Da Afghanistan Bank

Economic & Statistical Bulletin

First Quarter, FY 1399

Monetary Policy Department

Da Afghanistan Bank

Ibn-e-Sina Watt

Kabul

Afghanistan

Telephone: +93(0)-20-2103930

Internet: **www.dab.gov.af**

Email: **mp@dab.gov.af**

Note:

Afghanistan's fiscal year has changed effective from 2012 (1391). The new fiscal year begins from December 22nd each year. This bulletin analyzes economic developments during the first quarter of fiscal year 1399 (2020), which starts from 1st of Jadi, 1398 to 29th Hoot, 1398.

TABLE OF CONTENTS

CONTENTS

LIST OF FIGURES

LIST OF TABLES

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

Da Afghanistan Bank uses quantitative theory of money as a determinant of Reserve Money (RM) aiming to keep domestic prices stable. Maintaining domestic price stability is the primitive goal of the Da Afghanistan Bank (DAB), where reserve money is the main operational target while Currency in Circulation is the indicative target for liquidity.

In first quarter of FY 1399, Reserve Money was AFN 266,938.63 million with -8.21% growth, while Currency in Circulation was AFN 259,502.13 with -0.02% growth rate. Both, reserve money and currency in circulation were below the target. Narrow money growth is 7% standing at AFN 459,798 million, while broad money standing AFN 490,857 million with a growth rate of 5.57% in the first quarter of FY 1399.

Consumer Price Index (CPI) is calculated on the basis of April-2015 base prices. In the first quarter of FY 1399 (2020) average inflation reached to 3.54% (overall index) higher than average rate of 0.84% in the first quarter of the previous year (Y-o-Y). Comparing the index on Q-to-Q basis, inflation rate increased by 1.83% reaching 3.54% on average in the first quarter of FY 1399, where it was 1.71% in the fourth quarter of FY 1398.

Meanwhile, Merchandise trade deficit reduced by 19% to USD 1,326.42 million in the first quarter of FY 1399 lower than deficit of USD 1,603.77 million in the first quarter of the previous year, which was due to 12% increase in export earnings and 14% decrease in import expenditures. At the meantime, service account inflow and primary income account shown increase in the first quarter of FY 1399. As a result, balance of payment deficit reduced to almost USD 735 million in the first quarter of FY 1399, lower than the deficit of USD 1,276 million in the first quarter of FY 1398.

Capital account inflow decreased to USD 36.06 million (reduced by 35%) in the first quarter of FY 1399. Financial account balance was USD 200.68 million at the end of the first quarter of FY 1399. Primary income account net inflow increased by 10% which was Deficit of the service account reduced by 41%, and compensation of employees and investment income increased by 10%.

Meanwhile, budgeted expenditures was AFN 428.38 billion for FY 1399, 13% of the core budget was executed in the first quarter of 1399. Total revenue for the first quarter of FY 1399 recorded amount of AFN 54.57 billion compared with the AFN 57.63 billion in the same quarter of the previous year.

Total domestic revenue was AFN 38.66 billion, on the hand, donor contributions registered amount of AFN 16.72 billion during the first quarter of FY 1399. Total expenditure was AFN 57.81 billion, meanwhile, operating expenditures was AFN 48.70 billion, while development expenditures recorded AFN 9.11 billion in the first quarter of FY 1399.

In the Banking sector, statistics show decreasing trend for first quarter of FY 1399. Banking sector incurred loss of AFN 71.3 million with ROA of -0.13%. Assets of the banking system was AFN 284.67 billion, while gross loans recorded AFN 40.62 billion. Trade sector with share of 44.4% received the highest amount of loan from the banks, and service sector ranking the second in the list. Islamic Banking also witnessed decreasing trend in its main financial indicators. Assets of the Islamic banking reduced due to decrease in deposits. The Islamic banking sector earned profit of AFN 146.47 million during the first quarter of FY 1399. Deposits were the main source of fund for the Islamic banks.

1

Global Economic Environment

1
GLOBAL ECONOMIC ENVIRONMENT

The global outlook is highly uncertain as a result of COVID-19 pandemic which is a global health crisis. It has triggered the most severe economic recession in nearly a century and is causing enormous damage to people's health, jobs and well-being. Global growth is projected at –4.9% in 2020, 1.9% below the April 2020 World Economic Outlook (WEO) forecast.[1] Growth in the advanced economy group is projected at –8.0% in 2020, 1.9% lower than in the April 2020 WEO. Therefore, synchronized deep downturns are foreseen in the United States –8.0%, Japan –5.8%, the United Kingdom –10.2%, Germany –7.8%, France –12.5% Italy and Spain –12.8%.

In 2021 the advanced economy growth rate is projected to strengthen to 4.8%, leaving 2021 GDP for the group about 4% below its 2019 level. Growth in emerging market and developing economies group forecast is –3.0% in 2020, 2% below the April 2020 WEO forecast. The downward revision to growth prospects for emerging market and developing economies over 2020–21 is 2.8%, which exceeds the revision for advanced economies of 1.8%. Excluding China, the downward revision for emerging market and developing economies over 2020–21 is 3.6%.

The COVID-19 pandemic has had a more negative impact on activity in the first half of 2020 than anticipated, and the recovery is projected to be more gradual than previous forecast. Overall, this would leave 2021 GDP some 6½% lower than the pre-COVID-19 projections in January 2020. The adverse impact on low-income households is particularly critical, revealing the significant progress made in reducing extreme poverty in the world since the 1990s.

GDP in first quarter of FY 2020 was generally worse than expected the few exceptions include, for Chile, China, India, Malaysia, and Thailand, among emerging markets, and Australia, Germany, and Japan, among advanced economies. Moreover, according to the International Labor Organization, the global decline in work hours in the first quarter of FY 2020 compared to the same quarter of FY 2019 was equivalent to the loss of 130 million full-time jobs.

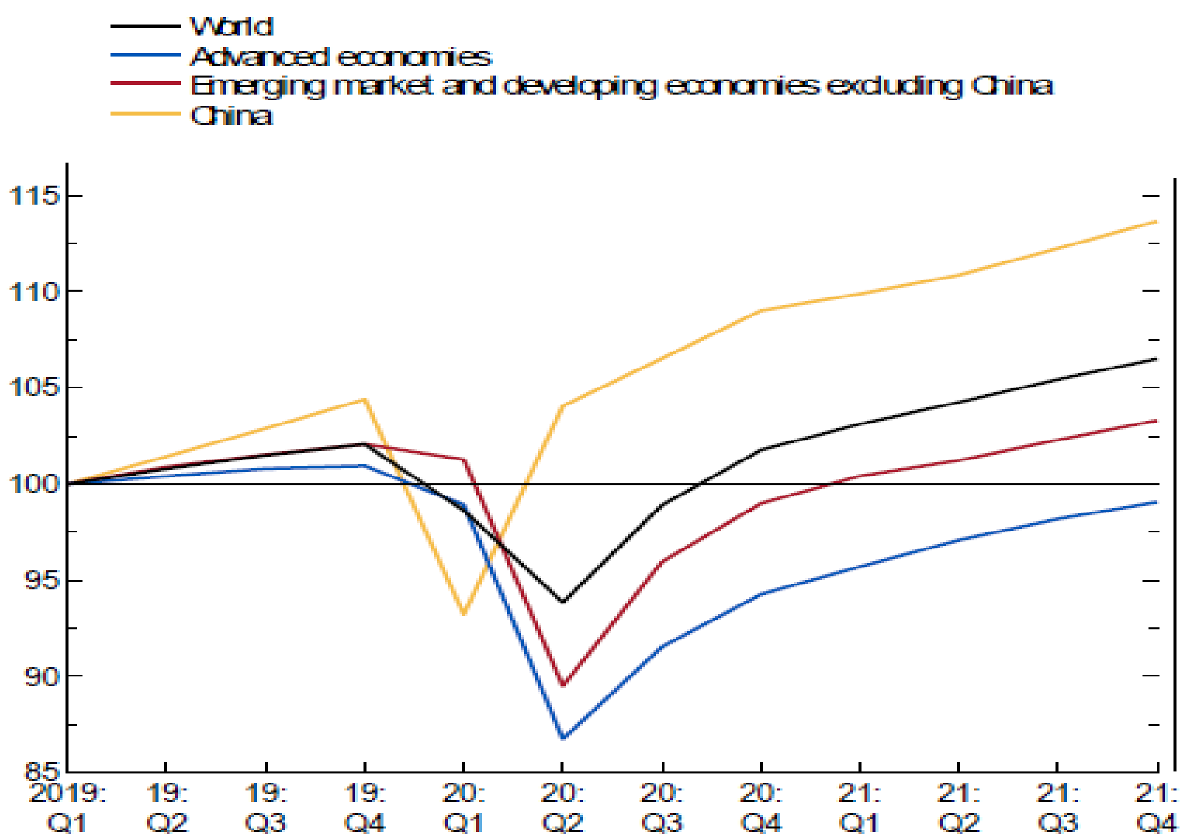
The decline in the quarter under review is likely to be equivalent to more than 300 million full-time jobs. Furthermore, Trade contracted by close to –3.5% (year over year) in the concerned period, reflecting weak demand, the collapse in cross-border tourism, and supply dislocations related to shutdowns (exacerbated in some cases by trade restrictions). Average inflation in advanced economies had dropped about 1.3% since the end of 2019, to 0.4% (year over year) as of April 2020, while in emerging market economies it had fallen 1.2%, to 4.2%.

Downward price pressure from the decline in aggregate demand, together with the effects of lower fuel prices, seems to have more than offset any upward cost-push pressure from supply interruptions so far.

[1] World Economic Outlook Report, IMF, June 2020

Global trade will suffer a deep contraction this year by –11.9%, reflecting considerably weaker demand for goods and services, including tourism. Consistent with the gradual pickup in domestic demand next year, trade growth is expected to increase to 8%.

Figure 1.1: Global growth, Advanced and Emerging economies' GDP growth



Source: IMF staff calculation

1.1. ADVANCED ECONOMIES:

1.1.1 United States' Economy

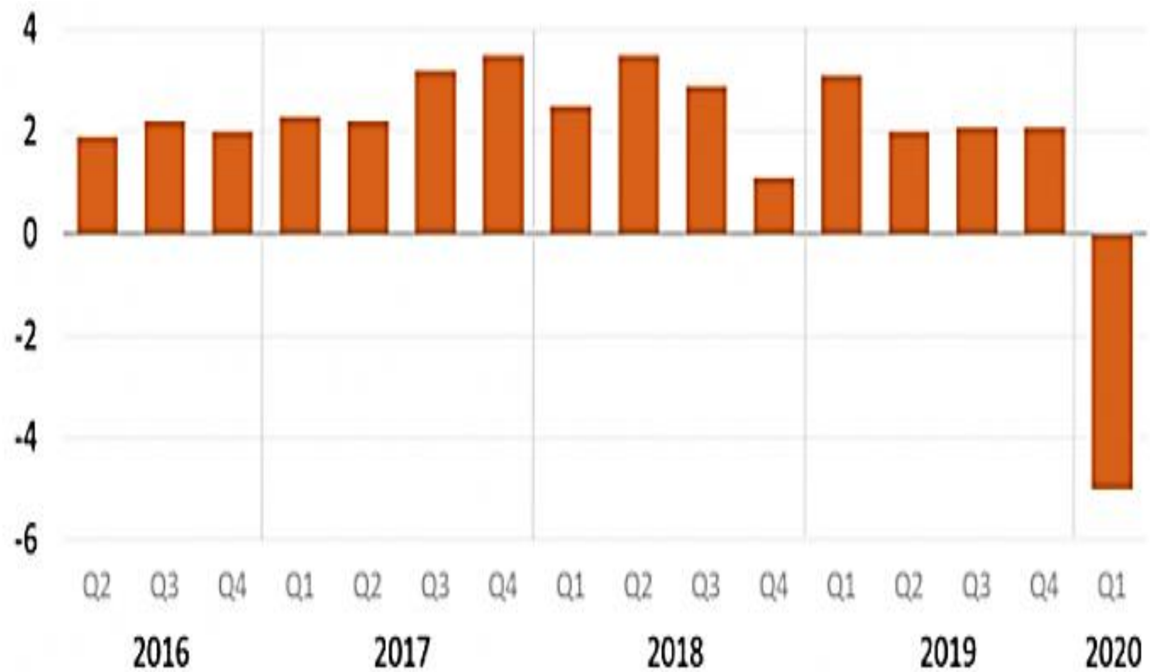
The real gross domestic product (GDP) decreased at an annual rate of 5.0% in the first quarter of FY 2020 according to the "third" estimate released by the Bureau of Economic Analysis Comparably in fourth quarter, real GDP increased by 2.1%. The decline in GDP reflected the response to the spread of COVID-19, as governments issued "stay-at-home" orders in March, 2020. This led to rapid changes in demand, as businesses and schools switched to remote work or canceled operations, and consumers canceled, restricted, or redirected their spending.

The full economic effects of the COVID-19 pandemic cannot be quantified in the GDP estimate for the first quarter of FY 2020 because the impacts are generally embedded in source data and cannot be separately identified. The 5.0% decrease in real GDP was the same as in the "second" estimate.

The updated estimates primarily reflected an upward revision to nonresidential fixed investment that was offset by downward revisions to private inventory investment, consumer spending, and exports. Moreover, BEA's featured measure of inflation in the U.S. economy, the price index for gross domestic purchases, increased by 1.7% in the first quarter of FY 2020, the same as in the second estimate. The price index for personal consumption expenditures (PCE) increased by 1.3%, the same as in the second estimate. Excluding food and energy prices, the PCE price index increased by 1.7%, an upward revision of 0.1%.

Meanwhile, U.S. International Transactions current account deficit, which reflects the combined balances on trade in goods and services and income flows between U.S. residents and residents of other countries, narrowed by $0.1 billion, or 0.1%, to $104.2 billion in the quarter under review, according to statistics from the U.S. Bureau of Economic Analysis (BEA).

Figure 1.2: US, Real GDP percentage change from preceding quarter



Source: U.S. Bureau of Economic Analysis

The revised deficit for fourth quarter of FY 2019 was $104.3 billion. The deficit for first quarter of FY 2020 was 1.9% of current dollar gross domestic product, up less than 0.1% from the fourth quarter of FY 2019. The $0.1 billion narrowing of the current account deficit mainly reflected a reduced deficit on goods that was largely offset by a reduced surplus on primary income and an expanded deficit on secondary income. Meanwhile, the declines in first quarter of FY 2020 current account transactions are, in part, due to the impact of COVID-19, as many businesses were operating at limited capacity or ceased operations completely, and the movement of travelers across borders was restricted.

Moreover, the U.S. net international investment position, the difference between U.S. residents' foreign financial assets and liabilities, was –$12.06 trillion at the end of the first quarter of FY 2020, according to statistics released by the U.S. Bureau of Economic Analysis (BEA). Assets totaled $26.77 trillion and liabilities were $38.82 trillion. It is worth mentioning that in the first quarter of FY 2020, the declines in U.S. assets and liabilities reflect the impact of the COVID-19 pandemic.

The disruption to global production and financial markets led to sharp declines in global stock prices, the appreciation of the U.S. dollar against most foreign currencies, and a shortage of U.S. dollar liquidity in foreign money markets. The stock price declined and the appreciation of the U.S. dollar are reflected in price changes and exchange rate changes.

1.1.2 The Economy of UK

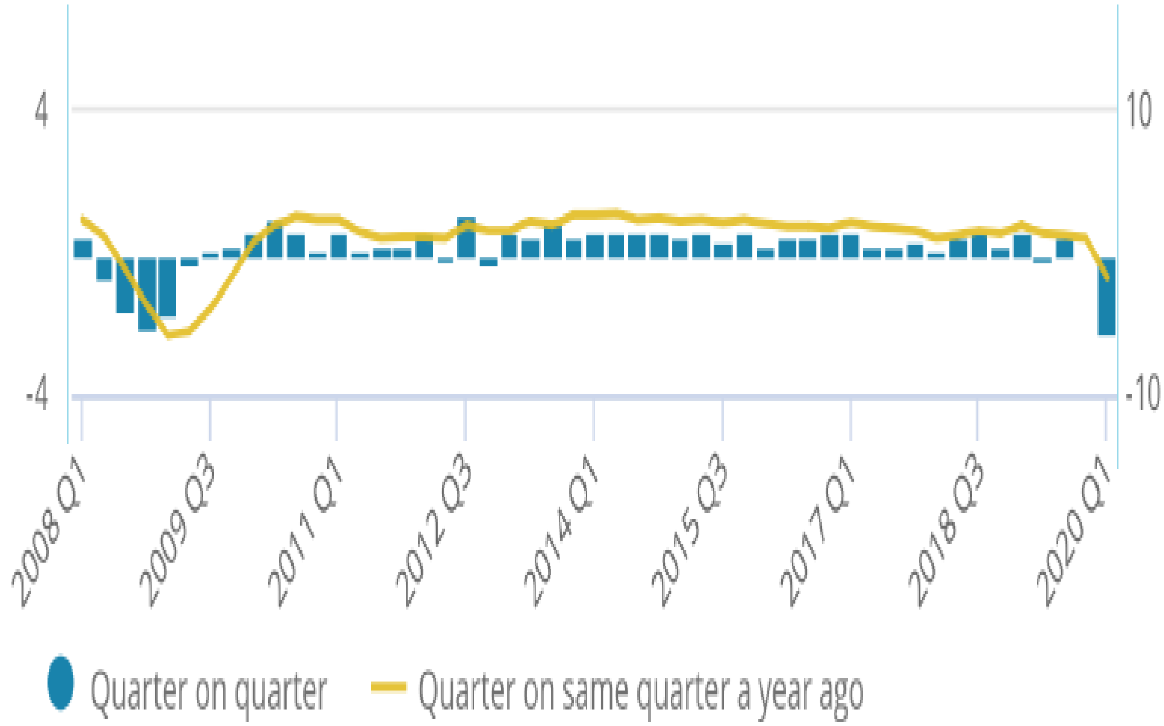
UK gross domestic product (GDP) in volume terms fell by 2.2% in first quarter of FY 2020, revised downwards by 0.2% from the first quarterly estimate; the largest fall in UK GDP since third quarter of 1979 when it also fell by 2.2%. The services, production and construction sectors provided a negative contribution to growth in the output approach to GDP in the quarter under review; with services output falling by a record 2.3% in the latest quarter.

Household consumption declined by 2.9%, revised downwards by 1.2% from the first quarter estimate; this is now the largest decline in household consumption since third quarter of 1979. The households saving ratio increased to 8.6%, compared with 6.6% in fourth quarter of FY 2019. Meanwhile, compared with the same quarter a year ago, UK GDP decreased by 1.7%, a downward revision of 0.1% from the previous estimate.

The first direct effects of the coronavirus pandemic and the government measures taken to reduce transmission of the virus as a result of the disruption to business and implementation of these government measures, which include restrictions in movement, facing increased number of challenges in production of the first quarter GDP estimate for the UK. Furthermore, private consumption, Government consumption and net trade are estimated to have had a negative contribution to growth in the quarter under review.

Beside, that estimates show that the UK posted a trade deficit of 0.2% of nominal GDP in first quarter of FY 2020, compared with an initial estimate of 0.9%. This revision reflects downward revisions to import volumes, which offsets much of export volumes downward revisions. In addition, total trade deficit, excluding non-monetary gold and other precious metals, narrowed by £1.3 billion to £2.3 billion in the quarter under review, where the narrowing of the underlying total trade deficit was largely driven by a £13.3 billion fall in imports, partly offset by a £12.0 billion fall in exports. Including non-monetary gold and other precious metals, the total trade balance decreased by £12.7 billion to a deficit of £4.8 billion in first quarter of FY 2020.

Figure 1.3: UK, GDP growth from first quarter of FY 2008 to first quarter of FY 2020



Source: Office for National Statistics, UK National Account

On the other hand, the total trade deficit narrowed by £37.4 billion to £8.6 billion in the 12 months to March 2020. Meanwhile, the Consumer Prices Index including owner occupiers' housing costs (CPIH) 12-month inflation rate was 1.5% in March 2020, down from 1.7% in February. The CPIH 1-month inflation rate was 0.0% in March 2020, compared with 0.2% in March 2019.

The Consumer Prices Index (CPI) 12-month inflation rate was 1.5% in March 2020, down from 1.7% in February. While, largest contribution to the CPIH 12-month inflation rate in March 2020 came from housing, water, electricity, gas and other fuels (0.51%). Falls in the price of motor fuels and clothing resulted in the largest downward contributions to the change in the CPIH 12-month inflation rate between February and March 2020. Beside, rise in air fares produced the largest, partially offsetting, upward contribution to change.

1.1.3 Economy of Japan

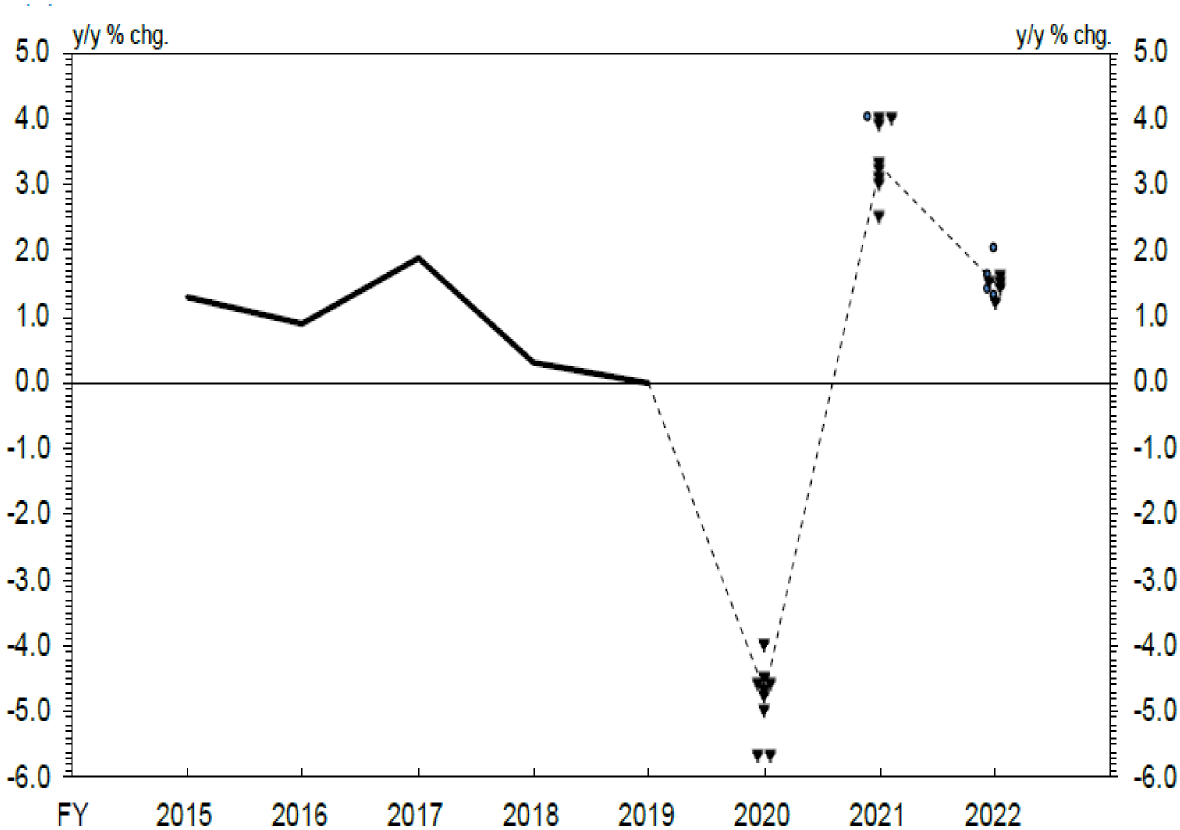
Japan's economy has been in an extremely severe situation with the impact of COVID-19 remaining at home and abroad, although economic activity has resumed gradually. Besides that, overseas economies have been depressed significantly, reflecting the impact of the COVID-19 pandemic, though they have shown signs of heading toward a pick-up. In this situation, exports and industrial production have declined substantially.

Meanwhile, corporate profits and business sentiment have deteriorated, and business fixed investment has been more or less flat. Furthermore, the continuing impact of COVID-19, the employment and income situation has been weak[2]. Although private consumption has decreased significantly, mainly in services such as eating and drinking as well as accommodations, where it has shown signs of a pick-up recently.

