Da Afghanistan Bank

# Economic & Statistical Bulletin

3rd Quarter Bulletin FY 2020

Monetary Policy Department

Da Afghanistan Bank

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Note:

Afghanistan's fiscal year has changed effective from 2012 (1391). The new fiscal year begins from December 22nd. This bulletin analyzes economic developments during the third quarter of fiscal year 1399, which starts from June 21st, 2020 to September 21st, 2020 (Jadi 01, 1399 – Saratan 31, 1399).

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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 |
| NSIA | National Statistics and Information Authority |
| 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 |

# EXECUTIVE SUMMARY

Afghan government gradually eased lockdown/restriction during third quarter of FY 1399. Borders and ports were reopened, trade (import and export) accelerated with trading partners along with air travel being confined only to a few countries where restriction were lifted. These all led to a notable increase in the economic activity, domestic consumption, exports and imports, remittance and personal transfer, and services related activities during the third quarter of FY 1399 (2020).

Da Afghanistan Bank maintains monetary aggregate targeting regime, under which Reserve Money is selected as the main operational target, and Currency in Circulation (CiC) as the indicative target for liquidity. To attain its operational target (reserve money target) and to keep domestic prices stable (which is the primary goal of Da Afghanistan Bank), DAB uses Open Market Operations (OMOs) for controlling and managing liquidity in the market.

Reserve Money had 1.82% growth which stood at Afs 314,764.84 million from start till end of the third quarter of FY 1399, on the other hand, Currency in Circulation as a major component of RM, with a 9.29% growth stood at Afs 284,149.14 at the end of the first three quarter of FY 1399. Both, reserve money and currency in circulation were below the targets. In order to absorb excess liquidity from the market and to smooth exchange rate fluctuations between Afghani and foreign currencies, DAB auctioned USD 1,512.31 million during the first three quarters of FY 1399 (2020).

Consumer Price Index (CPI) is computed based on April-2015 base prices. Measuring National inflation by Y-On-Y, the overall index on average stands at 5.97% in the third quarter of FY 1399 (2020) where it was 2.51% (on average) in the third quarter of FY 1398 (2019). Based on monthly measures, inflation rate (overall index) stood at 6.33%, 5.88%, 5.70% in July, August, and September of FY 2020 respectively. While by Q-On-Q basis, inflation had downward trend, decreasing from 7.10% in the previous quarter to 5.97% in the third quarter of FY 1399 (2020).

Balance of payment deficit was USD 884 million at the end of the third quarter of FY 1399 (2020). Current account deficit shows decrease of 13% standing at USD 893.51 million, while it stood at USD 1,028.38 million in the third quarter of FY 1398 (2019). The decrease in current account deficit was due to increase; in official grants, personal transfer, and receipts of services account in the third quarter of FY 1399 (2020).

Capital account stood at USD 109.53 with a 72% decrease, where it was recorded USD 391.57 million in the third quarter of the previous year. Considering the Financial account, FDI inflow were USD 4.78 million while outflow stood at USD 10 million, on the other hand, portfolio investment recorded USD 83.11 million which indicated increase in Afghanistan's investment abroad compared with USD -33.74 registered in the same quarter of FY 1398 (2019).

Core budget had a deficit of Afs 0.76 billion (excluding donor contribution) and a surplus of Afs 10.58 billion (including donor contribution).

Total revenue showed increase in the third quarter of FY 1399 and stood at Afs 109.22 billion while it was recorded Afs 91.63 billion in the third quarter of the last year, total expenditures on the other hand, increased to Afs 98.64 billion in the third quarter of FY 1399 compared to Afs 97.88 billion in the same quarter of the last year. as well and registered Afs 97.88 billion in the third quarter of FY 1399 (2020).

Total domestic revenue decreased to Afs 40.27 billion in the third quarter of FY 1399 compared to Afs 42.16 billion registered in the same quarter of last year, also, Donor contribution increased by 39.39% (Afs 19.49 billion) and recorded Afs 68.95 billion in the third quarter of FY 1399, where it was Afs 49.47 billion in the third quarter of the previous year. Meanwhile, budget execution rate (actual spending) reached to 55% from the total approved budget of Afs 471 billion at the end of third quarter of FY 1399 (2020).

Banking sector makes 21.7% of Afghanistan's GDP and comprises of twelve (12) duly licensed banks. Overall, main indicators (total assets, equity capital, deposits) of the banking sector performance demonstrated increase compared to the second quarter of FY 1399 (2020).

Assets of the banking sector registered Afs 318.7 billion with 0.84% increase which was due to increase in customer's deposits and profit in the banking sector, while liabilities of the sector show increase of Afs 2.2 billion standing at Afs 281.4 billion in the third quarter of FY 1399 (2020). On the other hand, financial capital of the sector is above the set regulatory limits, set regulatory threshold (12%), and Basel benchmark for capital to risk weighted (8%) and stands at Afs 37.28 billion, which shows the system is well capitalized.

Profitability of the sector was decreased due to increase in credit provision, operational cost, decrease in interest and non-interest income. The sector registered Afs 504 million net profit in the third quarter of FY 1399 (2020), meanwhile, Return on Assets (ROA) stood at 0.21% where Return on Equity (ROE) was 1.81%.

Islamic Banking sector's main financial indicators show that the sector performed well during the third quarter of FY 1399 (2020). Assets of the sector stood at Afs 39.44 billion with 6.48% growth, while liability also increased by 7% stood at Afs 35.34 billion in the third quarter of FY 1399. On the other hand, equity capital of full-fledged Islamic bank remained stable due to increase in profitability.

Liquidity position of all Islamic banking windows and one full-fledge bank was above the set minimum for broad liquidity ratio (15%) and quick liquidity ratio (20%). Meanwhile, capital of the Islamic banking sector stands at Afs 4.1 billion making 10.4% of the total assets of the sector in the third quarter of FY 1399 (2020).

# 1

# Global Economic Environment

# 1

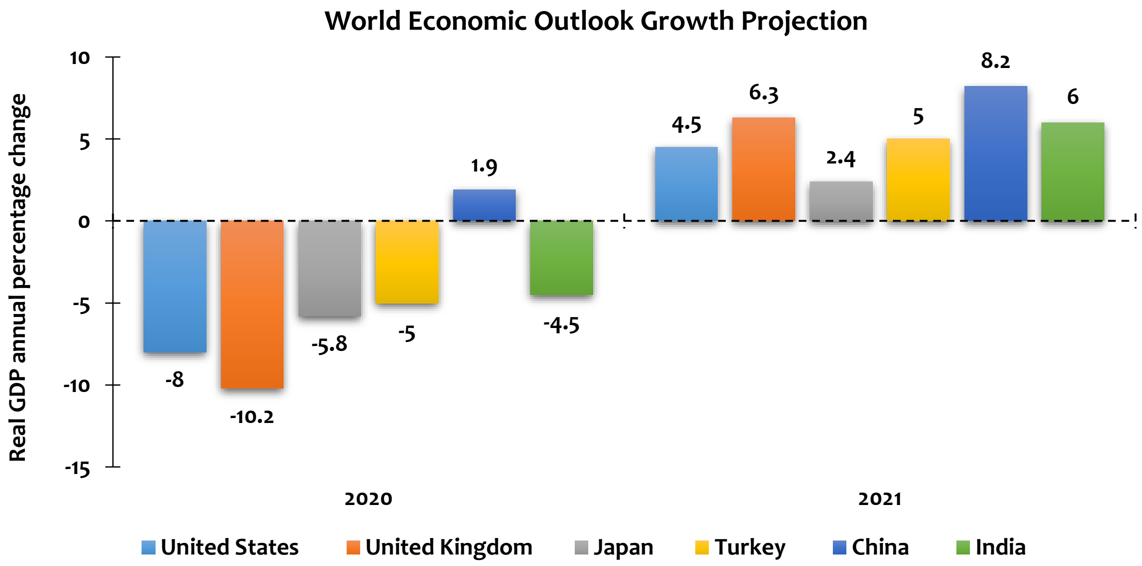
# GLOBAL ECONOMIC ENVIRONMENT

The COVID-19 pandemic has spread with astonishing speed to every part of the world and infected millions. The health and human toll is already large and continues to grow, with hundreds of deaths and many more suffering from diminished prospects and disrupted livelihood.

The pandemic represents the largest economic shock the world economy has witnessed in decades, causing a collapse in global activity. It is worth mentioning that Central banks in advanced economies have cut policy rates and taken other far-reaching steps to provide liquidity and to maintain investor confidence. In many Emerging and Developed Economies (EMDEs), central banks have also eased monetary policy. Global growth is projected at –4.4% in 2020 the global economy is expected to shrink by 5.2% in the year 2021 advanced economies are projected to shrink by 7% in 2020, EMDE GDP is forecast to contract by 2.5% in 2020[1].

In addition, after the rebound in 2021, global growth is expected to gradually slow to about 3.5% into the medium term. This implies only limited progress toward catching up to the path of economic activity for 2020–25 projected before the pandemic for developing emerging, and advanced economies. Moreover, in an upside scenario, a sharp economic rebound would begin promptly if pandemic-control measures could be largely lifted in the near term, and fiscal and monetary policy responses succeed in supporting consumer and investor confidence, leading to a prompt normalization of financial conditions and the unleashing of pent-up demand[2].

**Figure 1.1:** Real GDP Growth Advanced and Emerging Economies




**Source:** IMF, World Economic Outlook Update June 2020/MPD Staff Calculation

[1] World Bank Economic Outlook, October 2020

[2] IMF World Economic Outlook, October 2020

## 1.1. Advanced Economies:

### 1.1.1 United States' Economy:

The economy recovered robustly in third quarter, after second quarter's unprecedented contraction due to the blow dealt by Covid-19. GDP increased 38.0%, or $1.64 trillion, in the third quarter to a level of $21.16 trillion, while it had decreased 32.8%, or $2.04 trillion[3] in the second quarter. In September, the unemployment rate dropped 0.5 percentage points from the month prior, while non-farm payrolls continued to rise, although they were still down $10.7 million compared to February. This coupled with consumer confidence hitting a six-month high, likely boosted private spending, as suggested by a jump in auto and clothing sales in the same month.

Furthermore, upbeat construction activity and a surge in housing starts in third quarter should have supported residential investment. Meanwhile, Joe Biden and the Democrats are currently leading the polls ahead of the presidential elections on 3 November. Under a Biden administration, economic growth would likely benefit from increased spending on infrastructure and social security, as well as a less disruptive foreign trade policy. In addition, GDP should rebound on the back of ample monetary and fiscal stimulus, and as the impact of the pandemic fades.

A lower unemployment rate and rising consumer confidence levels should support household spending next year. U.S.–China trade tensions and renewed lockdown measures are key downside risks to the outlook. Besides that, Inflation fell to 1.2% in October, easing slightly from September's 1.4%. October's reading represented the weakest inflation rate since July. Annual average inflation remained at September's 1.4% in October. Lastly, core inflation edged down to 1.6% from the previous month's 1.7%.

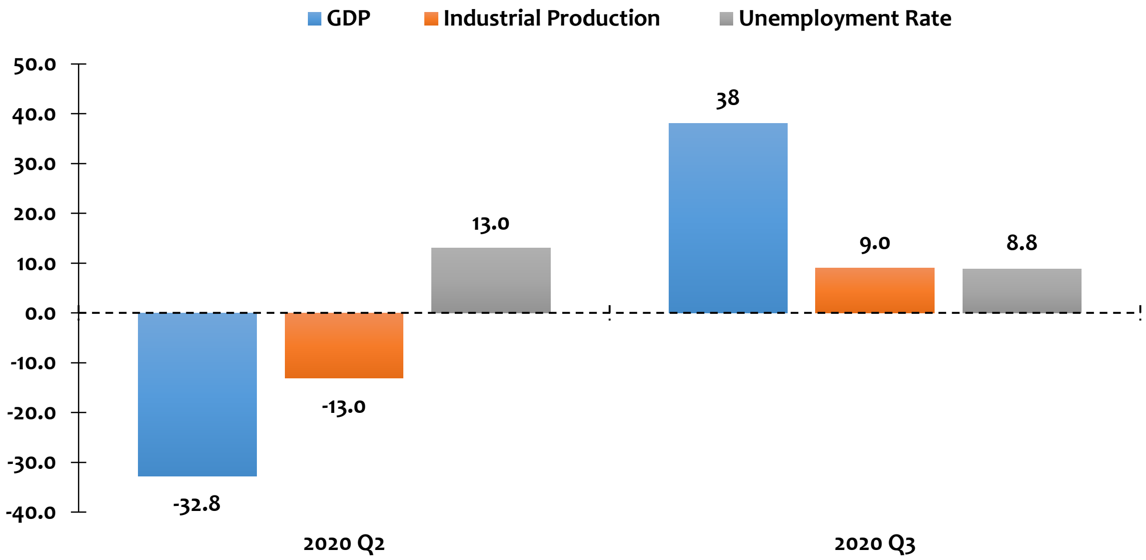
The core personal consumption expenditures price index a gauge of household spending closely tracked by the Fed-accelerated to 1.4% in September, the latest month for which data is available. This was up from 1.3% in September and moved slightly closer to the Fed's 2.0% target and forecast participants expect inflation to average 1.9% in 2021, which is up 0.1 percentage points from the last month's forecast.

For 2022, the panel expects inflation to average 1.9%. Furthermore, the unemployment rate decreased to 6.9% in October from 7.9% in September, as the labor force participation rate ticked up to 61.7% in October from 61.4% in September. Forecast panelists expect the unemployment rate to average 8.4% in 2021, which is down 0.2 percentage points from last month's estimate, and 6.8% in 2022[4]. Hourly earnings increased 0.1% month-on-month in October (September: +0.0% mom), while annual wage growth eased to 4.5% from 4.6% in September.

[3] Bureau of Economic Analysis USA

[4] Focus Economics

**Figure 1.2:** US Quarterly GDP Growth, Industrial production and unemployment rate (percentage growth rates Q-On-Q)




**Source:** Fed Reserve Bank of ST. Louis/MPD Staff Calculation

### 1.1.2 The Economy of UK:

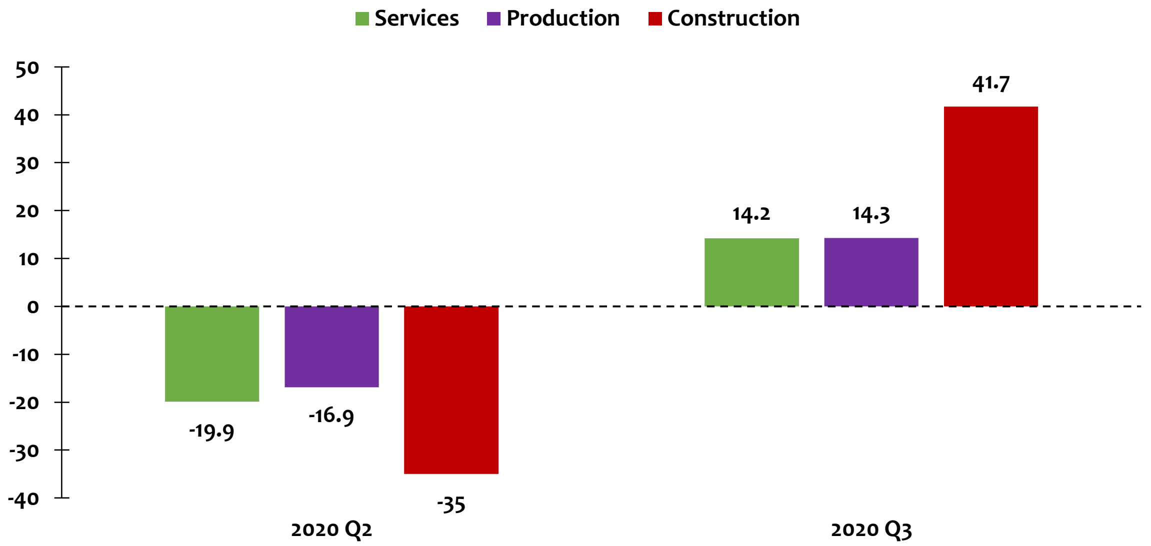
The monthly path of GDP in third quarter FY 2020 reveals that there has been a slowdown of growth in August and September as momentum has eased through the quarter. GDP increased by 6.3% in July, driven by accommodation and food services as lockdown restrictions were eased. Meanwhile, the UK gross domestic product (GDP) is estimated to have grown by a record 15.5% in third quarter (July to Sept) 2020, as lockdown measures were eased. Though this reflects some recovery of activities following the record contraction in second quarter (Apr to June) 2020, the level of GDP in the UK is still 9.7% below where it was at the end of 2019.

Compared with the same quarter a year ago, the UK economy fell by 9.6%. While output in the services, production and construction sectors increased by record amounts in third quarter 2020, the level of output remains below fourth quarter (Oct to Dec) level, before the impact of the coronavirus (COVID-19) pandemic was seen. Furthermore, the Consumer Prices Index including owner occupiers' housing costs (CPIH) 12-month inflation rate was 0.7% in September 2020, up from 0.5% in August 2020. The largest contribution to the CPIH 12-month inflation rate in September 2020 came from recreation and culture (0.31 percentage points).

Transport costs, and restaurant and café prices, following the end of the Eat Out to Help Out scheme, made the largest upward contributions (of 0.23 and 0.21 percentage points, respectively) to the change in the CPIH 12-month inflation rate between August and September 2020. While, items account for 1.1% of the CPIH basket by weight and made a small upward contribution of 0.01 percentage points to the change in the CPIH 12-month rate; for September, we have collected a weighted total of 90.2% of comparable coverage collected previously (excluding unavailable items). The Consumer Prices Index (CPI) 12-month rate was 0.5% in September 2020, up from 0.2% in August.

Besides that, UK employment rate in the three months to September 2020 was estimated at 75.3%, 0.8 percentage points lower than a year earlier and 0.6 percentage points lower than the previous quarter. The UK unemployment rate in the three months to September 2020 was estimated at 4.8%, 0.9 percentage points higher than a year earlier and 0.7 percentage points higher than the previous quarter. In the three months to September 2020, redundancies reached a record high of 314,000; an increase of a record 181,000 on the quarter. In October, 33,000 fewer people were in pay-rolled employment when compared with September, while the figure was 782,000 fewer when compared with March 2020.

**Figure 1.3:** UK GDP, Quarterly Percentage Changes (Q-On-Q percentage growth rate)




**Source:** Office for National Statistics/MPD Staff Calculation

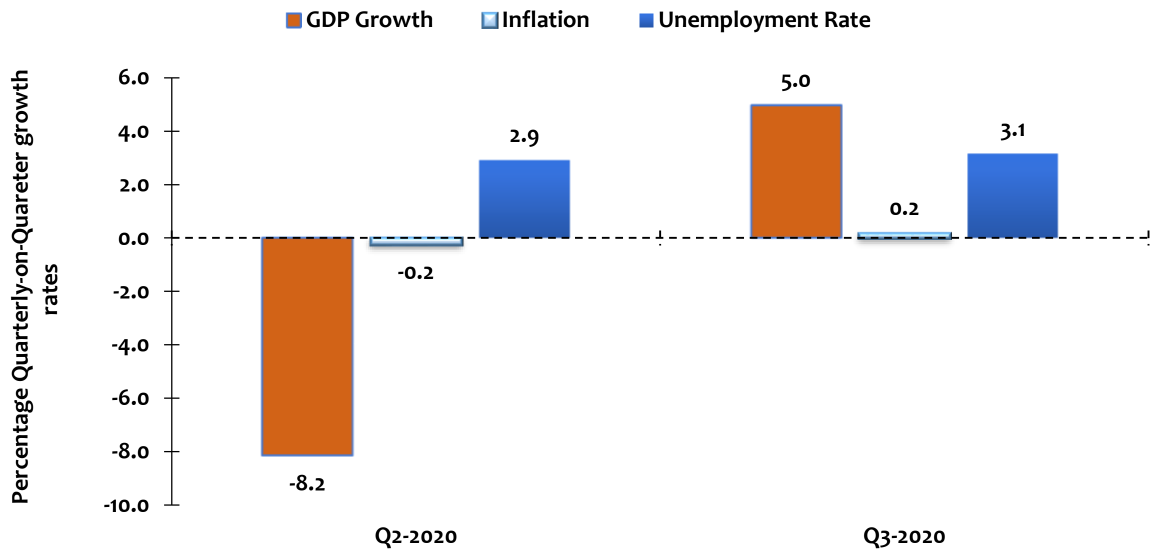
### 1.1.3 Economy of Japan:

The economy is expected to show movements of picking up, supported by the effects of the policies while the socio-economic activities will be resumed gradually with taking measures to prevent the spread of infectious disease of Coronavirus. However, attention should be given to the risk that domestic and overseas infections would affect economies. Beside that the Japanese economy is still in an extremely severe situation due to the Novel Coronavirus, but it almost stopped deteriorating in the month of June, and increased in July and August. While, severe situation due to the Novel Coronavirus, but it is showing movements of picking up recently in the month of July and the economy is still in a severe situation due to the Novel Coronavirus, but it is showing movements of picking up recently in the month of August.

Moreover, the industrial production shows gradual decrease in the month of June due to the influence of the infectious disease, while it shows sign of picking up recently in some sectors and it is decreasing as a whole. Industrial production shows movements of picking up in some sectors. Besides that, private consumption shows gradual changes such as showing movements of picking up recently upward trend as the state of emergency was lifted in the month of June, July and August. The outbreak of coronavirus also affected the foreign trade as exports represented huge decline during June-August.

Furthermore, export shows gradual changes during the third quarter as per record which shows exports are decreasing due to the influence of the infectious disease in the month of June, while indicating upward movement, although the influence of the infectious disease remains in the month of July and represents movements of picking up in the month of August respectively. It is worth mentioning that employment level has observed server changes during the pandemic which shows weakness and significant decrease in June, while, showing no changes in the month of July and August consecutively. Moreover, business investment shows notable changes during the period (Jun-Aug) indicating weak progress during the month of June with no changes in July and decrease August[5].

**Figure 1.4:** Japan Quarterly Percentage Changes of GDP, Inflation and Unemployment




**Source:** Fed Reserve Bank of ST. Louis/MPD Staff Calculation

## 1.2. Emerging Economies:

### 1.2.1. China:

Since the start of 2020, the COVID-19 pandemic has dealt a heavy blow to China's economic and social development. Meanwhile, under the strong leadership of the Communist Party of China (CPC) Central Committee, the entire nation worked as one and achieved significant results in coordinating pandemic containment with economic and social development. Besides that, looking beyond the near term, the fundamentals of steady economic growth in the long run and high-quality development remain unchanged.

Moreover, The Chinese economy has demonstrated strong resilience. With pandemic containment measures remaining in place, economic and social activities have basically

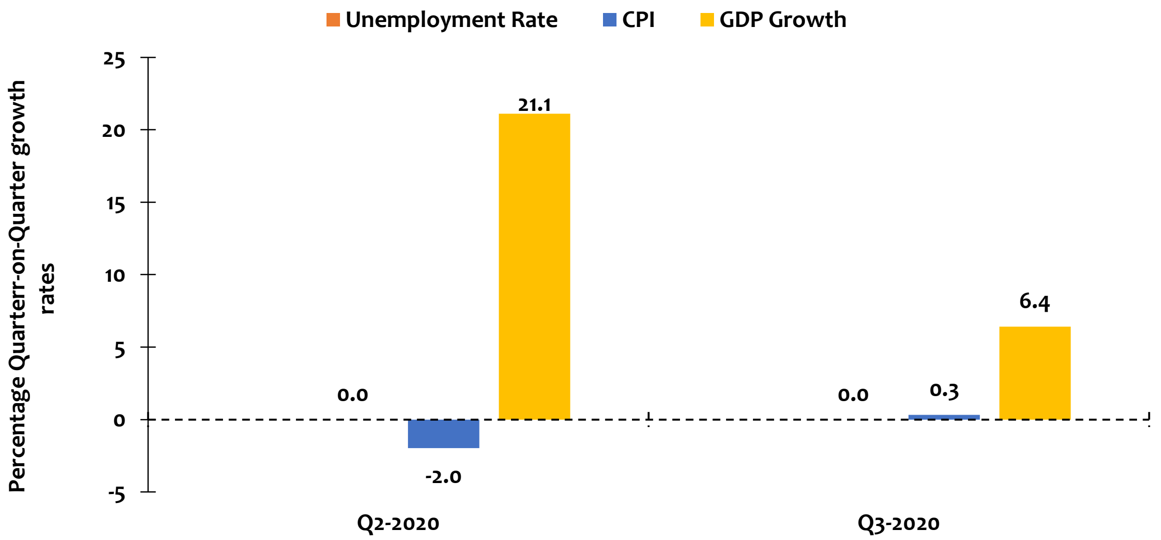
[5] Economic Development, Cabinet Office

returned to normal, thereby accelerating economic growth and recovery.

It is worth mentioning that the pandemic containment and economic recovery in China is among the fastest in the world. China's development is still and will continue to be for a long time at an important stage of strategic opportunities. Agricultural production was fairly satisfactory, industrial production recovered rapidly, and the decline of the service industry decelerated primary industry grew by 0.9% year on year, accounting for 5.7% of GDP. The total output of summer crops grew by 0.9% year on year and the value-added of Industrial Enterprises above a Designated Size (IEDS) decreased by 1.3% year on year. In addition, the proactive fiscal policy has been more impactful and the sound monetary policy has been more flexible and appropriate which shows deceleration in declining trend of fiscal revenue, and the employment situation was generally stable.

The financial sector has continuously enhanced its support for the real economy. Consumer prices exhibit a smaller overall increase, and there are no grounds for persistent inflation or deflation. Besides that, the CPI's year-on-year increase of above 5% at the beginning of 2020 was mainly due to the rapid rise in pork prices, added by the impact of the pandemic on supply, and therefore possessed both structural and time-specific characteristics. Meanwhile, monetary policy remained sound and the price increase has steadily dropped to below 3% since February. According to preliminary estimates, the average growth of the CPI in 2020 will fall into a reasonable range.

**Figure 1.5:** China's Quarterly Percentage Changes for GDP, CPI and Unemployment




**Source:** Fed Reserve Bank of ST. Louis/MPD Staff Calculation

### 1.2.2. The Economy of Turkey:

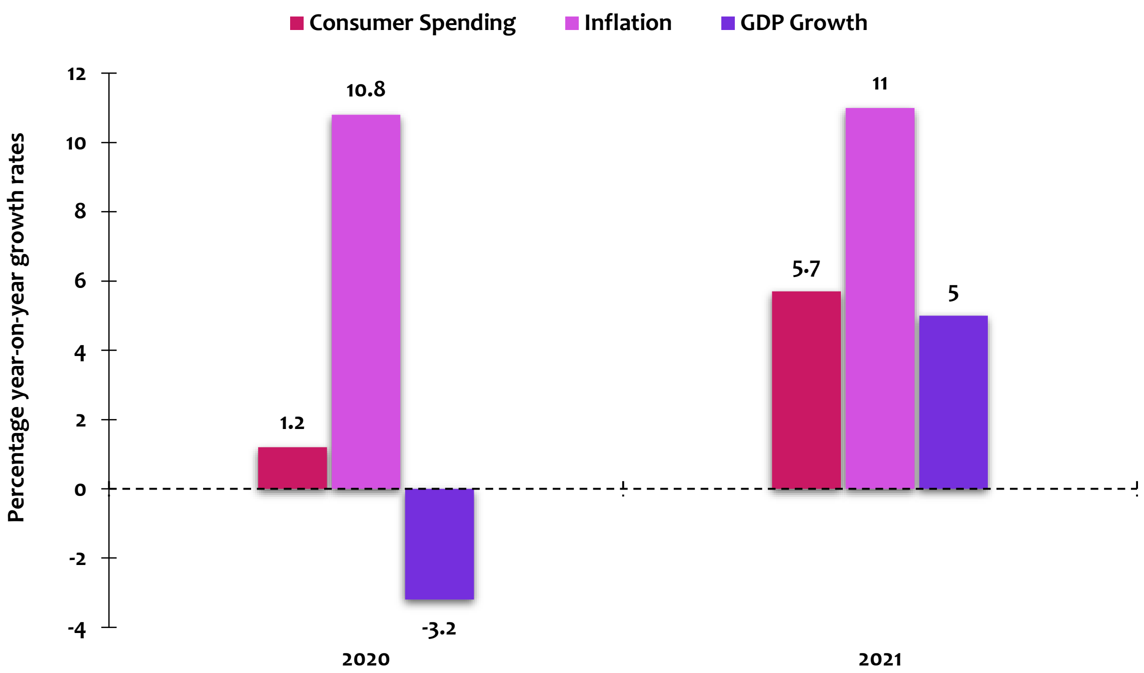
Consumer price index (CPI) increased by 11.77% annually and 0.86% monthly. Beside, a rise in general index was realized in CPI on the previous month by 0.86%, on December of the previous year by 7.29%, on same month of the previous year by 11.77% and on the twelve months moving averages basis by 11.27% in August 2020, while, the lowest annual increase was 2.44% in alcoholic beverages and tobacco and the highest monthly decrease was 2.11% in clothing and footwear.

The indicator for CPI having increased by 11.18% annually and 0.78% monthly. According to the general trade system exports decreased by 5.7%, while imports increased by 20.4% in August 2020. According to the Turkish Statistical Institute and the Ministry of Trade, in August 2020, exports were 12 billion and 464 million dollars with a 5.7% decrease and imports were 18 billion and 742 million dollars with a 20.4% increase compared with August 2019. Exports and imports decreased by 12.9% and 1.2% respectively in January-August 2020.

Moreover, the foreign trade deficit increased by 168.2% in August 2020 compared with August 2019. In August 2020, exports could cover 66.5% of imports, while it was 85.0% in August 2019. Foreign trade deficit increased by 69.9% in January-August 2020 compared with the same period of 2019. In the same time, exports/imports ratio was 75.6% while it was 85.8% in January-August 2019.

Furthermore, employment index including industry, construction, and trade-services sectors increased by 2.6% in the third quarter of 2020 compared with the same quarter of the previous year. When sub-sectors are examined; employment increased in industrial sector by 4.7%, in construction sector by 7.6%, and in trade-services sector by 0.3%. Similarly, employment index increased by 4.9% in the third quarter compared to the previous quarter. Going into more details; industrial sector increased by 4.3%, construction sector surged up by 9.3% and trade-services sector increased by 4.5%. Meanwhile, Gross wages-salaries index increased by 21.9% in the third quarter of 2020 compared with the previous quarter. The level of employment in was 22.5% in industries sector, 20.8% in construction sector and 21.6% in trade services sector, which are higher from the previous quarter.

**Figure 1.6:** Turkey's Annual GDP Growth, Inflation and Consumer Spending




**Source:** Fitch Ratings/MPD Staff Calculation

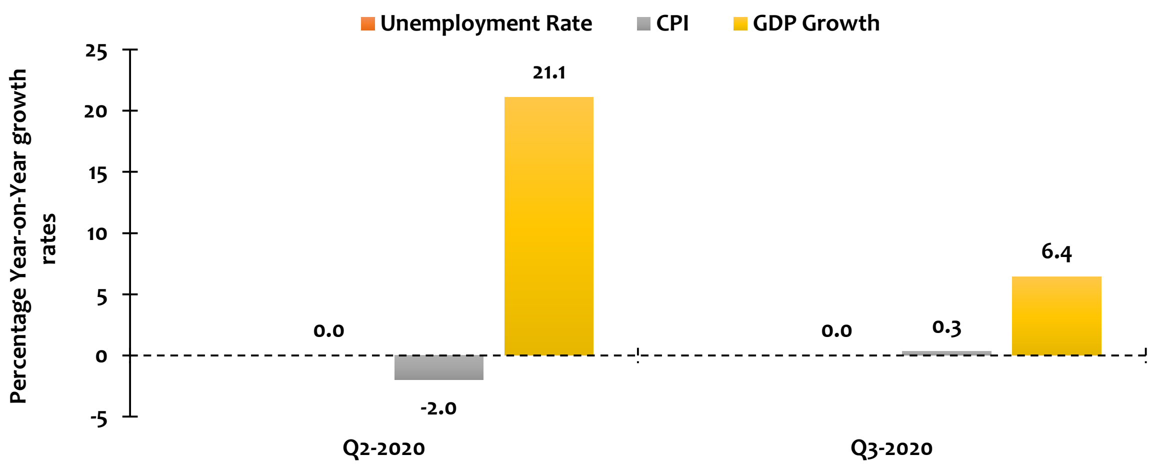
### 1.2.3. The Economy of India:

When global economic activity is besieged by the outbreak of the second wave of COVID-19, incoming data for the month of October 2020 have brightened the near-term outlook for the Indian economy and stirred up consumer and business confidence. The official release of the consumer price index (CPI) for October by the National Statistics Organization (NSO) is slated for November 12, 2020. Information on retail prices from the Ministry of Consumer Affairs, food and Public distribution indicates that pressures on food price that have persisted since the beginning of the financial year continued unabated in October.

These pressures have come from higher prices of cereals, tomato and sugar, which arises from transport barriers. In particular, prices of onions and potatoes which are sensitive to demand have stood at unrelentingly high levels during the month. On the other hand, cost-push pressures are likely to have been somewhat mitigated by the progressive easing of lockdowns, removal of restrictions on inter-state movements of goods and return of labor back to the cities. Besides that, Indicators of aggregate demand are still arriving in October stating that, electricity consumption increased by 11.5%, petrol and diesel also emerged out of contraction and posted growth rates of 4% and 6.6% respectively. Goods and services tax increased by 10.2% y-o-y which is the highest since the start of the financial year.

Moreover, according to the Centre for Monitoring the Indian Economy (CMIE), the unemployment rate in urban areas has receded almost continuously from a high rate of 23.5% in April 2020 to 7% in October. In addition, in the rural sector, employment demanded by households under Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) expanded by 91.3% in October, indicating that people are quickly restoring lost livelihood. Furthermore, India's merchandise trade released by the Ministry of Commerce and Industry reveals that exports declined by 5.4% y-o-y standing at USD 24.8 billion, against an acceleration of 6.0% in the previous month indicating that trade deficit widened to US $ 8.8 billion in October 2020, the highest in the current financial year.

**Figure 1.7:** India's Annual GDP Growth, Inflation and Industrial Production




**Source:** Bloomberg/MPD Staff Calculation

**Sources:**

| | |
|---|---|
| International Monetary Fund | www.imf.org |
| World Bank | www.worldbank.org |
| Bloomberg | www.bloomberg.com |
| Federal Reserve Bank of ST. Louis | www.fred.stlouisfed.org |
| National Bureau of Statistics of China, People's Republic of China | www.stats.gov.cn |
| Ministry of finance Department of Economic Affairs India | www.dea.gov.in |
| Turkish Statistical Institute | www.turkstat.gov.tr |
| Organization for Economic co-operation and Development | www.oecd.org |
| Bureau of Labor Statistics, U.S. Department of Labor, U.S.A. | www.bls.gov |
| Office for National Statistics, U.K. | www.ons.gov.uk |
| Cabinet Office, Government of Japan | www.esri.cao.go.jp |
| Global Economic Outlook/Fitch Ratings | www.fitchratings.com |

# 2

# Monetary and Capital Market Development

# 2

# MONETARY AND CAPITAL MARKET DEVELOPMENT

Based on the monetary and financial statistics of DAB, reserve money (RM) had slightly positive growth by 1.82% at the end of the third quarter and it had growth by 0.68% at the end of the same period in previous year.

Currency in circulation (CiC) as a major component of RM, had positive growth of 9.29% from the beginning of FY 1399 (2020) to the end of the third quarter. Reserve money (RM) growth, remained well below the target due to collecting additional liquidity from the market and banks during the period under review.

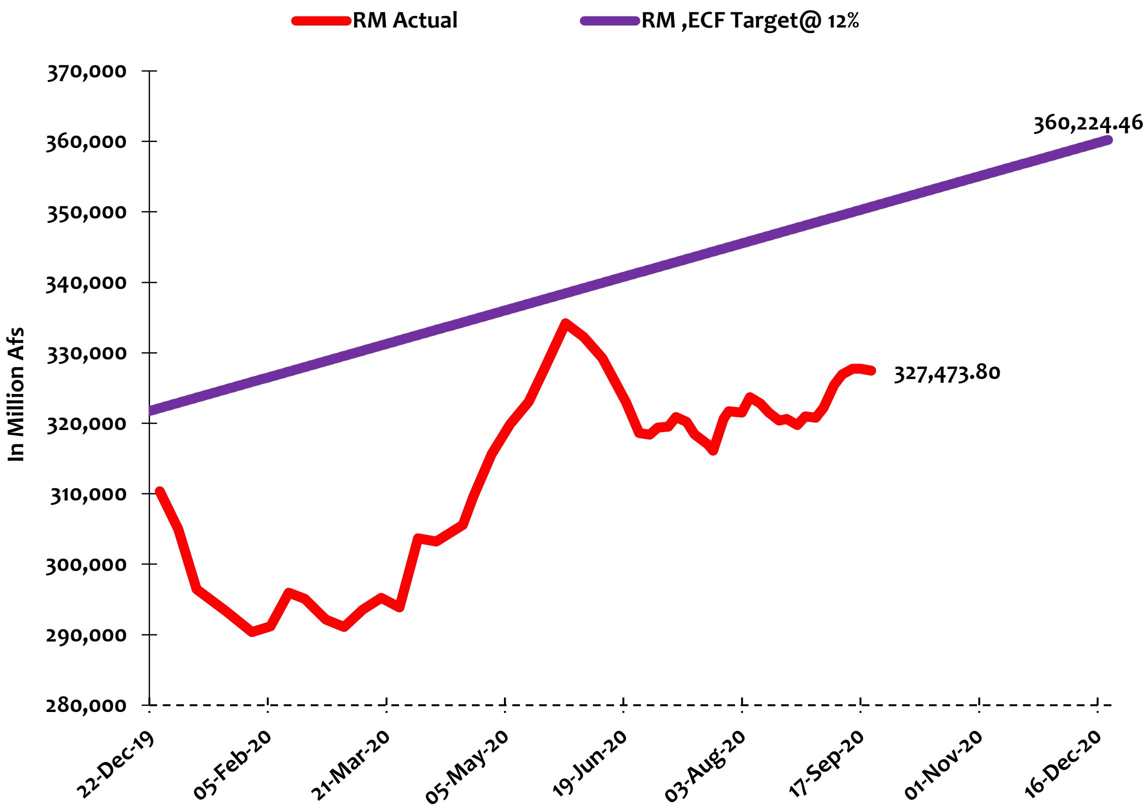
Narrow money (M1), stood at Afs 514,003 million at the end of the third quarter, registering a growth of 14%. Broad money (M2) demonstrated a growth rate of 12.24%, standing at Afs 546,475.01 million, due to decline in revenue collection and high government expenditures. In order to mitigate excessive fluctuations of Afghani exchange rate against foreign currencies and manage liquidity in the market, DAB uses FX and CNs auctions under the open market operations.

