets	0.38	40.58	47.01	55.82	63.75	73.18	73.28	75.05

*Excluding Kabul Bank

Source: *Financial Supervision Department, DAB*

V. PROFITABILITY

On a cumulative basis at the end FY 2015 the banking sector earned AF 522 million net profit as compared to AF 2.02 billion net profit in 2014, showing 74 percent decrease over the year.

The decrease in profitability of the banking sector, shown in table 6.5, is mostly ascribed to significant increase in credit provisions created for problem assets, other contributing factors are decrease in net-interest income and increase in salary cost. While non-interest income showed increase and non-interest expense decreased in the year under analysis.

As a result the returns on assets (ROA) decreased to 0.20 from 0.83 percent and return on equity (ROE) became 1.69 percent from 6.84 percent in the previous year. Table 6.5

On a cumulative basis four banking institutions have incurred AF 1.28billion losses in the year under analysis against AF 366 million losses posted by two banks in the year ending 2014.

On core income basis two banks ended with losses, against the one bank in the previous year. income and a decrease in non-interest expense and credit provisions. While Group wise analysis reveals Private Banks (PB) and branches of foreign banks (BFB) ended up with profits, while State-owned banks (SOB) ended up with losses for the year under review. Figure6.10

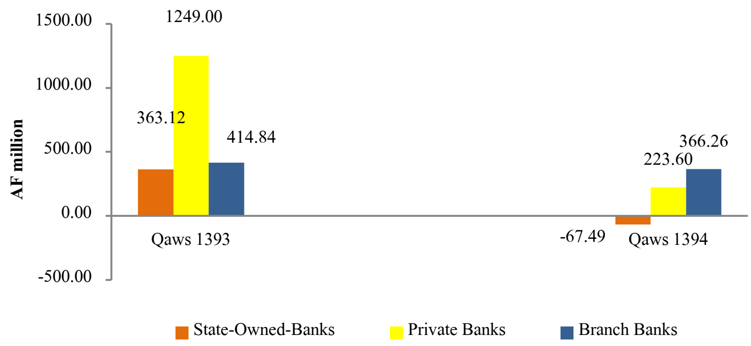
Major portion of the profitability of the banking sector is attributed to branches of foreign banks standing AF 366 million, decreased by 6 million or 1.61 percent, private banks are at second place with AF 224 million, registering AF 1.06 billion decrease over the year while State-owned banks are at loss stands at AF 67 million decreased mainly attributed to increase in credit provisions.

Table 6.4: P/L Schedule

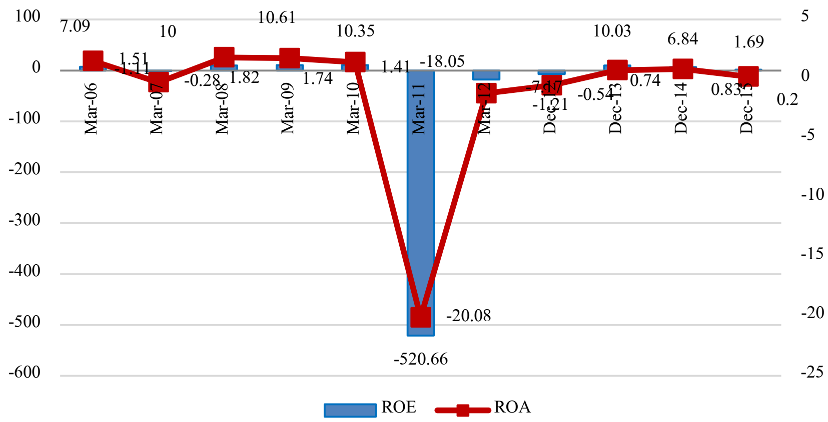
	1393 (Dec. 2014	1394 (Dec. 2015)	% change Y-o-Y
interest income	9,658	9,076	-6.02
interest expense	1,893	2,044	7.97
Net interest income	7,765	7,032	-9.44
Non-interest income	5,310	5,981	12.63
Non-interest expenses	5,791	5,612	-3.09
Salary cost	3,551	3,687	3.83
Credit provisions	1,289	2,952	129.01
P/L before tax	2,444	762	-68.82
P/L after tax	2,027	522	-74.24

Source: *Financial Supervision Department, DAB*

Figure 6.10: Profitability of the Banking Sector

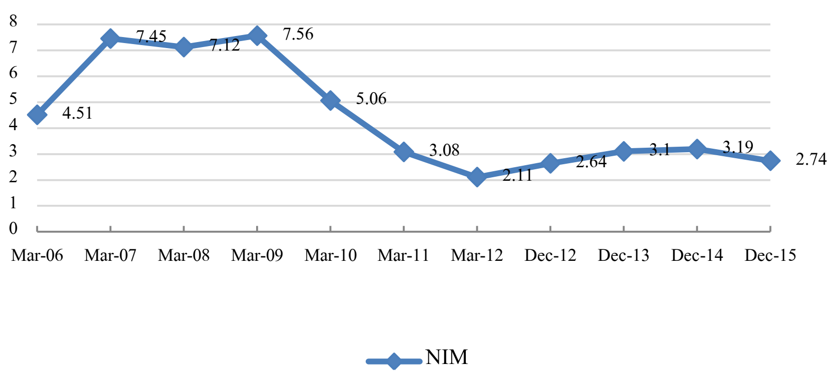


Source: *Financial Supervision Department/ DAB*



Source: *Financial Supervision Department/ DAB*

Net Interest Margin



Source: *Financial Supervision Department/DAB*

VI. FOREIGN EXCHANGE RISK

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

The impact of change in exchange rate upon regulatory capital of the system reveals that a 20 percent appreciation in exchange rate would increase the regulatory capital of the system by AF 9.03 billion, and vice versa. Similarly, a 4 percent change would correspond to AF1.80 billion and vice versa.

VII. INTEREST RATE RISK

Overall the banking system is in an interest-rate sensitive position. However, calculations made from the Interest Rate Sensitivity Schedules of all banks reveal that, the net-interest income of the system over the next 12 months may increase by AF1.72 billion in an 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 byAF1.72billion. For one banking institution, if the interest-rate increases by 3 percentage points, that will decrease in 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-bearing assets over interest-bearing liabilities. Although it may improve the net interest margin and overall profitability of the bank, this situation makes the banks more vulnerable to a sudden decrease in market rates.

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