Housing investment has declined moderately and public investment has increased moderately. Financial conditions have been accommodative on the whole, but those for corporate financing have remained less so, as seen in deterioration in firms' financial positions. On the price front, the year-on-year rate of change in the CPI (all items less fresh food, and the same hereafter) is at around 0%, mainly affected by the decline in crude oil prices.

Inflation expectations have weakened somewhat. On the other hand, the real GDP growth rate for first quarter of FY 2020 registered negative growth for two consecutive quarters, marking -0.6% on a quarter-on-quarter basis and -2.2% on an annualized basis.

Figure 1.4: Real GDP Growth of Japan (Year-on Year)



Source: The Bank of Japan

[2] Economic Outlook Activity and Prices, Bank of Japan, July 2020

It is worth mentioning this is attributable to the fact that components such as private consumption and exports declined, mainly due to the impact of the spread of COVID-19. Since April, COVID-19 has brought about a considerable decline in aggregate demand through the following channels: a decline in goods exports reflecting a depression in overseas economies; a decline in inbound tourism demand (services and exports); and a decline in domestic private consumption, mainly due to self-restraint from going outside and business restrictions.

In reflection of the decline in aggregate demand, labor demand has weakened significantly. The unemployment rate and active job openings-to-applicants' ratio have deteriorated, and the number of employed persons has turned to a clear decline. Under these circumstances, the output gap which captures the utilization of labor and capital narrowed within positive territory for the quarter under review, reaching almost 0%. The gap seems to have continued to narrow and become significantly negative for the second quarter of FY 2020.

Exports have declined substantially with overseas economies being depressed significantly. Beside, by region, exports to advanced economies such as the United States and the European Union (EU) have declined substantially, mainly for automobile-related goods, with the impact of strict public health measures taken by each economy remaining.

In addition, imports decreased in first quarter of FY 2020 due to the impact of the spread of COVID-19 in China, but have picked up recently, mainly for consumer goods such as personal computers, mobile phones, and masks reflecting a resumption of production activity in China imports are likely to be under downward pressure stemming from weak production activity in Japan for the time being, but an uptrend is expected to become evident thereafter, reflecting the resumption of domestic economic activity.

The nominal current account surplus has declined looking at the breakdown of developments in the current account balance, the nominal trade balance has marked a relatively large deficit, mainly due to a significant decline in goods exports. Furthermore, the services balance also has marked a deficit, reflecting a significant deterioration in the travel balance that is due to a decline in inbound tourism demand. On the other hand, the primary income balance has maintained a relatively large surplus, supported mainly by the interest income from past securities investment.

1.2 EMERGING ECONOMIES:

1.2.1 Economy of China

During the first quarter of FY 2020 an earth shaking reversal of the economic environment at home and abroad. The unexpected spread of COVID-19 pandemic around the world, coupled by commodity price slumps and global financial market upheaval, has dealt the heaviest blow to the Chinese economy since its start of reform and opening-up[3].

It is worth mentioning that China's GDP growth is likely to enter a rarely seen negative territory and hit

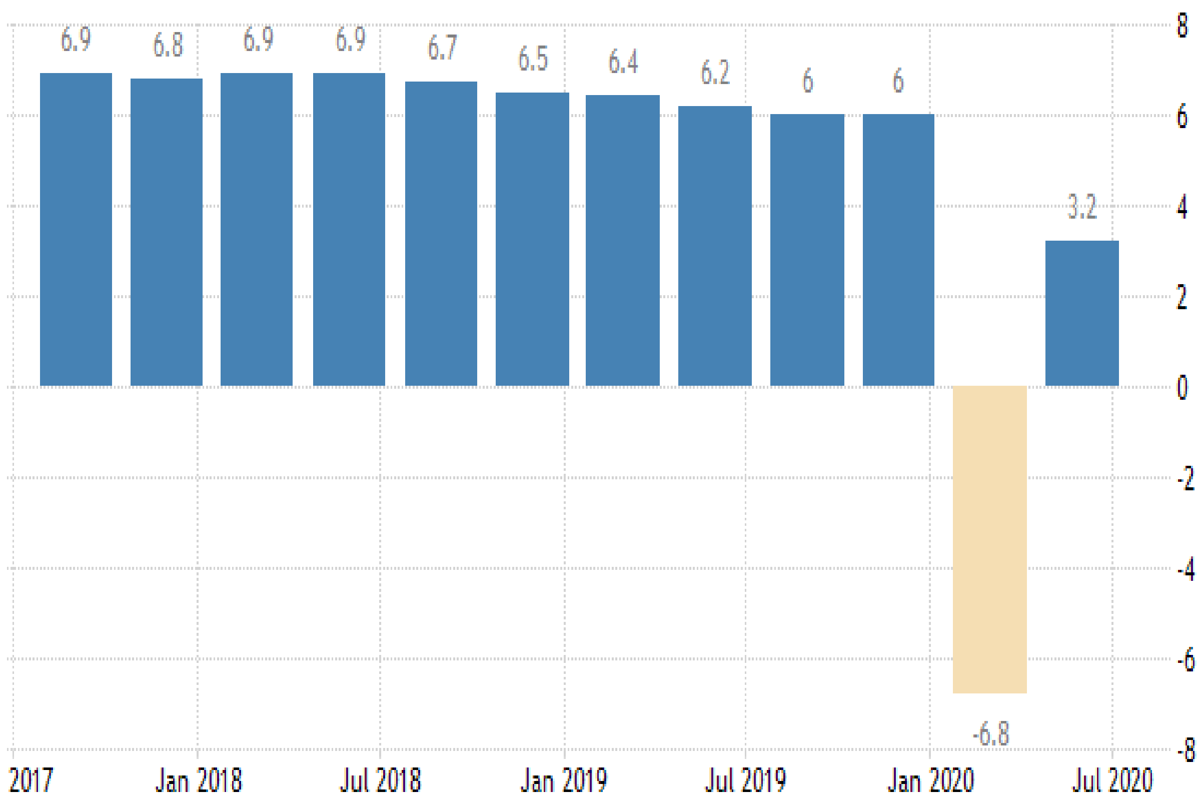
[3] Economic and Financial Outlook, Bank of China, March 2020

a 45-year low. Furthermore, looking forward to the second quarter of FY 2020, China will find the economic impact of local COVID-19 epidemic abating gradually, but still remain under pressure from various aspects as the virus is expected to spread worldwide and send its ripples back to the country.

China's economy is estimated to regain positive growth in the second quarter of FY 2020 as the government is stepping up the implementation of policies on resumption of work and production, and launching increasingly strong policies to stabilize growth. Therefore, the macro-policy maker should take strong actions resolutely to make adjustments and give top priority to stabilizing employment, supporting SMEs and ensuring basic living standards.

Moreover, the COVID-19 outbreak turned China's economic growth negative in the first quarter of FY 2020 for the first time since its reform and opening-up began. As production and work have been resumed in a well-organized manner across the country, China is expected to see its economic activity improving in March as compared with February, yet still below the normal level. GDP growth in first quarter is estimated -10% for production, 10% for services and -5% for agriculture, while it shows GDP growth -9% for (Agriculture, Production and Services) sectors in first quarter of FY 2020.

Figure 1.5: China's GDP annual growth rate



Source: National bureau of statistics of China

Consumption has been severely affected by COVID-19, which forced up the proportion of online retail sales. Consumption dropped by 20.5% Y-o-Y from January through February, down 28.7% from the same period last year and becomes the lowest on record. Furthermore, exports dropped significantly and the trade balance turned from surplus to deficit and growth of either exports or imports dived.

Besides that, after offsetting imports against exports, the trade balance of China turned from surplus to deficit from $ 41.45 billion a year ago to $ -7.1 billion. While, China's exports to the United States, EU, Japan and ASEAN grew by -27.7%, -18.4%, -24.5% and -5.1%, down 13.6, 20.8, 23.4 and 7.1 percentage points respectively.

On the other hand, CPI growth remained above 5% while PPI was subdued and prices continued to diverge in first quarter. CPI and PPI demonstrated different trend, showing a widening gap in between. CPI inflation lingered around all-time highs, standing at 5.4% and 5.2% respectively in the first two months, mainly due to the impact of COVID by contrast, PPI growth was softened to 0.1% and -0.4% Y-o-Y respectively in the first two months amid the weak demand and global oil price slump resulting from the pandemic. While, the core CPI (excluding food and energy) showed a divergent trend from overall CPI. In the first two months, the core CPI rose by 1.5% and 1% Y-o-Y respectively.

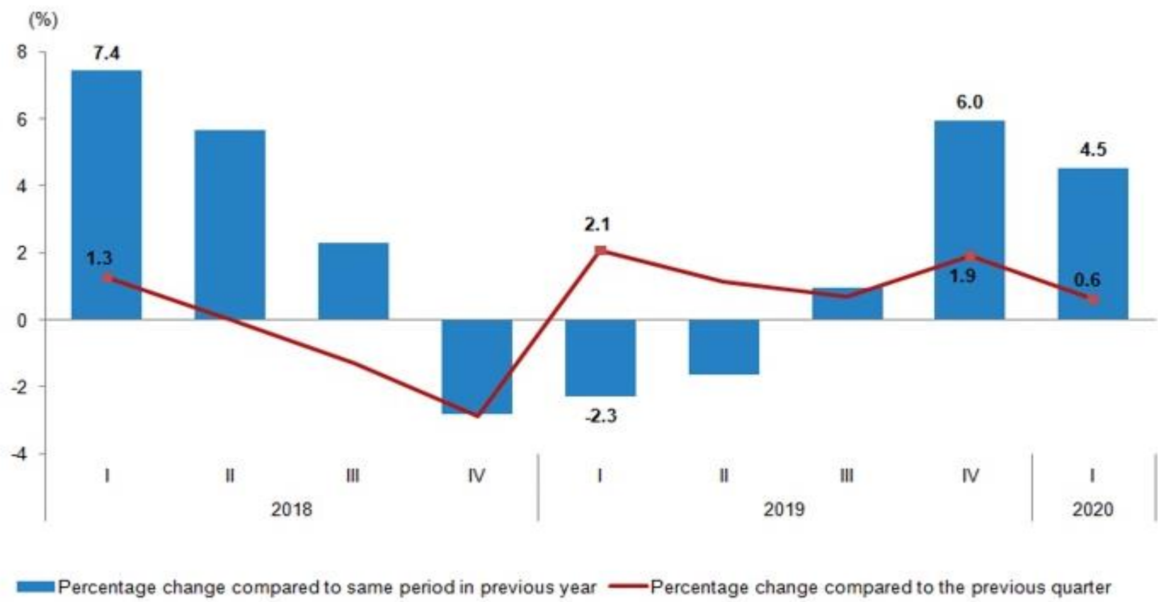
1.2.2 Economy of Turkey

The spread of the coronavirus (Covid-19) outbreak across the globe is taking its toll through various channels, leading to a sharp contraction in the global economic activity. While measures to contain the pandemic initially affected the supply chain and production, the increase in uncertainty, tightening in financial conditions, loss of household income and deterioration in firms' cash flows, all led by the global spread of the virus, also cause a significant weakening in demand. Social isolation measures to counter the pandemic had a considerable adverse impact on the services sector in March. Moreover, Manufacturing industry is likely to accompany the weakening in services in the coming period through demand and uncertainty channels in addition to tighter financial conditions. It is worth mentioning that quarterly Gross Domestic Product increased by 4.5% in first quarter of FY 2020.

Furthermore, first estimation of GDP with chain linked volume index (2009=100) increased by 4.5% in first quarter of FY 2020 compared with the same quarter of the previous year. Beside, Government final consumption increased by 6.2%, final consumption expenditure of resident households and NPISH increased by 5.1% and gross fixed capital formation decreased by 1.4% in the quarter under review compared with the same quarter of the previous year in the chained linked volume index.

Moreover, imports of goods and services increased by 22.1% in the first quarter of FY 2020 compared with the same quarter of the previous year, exports of goods and services decreased by 1.0%. Beside, compensation of employees and net operating surplus/mixed income are increased by 14.6% and 19.6% compared with the same quarter of the previous year, respectively. The unemployment rate occurred as 12.8% (with 0.2% decrease). Non-agricultural unemployment rate occurred as 14.9% (with 0.1% decrease). Exports were USD 42.80 billion with 4.0% decrease and imports were USD 55.70 billion with 10.3% increase compared with the same quarter of FY 2019.

Figure 1.6: Turkey's GDP for first quarter of FY 2020 (in %)



Source: Turkish Statistical Institute

1.2.3. The Economy of India

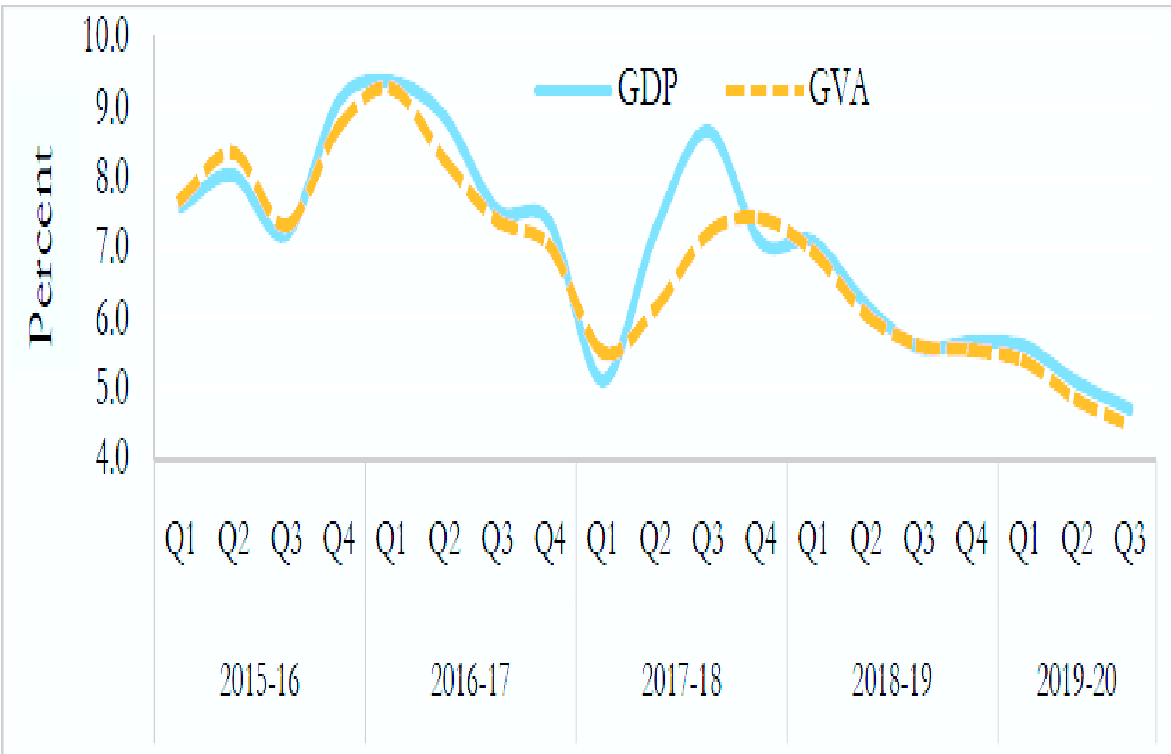
COVID-19 pandemic has emerged as a key risk to human health and is causing significant and rising human costs and economic disorder. India imposed a strict lockdown from March 25, 2020 to control the effect of COVID-19 pandemic. Economy was under complete standstill in April and resumed partially with restrictions on various activities in May as the Government made a courageous choice of supporting livelihoods.

Moreover, these green shoots have a conducive policy environment to grow further and push the economy early on the path of economic recovery and growth. India's real GDP growth rate was 4.2% in 2019-20 as per the provisional estimates released by National Statistical Office (NSO) compared to 6.1% recorded in the previous year. Beside, Nominal GDP for the year was estimated at $ 2.88 trillion, lower than the budget estimates.

Meanwhile, the growth of India's real GDP in 2019-20 is estimated at 5.0% (Second Advance Estimates) as compared to 6.1% (First Revised Estimates) in 2018-19. However, with the onset of COVID-19 pandemic, its intensity, spread and duration will now majorly determine whether India is able to realize its estimated and projected GDP growth.

There were some signs of uptick in growth prior to the onset of COVID-19 pandemic in India. Index of Industrial Production (IIP) grew by 4.5% (y-on-y) during February 2020, as compared to 2.1% in January 2020 and industries registered a growth of 5.5% (y-on-y) in February 2020, highest growth since March 2019 and consecutive increase since the previous four months. On the other hand, the adverse impact of COVID-19 has started to severely halt the growth momentum. Merchandise exports, subsequent to witnessing positive growth in February (y-on-y), showed negative growth of -34.6% in March 2020 (y-on-y). Imports, also, reported negative growth of -28.7% (y-on-y) in March 2020 after a positive growth of 2.5% in February 2020.

Figure 1.7: Quarter-wise Growth of GDP & GVA for India



Source: Ministry of Finance Department of Economic Affairs, India

In addition, consumer price inflation eased to 5.9% (y-on-y) in March 2020, as compared to 6.6% (y-on-y) in February 2020, resulting in 4.8% overall inflation during 2019-20. Food Inflation declined from 10.8% (y-on-y) in February, 2020 to 8.8% (y-on-y) in March, 2020, resulting in 6.7% overall food inflation during 2019-20. WPI Inflation also declined from 2.3% (y-on-y) in February, 2020 to 1.0% (y-on-y) in March, 2020, resulting in 1.7% overall inflation during 2019-20. Meanwhile, growth of M3 (y-on-y) as on 27th March 2020 stood at 8.8%, as compared to a growth rate of 10.6% in the same period of the previous year.

Sources:

International Monetary Fund	www.imf.org
Bureau of Economic Analysis, U.S. Department of Commerce, U.S.A.	www.bea.gov
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
Federal Statistical Office (DESTATIS), Germany	www.destatis.de
Cabinet Office, Government of Japan	www.esri.cao.go.jp
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

2

Money and Capital Market Development

2
MONETARY AND CAPITAL MARKET DEVELOPMENT

According to the monetary statistics, reserve money (RM) has a negative growth of 8.21% at the end of first quarter of FY 1399, greater than negative growth of 6.52 % at the end of the same quarter in previous year. The reason for this negative growth is decline in commercial banks deposits, which is a part of RM due to Covid-19. Currency in circulation (CiC) as a major component of RM recorded negative growth of 0.02% from the beginning to the end of first quarter, FY1399.

Reserve money (RM) and Currency in Circulation (CiC) growth which are Da Afghanistan Bank's operational and indicative targets remains well below the targets due to collecting liquidity from the market and banks during the quarter under review. Narrow money (M1), stood at AFN 459,798 million, registered a growth of 7 % due to the issuance of new banknotes. Broad money (M2) demonstrated similar behavior, represented a growth rate of 5.57%, which stood at AFN 490,857.02 million at the end of the quarter under review.

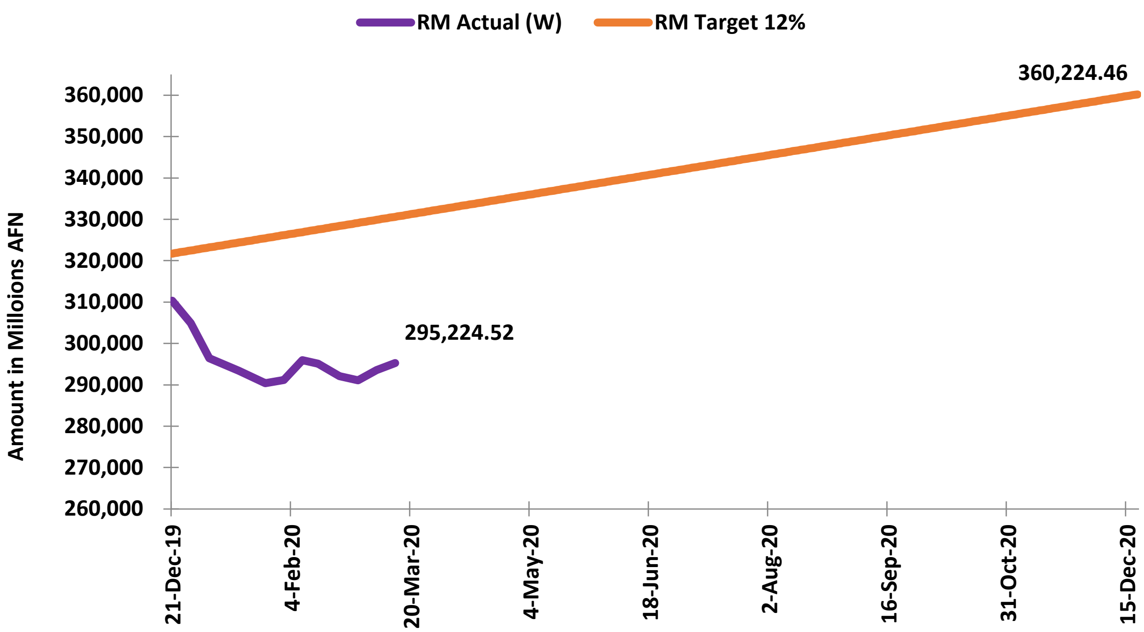
In order to mitigate excessive fluctuations of AFN exchange rate against foreign currencies and manage liquidity in the market, DAB uses FX and CNs auctions under the open market operations. During the first quarter of FY1399, DAB has auctioned a total amount of USD 426.19 million and sold USD 65 million to Brishna, (Afghan state owned electricity enterprise) via commercial banks to absorb the excess liquidity from the market and as well as to mitigate the sharp fluctuations in the exchange rate of Afghani against foreign currencies. The total outstanding amount of CNs stood at AFN 30.45 billion at the end of the first quarter of FY 1399. Meanwhile, Afghani appreciated 3.10 % against the US during the quarter under review.

2.1. MONETARY PROGRAM

Reserve money remains operational target of the monetary policy, while currency in circulation is the 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.

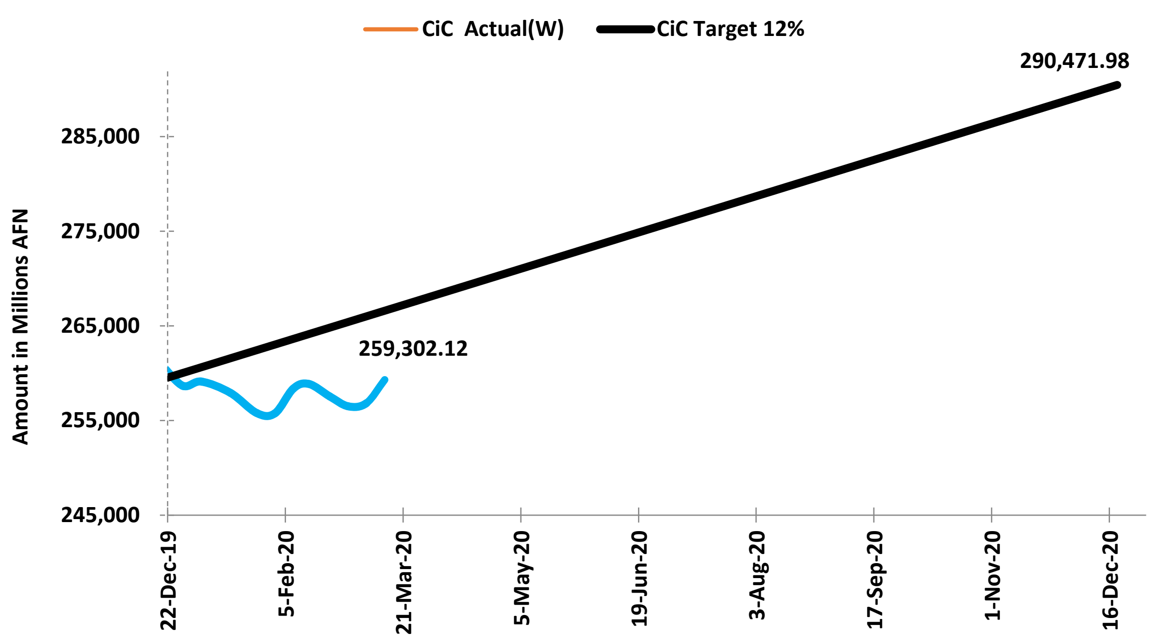
For the fiscal year 1399, the ceilings for reserve money and currency in circulation growth is 12 %. It is worth mentioning that in first quarter actual RM and CiC had negative growth by 8.21% and 0.02% respectively, almost both are below the targets. DAB has auctioned USD 426.19 million via open market operation to mop up the excess liquidity from the market and to prevent intense fluctuations of Afghani nominal exchange rate against foreign currencies, especially internationally convertible currencies. The Figure 2.1 and 2.2 illustrate the ceiling and the actual reserve money and currency in circulation for the period under review.