During the first three quarter of FY 1399 (2020), DAB has auctioned a total amount of USD 1512.31 million to absorb the excess liquidity from the market and as well as to smoothen sharp fluctuations in the exchange rate of Afghani against foreign currencies. the total outstanding amount of CNs stood at Afs 39.59 billion at the end of period under review. Meanwhile, Afghani appreciated by 2.07% against the US dollar during the period under review.

## 2.1. Monetary Program:

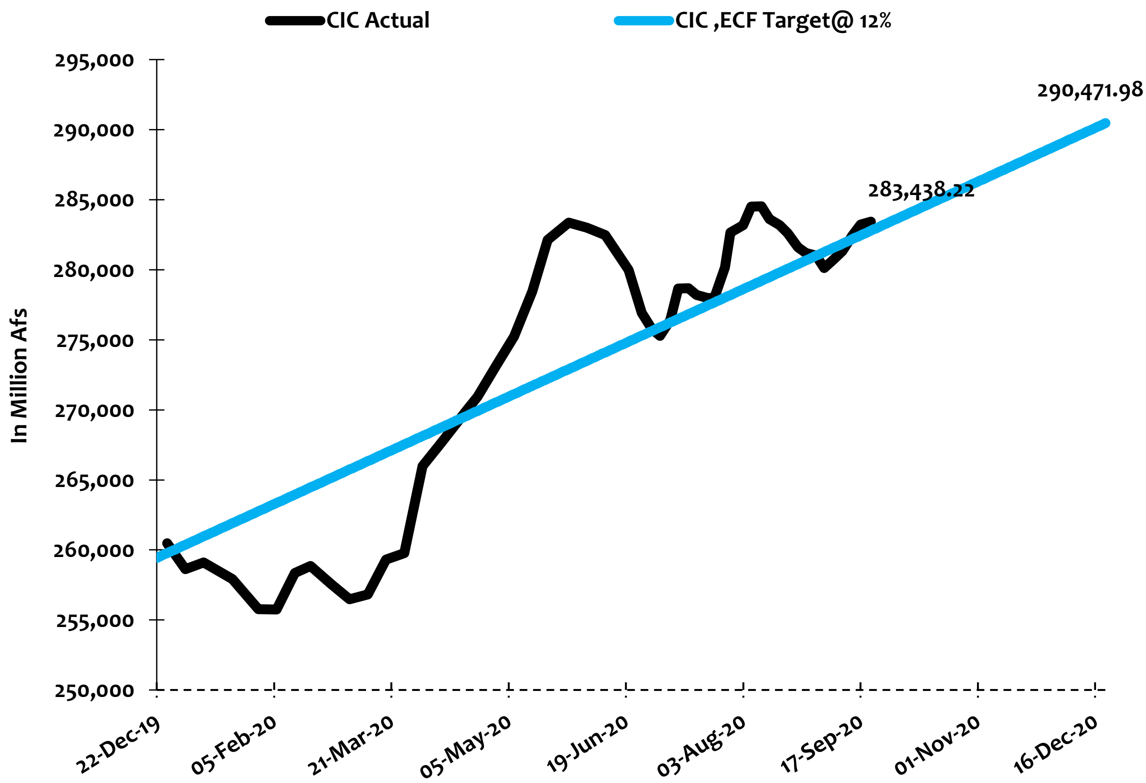
Reserve money is the operational target, while currency in circulation remained as indicative target. DAB applies quantitative theory of money to determine the amount of reserve money (RM) for the purpose of maintaining domestic price stability, which is DAB's primary objective. Hence, targets for RM and CiC are based on expected economic growth and expected inflation during the concerned period. For the fiscal year 1399 (2020), the ceilings for reserve money and currency in circulation growth is 12%.

**Figure 2.1:** Reserve Money during the first three quarters of FY 1399 (2020)




**Source:** Monetary Policy Department/DAB

**Figure 2.2:** Currency in Circulation during the first three quarters of FY 1399 (2020)



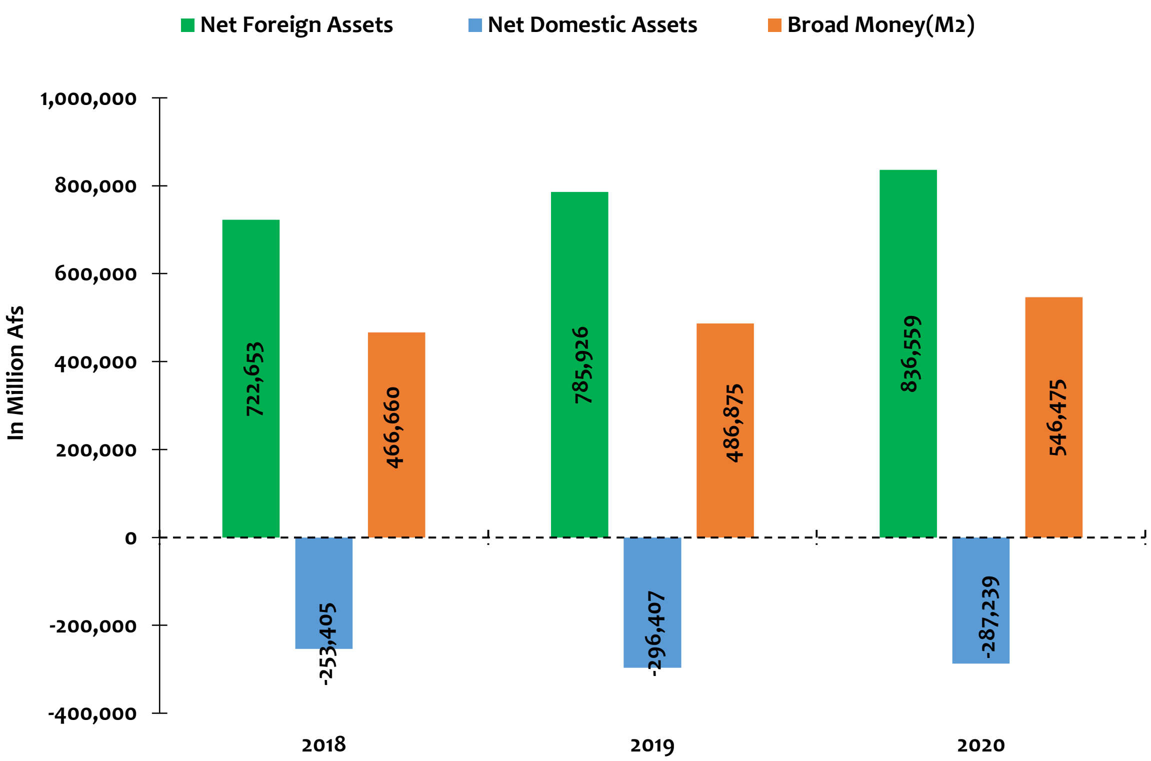

**Source:** Monetary Policy Department/DAB

## 2.2. Monetary Aggregates:

Narrow money and broad money are compiled based on Monetary and Financial Statistics Manual and Compilation Guide (MFS Guide). Narrow money (M1) includes currency outside depository corporations and demand deposits, while broad money (M2) includes narrow money components and other less liquid assets or quasi money. As shown in table 2.3, narrow money (M1) grew by 14% at the end of the third quarter of fiscal year 1399 (2020), almost higher than the growth in the same period of FY 1398 (2019).

Currency outside depository corporations, which accounts for 50% of M2, grew by 14.71%, higher than 9.7% growth of the same period in the previous year, showing difference of Afs 34,811.83 million.[6] Demand deposits, which are other components of M1, experienced 12.22% growth at the end of the third quarter of FY 1399 (2020), while its growth rate was 0.8% in the same period of previous year. Most projects implemented after pandemic period increased demand deposits in foreign currency automatically. Demand deposit in comparison with the previous year in same quarter shows a difference of Afs 26,402.88 million.

**Figure 2.3:** Net Foreign Assets, Net Domestic Assets, and M2 for the first three quarters of FY 1399




**Source:** Monetary Policy Department/DAB

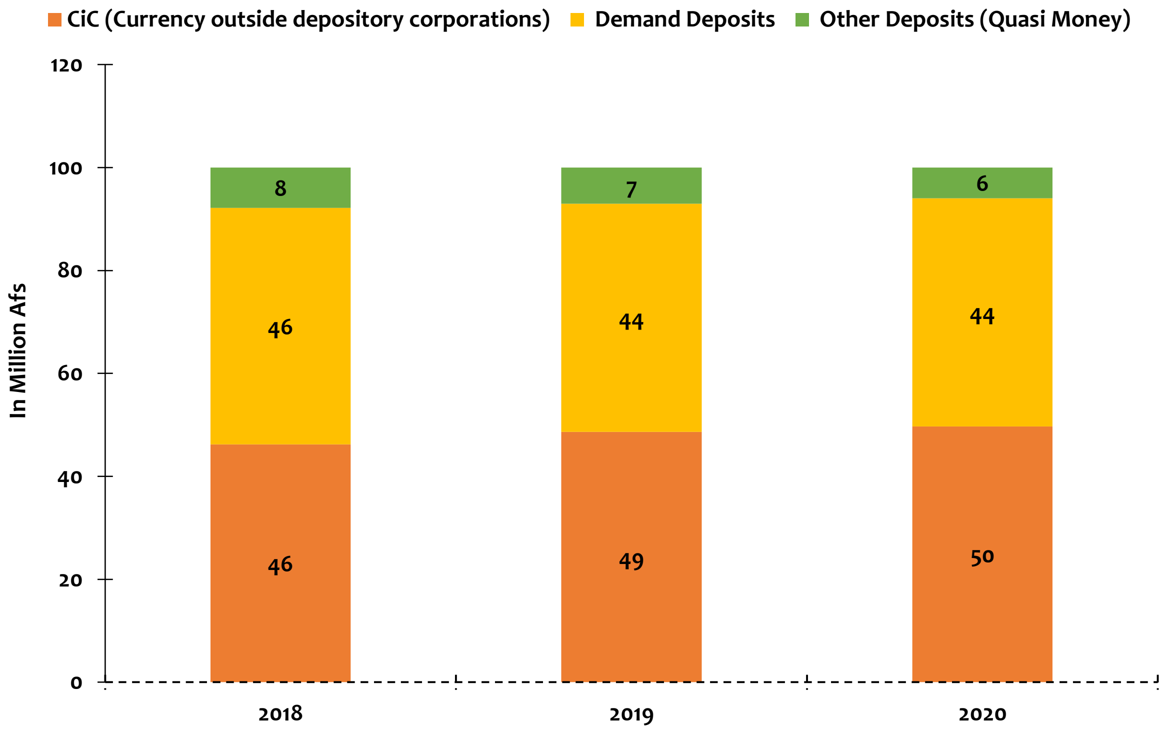
Broad money (M2) expanded by Afs 546,475.01 million in the period under review from Afs 483, 875.5 million in the previous year, showing an increase of 12.24%, greater than 4.3% growth of the same period in the previous year, due to the reasons already discussed in the previous

6 this increase in expenditure was financed by grants not from revenue collection

paragraph. The data show that M1 with a share of 94.06% remained main contributing component of M2. Quasi money (other deposits), which is other component of M2, had negative growth of 4.74% at the end of the period under review. This decline is because of low investment and economic activities during quarantine.

Quasi money constitutes 5.94% of broad money in the period under review, which is lower than 7% in the same period of the previous year. Therefore, the impact of changes in quasi money on M2 is negligible. The year-on-year quarterly change of Afghani denominated time deposits stood at Afs 8,820.48 million, showing a negative growth of 4.46%, while the foreign currency denominated time deposits negatively rose by 4.84%, reaching to Afs 412.21 million. Afghani-denominated time deposits and foreign currencies denominated time deposits constituted 1.61% and 4.33% of M2 respectively. Demand deposits as a share of broad money stood at 44.38% at the end of the third quarter of the year under review (Figure 2.4).

**Figure 2.4:** Quasi Money and Demand Deposits during the first three quarters of FY 1399




**Source:** Monetary Policy Department/DAB

**Table 2.1:** Monetary Aggregates in the first three quarters of FY 1399

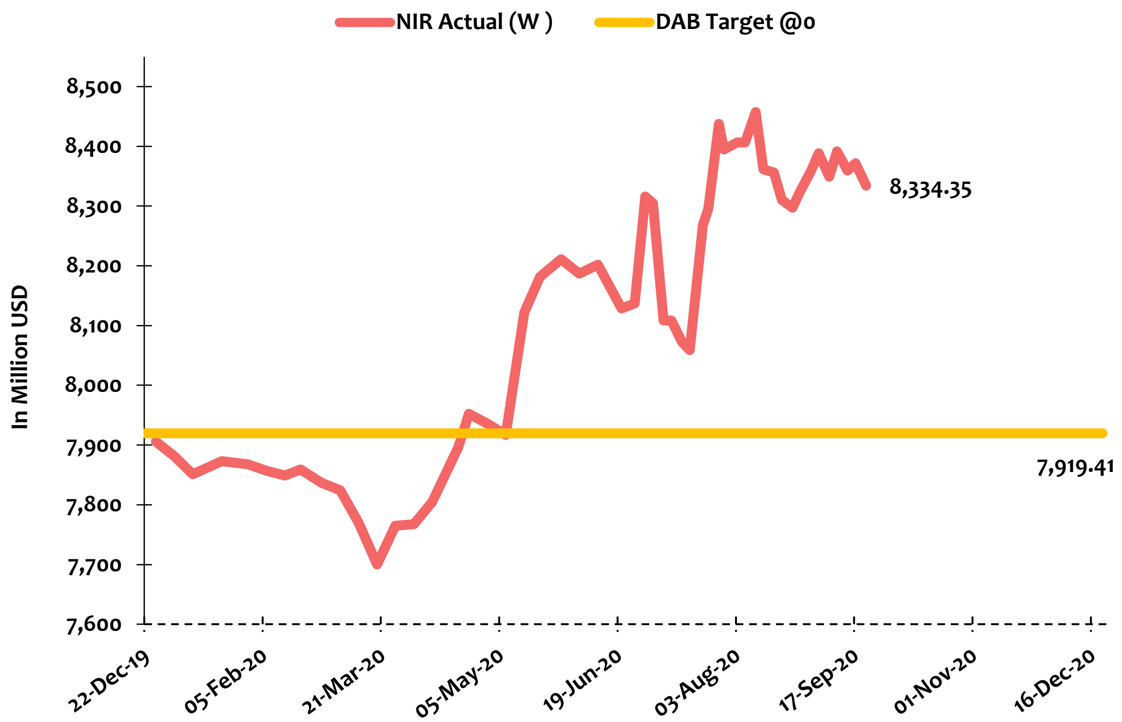
| In Million Afs | Sep-18 (Q3) Amount | Sep-19 (Q3) Amount | Y-o-Y Δ | Difference | Sep-20 (Q3) Amount | Y-o-Y Δ | Difference |
|---|---|---|---|---|---|---|---|
| | | | | | | | |
| **1- Net Foreign Assets** | **722,653.50** | **785,925.73** | **8.8%** | **63,272** | **836,558.65** | **6.44%** | **50,633** |
| (a) Foreign Assets | 736,722 | 796,332 | 8.1% | 59,610 | 846,452 | 6.29% | 50,120 |
| DAB Foreign exchange reserves | 610,646 | 665,818 | 9.0% | 55,171 | 714,983 | 7.38% | 49,165 |
| Gold | 64,078 | 82,580 | 28.9% | 18,502 | 102,988 | 24.71% | 20,408 |
| Other | 546,568 | 583,238 | 6.7% | 36,669 | 611,995 | 4.93% | 28,757 |
| Other foreign assets | 126,076 | 130,515 | 3.5% | 4,439 | 131,469 | 0.73% | 954 |
| (b) Foreign Liabilities | 14,069 | 10,407 | -26.0% | -3,662 | 9,893 | -4.93% | -513 |
| **2. Net Domestic Assets** | **-253,404.66** | **-296,407.27** | **17.0%** | **-43,003** | **-287,238.76** | **-3.09%** | **9,169** |
| (a) Net Domestic Credit | -85,849 | -94,061 | 9.6% | -8,211 | -81,871 | -12.96% | 12,190 |
| Net Credit to Nonfinancial Public Sector | -134,258 | -141,932 | 5.7% | -7,674 | -129,870 | -8.50% | 12,062 |
| Net Credit to Central Government | -134,353 | -142,026 | 5.7% | -7,674 | -130,156 | -8.36% | 11,871 |
| Credit to Central Government | 10,918 | 7,185 | -34.2% | -3,733 | 181 | -97.49% | -7,004 |
| Liabilities to Central Government | 145,271 | 149,211 | 2.7% | 3,941 | 130,336 | -12.65% | -18,875 |
| Net Credit to State & Local Government | 0.000 | 0.000 | 0.0% | 0 | 0.000 | 0.00% | 0 |
| Net Credit to Public Nonfinancial Corporations | 94 | 94 | 0.0% | 0 | 286 | 202.49% | 191 |
| Credit to Private Sector | 49,506 | 48,434 | -2.2% | -1,072 | 48,398 | -0.07% | -36 |
| Net Credit to Other Financial Corporations | -1,098 | -563 | -48.7% | 535 | -399 | -29.19% | 164 |
| (b) Capital Accounts | 191,747 | 223,770 | 16.7% | 32,023 | 224,379 | 0.27% | 609 |
| (c)Other Items Net | 24,192 | 21,423 | -11.4% | -2,769 | 19,011 | -11.26% | -2,412 |
| **3- Broad Money(M2)** | **466,660.09** | **486,875.50** | **4.3%** | **20,215** | **546,475.01** | **12.24%** | **59,600** |
| Narrow Money(M1) | 430,049 | 452,788 | 5% | 22,739 | 514,003 | 14% | 61,215 |
| CiC (Currency outside depository corporations) | 215,703 | 236,691 | 9.7% | 20,988 | 271,503 | 14.71% | 34,812 |
| Demand Deposits | 214,346 | 216,097 | 0.8% | 1,751 | 242,500 | 12.22% | 26,403 |
| Other Deposits (Quasi Money) | 36,611.40 | 34,087.57 | -6.9% | -2,524 | 32,472.37 | -4.74% | -1,615 |
| In Afghani | 12,308 | 9,233 | -25.0% | -3,075 | 8,820 | -4.46% | -412 |
| In Foreign currency | 24,304 | 24,855 | 2.3% | 551 | 23,652 | -4.84% | -1,203 |
| Securities Other Than Shares | 0.00 | 0.00 | 0.0% | 0 | 0.00 | 0.00% | 0 |

**Source:** Monetary Policy Department/DAB

## 2.3. Net International Reserve (NIR):

Da Afghanistan Bank holds international reserves, which consists of monetary gold, reserve position and holdings of Special Drawing Rights (SDR) with the IMF, as well as major foreign exchange such as US dollars, Euro, Great British Pound and other currencies. The Net International Reserves (NIR) of Afghanistan, which expressed in terms of US dollar, is defined as reserve assets minus reserve liabilities. NIR increased by 5.2% and had Accumulation of USD 414.94 million at the end of the third quarter of FY 1399 (2020). NIR target was set at USD 7,919.41 million, while in actual case, NIR in ECF market rate compiled weekly, reached to USD 8,334.35 million for the mentioned period under review.

**Figure 2.5**: Actual and target NIR during the first three quarters of FY 1399



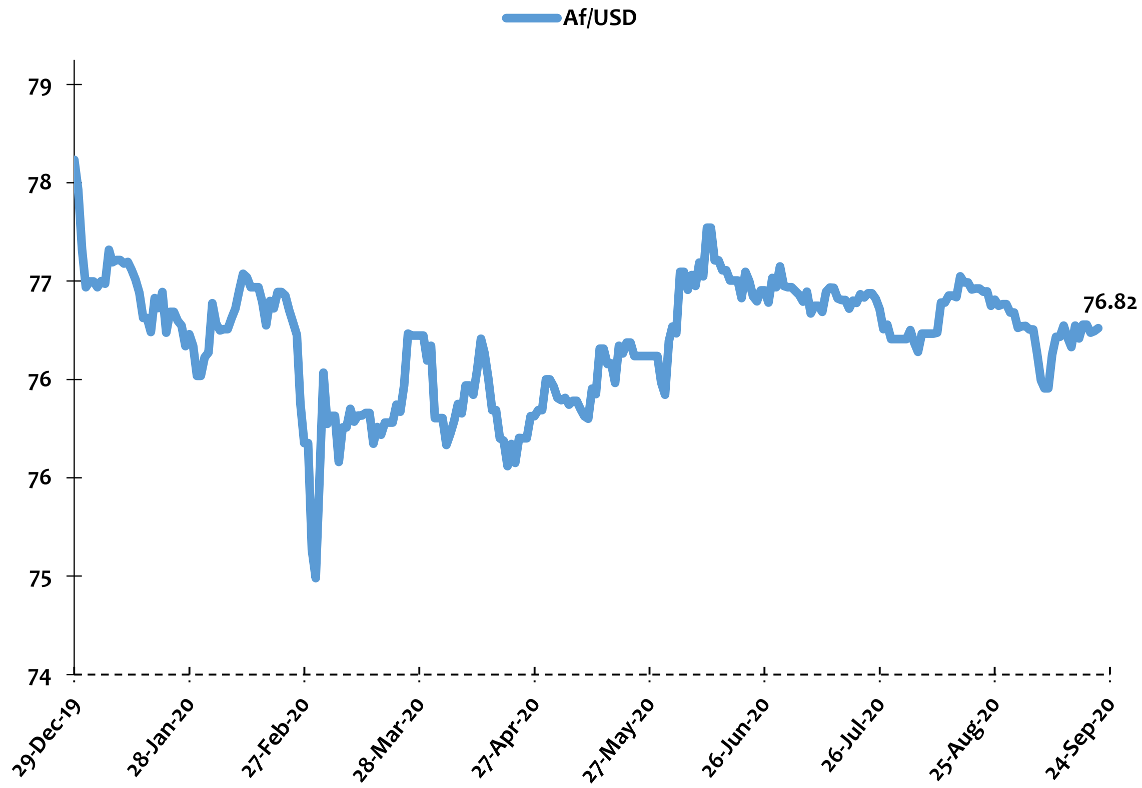

**Source:** Monetary Sector, Monetary Policy Department/ DAB

## 2.4. Foreign Exchange Market

### 2.4.1. Foreign Exchange Rates

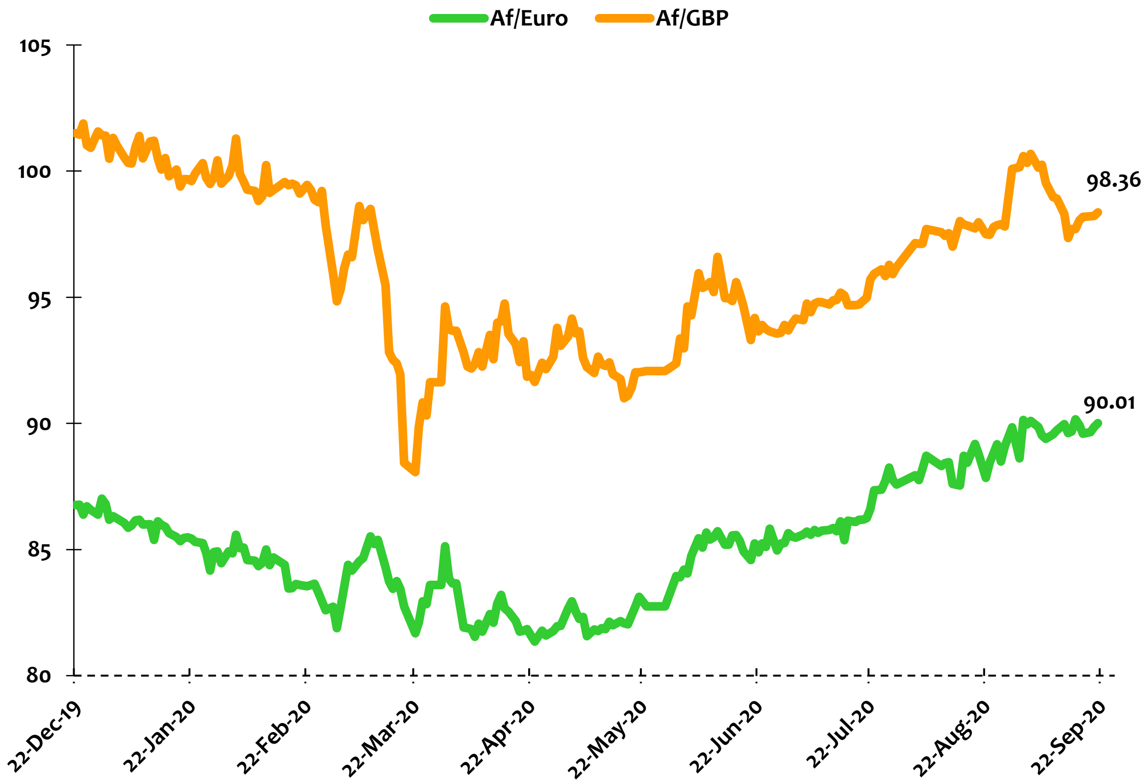
Da Afghanistan Bank's (DAB) ultimate goal is to maintain price stability. In order to achieve and maintain this goal, DAB puts its focus to utilize its monetary instruments via the open market operations, effectively with sound policy implementation. During the first three quarters of FY 1399 (2020), Afghani relatively depreciated against the Euro and Swiss France, but appreciated against Indian rupee, Pakistani Rupee, Chinese Yuan, Iranian Toman, United States Dollar, United Arab Emirates dirham, British Pound and Saudi Riyal. The daily historic review of the average exchange rate of Afghani against the U.S. dollars and other foreign currencies during the first three quarters of FY 1399 (2020) are shown in below figures:

**Figure 2.6:** Daily average ex- rate of Afghani against USD during the first three quarters of FY 1399



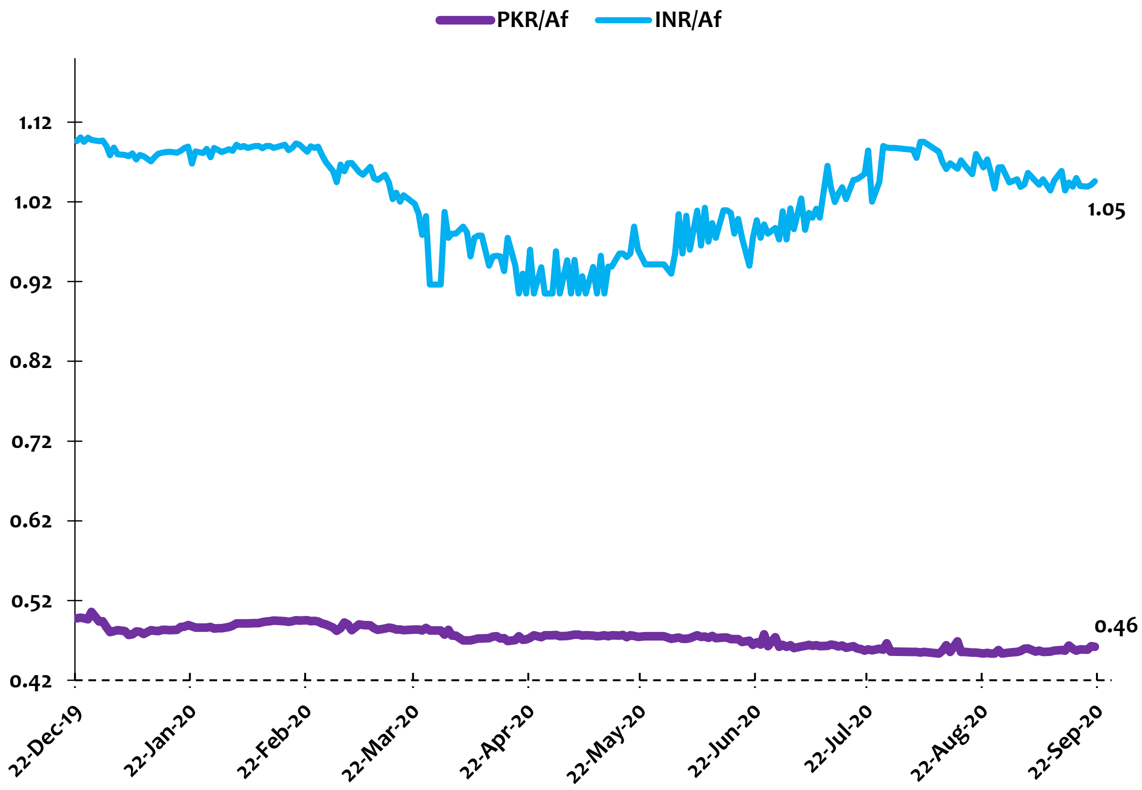

**Source:** Monetary Sector, Monetary Policy Department/ DAB

**Figure 2.7:** Daily average ex- rate of Afghani against GBP and Euro during the first three quarters of FY 1399



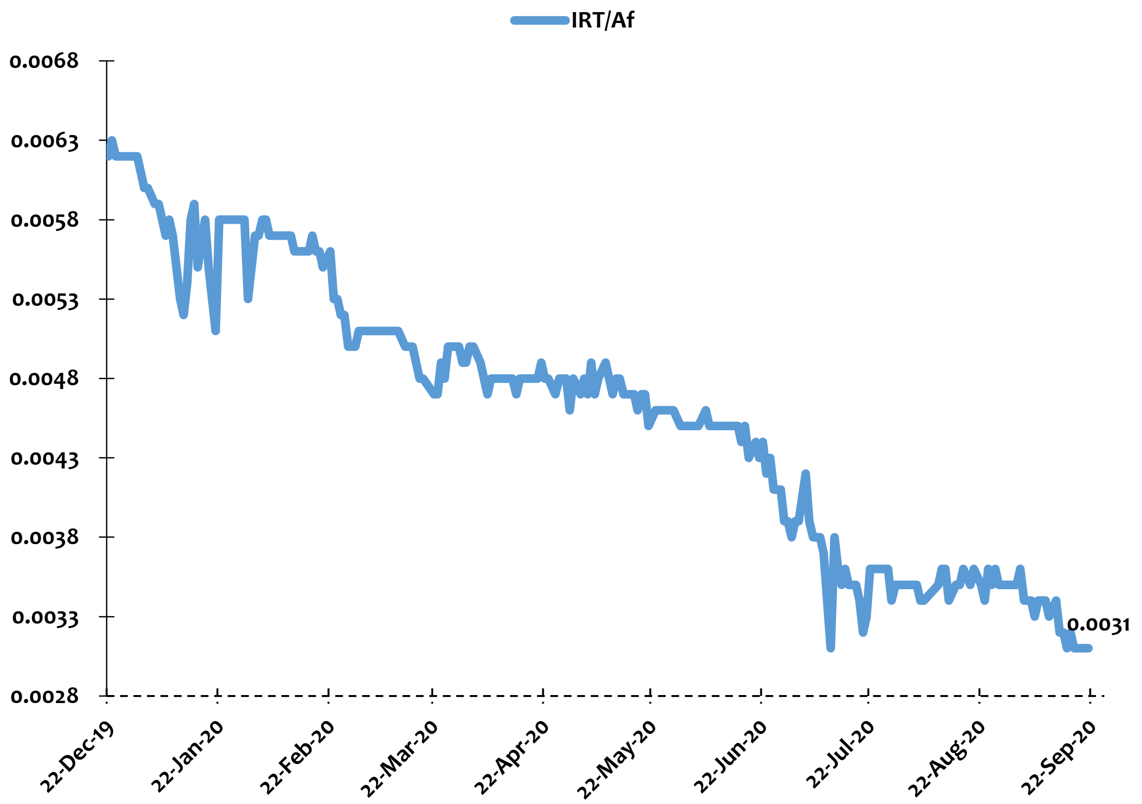

**Source:** Monetary Sector, Monetary Policy Department/ DAB

**Figure 2.8:** Daily avarage ex-rate of Afghani against INR and PKR during the third quarter of FY 1399




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

**Figure 2.9:** Dailly average ex- rate of Afghani against IRT during the first three quarters of FY 1399




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

### 2.4.2. Foreign Exchange Auction

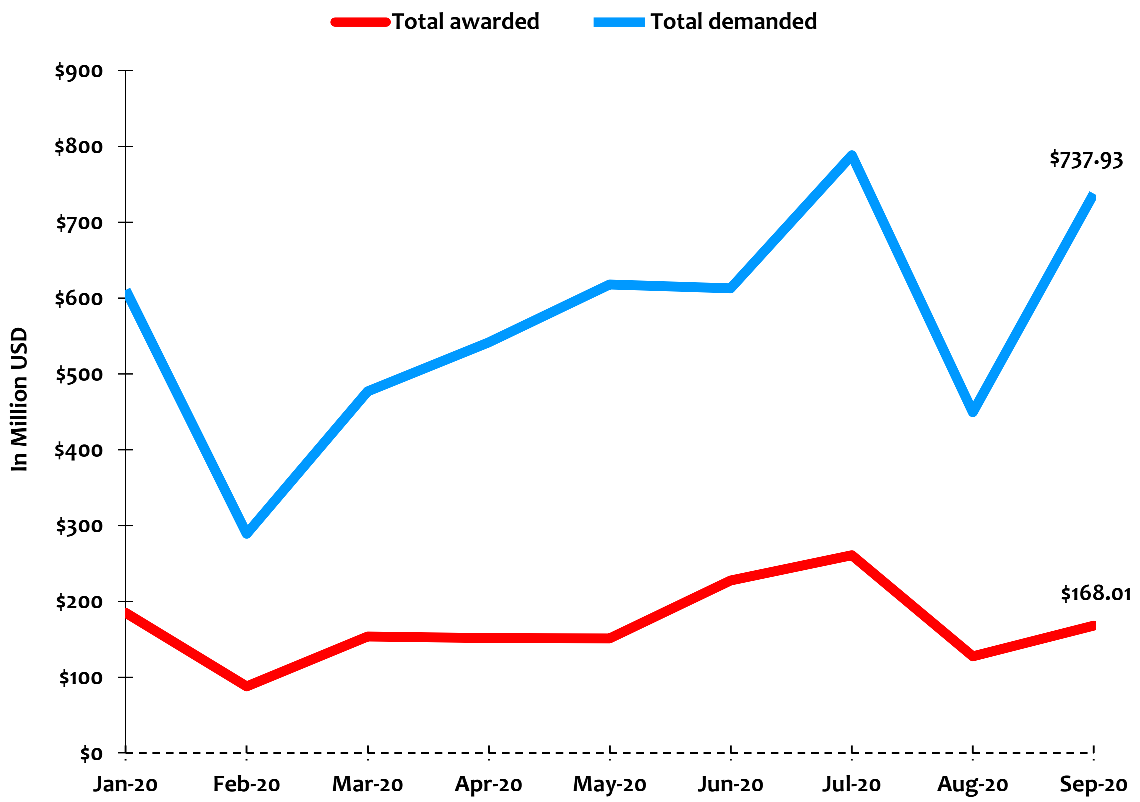
In order to control the money supply and maintain price stability in domestic market, DAB manages the reserve money growth by conducting FX (USD) auctions three times a week and a weekly capital notes auctions. DAB continued the FX auction to mop up excess liquidity from the market and to smoothen excessive volatility of the exchange rate of Afghani against foreign currencies, especially the US dollar.

During the first three quarters of FY 1399 (2020), DAB auctioned a total amount of USD 1512.31 million, while the total demand was USD 5,124.59 million. On average 55.27 bidders participated in each auction and 40 bids were announced as the winning bids with the average amount of USD 13.60 million sold in each auction and the total withdrawal is recorded Afs 73.31 billion.

The data during the first three quarters of FY 1398 (2019) recorded a total auctioned amount of USD 1,781.28 million, with a total demand of USD 4,193.21 million. On average, 56 bidders participated in each auction and 40 bids were awarded with an average amount of USD 16.64 million in each auction and the total withdrawal is recorded Afs 138.43 billion.

According to the approval of DAB executive board members on 6th March, 2020, DAB started selling US dollar to Da Afghanistan Brishna Sherkat (DABS) through commercial banks. The total amount sold to DABS was USD 182 million during the first three quarters of the period under review.

**Figure 2.10:** US Dollar awarded and demanded amount during the first three quarters of FY 1399




**Source:** Monetary Policy Department/DAB

## 2.5. Capital Market &Liquidity Conditions

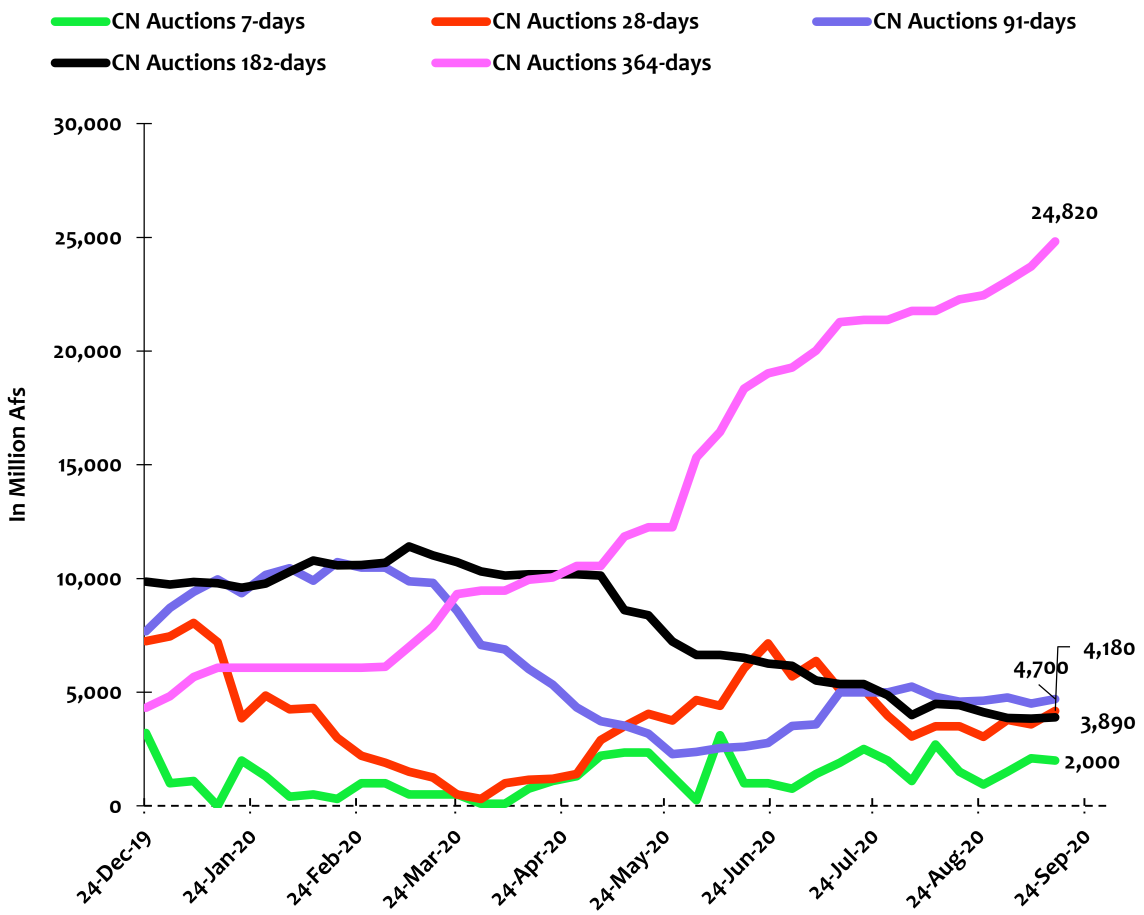
### 2.5.1. Capital Notes Auction

Capital notes are Afghani denominated short–term securities offered by DAB to licensed commercial banks on weekly basis. Da Afghanistan Bank uses Capital Notes (CNs) as a monetary tool to manage the money supply growth and absorb the excess liquidity of the commercial banks. Currently, DAB offers capital notes with the maturities of one week, one month, three months, six months and one year.