Figure 2.1: Reserve Money for the 1st Quarter of FY 1399



Source: Monetary Policy Department/DAB

Figure 2.2: Currency in circulation for the 1st Quarter of FY 1399



Source: Monetary Policy Department/DAB

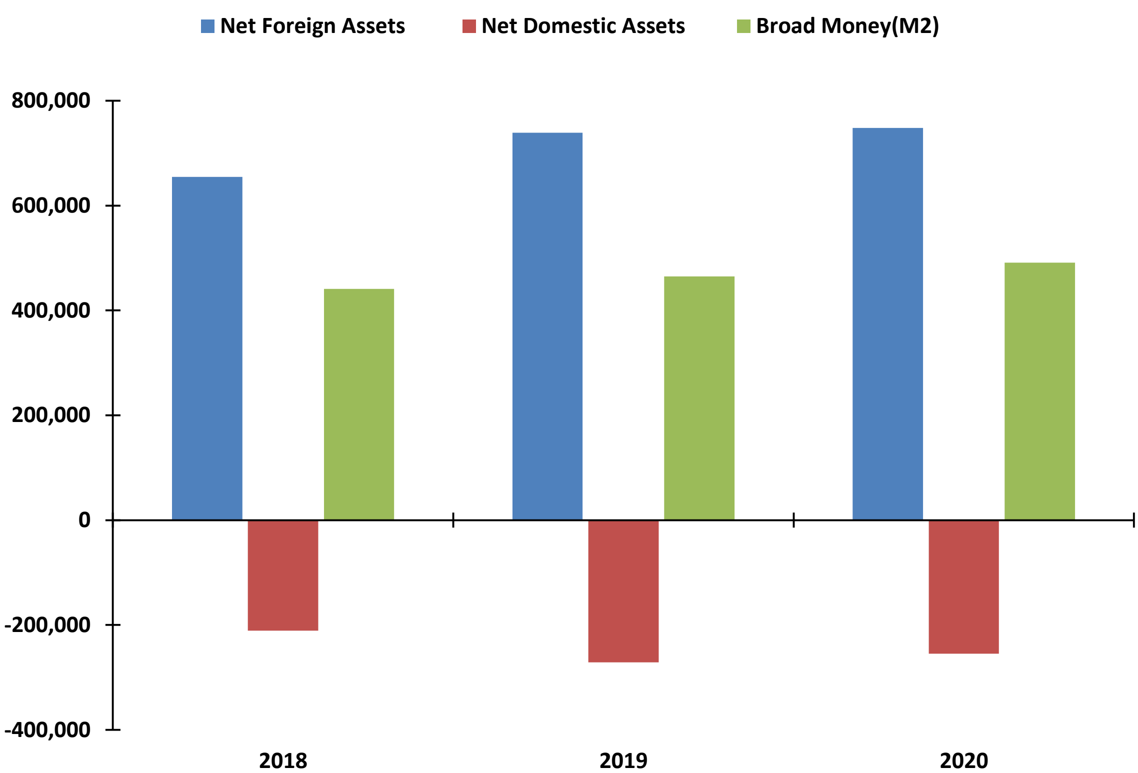
2.2. MONETARY AGGREGATES

Narrow money and broad money are compiled based on Monetary and Financial Statistics Manual and Compilation Guide. 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 7% at the end of the first quarter of fiscal year 1399, almost had higher growth than the same period of FY 1398. Currency outside depository corporations or CiC, which accounts for 51% of M2, grew by 17.30% due to new banknotes issuance during the period under review, higher than 3.8% growth in the same period of the previous year, shown difference of AFN 36,913 million.

Demand deposits, which are the other components of M1, experienced negative growth of 4.04% at the end of first quarter of FY 1399, while its growth rate was 8.6% in same period of previous year. The main reason for the last year higher growth was due to more deposits by people to commercial banks and this year it was decreased because of Covid-19.

Figure 2.3: Net Financial Assets, Net Domestic Assets, and Broad Money



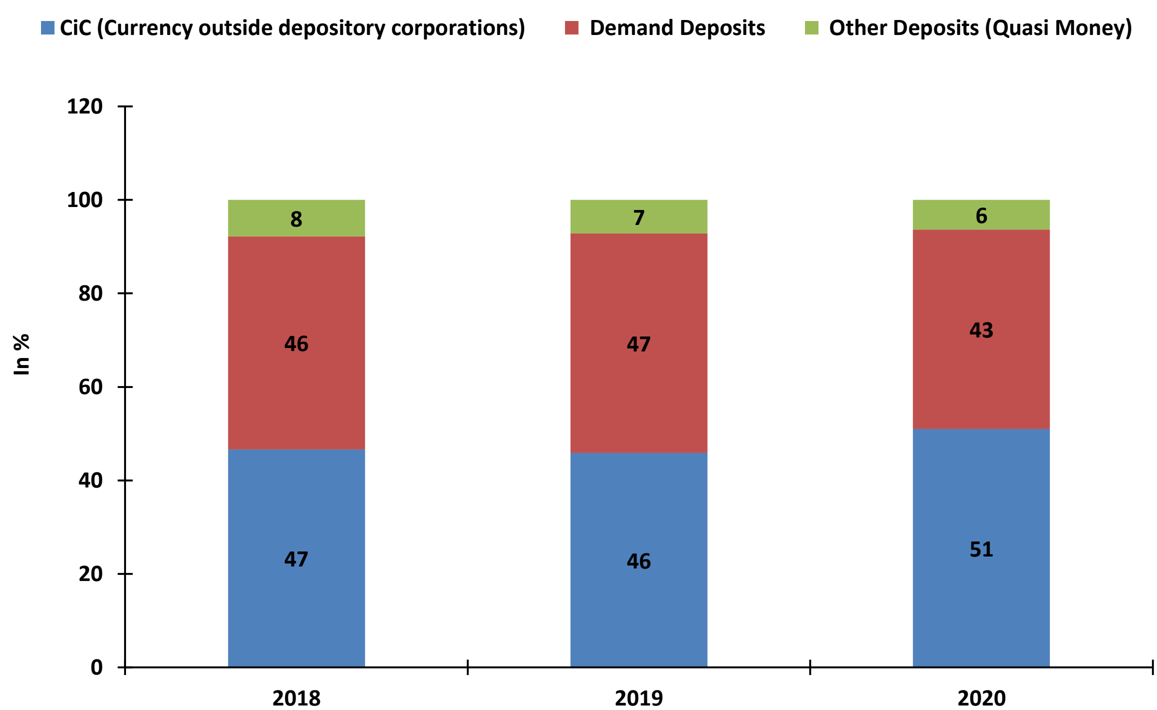
Source: Monetary Policy Department/DAB

Demand deposit in comparison with the same quarter of the previous year shows a negative difference of AFN 8,822 million. Broad money (M2) expanded by AFN 490,857.02 million in the quarter under review from AFN 464,973.331 million in the previous year, showed an increase of 5.57% greater than 5.4% growth in the same period of the last year. Greater growth in broad money is mainly attributed to money supply in the market. The data showed that M1 with a share of 93.67% remained the main contributing component of M2.

Quasi money (other deposits), which is the other component of M2, had negative growth of 6.63% at the end of the first quarter of FY 1399. Quasi money constituted 6.33% of broad money at the quarter under review, which is lower than 7.15% at the end of first quarter of FY 1398 (2019).

Therefore, the impact of changes in quasi money on M2 is negligible. The year-on-year in quarter bases change of Afghani denominated time deposits stood at AFN 7,652 million, shown a negative growth of 18.92%, while the foreign currency denominated time deposits rose by 1.7%, reaching to AFN 23,406 million. Afghani-denominated time deposits and foreign currencies denominated time deposits constituted 1.56% and 4.77% of M2 respectively. Demand deposits as a share of broad money stood at 42.68% at the end of the first quarter of year under review (Figure 2.4).

Figure 2.4: CiC, Demand deposits and quasi money as share of broad money



Source: Monetary Policy Department/DAB

Table 2.1: Monetary aggregates for the 1st Q of FY 1399 (3/19/2019 to 3/20/2020)

Amounts In Million AFN	Mar-18	Mar-19	Y-o-Y Δ	Difference	Mar-20	Y-o-Y Δ	Difference
1- Net Foreign Assets	**654,465**	**738,943**	**12.9%**	**84,479**	**748,330**	**1.27%**	**9,387**
(a) Foreign Assets	670,453	750,544	11.9%	80,090	751,236	0.09%	692
DAB Foreign exchange reserves	561,526	622,883	10.9%	61,358	626,480	0.58%	3,597
Gold	63,757	69,164	8.5%	5,407	78,819	13.96%	9,655
Other	497,769	553,720	11.2%	55,951	547,662	-1.09%	-6,058
Other foreign assets	108,928	127,660	17.2%	18,733	124,755	-2.28%	-2,905
(b) Foreign Liabilities	15,988	11,600	-27.4%	-4,388	2,906	-74.95%	-8,695
2. Net Domestic Assets	**-210,591.92**	**-271,426.48**	**28.9%**	**-60,835**	**-254,803.65**	**-6.12%**	**16,623**
(a) Net Domestic Credit	-76,371	-96,821	26.8%	-20,450	-78,741	-18.67%	18,080
Net Credit to Nonfinancial Public Sector	-120,069	-143,029	19.1%	-22,959	-125,685	-12.13%	17,344
Net Credit to Central Government	-120,164	-143,123	19.1%	-22,959	-125,959	-11.99%	17,164
Credit to Central Government	15,201	7,185	-52.7%	-8,016	167	-97.68%	-7,018
Liabilities to Central Government	135,365	150,308	11.0%	14,943	126,126	-16.09%	-24,182
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	275	190.90%	180
Credit to Private Sector	45,001	47,087	4.6%	2,087	47,402	0.67%	315
Net Credit to Other Financial Corporations	-1,302	-880	-32.5%	423	-458	-47.92%	422
(b) Capital Accounts	159,027	200,472	26.1%	41,445	193,457	-3.50%	-7,014
(c)Other Items Net	24,806	25,866	4.3%	1,060	17,394	-32.75%	-8,472
3- Broad Money(M2)	**441,161.883**	**464,973.331**	**5.4%**	**23,811**	**490,857.02**	**5.57%**	**25,884**
Narrow Money(M1)	406,725	431,707	6%	24,983	459,798	7%	28,091
CiC (Currency outside depository corporations)	205,617	213,388	3.8%	7,770	250,300	17.30%	36,913
Demand Deposits	201,108	218,320	8.6%	17,212	209,498	-4.04%	-8,822
Other Deposits (Quasi Money)	34,437.009	33,265.906	-3.4%	-1,171	31,058.925	-6.63%	-2,207
In Afghani	12,220	9,438	-22.8%	-2,782	7,652	-18.92%	-1,785
In Foreign currency	22,217	23,828	7.3%	1,611	23,406	-1.77%	-422
Securities Other Than Shares	0.000	0.000	0.000	0.000	0.000	0.000	0.000

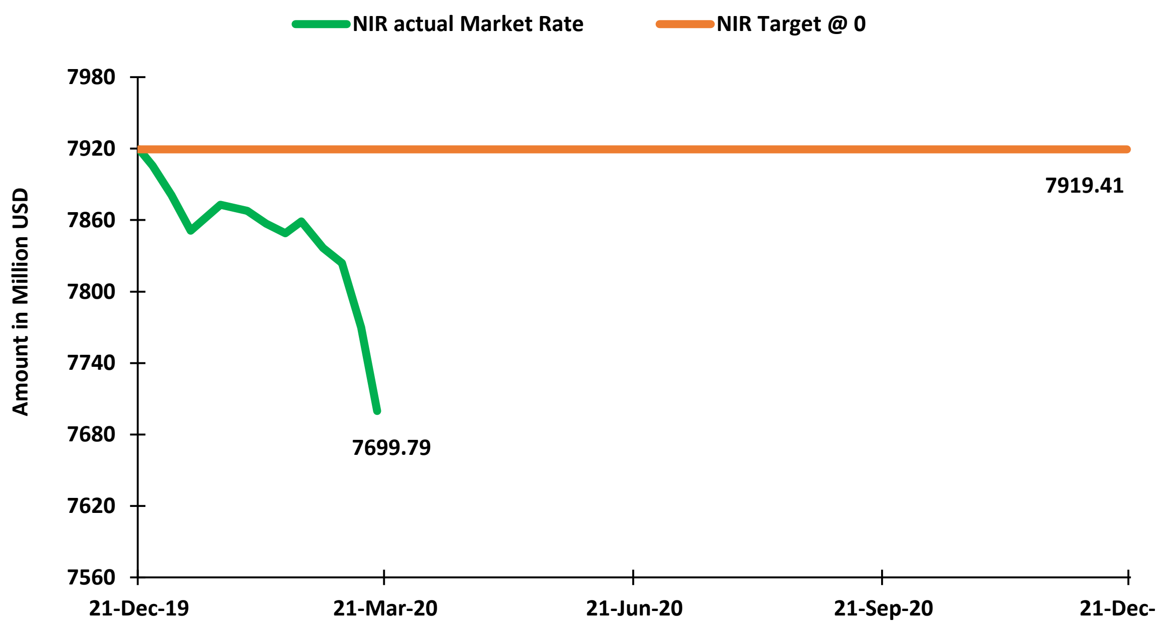
Source: Monetary Sector, Monetary Policy Department/ DAB

2.3. NET INTERNATIONAL RESERVE (NIR)

Da Afghanistan Bank holds international reserves, which consist 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 others. The Net International Reserves (NIR) of Afghanistan, which expressed in terms of US dollar, is defined as reserve assets minus reserve liabilities.

NIR decreased slightly by 2.77% de-accumulation of USD 219.62 million at the end of the first quarter of FY 1399. NIR accumulation ceiling was set at USD 7,919.41 million, while in actual case, NIR reached to USD 7,699.79 million for the period under review. Figure 2.5 illustrates actual and target trend of NIR at Market Rate during the first quarter of 1399.

Figure 2.5: Net International Reserves During 1st Quarter of FY 1399



Source: Monetary Sector, Monetary Policy Department/ DAB

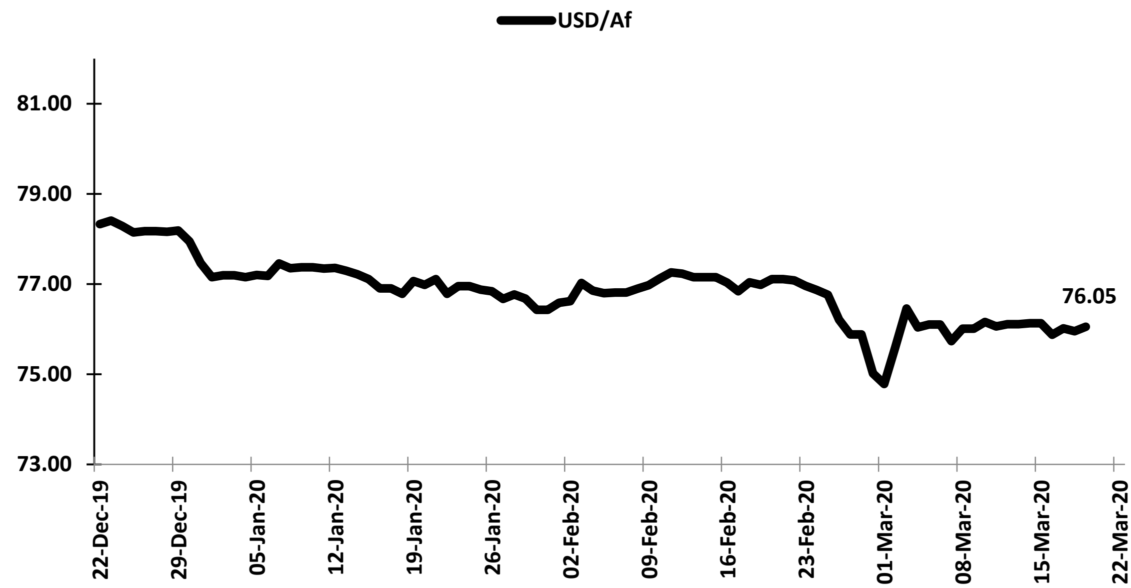
2.4. FROEIGN EXCHANGE MARKET

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 quarter of FY 1399 (2020), Afghani relatively appreciated against the Great British pound, European Euro and Swiss Franc, United

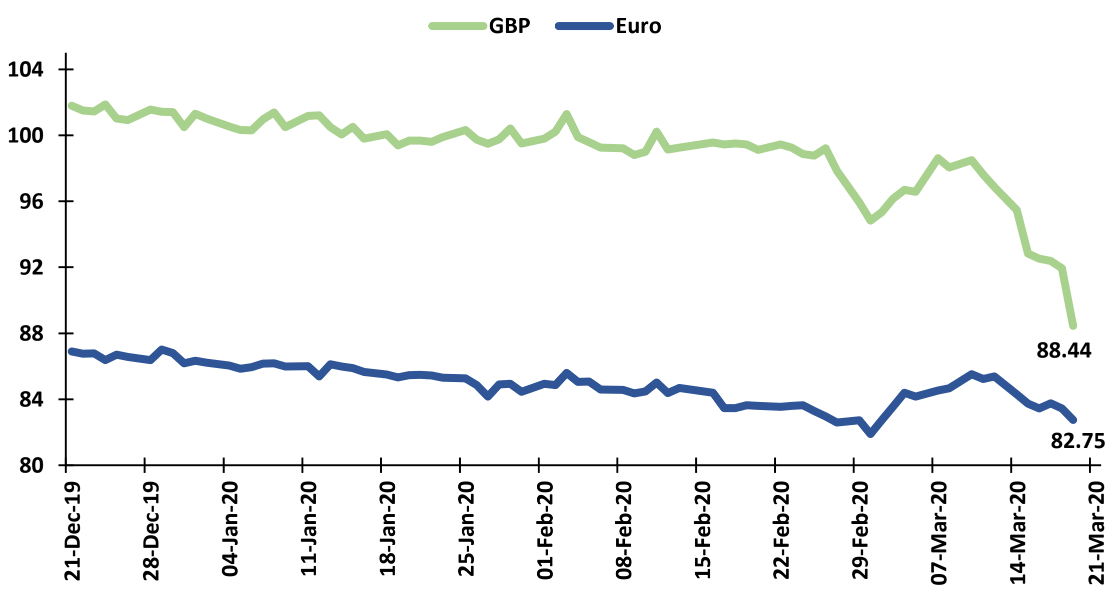
States Dollar, United Arab Emirates dirham and Saudi Riyal, Indian rupee, Pakistani Rupee, and Iranian Toman. The daily historic review of the average exchange rate of Afghani against the U.S. dollars and other foreign currencies in the first quarter of FY 1399 (2020) that are shown in figures below:

Figure 2.6: Exchange Rate of AFN against USD During 1st Quarter of FY 1399



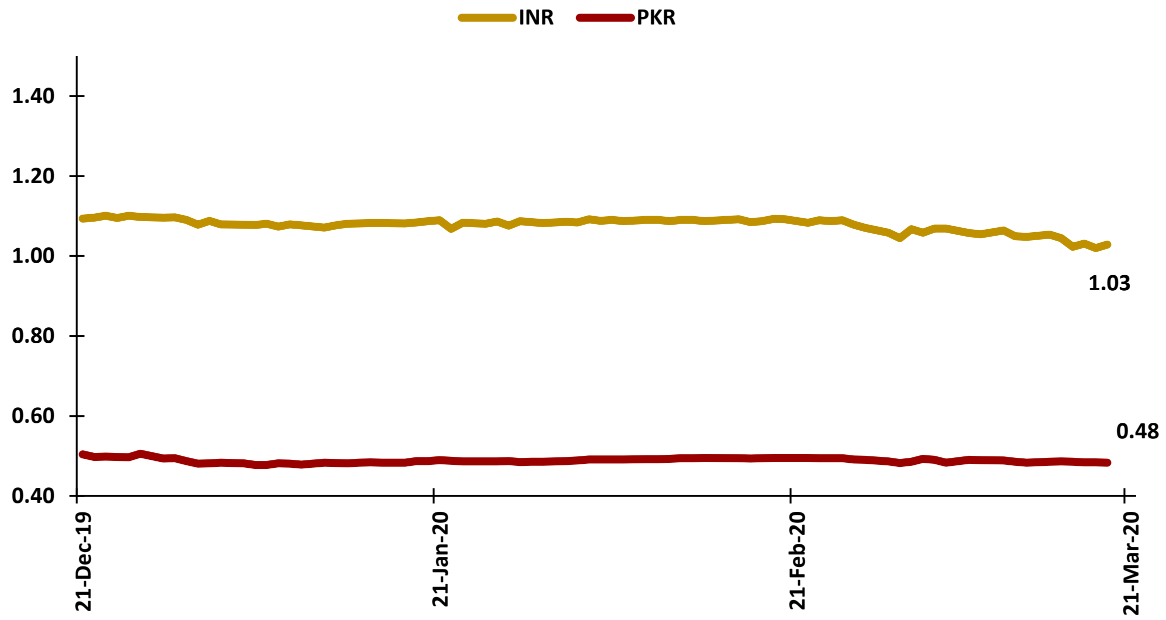
Source: Monetary Sector, Monetary Policy Department/ DAB

Figure 2.7: Ex-rate of Afghani against GBP and Euro during 1st Quarter of FY 1399



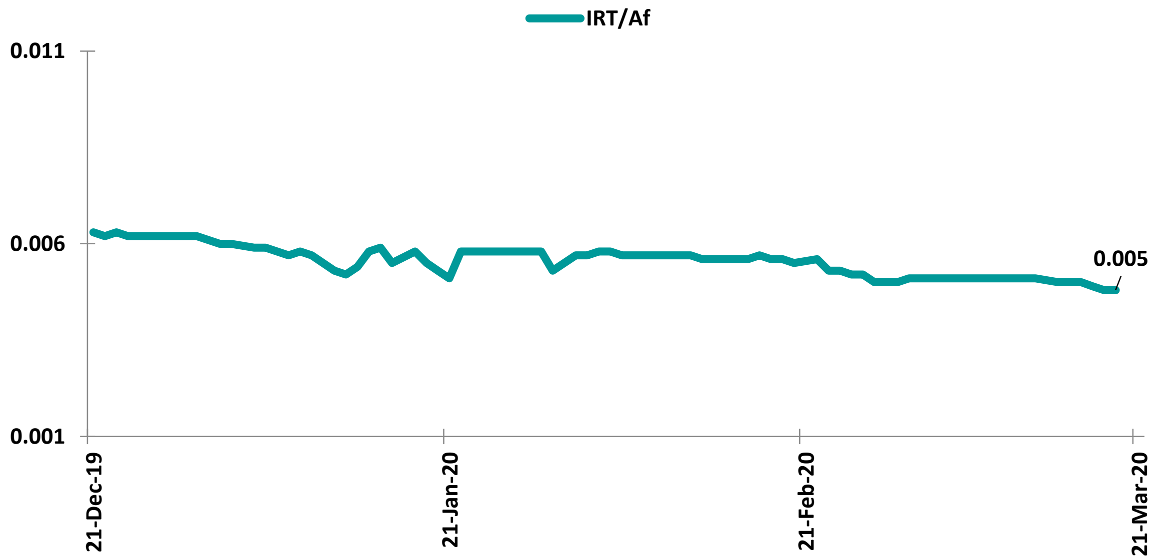
Source: Monetary Sector, Monetary Policy Department/ DAB

Figure 2.8: Ex-rate of Afghani against INR and PKR during 1st Q of FY 1399 (2020)



Source: Monetary Sector, Monetary Policy Department/ DAB

Figure 2.9: Ex-rate of Afghani against IRT during 1st Q of FY 1399 (2020)



Source: Monetary Sector, Monetary Policy Department/ DAB

2.4.2. Foreign Exchange Auction

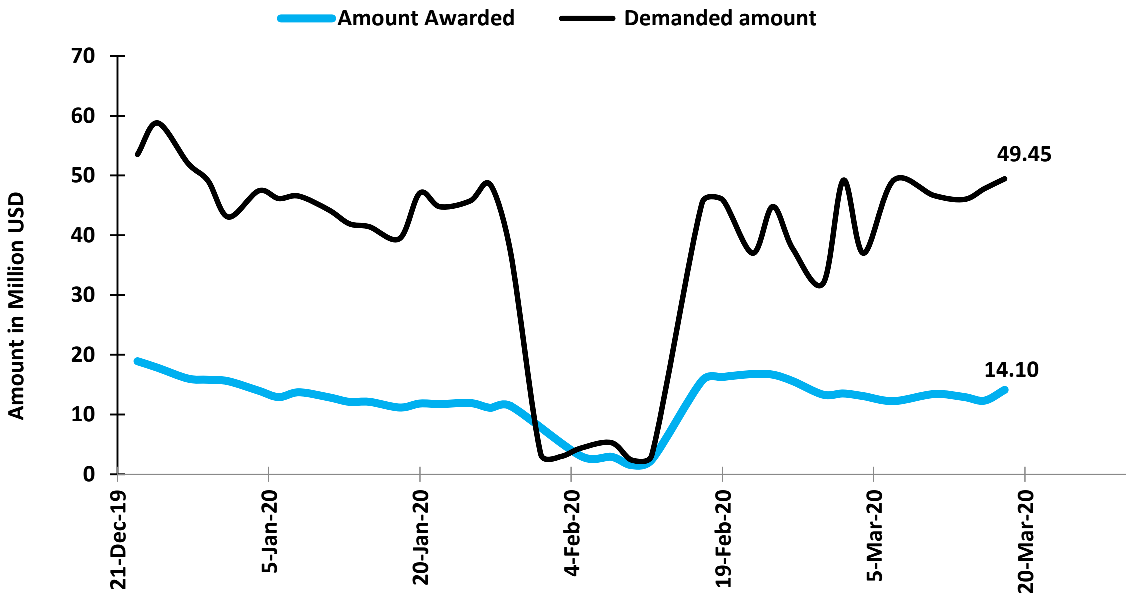
In order to control the money supply and maintain price stability in domestic market, DAB manages the reserve money growth close to its ceiling by conducting FX (USD) auctions three times a week and a weekly capital notes auctions, which are the primary monetary instruments. DAB continued the FX auction to mop up excess liquidity from the market and to smooth out excessive volatility of the exchange rate of Afghani against foreign currencies, especially the U.S dollar.

During the first quarter of FY 1399, DAB auctioned a total amount of USD 426.19 million, while the total demand was USD 1,376.70 million. On average, 49 bidders participated in each auction and

35 bids were announced as the winning bids with the average amount of USD 11.52 million sold in each auction and the total withdrawal is recorded AFN 32.72 billion.

During the first quarter of FY 1398 total auctioned amount of USD 541.94 million recorded, with a total demand of USD 1,370.01 million. On average, 59 bidders participated in each auction and 42 bids were awarded as the winning bids with an average amount of USD 14.26 million in each auction and the total withdrawal is recorded AFN 40.71 billion. Figure 2.10 shows the total amount of USD awarded and demanded through auctions in the first quarter of FY 1399.

Figure 2.10: FX report during 1st quarter of FY 1399



Source: Monetary Sector, Monetary Policy Department/ DAB

2.5. CAPITALMARKET &LIQUIDITY CONDITIONS

2.5.1. Capital Notes Auction

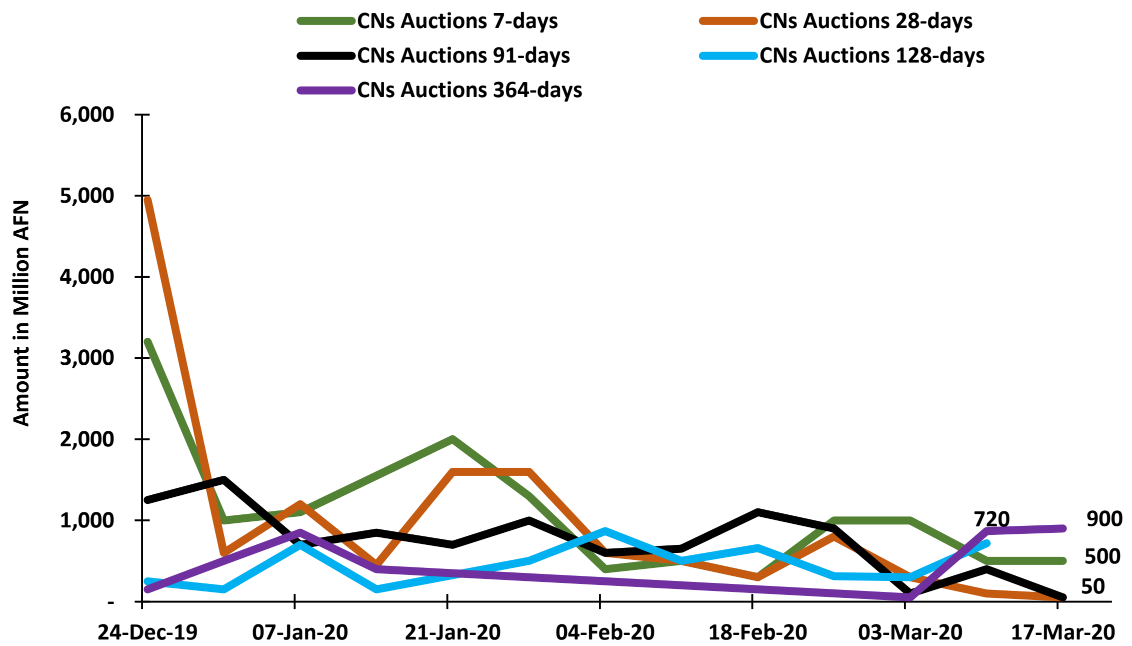
Capital notes are Afghani denominated short–term securities offered by DAB to the primary market customers, which are licensed commercial banks on weekly basis. Da Afghanistan Bank uses Capital Notes (CNs) as a monetary tool to manage the money supply growth, and are used to absorb the excess liquidity 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 to AFN 30.45 billion at the end of the first quarter of FY 1399, which shows an increase of AFN 3.79 billion compared to AFN 26.66 billion at the end of the first quarter of FY 1398. Increase in outstanding amount of capital notes was due to higher sales compared to the same quarter of the last year.

The outstanding stock of 7-days capital notes stood at AFN 0.5 billion, 28-days CNs outstanding amount stood at AFN 1.25 billion, 91-days outstanding stock of CNs recorded the amount of AFN 9.8 billion, 182-days stood at AFN 11.01 billion and the stock of outstanding capital notes for 364-days stood at AFN 7.89 billion. Total interest paid to CNs figured out to AFN 23.34 million till the end of the first quarter under review.

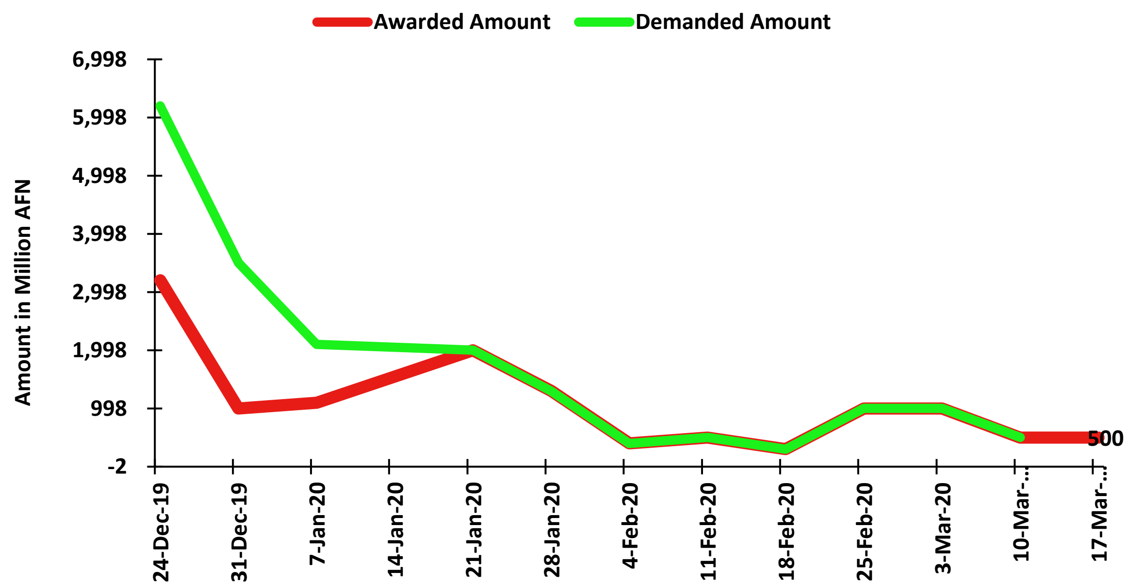
In addition, the weighted average interest rate for 7-days, 28-days, 91-days, 182-days and 364-days capital notes were 0.62%, 0.90%, 1.40%, 1.86%, and 2.5% respectively.

Figure 2.11: Stock of outstanding capital notes during the 1st Quarter of FY 1399



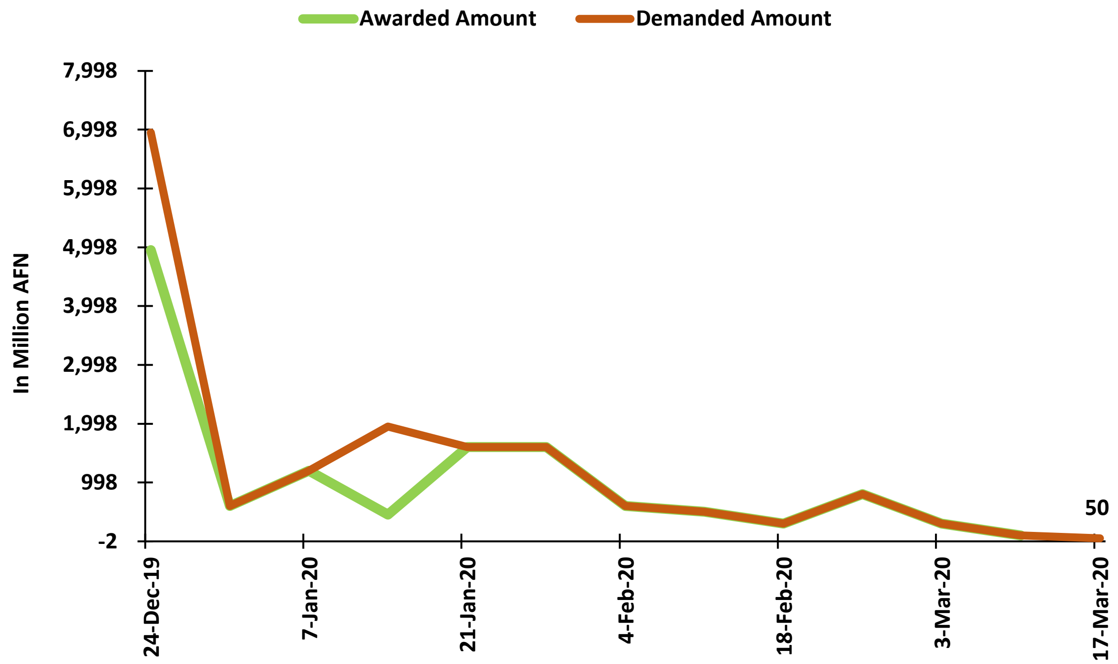
Source: Monetary Sector, Monetary Policy Department/ DAB

Figure 2.12: 7-days CNs demanded and awarded during the 1st Quarter of FY 1399



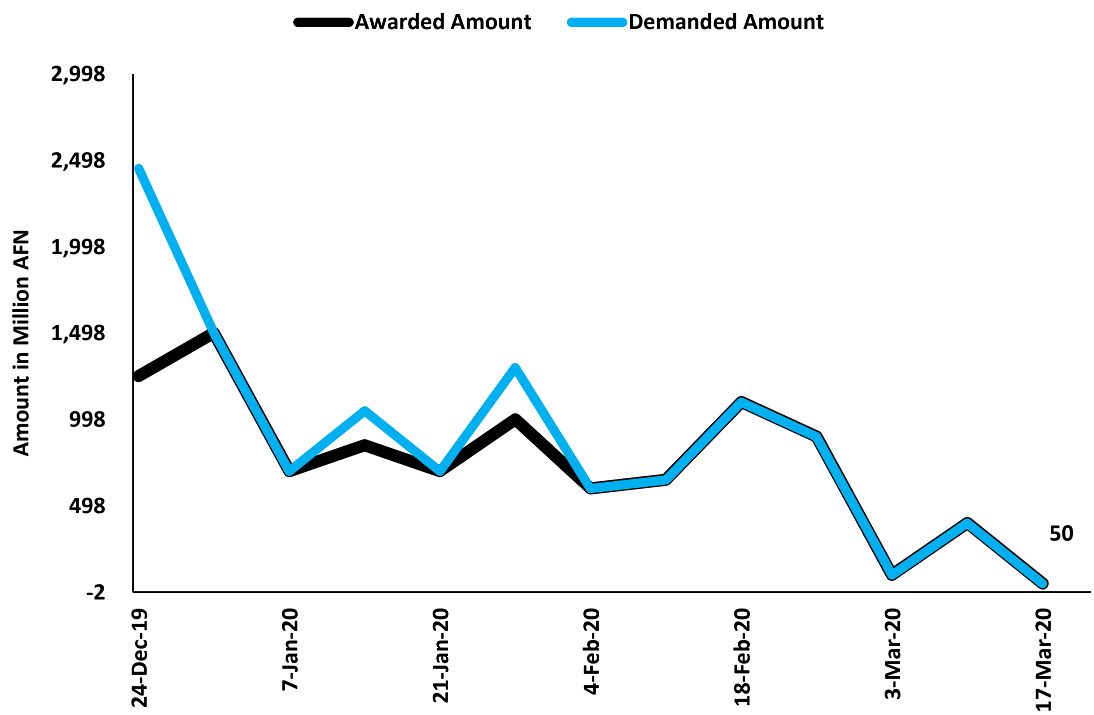
Source: Monetary Sector, Monetary Policy Department/ DAB

Figure 2.13: 28-days CNs demanded and awarded during the 1st Quarter of FY 1399



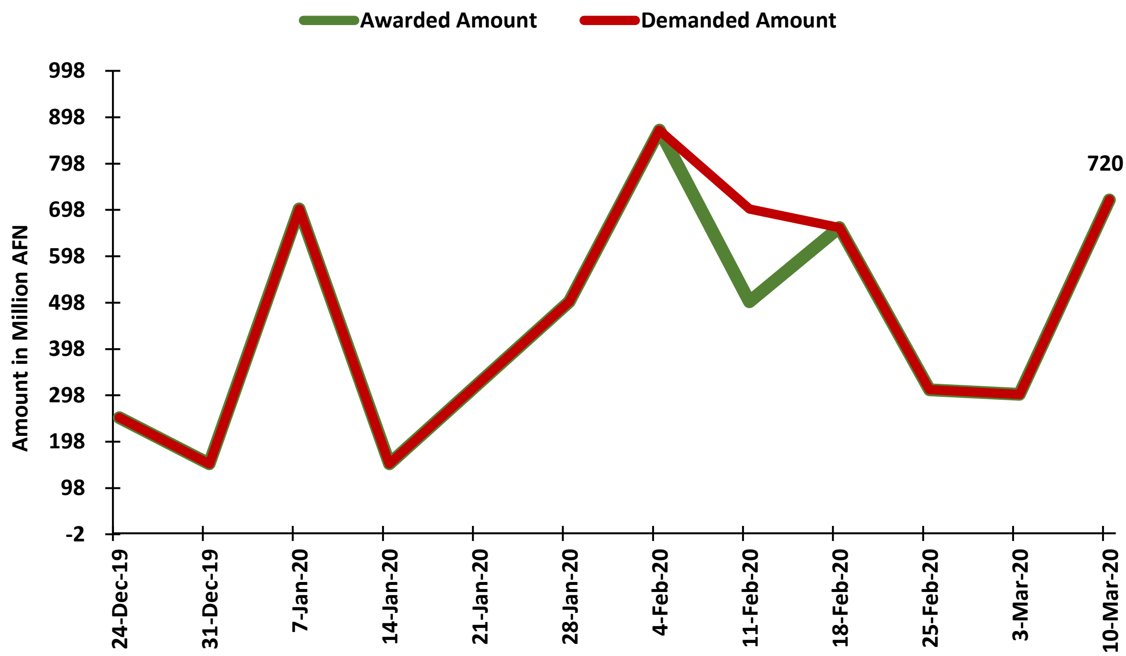
Source: Monetary Sector, Monetary Policy Department/ DAB

Figure 2.14: 91-days CNs demanded and awarded during the 1st Quarter of FY 1399



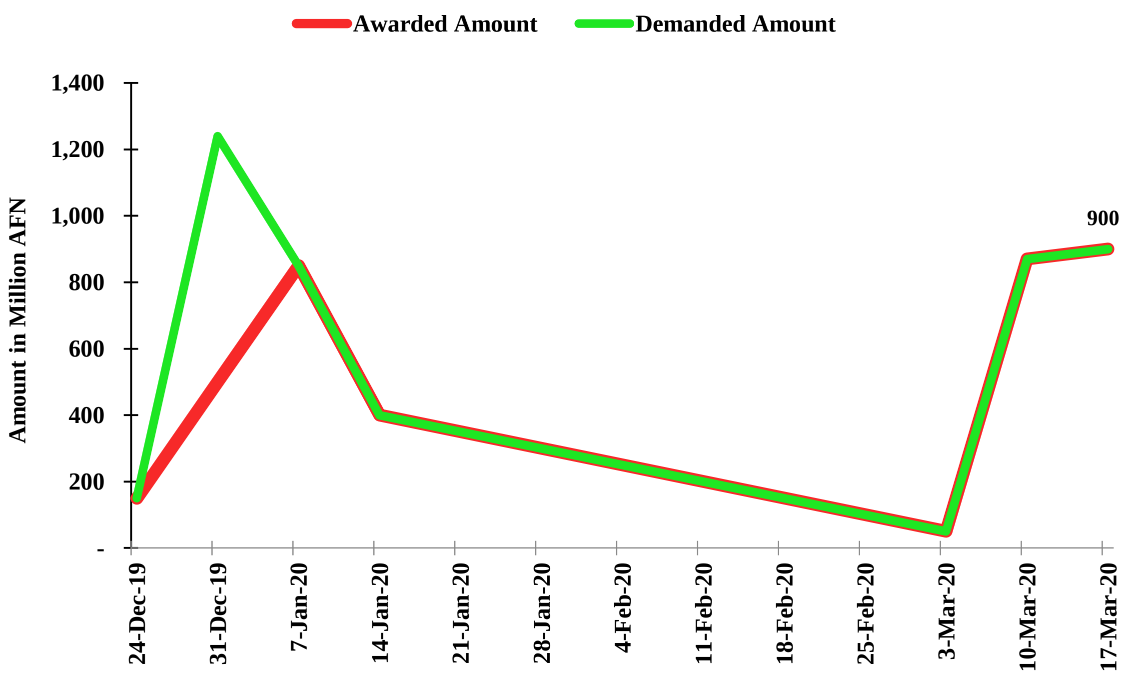
Source: Monetary Sector, Monetary Policy Department/ DAB

Figure 2.15: 128-days CNs demanded and awarded during the 1st Quarter of FY 1399



Source: Monetary Sector, Monetary Policy Department/ DAB

Figure 2.16: 364-days CNs demanded and awarded during the 1st Quarter 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, which required reserves for all deposits were maintained in domestic currency. No interest is given for such deposits to commercial banks. It shows AFN 5,928.75million, USD 207.80 million and Euro 13.40 million recorded at the end of the first quarter of FY 1399.

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 recorded AFN 3,604.58 million at the end of the first quarter of FY 1399 and the payment of interest rate to the mentioned facility reached to AFN 1.54 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 credit facility.

3

Inflation Trend and Outlook

3
INFLATION TREND AND OUTLOOK

3.1. GLOBAL COMMODITY REVIEW

3.1.1. Executive Summary

Almost all commodity prices saw sharp decline during the first three months of 2020 as the market demand worsened due to COVID-19 pandemic. Mitigation measures for the epidemic have significantly reduced transport activities, causing an unprecedented decline in demand for oil. Moreover, weaker economic growth resulting from the pandemic will further reduce overall commodity demand. Crude oil prices are expected to average $35/bbl this year and $42/bbl in 2021, a sharp downward revision from October forecast. Non-energy prices are also expected to fall this year. Metals are projected to decline more than 13% in 2020, before recovering in 2021, while food prices are expected to be broadly stable.

The risks to the price forecasts are large in both directions and depend on the speed at which the pandemic is contained and mitigation measures are lifted. A Special Focus investigates the impact of COVID-19 on commodity markets and compares it with previous disruption episodes. It finds that the impact of COVID-19 has already been larger than most previous events and may lead to long-term shifts in global commodity demand and supply.

3.1.2. Recent Trends

Commodity markets have been buffeted by the COVID-19 pandemic, which has already caused a historical sudden stop in economic activity (Special Focus). The pandemic has affected both the demand and supply of commodities through the impact of mitigation measures on activity and supply chains. The prices of most commodities have fallen since January, especially those that are related to the transportation industry triggered the largest one-day price rise in Brent crude oil since 1988.

The spike unwound rapidly as market participants concluded that the impact would not be long-lasting. Also, on the supply side, growth in the United States has been much weaker than the record pace of 2018, and OPEC and its partners have agreed to continue with their production cuts. While oil production growth has slowed, the weakness in demand has been more severe. Energy prices fell 18.4% (q/q) in 2020 Q1, with a marked deterioration throughout the quarter as the severity of COVID-19 became increasingly apparent. Crude oil prices averaged $32/bbl in March, a decline of 50 percent compared with January. Prices reached a historical low level in April with some benchmarks trading at negative levels.

Demand for oil has collapsed as a result of COVID-19 mitigation measures which have sharply curtailed travel and transport-around two-third of oil demand. The fall in prices was exacerbated by the breakdown of the production agreement between OPEC and its partners in early March, and prices failed to rally when a new agreement to reduce production by 9.7 mb/d disappointed markets in April (Box, Energy section).

While natural gas prices have also seen sizeable declines, albeit less than for crude oil, coal prices have seen smaller decline partly because demand for heating and electricity has been somewhat less affected by mitigation measures. Most non-energy prices also fell in 2020 Q1, but by less than energy prices. The metals and minerals price index fell 5% on the quarter, but with significant variation among its components.

Copper and zinc prices declined by around 15% relative to their January peak, reflecting their close relationship with global economic activity. In contrast, iron mineral prices have fallen just 7%, with weakening demand partly balanced by supply disruptions. Among precious metals, gold prices rose modestly amid heightened uncertainty and safe-haven flows, while platinum prices dropped by 23% reflecting their scant use in the production of catalytic converters in the transportation industry.

With some exceptions, agricultural commodity prices saw minor decline during the first quarter reflecting their indirect relationship to economic growth. However, natural rubber prices fell 25% from their January peak largely because two-third of the crop is used in the manufacture of tires, which is negatively affected by the lockdown. Prices of maize and some edible oils fell as well due to the collapse of biofuel demand.

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.

The year-on-year measure of changes in the consumer price index increased to 3.54% on average in the first quarter of 2020 from 0.84% recorded in the first quarter of the previous year. National inflation measured on quarter-on-quarter basis, indicated an incline in the period under review. Observing the data, the average inflation rate reached to 3.54% in the first quarter of 2020, higher than average rate of 1.71% in the fourth quarter of 2019.

The year-on-year measure of changes in the consumer price index showed an increase in inflation rate of 3.54% on average in the first quarter of 2020 higher than 0.84% recorded in the first quarter of the previous year.

Observing the Kabul headline CPI, the inflation rate on year over year basis increased to 3.27% on average in the first quarter of 2020 from 0.92% in the same quarter of the previous year. This index also increased on quarter-to-quarter basis reaching to 3.27% on average in the first quarter of 2020 from 1.09% in the fourth quarter of 2019.

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 first quarter of 2020. As per the available data, the headline inflation by this measure increased to 3.54% on average in the first quarter of 2020 from 0.84% in the same period of the previews year while on monthly basis, the inflation rate was recorded at 3.75%, 3.84%, and 3.02% in the months of January, February and March respectively.

In the food index, inflation increased to 5.83% on average in the first quarter of 2020 from 0.78% in the same quarter of the previous year. In the above mentioned index, the inflationary pressures came from higher prices of meat, oil and fats, vegetables, sugar and sweets, and spices. The highest increase in the index was recorded in the prices of vegetables and spices which increased to 13.30% and 19.08% on average from -11.17% and 2.85%.