Total outstanding stock of capital notes reached Afs 39.59 billion at the end of the third quarter of FY 1399 (2020), which shows an increase of Afs 15.67 billion compared to Afs 23.92 billion at the end of the same period of FY 1398 (2019). The main reason for the increase in outstanding compared to the same period of last year is the higher CNs sales.

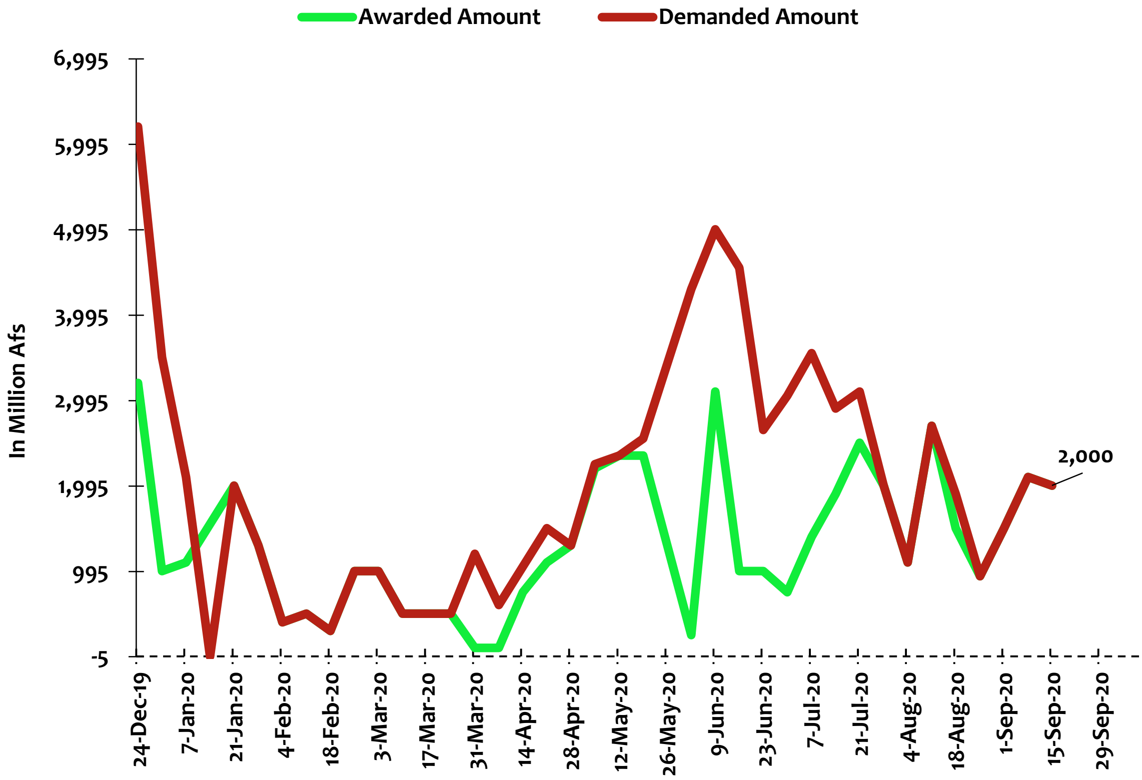
The outstanding stock of 7-days, 28-days, 91-days, 182-days and 364-days capital notes stood at Afs 2 billion, Afs 4.18 billion, Afs 4.7 billion, Afs 3.89 billion and Afs 24.82 billion. Total interest paid to CNs is Afs 151.09 million till the end of the period under review. In addition, the weighted average interest rate for 7-days, 28-days, 91-days, 182-days and 364-days capital note were 0.62%, 0.96%, 1.49%, 1.75 % and 3 % from the beginning to the end of the third quarter of FY 1399 (2020).

**Figure 2.11:** Stock of outstanding Capital Notes during the first three quarters of FY 1399



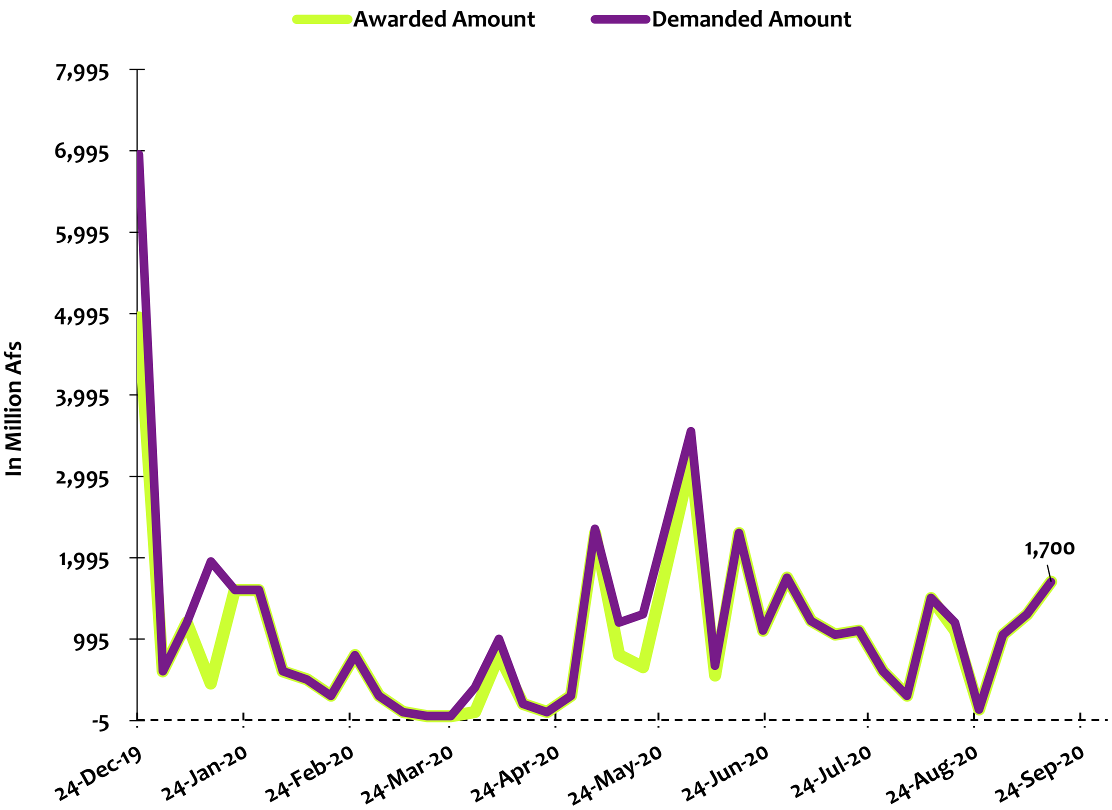

**Source:** Monetary Sector, Monetary Policy Department/ DAB

**Figure 2.12:** 7-days CNs demanded and awarded amount during the first three quarters of FY 1399



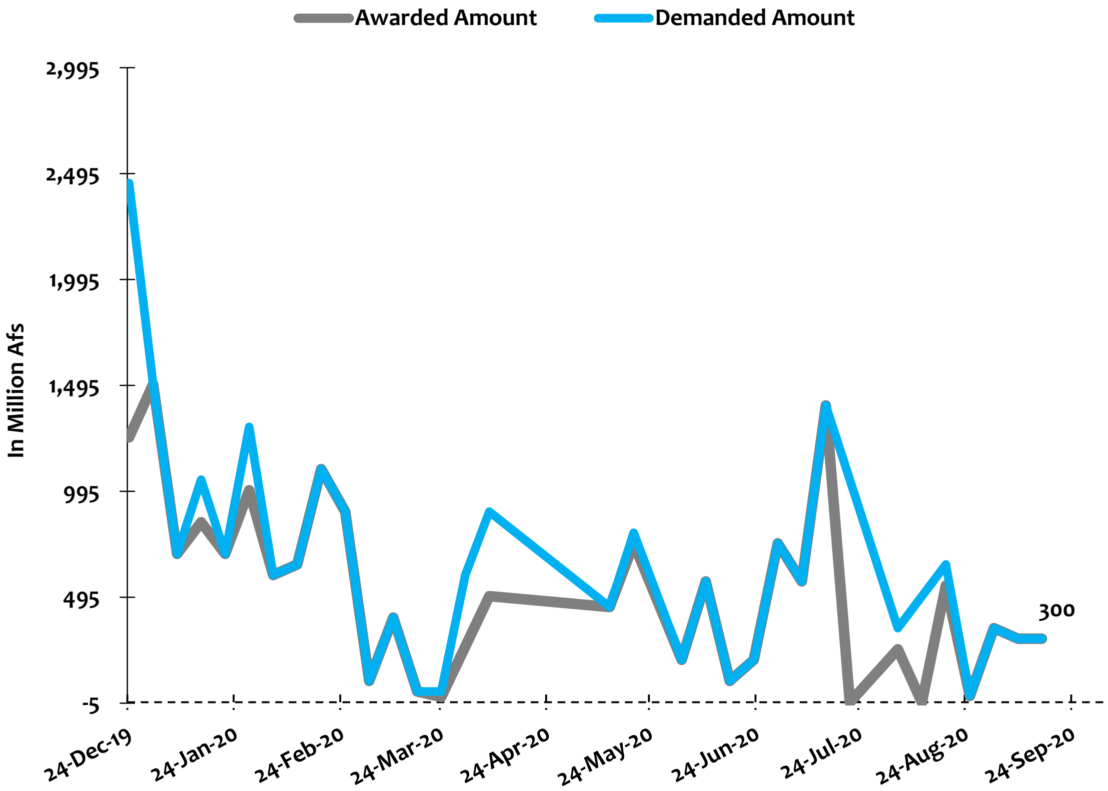

**Source:** Monetary Sector, Monetary Policy Department/ DAB

**Figure 2.13:** 28-days CNs demanded and awarded amount during the first three quarters of FY 1399



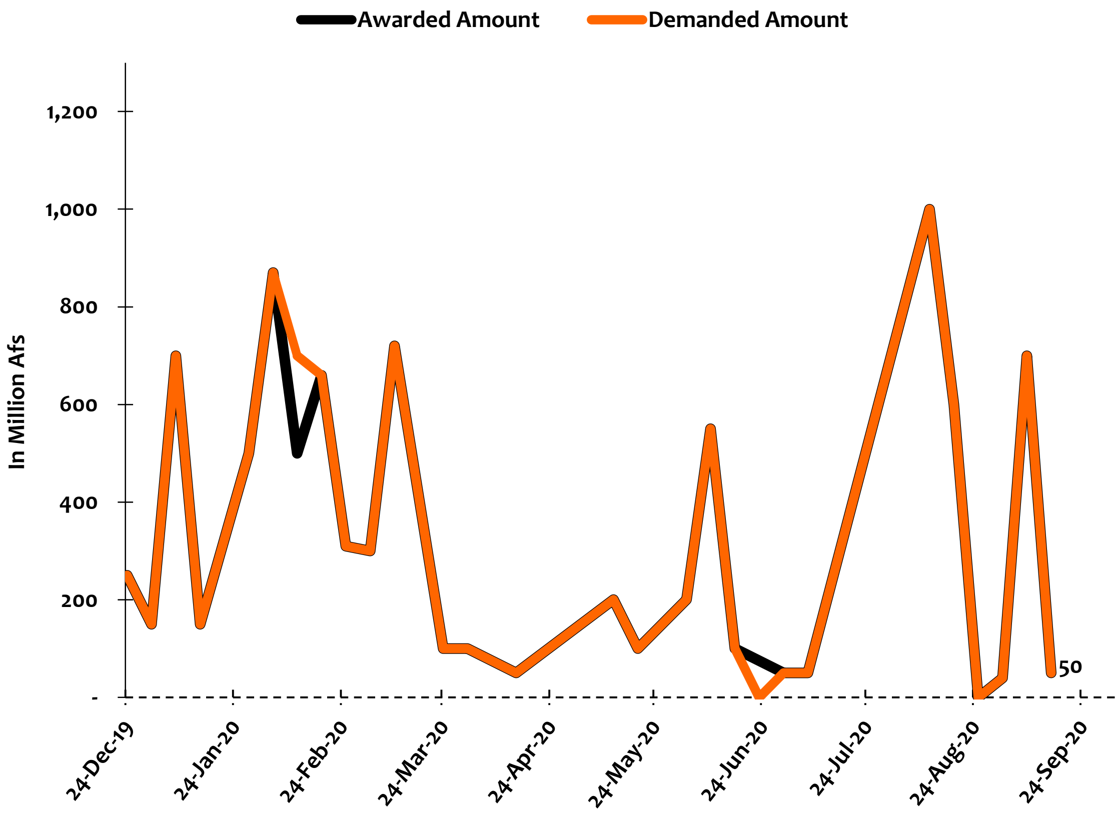

**Source:** Monetary Sector, Monetary Policy Department/ DAB

**Figure 2.14:** 91-days CNs demanded and awarded amount during the first three quarters of FY 1399



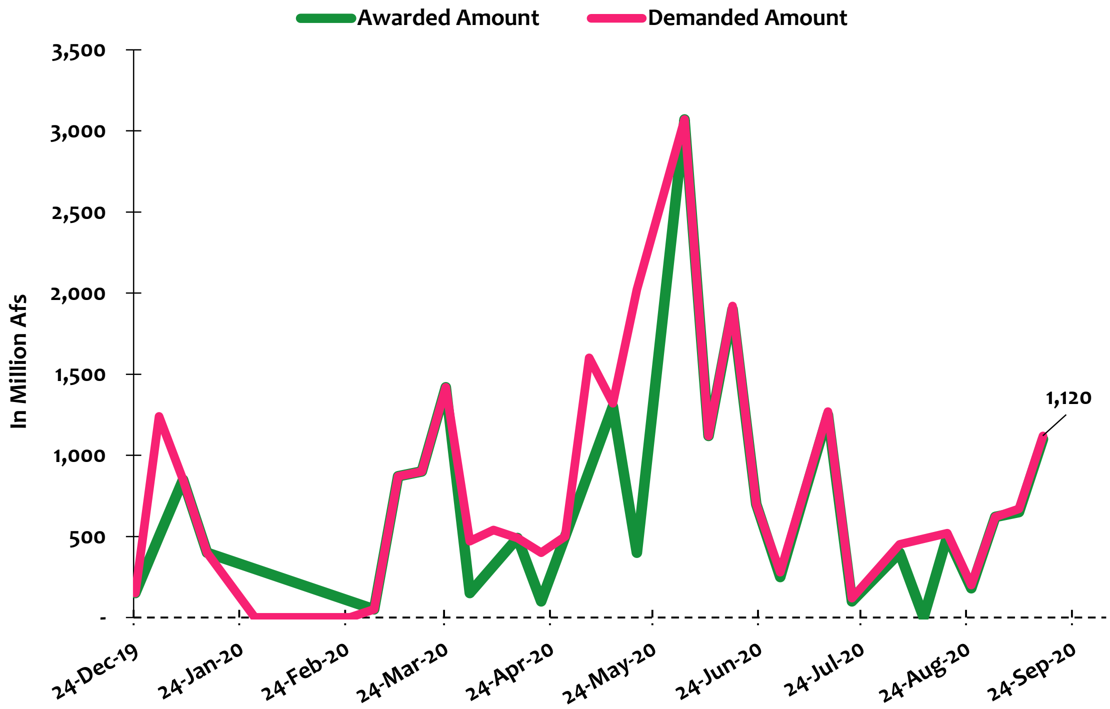

**Source:** Monetary Sector, Monetary Policy Department/ DAB

**Figure 2.15:** 182-days CNs demanded and awarded amount during the first three quarters of FY 1399




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

**Figure 2.16:** 364 -days CNs demanded and awarded amount during first three quarters of FY 1399




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

## 2.5.2. Required and Excess Reserves

Commercial banks are required to hold 8% of their total deposits as obligatory reserves with DAB for their Afghani denominated accounts and 10% for foreign currency denominated accounts. Now the required reserves are held in the currency of denomination (Domestic and foreign), unlike the previous practice, in which required reserves for all deposits were maintained in domestic currency. No interest is given for such deposits to commercial banks. It shows Afs 6,914.36 million, USD 221.49 million and Euro 13.69 million recorded at the end of period under review.

### Overnight Deposit Facility (ODF)

This facility is available to all commercial banks to gain interest on their excess balances. The interest rate on the overnight deposit facility, based on a circular to all banks, approved by DAB Supreme Council on September 11, 2017, is now 10 basis points. The outstanding amount of overnight deposit facility stood at Afs 7,959.59 million at the end of the third quarter of FY 1399 (2020) and the payment of interest rate to the mentioned facility reached to Afs 5.3 million for the same period.

### Overnight Credit Facility (OCF)

This facility is used by banks for short term cash needs. The facility allows banks to borrow Afghani from Central Bank on an overnight basis when they face a shortfall in cash flow. The rate that the commercial banks are charged for this facility is 3.5% above the last 28-days CNs auction interest rate. This borrowing is collateralized with outstanding capital notes only. During the period under review, no bank has used from the credit facility.

# 3

# Inflation Trend and Outlook

# 3

# INFLAITON TREND AND OUTLOOK

## 3.1. Global Commodity Review

### 3.1.1. Executive Summary

Almost all commodity prices recovered in the third quarter of FY 2020 following steep declines earlier in the year due to the COVID-19 pandemic. Crude oil prices have doubled since their April low, supported by sharp oil supply cuts by OPEC+, but prices remain one-third lower than their pre-pandemic levels. Metal prices recovered rapidly in response to a faster-than-expected pick up in China's industrial activity. Some food prices have also risen due to production shortfalls in edible oils. Looking ahead, oil prices are expected to increase very gradually from current levels and average $44/bbl in FY 2021, up from an estimated $41/bbl in FY 2020, as a slow recovery in demand is matched by an easing in supply restrictions.

Metal and agricultural prices are projected to see modest gains of 2% and 1%, respectively, in FY 2021. The main risk to the price forecasts is the duration of the pandemic, including the risk of an increasing second wave in the Northern Hemisphere and the speed at which a vaccine is developed and distributed. The COVID-19 pandemic is a shock to global commodity markets that presents a challenge to policy makers in commodity exporters to the extent that it is short-lived, policy stimulus can buffer its impact; to the extent that it is lasting, policy makers need to allow their economies to adjust smoothly to a new normal.

Identifying the duration of commodity price shocks is a challenge that frequently confronts policy makers and commodity exporters, as documented in a Special Focus section. The Focus finds that industrial commodity markets are mainly buffeted by transitory shocks, whereas agricultural commodity markets are chiefly subject to permanent shocks.

### 3.1.2. Recent Trends

The COVID-19 pandemic has delivered a significant shock to commodity markets but its impact has varied in magnitude for different types of commodities. This contrasts with the previous global recession in 2008-09, when almost all commodity prices saw large, and persistent, declines. Energy prices rebounded by one-third in FY 2020-Q3 following their steep fall in FY 2020-Q2, but remain nearly one-third below their pre-pandemic levels. Crude oil prices drove the recovery, almost doubling to an average of $41/bbl in September from their low of $21/bbl in April. The recovery in prices was driven by a sharp reduction in production, particularly among OPEC+. Compared to the fall in oil prices during the global financial crisis, the most recent decline was a little steeper but also saw a faster recovery. However, the recovery in prices stalled in September amid renewed outbreaks of COVID-19.

Natural gas prices also rose sharply in FY 2020-Q3, while coal prices were broadly stable. Non-energy prices rose by 10% in FY 2020-Q3, with increases in almost all commodities. The metals and minerals price index rose 20% (q/q) and most metal prices are above their pre pandemic levels. The robust recovery in China has led to a surge in consumption of metals, while consumption in advanced economies has proved resilient. The rapid rebound in prices is a marked difference compared to the global financial crisis, when prices saw larger declines that lasted for many months. Precious metal prices also rose sharply, boosted by the depreciation in the U.S. dollar and lower interest rates. Agricultural commodity prices rose by 6% in FY 2020-Q3, but with divergence between broadly stable grain prices and rising prices of other agricultural commodities.

## 3.2. Consumer Prices in Afghanistan

Since being revised by the National Statistics and Information Authority (NSIA), consumer price index (CPI) in Afghanistan has been compiled on the base prices of April 2015 while previously; it was calculated on the base prices of March 2011. Similarly, in this revision, the CPI components are also aligned with new weights. As per data from the (NSIA) and analysis of Da Afghanistan Bank (DAB), the following results were observed in the consumer price index of Afghanistan.

Headline inflation, year-on-year measure of changes in the consumer price index showed an increase stand at 5.97% on average in the third quarter of FY 2020 from 2.51% recorded in the third quarter of the previous year. On the other hand, National inflation measured on quarter-on-quarter basis, indicates decline in the period under review. Observing the data, the average inflation rate went down to 5.97% in the third quarter of FY 2020, lower than average rate of 7.10% in the second quarter of FY 2020.

Observing the Kabul headline CPI, the inflation rate on year over year basis increased to 4.48% on average in the third quarter of FY 2020 from 2.04% in the same quarter of the previous year. On the other hand, this index decreased on quarter-to-quarter basis down to 4.48% on average in the third quarter of FY 2020 from 4.95% in the second quarter of FY 2020.

### 3.2.1. Developments in the National Headline Inflation (year-on-year changes)

The headline consumer price index increased on year-on-year basis in the third quarter of FY 2020. As per the available data, the headline inflation by this measure increased to 5.97% on average in the third quarter of FY 2020 from 2.51% in the same period of the previews year while on monthly basis, the inflation rate was recorded at 6.33%, 5.88%, and 5.70% in the months of July, August and September FY 2020 respectively.

In the food index, inflation increased to 11.00% on average in the third quarter of FY 2020 from 4.71% in the same quarter of the previous year. In the above mentioned index, the inflationary pressures came from higher prices of bread and cereals, meat, milk, cheese and eggs, oil and fats, fresh and dried fruits, and vegetables. The highest increase in the index was recorded in the prices of oils and fats, and fresh and dried fruits which increased to 17.72% and 15.08% on average from -1.85% and 3.35% respectively. Overall inflation in non-food category increased to average 1.19% from 0.51% in the third quarter of FY 2020 compared to same quarter of previous year. This increase was due to higher prices of tobacco, clothing, and housing increased over the one-year period. In the mentioned category, the highest increase was noted in price index of communication and miscellaneous, which increased to 8.22% and 11.61% on average from 5.64% and 4.39% respectively.

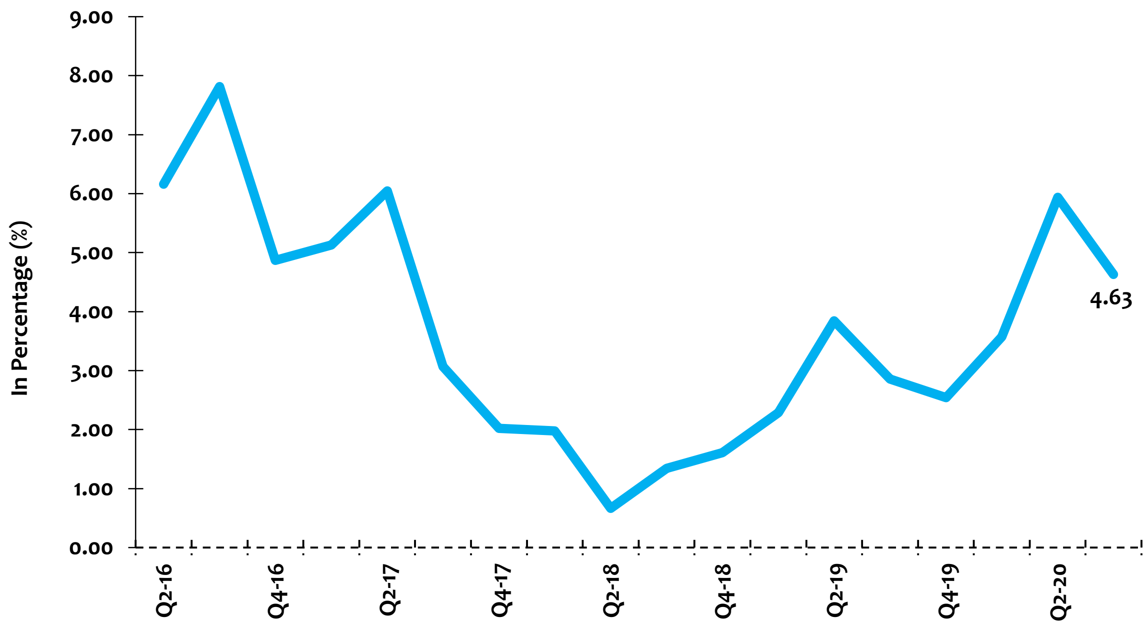
Core inflation also shows upward slope in the third quarter of FY 2020 compared to the third quarter of FY 2019. Trimmed mean which is the most common measure of core inflation, jumped to 4.63% from 2.86%. In addition, the CPI inflation, excluding bread and cereals, oil and fats and transportation, increased to 4.66% in the third quarter of FY 2020 from 2.37% in the same period of the previous year.

### 3.2.2. Developments in the National Headline Inflation (Quarter on Quarter Changes)

The short term measure of inflation shows downward trend. The national headline inflation on quarter to quarter basis decreased to 5.97% on average in the third quarter of FY 2020 from 7.10% recorded in the previous quarter. Food items represented low prices during the review period but on the other hand Non-food items represented high prices. Food inflation decreased to 11.00% in the third quarter of the current year from 14.12% in the second quarter of the current year. This decrease was the result of price decrease in bread and cereals, meat, milk, oil and fats, vegetables, sugar and sweets, and spices items. The price indices of food sub-items, milk, cheese and eggs, and fresh and dried fruits, have increased in the third quarter of FY 2020 compared to the second quarter of the same period.

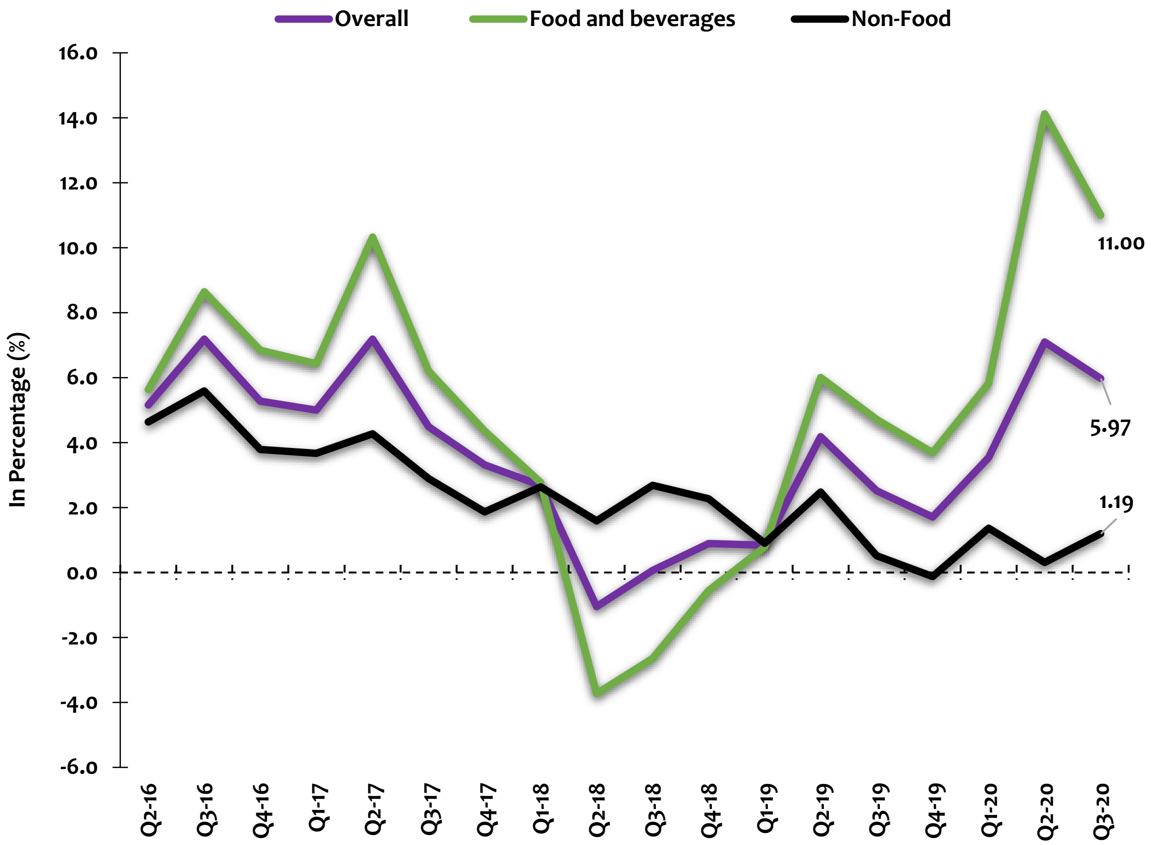
On the other hand, Non-food inflation increased in the third quarter of FY 2020 from the previous quarter. Observing the data, inflation in this index went up to 1.19% from 0.31%. In this category, the prices of housing and communication increased with big margin compared to the other non-food items. On the other hand, prices decreased in some other sub items of non-food category, such as clothing, transportation, information and culture.

**Figure 3.1:** Quarterly Trimmed mean (Q-o-Q) for the 3rd Quarter of FY 2020



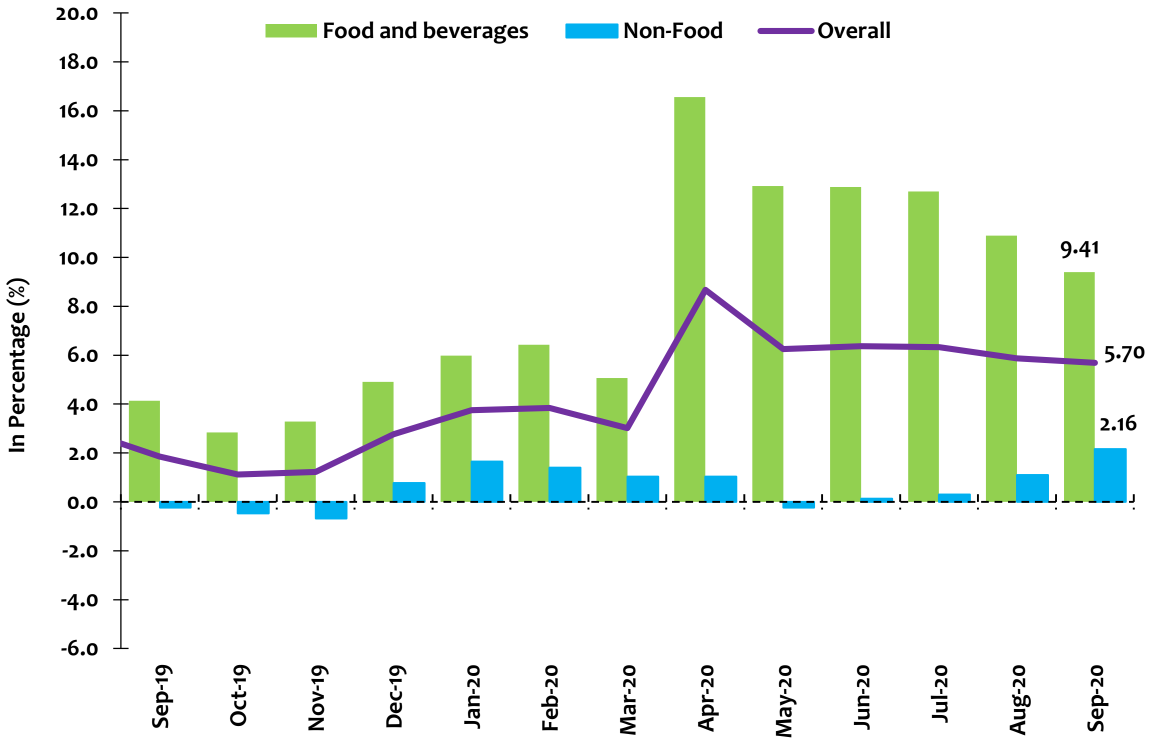

**Source:** NSIA/Monetary Policy Department, DAB staff calculation

**Figure 3.2:** Average National CPI (Q-o-Q) for the 3rd Quarter of FY 2020




**Source:** NSIA/Monetary Policy Department, DAB staff calculation

**Figure 3.3:** National Headline Inflation (Y-o-Y) for the 3rd Quarter of FY 2020




**Source:** NSIA/Monetary Policy Department, DAB staff calculation

**Table 3.1:** National Headline Inflation for the 3rd Quarter of FY 2020

| Based on April 2015 | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Periods | 2019 | | | | 2020 | | | | | | | | |
| | Weight | Jul 19 | Aug 19 | Sep 19 | Average (3months) | Apr 20 | May 20 | Jun 20 | Average (3months) | Jul 20 | Aug 20 | Sep 20 | Average (3months) |
| Overall Index | 100 | 2.77 | 2.92 | 1.85 | 2.51 | 8.67 | 6.26 | 6.36 | 7.10 | 6.33 | 5.88 | 5.70 | 5.97 |
| Food & Non-Alcoholic Beverages | 47.8 | 4.71 | 5.28 | 4.13 | 4.71 | 16.56 | 12.92 | 12.88 | 14.12 | 12.71 | 10.90 | 9.41 | 11.00 |
| Bread and Cereals | 14.6 | 8.33 | 6.05 | 4.08 | 6.15 | 15.19 | 14.76 | 15.78 | 15.24 | 14.07 | 16.13 | 14.49 | 14.90 |
| Meat | 7.5 | 6.68 | 9.23 | 8.79 | 8.23 | 12.03 | 10.70 | 12.49 | 11.74 | 12.63 | 10.98 | 9.72 | 11.11 |
| Milk, cheese and eggs | 4.7 | 2.11 | 0.95 | 0.27 | 1.11 | 0.02 | 4.04 | 3.58 | 2.55 | 3.35 | 4.05 | 2.16 | 3.19 |
| Oils and fats | 4.6 | -1.94 | -2.70 | -0.91 | -1.85 | 13.41 | 19.15 | 21.62 | 18.06 | 19.60 | 18.13 | 15.44 | 17.72 |
| Fresh and dried fruits | 5.0 | 5.03 | 5.32 | -0.30 | 3.35 | 14.32 | 10.35 | 10.88 | 11.85 | 20.05 | 12.03 | 13.15 | 15.08 |
| Vegetables | 6.0 | -4.92 | 0.17 | 1.60 | -1.05 | 43.46 | 23.02 | 16.15 | 27.54 | 14.60 | 6.56 | 2.06 | 7.74 |
| Sugar and sweets | 2.7 | 8.32 | 13.05 | 10.28 | 10.55 | 7.40 | 3.66 | 3.59 | 4.88 | 2.84 | 0.15 | 0.67 | 1.22 |
| Spices | 1.3 | 19.27 | 23.03 | 23.59 | 21.97 | 30.82 | 9.59 | 11.57 | 17.33 | 1.70 | -1.26 | -1.18 | -0.25 |
| Non-alcoholic beverages | 1.4 | 4.42 | 4.22 | 4.28 | 4.31 | 3.72 | 4.13 | 4.08 | 3.98 | 5.15 | 4.84 | 4.89 | 4.96 |
| Non-Food Items, Tobacco & Services | 52.2 | 1.00 | 0.78 | -0.24 | 0.51 | 1.03 | -0.24 | 0.13 | 0.31 | 0.31 | 1.10 | 2.16 | 1.19 |
| Tobacco | 0.3 | 1.74 | 1.53 | 0.28 | 1.18 | 1.11 | 1.12 | 1.40 | 1.21 | 2.73 | 2.46 | 2.73 | 2.64 |
| Clothing | 4.6 | 5.44 | 6.30 | 5.36 | 5.70 | 7.47 | 10.08 | 7.54 | 8.36 | 6.77 | 5.38 | 7.84 | 6.66 |
| Housing | 19.1 | -2.83 | -3.25 | -5.00 | -3.69 | -1.78 | -4.38 | -4.02 | -3.39 | -2.77 | -0.75 | 1.03 | -0.83 |
| Furnishing and household goods | 11.9 | 3.61 | 3.47 | 2.97 | 3.35 | 0.35 | 1.39 | 0.78 | 0.84 | 1.89 | 2.38 | 3.40 | 2.56 |
| Health | 6.2 | 5.43 | 6.02 | 5.47 | 5.64 | 6.50 | 4.36 | 8.86 | 6.57 | 8.72 | 8.10 | 7.82 | 8.22 |
| Transportation | 4.3 | -0.33 | -2.27 | -3.86 | -2.15 | -3.44 | -10.14 | -10.44 | -8.01 | -14.76 | -13.76 | -13.38 | -13.97 |
| Communication | 1.7 | -5.10 | -5.84 | -6.63 | -5.86 | -3.89 | -4.22 | -2.40 | -3.50 | -2.06 | -0.99 | -0.58 | -1.21 |
| Information and Culture | 1.1 | 2.66 | 3.44 | 2.98 | 3.02 | 0.87 | 1.77 | 3.15 | 1.93 | 0.68 | -0.45 | 0.72 | 0.31 |
| Education | 0.4 | 0.45 | 3.07 | 1.84 | 1.79 | 6.55 | 1.24 | 0.83 | 2.87 | 1.16 | 2.56 | 4.35 | 2.69 |
| Restaurants and Hotels | 1.1 | 3.79 | 0.27 | 1.36 | 1.81 | 2.03 | 1.76 | 0.97 | 1.59 | -1.20 | 3.13 | 2.31 | 1.41 |
| Miscellaneous | 1.4 | 2.95 | 4.06 | 6.15 | 4.39 | 13.23 | 12.40 | 14.17 | 13.27 | 13.37 | 11.99 | 9.49 | 11.61 |
| CPI ex. B & C, O & F, and T | | 2.20 | 2.98 | 1.93 | 2.37 | 7.84 | 4.82 | 4.61 | 5.75 | 5.23 | 4.27 | 4.47 | 4.66 |
| 30% trimmed mean | | 3.00 | 3.04 | 2.53 | 2.86 | 6.36 | 5.47 | 5.99 | 5.94 | 5.28 | 4.38 | 4.23 | 4.63 |

**Source:** NSIA/Monetary Policy Department, DAB staff calculation

### 3.2.3. Development in the Kabul Headline Inflation (year-on-year changes)

The headline CPI inflation in Kabul (year on year) has increased to 4.48% on average in the third quarter of FY 2020 from 2.04% in the same quarter of the previous year. **Th**e food index, which is accounted for 37.2% of the overall weight of the CPI, reflected upward movement in one-year period. In this category, inflationary pressures came from most of the food items. In the food category, higher prices of meat, oils and fats, fresh, and vegetables pushed the inflation rate to 7.89% on average in third quarter of FY 2020, while it was calculated 4.34% in the third quarter of FY 2019. **Inf**lation in non-food item, which comprises 62.8% weight of the whole index, has increased to 2.31% on average in the third quarter of FY 2020 from 0.23% in the same period of the previous year. This increase is attributed to high prices of clothing, housing, health, transportation, communication, information and culture, and restaurants and hotels. In this category clothing increased to 8.06% on average from 3.52%, housing increased to 0.40% from -4.94%, health increased to 13.45% from 8.74%, transportation increased to -12.15% from -1.34%, communication increased to 0.42% from -0.60%, information and culture increased to 3.33% from 3.28%, restaurants and hotels increased to 5.84% from 0.63% in the third quarter of FY 2020 compared to the same quarter of previews year. **Co**re inflation excluding bread & cereals, fats and oils, and transportation also indicates increase in the period under review compared to the same period of the previous year. In the third quarter of FY 2020, core inflation rate increased to 4.34% on average while the rate was recorded 1.87% in the same quarter of the previews year. The 30% trimmed mean also reflected higher inflation rate standing at 4.16% on average in the third quarter of FY 2020 compared to 2.61% in same quarter of FY 2019.