Overall inflation in non-food category inclined to average 1.36% from 0.90% in the first quarter of 2020 compared to same quarter of previous year. This increase was due to higher prices of clothing, housing, health, information and culture, and miscellaneous, while prices of tobacco, furnishing and household goods, transportation, education, and restaurants and hotels declined over the one-year period. In the mentioned category, the highest increase was noted in price index of clothing and information and culture, which increased to 7.76% and 3.36% on average from 4.17% and 0.35% respectively. On the other hand, price index of tobacco and transportation decreased to -0.78% and -4.56% from 4.85% and 6.12% respectively.

Core inflation also showed upward slope in the first quarter of 2020 compared to the first quarter of 2019. Trimmed mean which is the most common measure of core inflation, jumped to 3.57% from 2.29%. In addition, the CPI inflation, excluding bread and cereals, oil and fats and transportation, increased to 3.79% in the first quarter of 2020 from -0.13% in the same period of the previous year.

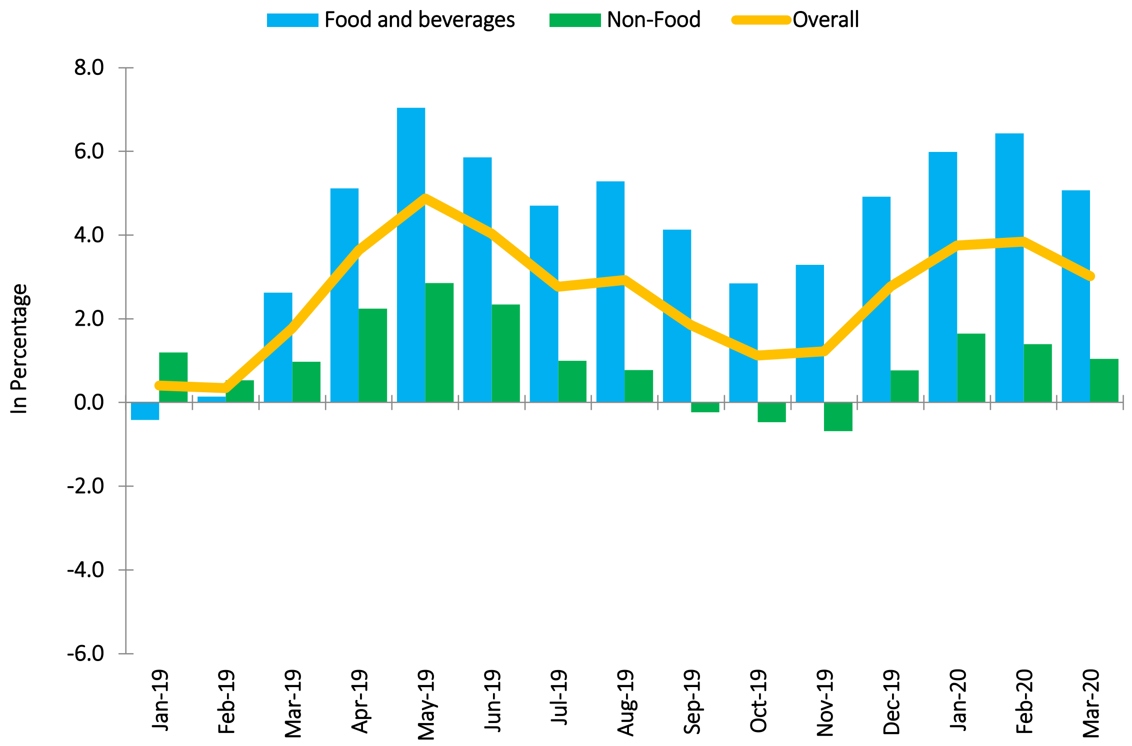
3.2.2. Developments in the National Headline Inflation (Quarter on Quarter Changes)

The short term measure of inflation also reflected upward trend. The national headline inflation on quarter on quarter basis increased to 3.54% on average in the first quarter of 2020 from 1.71% recorded in the previous quarter. Both, food and non-food items represented higher prices during the review period.

Food inflation increased to 5.83% in the first quarter of the current year from 3.68% in the last quarter of the previous year. This increase was the result of price increase in bread and cereals, meat, oil and fats, fresh and dried fruits, and vegetables items. The price indices of food sub-items such as milk, cheese and eggs, sugar and sweets, and spices have decreased in the first quarter of 2020 compared to the fourth quarter of 2019.

Non-food inflation also increased in the first quarter of 2020 from the previous quarter. Observing the data, inflation in this item rose to 1.36% from -0.13%. In this category, the prices of transportation and housing items increased with big margins compared to the other non-food items. On the other hand, prices decreased in some other sub items of non-food category, such as health, education, and restaurants and hotels.

Figure 3.1: National headline inflation (Y-o-Y)



Source: NSIA/ DAB staff calculation

Figure 3.2: Quarterly average national inflation

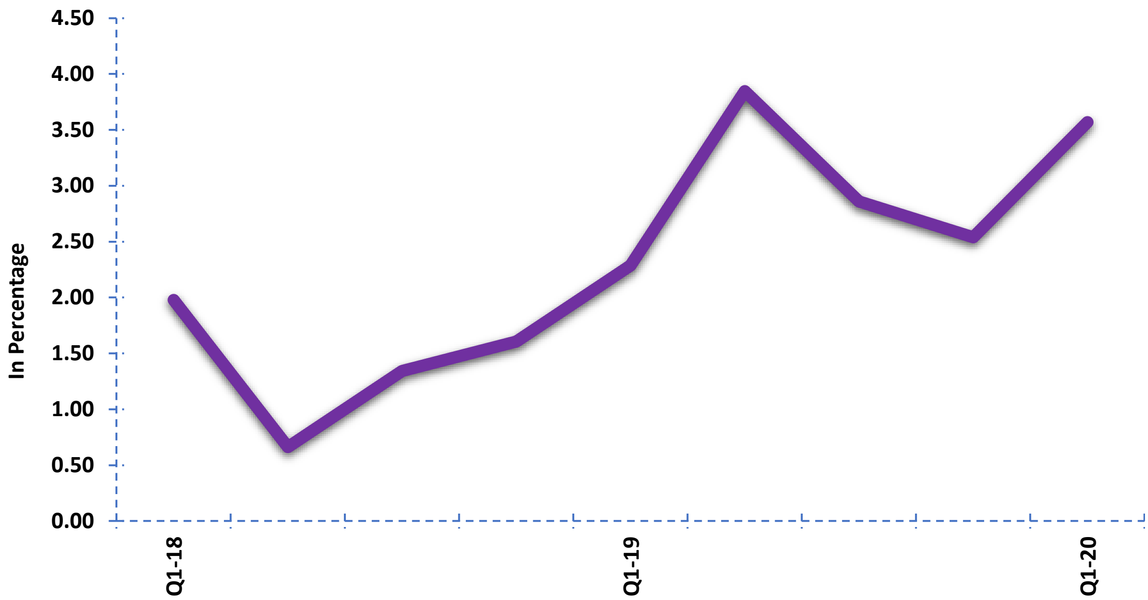
Source: NSIA/ DAB staff calculation

Table 3.1: National headline inflation for 1st quarter of FY 1399

Based on Apr 2015													
Period	2019									2020			
	Weight	Jan 19	Feb 19	Mar 19	Average	Oct 19	Nov 19	Dec 19	Average	Jan 20	Feb 20	Mar 20	Average
Overall Index	100	0.41	0.34	1.77	0.84	1.12	1.22	2.77	1.71	3.75	3.84	3.02	3.54
Food & Non-Alcoholic Beverages	47.8	-0.41	0.14	2.62	0.78	2.85	3.29	4.91	3.68	5.99	6.43	5.07	5.83
Bread and Cereals	14.6	6.14	5.65	6.88	6.22	1.31	1.29	2.06	1.55	3.45	4.29	3.76	3.83
Meat	7.5	1.39	1.37	1.16	1.30	7.57	8.34	8.00	7.97	8.63	9.28	8.67	8.86
Milk, cheese and eggs	4.7	1.38	1.35	1.92	1.55	-0.92	-2.31	-1.74	-1.66	-3.21	-2.63	-3.27	-3.04
Oils and fats	4.6	-2.81	-4.19	-5.46	-4.15	-0.71	0.25	2.18	0.58	5.10	6.27	7.22	6.20
Fresh and dried fruits	5.0	2.45	3.34	5.47	3.75	2.88	3.89	3.74	3.50	3.58	3.06	4.50	3.72
Vegetables	6.0	-17.44	-13.67	-2.40	-11.17	-0.50	3.34	13.24	5.36	16.44	15.90	8.17	13.50
Sugar and sweets	2.7	-0.85	-0.33	4.14	0.98	6.28	3.96	4.66	4.97	5.05	6.30	1.08	4.14
Spices	1.3	0.42	3.92	4.21	2.85	24.01	23.29	21.34	22.88	20.78	17.68	18.78	19.08
Non-alcoholic beverages	1.4	5.15	5.39	6.40	5.65	4.54	3.70	4.10	4.11	4.01	4.18	3.45	3.88
Non-Food Items, Tobacco & Services	52.2	1.19	0.53	0.97	0.90	-0.47	-0.69	0.77	-0.13	1.65	1.39	1.04	1.36
Tobacco	0.3	5.56	4.96	4.04	4.85	-1.08	-2.44	-2.18	-1.90	-1.65	-0.73	0.04	-0.78
Clothing	4.6	5.22	4.05	3.25	4.17	6.02	7.48	7.52	7.01	6.89	8.42	7.97	7.76
Housing	19.1	-2.73	-3.36	-2.31	-2.80	-4.07	-4.17	-1.49	-3.25	0.89	-1.23	-1.63	-0.66
Furnishing and household goods	11.9	2.59	2.71	3.20	2.83	1.42	-0.03	0.42	0.60	1.02	1.42	1.08	1.18
Health	6.2	3.04	2.14	1.89	2.36	5.53	5.67	6.08	5.76	4.41	5.60	5.83	5.28
Transportation	4.3	7.79	4.80	5.77	6.12	-6.67	-7.59	-6.18	-6.81	-4.69	-3.86	-5.14	-4.56
Communication	1.7	-2.63	-2.39	-2.83	-2.62	-6.68	-5.32	-4.43	-5.48	-3.93	-3.60	-4.42	-3.98
Information and Culture	1.1	-0.24	0.95	0.35	0.35	0.61	3.98	4.33	2.97	4.34	3.66	2.07	3.36
Education	0.4	7.88	5.32	6.24	6.48	2.83	0.33	1.58	1.58	-0.85	0.80	0.26	0.07
Restaurants and Hotels	1.1	3.06	3.62	3.20	3.30	1.82	4.07	4.26	3.38	3.61	3.12	3.09	3.27
Miscellaneous	1.4	1.74	0.69	0.35	0.93	6.77	5.53	9.83	7.38	9.79	10.82	12.35	10.99
CPI ex. B & C, O & F, and T		-0.85	-0.60	1.06	-0.13	1.66	1.80	3.48	2.31	4.22	4.05	3.10	3.79
30% trimmed mean		2.02	2.23	2.62	2.29	2.14	2.23	3.26	2.55	3.46	3.89	3.35	3.57

Source: NSIA/ DAB staff calculation

Figure 3.3: Quarterly Trimmed mean



Source: NSIA/ 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 inclined to 3.27% on average in the first quarter of 2020 from 0.92% in the same quarter of the previous year.

The 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 both, food and non-food items. In the food category, higher prices of oils and fats, fresh and dried fruits, vegetables, sugar and sweets; and spices, pushed the inflation rate to 4.88% on average in first quarter of 2020, while it was calculated1.98% in the first quarter of 2019.

inflation IN non-food item, which comprises 62.8% weight of the whole index, has increased to 2.22% on average in the first quarter of 2020 from 0.24% in the same period of the previous year. This increase is attributed to higher prices of clothing, housing, health, communication, information and culture, and restaurants and hotels. In this category, the inflation in clothing item increased to 11.30% on average from 1.29%, housing surged up to -0.22% from -3.95%, health stood at 13.63% higher from 1.75%, communication increased to 0.23% from -0.49%, information and culture turned around to 7.84% from -1.41%; and restaurants and hotels increased to 10.92% from 2.02% in the first quarter of 2020 compared to the same quarter of 2019.

Core 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 first quarter of 2020, core inflation rate increased to 3.57% on average while the rate was recorded 0.19% in the same quarter of the previews year. The 30% trimmed mean also reflected higher inflation rate standing at 4.60% on average in the first quarter of 2020 compared to 2.62% in same quarter of 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 upward movement which reflects higher inflation in both food and non-food items of the CPI. The headline inflation in Kabul inclined to 3.27% on average in first quarter of 2020 from 1.09% recorded in the fourth quarter of 2019.

Inflation in the food index increased to 4.88% on average in the first quarter of 2020 from 2.71% in the previous quarter. In this category, the prices of bread and cereals, oil and fats, fresh and dried fruits, vegetables, sugar and sweets, and non-alcoholic beverages increased which led to higher inflation rate during the period under review. The highest incline was observed in the price index of vegetables which dramatically increased to 15.02% on average in the first quarter of 2020 from 2.97% in the fourth quarter of 2019. On the other hand, few other food sub-items showed decrease on quarterly basis such as meat, and milk, cheese and eggs, which eased to 1.77% from 2.60%, and -6.53% from -5.28% respectively.

The Non-food category of the CPI also showed increase in inflation rate during the first quarter of 2020 compared to the fourth quarter of 2019. Inflation in this category rose to 2.22% on average from 0.06%. The increase in non-food inflation is driven by higher prices of tobacco, housing, furnishing and household goods, transportation, communication, restaurant and hotels which the largest increase was observed in the price of clothing item reaching to 11.30% from 5.20%.

3.3. AFGHANISTAN INFLATION OUTLOOK FOR THE 2nd QUARTER OF FY 1399

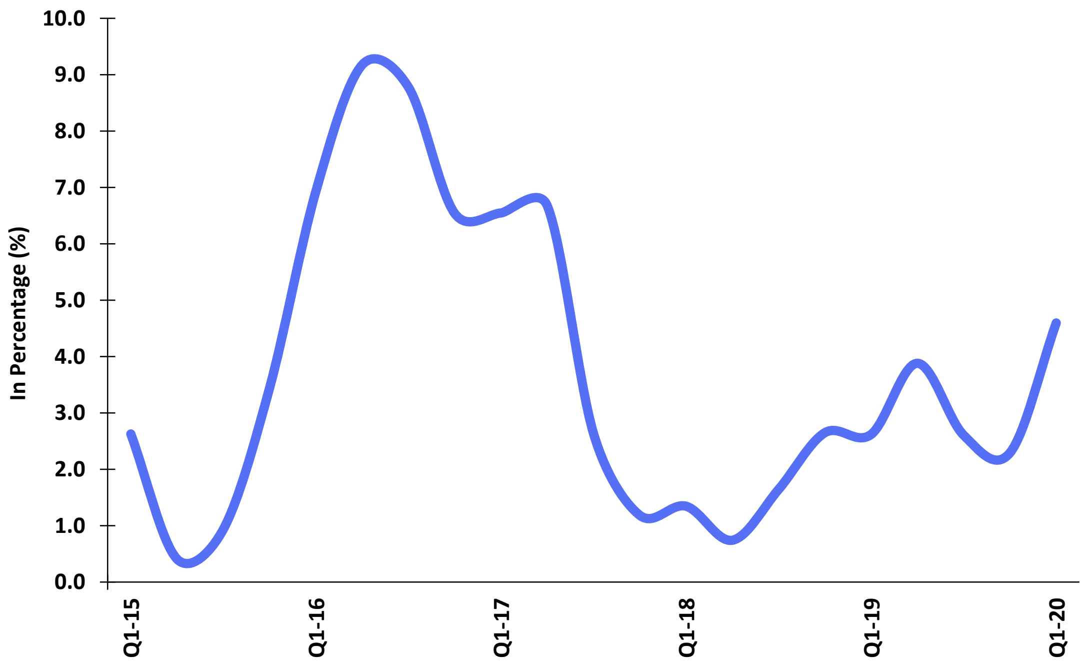
The near-term outlook of inflation is likely to move upward gradually due to COVID-19 pandemic. Monetary policy department forecasts inflation rate 4% to 6% for the second quarter of 2020. The forecast is based on the following course of factors.

Since Afghanistan is an imported 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 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 inflation rate. Looking into the inflation reports of the country's major trading partners, and their forecast for the second quarter of 2020, inflation in most of those countries has been increasing in the first quarter, and their forecast show slight increase for the second quarter compared to the first quarter's actual rate.

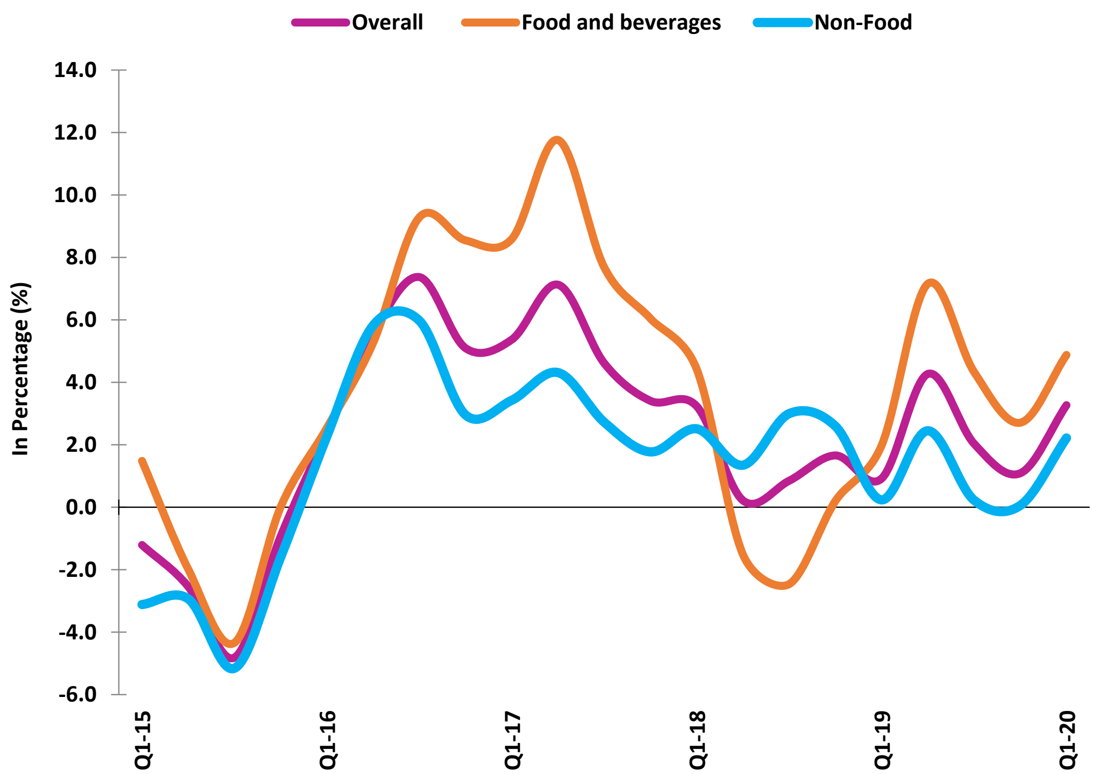
On the other hand, the Afghani exchange rate trends against US dollar have been stable since the starting of the first quarter of 2020, and the expectation for the upcoming months is optimistic. Inflation forecast in Afghanistan may also be conditional to the further spread of COVID-19 pandemic. Continuity 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 second quarter.

Figure 3.4: Kabul quarterly average (30% trimmed mean)



Source: NSIA/ DAB staff calculation

Figure 3.5: Kabul quarterly average inflation



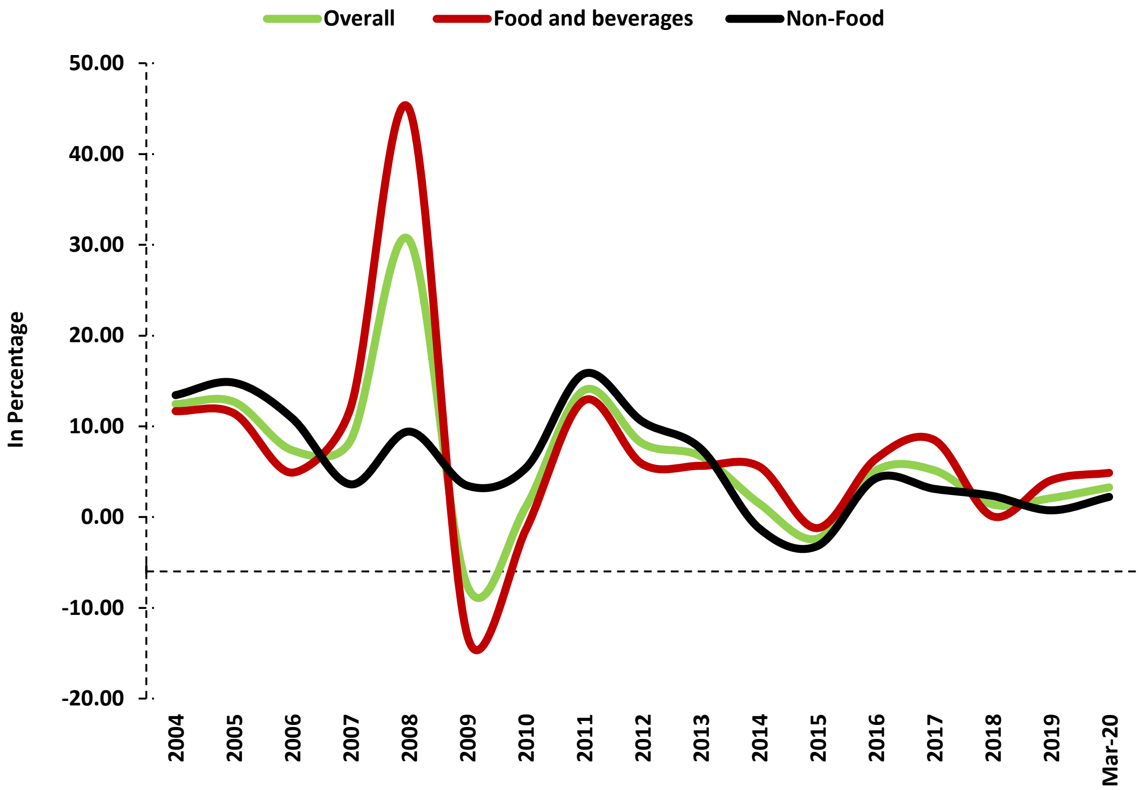
Source: NSIA/ DAB staff calculation

Table 3.2: Kabul headline inflation for 1st quarter of FY 1399

Based on Apr 2015													
Period		2019								2020			
	Weight	Jan 19	Feb 19	Mar 19	Average	Oct 19	Nov 19	Dec 19	Average	Jan 20	Feb 20	Mar 20	Average
Overall Index	100	0.64	0.35	1.77	0.92	-0.52	0.30	3.48	1.09	4.14	3.70	1.96	3.27
Food & Non-Alcoholic Beverages	37.2	0.88	1.14	3.93	1.98	-0.08	2.24	5.98	2.71	6.24	6.05	2.35	4.88
Bread and Cereals	9.8	7.35	8.07	8.35	7.92	1.45	2.76	5.75	3.32	4.85	2.90	2.23	3.33
Meat	6.4	4.24	4.41	2.79	3.81	2.21	3.42	2.16	2.60	2.69	1.58	1.04	1.77
Milk, cheese and eggs	3.2	4.54	5.35	2.78	4.22	-3.50	-6.38	-5.98	-5.28	-6.99	-5.82	-6.78	-6.53
Oils and fats	3.6	-0.49	-1.81	-5.55	-2.62	-1.59	-3.89	-0.47	-1.98	4.86	2.79	6.87	4.84
Fresh and dried fruits	5.2	1.49	0.32	2.51	1.44	-1.75	4.20	7.54	3.33	5.90	6.48	8.23	6.87
Vegetables	4.2	-17.64	-15.22	2.55	-10.10	-14.95	-0.01	23.88	2.97	22.69	25.10	-2.73	15.02
Sugar and sweets	2.8	0.53	-2.13	7.54	1.98	6.41	2.70	4.07	4.39	6.10	11.11	0.15	5.78
Spices	1.0	4.29	8.38	8.70	7.12	25.78	30.85	22.22	26.28	20.11	14.41	18.12	17.55
Non-alcoholic beverages	0.9	5.76	7.43	6.01	6.40	4.97	4.54	3.78	4.43	6.47	4.82	4.25	5.18
Non-Food Items, Tobacco & Services	62.8	0.49	-0.16	0.39	0.24	-0.80	-0.91	1.88	0.06	2.77	2.18	1.71	2.22
Tobacco	0.3	3.85	3.87	3.19	3.64	-0.37	-2.31	-2.07	-1.59	-1.23	-0.05	0.38	-0.30
Clothing	4.8	3.74	0.73	-0.59	1.29	2.74	5.51	7.38	5.21	9.38	13.15	11.37	11.30
Housing	23.5	-3.80	-4.63	-3.42	-3.95	-3.59	-3.39	1.30	-1.90	2.70	-1.37	-1.98	-0.22
Furnishing and household goods	17.6	2.79	3.31	4.01	3.37	-0.58	-2.60	-2.00	-1.73	-1.10	-0.83	-1.17	-1.04
Health	5.3	1.69	2.13	1.42	1.75	7.25	9.69	13.37	10.10	12.29	14.03	14.57	13.63
Transportation	4.6	4.73	1.11	3.79	3.21	-5.76	-7.62	-5.43	-6.27	-4.47	-2.67	-3.67	-3.60
Communication	2.0	-0.56	0.08	-0.99	-0.49	-1.47	-1.38	-0.84	-1.23	-0.21	0.75	0.16	0.23
Information and Culture	1.7	-1.77	-0.25	-2.20	-1.41	-0.67	6.62	7.11	4.35	7.77	8.50	7.24	7.84
Education	0.7	9.76	6.22	7.55	7.84	1.13	-2.36	-0.76	-0.66	-4.06	-2.04	-2.77	-2.95
Restaurants and Hotels	1.0	1.99	3.33	0.75	2.02	3.41	9.36	9.31	7.36	9.94	10.73	12.10	10.92
Miscellaneous	1.3	5.80	3.99	3.02	4.27	11.80	8.65	18.17	12.87	16.04	17.40	20.70	18.05
CPI ex. B & C, O & F, and T		-0.26	-0.43	1.26	0.19	-0.40	0.66	3.89	1.38	4.50	4.18	2.04	3.57
30% trimmed mean		2.76	2.34	2.77	2.62	0.89	1.88	4.12	2.30	5.03	5.33	3.44	4.60

Source: NSIA/ DAB staff calculation

Figure 3.6: Kabul annual average inflation



Source: NSIA/ DAB staff calculation

4

External Sector Developments

4

EXTERNAL SECTOR DEVELOPMEN

4.1. SUMMARY

The external sector exhibited a significant improvement in the first quarter of the FY 1399, with a notable decline in trade deficit and continued inflows to the primary income account together with current and capital transfers to the country. Higher export earnings, which recorded almost 12% growth for the three consecutive months, and a deceleration in import expenditure, resulted in a significant quarter-on-quarter decline in trade deficit in the first quarter of the FY 1399.