### 3.2.4. Development in the Kabul Headline Inflation (Quarter on Quarter Changes)

The quarter on quarter measure of headline inflation in Kabul indicated downward movement which reflects lower inflation in foods items of the CPI. The headline inflation in Kabul declined to 4.48% on average in third quarter of FY 2020 from 4.95% recorded in the second quarter of FY 2020.

Inflation in the food index decreased to 7.89% on average in the third quarter of FY 2020 from 10.71% in the previous quarter. In this category, the prices of bread and cereals, vegetables, sugar and sweets, and spices decreased which led to low inflation rate during the period under review. The highest decline was observed in the price index of vegetables which dramatically decreased to 1.66% on average in the third quarter of FY 2020 from 29.10% in the second quarter of FY 2020.

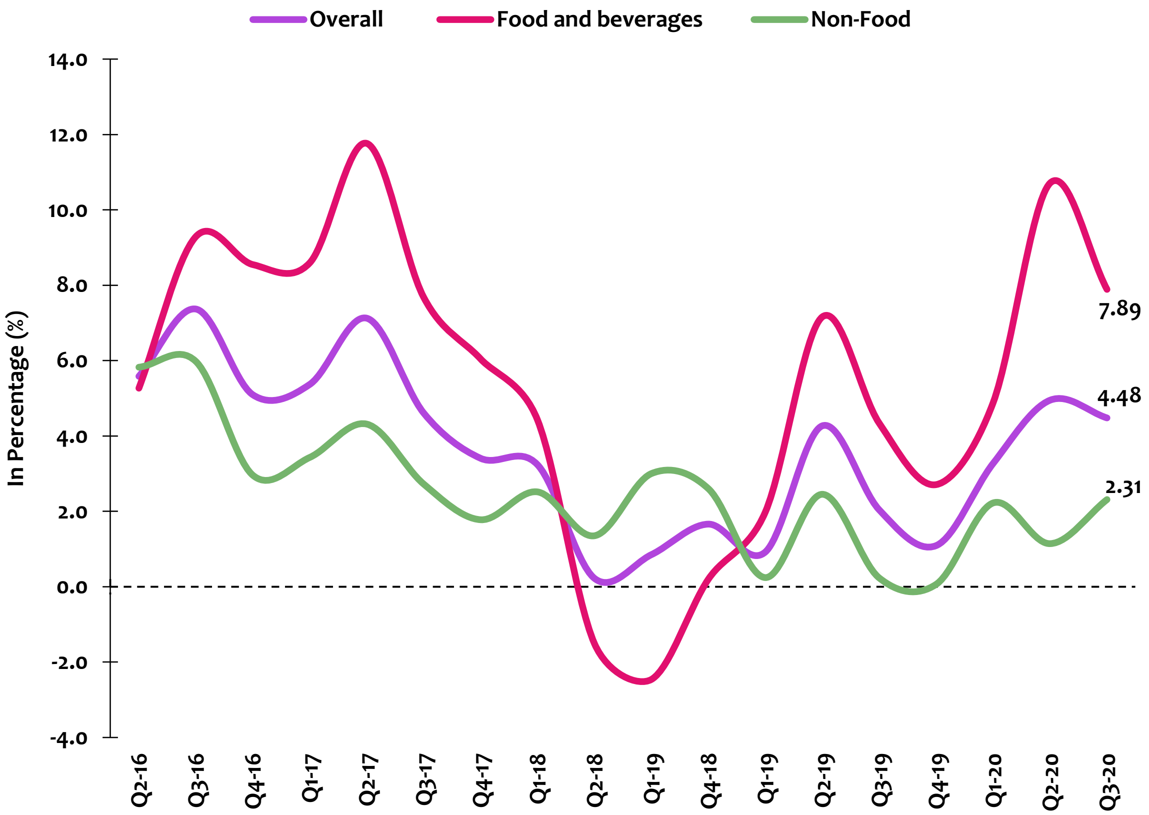
The Non-food category of the CPI shows increase in inflation rate during the third quarter of FY 2020 compared to the second quarter of FY 2020. Inflation in this category went up to 2.31% on average from 1.14%. The increase in non-food inflation is driven by high prices of tobacco, housing, and furnishing and household goods, which the highest increase was observed in the price of housing index up to 0.40% from -3.80% compare to the previous quarter of the current year.

## 3.3. Afghanistan Inflation Outlook for The End of FY 1399

The near-term outlook of inflation is likely to move slightly upward gradually due to COVID-19 pandemic. Monetary policy department forecasts inflation rate 5% to 6% for the fourth quarter of FY 2020. The forecast is based on the following course of factors. Since Afghanistan is an import oriented country and imports are at a greater quantity from neighboring countries; national inflation rate is often influenced by imported inflation from Iran, Pakistan, China, Turkey and other regional countries. There are so many factors which affect inflation rate but most importantly, Afghanistan's inflation is correlated with its trade partner countries' inflation rate and Afghani currency exchange rate against the US dollar.

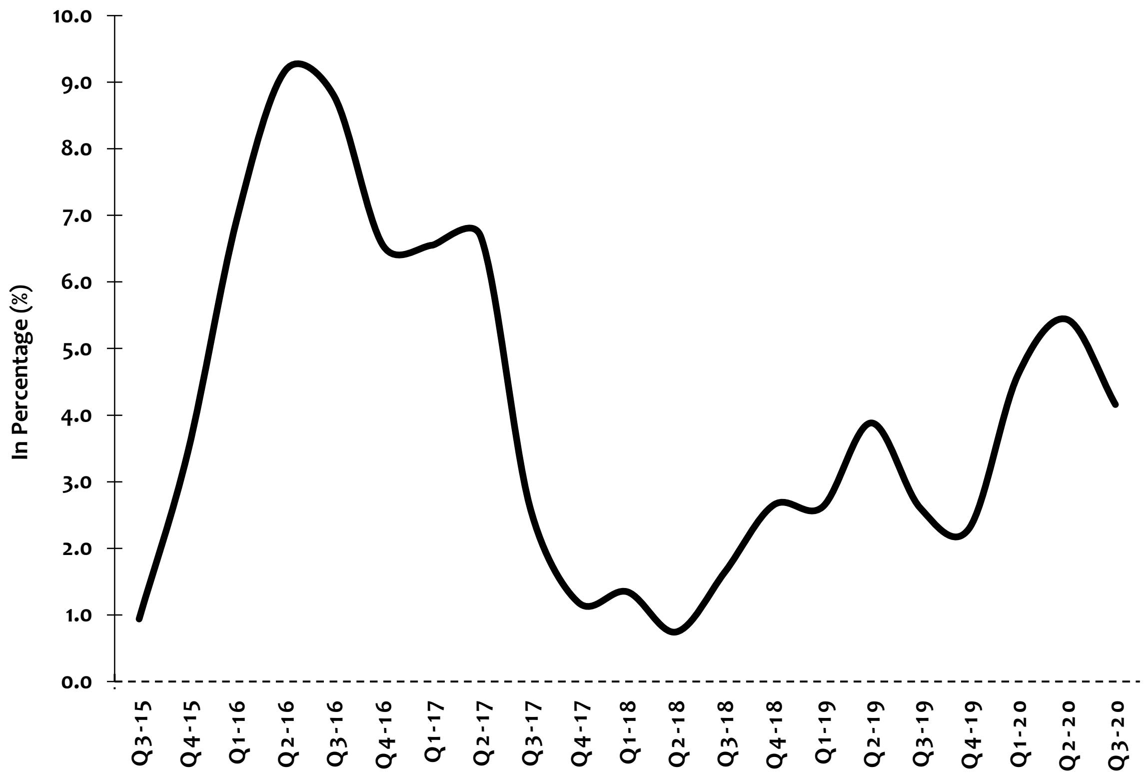
Regional inflation forecast may have some effects on Afghanistan's inflation rate. Looking into the inflation reports of the country's major trading partners, and their forecast for the fourth quarter of FY 2020, inflation in most of those countries has been increasing in the second quarter, and their forecast shows slight increase for the fourth quarter compared to the third quarter's actual rate. Inflation forecast in Afghanistan may also be conditional to the further spread of COVID-19 pandemic. Continuity of restrictive measures may cause to supply shortage which may result in higher commodity prices. Also, security is another concern that increases the uncertainty level in forecasting inflation for the fourth quarter.

**Figure 3.4:** Kabul Quarterly Average CPI (Q-o-Q) for the 3rd Quarter of FY 2020



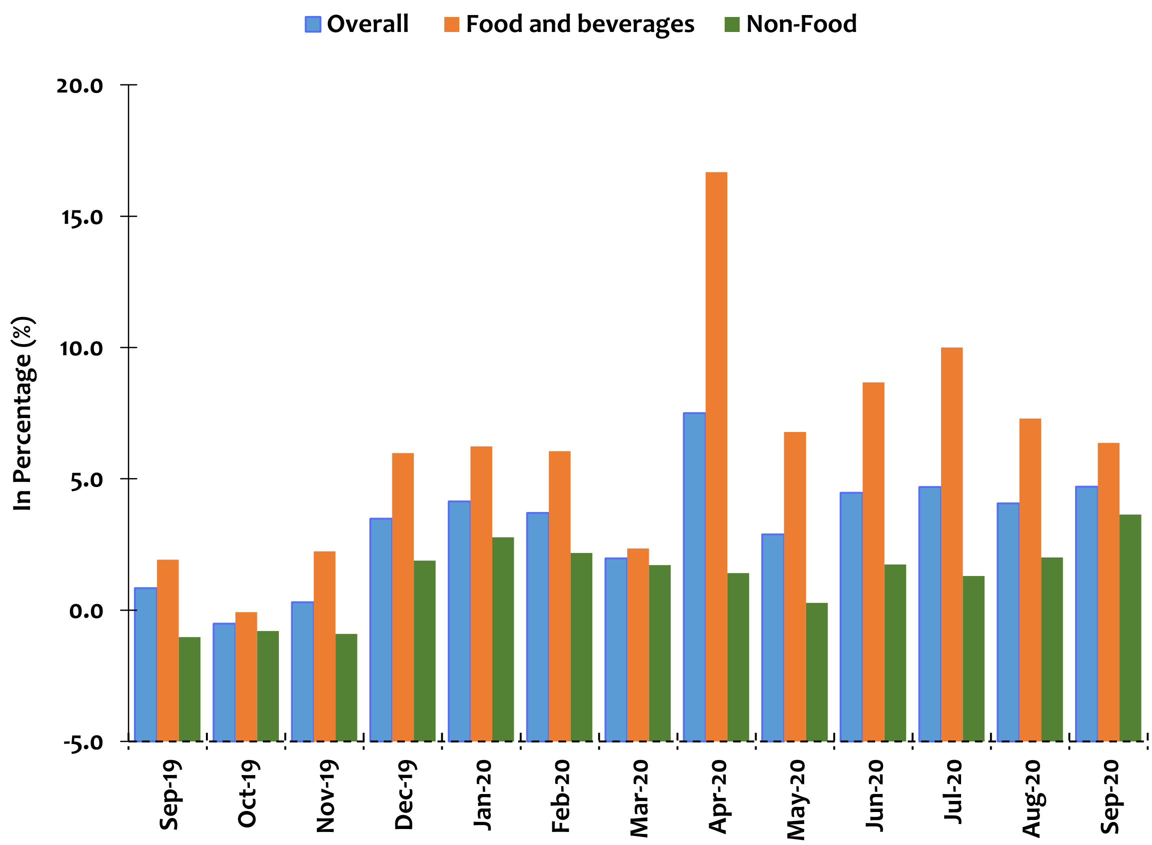

**Source:** NSIA/Monetary Policy Department, DAB staff calculation

**Figure 3.5:** Kabul Quarterly Average CPI 30% Trimmed Mean (Q-o-Q) for the 3rd Quarter of FY 2020




**Source:** NSIA/Monetary Policy Department, DAB staff calculation

**Figure 3.6:** Kabul Annual Headline Inflation for the 3rd Quarter of FY 2020




**Source:** NSIA/Monetary Policy Department, DAB staff calculation

**Table 3.2:** Kabul Headline Inflation for the 3rd Quarter of FY 2020

| Based on Apr 2015 | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Period | 2019 | | | | 2020 | | | | | | | | |
| | Weight | Jul 19 | Aug 19 | Sep 19 | Average (3months) | Apr 20 | May 20 | Jun 20 | Average (3months) | Jul 20 | Aug 20 | Sep 20 | Average (3months) |
| **Overall Index** | 100 | 2.52 | 2.76 | 0.84 | 2.04 | 7.50 | 2.88 | 4.47 | 4.95 | 4.69 | 4.07 | 4.69 | 4.48 |
| **Food & Non-Alcoholic Beverages** | 37.2 | 5.31 | 5.81 | 1.92 | 4.34 | 16.68 | 6.78 | 8.67 | 10.71 | 9.99 | 7.30 | 6.37 | 7.89 |
| **Bread and Cereals** | 9.8 | 11.37 | 8.00 | 4.73 | 8.03 | 11.87 | 9.60 | 8.59 | 10.02 | 4.35 | 9.49 | 5.98 | 6.61 |
| **Meat** | 6.4 | 8.03 | 6.43 | 5.11 | 6.52 | 5.93 | 8.10 | 9.56 | 7.87 | 8.48 | 10.02 | 5.77 | 8.09 |
| **Milk, cheese and eggs** | 3.2 | 0.01 | -0.09 | -1.09 | -0.39 | -1.55 | 0.97 | -2.32 | -0.97 | -0.70 | 0.34 | -1.70 | -0.69 |
| **Oils and fats** | 3.6 | -5.23 | -6.33 | -2.78 | -4.78 | 8.26 | 13.72 | 26.29 | 16.09 | 28.95 | 25.04 | 19.45 | 24.48 |
| **Fresh and dried fruits** | 5.2 | 6.57 | 5.56 | -8.63 | 1.17 | 16.42 | 7.49 | 6.44 | 10.12 | 26.18 | 13.51 | 20.02 | 19.90 |
| **Vegetables** | 4.2 | -12.04 | -3.22 | -5.78 | -7.01 | 63.34 | 9.29 | 14.67 | 29.10 | 8.94 | -2.25 | -1.70 | 1.66 |
| **Sugar and sweets** | 2.8 | 11.66 | 19.09 | 13.80 | 14.85 | 5.50 | -2.81 | -0.23 | 0.82 | 0.60 | -6.79 | -4.98 | -3.72 |
| **Spices** | 1.0 | 24.66 | 32.32 | 28.09 | 28.36 | 41.11 | -3.44 | 9.83 | 15.84 | -8.41 | -6.66 | -3.31 | -6.13 |
| **Non-alcoholic beverages** | 0.9 | 4.49 | 4.37 | 0.37 | 3.08 | 3.58 | 2.74 | 6.66 | 4.33 | 7.48 | 5.61 | 11.15 | 8.08 |
| **Non-Food Items, Tobacco & Services** | 62.8 | 0.81 | 0.90 | -1.03 | 0.23 | 1.40 | 0.28 | 1.74 | 1.14 | 1.30 | 2.00 | 3.63 | 2.31 |
| **Tobacco** | 0.3 | -0.39 | 0.79 | 0.08 | 0.16 | -1.77 | -2.31 | -2.95 | -2.34 | 0.61 | -0.38 | 0.05 | 0.09 |
| **Clothing** | 4.8 | 4.30 | 5.20 | 1.08 | 3.52 | 10.13 | 16.67 | 10.11 | 12.30 | 6.63 | 4.88 | 12.68 | 8.06 |
| **Housing** | 23.5 | -4.15 | -4.16 | -6.49 | -4.94 | -2.69 | -5.85 | -2.87 | -3.80 | -1.38 | 0.82 | 1.75 | 0.40 |
| **Furnishing and household goods** | 17.6 | 3.45 | 3.10 | 1.99 | 2.85 | -2.12 | -0.38 | -1.40 | -1.30 | 0.78 | 1.77 | 3.90 | 2.15 |
| **Health** | 5.3 | 8.92 | 10.16 | 7.12 | 8.74 | 14.74 | 6.46 | 19.36 | 13.52 | 15.39 | 12.41 | 12.53 | 13.45 |
| **Transportation** | 4.6 | 0.03 | -0.82 | -3.23 | -1.34 | 1.96 | -3.30 | -3.51 | -1.62 | -12.83 | -11.91 | -11.70 | -12.15 |
| **Communication** | 2.0 | -0.47 | 0.27 | -1.62 | -0.60 | 0.15 | -0.50 | 1.74 | 0.46 | 0.05 | 0.22 | 0.98 | 0.42 |
| **Information and Culture** | 1.7 | 1.96 | 4.22 | 3.66 | 3.28 | 4.92 | 5.88 | 9.10 | 6.63 | 4.56 | 1.70 | 3.71 | 3.33 |
| **Education** | 0.7 | -0.17 | 2.42 | 0.16 | 0.80 | 5.63 | -1.38 | -2.35 | 0.63 | -2.30 | 0.02 | 2.93 | 0.22 |
| **Restaurants and Hotels** | 1.0 | 2.77 | -2.39 | 1.51 | 0.63 | 8.12 | 8.74 | 10.71 | 9.19 | 2.07 | 9.33 | 6.13 | 5.84 |
| **Miscellaneous** | 1.3 | 7.23 | 8.68 | 11.35 | 9.09 | 17.99 | 18.44 | 20.38 | 18.94 | 17.90 | 14.09 | 11.58 | 14.52 |
| **CPI ex. B & C, O & F, and T** | | 2.03 | 2.78 | 0.79 | 1.87 | 7.27 | 2.03 | 3.57 | 4.29 | 4.72 | 3.48 | 4.82 | 4.34 |
| **30% trimmed mean** | | 3.34 | 3.27 | 1.22 | 2.61 | 6.83 | 3.71 | 5.79 | 5.44 | 4.13 | 3.86 | 4.50 | 4.16 |

**Source:** NSIA/Monetary Policy Department, DAB staff calculation

# 4

# External Sector Developments

# 4

# EXTERNAL SECTOR DEVELOPMEN

## 4.1. Summary:

Afghanistan's external sector recovered further in the third quarter of the FY 1399 supported by a significant increment in inflows in the form of official grants together with a substantial enhancement in personal transfers and services account related receipts.

Several notable achievements were observed in spite of the COVID-19 pandemic. Earnings from merchandise exports slightly declined and merchandise imports recorded a positive quarter-on-quarter growth in the third quarter of the FY 1399. However, with a more than expected rebound in merchandise exports and a sustained growth in merchandise imports the trade deficit narrowed in the third quarter of the FY 1399 in comparison with the same period in 1398. Due to trade acceleration with trading partners and air travel between some countries after relaxing trade restrictions the services sector related activities were rebounded during the third quarter of the FY 1399. Official grants (Operating and development) together with Personal transfers and Worker home remittances had upward trends during the third quarter of the FY 1399.

However, in the financial account, a substantial increase was observed in foreign direct investment (FDI) inflows and outflow during the

At the same time, the value of merchandise imports as a total increased by 18% to a value of USD 1,731.42 million in the third quarter of the FY 1399 from a value of USD 1,461.67 million recorded in the third quarter of the FY 1398.

quarter under review. Meanwhile, the level of reserves assets indicated a significant decline mainly on account of a decrease in foreign currency assets, reflecting these developments; the BOP recorded an overall deficit of around USD 884 million at end of the third quarter of the FY 1399.

## 4.2. Balance of Payments:

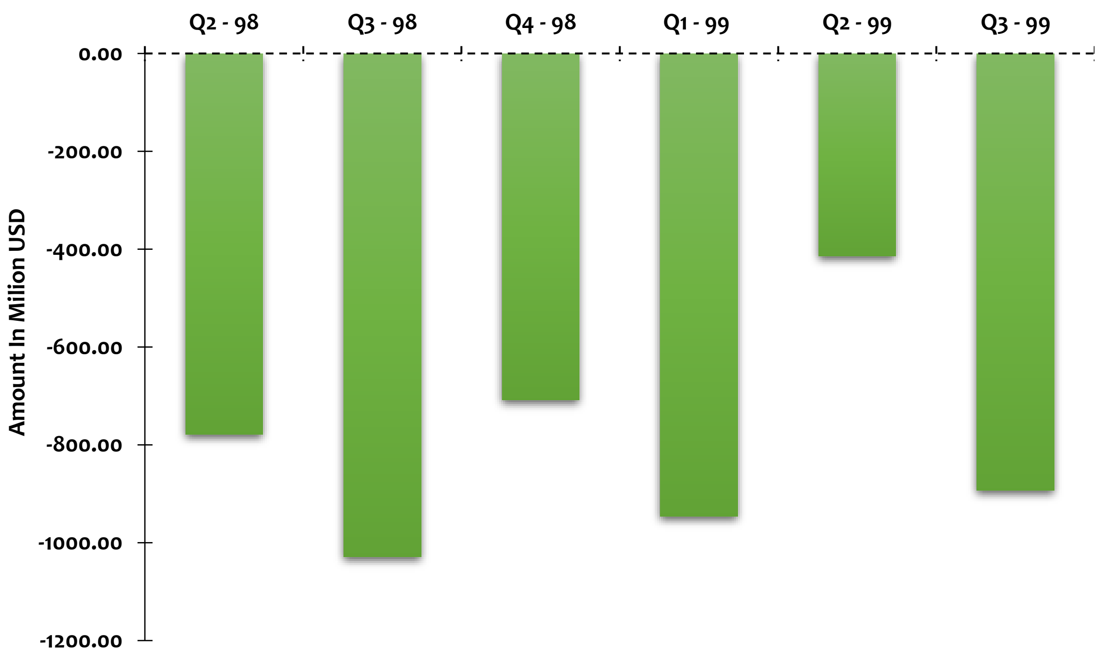
### 4.2.1. Current Account:

The balance of payments (BOP's) current account deficit decreased by 13% to a value of USD 893.51 million in the third quarter of the FY 1399 from a value of USD 1,028.38 million recorded in the third quarter of the FY 1398 (see table 4.1 and figure 4.1). This decline was mainly due to an expansion in official grants as well as personal transfers and services account related receipts during the third quarter of the FY 1399.

Base on quarter to quarter comparison the deficit of trade balance on BoP bases, expanded by 22% in the third quarter of the FY 1399 as a result of a sustainable decline in merchandise exports and a notable increase in merchandise imports. Considering the statistics, the value of merchandise exports as a total declined by 5% to a value of USD 198.42 million in the third quarter of the FY 1399 from a value of USD 208.77 million recorded in the third quarter of the FY 1398.

Meanwhile, compensation of employees together with investment income inflows declined by 14% to a value of USD 65.35 million in the third quarter of the FY 1399 from a value of USD 75.79 million recorded in the similar quarter of the last year. As well as, official grants to the government sector and personal transfers from foreign countries increased by 110% and stood at a value of USD 717.57 million in the third quarter of the FY 1399 from a value of USD 341.27 million recorded in the similar quarter of the last year.

**Figure 4.1:** Current account balance for the 3rd Quarter of FY 2020 (1399)




**Source:** NSIA/Monetary Policy Department, DAB staff calculation

### 4.2.2. Capital Account:

Inflow to the capital account decreased by 72% to a value of USD 109.53 million in the third quarter of the FY 1399 from a value of USD 391.57 million recorded in the third quarter of the FY 1398, as a result of lower inward of capital transfers to the government sector.

### 4.2.3. Financial account:

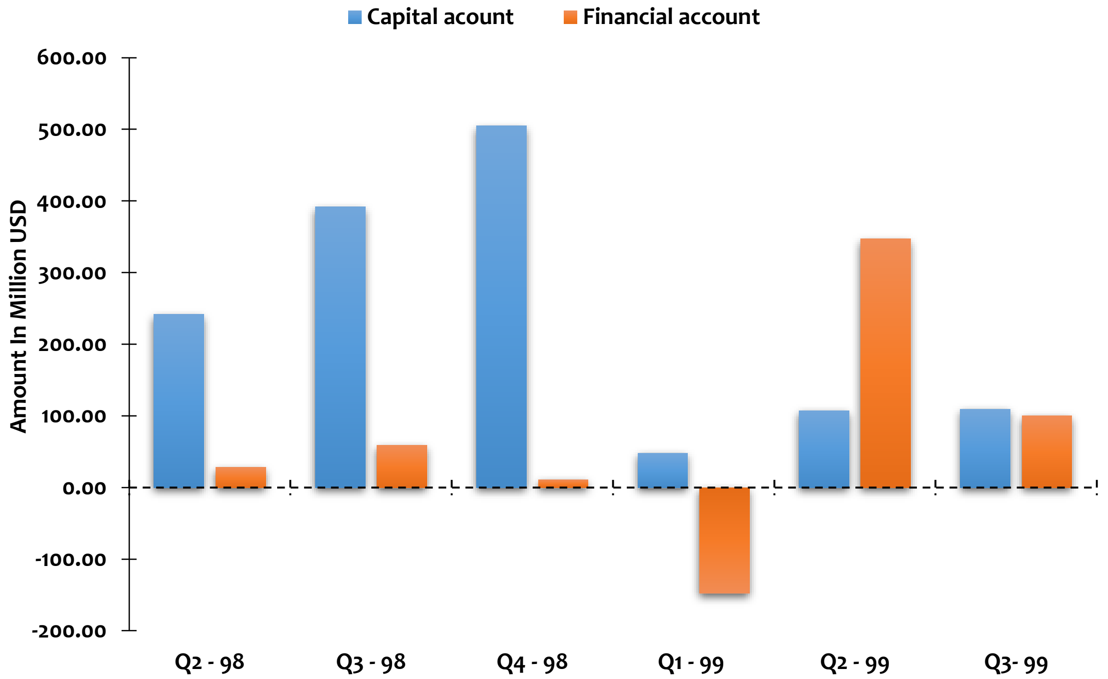
Under financial account of the Balance of Payments (BOPs), foreign investment is an important component which consists of foreign direct investment (FDI), foreign portfolio investment (FPI) and Other Investments.

Considering the statistics, FDI inflow stood at a value of USD 4.78 million in the third quarter of the FY 1399 from a value of USD -4.18 million recorded in the third quarter of the FY 1398. While, FDI outflow reached to a value of USD 10 million in the third quarter of the FY 1399 in comparison with a value of USD 4.86 million recorded in the similar quarter of the last year. In the meantime, portfolio investment exhibits USD 83.11 million which reflects insertion of Afghanistan investment in foreign countries during the third quarter of the FY 1399 from the value of USD -33.74 million in the third quarter of the FY 1398.

Further analysis reveals that the country's other aggregated financial assets abroad dropped significantly to a value of USD 0.24 million in the third quarter of the FY 1399 from a value of USD 17.86 million recorded in the third quarter of the FY 1398. Other aggregated financial liabilities, followed downward trend and stood at a value of USD 9.50 million in the third quarter of the FY 1399 from a value of USD 55.14 million recorded in the similar quarter of the previews year.

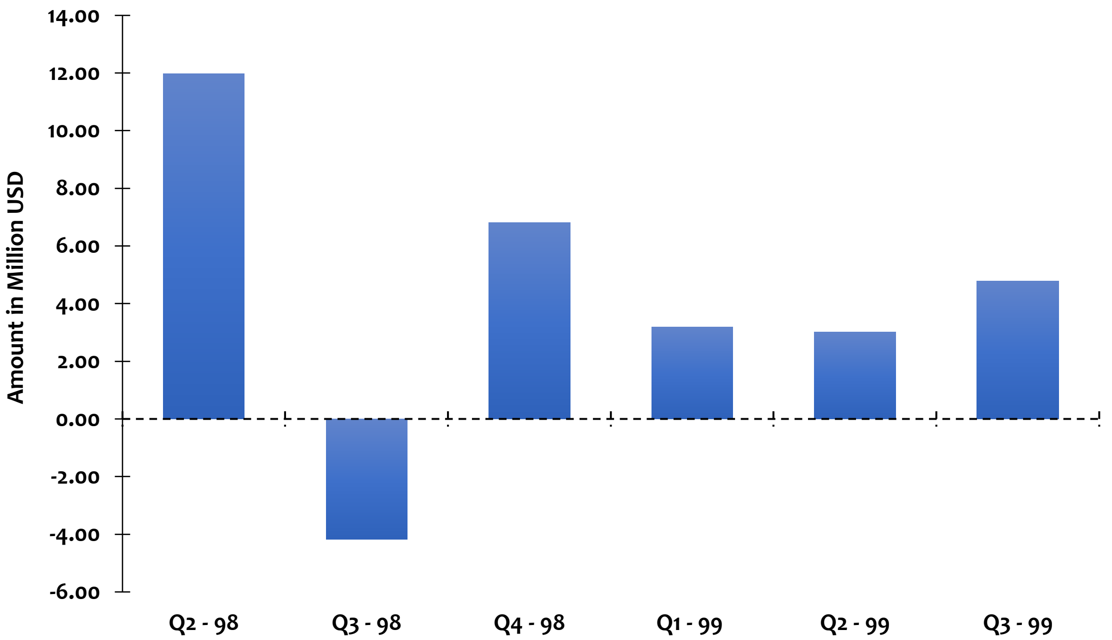
The financial account balance as a total stood at USD 100.42 million in the third quarter of the FY 1399 which was well above the value of USD 59 million recorded in the third quarter of the FY 1398 (see table 4.1 and figures 4.2, and 4.3).

**Figure 4.2:** Capital and Financial Account for the 3rd Quarter of FY 2020 (1399)




**Source:** Monetary Policy Department, DAB staff calculation

**Figure 4.3:** FDI inflows for the 3rd Quarter of FY 2020 (1399)




**Source:** Monetary Policy Department, DAB staff calculation

## 4.3. Developments in Merchandise Trade:

### 4.3.1. Exports:

In comparison to the same quarter of the preceding year earnings from merchandise exports declined slightly by 5% to a value of USD 198.42 million in the third quarter of the FY 1399 from a value of USD 208.77 million recorded in the similar quarter of the previous year. This was mainly attributable to improvements in earnings from all components of exports, except food items (fresh and dry fruits). Export of medical seeds and other recorded a notable performance in the review period.

**Earnings from medical seeds export increased by 19%** to a value of USD 128 million in the period under review from a value of USD 107.24 million in the third quarter of the FY 1398.

**Receipts from exports of leather and wool products continued to rise by 51%** and reached to a value of USD 8.61 million in the third quarter of the FY 1399 from a value of USD 5.70 million recorded in the third quarter of the FY 1398.

**Likewise, carpet and rug exports jumped to a value of USD 6.25** million in the third quarter of the FY 1399 from a value of USD 5.93 million in the similar quarter of the preceding year.

**Exports of food item (fresh and dry fruit), which is counted as the major exporting products of the country in the recent period declined by 38%** and reached to a value of USD 55.52 million in the third quarter of the FY 1399 from a value of USD 89.91 million in the third quarter of the FY 1398.

### 4.3.2. Imports:

Total merchandise import surged to a value of USD 1,923.79 million in the third quarter of the FY 1399 compared to a value of USD 1,591.20 million recorded in the third quarter of the previous year, owing to improvements in all components of imports except industrial supplies as a result of trade acceleration with trading partners (Iran, China, Pakistan, India, Uzbekistan and Tajikistan) after relaxing trade restrictions.

**Figure 4.4:** Trade performance and Trade balance for the 3rd Quarter of FY 2020 (1399)


**Source:** NSIA /DAB staff calculation

Imports of capital goods increased by 44% and reached to a value of USD 860.26 million in the third quarter of the FY 1399 from a value of USD 597.56 million recorded in the third quarter of the FY 1398, reflecting the continued rise in imports of spare parts machinery and transport equipment associated with ongoing private sector activities during the quarter under review.

Import of consumer goods also, increased by 28% to a value of USD 633.48 million in the third quarter of the FY 1399 from a value of USD 493.56 million in the comparable quarter of last year. This was basically due to higher imports of flour and wheat flour, fabrics, sugar, cloths, footwear, soaps, cigarettes and electricity.

Imports of fuel and lubricants depicted an increase of 13% to a value of USD 300.46 million in the third quarter of the FY 1399 from a value of USD 266.85 million in the third quarter of the FY 1398, wholly on account of speed up in the volume of petroleum products imports.

Industrial supplies on the other hand declined to a value of USD 129.60 million in the third quarter of the FY 1399 from a value of USD 233.23 million in the third quarter of the FY 1398, largely due to slow-down in construction activities during the period as well as import substitution.

## 4.4. Direction of Trade:

Trade between Afghanistan and its trading partners are categorized as export destinations and import origins. Figures 4.5 and 4.6 show Afghanistan's direction of trade with its trading partners during the third quarter of the FY 1399.

Based on the statistics, Commonwealth of Independent States (CIS), Iran, China, Pakistan and India remained the major trading partners with Afghanistan. Out of the total exports to the trading partners the major recipients of Afghanistan's exports are India, Pakistan, China, United Arab Emirate and Turkey.

### 4.4.1. Direction of Exports:

In the third quarter of the FY 1399 **India ranked as the first and top export destination for Afghanistan.**

The share of total exports to India reached to 44% which is well above than 38% registered in the third quarter of the FY 1398. In terms of value, total exports to India increased by 10% to a value of USD 87.10 million in the third quarter of the FY 1399 from a value of USD 79.53 million recorded in the third quarter of the previous year.

**Pakistan ranked the second largest buyer of Afghanistan export during the third quarter of the FY 1399.** Share of the total exports to Pakistan declined to 39% which is below than 49% registered in the third quarter of the FY 1398. In term of value, total exports to Pakistan also dropped by 24% to a value of USD 77.17 million in the third quarter of the FY 1399 compared to a value of USD 101.52 million recorded in the third quarter of the FY 1398.

**United Arab Emirates (UAE) ranked the third largest buyer of Afghanistan export during the third quarter of the FY 1399.** The share of Afghanistan's exports to UAE remained unchanged 3% in the third quarter of the FY 1399, but in respect of value, Afghanistan's total exports to UAE decreased to a value of USD 5 million in the third quarter of the FY 1399 compared to a value of USD 6.3 million in the same quarter of the FY 1398.

**The last three largest export destinations are Turkey, Iran and China countries during the third**

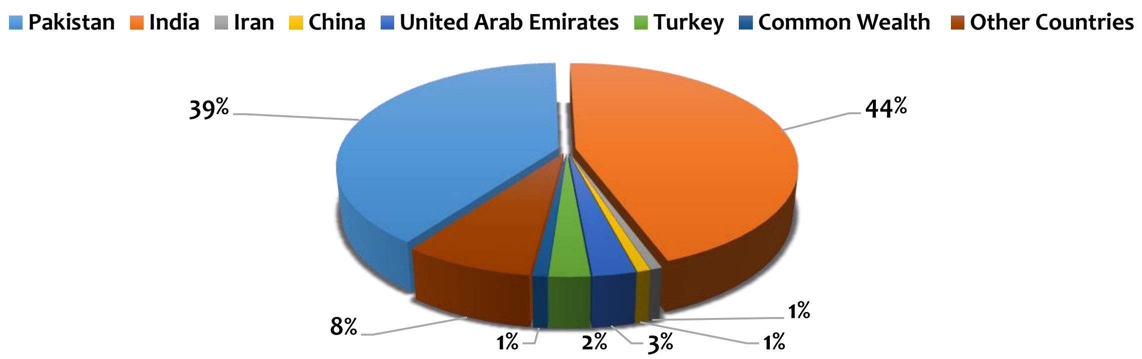
**quarter of the FY 1399.** The share of total exports to Turkey slightly increased to 2.5% in the third quarter of the FY 1399 from 2% registered in the third quarter of the FY 1398.

In term of value, Afghanistan total exports to Turkey remained unchanged during the period under review. Whereas, the share of total export to Iran also indicate a little decline to 0.9% in the third quarter of the FY 1399 from 1.3% registered in the third quarter of the FY 1398.

In respect of value, total exports to Iran decreased to a value of USD 1.38 million in the third quarter of the FY 1399 from a value of 2.86 million registered in the similar quarter of the last year.

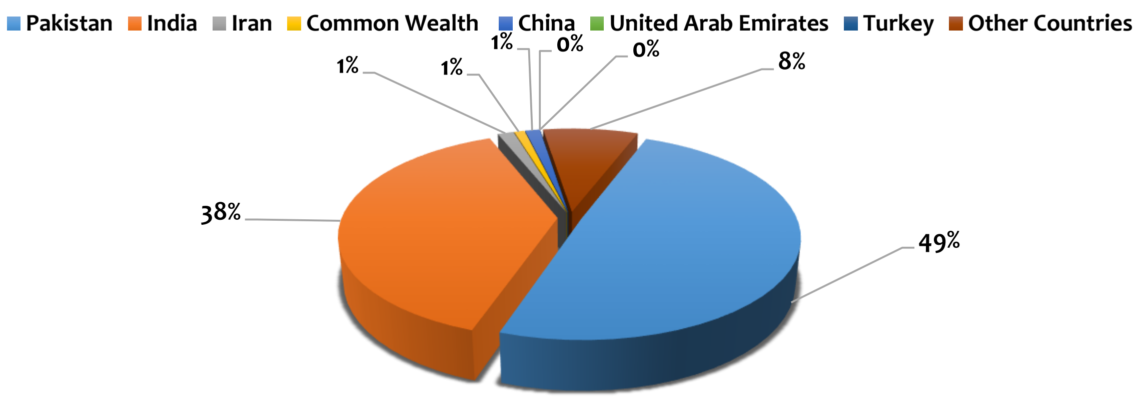
While, the share of total exports to China declined significantly to 0.8% in the third quarter of the FY 1399 from 1.20% which recorded in the third quarter of the FY 1398. In respect of value, the total exports to China decline to a value of USD 1.61 million in the third quarter of the FY 1399 from a value of USD 2.65 million recorded in the third quarter of last year (see tables 4.4, 4.5 and figures 4.5, 4.6).