However, inflows to the financial account of the BOP continued amidst decreased foreign investments during the quarter under review. Reflecting these developments, the BOP recorded an overall deficit of around USD 735 million at end of the first quarter of the FY 1399. Meanwhile, the level of gross official reserves indicated a slightly decline particularly with the injection of foreign currency liquidity to the domestic foreign exchange market by the Central Bank during the quarter under review.

4.2. BALANCE OF PAYMENTS

4.2.1. Current Account

The balance of payments (BOP's) current account deficit significantly decreased by 24% to a value of USD 972.10 million in the first quarter of the FY 1399 as compared to a value of USD 1,276.92 million recorded in the first quarter of the FY 1398, (table 4.1 and figure 4.1).

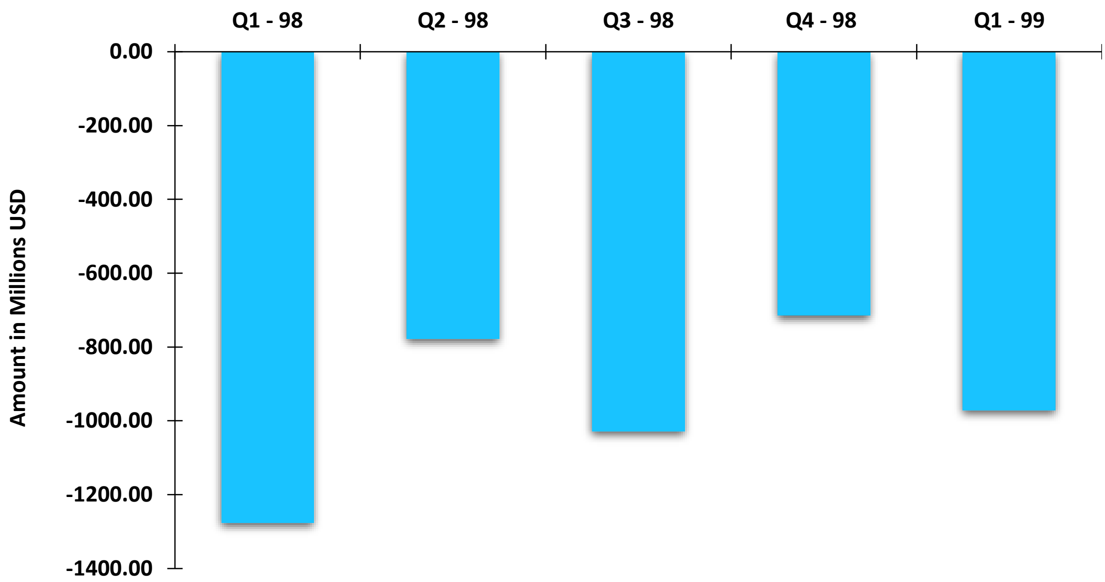
This development was mainly due to a notable decline 21% in merchandise trade deficit, a modest increase of 10% in net inflows to the primary income account together with official grants to the country during the quarter under review. The deficit of merchandise trade account contracted by 19% in the first quarter of the FY 1399 in comparison with the corresponding quarter of the previous year mainly due to a healthy performance in export earnings.

However, the cumulative trade deficit expanded at a moderate rate during the first nine months of the FY 1398. Expenditure on imports decelerated in the quarter under review, mainly due to the decline in expenditure on flour and wheat flour, vegetable oil and fabrics imports owing to lower volumes. Fuel imports declined as a result of low crude oil imports in volumes despite an increase in prices. Expenditure on construction sector related imports showed a mixed performance, as building materials led by cement imports increased, while imports of metal production (iron, steel) of both finished and raw forms decreased in the first quarter of the FY 1399.

During the first quarter of the FY 1399 the deficit of services account dropped dramatically by 41% and stood at a value of USD 94.99 million which followed by marginal decreases in payments of transportation, travel and construction services. Meanwhile, compensation of employees together with investment income inflows increased by 10% to a value of USD 83.52 million in the first quarter of the FY 1399 from a value of USD 75.91 million recorded in the similar quarter of the last year.

As well as, official grants to the government sector and worker personal home remittances from foreign countries declined by 16% and stood at a value of USD 225.60 million in the first quarter of the year under review from a value of USD 267.65 million recorded in the similar quarter of the last year.

Figure 4.1: Current account balance



Source: NSIA/DAB staff calculations

4.2.2. Capital Account

Inflows to the capital account decreased during the quarter under review significantly on account of inflows to the government sector in the form of official grants. This change was mainly attributed to low level of donors' grants in development projects and shrinking of the debt relief by the creditors.

Based on the available data, inflows to the capital account declined significantly by 35% to a value of USD 36.06 million in the first quarter of the FY 1399 from a value of USD 55.49 million recorded in the first quarter of the FY 1398.

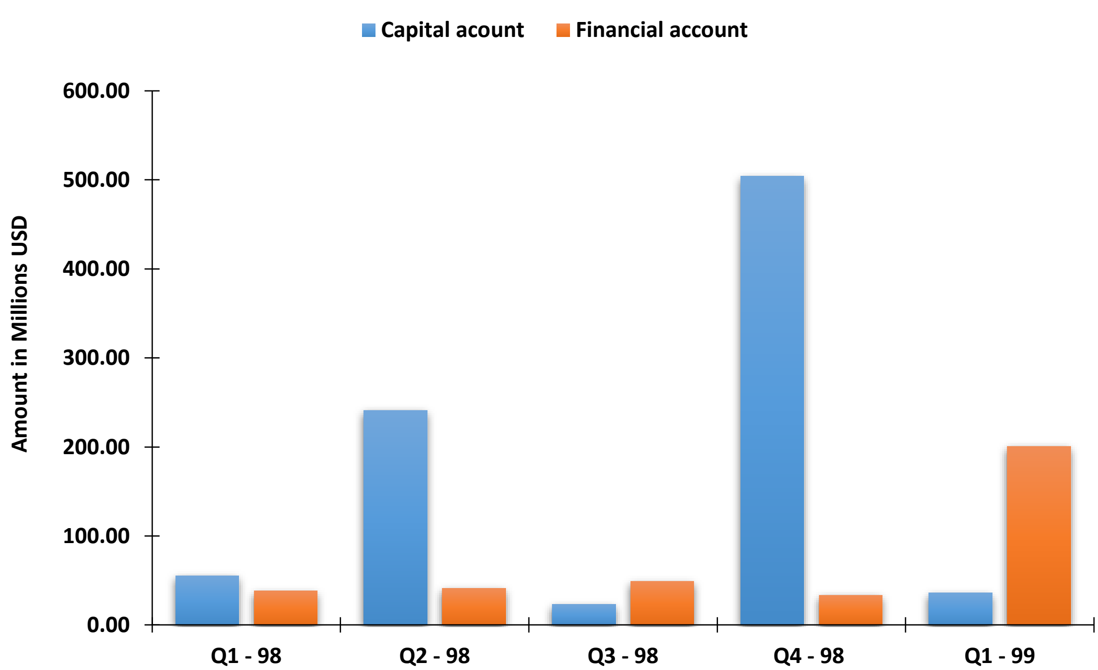
4.2.3. Financial account

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. Sustained security and political concerns hit the level Net FDI inflows in the country. Considering the statistics, FDI inflow stood at USD 5.85 million in the first quarter of the FY 1399 from a value of USD 8.81 million recorded in the first quarter of the FY 1398.

Meanwhile, portfolio investment exhibits USD -4.05 million which reflects withdrawal of Afghanistan investment from foreign countries in the first quarter of the FY 1399 from the value of USD -16.46 million registered in the first quarter of the FY 1398. Further analysis reveals that the country's other aggregated financial assets abroad dropped significantly to a value of USD 28.25 million in the first quarter of the FY 1399 from a value of USD 86.19 million that was captured in the first quarter of the FY 1398 (figure 4.2 & 4.3).

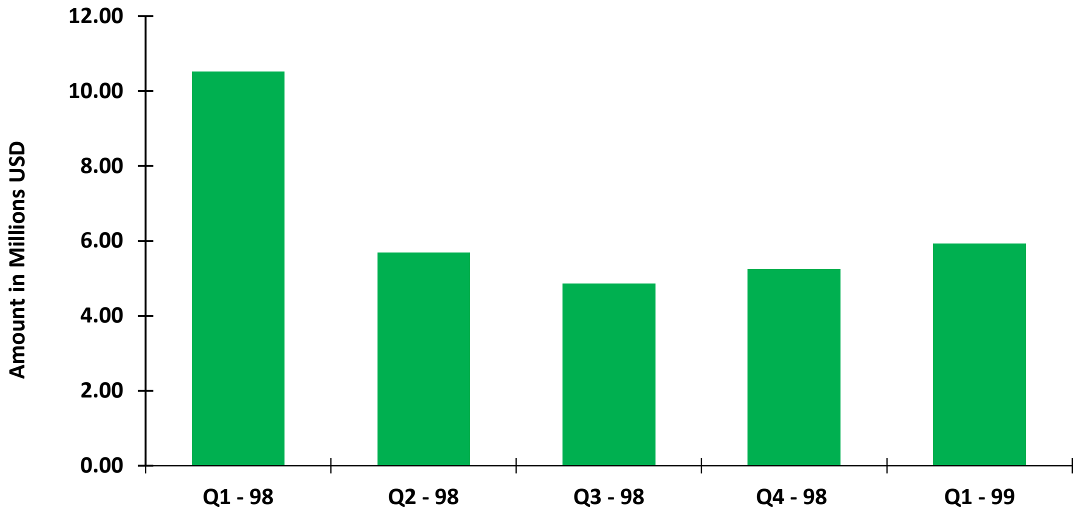
in the meantime, other aggregated financial liabilities, followed upward trend and stood at a value of USD 31.75 million in the first quarter of the FY 1399 from a value of USD -14.58 million recorded in the similar quarter of the previews year. The financial account balance as a total stood at USD 200.68 million in the first quarter of the FY 1399 which is well above the value of USD 38.3 million recorded in the first quarter of the FY 1398.

Figure 4.2: Capital and Financial Account



Source: NSIA/DAB staff calculations

Figure 4.3: FDI inflows



Source: DAB staff calculations

4.3. MERCHANDISE TRADE

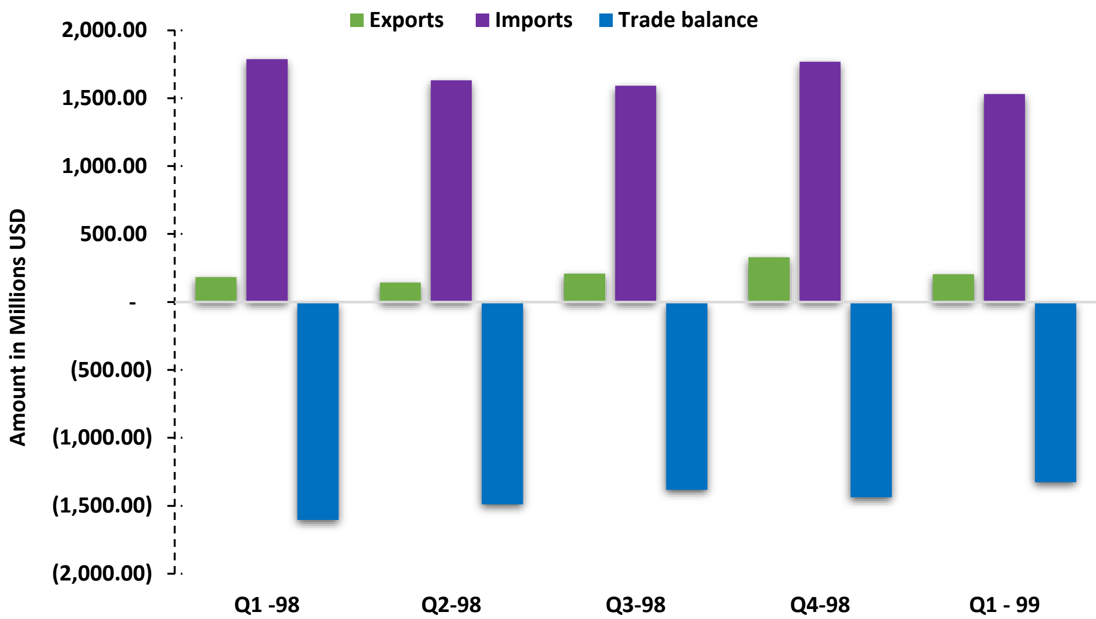
Afghanistan's merchandise trade balance has been in a deficit position for a long period of time. This indicates that the total value of imported goods has been greater than the total value of exported goods.

Base on the available data, deficit of merchandise trade balance had a downward slope and stood at USD 1,326.42 million in the first quarter of the FY 1399 from a deficit of USD 1,603.77 million recorded in the first quarter of the FY 1398. This shows approximately 17% declines in trade deficit as compared to the same quarter of the previous year (table 4.2, figure 4.4).

The record showed that the total earnings from exports of goods increased by 12% to a value of USD 203.64 million in the first quarter of the FY 1399, from a value of USD 182.57 million recorded in the first quarter of the FY 1398. Looking to export components, the exports of food item (oil seeds, fresh and dry fruit), and medical seeds shows upward trends; while carpet and rugs and leather and wools followed downward trend during the quarter under review.

Aggregated expenditure on import of goods declined by almost 14% to a value of USD 1,530.05 million in the first quarter of the FY 1399 compared to a value of USD 1,786.34 million recorded in first quarter of the previous year. Observing the data in composition of imports, the decreases in expenditure on imports were mainly due to slowing down of local demand for consumer goods, fuel and lubricant and industrial supplies during the quarter under review.

Figure.4.4: Trade performance and Trade balance



Source: NSIA/DAB staff calculations

4.4. DIRECTION OF TRADE

Trade between Afghanistan and its trading partners are categorized; as export destinations and import origins. Figure 4.5 and 4.6 shows Afghanistan's direction of trade with its trading-partners during the first 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.

4.4.1. Direction of Exports

Observing the data, **India ranked as the first and top export destination for Afghanistan during the first quarter of the FY 1399.**

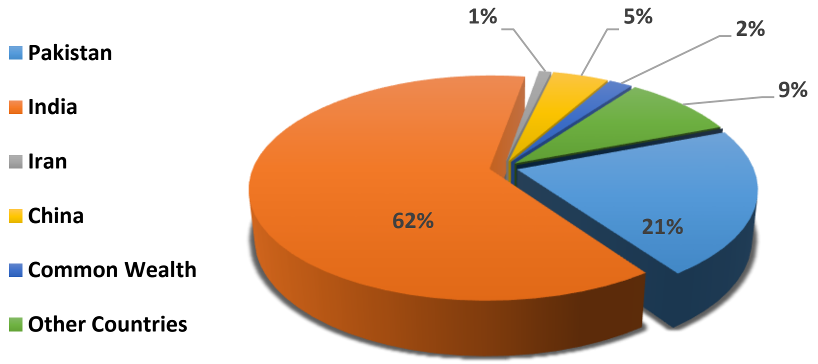
The share of Afghanistan's total exports to India reached to 61% which is well above 52% registered in the first quarter of the FY 1398. In terms of value, total exports to India rose by 30% to a value of USD 124.20 million in the first quarter of the FY 1399 from a value of USD 95.33 million recorded in the first quarter of the previous year.

Pakistan ranked the second largest buyer of Afghanistan export during the first quarter of the FY 1399. The share of Afghanistan's exports to Pakistan dropped down to 21% in the first quarter of the FY 1399 from 27% that was recorded in the similar quarter of the last year. In respect of value, Afghanistan's total exports to Pakistan also decreased by 15% to a value of USD 41.97 million in the first quarter of the FY 1399 compared to a value of USD 49.19 million recorded in the first quarter of the FY 1398.

The next two largest export destinations are China and Iran countries during the first quarter of the FY 1399. The share of total exports to China slightly rose to 4.41% in the first quarter of the FY 1399 from 3.80% registered in the first quarter of the FY 1398. Total exports to China increased by 30% to a value of USD 8.98 million in the first quarter of the FY 1399 from a value of USD 6.93 million captured in the first quarter of the FY 1398. (Figure 4.5 & 4.6).

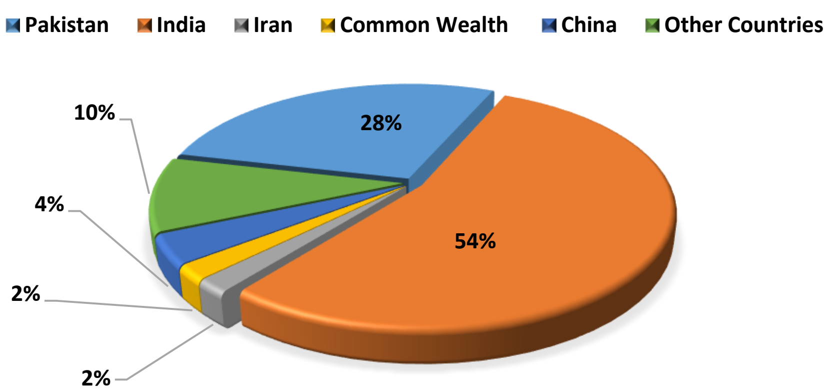
Likewise, total export to Iran declined by 40% to a value of USD 1.97 million in the first quarter of the FY 1399 from a value of USD 3.28 million recorded in the first quarter of the FY 1398. While, the share of total exports to Iran declined to 1% in the first quarter of the FY 1399 from 2% which recorded in the first quarter of the FY 1398 (see tables 4.3, 4.4 and figures 4.5, 4.6).

Figure 4.5: Direction of Exports (% share) for first quarter of FY 1399



Source: NSIA/DAB staff calculations

Figure 4.6: Direction of Exports (% share) for first quarter of FY 1398



Source: NSIA/DAB staff calculations

4.4.2. Direction of Imports

CIS countries were the first largest sources of imports for Afghanistan during the first quarter of the FY 1399. Total Imports from CIS countries exhibits a decline during the quarter under review. Based on statistics the total imports from mentioned sources declined by 5% to a value of USD 442.07 million with share of 29% in the first quarter of the FY 1399 from a value of USD 467.73 million with share of 26% in the first quarter of the FY 1398.

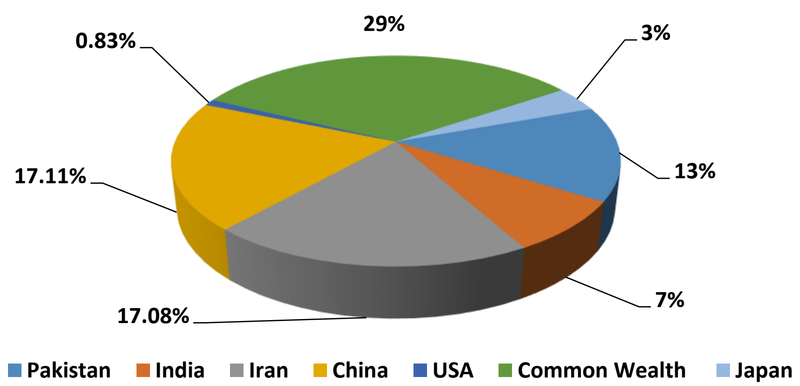
China ranked the second largest imports origin for Afghanistan in the first quarter of the FY 1399. The total imports from china decreased by 22% and stood at a value of USD 261.73 million with share of 17.11% in the first quarter of the FY 1399 from a value of USD 336.22 million with share of 19% recorded in the first quarter of the FY 1398.

Iran was the third largest source of imports for Afghanistan in the first quarter of the FY 1399. The total Imports from Iran declined by 17% to a value of USD 261.38 million with share of 17.08% in the first quarter of the FY 1399 from a value of USD 314.30 million with shares of 18% registered in the first quarter of the FY 1398.

Pakistan graded the fourth largest import origin to Afghanistan in the first quarter of the FY 1399. As per the statistics, imports from Pakistan significantly declined by 25% to a value of USD 192.37 million with share of 13% in the first quarter of the FY 1399 from a value of USD 255.66 million with share of 14% in the first quarter of the FY 1398.

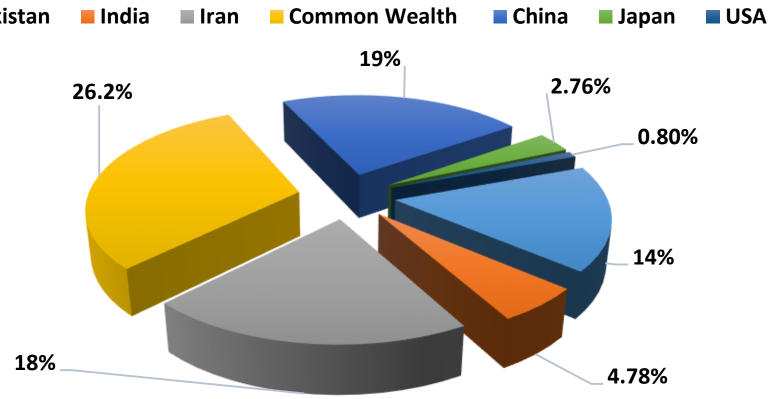
India, Japan, United Arab Emirates and Germany were the last largest sources of imports for Afghanistan in the first quarter of the FY 1399. The shares of each source in the total imports were accounted as 7%, 3%, 2%, and 1% respectively. (Figure 4.7 & 4.8).

Figure 4.7: Direction of Imports (% share) for first quarter of FY 1399



Source: NSIA/DAB staff calculations

Figure 4.8: Direction of Imports (% share) for first quarter of FY 1398



Source: NSIA/DAB staff calculations

4.5. COMPOSITION OF TRADE

4.5.1. Composition of Imports

The total imports of Afghanistan in the first quarter of the FY 1399 are classified into four categories which were described as below:

- ✓ Imports of Capital goods had the first largest share in the basket of imports during the first quarter of the FY 1399, which expanded to 39% from 32% recorded in the similar quarter of the last year.