**Figure 4.5:** Direction of Exports (% share) for the 3rd Quarter of FY 2020 (1399)




**Source:** NSIA /DAB staff calculation

**Figure 4.6:** Direction of Exports (% share) for the 3rd Quarter of FY 2019 (1398)




**Source:** NSIA /DAB staff calculation

### 4.4.2. Direction of Imports:

Major parts of Afghanistan import are sourced from CIS countries, Iran, China, Pakistan, India, United Arab Emirates and Japan.

**CIS countries, followed by "**Russia, Tajikistan, Uzbekistan, Turkmenistan and Kazakhstan**" were the first largest sources of imports for**

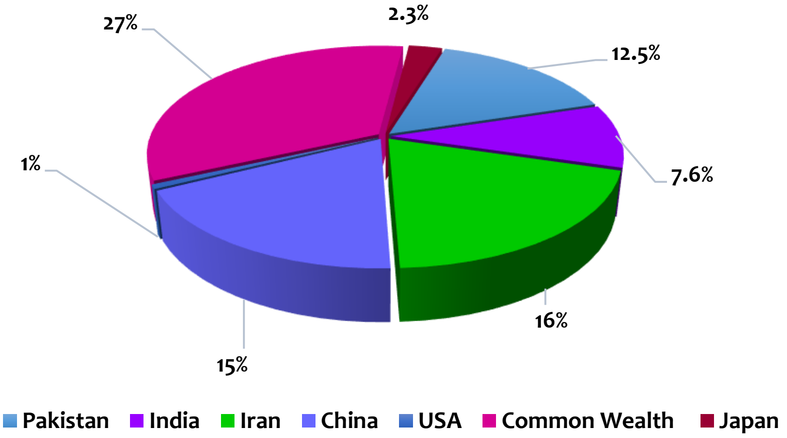
**Afghanistan during the third quarter of the FY 1399.** Imports from CIS countries stood at a value of USD 525.14 million with share of 27% in the third quarter of the FY 1399 from a value of USD 373.54 million with share of 23.5% in the third quarter of the FY 1398.

**After CIS countries the next largest import source is Iran in the third quarter of the FY 1399.** The share of Iran has decreased marginally from 20% in the third quarter of the FY 1398 to 16% in the third quarter of the FY 1399. Total Imports from Iran slightly declined by 1% to a value of USD 308.37 million in the third quarter of the FY 1399 from a value of USD 311.89 million registered in the third quarter of the FY 1398.

**After Iran the next largest import sources is China in the third quarter of the FY 1399.** The total imports from china increased by 5% and stood at a value of USD 283.64 million with share of 15% in the third quarter of the FY 1399 from a value of USD 269.57 million with share of 17% recorded in the third quarter of the FY 1398.

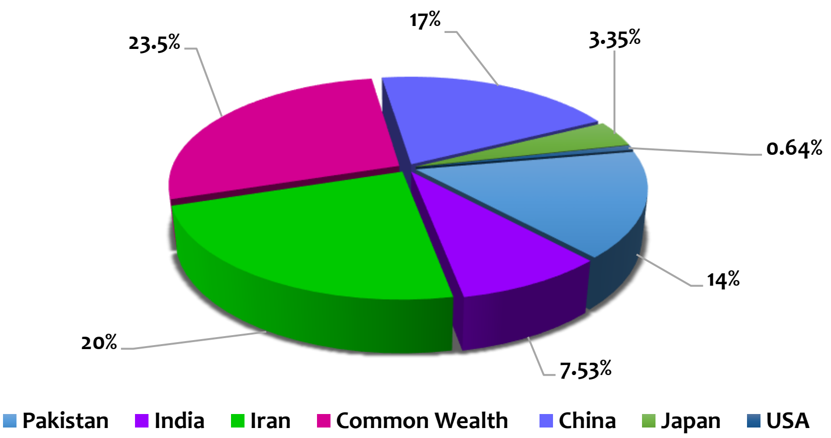
**Pakistan graded the fourth largest import origin to Afghanistan in the third quarter of the FY 1399.** As per the statistics, imports from Pakistan increased by 12% to a value of USD 240.98 million with share of 12.5% in the third quarter of the FY 1399 from a value of USD 215.69 million with share of 14% in the third quarter of the FY 1398.

**Figure 4.7:** Direction of Imports (% share) for the 3rd Quarter of FY 2020 (1399)




**Source:** NSIA /DAB staff calculation

**Figure 4.8:** Direction of Imports (%share) for the 3rd Quarter of FY 2019 (1398)




**Source:** NSIA /DAB staff calculation

**India was the fifth largest import origin to Afghanistan in the third quarter of the FY 1399.** Total Imports from India increased by 23% to a value of USD 146.95 million with share of 7.6% in the third quarter of the FY 1399 from a value of USD 119.84 million with share of 7.53% in the third quarter of the FY 1398.

**UAE, Japan and Germany were the last largest sources of imports for Afghanistan in the third quarter of the FY 1399.** The shares of each source in the total imports were accounted as 2.5%, 2.3% and 1.5% respectively.

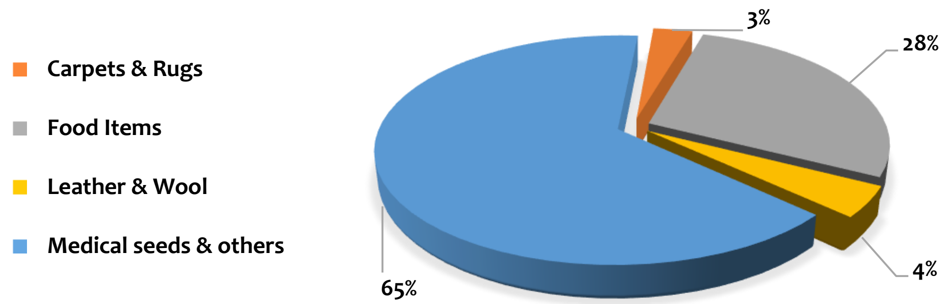
**Export of medical seeds products have registered high growth of 19%** and stood at a value of USD 128.05 million in the third quarter of the FY 1399 from a value of USD 107.24 million recorded in the third quarter of the FY 1398. The major medical seeds commodities exported by Afghanistan included in Red asafetida, Green caraway, Water melon seed and Wild rue seed. In terms of share in overall exports, the share of medical seeds commodities rose to 65% in the third quarter of the FY 1399 from 51% recorded in the similar quarter of the preceding year.

## 4.5. Composition of Trade:

### 4.5.1. Commodity Composition of Exports:

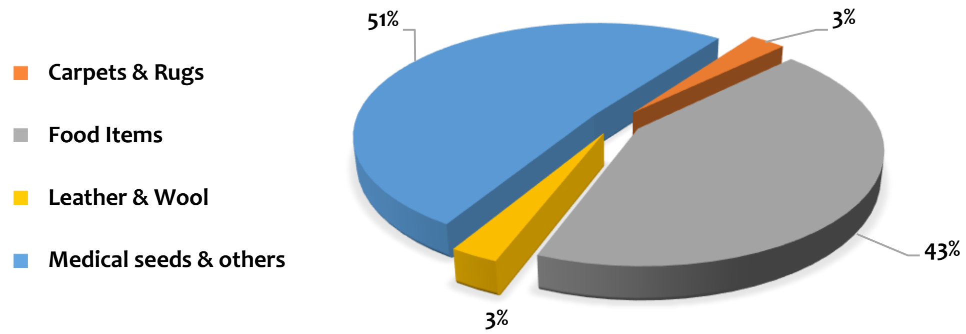
Commodity exports of the country has been categorized and analyzed as bellow:

**Figure 4.9:** Composition of Exports (share in %) for the 3rd Quarter of FY 2020 (1399)




**Source:** NSIA/DAB staff calculation

**Figure 4.10:** Composition of Exports (share in %) for the 3rd Quarter of FY 2019 (1398)




**Source:** NSIA/DAB staff calculation

**Exports of food items (oil seeds, fresh and dry fruits) drastically faded by 38%** to touch USD 55.52 million in the third quarter of the FY 1399 from a value of USD 89.91 million recorded in the third quarter of the FY 1398. At the same time the share of food items declined to 28% in the quarter under review from 43% recorded in the similar quarter of the last year.

**Export of leather and wool increased by 51%** and reached to a value of USD 8.61 million in the third quarter of the FY 1399 from a value of USD 5.70 million recorded in the corresponding quarter of the preceding year. In terms of shares the leather and wool products had the third largest share in the basket of total exports which is increased to 4.3% in third quarter of the FY 1399 from 3% recorded in the same quarter of the previous year.

**Export of carpet and rugs which are considered as a main component of Afghanistan's exports in the past decades had the 4th largest share in total exports which has been rather stable at 3.2%** in the third quarter of the FY 1399 and 2.8% in the third quarter of the FY 1398. While the exports value of carpet and rugs had upward movement and stood at a value of USD 6.25 million which showed a normal increment of 5% as compared to the value of USD 5.93 million recorded in the third quarter of the last year (figures 4.11 and 4.12 indicate composition of exports in the related periods).

### 4.5.2. Composition of Imports:

Commodity imports of the country are classified into four categories which are described as below:

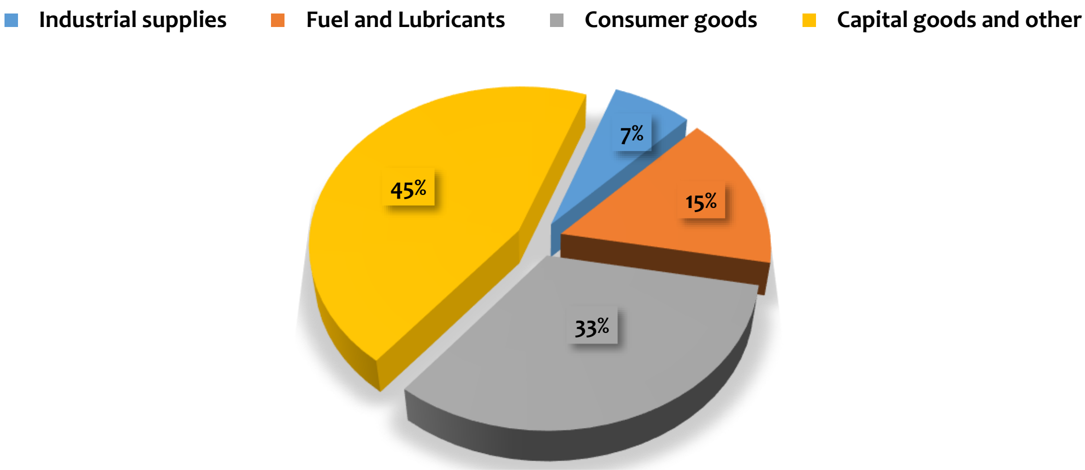
**Imports of capital goods has grown by 44% to a value of USD 860.26 million** in the third quarter of the FY 1399 from a value of USD 597.56 million in the third quarter of the FY 1398. The share of capital goods in overall imports was the highest in the basket of imports during the third quarter of the FY 1399, which expanded to 45% in the third quarter of the FY 1399 from 38% recorded in the third quarter of the preceding year.

**Import of consumer goods on the other hand have grown by 28% over this period**, and stood at a value of USD 633.48 million in the third quarter of the FY 1399 from a value of USD 493.56 million in the third quarter of the FY 1398. Consumer goods is comprised of major import items such as flour and wheat flour, fabrics, sugar, electricity, vegetable-oil, cigarettes, medicines, soaps, cloths, footwear, tire and tubes and electronic goods. Observing the data, the share of consumer goods has also increased to 33% in the third quarter of the FY 1399 from 31% in the third quarter of the last year.

**The other major segment is fuel and lubricant Imports**. Under the fuel and lubricant related items, petroleum oil imports are the major component. The value of petroleum oil in the basket of total imports increased by 13% and stood at a value of USD 300.46 million in the third quarter of the FY 1399 from a value of USD 266.85 million recorded in the third quarter of the FY 1398, the share of which slightly decreased to 16% in the third quarter of the FY 1399 from 17% recorded in the third quarter of the FY 1398.

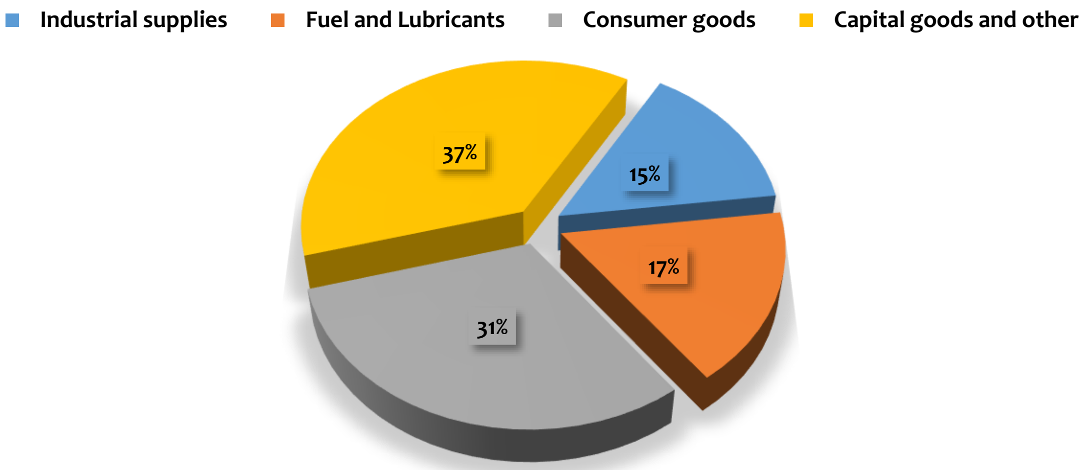
**In the import category the industrial supplies hold the smallest share in the basket of Afghanistan's imports which is decreased to 7%** in the third quarter of the FY 1399 from 15% recorded in the third quarter of the FY 1398. In term of value it exhibited that the imports of such goods contracted notably by 44% and stood at a value of USD 129.60 million in the third quarter of the FY 1399 compared to a value of USD 233.23 million captured in the third quarter of the FY 1398, (see table 4.2, and figures 4.9 and 4.10).

**Figure 4.11:** Composition of Imports (share %) for the 3rd Quarter of FY 2020 (1399)




**Source:** NSIA/DAB staff calculation

**Figure 4.12:** Composition of Imports (share %) for the 3rd Quarter of FY 2019 (1398)




**Source:** NSIA/DAB staff calculation

## 4.6. External Debt:

Afghanistan's external debt stood at a value of USD 2,123.34 million at the end of third quarter of the FY 1399, recorded an increase of USD 45.53 million over its level at the end of the third quarter of the FY 1398, mainly on account of a rise in official borrowings.

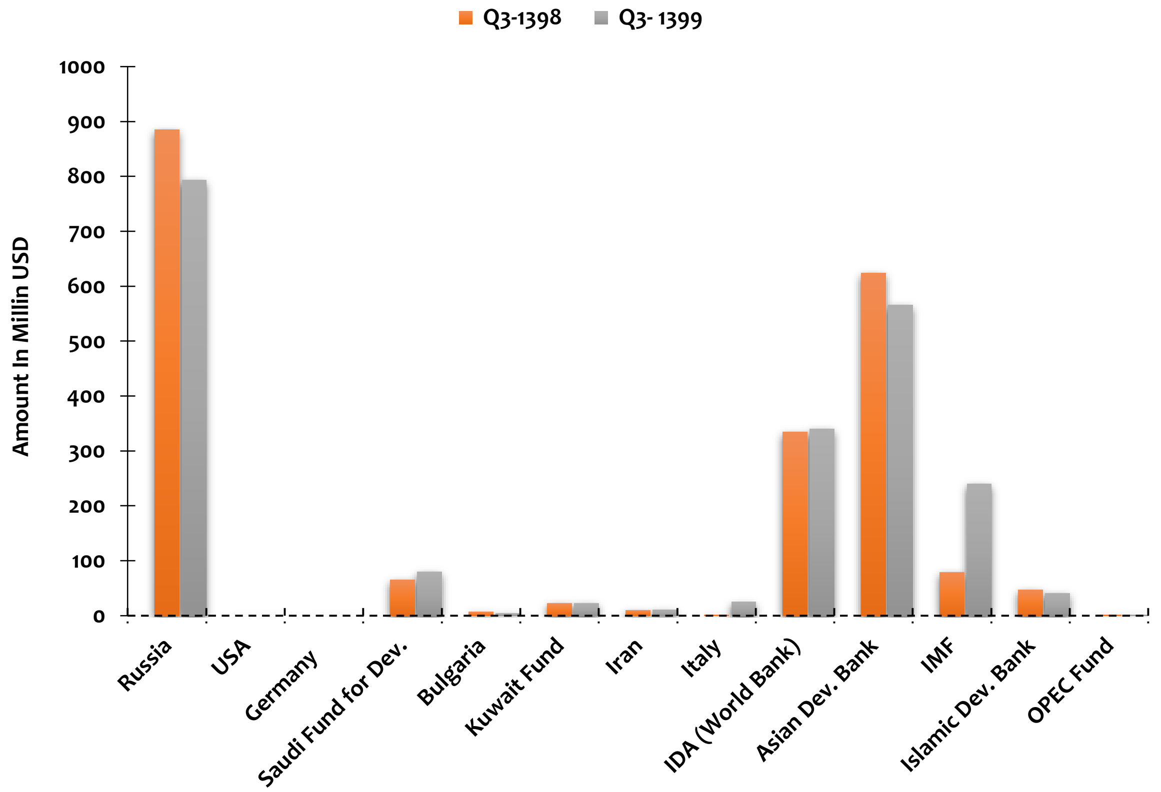
Considering the statistics, the total public external debts grew by 2% during the quarter under review (see figure 4.13). Loan principal repayments made to the Asian Development and Islamic development bank, while service charges were paid to the World Bank, Asian Development Bank and Islamic development bank. The World Bank, Asian Development Bank and International Monitory Fund (IMF) as a major multilateral creditor to Afghanistan made USD 2.52 million debt release on principles as well as USD 0.28 million as services charges during the quarter under review.

Bilateral loan is segregated into two parts: Paris club and Non-Paris Club creditors;

The total amount of loan payable to Paris Club creditors especially Russian federation stood at a value of USD 793.52 million at the end of third quarter of the FY 1399 from the amount of USD 885.46 million recorded in the same quarter of last year. Based on quarter-on-quarter comparison, it registered 6% decline to debt stocks to the mentioned creditor.

Compared to the third quarter of the last year, the total debt from Non-Paris Club members (Saudi Fund for Development, Bulgaria, Kuwait fund, Iran and Italy) rose by 35% to a value of USD 141.93 million in the third quarter of the FY 1399 from a value of USD 105.36 million recorded in the third quarter of the FY 1398. On the other hand, total debt from multilateral creditors to Afghanistan increased by 9% and stood at a value of USD 1,187.90 million in the third quarter of the FY 1399 from a value of USD 1,086.99 million recorded in the third quarter of the FY 1398 which shown USD 100.90 million increase in the total debt during the quarter under review.

**Figure 4.13:** External Debt Comparison for the 3rd Quarter of FY 2019 (1398) & 2020 (1399)




**Source:** NSIA/DAB staff calculation

## 4.7. Net International Reserves:

**The foreign International reserves include four items;** monetary gold, reserve position in the fund, SDRs (special drawing rights of the IMF) and foreign currency assets **accumulated by Afghanistan and controlled by the central Bank of Afghanistan (Da Afghanistan Bank).**

The Afghanistan Net International Reserve (NIR) is measured as country Gross International Reserves (GIR) minus reserve related liabilities. At the end of the third quarter of the FY 1399 the level of country's GIR has steadily increased by 7% and stood at a value of USD 9,108.31 million from the amount of USD 8,522.23 million registered in the similar quarter of the previous year.

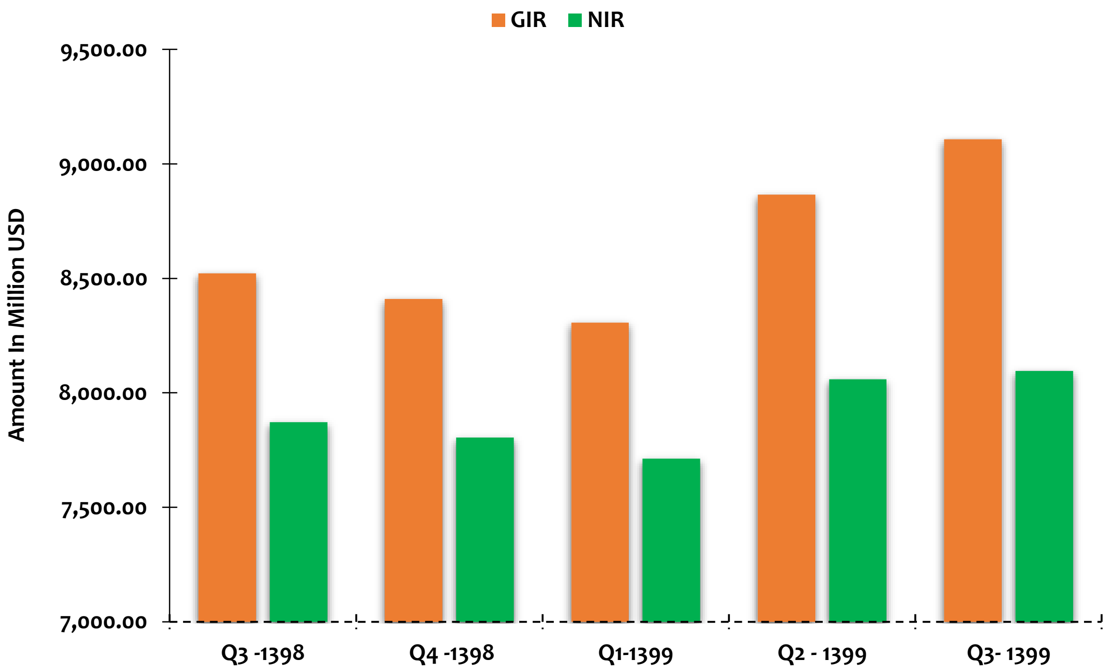
Based on the figure, the country GIR jumped by a record of USD 586.08 million during the quarter under review.

The NIR has also followed upward trend during the third quarter of the FY 1399 and surged to the value of USD 8,096.17 million from a value of USD 7,871.89 million recorded in the third quarter of the last year, it showed for about USD 224.28 million increments in the country's NIR (see figure 4.14). At the same time, Reserve related liabilities increased by 56% to a value of USD 1,012.14 million in the third quarter of the FY 1399 from a value of USD 650.34 million recorded in the third quarter of the FY 1398. The increment in reserve related liabilities was mainly due to insertion of foreign currency in commercial bank deposits with DAB which jumped up by 24% to a value of USD 734 million in the third quarter of the FY 1399 from a value of USD 592.37 million recorded in the similar quarter of the previous year.

The Use of Fund Resourced significantly increased to a value of USD 277.94 million in the third quarter of the FY 1399 from a value of USD 57.31 million recorded in the third quarter of the previous year. The reserve liability of nonresident deposits in foreign currency almost remained unchanged in the third quarter of the FY 1399.

The current position of Afghanistan Net International Reserves (NIR) is best cushion for conducting a sound and appropriate monetary policy in the country.

**Figure 4.14:** Gross and Net Internation Reserves during the past periods




**Source:** DAB staff calculations

**Table 4.1:** Afghanistan Balance of Payments in Million USD for the 3rd Quarter of FY 2020 (1399)

| Items / Years | Q2 - 98 | Q3 - 98 | Q4 - 98 | Q1 - 99 | Q2 - 99 | Q3 - 99 | % change |
|---|---|---|---|---|---|---|---|
| **Current Account** | -778.30 | -1028.38 | -708.35 | -946.42 | -414.33 | -893.51 | -13% |
| Credit | 1013.86 | 851.64 | 1280.46 | 815.50 | 857.16 | 1261.72 | 48% |
| Debit | 1792.16 | 1880.02 | 1988.81 | 1761.92 | 1271.50 | 2155.22 | 15% |
| **Goods and Services Account** | -1427.22 | -1438.50 | -1368.85 | -1250.12 | -1041.59 | -1662.61 | 16% |
| Credit | 283.90 | 344.64 | 516.73 | 399.73 | 146.63 | 380.24 | 10% |
| Debit | 1711.12 | 1783.14 | 1885.57 | 1649.85 | 1188.22 | 2042.85 | 15% |
| Goods Account | -1323.05 | -1252.91 | -1259.63 | -1177.43 | -960.89 | -1533.00 | 22% |
| Credit | 143.29 | 208.77 | 329.21 | 203.64 | 32.00 | 198.42 | -5% |
| Debit | 1466.34 | 1461.67 | 1588.84 | 1381.07 | 992.89 | 1731.42 | 18% |
| Services Account | -104.17 | -185.59 | -109.22 | -72.69 | -80.70 | -129.61 | -30% |
| Credit | 140.61 | 135.87 | 187.52 | 196.09 | 114.63 | 181.82 | 34% |
| Debit | 244.78 | 321.47 | 296.74 | 268.78 | 195.33 | 311.44 | -3% |
| **Primary Income Account** | 101.08 | 68.84 | 61.07 | 63.08 | 30.21 | 51.53 | -25% |
| Credit | 111.98 | 75.79 | 71.48 | 74.89 | 42.13 | 65.35 | -14% |
| Debit | 10.89 | 6.95 | 10.40 | 11.82 | 11.92 | 13.81 | 99% |
| **Secondary Income Account** | 547.83 | 341.27 | 599.43 | 240.62 | 597.04 | 717.57 | 110% |
| Credit | 617.99 | 431.21 | 692.26 | 340.88 | 668.40 | 816.12 | 89% |
| Debit | 70.15 | 89.93 | 92.83 | 100.26 | 71.36 | 98.55 | 10% |
| **Current transfers (Official grants)** | 432.9 | 233.1 | 497.7 | 177.4 | 513.7 | 585.7 | 151% |
| Credit | 432.91 | 233.13 | 497.7 | 177.4 | 513.7 | 585.7 | 151% |
| Debit | 0.00 | 0.00 | 0.0 | 0.0 | 0.0 | 0.0 | |
| **Personal transfers** | 145.36 | 142.51 | 139.87 | 95.91 | 107.71 | 176.74 | 24% |
| Credit | 185.08 | 198.08 | 194.51 | 163.50 | 154.75 | 230.38 | 16% |
| Debit | 39.72 | 55.57 | 54.64 | 67.59 | 47.04 | 53.64 | -3% |
| **Capital account** | 241.57 | 391.57 | 504.68 | 48.21 | 107.17 | 109.53 | -72% |
| Credit | 241.57 | 391.57 | 504.68 | 48.21 | 107.17 | 109.53 | -72% |
| Debit | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | |
| **Capital transfers** | 241.57 | 391.57 | 504.68 | 48.21 | 107.17 | 109.53 | -72% |
| Credit | 241.57 | 391.57 | 504.68 | 48.21 | 107.17 | 109.53 | -72% |

| Items / Years | Q2 - 98 | Q3 - 98 | Q4 - 98 | Q1 - 99 | Q2 - 99 | Q3 - 99 | % change |
|---|---|---|---|---|---|---|---|
| Debit | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | |
| Financial account | 27.9 | 59.0 | 10.9 | -147.50 | 346.99 | 100.42 | 70% |
| Direct investment | -6.28 | 9.04 | -1.55 | 2.91 | -0.4 | 5.2 | -42% |
| Net acquisition of financial assets | 5.69 | 4.86 | 5.26 | 6.10 | 2.59 | 10.00 | 106% |
| Net incurrence of liabilities | 11.97 | -4.18 | 6.81 | 3.19 | 3.02 | 4.78 | -214% |
| Portfolio investment | 15.42 | -33.74 | 20.16 | -18.20 | 41.19 | 83.11 | -346% |
| Net acquisition of financial assets | 15.42 | -33.74 | 20.16 | -18.20 | 41.19 | 83.11 | -346% |
| Net incurrence of liabilities | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | |
| Other investment | -9.42 | -72.99 | 124.26 | -22.54 | -290.93 | -9.74 | -87% |
| Assets | -23.13 | -17.86 | 89.24 | -38.22 | -74.09 | -0.24 | -99% |
| Liabilities | -13.71 | 55.14 | -35.02 | -15.67 | 216.84 | 9.50 | -83% |
| Reserve Assets | 28.13 | 156.66 | -131.94 | -109.67 | 597.16 | 21.84 | -86% |
| Net errors and omissions | 565 | 696 | 215 | 751 | 654 | 884 | 27% |

**Source:** NSIA and DAB staff calculations

**Table 4.2:** Merchandise Trade in Million USD for the 3rd Quarter of FY 2020 (1399)

| Years | Q3- 1398 | | Q2 - 1399 | | Q3- 1399 | |
|---|---|---|---|---|---|---|
| | Total | Share (%) | Total | Share (%) | Total | Share (%) |
| Imports | 1,591.20 | 100% | 1,093.24 | 100% | 1,923.79 | 100% |
| Industrial supplies | 233.23 | 15% | 51.73 | 4.7% | 129.60 | 7% |
| Fuel and Lubricants | 266.85 | 17% | 242.33 | 22.2% | 300.46 | 16% |
| Consumer goods | 493.56 | 31% | 378.75 | 34.6% | 633.48 | 33% |
| Capital goods and other | 597.56 | 38% | 420 | 38.5% | 860.26 | 45% |
| Exports | 208.77 | 100% | 32.00 | 100% | 198.42 | 100% |
| Carpets & Rugs | 5.93 | 2.8% | 0.1 | 0.3% | 6.25 | 3.2% |
| Food Items | 89.91 | 43% | 12.96 | 40.5% | 55.52 | 28% |
| Leather & Wool | 5.70 | 3% | 0.08 | 0.3% | 8.61 | 4.3% |
| Medical seeds & others | 107.24 | 51.4% | 18.86 | 58.9% | 128.05 | 65% |
| Trade Balance | -1,382.43 | | -1,061.23 | | -1,725.37 | |

**Source:** NSIA and DAB staff calculations

**Table 4.3:** Direction of External Trade for the 3rd Quarter of FY 2020 (1399) (in Million USD)

| Country Name | Exports | % Shares | Imports | % Share | Trade Balance |
|---|---|---|---|---|---|
| Pakistan | 77.17 | 39% | 240.98 | 12.5% | -163.81 |
| India | 87.10 | 44% | 146.95 | 7.6% | -59.85 |
| Iran | 1.38 | 1% | 308.37 | 16% | -306.99 |
| Germany | 0.96 | 0.5% | 29.12 | 1.5% | -28.16 |
| China | 1.61 | 1% | 283.64 | 15% | -282.03 |
| England | 0.05 | 0.03% | 0.65 | 0.03% | -0.60 |
| Saudi Arabia | 1.94 | 0.98% | | 0.00% | 1.94 |
| United Arab Emirates | 5 | 3% | 47.14 | 2% | -41.92 |
| Turkey | 4.92 | 2% | 14.51 | 0.75% | -9.59 |
| USA | 0.77 | 0.4% | 10.20 | 1% | -9.43 |
| Common Wealth | 1.75 | 1% | 525.14 | 27% | -523.39 |
| Japan | 0.00 | 0.00% | 43.30 | 2.3% | -43.30 |
| Other Countries | 15.55 | 8% | 273.78 | 14% | -258.23 |
| Total | 198.42 | 100% | 1,923.79 | 100% | (1,725.37) |

**Source:** NSIA and DAB staff calculations

**Table 4.4:** Direction of External Trade for the 3rd Quarter of FY 2019 (1398) (in Million USD)

| Country Name | Exports | % Shares | Imports | % Share | Trade Balance |
|---|---|---|---|---|---|
| Pakistan | 101.52 | 49% | 215.67 | 14% | -114.15 |
| India | 79.53 | 38% | 119.84 | 7.53% | -40.31 |
| Iran | 2.86 | 1% | 311.89 | 20% | -309.03 |
| Germany | 2.20 | 1.1% | 24.14 | 1.52% | -21.94 |
| Common Wealth | 1.88 | 1% | 373.54 | 23.5% | -371.66 |
| China | 2.65 | 1% | 269.57 | 17% | -266.93 |
| United Arab Emirates | | 0% | 29.29 | 2% | -29.29 |
| Saudi Arabia | 0.99 | 0% | | 1.84% | -29.29 |
| Turkey | | | 12.15 | 0.76% | |
| Japan | | 0.00% | 53.34 | 3.35% | -53.34 |
| England | | 0.0% | 1.31 | 0% | -1.31 |
| USA | | 0.00% | 10.14 | 0.64% | -10.14 |
| Other Countries | 17.14 | 8% | 170.31 | 10.70% | -153.17 |
| Total | 208.77 | 100% | 1,591.20 | 102% | (1,400.57) |

**Source:** NSIA and DAB staff calculations

**Table 4.5:** External Debt for the 3rd Quarter of FY 2020 (1399) (in million USD)

| | Q2 1398 | % share | Q2 1399 | % share |
|---|---|---|---|---|
| Total external debt | 2,077.81 | 100.00 | 2,123.34 | 100.00 |
| 1- Bilateral | 990.81 | 47.69 | 935.44 | 44.06 |
| a- Paris Club: | 885.46 | 42.62 | 793.52 | 37.37 |
| Russian Federation | 885.46 | 42.62 | 793.52 | 37.37 |
| United States | | 0.00 | - | 0.00 |
| Germany | | 0.00 | - | 0.00 |
| b- Non-Paris Club: | 105.36 | 5.07 | 141.93 | 6.68 |
| 2- Multilateral | 1,086.99 | 52.31 | 1,187.90 | 55.94 |
| of which: IDA (World Bank) | 334.93 | 16.12 | 340.05 | 16.01 |
| Asian Development Bank | 624.47 | 30.05 | 565.97 | 26.65 |
| International Monetary Fund | 78.92 | 3.80 | 240.06 | 11.31 |
| Islamic Development Bank | 47.01 | 2.26 | 40.33 | 1.90 |
| OPEC Fund | 1.66 | 0.08 | 1.48 | 0.07 |

**Source:** MOF and DAB staff calculations

**Table 4.6:** Net International Reserves for the 3rd Quarter of FY 2020 (1399) (in million USD)

| Changes on the previous quarter | Q3 -1398 | % Change | Q2 - 1399 | % change | Q3- 1399 | % change |
|---|---|---|---|---|---|---|
| Net international Reserves (million US Dollar) | 7,871.89 | -0.21 | 8,059.46 | 4.51 | 8,096.17 | 2.8 |
| Reserve Assets | 8,522.23 | -0.09 | 8,865.41 | 6.73 | 9,108.31 | 6.9 |
| Reserve Liabilities | 650.34 | 1.33 | 805.95 | 35.54 | 1012.14 | 55.6 |
| Commercial bank deposits in foreign currency | 592.37 | 2.01 | 749.89 | 40.49 | 734.06 | 23.9 |
| Nonresident deposits in foreign currency | 0.66 | 1.31 | 0.14 | -0.06 | 0.14 | -79.1 |
| Use of Fund resources | 57.31 | -5.78 | 55.92 | -7.88 | 277.94 | 385.0 |
| Gross Intl. Reserves (in months of import) | 16.07 | | 24.33 | | 14.20 | |
| Net Intl. Reserves (in months of import) | 15 | | 22 | | 13 | |

**Source:** DAB staff calculation

# 5

# Fiscal Developments

# 5

# FISCAL SECTOR DEVELOPMENT

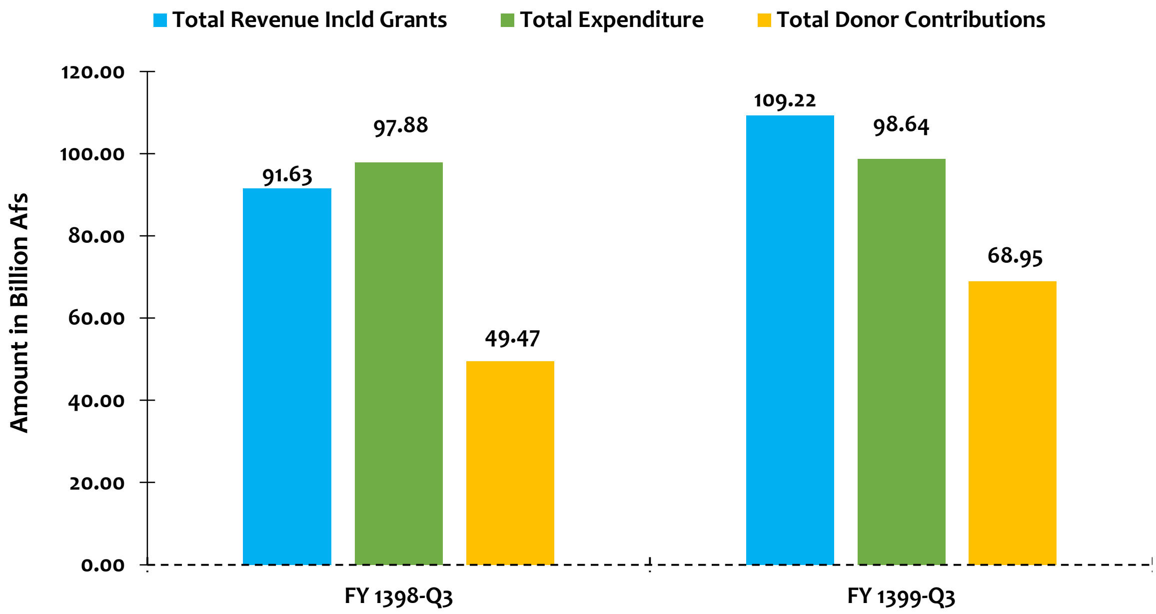
The key objective in the fiscal area is to achieve sustained increase in revenue collection and to permit the gradual takeover of externally financed operating & development spending and to ensure an expenditure allocation consistent with Afghanistan National Peace and Development Framework (ANPDF). The other goals include improvements in public expenditure management, fiscal policy formulation, efficiency in public enterprises, taxes and customs administration. Resembling other emerging and under developing economies around the world Afghanistan continuously faces budget deficit. Total core expenditures exceeded total domestic revenue in the third quarter of FY 1399 leading to Afs 0.76 billion budget deficit, and by including other revenue (grants) a budget surplus of Afs 10.58 billion is observed comparably and it is due to huge increase in revenue from donor contributions and foreign loans. Total domestic revenue is decreased from Afs 42.16 billion in third quarter of FY 1398 to Afs 40.27 billion in third quarter of FY 1399, which shown a decrement of Afs 1.9 billion or 4.50% in domestic revenue collection. Meanwhile decrease in employees spending, capital expenditure, subsidies, grants and loan contributions and pension expenditures resulted to decline the total core expenditure from Afs 98.6 billion in third quarter of FY 1399 to Afs 97.88 billion in third quarter of FY1398, that shows decrease of Afs 0.76 billion or 0.78% in third quarter 1399.

**Table 5.1:** Actual and Estimated budget for the 3rd Quarter of FY 1398 and 1399

| National Budget (Amounts in billion Afs) | | | |
|---|---|---|---|
| | **Estimated FY- 1399** | **Actual Q2 FY- 1399** | **Actual Q3 FY-1399** |
| **Total Expenditures** | 449.41 | 103.72 | 98.64 |
| **Operating** | 295.63 | 69.36 | 65,96 |
| **Development** | 153.78 | 34.36 | 32,68 |
| **Total Revenue** | 401.28 | 83.26 | 109.22 |
| **Internal Sources** | 175.80 | 39.04 | 40.27 |
| **External Sources** | 225.48 | 44.22 | 68.95 |
| **Budget Deficit/Surplus** | 48.13 | -20.46 | 10.58 |

**Source:** MoF Financial Statement/MPD Staff Calculation

**Figure 5.1:** Comparison of Total Revenue including donor contributions, Total Expenditure, Total donor contributions between 3rd Quarter of FY 1399 & FY 1398




**Source:** MoF Financial Statement/MPD Staff Calculation

Donor contributions are used to finance both operating and development expenditures. The total donor contributions (grants and loans) allocated to operating and development expenditures represented a considerable increase to Afs 68.95 billion in the quarter under review from Afs 49.47 billion in the same quarter of the 1398, indicating an increase of Afs 19.49 billion or 39.39% in the level of donor contributions.

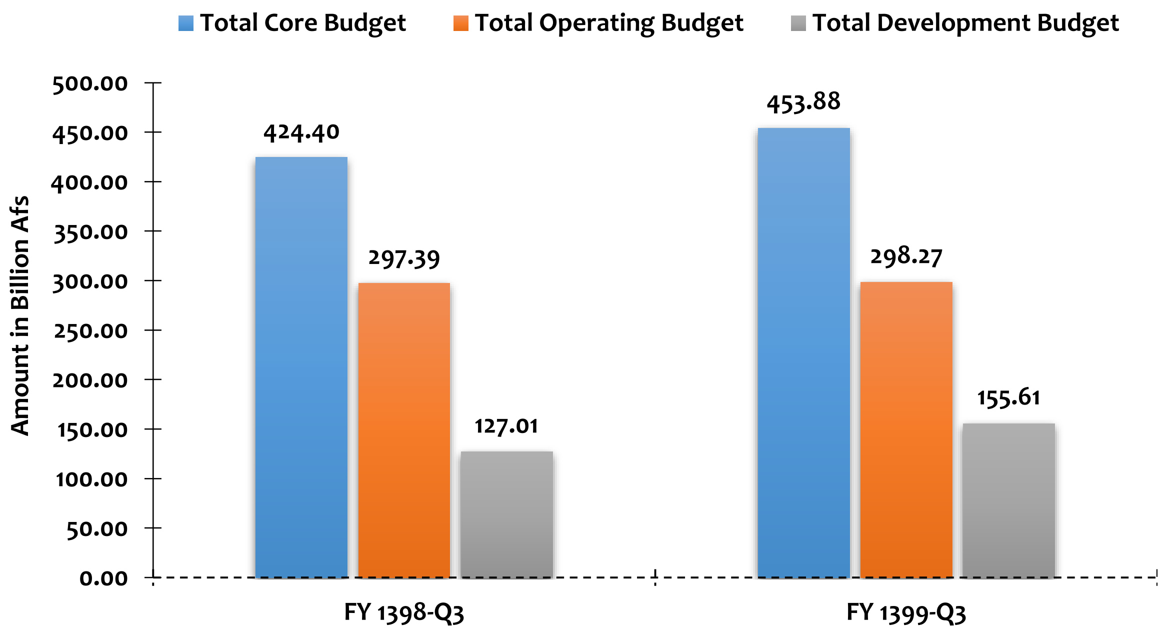
The increase is as a result of change in annual pledge, commitment and disbursement in which the main donor contributors are for ARTF, LOTFA, CSTC-A. Furthermore, total core budget is increased to Afs 453.88 billion in the third quarter of FY 1399 from AFN 377.19 billion in the third quarter of FY 1398, showing a vital increase of Afs 29.48 billion (6.9%) in total core budget.

Moreover, operating budget is increased from Afs 297.39 billion in the third quarter of FY 1398 to Afs 298.27 billion in the third quarter of FY 1399, indicating 0.3% increase. Similarly, development budget is increased to Afs 155.61 billion in the third quarter of FY 1399 from Afs 127.01 billion in the same quarter of the previous year, representing 22.5% increment that shows a significant change relatively.

## 5.1. Budget Execution Rate:

During the reference period, government spent 55% of Afs 471 billion (Approved budget) in FY 1399 comparing with 61% execution rate from approved budget of Afs 446.47 billion in FY 1398, which represents a decrease of 4.4% in total core budget. This change is attributed to several factors particularly effect of covid-19 pandemic. The total annual core budget increased to Afs 453.88 billion in FY 1399 from Afs 424.40 billion in FY 1398, which represents 6.9% (Afs 17.59 billion) increase in annual budget (total core budget).

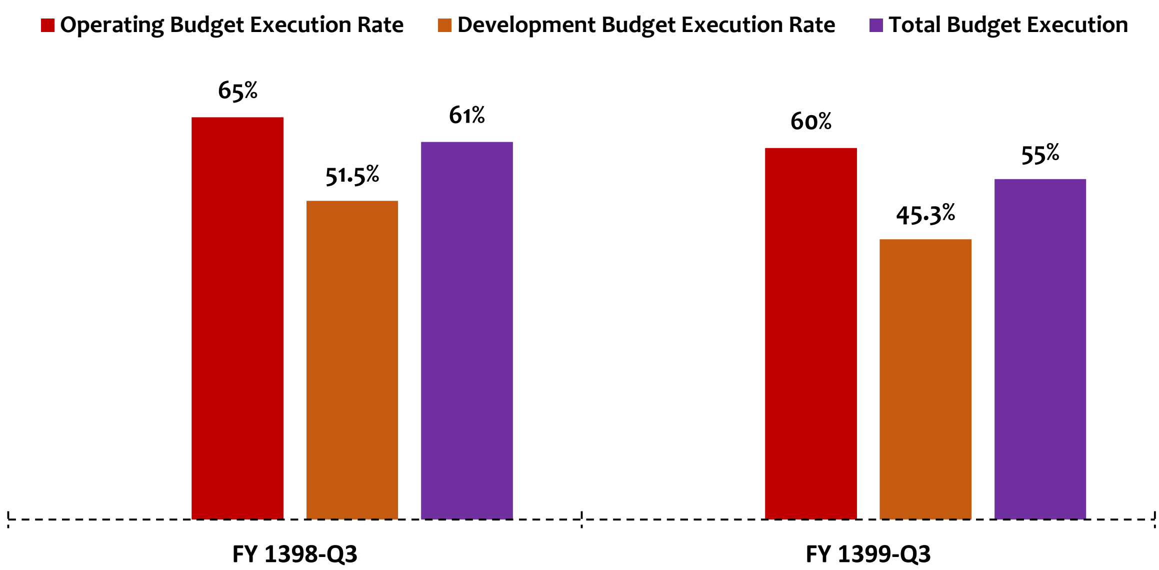
**Figure 5.2:** Comparison of Total Budget between 3rd Quarter of FY 1398 & FY 1399




**Source:** MoF Financial Statement/MPD Staff Calculation

Development budget execution rate evidently represents decrease of 3.7% from Afs 77.8 billion of 3rd quarter 1398 to Afs 74.99 billion in third quarter of FY 1399.

**Figure 5.3:** Comparison of Operating Budget & Development Budget Execution Rates for the 3rd Quarter of FY 1399 and FY 1398

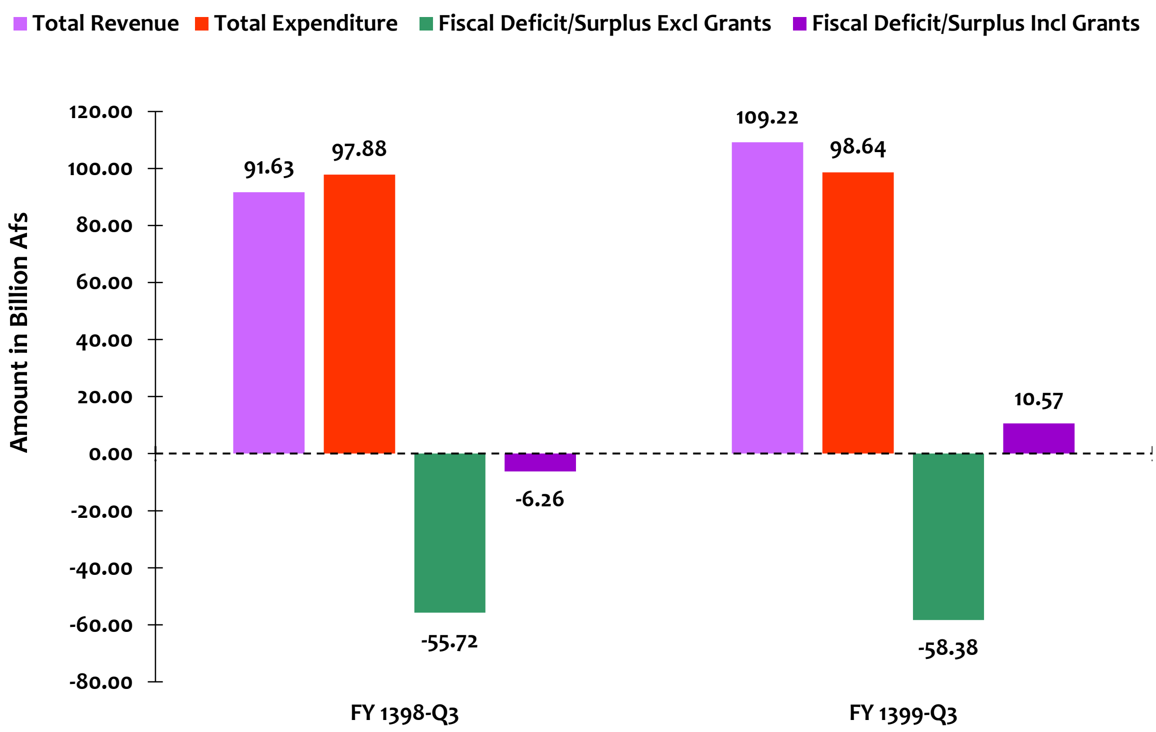



**Source:** MoF Financial Statement/MPD Staff Calculation

## 5.2. Core Budget (Deficit & Surplus):

The overall budget prior to donor's contribution had a deficit of Afs 58.38 billion in the third quarter of FY 1399 compared to Afs 55.72 billion deficit in the same quarter of the previous year, which is increased by Afs 2.66 billion that is equal to 4.7%. Meanwhile, donor contribution is increased to Afs 68.95 billion in the third quarter of FY 1399 from Afs 49.47 billion in the same quarter of the previous year. Total annual planned amount for external funding in FY 1399 represents an increase of 10.81% or Afs 21.9 billion (from Afs 202.8 billion in FY 1398 to Afs 224.76 billion in FY 1399) which is affected by commitment and disbursement in donor's contribution on annual basis.

**Figure 5.4:** Core Budget Deficit & Surplus (including & excluding donor contributions) for the 3rd Quarter of FY 1399 & 1398

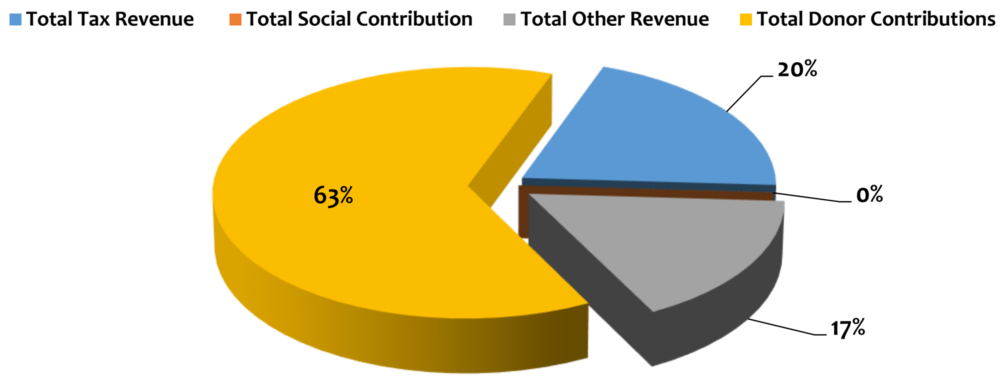



**Source:** MoF Financial Statement/MPD Staff Calculation

## 5.3. Total Revenue:

During the third quarter of FY 1399, total revenues including donor contributions increased significantly with total collection of Afs 109.22 billion from Afs 91.63 billion in third quarter of FY 1398, presenting increase of Afs 17.59 billion equal to 19% compared to same quarter of previous year. Annual collection of planned domestic sources indicates Afs 31 billion of decrement from Afs 208.9 billion in FY 1398 to 177.8 billion in FY 1399 leading to 14.9% decrease compared. To meet budget deficit total domestic revenue, donor contribution and foreign loans play a vital role. Moreover, the negative trend in total revenue collection for FY 1399 was as a result of momentous decrement in custom duties, revenue generated from income taxes, fixed taxes, sale taxes, tax penalties and fines and retirement contributions. However there had been improvement in collecting property taxes, administrative fees, miscellaneous revenue and sale of land and building during the third quarter of the fiscal year 1399.

**Figure 5.5:** Components of Total Revenue for the 3rd Quarter of FY 1399




**Source:** MoF Financial Statement/MPD Staff Calculation

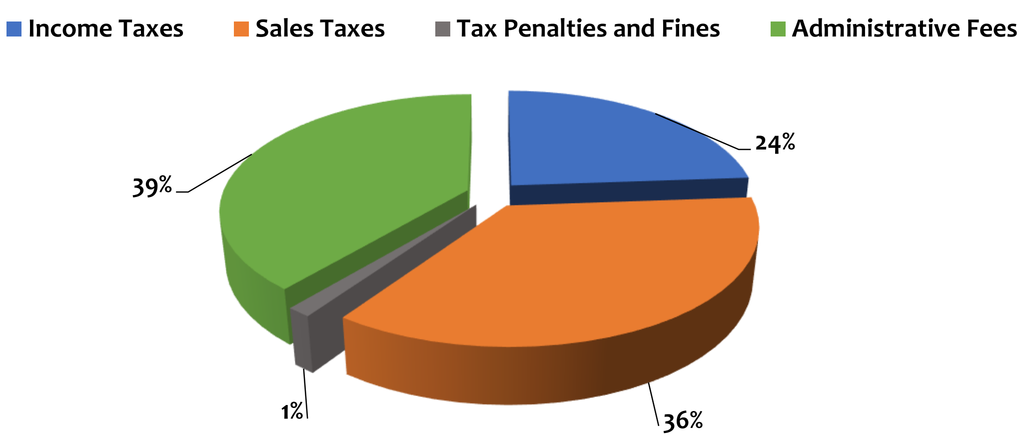
### 5.3.1. Domestic Revenue:

The total collection of domestic revenue is declined in the third quarter of fiscal year 1399 compared to third quarter of FY 1398. Measures taken by the government are not deemed to be sufficient to ensure the achievement in terms of the GDP deficit in FY 1399.

The decrement in domestic revenue collection was due to lower receipts from fixed Income tax, income tax, sale tax, administrative fees, retirement contribution and notable change in custom duties. Furthermore, breakdown of the total revenue collection showed a mild deceleration in various domestic revenue components such as fixed tax that showed a momentum decrease of 24.17% from Afs 3.65 billion in the third quarter of FY 1398 to Afs 2.77 billion in the quarter of under review.

Income tax shows decrease of 3.42% (from Afs 4.9 billion in the third quarter of FY 1398 to Afs 4.8 billion in the quarter under review), sales tax represents significant decrease of 19.12% (decreasing form Afs 8.95 billion in the third quarter of FY 1398 to Afs 7.24 billion in the third quarter of FY 1399), while custom duties show decrease of 41.97%, changing from Afs 12 billion in the third quarter of FY 1398 to Afs 7 billion in the third quarter of FY 1399 compared.

**Figure 5.6:** Major Components of Domestic Revenue for the 3rd Quarter of FY 1399

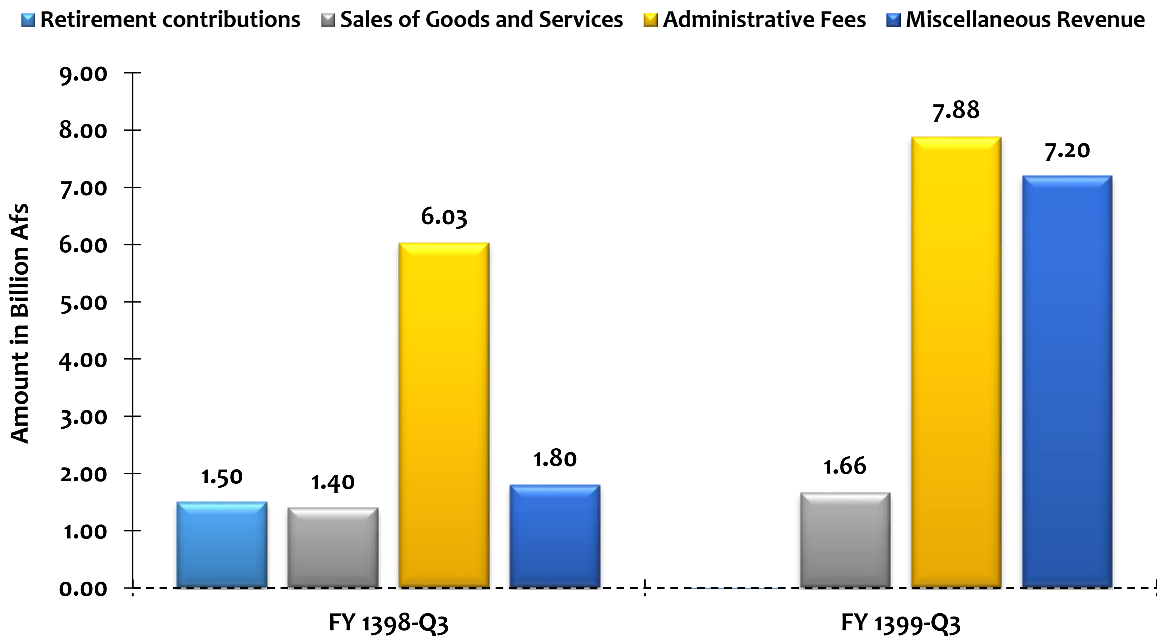



**Source:** MoF Financial Statement/MPD Staff Calculation

- **Non Tax Revenue:**

One of the initial component of domestic revenues is non-tax revenues that represents a notable increase of 55.5% from Afs 11.6 billion in the third quarter of FY 1398 to Afs 18 billion in the third quarter of FY 1399, which shows an increase of Afs 6.4 billion. This is largely as a result of miscellaneous revenue, change in sale of goods and services, and a notable change in administrative fees. The other components of the non-tax revenues are retirement contribution which is decreased from Afs 1.5 billion in the third quarter of FY 1398 to Afs -0.01 billion in the same period of the current year, indicated 100.8% decrement, while miscellaneous revenue increased from Afs 1.8 billion the third quarter of FY 1398 to Afs 7.2 billion in the third quarter of FY 1399, that signified 300.41% raise, on the other hand, administrative fees increased to Afs 7.88 billion in the third quarter of FY 1399 from Afs 6.03 billion in the same quarter of the previous year.

**Figure 5.7:** Major Components of Non-Tax Revenue for the 3rd Quarter of FY 1399 & FY 1398

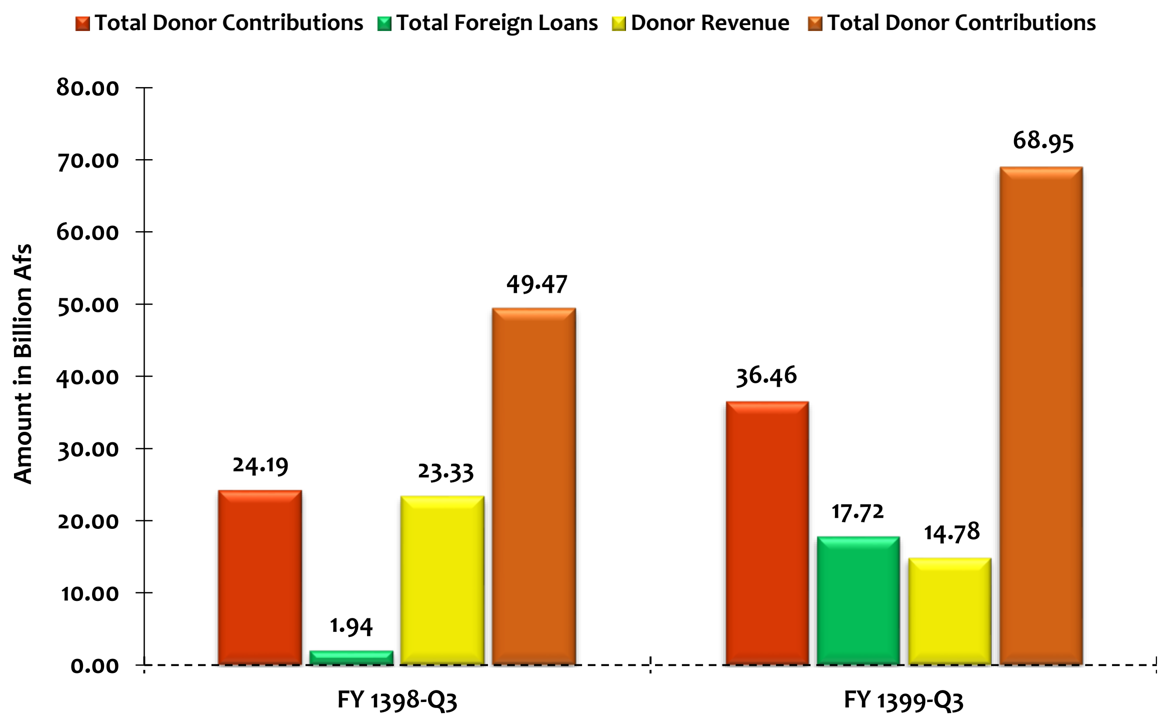



**Source:** MoF Financial Statement/MPD Staff Calculation

### 5.3.2. Grants and Loans:

Donor contribution forms an important part of the national budget, at the meantime donor contributions (grants and loans) finances major expenditure items in both operating and development budget. Government receives grants and occasional loans from various donors, trusts and international committees to finance variety of programs in both operating and development expenditures, Moreover, In Afghanistan's context, fiscal sustainability is defined as the ability of the government to finance its domestic expenditures without making any stark changes in the fiscal policy e.g. the total domestic expenditure it should be financed by total domestic revenue where recently it is being financed partially by external sources and rest by domestic revenue.

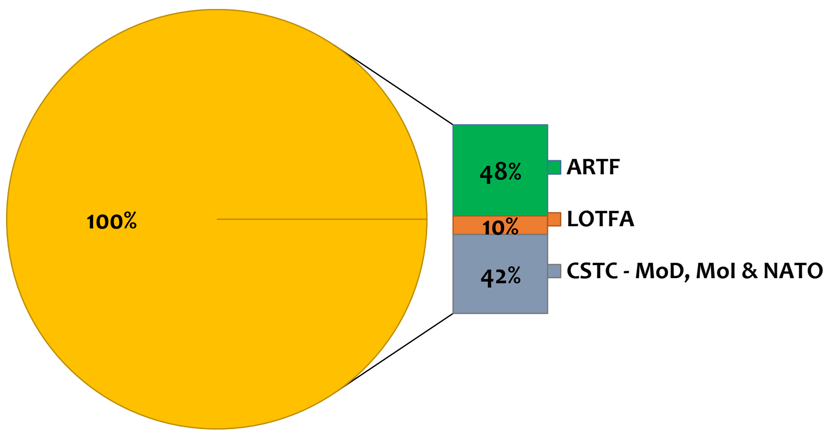
**Figure 5.8:** Analysis of Annual Donor Contributions (Grants and Loans) for the 3rd Quarter of FY 1399 & 1398




**Source:** MoF Financial Statement/MPD Staff Calculation.

Total development and operating grants and loans show significant increase of Afs 19.49 billion from Afs 49.47 billion in the third quarter of FY 1398 to Afs 68.95 billion in the third quarter of FY 1399, which clearly indicates substantial increase of 39.39%.

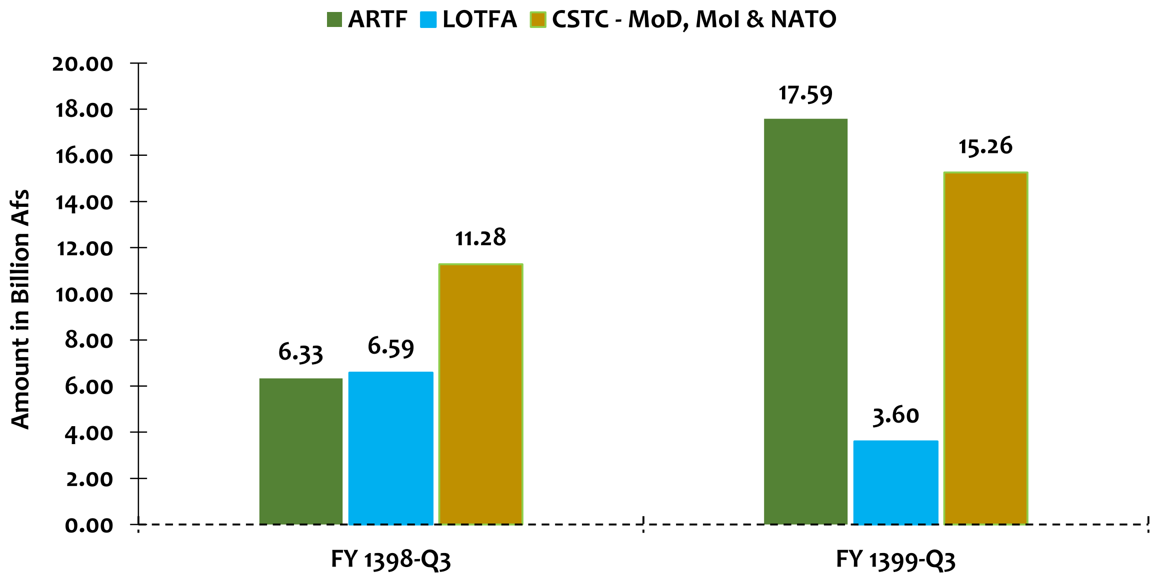
**Figure 5.9:** Components of Donor Contribution for the 3rd Quarter of FY 1399




**Source:** MoF Financial Statement/MPD Staff Calculation.

Combined Security Transition Committee – Afghanistan CSTC-A (MoD, MoI & NATO) aid is raised by 35% from Afs 11 billion in the third quarter of FY 1398 to Afs 15 billion in the third quarter of FY 1399, while LOTFA contribution was Afs 6.5 billion in the third quarter of FY 1398 which is decreased to Afs 3.6 billion in the same quarter of the current year that showed 45% decrement.

**Figure 5.10:** Comparison of Donor Contributions for the 3rd Quarter of FY 1398 & FY 1399

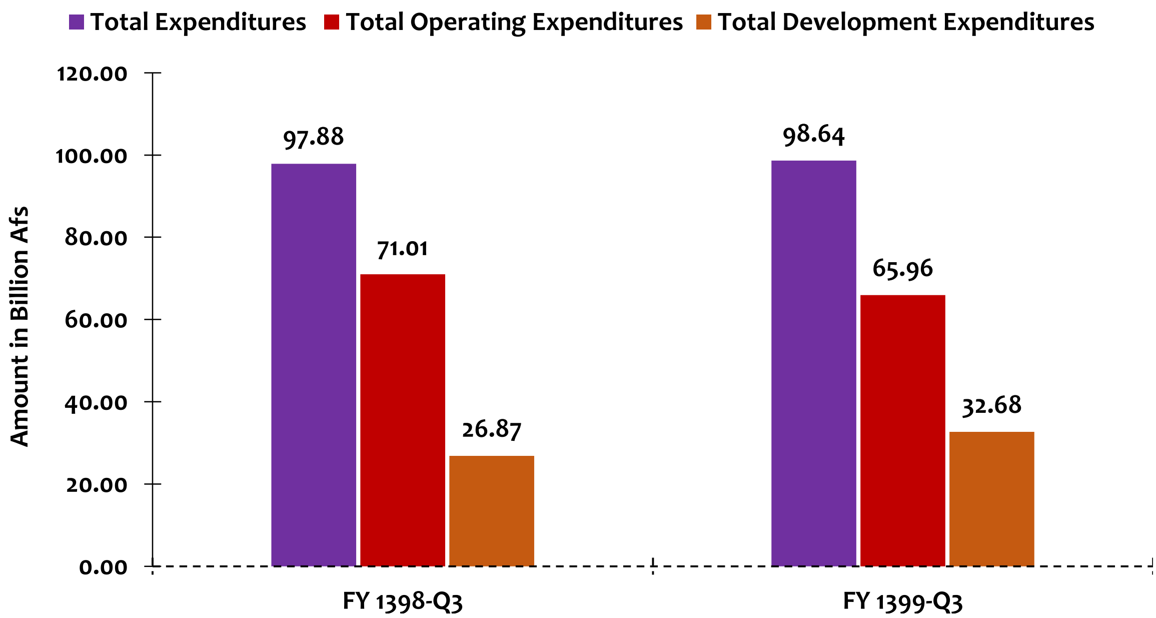



**Source:** MoF Financial Statement/MPD Staff Calculation

## 5.4. Expenditure:

Core expenditures are classified into development and operating expenditures which are allocated in eight different sectors such as security, governance, education, health, agriculture, social protection, infrastructure, and economic governance. Moreover, the sector wise expenditure is provided for both operating and development budget, while increase in expenditure on infrastructure, economic governance, and agriculture sectors are in line with Afghanistan National Peace and Development Framework (ANPDF) priorities.

**Figure 5.11:** Comparison of Total Expenditure between 3rd Quarter of FY 1398 & FY 1399




**Source:** MoF Financial Statement/MPD Staff Calculation

The total core expenditure presents 0.78% increase from Afs 97.88 billion in the third quarter of FY 1398 to Afs 98.64 billion in the third quarter of FY 1399, indicating Afs 0.76 billion increase in overall development and operating expenditure compare to same period of previous year. The increment is as a result of rise in development expenditures. In addition, operating expenditures decreased to Afs 65.96 billion in the third quarter of FY 1399 from Afs 71.01 billion in the same quarter of the previous year, which presented Afs 5.05 billion (7.11%) decrement in operating expenditures. Meanwhile development expenditure increased by 21.63%, changed from Afs 26.87 billion in the third quarter of FY 1398 to Afs 32.68 billion in third quarter of FY 1399, indicated Afs 5.81 billion increase in development expenditures. A small increase in overall expenditure is indicated due to increase in annual approved budget as well as due to increase in annual core expenditure.

# 6

# Banking Systems Performance

# 6

# BANKING SYSTEM PERFORMANCE

The banking sector making 21.7% of GDP comprises of twelve (12) duly licensed and permitted banking organizations, of which three (3) are re-licensed state owned banks, six (6) are private commercial banks, and there is one (1[7]) Islamic bank and two (2) are the branches of foreign banks.

The performance of the banking sector in the third quarter of FY 2020 is described below:
Overall the soundness indicators of the banking sector demonstrated increase to various degrees compared to previous quarter. Total assets, deposits and equity capital increased, Liquidity remained adequate, however, the quality of loans still remained low.

- Asset base of the banking sector increased by 0.84% in the quarter under review, reached to Afs 318.7 billion. The increase in total assets of the banking sector is mainly attributed to increase in total customer deposits and net profit of the banking sector.
- Total gross loan portfolio of the banking sector recorded a decrease of 0.26% in the third quarter of FY 2020, which stood at Afs 39.3billion. The decrease in total gross loans is mainly attributed to loans' settlement, charged off and less Over Draft utilization.
- Deposits being the main funding source in the banking sector and the major component of liabilities, comprising of interbank and customer deposits, stand at Afs 269.4 billion which show increase of Afs 1.7 billion (95.7% of the total liabilities). Deposits were largely denominated in USD (63.02%) with Afghani denominated deposits lagged at 34.92%, while deposits in other currencies lagged at 2.06%. Afs-denominated deposits indicated 4.18% increase, while USD denominated deposits declined by 1.78% in the quarter under review.
- The capital base of the banking sector remained adequate and increased by 1.04% or Afs 384 million, which was as a result of profitability. Capital adequacy ratios of all banks were above the set limit and the overall banking sector Capital Adequacy Ratio was 26.81%. The Basel benchmark is 8%.
- The banking sector was profitable during the quarter under review, though it decreased compared to previous quarter which was attributed to decrease in non-interest income; interest income as well as increase in operating cost. Return on Assets (ROA) and Return on Equity (ROE) decreased in the quarter under review and stood at 0.21% and 1.81% respectively. Group wise banks ended with profit in the third quarter.

[7] In the banking sector bulletin Islamic bank is a part of private banks.

## 6.1. Assets of The Banking System:

The assets size of the banking sector increased by 0.84% in the third quarter of FY 2020 against 11% increase in the second quarter of FY 2020 (see Table 6.1). The increase in total assets mainly attributed to deposits and profitability. This increase in total assets mainly reflected in DAB capital notes, investment & All other assets.

The most important components of the system's total asset portfolio were cash in vault and claims on DAB, interbank claims, net loans, investments, other assets & fixed assets with shares of 44.0%, 22.9%, 10.9%, 11.3%, 6.0%, and 3.3% in total assets respectively, see table 6.1.

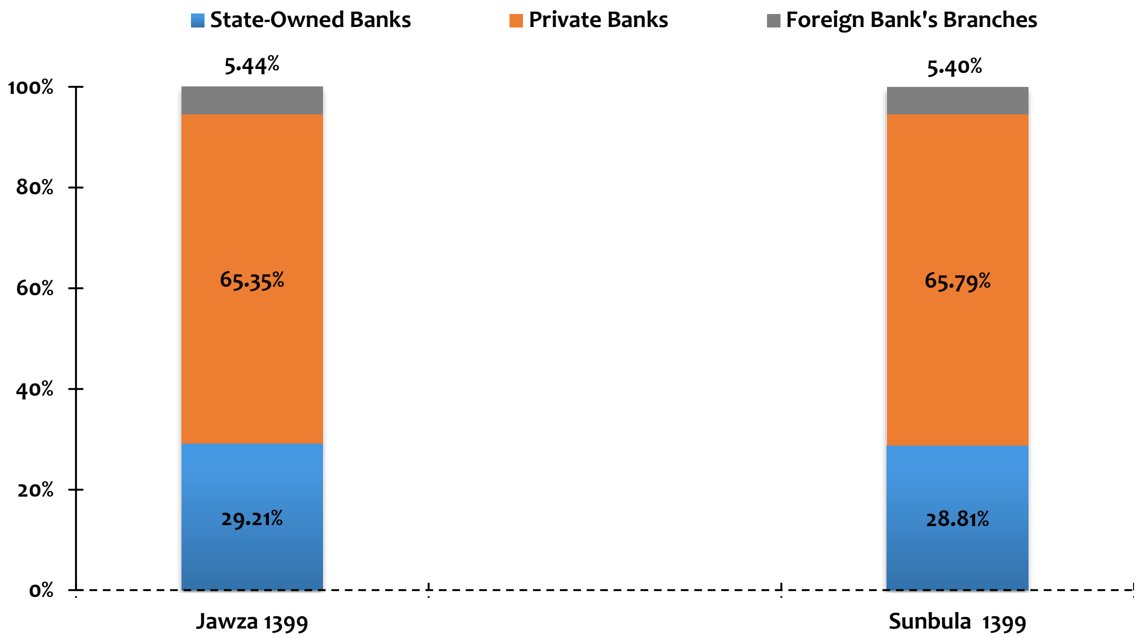
Private Banks are the leading player in the banking sector accounting for 65.8% of total banking sector assets (Islamic bank makes 6.9% of the sector total assets) followed by State-owned banks with 28.8% share in the market, while branches of foreign banks held 5.4% of the total assets.

**Table 6.1:** Assets of the banking system for the 2nd and 3rd Quarters of FY 2020 (1399)

| Description | Q2-2020 (Q2-1399 ) | Q3-2020 (Q3-1399 ) | % of Total Assets/Liability | Growth |
|---|---|---|---|---|
| **Assets** | **Amount in million Afs** | | | |
| Cash in vault and claims on DAB | 141,078 | 140,341 | 44.0% | -0.5% |
| Interbank claims(Net) | 74,043 | 72,987 | 22.9% | -1.4% |
| Investments (Net) | 33,798 | 36,024 | 11.3% | 6.5% |
| Loans (Net) | 34,903 | 34,872 | 10.9% | 0.09% |
| Intangible assets | 900 | 864 | 0.3% | -3.9% |
| Un- consolidated investment | 3,080 | 3,080 | 1.0% | 0.0% |
| Repossessed Assets | 1,019 | 1,016 | 0.3% | -0.3% |
| Fixed Assets | 10,417 | 10,448 | 3.3% | 0.3% |
| Others (Net) | 16,870 | 19,120 | 6.0% | 13.3% |
| **Total** | 316,106 | 318,751 | 100.0% | 0.8% |
| **Liabilities** | | | | |
| Deposits | 267,730 | 269,417 | 96% | 0.6% |
| Borrowings | 3,989 | 3,885 | 1% | -2.6% |
| Other | 7,488 | 8,166 | 3% | 9.06% |
| **Total** | 279,207 | 281,468 | 100% | 0.8% |
| **Financial Capital** | 36,899 | 37,283 | | 1.04% |

**Source:** Banking Supervision Department, DAB

**Figure 6.1:** Share of Banking Sector (Total assets) across the banking group for the 2nd and 3rd Quarter of FY 2020 (1399)

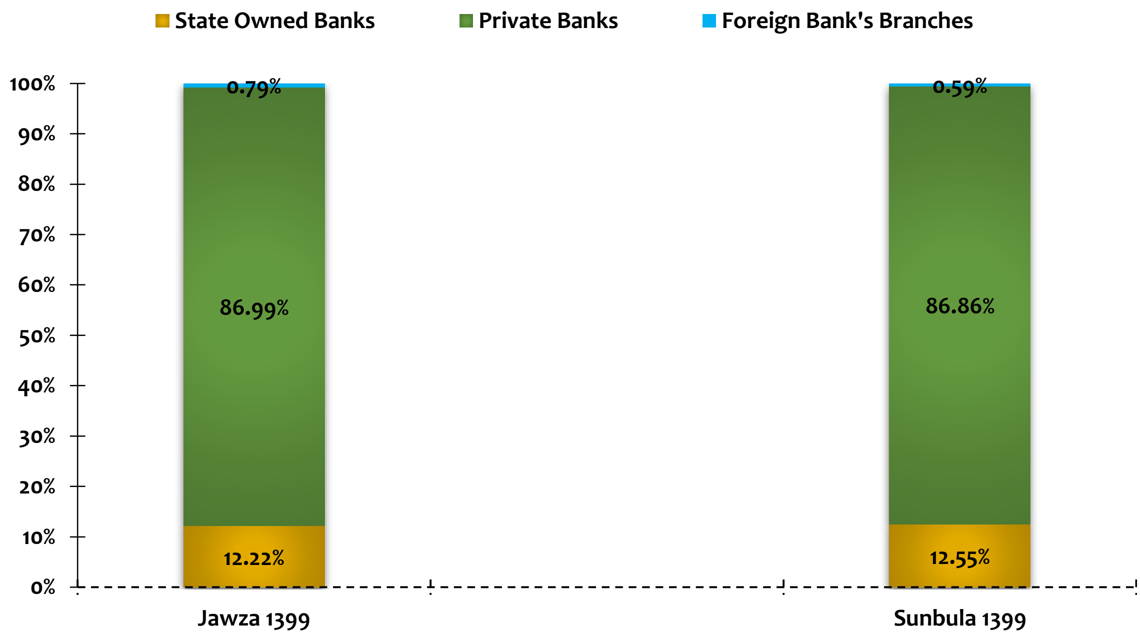



**Source:** Banking Supervision Department, DAB

### 6.1.1. Gross Loans:

Total gross loans portfolio of the banking sector at the end of September 2020 stands at Afs 39.36 billion, indicating Afs 0.102 billion or 0.26% decrease over the quarter, constituting 12.35% of the total assets and 2.68% of GDP. The decrease in total gross loans is mainly attributed to loan settlement, charged off & less OD utilization.