  At the same time, the import value of such goods also grew by 5% to a value of USD 599.49 million in the first quarter of the FY 1399 from a value of USD 568.74 million registered in the first quarter of the FY 1398.

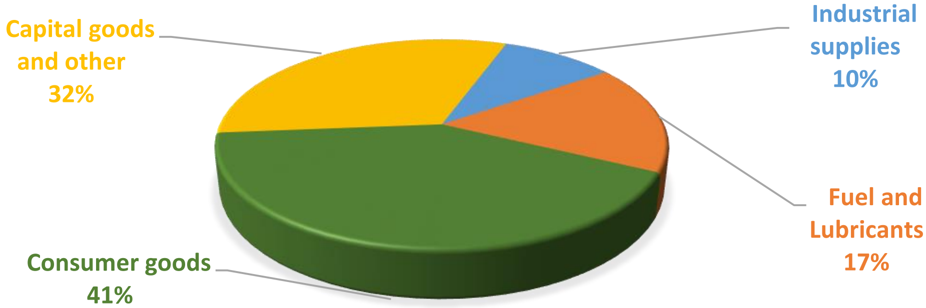
- ✓ Imports of consumer goods faded and hold the second largest share in the imports basket. Observing the data, the share of consumer goods decreased from 42% to 33%. In terms of value, imports of consumer goods significantly declined by 31% to a value of USD 510.61 million in the first quarter of the FY 1399 from a value of USD 741.35 million recorded in the same quarter of the previous year.

- ✓ Imports of fuel and lubricants (petroleum oil) hold the third largest share in the basket of Afghanistan's imports which is remaining unchanged 17% in the first quarter of the FY 1399.

  In terms of value, imports of fuel and lubricants in total imports declined by 13% to a value of USD 261.60 million in the first quarter of the FY 1399 from a value of USD 302.34 million recorded in the first quarter of the FY 1398.

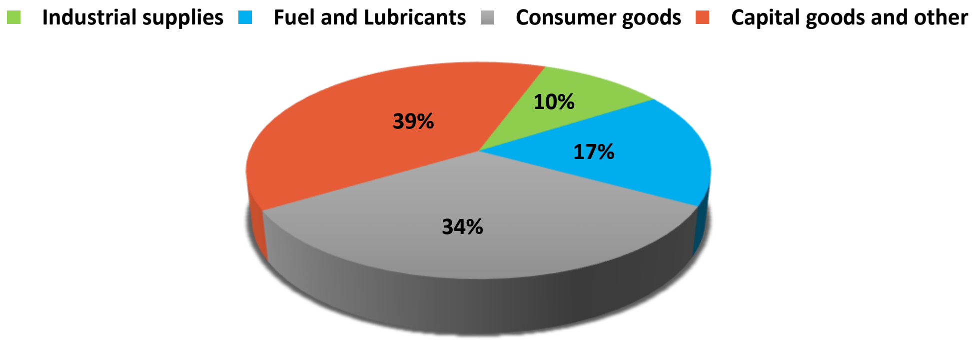
- ✓ In the import category the industrial supplies hold the smallest share in the basket of Afghanistan's imports which is increased to 10.35% in the first quarter of the FY 1399 from 9.74% recorded in the first quarter of the FY 1398. In term of value it exhibits that the imports of such goods shrank by 9% and stood at a value of USD 158.35 million in the first quarter of the FY 1399 from a value of USD 173.92 million captured in the first quarter of the FY 1398, (Figure 4.9 - 4.10).

Figure 4.9: Composition of Imports (share %) for first quarter of FY 1398



Source: NSIA/DAB staff calculations

Figure 4.10: Composition of Imports (share%) for first quarter of FY 1399



Source: NSIA/DAB staff calculations

4.5.2. Composition of Exports

The total merchandise exports of the country have been categorized and analyzed as bellow:

- ✓ Exports of medical seeds had the largest share in the category of total basket of Afghanistan's exports, which slightly rose to 46.7% in the first quarter of the FY 1399 from 45% recorded in the similar quarter of the previous year. The increment was mainly due to rises in the exports of medical seeds and saffron to USD 44.84 million and USD 9.29 million in the first quarter of the FY 1399 from USD 39.26 million and 8.05 million recorded in the first quarter of the FY 1398 respectively.

At the same time, Earnings from exports of medical seeds grew by 15% to a value of USD 95.09 million in the first quarter of the FY 1399 from a value of USD 82.37 million recorded in the same quarter of the previous year.

- The food items (oil seeds, fresh and dry fruits) had the second largest share in total exports during the quarter under review. Based on statistics, share of the mentioned item slightly increased to 46.5% in the first quarter of the FY 1399

  from 46% recorded in the comparable quarter of the last year. At the same time export value of food items increased by 13% to a value of USD 94.61 million in the first quarter of the FY 1399 from a value of USD 83.93 million registered in the first quarter of the FY 1398. The same has occurred mainly due to increment in harvesting of oil seeds and fruits all over the country.

- The Leather and wool products stood the third largest share in the basket of total exports. Share of this item recorded 5% in the quarter under review and as well as in the same quarter of the previous year respectively.

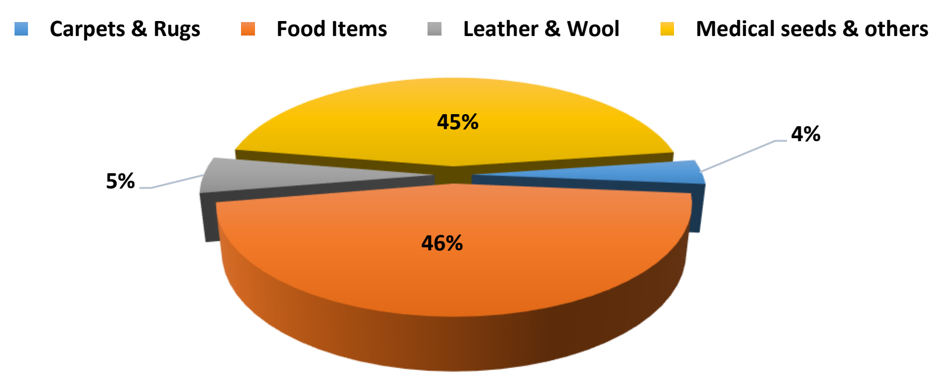
  In term of value, the earning from exports of leather and wool slightly declined by 3% and reached to a value of USD 9.39 million in the first quarter of the FY 1399 from a value of USD 9.69 million recorded in the corresponding quarter of the preceding year.

- Carpet and rugs are considered as a main component of Afghanistan's exports in the past decades. It has constituted the last largest share in total exports which is declined to 2% in the first quarter of the FY 1399 as compared to 4% registered in the first quarter of the FY 1398.

  The total value of exports on carpet and rugs had a downward movement and stood to USD 4.54 million which showed a noticeable decrement of 31% as compared to the value of USD 6.57 million recorded in the first quarter of the last year.

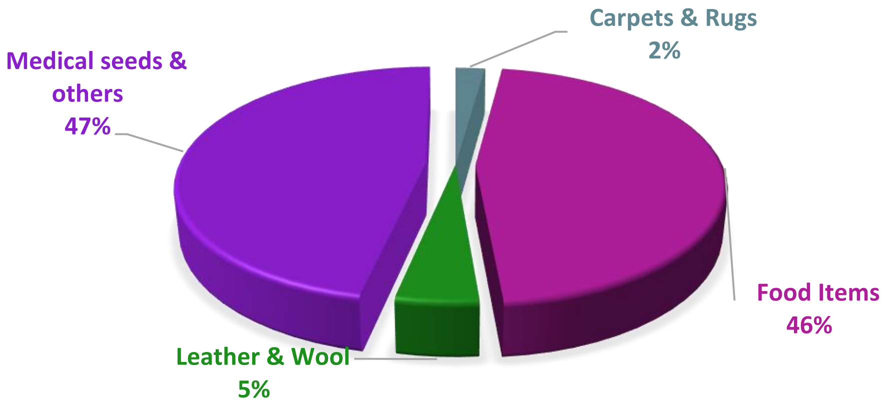
(Figures 4.11 and 4.12) indicate composition of exports in the related periods.

Figure 4.11: Composition of Exports (share%) for first quarter of FY 1398



Source: NSIA/DAB staff calculations

Figure 4.12: Composition of Exports (share%) for first quarter of FY 1399



Source: NSIA/DAB staff calculations

4.6. EXTERNAL DEBT

Afghanistan's total public external debt stood at USD 1,908.55 million at the end of first quarter of the FY 1399, which showed USD 541.79 million reductions from the value of USD 2,450.34 million recorded in first quarter of the previous year. Considering the statistics, the total public external debt shrank by 22% during the quarter under review. The reduction was not only due to repayment of the loan principle and the accumulated interest of the previous periods but it was also due to the exchange rate fluctuations during the period under review (figure 4.13).

Among all, the Asian Development Bank, Islamic Development Bank and OPEC Fund were the creditors received their loan principles, while service charges were paid only to the World Bank, Asian Development Bank and Islamic Development Bank during the quarter under review. The World Bank and Asian Development Bank as a major multilateral creditor to Afghanistan made USD 187.9 million debt release on principle as well as USD 19.8 million as services charge during the quarter under review. Bilateral loan is segregated into two parts; Paris club and Non-Paris Club creditors.

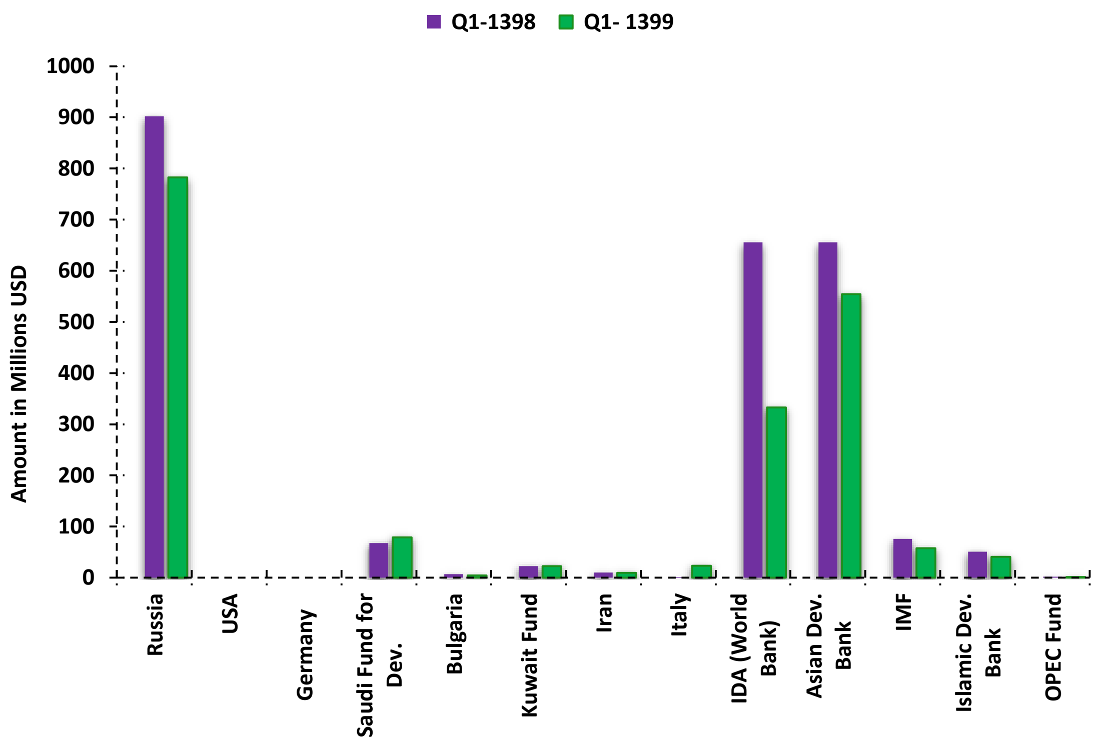
The total amount of loan payable to Paris Club creditors especially Russian federation stood at a value of USD 782.90 million at the end of first quarter of the FY 1399 from the amount of USD 902.09 million recorded in the same quarter of last year. Based on quarter-on-quarter comparison, it registered 13% decline to debt stocks to the mentioned creditor. The reduction was mainly due to the depreciation of Russian's Ruble against USD.

Total debt from Non-Paris Club members (Saudi Fund for Development, Bulgaria, Kuwait fund, Iran and Italy) rose by 27% to a value of USD 138.46 million in the first quarter of the FY

1399 from a value of USD 108.81 million recorded in the first quarter of the FY 1398.

On the other hand, total debt from multilateral creditors to Afghanistan dropped by 31% and stood at a value of USD 987.19 million in the first quarter of the FY 1399 from a value of USD 1,439.44 million recorded in the first quarter of the FY 1398 which shows USD 452.25 million decline in the total debt during the quarter under review.

Figure 4.13: External Debt Comparison; end of Q1-1398 & end of Q1-1399



Source: Debt Management Unit, Ministry of Finance

4.7. NET INTERNATIONAL RESERVES

The Da Afghanistan Bank holds and manages the Gross and Net International Reserve, which consist of monetary gold, reserve position in the fund, Special Drawing Rights (SDR) other liquid foreign exchanges such US dollars, Euro and Great British Pound. The Afghanistan Net International Reserve (NIR) is measured as country Gross International Reserves (GIR) minus reserve related liabilities.

The country GIR stood at USD 8,306.47 million at the end of the first quarter of the FY 1399 from the amount of USD 8,345.44 million registered in the similar quarter of the previous year. Based on the figure, about a USD 38.99 million have been restricted in the GIR during the quarter under review.

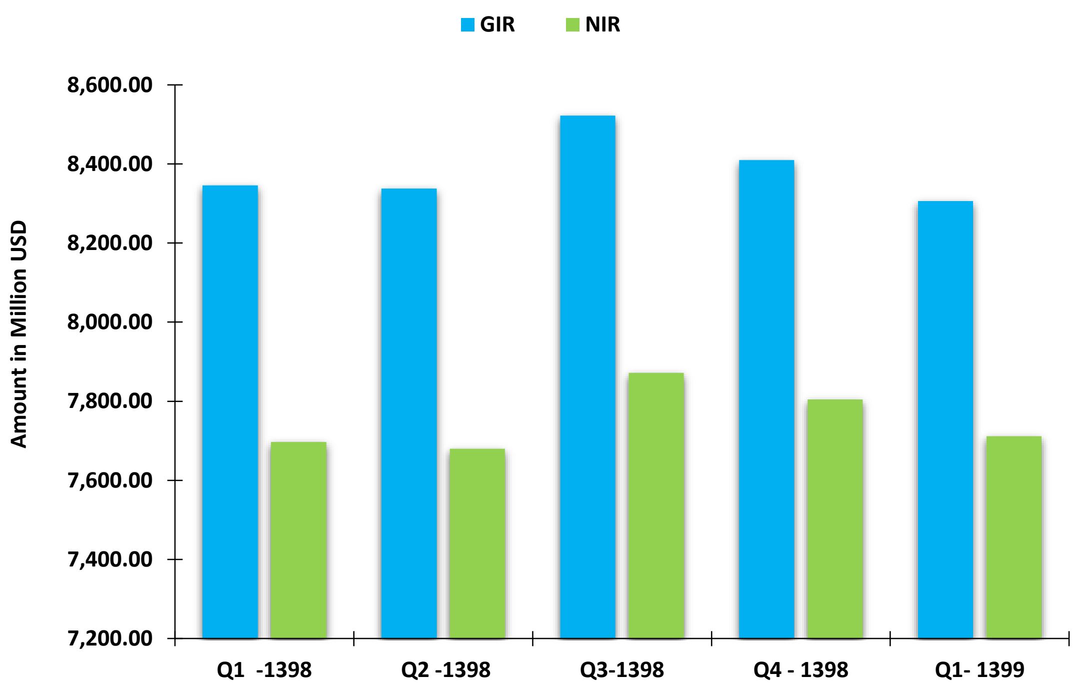
The NIR has followed upward trend during the first quarter of the FY 1399 and surged to the value of USD 7,711.85 million from a value of USD 7,696.80 million recorded in the first quarter of the last year, it showed the increment of about USD 15 million in NIR during the quarter under review (Figure 4.14).

Reserve related liabilities declined by 8.3% to a value of USD 594.62 million in the first quarter of the FY 1399 from a value of USD 648.65 million recorded in the first quarter of the FY 1398.

The decline in reserve related liabilities was mainly due to withdrawal of commercial bank deposits in foreign currency from Da Afghanistan Bank which dropped by 9.8% to a value of USD 533.78 million in the first quarter of the FY 1399 from a value of USD 591.78 million.

The Use of Fund Resources grew by 7% to the value USD 60.70 million in the first quarter of the year under review from a value of USD 56.74 million recorded in the first quarter of the previous year. The reserve liability of nonresident deposits in foreign currency almost remained unchanged in the first 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 International Reserves during first quarter of FY 1399 (in million USD)



Source: DAB staff calculations

Table 4.1: Afghanistan Balance of Payments (in Million USD)

Items / Years	Q1 - 98	Q2 - 98	Q3 - 98	Q4 - 98	Q1 - 99	% change
Current Account	-1276.92	-778.34	-1028.44	-714.90	-972.10	-24%
Credit	807.12	1013.84	851.58	1273.70	813.71	1%
Debit	2084.04	1792.18	1880.02	1988.60	1785.81	-14%
Goods and Services Account	-1620.48	-1427.23	-1438.49	-1375.16	-1281.22	-21%
Credit	370.49	283.89	344.64	510.20	395.10	7%
Debit	1990.96	1711.12	1783.13	1885.36	1676.32	-16%
Goods Account	-1458.59	-1323.05	-1252.91	-1259.63	-1186.23	-19%
Credit	182.57	143.29	208.77	329.21	203.64	12%
Debit	1641.16	1466.34	1461.67	1588.84	1389.86	-15%
Services Account	-161.89	-104.18	-185.59	-115.53	-94.99	-41%
Credit	187.92	140.60	135.87	180.99	191.46	2%
Debit	349.81	244.78	321.46	296.53	286.45	-18%
Primary Income Account	75.91	101.07	68.84	60.84	83.52	10%
Credit	93.56	111.98	75.79	71.25	92.48	-1%
Debit	17.66	10.91	6.95	10.40	8.96	-49%
Secondary Income Account	267.65	547.83	341.21	599.42	225.60	-16%
Credit	343.07	617.98	431.14	692.25	326.14	-5%
Debit	75.42	70.15	89.93	92.83	100.54	33%
Current transfers (Official grants)	167.4	432.9	233.1	497.7	162.7	-3%
Credit	167.39	432.90	233.1	497.7	162.7	-3%
Debit	0.00	0.00	0.0	0.0	0.0	
Personal transfers	141.80	145.36	142.46	139.87	95.96	-32%
Credit	175.68	185.08	198.03	194.51	163.47	-7%
Debit	33.88	39.72	55.57	54.64	67.52	99%
Capital account	55.49	241.03	22.97	504.07	36.06	-35%
Credit	55.49	241.03	22.97	504.07	36.06	-35%
Debit	0.00	0.00	0.00	0.00	0.00	
Capital transfers	55.49	241.03	22.97	504.07	36.06	-35%
Credit	55.49	241.03	22.97	504.07	36.06	-35%

Debit	0.00	0.00	0.00	0.00	0.00	
Financial account	-38.3	40.9	49.2	-33.54	-200.68	423%
Direct investment	1.71	-6.30	9.04	-1.55	0.1	-95%
Net acquisition of financial assets	10.52	5.69	4.86	5.26	5.94	-44%
Net incurrence of liabilities	8.81	11.98	-4.18	6.81	5.85	-34%
Portfolio investment	-16.46	15.42	-33.74	20.16	-4.05	-75%
Net acquisition of financial assets	-16.46	15.42	-33.74	20.16	-4.05	-75%
Net incurrence of liabilities	0.00	0.00	0.00	0.00	0.00	
Other investment	-71.61	1.35	-82.58	78.72	-60.00	-16%
Assets	-86.19	-12.36	-27.20	84.70	-28.25	-67%
Liabilities	-14.58	-13.71	55.39	5.98	31.75	-318%
Reserve Assets	48.03	30.40	156.46	-130.87	-136.72	-385%
Net errors and omissions	1183	578	1055	177	735	-38%

Source: NSIA/DAB staff calculations

Table 4.2: Merchandise Trade (in Million USD)

Years	Q1- 1398		Q4 - 1398		Q1- 1399	
	Total	Share (%)	Total	Share (%)	Total	Share (%)
Imports	1,786.34	100%	1,767.33	100%	1,530.05	100%
Industrial supplies	173.92	9.74%	212.28	12.0%	158.35	10.35%
Fuel and Lubricants	302.34	17%	260.29	14.7%	261.60	17%
Consumer goods	741.35	42%	632.84	35.8%	510.61	33%
Capital goods and other	568.74	32%	662	37.5%	599.49	39%
Exports	182.57	100%	329.21	100%	203.64	100%
Carpets & Rugs	6.57	4%	6.1	1.8%	4.54	2%
Food Items	83.93	46.0%	172.97	52.5%	94.61	46.5%
Leather & Wool	9.69	5%	13.78	4.2%	9.39	5%
Medical seeds & others	82.37	45.1%	136.41	41.4%	95.09	46.7%
Trade Balance	-1,603.77		-1,438.12		-1,326.42	

Source: NSIA/DAB staff calculations

Table 4.3: Direction of External Trade for first quarter of FY 1399 (in Million USD)

Country Name	Exports	% Shares	Imports	% Share	Trade Balance
Pakistan	41.97	21%	192.37	13%	-150.40
India	124.20	61%	105.89	7%	18.31
Iran	1.97	1.0%	261.38	17.08%	-259.41
Germany	1.89	0.9%	19.05	1%	-17.16
China	8.98	4.41%	261.73	17.11%	-252.75
England		0.00%	1.75	0.11%	-1.75
Saudi Arabia	2.73	1.34%		0.00%	2.73
United Arab Emirates		0.00%	37.25	2%	-37.25
Turkey		0.00%	12.93	0.85%	-12.93
USA		0.00%	12.69	0.83%	-12.69
Common Wealth	3.75	1.8%	442.07	29%	-438.32
Japan		0.00%	51.40	3%	-51.40
Other Countries	18.16	8.92%	131.55	8.60%	-113.39
Total	203.64	100%	1,530.05	100%	(1,326.42)

Source: NSIA/DAB staff calculations

Table 4.4: Direction of External Trade for first quarter of FY 1398 (in Million USD)

Country Name	Exports	% Shares	Imports	% Share	Trade Balance
Pakistan	49.19	27%	255.66	14%	-206.47
India	95.33	52%	85.40	4.78%	9.93
Iran	3.28	2%	314.30	18%	-311.02
Germany	3.31	1.8%	15.61	0.87%	-12.30
Common Wealth	3.51	2%	467.73	26.2%	-464.22
China	6.93	3.80%	336.22	19%	-329.29
United Arab Emirates			28.78		
Saudi Arabia	3.33	0.00%		1.61%	-28.78
Turkey			19.12	1.07%	
Japan		0.00%	49.26	2.76%	-49.26
England		0.0%	1.01	0%	-1.01
USA		0.00%	14.24	0.80%	-14.24
Other Countries	17.69	9.69%	199.02	11.14%	-181.33
Total	182.57	98%	1,786.3	100%	(1,587.99)

Source: NSIA/DAB staff calculations

Table 4.5: External debt (in millions USD)

	Q1 1398	% share	Q1 1399	% share
Total external debt	2,450.34	100.00	1,908.55	100.00
1- Bilateral	1,010.90	41.26	921.36	48.28
Paris Club	902.09	36.81	782.90	41.02
Russian Federation	902.09	36.81	782.90	41.02
United States		0.00	-	0.00
Germany		0.00	-	0.00
Non-Paris Club	108.81	4.44	138.46	7.25
2- Multilateral	1,439.44	58.74	987.19	51.72
IDA (World Bank)	655.82	26.76	333.00	17.45
Asian Development Bank	655.82	26.76	554.31	29.04
International Monetary Fund	75.61	3.09	57.70	3.02
Islamic Development Bank	50.50	2.06	40.69	2.13
OPEC Fund	1.69	0.07	1.50	0.08

Source: NSIA/DAB staff calculations

Table 4.6: Gross and net International Reserves (in millions USD)