**Figure 6.2:** Share of Gross Loans Portfolio among banking group for the 2nd and 3rd Quarter of FY 2020 (1399)




**Source:** Banking Supervision Department, DAB

Three banking institutions recorded decrease in their loan portfolio. Disaggregated analysis among the banking groups shows that Private Banks with major share of 86.86% in the banking sector portfolio registered 0.4% decrease, State Owned banks with share of 12.55% of the total banking sector portfolio demonstrated 2.49% increase, while Branches of Foreign banks with 0.59% share in the banking sector loan portfolio showed 25.82% decrease in the quarter under review.

- **Loan Loss Reserve**

While assessing the level of credit risk, banks must give due attention to credit risk mitigation tools within their risk management 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. As per the Asset classification and provisioning regulation, the creation of reserve for standards loans is optional. By the end of the third quarter of FY 2020, total provision cover of the system was 11.42% of total gross loans as opposed to 11.57% recorded at the end of the second quarter of FY 2020.

- **Distribution of Credit:**

Breakup of gross loans across the various sectors indicates that some sectors are receiving greater credit while others witnessing a contraction. Noticeably loans disbursed to trade sector made 40.92% in the third quarter of FY 2020 against 41.44% in the second quarter of FY 2020. Disbursement of loans in Cement and other construction material items was 3.35% in the quarter under review against 3.86% of the previous quarter; other main sectors include: Services sector (25.72% against 25.30%) in which disbursement was mainly in telecommunications/scratch cards distributers (8.15%), Manufacturing and Industry sector (10.20% against 10.08%), Infrastructure Projects (8.87% against 9.05%), Commercial real estate and Construction sector (8.15% against 8.11%), Agriculture, livestock and farms sector (3.63% against 3.66%) and Consumer sector (2.51% against 2.35%). Increase were observed in four sectors such as Commercial Real Estate and Construction, Manufacturing and industry, consumer and services, while, trade, Agriculture and infrastructures projects sectors witnessed decrease.

Loans designated to Medium, Small and Micro sectors increased in the quarter under review, which is provided by 9 banking institutions (see figure 6.3). Concentration of loans to a few sectors of the economy would expose banks to credit risk in the event of crises situation associated to that sector, inversely affecting the overall banking sectors. About 74% of the loans were designated in Kabul while Balkh and Heart provinces are in the second and third places with Badghis and Kandahar provinces are at fourth and fifth places respectively.

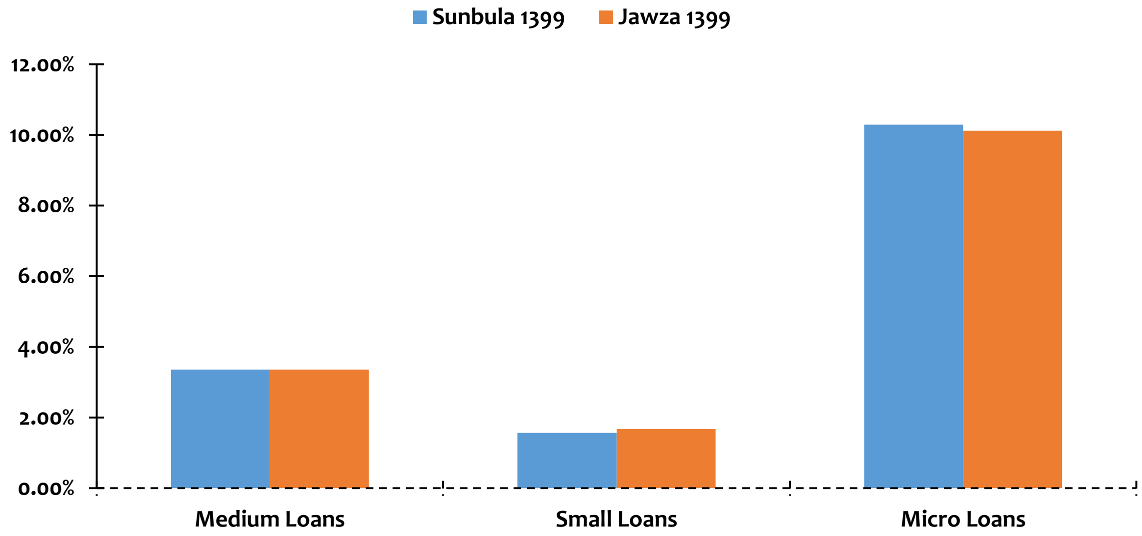
The proportion of loans in other provinces were negligible. The designation of loans by sector, geography and institution is not adequately diversified, but it is expected that over time the distribution of loans will improve. It is desirable that all banks take active part in lending, so as to diversify lending services and properly perform their role in financial intermediation.

**Table 6.2:** Distribution of credit sector wise for the 3rd Quarter of FY 2020 (1399)

| Sectors | Q4-2014 (Q4-1393) | Q4-2015 (Q4-1394) | Q4-2016 (Q4-1395) | Q4-2017 (Q4-1396) | Q4-2018 (Q4-1397) | Q4-2019 (Q4-1398) | Q3-2020 (Q3-1399) |
|---|---|---|---|---|---|---|---|
| **Commercial Real Estate and Construction** | | | | | | | |
| Construction and Buildings | 14.32% | 9.44% | 11.12% | 8.70% | 9.03% | 7.51% | 8.15% |
| **Infrastructure Projects** | | | | | | | |
| Power | 0.35% | 0.22% | 0.38% | 0.40% | 0.48% | 0.12% | 0.05% |
| Road and Railway | 2.41% | 1.17% | 0.64% | 1.32% | 2.18% | 2.84% | 2.69% |
| Dames | 0.61% | 0.09% | 0.04% | 0.00% | 0.36% | 0.38% | 0.39% |
| Mines | 0.08% | 1.48% | 0.52% | 0.48% | 0.52% | 0.49% | 0.47% |
| Other infrastructure projects | 1.81% | 2.44% | 2.44% | 3.46% | 3.28% | 4.92% | 5.27% |
| **Manufacturing and Industry** | | | | | | | |
| Manufacturing &Products of Metal wood plastic rubber leather paper | 2.48% | 4.42% | 3.47% | 2.67% | 4.10% | 5.38% | 4.24% |
| Manufacturing handmade and machine products | 4.19% | 4.24% | 3.74% | 3.16% | 3.67% | 3.63% | 3.84% |
| Cement and Construction Materials | 2.86% | 1.96% | 1.27% | 3.52% | 4.42% | 2.01% | 2.12% |
| **Trade** | | | | | | | |
| Textile | 2.59% | 0.52% | 0.72% | 1.54% | 2.21% | 1.90% | 1.71% |
| Wholesale | 4.93% | 9.89% | 4.34% | 4.67% | 3.62% | 4.74% | 5.51% |
| Machineries | 0.12% | 0.25% | 0.13% | 0.09% | 0.41% | 0.37% | 0.30% |
| Petroleum and Lubricants | 8.74% | 9.80% | 11.08% | 10.78% | 11.48% | 11.30% | 11.09% |
| Spare parts | 0.24% | 1.42% | 0.26% | 1.39% | 1.78% | 1.89% | 1.81% |
| Electronics | 1.40% | 1.58% | 1.91% | 2.76% | 3.21% | 2.66% | 3.35% |
| Cement and other construction Material | 1.87% | 2.73% | 2.35% | 2.57% | 5.14% | 3.99% | 3.35% |
| Food Items | 4.52% | 8.24% | 7.80% | 7.27% | 6.44% | 8.21% | 6.53% |
| All other Items | 5.72% | 3.47% | 4.17% | 3.28% | 7.92% | 6.36% | 4.48% |
| Retail trading | 3.92% | 3.28% | 7.31% | 8.15% | 3.13% | 2.94% | 2.77% |
| **Service** | | | | | | | |
| Education | 0.00% | 0.00% | 0.00% | 0.00% | 0.03% | 0.03% | 0.08% |
| Hotel and Restaurant | 1.20% | 1.46% | 1.33% | 2.04% | 2.16% | 2.44% | 2.53% |
| Telecommunication/Scratch cards Distributers | 2.92% | 5.70% | 5.96% | 5.52% | 5.98% | 6.57% | 8.15% |
| Ground Transportation | 4.87% | 5.31% | 4.86% | 1.86% | 3.08% | 4.13% | 5.18% |
| Air Transportation | 4.18% | 2.66% | 2.35% | 2.90% | 1.21% | 0.91% | 0.90% |
| Health and Hygienic | 0.71% | 1.16% | 1.42% | 1.73% | 1.74% | 1.66% | 1.73% |
| Media, Advertisements, Printer | 0.04% | 0.04% | 0.05% | 1.18% | 1.28% | 1.92% | 1.89% |
| All other Services | 6.19% | 11.36% | 13.22% | 12.26% | 5.07% | 4.50% | 5.27% |
| **Livestock and farms** | | | | | | | |
| Livestock and farming | 0.04% | 0.03% | 0.06% | 0.23% | 0.30% | 0.50% | 0.50% |
| **Agricultural Loans** | 2.61% | 2.67% | 3.20% | 3.94% | 3.86% | 3.07% | 3.13% |
| **Consumer Loans** | 0.26% | 0.30% | 0.65% | 0.86% | 1.90% | 2.63% | 2.51% |
| **Residential Mortgage Loans to Individuals** | 7.14% | 2.68% | 2.78% | 0.71% | 0.00% | 0.00% | 0.00% |
| **All Other Loans** | 6.68% | 0.00% | 0.43% | 0.57% | 0.00% | 0.00% | 0.00% |

**Source:** Banking Supervision Department, DAB

**Figure 6.3:** Shares of Small, Macro and Medium Loans as % age of total gross Loans for the 2nd and 3rd Quarter of FY 2020 (1399)




**Source:** Banking Supervision Department, DAB

- **Classification of Loans:**
  - **Non-performing loans[8]:**

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

Banks should closely monitor the potential risk associated with key sectors given the high Non-Performing Loans (NPL) ratio. Sectoral analysis of the NPLs shows that major portion of the NPLs originate from Trade sector (42.64%) with Cement & other construction material (8.43%) being the major item, also Services sector is in the second place with 20.12% of the sector NPLs, having ground transportation (8.71%) with highest share; Infrastructure projects sector with 16.43% of total NPLs is in third place, while, Commercial real estate & construction and Manufacturing & industry sector hold 13.19% and 6.58% of the sector NPLs respectively. Banking Supervision Department (BSD) is closely working with banks with poor loan performance to design and implement plans to improve their asset quality. This situation requires regulatory oversight and prompt remedial action to improve governance of credit risk to avoid negative impact over the profitability and capital adequacy of the banks with poor credit quality.

[8] Defaulted assets and advances for which the principal and/or interest is due and remains outstanding for 121-480 days and more as per the assets classification and provision regulation- (Doubtful and Loss).

- **Adversely-classified loans:**

Adversely classified loans (substandard, doubtful, Loss)[9] depicted Afs 98 Million decrease in the quarter under review. These loans require strong board oversight and remedial actions by management to reduce the level of Adversely Classified loans to an acceptable level.

In addition, more emphasis should be given on strengthening corporate governance in banks with poor credit quality, enhancing effectiveness and efficiency of internal controls, and adequately managing inherent and unsystematic risk. Management should take appropriate measures to address issues and weaknesses that have resulted in poor credit performance as per prudential regulations. Though systematic risk and economic downturn may have affected weak and systematically important bank's asset quality especially loans; however, banks management should have mechanisms to predict such risks, hedge their potential risk and take proper precautionary measures as per prudential regulations.

- **Loans classified Watch:**

Loans classified in the "watch"10 category amounted to Afs 4.2 billion, which makes 10.62% of total gross loans (decreased by 5.7% since last quarter). The decrease is mostly attributed to three banks in the system which came from repayment and deterioration (transfer to the lower classes) in the loan quality. This category of loans requires close monitoring as it may lead to more adversely classified loans (Substandard, Doubtful and losses) in the future.

- **Charged-off Loans[11]:**

Loans charged-off at the end of the third quarter of FY 2020 amounts to Afs 21.1 million which makes 0.05% of total gross loans. Charged-off loans are attributed to three banks.in the sector.

### 6.1.2. Interbank Claims:

Gross Interbank Claims are the second largest among various asset categories, currently comprising Afs 73.1 billion (22.94% of total assets) which show Afs 1.0 billion or 1.41% decrease since the second quarter of FY 2020. The decrease was mostly attributed to time deposit in two banking institutions. In the meantime, Afs placements increased which indicated that the banking sector has channeled a portion of its available funds to less interest earning assets in other banking institutions. Banks should not only appropriately measure risks associated with individual bank's but also country or countries in which they have placed funds (see figure 6.4).

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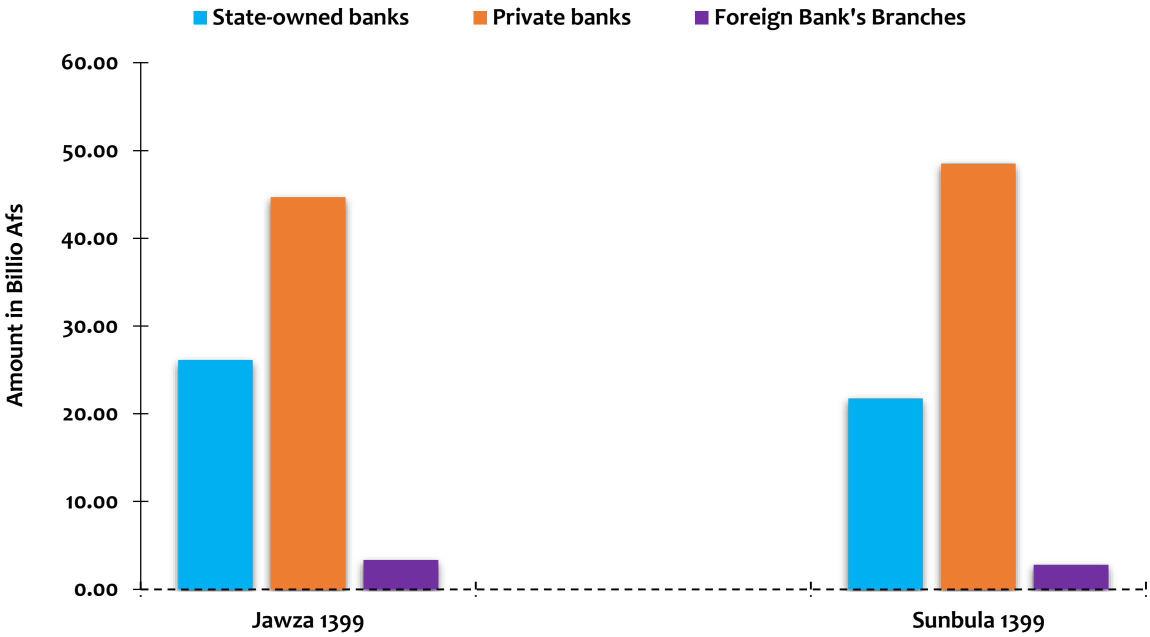
[9] An asset for which the principal and /or interest remains outstanding for 61-120 days - (Substandard), [9] Defaulted assets and advances for which the principal and/or interest is due and remains outstanding for 121-480 days - (Doubtful), An asset for which the principal and /or interest remains outstanding for 481 or more days - (Loss) as per the assets classification and provisioning regulation.

[10] An asset for which the principal and/or interest remains outstanding due for 31-60 days as per the assets classification and provisioning regulation-(Watch)

[11] Default assets and advances for which the principal and/or interest remains outstanding for 481 days or more days and retained on the books of banks for the period of 12 months (Loss), after 12 months they are immediately charged-off as per the assets classification and provisioning regulation.

**Figure 6.4:** Share of Inter-Bank Claims among banking groups for the 2nd and 3rd Quarter of FY 2020 (1399)




**Source:** Banking Supervision Department, DAB

### 6.1.3. Investment:

The net-investment[12] portfolio of the banking sector comprises of bonds, Government Securities, investment in associated companies which shows increase of 6.59% or Afs 2.2 billion from the second quarter of FY 2020, standing at Afs 36.0 billion or 11.30% of total assets and the increase mostly come from four banking institutions, attributed to new investments. Major part of the sector's investment took place outside Afghanistan, and investment portfolio is attributed to four commercial banks and a branch of foreign banks.

### 6.1.4. Cash in Vault and Claims on DAB:

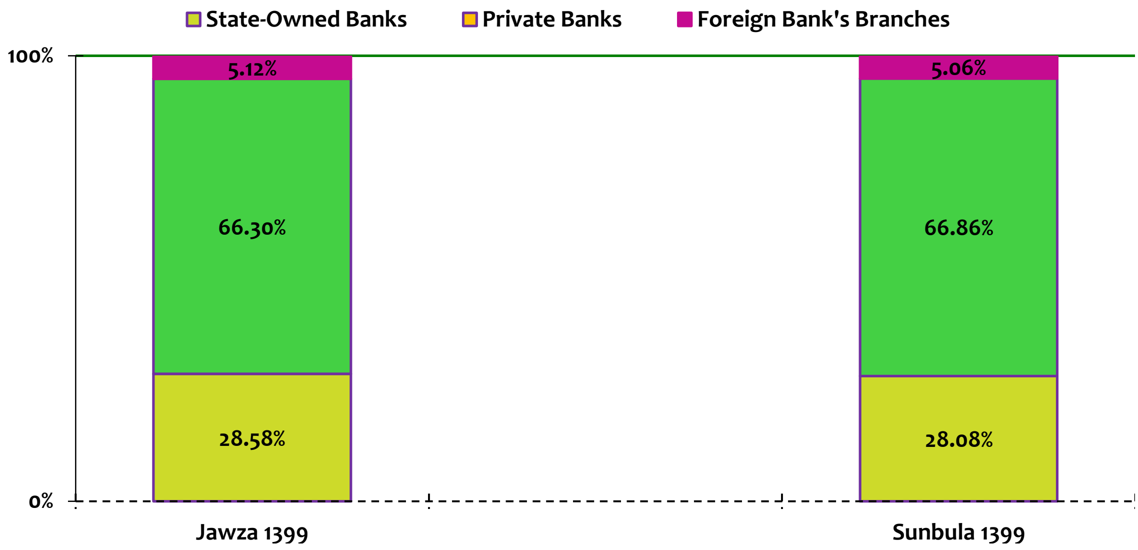
Cash in vault and claims on DAB remains the largest category making 44.03% of the total assets showing decrease of Afs 736.8 million during the third quarter of FY 2020 standing at Afs 140.3 billion. The decrease was observed in Correspondent Account with DAB and Overnight deposits account with DAB. Banking sector is fully compliant with required reserves regulations and is deploying slowly and prudently the attracted funds into other types of assets.

## 6.2. Liabilities:

Total liabilities of the banking sector increased by Afs 2.2 billion or 0.81% in the current quarter, stood at Afs 281.4 billion against Afs 279.2 billion in previous quarter of FY 2020. All components of total liabilities climbed in the quarter under review. The majority of liabilities are made up of deposits (95.72%), with "other Liabilities" at second and borrowings in third place (see table 6.1).

[12] Investments include investment in bonds, securities, associated companies and in subsidiaries.

**Figure 6.5:** Share of Liabilities among banking groups for the 2nd and 3rd Quarter of FY 2020 (1399)

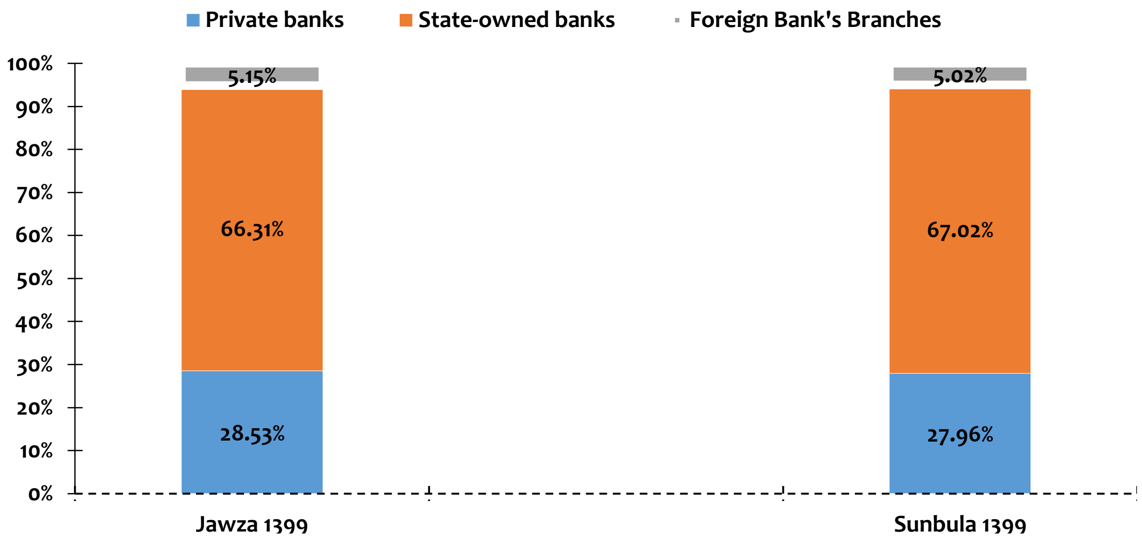



**Source:** Banking Supervision Department, DAB

### 6.2.1. Deposits:

Deposits being the main funding source in the banking sector comprising of interbank and customer deposits, amounts to Afs 269.4 billion during the quarter under review, which shows increase of Afs 1.7 billion or 0.63% Compare to the second quarter of the FY 2020. The total deposits cover Afs 4.83 billion interbank and Afs 264.59 billion customer deposits. The increase in deposit base of the banking sector is mainly attributed to customer time and savings.

**Figure 6.6:** share of Deposits among banking group for the 2nd & 3rd quarter of FY 2020 (1399)

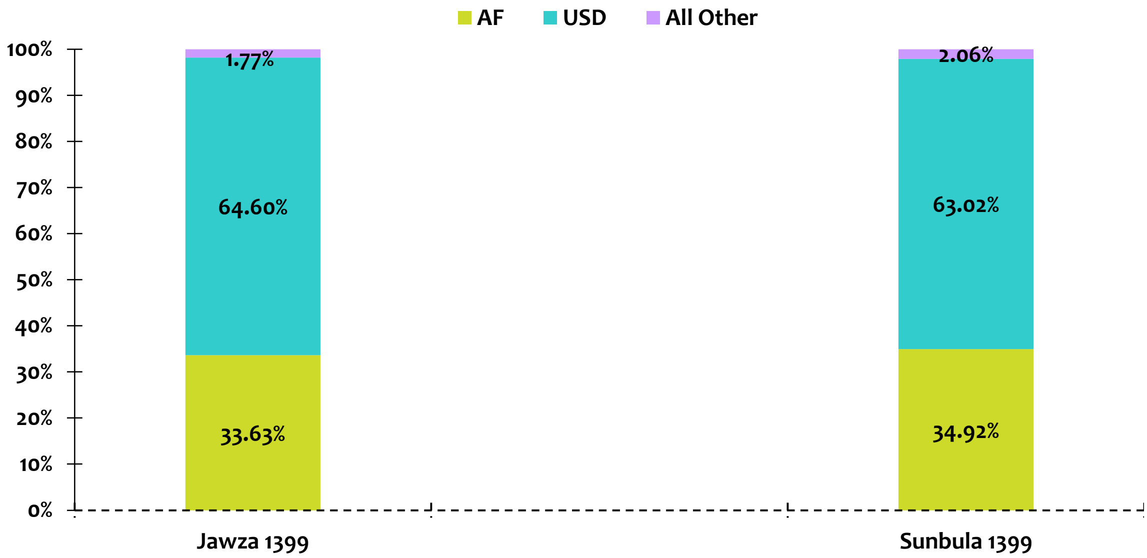



**Source:** Banking Supervision Department, DAB

Currency wise analysis shows that Afghani denominated deposits indicate 4.51% increase accounting for 34.92% of total deposits, while US dollar denominated deposits shows decrease of 1.84% making 63.02% of the total deposits of the system. Private Banks attracted Afs 180.5 billion deposits, which increased by 1.71% made up 67.02% of the system's total deposits. While, the share of state-owned banks were Afs 75.3 billion, decreased by 1.40% since June 2020 and accounted for 27.96% of the system's deposits.

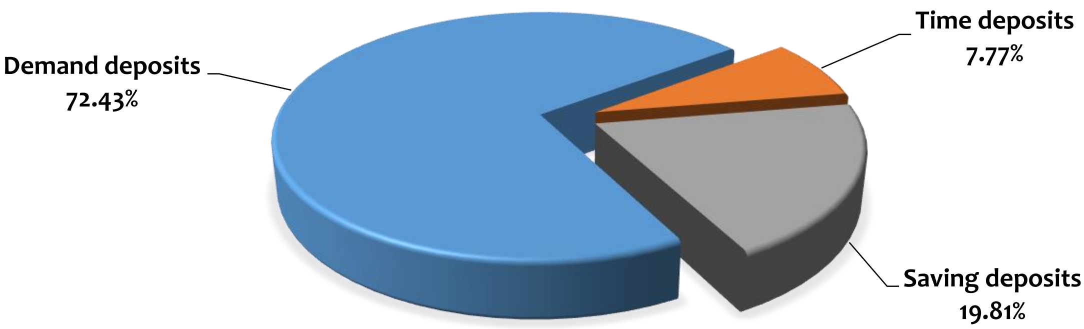
On the other hand, share of foreign banks' branches stood at Afs 13.5 billion which decreased by 2.06% made up 5.02% of total deposits of the system. In terms of types of deposits, demand deposits accounted for 72.43% of the total deposit base, decreased by 0.37% and saving deposits with 19.81% of total deposits was in the second place, and depicted 1.37% increase, while time deposit made up 7.77% of the total deposits portfolio increased by 8.80% since the second quarter of FY 2020.

**Figure 6.7:** Currency Composition of Deposits for the 2nd & 3rd quarter of FY 2020 (1399)




**Source:** Banking Supervision Department, DAB

**Figure 6.8:** Breakdown of Deposits for the 3rd Quarter of FY 2020 (1399)




**Source:** Banking Supervision Department, DAB

## 6.2.2. Borrowings:

The share of borrowings in total funding structure of the system decreased by 2.61% stood at Afs 3.88 billion at the end of the quarter under review, made 1.38% of total liabilities. The current borrowing position is attributed to four banking institutions.

## 6.3. 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 according to the policies of the bank.

### 6.3.1. Liquidity Ratio (broad measure):

Banks are required to maintain a liquid asset ratio not less than 15%. This should provide a comfortable safeguard against any liquidity shortfall. Generally, a surplus liquidity position was observed in the banking sector during the period, where 66.96% of the sector's total assets were comprised of liquid assets. Ratio of the broad liquidity as a median for the whole system stood at 60.18% and all banking institutions were well above the minimum required level (see table 6.3).

**Table 6.3:** Important ratios of the banking system for the 3rd Quarter of FY 2020 (1399)

| Ratio in% | Q4 2014 | Q4 2015 | Q4 2016 | Q4 2017 | Q4 2018 | Q4 019 | Q3 2020 |
|---|---|---|---|---|---|---|---|
| Total Capital Adequacy Ratio | 26.46 | 19.94 | 27.68 | 29.81 | 25.91 | 25.93 | 26.81 |
| Tier 1 Capital Adequacy Ratio | 26.09 | 19.66 | 22.93 | 28.17 | 24.56 | 24.50 | 25.96 |
| Return on Assets ( ROA) | 0.9 | 0.2 | 0.11 | 0.64 | 0.81 | 0.83 | 0.21 |
| Return on Equity ( ROE) | 7.35 | 1.69 | 1.08 | 3.38 | 6.91 | 7.24 | 1.81 |
| liquidity Ratio (Broad Measure Median) | 73.6 | 68.22 | 67.74 | 65.92 | 76.62 | 55.89 | 60.18 |
| liquid Assets to Total Assets | 73.28 | 75.05 | 71.98 | 73.95 | 72.88 | 68.63 | 66.96 |
| *ROA, ROE Sep, 2020 based on quarterly data | | | | | | | |

**Source:** Banking Supervision Department, DAB

## 6.4. Capital:

The system is well capitalized. The capital fund of the banking sector stood at Afs 37.28 billion, increased by 1.04% or Afs 384 million since the second quarter of FY 2020, and the increase in total financial capital is mainly attributed to profit of banking sector. On an aggregate basis the Capital Adequacy ratio of the banking sector stood at 26.81% (see table 6.3).

Disaggregated analysis shows that the financial capital of all banks are above the regulatory limits. The regulatory capital ratio of all banks is above the set regulatory threshold (12% of the risk weighted assets) and the Basel benchmark for capital to risk weighted is 8%.

## 6.5. Profitability:

For the quarter under review the banking sector earned Afs 504 million net profits which shown decrease as compared to previous quarter. The decrease was attributed to increase in Credit Provision, operating cost and decrease in Interest income & Non-interest income.

The return on assets (ROA) show how well a bank is being managed by conveying how much profit the bank earns per unit of its assets used. ROA of the banking sector stood at 0.21%, while the returns on equity (ROE) which measured shareholders return on their invested equity in a bank recorded at 1.81%. Deterioration in the return ratios were on account of decline in net income of the sector. The ROA of SOB[13] recorded at 0.97%, while PB[14] registered 1.21%, and BOFB[15] recorded 0.25% at the end of third quarter of FY 2020.

**Table 6.4:** Profit & Loss Schedule (P/L) for the 2nd and 3rd Quarter of FY 2020 (1399)

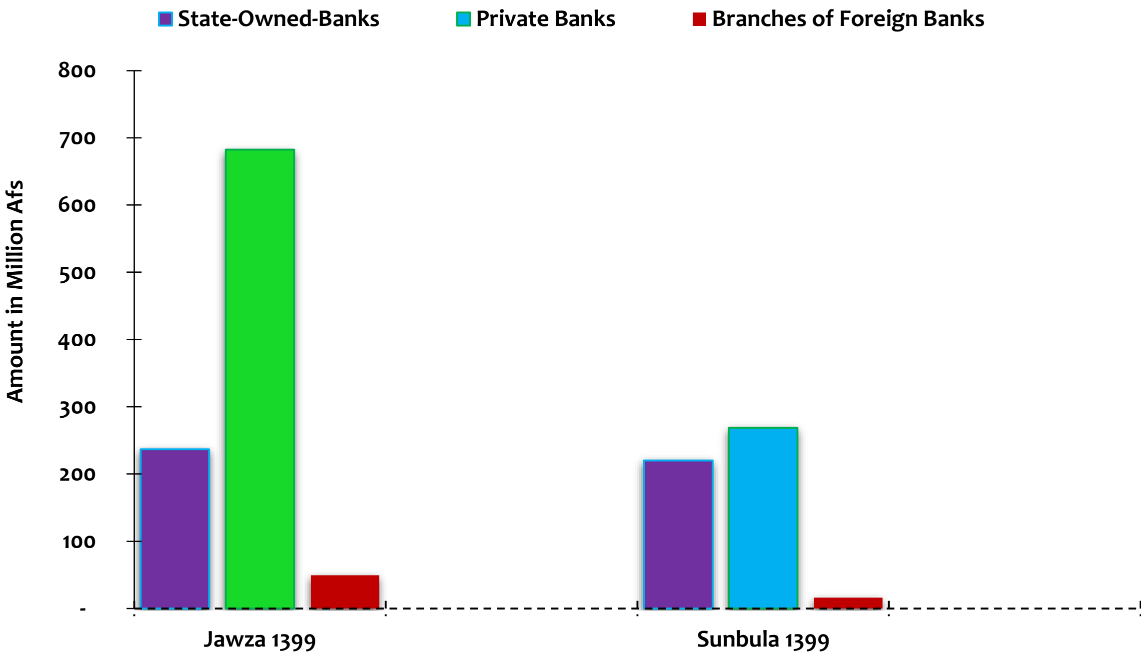
| Items | Q2-2020 (Q2-1399) | Q3-2020 (Q3-1399) | %change |
|---|---|---|---|
| | Amount in AFs | | |
| interest income | 1,642 | 1,594 | -2.89% |
| interest expense | 240 | 235 | -2.18% |
| Net interest income | 1,402 | 1,359 | -3.01% |
| Non-interest income | 2,072 | 1,694 | -18.26% |
| Non-interest expenses | 1,519 | 1,596 | 5.07% |
| Salary cost | 1,075 | 1,064 | -1.03% |
| Gain/Loss on Investments | (27) | 66 | -345.13% |
| Credit provisions | 27 | 107 | 301.37% |
| P/L before tax & FX revaluation | 826 | 353 | -57.29% |
| P/L After tax & FX revaluation | 968 | 504 | -47.93% |

**Source:** Banking Supervision Department, DAB

Group wise analysis revealed that State-Owned banks, Private Banks and foreign bank's branches ended up with profit for the quarter under review (see figure 6.11). Major portion of the profitability of the banking sector is attributed to private banks which recorded Afs 268 million, state-owned banks recorded profit of Afs 220 million and Branches of Foreign banks earned Afs 16 million profit during the quarter under review.

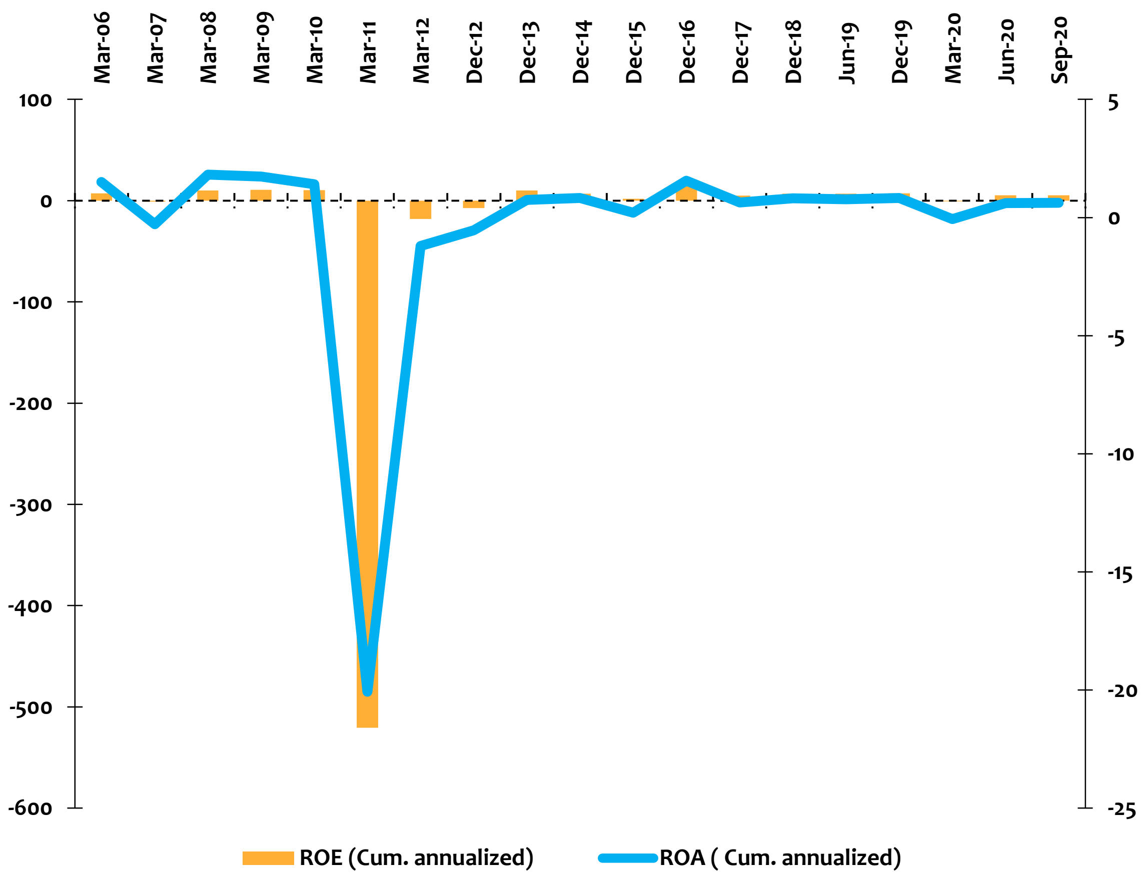
[13] SOB- Stated-Owned Banks
[14] PB- Private Banks
[15] BOFB- Branches of Foreign Banks

**Figure 6.9:** Profitability of the Banking Sector for the 2nd & 3rd Quarter of FY 2020 (1399)



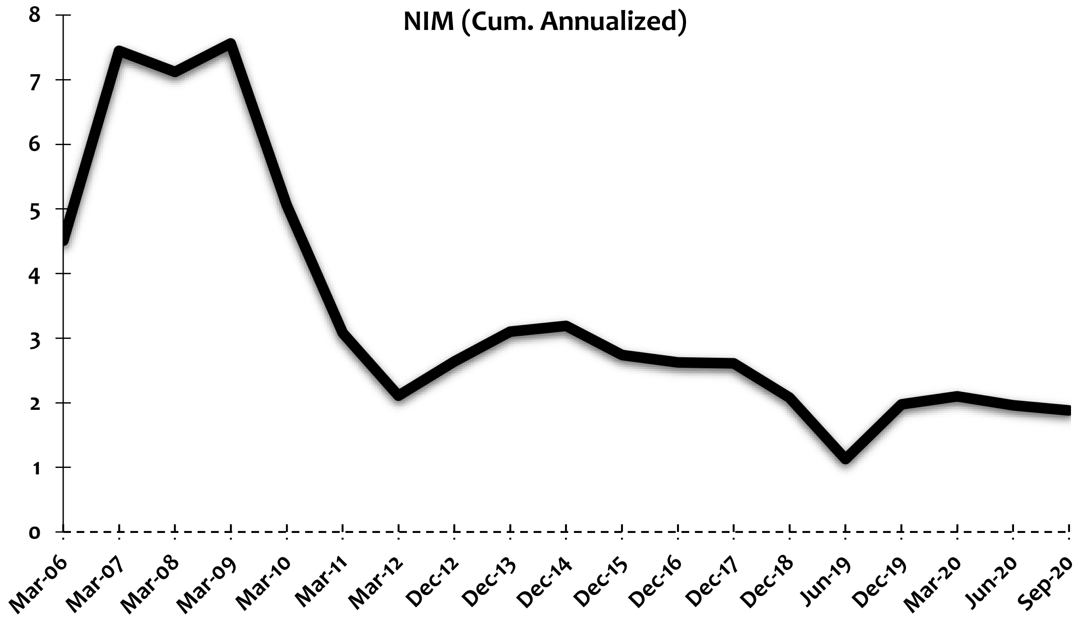

**Source:** Banking Supervision Department/ DAB

**Figure 6.10:** Return on Equity (ROE) and Return on Assets (ROA) of the Banks for the 3rd Quarter of FY 2020 (1398)




**Source:** Banking Supervision Department/ DAB

**Figure 6.11:** Net Interest Margin (NIM) for the 3rd Quarter of FY 2002 (1399)




**Source:** Banking Supervision Department/ DAB

## 6.6. Foreign Exchange Risk:

The level of overall open FX position risk being taken by banks was largely within the levels set by DAB. In general, all the banking institutions were within the limits set for the overall open FX position except for four banking institutions holding open FX positions on overall and on an individual currency (USD long position) basis violated the limits. Those banks need to bring their FX positions under the set limit; otherwise, depreciation (decrease in the value) of US dollar can lead the banks to more losses. The impact of change in exchange rate upon regulatory capital of the system reveals that a 20% appreciation in exchange rate would increase the regulatory capital of the system by Afs 2.7 billion and vice versa. Similarly, a 4% change would correspond to Afs 542 million and vice versa.

## 6.7. 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 revealed that the net-interest income of the system over the next 12 months may increase by Afs 240 million in the event of 3% increase in the market interest rate (upward interest rate shock). Conversely, if the interest rate decreases by 3% (downward interest rate shock) interest income will decline by Afs 240 million. For six banking institution, if the interest-rate increases by 3%, it will decrease their net interest income over the next 12 months.

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

## 6.8. ISLAMIC BANKING PERFORMANCE

In General, the Islamic banking sector performed well and its main financial indicators recorded a positive trend during the third quarter of FY 1399, as apparent from the increase in total assets, which was mostly due to increase in deposits. The equity capital of one full-fledged bank remained in stable level attributed to rise in the profitability along with adequate level of liquidity position and capital adequacy ratio of bank was above the set regulatory threshold.

There is no statutory requirement for Islamic banking windows of conventional banks to maintain a separate limit of equity capital, therefore equity capital of four windows out of six windows is negative. However, gross financing had downward trend due to settlement and FX variation and meanwhile new financing is taken place also. Investment has growth trend mainly due to new investment in Sukuk in foreign countries and Ijara inside the country.

The total assets of the Islamic banking sector during the third quarter of FY 1399, demonstrated 6.48% increase compared to the previous quarter which stood at Afs 39.44 billion at the end of the third quarter as compared to Afs 37.04 billion in the same preceding quarter. The increase in total assets mostly originates from increase in investment and interbank claims.

Deposits, which were the main source of funding in the Islamic banking sector witnessed 7% increase over the quarter under review and reported Afs 32.27 billion. The increase in total deposits was due to increase in the time, saving and demand deposits of the sector. Liquidity and FX positions of windows were in accordance with the benchmarks set by the central bank (20% Quick and 15% Broad Liquidity Ratios and ± 40% for overall FX position and ± 20% on individual currency position) on overall and individual currency basis (USD long position). On the other hand, the full fledge Islamic bank lies in violation of both FX limits set by Da Afghanistan Bank.

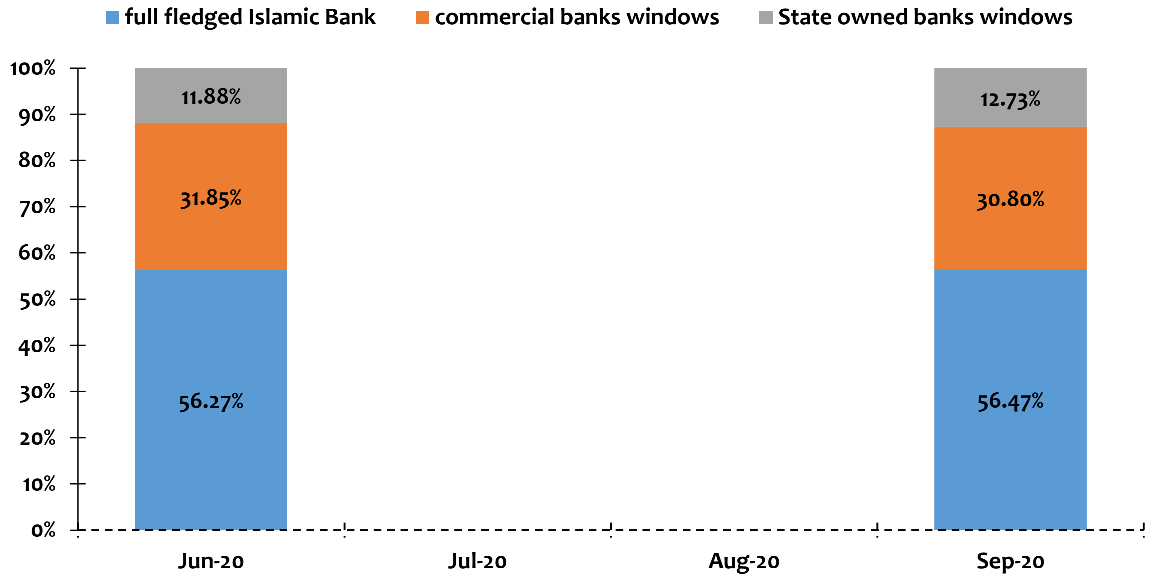
### 6.8.1. Total Assets:

The total assets of the Islamic banking sector registered growth of 6.48% in the third quarter of FY 2020 (1399), which stood at Afs 39.44 billion (USD 513.09 Million), while in previous quarter (June 2020) the total assets of the sector recorded 4.38% increase. The increase in total assets was mostly contributed by increase in total deposits of the sector during the quarter under review. The individually item wise analysis of total assets confirmed that the considerable increasing items were investment in Sukuk and Ijara and interbank claims, whereas the cash in vault and Murabaha financing showed slight decrease for the mentioned period.

The components of the Islamic banking sector assets portfolio were cash in vault and claims on DAB without interest (39.4%), interbank claims (10.17%), net Murabaha financing (9.85%), investment (Musharaka, Sukuk and assets acquired for leasing) was 30.13%, other assets (8.6%) and fixed and intangible assets made 1.8% of the total assets.

The full-fledged Islamic bank has leading share in the sector's total assets and was reported 56.5%; four Islamic windows of private commercial banks had second position with 31.3% shares and state-owned banks' Islamic windows made 12.7% of the sector's total assets. Looking at the increase in total assets across the sector, the 59.54% growth has taken place in full-fledged Islamic bank and remaining 40.45% reported in the assets of Islamic banking windows as compared to last quarter.

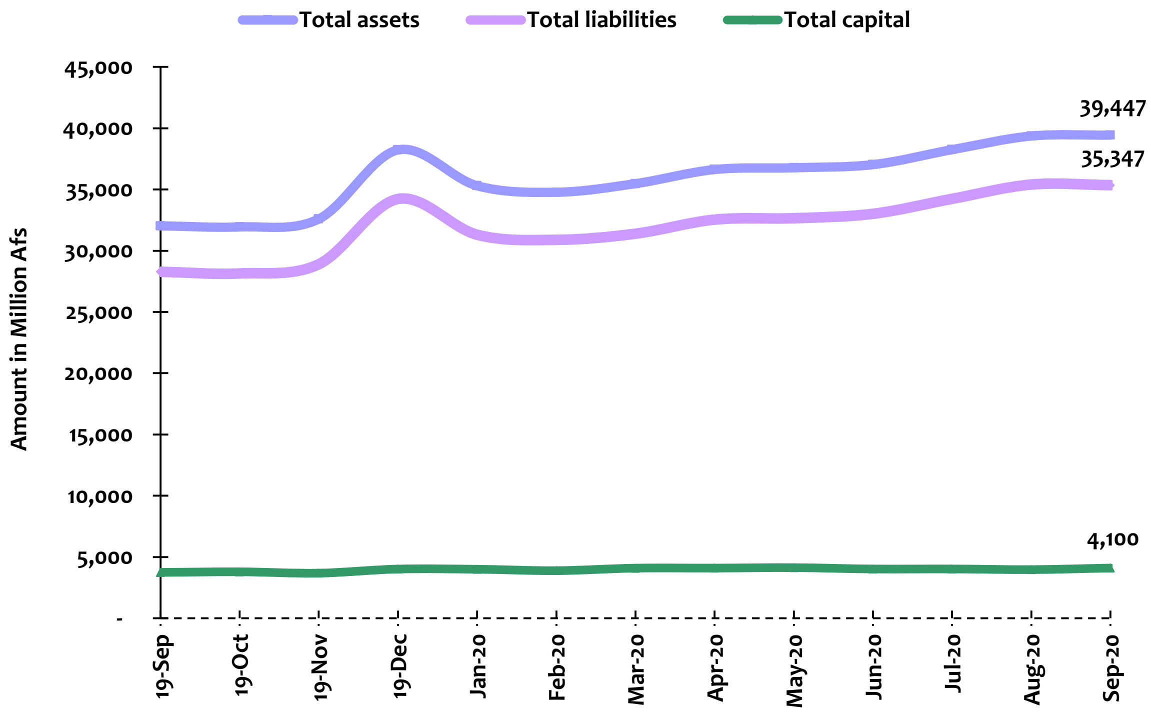
**Figures 6.12:** Percentage Share of full-fledged Islamic banks, commercial banks' Islamic window and state owned banks' Islamic window in Islamic banking sector Assets for the 3rd Quarter of FY 2020 (1399)




**Source:** Islamic Banking & Finance Department, DAB

The trend of assets of the Islamic Banking Sector from Sep 2019 to Sep 2020 is depicted in figure 6.13.

**Figure 6.13:** Trend of assets of the Islamic Banking Sector for the 3rd Quarter of FY 2020 (1399)




**Source:** Islamic Banking & Finance Department, DAB

**Table 6.5:** Assets, Liabilities and Capital of Islamic Banking Sector for the 3rd Quarter of FY 2020 (1399)

| Amount in million Afs | June-2020 | Sep-2020 | % of Total Asset/liabilities | Growth |
|---|---|---|---|---|
| **Assets** | | | | |
| Cash in vault and claims on DAB | 15,566 | 15,547 | 39.41% | -0.12% |
| Investment (Net) | 9,728 | 11,888 | 30.13% | 22.21% |
| Interbank claims(Net) | 3,737 | 4,013 | 10.17% | 7.39% |
| Financing (Net) | 3,935 | 3,887 | 9.85% | -1.22% |
| Other Asset (Net) | 3,343 | 3,395 | 8.6% | 0.11% |
| Intangible assets | 280 | 270 | 0.69% | -3.5% |
| Fixed Assets | 455 | 446 | 1.13% | -2.1% |
| **Total Asset** | 37,044 | 39,447 | 100% | 6.48% |
| **Liabilities** | | | | |
| Total Deposits | 30,161 | 32,272 | 91.3% | 7% |
| Borrowings | 1,162 | 1,157 | 3.27% | -0.37% |
| Other Liability | 1,187 | 1,918 | 5.42% | 13.68% |
| Total Liability | 33,009 | 35,347 | 100% | 7.08% |
| **Equity Capital** | 4,035 | 4,100 | | 1.63% |
| **Total Liabilities and capital** | 37,044 | 39,447 | | 6.48% |

**Source:** Islamic Banking & Finance Department, DAB

- **Gross Murabaha Financing and Investment (Sukuk):**

The gross Murabaha financing and investments (Sukuks and others) portfolio of the Islamic banking sector recorded increase of 14.5% over the third quarter of FY 2020 (1399) which stood at Afs 16.71 billion constituted 42.37% of the total assets, whereas at the end of second quarter it was Afs 14.59 billion and made 39.4% of total assets of the sector.

The breakup of total gross financing and investment of sector consists of investment in Sukuk Afs 7.79 billion which shows increase of Afs 1.11 billion or (17%), making 46.66% of total gross financing and investment. Murabaha receivables were Afs 4.81 billion that decreased by 0.9% and made 28.79% of total gross financing and investment, while assets acquired for leasing amounted to Afs 3.94 billion and showed 36.3% increase whichcovered23.58% of gross financing and investment. Diminishing Musharaka recorded Afs 111.01 million or 0.66% and constant Musharaka Afs 51.75 million during the third quarter of FY 2020 (1399).

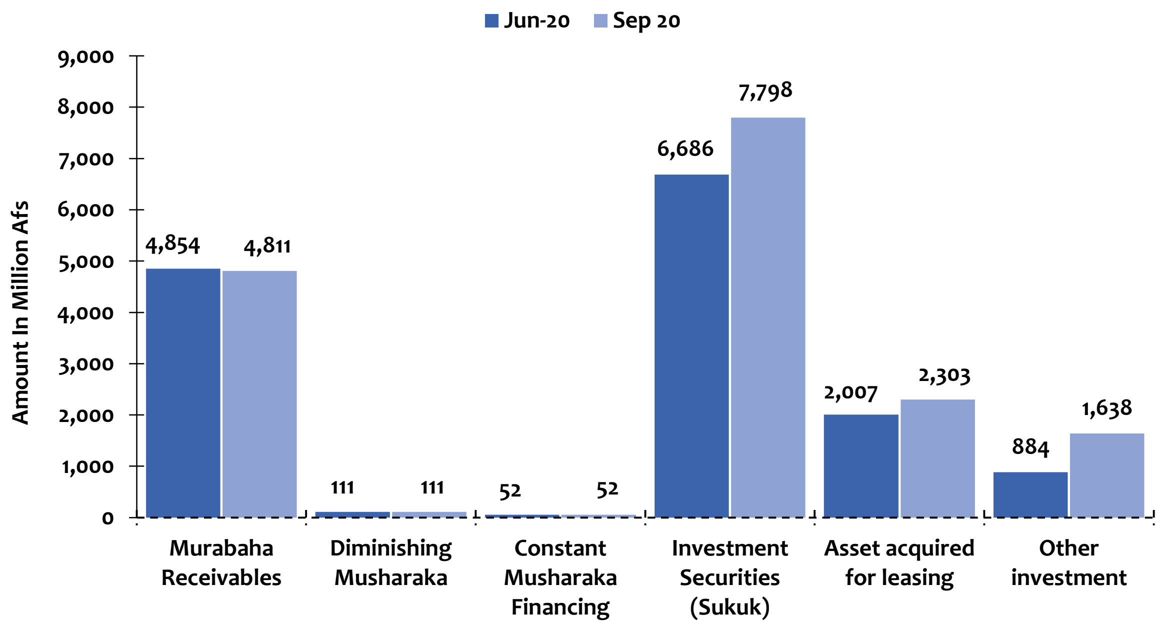
The increase in Gross Murabaha financing and investments has observed 6.65% in investment in Sukuk by full-fledged bank and by a window and 6.28% recorded in assets acquired for leasing by a window, meanwhile the Murabaha financing have been decreased. The increase in total investment portfolio is mainly due to new investment in Sukuk and Ijara and at the same time, settlement and instalment of Murabaha financing have been collected during the quarter. It is worth mentioning that one out of six Islamic banking windows has no financing and investment activities due to DAB restriction.

**Table 6.6:** Product wise Islamic Banking Sector Financing and investment (gross) for the 3rd Quarter of FY 2020 (1399)

| No | Product | June-20 | Sep-20 | Difference in Amount | Difference in % | Products as % of Gross Investment & Financing |
|---|---|---|---|---|---|---|
| | | Amount in million Afs | | | | |
| 1 | Investment in Sukuk | 6,686 | 7,798 | 1,111 | 17% | 46.66% |
| 2 | Murabaha Receivables | 4,854 | 4,811 | (43.5) | -0.9% | 28.78% |
| 3 | Asset acquired for leasing | 2,007.48 | 2,302.9 | 295.4 | 15% | 13.78% |
| 4 | Other investment | 884.37 | 1,638.38 | 754 | 85% | 9.8% |
| 5 | Diminishing Musharaka | 111 | 111 | -0.3 | -0.28% | 0.66% |
| 6 | Constant Musharaka | 52 | 52 | -0.1 | -0.28% | 0.31% |
| | Grand Total | 14,596.11 | 16,712.96 | 2,116.84 | 14.5% | 100% |

**Source:** Islamic Banking and Finance Department, DAB

**Figure 6.14:** Product wise Investment and Financing of the Islamic Banking Sector: comparison between 2nd and 3rd Quarters of FY 2020 (1399).

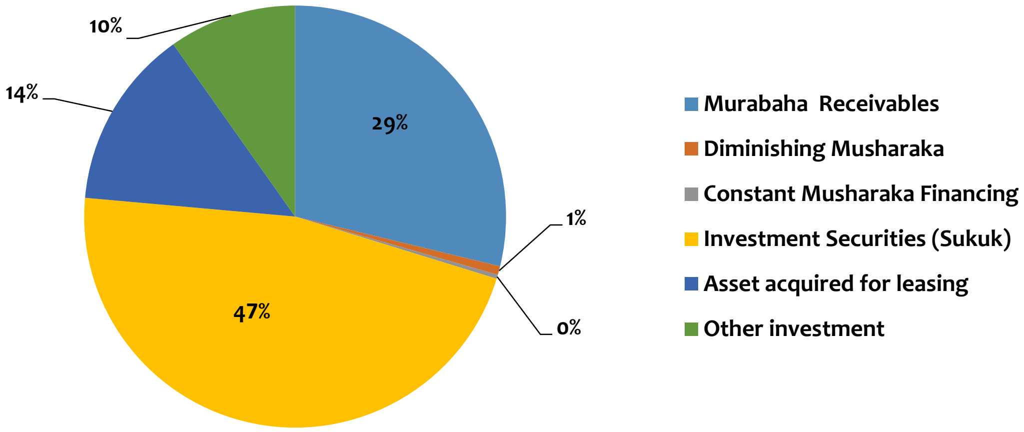



**Source:** Islamic Banking and Finance Department, DAB

Total Afghani denominated financing and investment recorded at Afs 4.87 billion which made 29.15% of total Gross financing and investment or 12.35% of total assets of the sector.

While the US Dollar denominated financing and investment are Afs 11.84 billion and makes 70.84% of total gross financing and investment or 30.02% of total assets. The sector wise lending of Murabaha financing in Afghanistan is dominated by Islamic banking windows, constituted 85.4% of total gross Murabaha financing of the sector while the share of full-fledged bank in total Murabaha financing was only 14.6%. Whereas the total overseas investment in Sukuk of the sector is dominated 88.2% by full-fledged Islamic bank and remaining 11.84% by two Islamic banking windows of commercial bank.

**Figure 6.15:** Product wise investment and financing as percentage (%) share for the 3rd Quarter of FY 2020 (1399)




**Source:** Islamic Banking and Finance Department, DAB

- **Financing & Investment Loss Reserve:**

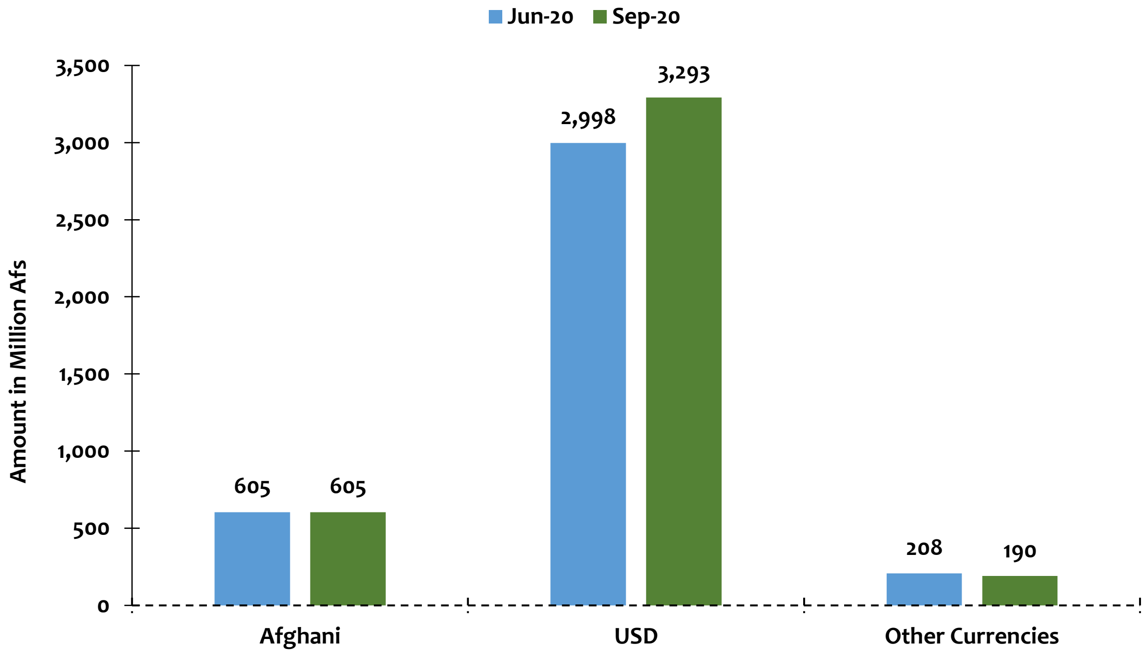
At the end of Sep 2020 (Sunbula 1399), total provision of Islamic banking sector for financing and investment stands at Afs 1.03 billion and shows increase of 1% as compared to previous quarter (June 2020), and the increase amount comes from Murabaha financing. The provision of the sector is consisting of Afs 924.11 million for Murabaha financing and makes 19% of total Murabaha financing, Afs 74.8 million for interbank claims, Afs 13.6 for investment and Afs 25.9 million for account receivable. The provision for Murabaha financing encompasses 9% of total gross financing of Islamic banking.

- **Interbank Claims:**

The Interbank Claims of the Islamic Banking Sector are the fourth largest among various asset categories, which at the end of third quarter of 2020, stands at Afs 4.08 billion, constituting 10.3% of total assets and shows increase of Afs 478 million or 7% in the quarter under review. Interbank claims were denominated by Afghani 15%, US Dollar 80.5% and other currencies 4.6% (See figure 6.16).

Three out of six Islamic banking windows and one full-fledged Islamic bank have interbank claims which consist of Afs 643 million time deposits which make 16% of total interbank claims, and Afs 3.44 billion demand deposits which make 84% of total interbank claims of the sector.

**Figure 6.16:** Interbank claims for the 3rd Quarter of FY 2020 (1399)




**Source:** Islamic Banking and Finance Department, DAB

- **Cash in Vault and Claims on DAB:**

Cash in vault and claims on DAB is the largest category and making 39.4% of total asset of the sector, at the end of third quarter 2020 stands at Afs 15.54 billion and shows decrease of0.12% as compare to preceding quarter (June 2020). Cash in vault and claims on DAB consists of Afs 4.7 billion cash in vault, Afs 7.9 billion non-interest bearing current account with DAB and Afs 2.88 billion required reserve account with DAB.

### 6.8.2. Liabilities

Total liabilities of the Islamic Banking sector increased by Afs 2.33 billion or 7% in the third quarter of FY 2020 (1399) and stood at Afs 35.34 billion against Afs 33 billion in the second quarter of the current year. The increase in total liabilities of the sector was mainly contributed by increase in total deposits (dominant in customer and banks time deposits mostly in USD currency). The majority of liabilities of the sector are made up of deposits (91.3%), followed by other liabilities (5.4%) and short term borrowings placed in third position (3.2%).

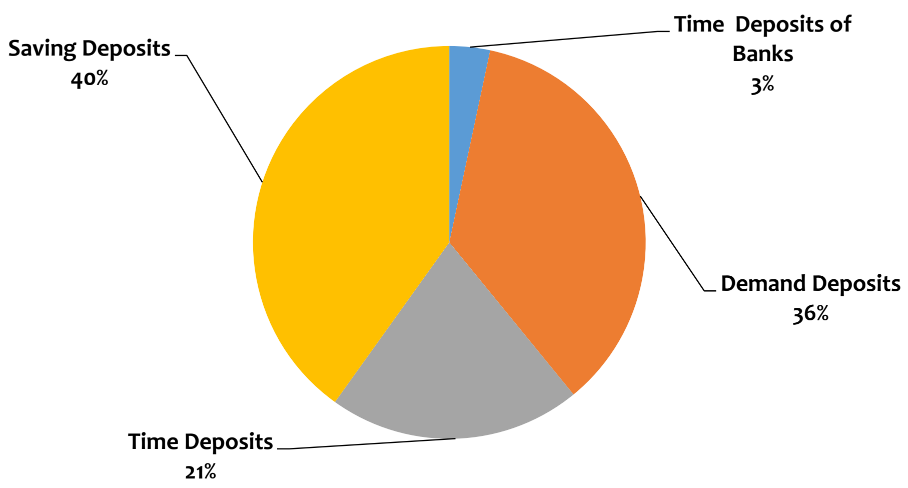
- **Total Deposits**

Deposits are the main source of funding and the largest component of liabilities, stands at Afs 32.27 billion, making 91.3% of total liabilities of the sector and shows increase of 7% since last quarter of FY1399 (June 2020). The increase in total deposits were mostly obvious in time and saving deposits, the increase has taken place Afs1.22billion or 18.6 % in time deposits, Afs 671 million or 5.46% in saving deposits and Afs217million or 1.9% in demand deposits during the reviewed period. Furthermore, the increase is mostly occurred in Afs deposits, as well as USD deposits registered positive trend in its position.

Afs denominated deposits of the sector were Afs 12.6billion or 39.15% of the total deposits, increased by 12.7% while the USD-denominated deposits of the sector stood at Afs 19.63 billion or 60.8% of total deposits which is increased by 3.59%. Full-fledged Islamic bank has the highest percentage share in total deposits of the sector, standing at 59.4% followed by Islamic banking windows with 40.6% share.

The total deposits of the sector consist of Afs 11.54 billion of demand deposits, Afs 12.94 billion of saving deposits and Afs 7.79 billion of time deposits. From total deposits of the sector, demand deposits make 35.76%, saving deposits make 41.49% and time deposits make 24.14%, comprises of Afs 31.19 billion of customers deposits and Afs 1.07billion of banks deposits. The deposits of banks make only 3.34% of total deposits of the sector.

**Figure 6.17:** Breakdown of Deposits for the 3rd Quarter of FY 2020 (1399)




**Source:** Islamic Banking & Finance Department, DAB,

### 6.8.3. Liquidity:

The liquidity position of all Islamic banking windows and full-fledged Islamic bank is above the set minimum for the broad liquidity ratio (15%) and the quick liquidity ratio (20%). Broad liquidity ratio of the Islamic banking sector as a median stand at 48.6% against 49.94% in the preceding quarter (March 2020), showing a decrease of 1.3%.

Generally, the 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 liquidity ratio level, in order to avoid any liquidity problem.

**Table 6.7:** Key Financial Soundness Indicators of the Islamic Banking Sector for the 3rd Quarter of FY 2020 (1399)

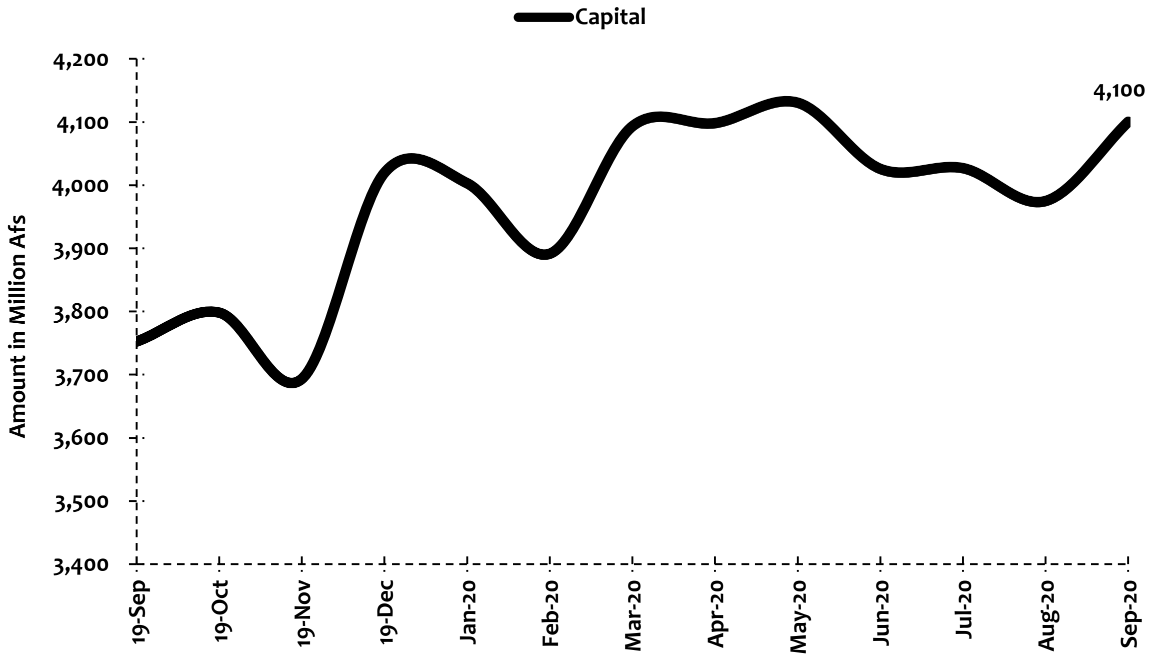
| Ratio in % | (June, 2020) | (Sep,2020) |
|---|---|---|
| Liquid Assets to Total Assets | 52.11% | 49.59% |
| Liquid assets to short term liabilities | 155% | 154% |
| Total financing to Total Assets | 37% | 42.4% |
| Total financing to Total Time & Saving deposits | 77.41% | 80.6% |
| Time & Saving deposits to Total deposits | 62.42% | 64.24% |
| Foreign-Currency denominated funding to total funding | 62.86% | 60.85% |
| Foreign- Currency denominated financing to total financing | 73.62% | 70.85% |
| Return on Assets ( ROA) Cumulative | 1.2 | 0.96 |
| Return on Equity ( ROE) Cumulative | 8.3 | 7.66 |

**Source:** Islamic Banking & Finance Department, DAB

### 6.8.4. Capital:

The equity capital of the sector stands at Afs 4.1 billion, making 10.4% of total assets and shows increase of 1.63% since previous quarter which was Afs 4.03 billion. The increase in the total capital is due to profit of the sector during the quarter under review. CAR of full-fledged Islamic bank remains above the regulatory limit.

**Figure 6.18:** Trend of Capital of the Islamic Banking Sector for the 3rd Quarter of FY 2020 (1399)




**Source:** Islamic Banking & Finance Department, DAB

The equity capital of windows consists of owner's equity (which is not in the form of liquid assets, but it is the value of investment property which is transfer/given from the conventional bank to Islamic banking windows), retained profit/loss of previous years, other comprehensive income (income from the revaluation of fixed assets) and profit/loss of the current year. The trend of the sector equity capital as described above is given in the figure 6.20.

One of commercial Islamic banking windows has the highest share in total equity capital of the sector which is 72% and in the second place is the full-fledged bank with 34% contributions in total equity capital of the sector.

### 6.8.5. Profitability:

- **Quarter – to – Quarter:**

During the third quarter of FY 2020, the Islamic banking sector earned Afs 65.5 million net profit against Afs 7.5 million net profits in last quarter. The increase in the profit of the sector was mainly due to increase of Afs 56.2 million in FX revaluation gain for the mentioned period. Another contributing factor for the increase in the profit of the sector is Afs 164.6 million as nonprofit income for the third quarter of FY 2020, which shows 62.2 million increases comparing with the last quarter.

- **Cumulative: (Jan - June, 2020- Jadi 1398 – Sunbula 1399):**

Islamic banking sector profitability on cumulative basis (from Jan to Sep, FY 2020) ended with Afs 219.6 million net-profit for the first three quarter of the FY 2020 (1399) against Afs 303.4 million net-losses recorded in the same period of the last year, which resulted in ROA of 0.96% and ROE of 7.67% on annualized against the ROA of -1.5% and ROE of -11.04% on annualized in first three quarter of FY 2019 (1398).

**Table 6.8:** Profit and Loss Schedule of the Islamic Banking Sector

| Profit and loss Schedule (Amount in millions Afs) | | | |
|---|---|---|---|
| **Item** | **June-20** | **Sep-20** | **Difference** |
| Profit income | 132.52 | 149.53 | 17.01 |
| Profit expense | 61.33 | 64.17 | 2.17 |
| Net profit income | 71.18 | 85.36 | 14.17 |
| Net Credit provisions | (20.02) | 10.69 | 30.7 |
| Other nonprofit income | 102.45 | 164.67 | 62.2 |
| Other nonprofit expense | 289.67 | 322.7 | 33.04 |
| Income (Loss) before FX revaluation | (96.003) | (83.38) | (12.62) |
| FX revaluation Gain/loss | 109.62 | 165.88 | 56.26 |
| Tax | 9.38 | 16.9 | 7.5 |
| **Net profit income/Loss after Tax** | **7.58** | **65.58** | **58** |

**Source:** Islamic Banking and Finance Department, DAB

The main reason for increase in the profit of the sector as compared to the same period of previous year was mainly due to calculated Afs 520 million as net credit provisions in first three quarters in last year. Whereas the sector reported Afs 172.6 million as reintegrated provisions since Jan 2020. The other contributing factors in the profit of the sector is the increase of Afs 73 million nonprofit income of the sector, meanwhile the non-profit expenses (operating expense) shows increase of Afs 58.9 million. Three out of six Islamic windows ended with profit of Afs 239 million against Afs 342.8 million net losses in the same period of the last year (Sep 2019), where all Islamic banking windows were at loss for that period.

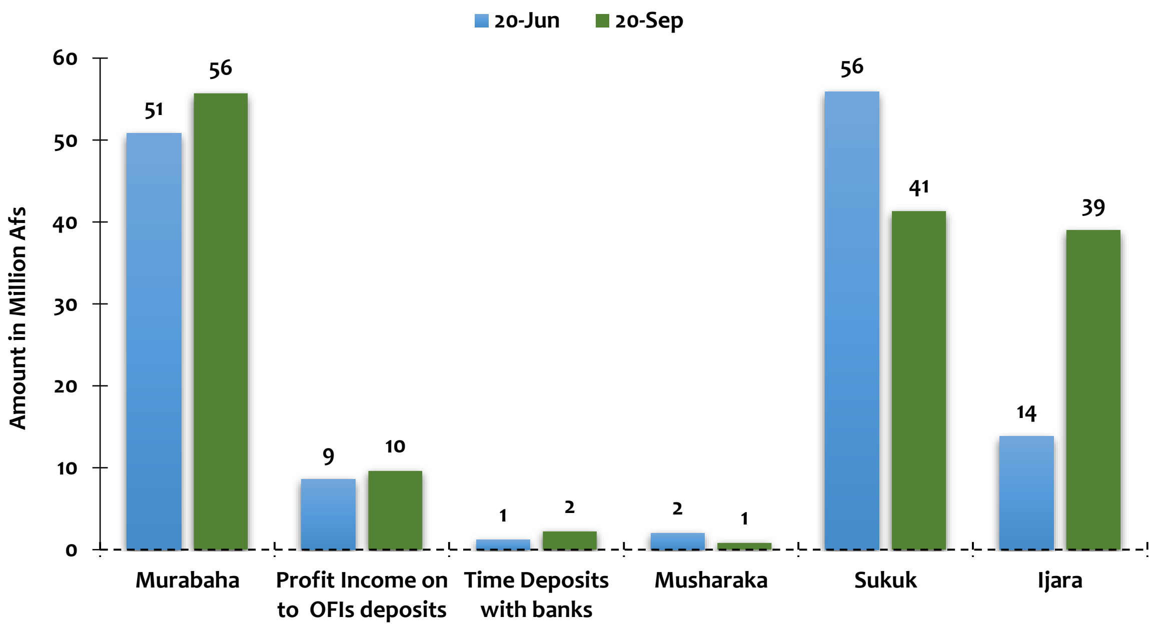
In general, the Islamic banking sector was offering six types of Islamic financial products. The returns from financing and investment for the quarter (Sep 2020) are shown in the following table:

**Table 6.9:** Returns by Major Types of Shariah Compliant Products

| Value of returns by major type of Shariah-compliant contract (Amount in million Afs) | | | |
|---|---|---|---|
| **Product** | **June-20** | **Sep-20** | **Difference** |
| Time Deposits with banks | 1.2 | 1.9 | 1.7 |
| Profit Income on to OFIs deposits | 8.65 | 9.65 | 1 |
| Murabaha financing | 50.86 | 55.79 | 4.9 |
| Musharaka and Diminishing Musharaka | 2.02 | 0.8 | (1.2) |
| Sukuk investment | 55.94 | 41.33 | (14.6) |
| Ijara | 13.8 | 39.04 | 25.2 |
| **Total Profit Income** | 132.5 | 149.5 | 17.01 |

**Source:** Islamic Banking and Finance Department, DAB

**Figure 6.19:** Return by Major Types of Shariah Complaint Products for the 3rd Quarter of FY 2020 (1399)




**Source:** Islamic Banking & Finance Department, DAB

Total number of employees, borrowers and depositors of the Islamic banking sector as of Sep, 2020, all across the country are shown in following table 6.10:

**Table 6.10:** Number of Employees, borrowers, and depositors of the Islamic Banking Sector for the 3rd Quarter of FY 2020 (1399)

| Particulars | No. |
|---|---|
| Full-time all Employees | 1,029 |
| Present Borrowers | 835 |
| Present Depositors | 557,869 |

**Source:** Islamic Banking & Finance Department, DAB

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