	Q1 -98	% change	Q4 - 98	% change	Q1- 99	% change
Net international Reserves (million US Dollar)	7,696.80	-0.11	7,804.72	-0.85	7,711.85	0.2
Reserve Assets	8,345.46	-0.20	8,409.69	-1.32	8,306.47	-0.5
Reserve Liabilities	648.65	-1.27	604.98	-6.98	594.62	-8.3
Commercial bank deposits in foreign currency	591.78	-1.02	549.22	-7.28	533.78	-9.8
Nonresident deposits in foreign currency	0.14	0.00	0.14	-79.06	0.14	0.0
Use of Fund resources	56.74	-4.19	55.62	-2.95	60.70	7.0
Gross Intl. Reserves (in months of import)	14.02		14.28		16.29	
Net Intl. Reserves (in months of import)	13		13		15	

Source: DAB staff calculations

5

Fiscal Developments

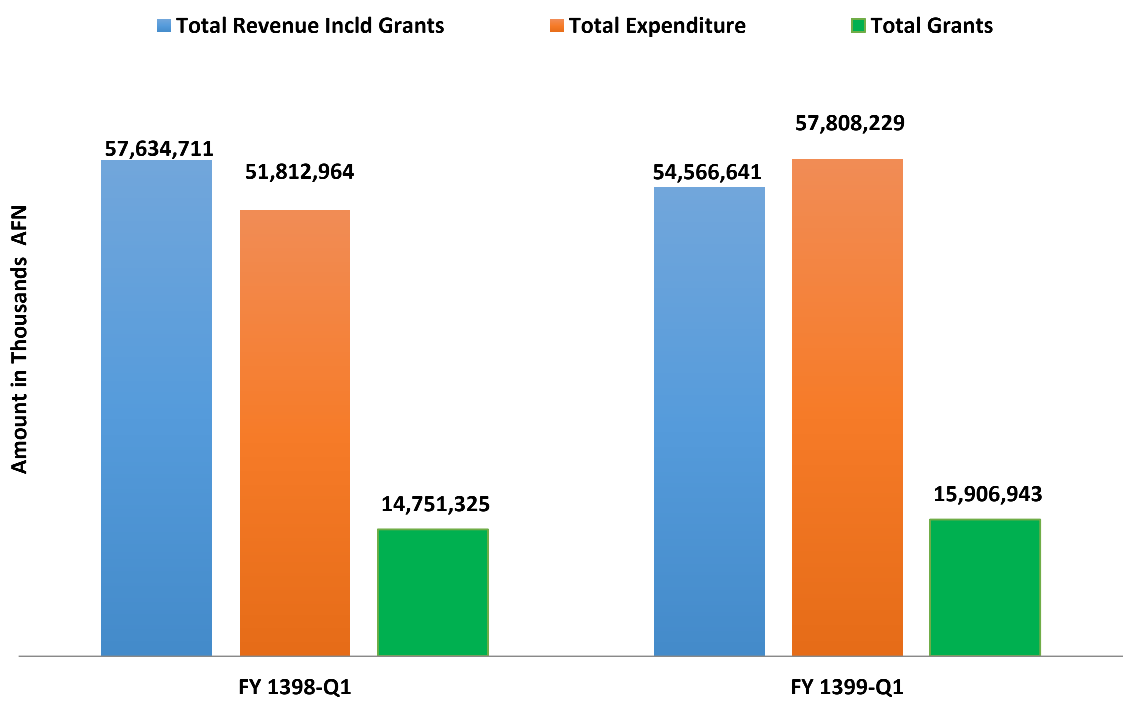
5
FISCAL SECTOR DEVELOPMENT

Fiscal sector of monetary policy directorate is responsible to keep coordination between fiscal and monetary policy implementation by the Ministry of Finance (MOF) and Da Afghanistan Bank (DAB). 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 are included improvement in public expenditure management, fiscal policy formulation, efficiency in public enterprises, taxes and customs administration. While monetary area regulates inflation, interest rate and money supply.

Resembling the other emerging and under developing economies around the world Afghanistan continuously faces budget deficit, the total core expenditure exceeds total domestic revenue in the first quarter of the fiscal year 1399 leading to AFN 3.24 billion budget deficit, and by including other revenue and grants a budget surplus of AFN 19.15 billion is being observed. There is a substantial fall in total domestic revenue collection. Meanwhile increase of employees spending, supplier expenditure, capital expenditure and subsidies, resulted to raise the total core expenditure to AFN 57.81 billion in the first quarter of FY 1399.

Figure 5.1: Comparison of Total Revenue, Total Expenditure, & Grants for the first quarter of FY 1398 & FY 1399



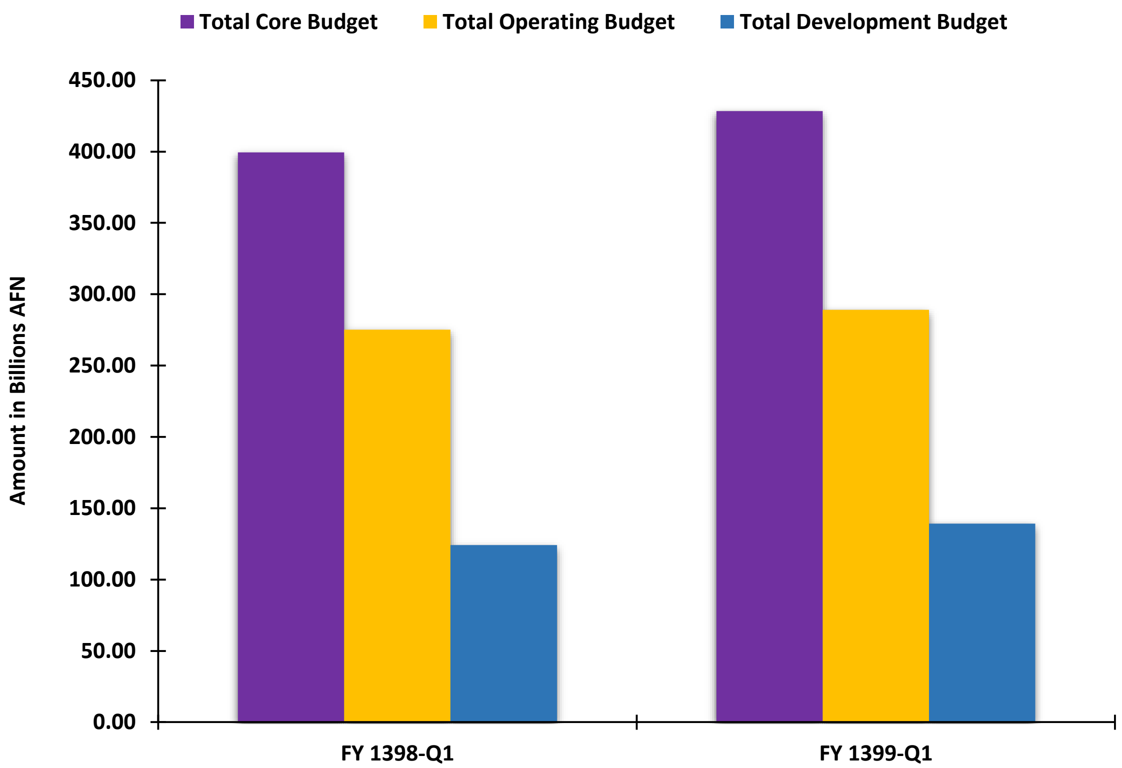
Source: MoF Financial Statement/MPD Staff Calculation

Donor contributions are used to finance both operating and development expenditures, and the main donor contributors to the government is ARTF (Afghanistan Reconstruction Trust Fund), LOTFA (Law & Order Trust Fund for Afghanistan), and CSTC-A (Combined Security Transition Command-Afghanistan). The total donor contributions (grants) allocated to operating and development expenditures represented a mild increase of AFN 15.91 billion.

5.1. BUDGET EXECUTION RATE

During the first quarter of FY 1399, government spent 13% of the total AFN 428.38 billion (allocated budget). When compared with 14% execution from the total of AFN 399.41 billion in the first quarter of FY 1398, it indicated 1% decrease in overall budget execution rate. This change was attributed to several factors particularly late processing and approval of expenses by the National Procurement Authority, bad security condition in provinces and weak performances by the budgetary units.

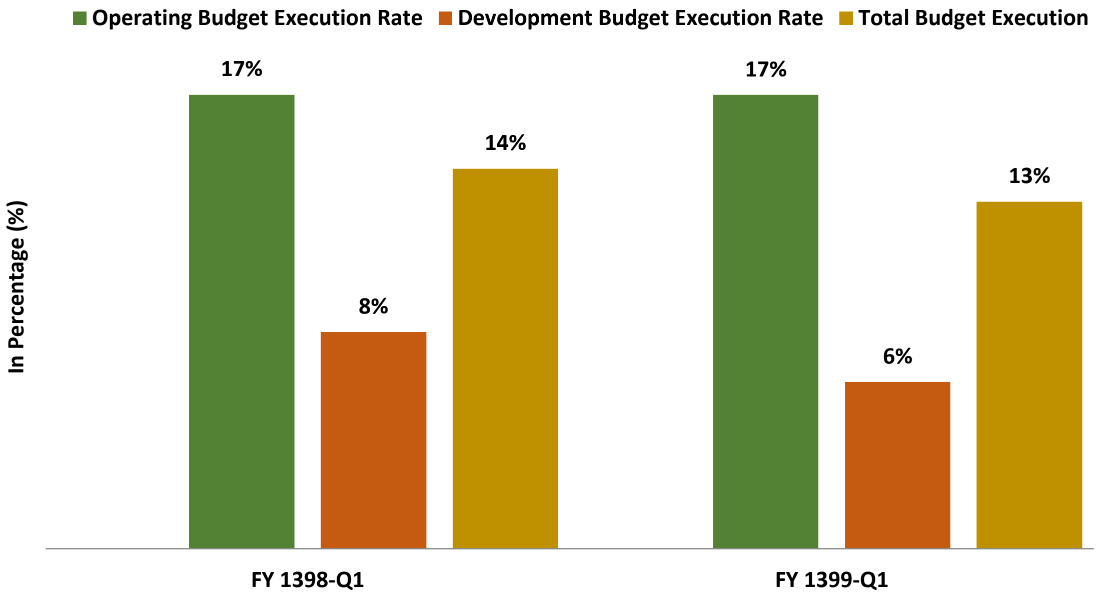
Figure 5.2: Comparison of Budget for first quarter of FY 1398 and FY 1399



Source: MoF Financial Statement/MPD Staff Calculation

Operating budget execution rate indicates 17% increase from AFN 47.38 billion in the first quarter of FY 1398 to AFN 50.45 in the period under review. The development budget execution rate evidently represents decrease of AFN 13.7% comparing both AFN 10.2 billion in the first quarter of the FY 1398 and AFN 8.8 billion in the first quarter of FY 1399.

Figure 5.3: Comparison of budget execution rates for first quarter of FY 1398 and FY 1399.

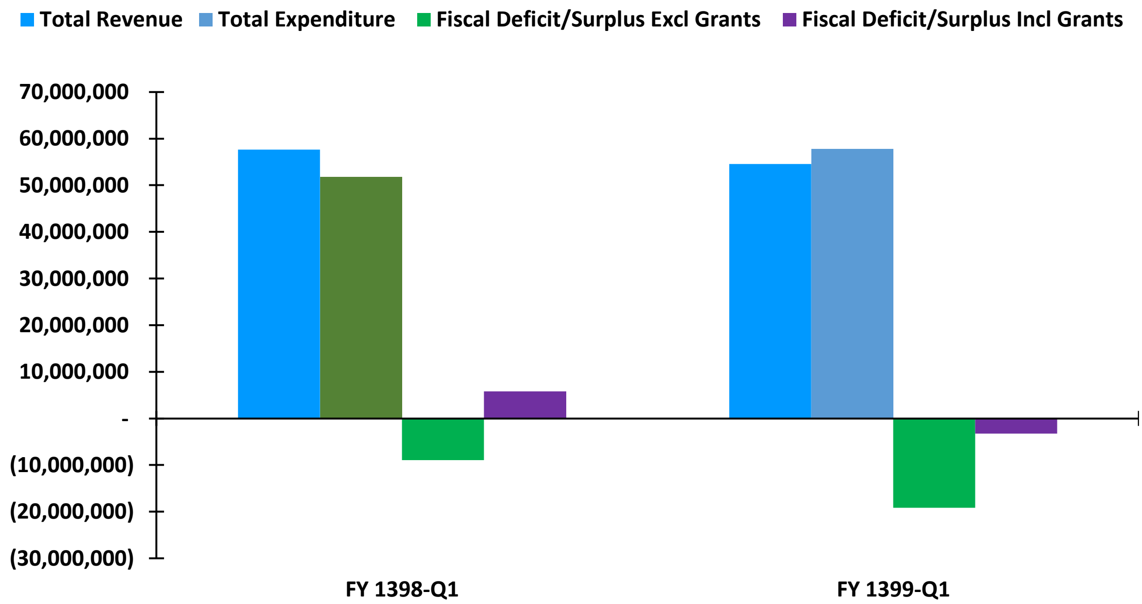


Source: MoF Financial Statement/MPD Staff Calculation

5.2. CORE BUDGET DEFICIT/SURPLUS

The total core budget is increased form AFN 399.42 billion in FY 1398 to AFN 428.38 billion in FY 1399 which shown a notable increase of AFN 28.96 billion or 7% rise in total core budget. Operating budget increased from AFN 275.22 billion in FY 1398 to AFN 289.10 billion in FY 1399 and signified 5% of increment. Similarly, development budget is showing a significant increase from AFN 124.19 billion in FY 1398 to AFN 139.28 billion in FY 1399 representing 12.1% raise which is as a result of high budget approval and allocation for the FY 1399 comparably.

Figure 5.4: Core Budget Deficit/ Surplus (Including and Excluding Grants) for first quarter of FY 1398 & FY 1399



Source: MoF Financial Statement/MPD Staff Calculation

The overall budget prior to donor's contribution had a deficit of AFN 19.15 billion in the first quarter of FY 1399 compared to AFN 8.93 billion deficit in the same quarter of FY 1398 that shown AFN 10.22 billion (114.4%) raise in fiscal deficit compared.

Meanwhile, donor contributions increased from AFN 14.75 billion in the first quarter of FY 1398 compared to AFN 15.91 billion in the period under review. The total annual external source funding amount in the first quarter of FY 1399 was AFN 207 billion, when compared with AFN 199.02 billion in first quarter of the last year, it indicated an increase of 4.05% in annual planed external sources of fund and it is as a result of commitment from the donor's contribution on annual basis.

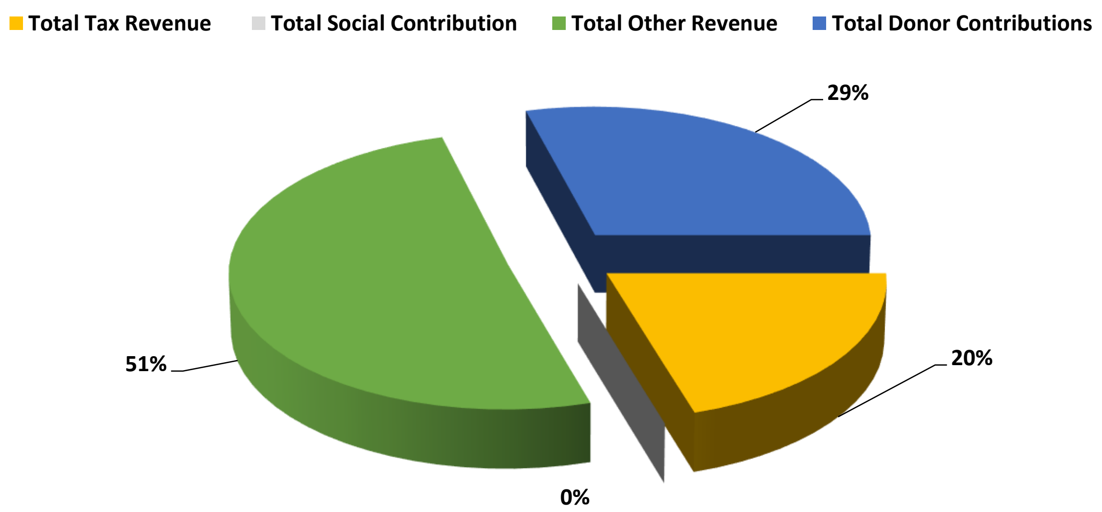
5.3. TOTAL REVENUE

With reference period of FY 1398 total revenues including grants decreased significantly with total collection of AFN 54.57 billion in the first quarter of FY 1399 compared to AFN 57.63 billion in the same quarter of FY 1398, which presented a mild decrease of AFN 3.07 billion or 5.3% as compared to same quarter of previous year.

Collection of annual planned revenue from domestic sources indicates AFN 20.89 billion increment from AFN 188.01 billion in FY 1398 to AFN 208.90 billion in FY 1399 leading to 11% increases comparably. To meet FY 1399 budget deficit total domestic revenue & donor contribution play a vital role and revenue collection that steer to annual budget surplus.

Moreover, the increase in total revenue collection of FY 1399 is as a result of momentous improve in income taxes, sales of goods and services, sale of land and buildings, custom duties and administrative fees however there is decline in social contribution and other non-tax revenues including income from capital property, royalties, extractive industry, and large difference in miscellaneous revenues during the first quarter of the year and negatively reflected retail activity from the low base last year comprise of property tax, Fixed tax and custom duties.

Figure 5.5: Total Revenue Contribution for first quarter of FY 1399



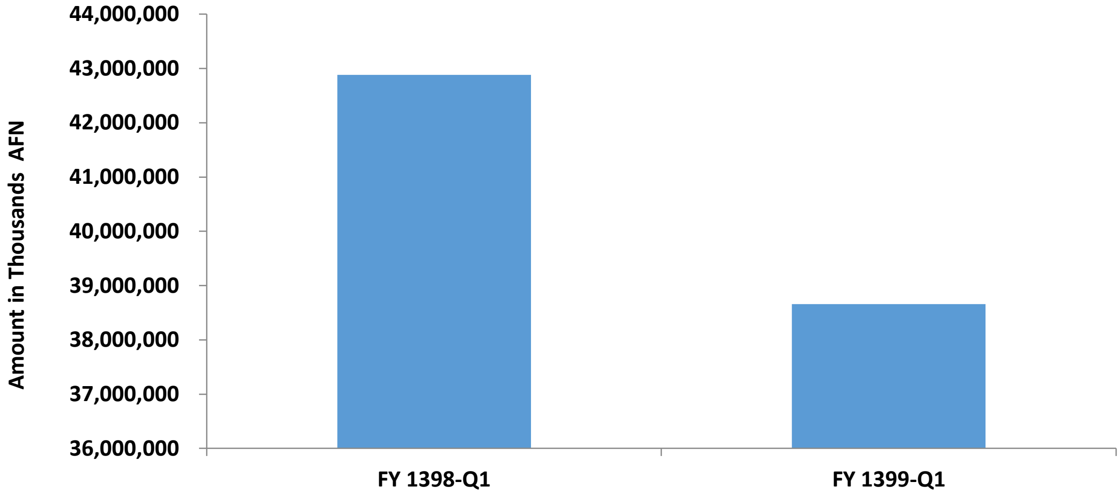
Source: MoF Financial Statement/MPD Staff Calculation

5.3.1. Domestic Revenue:

The total collection of domestic revenue performance felt down in the first quarter of fiscal year 1399, however it was sophisticated compared to the first quarter of FY 1398. These measures are deemed sufficient by the government to ensure the achievement in terms of the GDP deficit in FY 1399. The decrement in domestic revenue collection was attributed to fall in receipts from taxations and custom revenue that included Income tax, property tax, sales tax, fixed taxes and a notable change in retirement contributions.

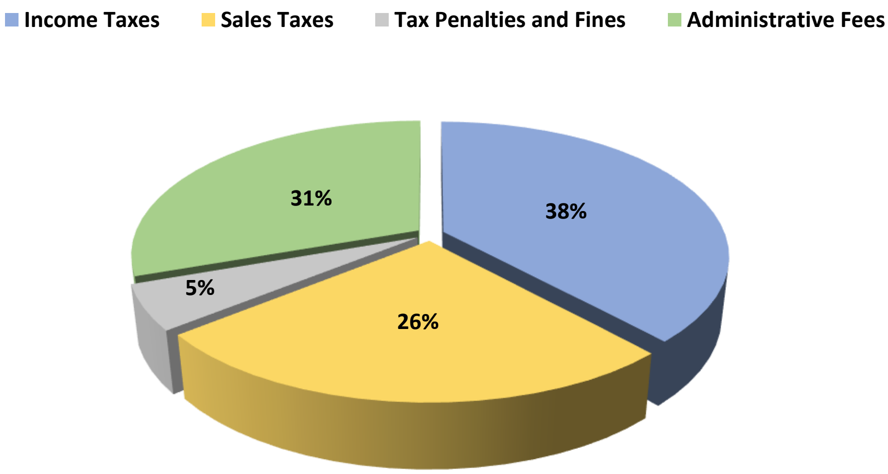
Total domestic revenue is decreased from AFN 42.88 billion in the first quarter of FY 1398 to AFN 38.66 billion in the first quarter of FY 1399 that showed AFN 4.22 billion or 9.85% decrease in domestic revenue collection.

Figure 5.6: Total Domestic Revenue Comparison for first quarter of FY 1398 & FY 1399



Source: MoF Financial Statement/MPD Staff Calculation

Figure 5.7: Major Domestic Revenue for first quarter of FY 1399



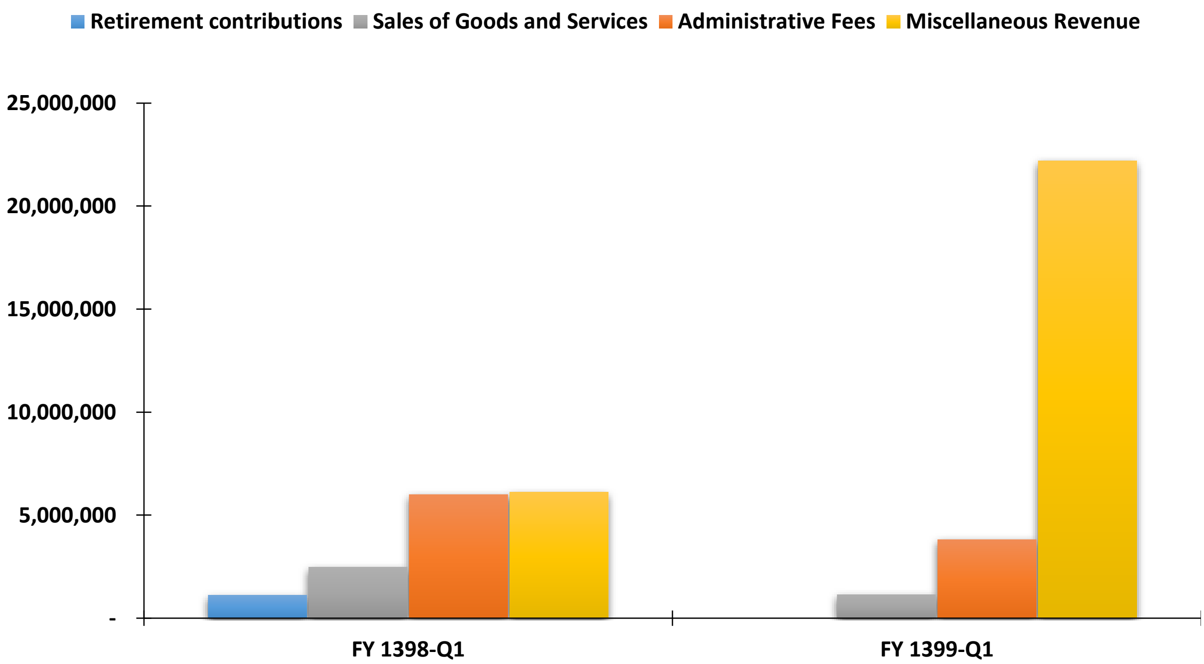
Source: MoF Financial Statement/MPD Staff Calculation

Beside this, a breakdown of the total revenue collection showed a mild deceleration in various domestic revenue components such as; income from capital property that showed a momentum decrease of 20.87% from AFN 0.31 billion in the first quarter of FY 1398 to AFN 0.25 billion in the quarter under review, the income tax showed decrease of 46.06% from AFN 8.85 billion in the first quarter of the previous year to AFN 4.74 billion in the first quarter of FY 1399, sale taxes represented a significant decrease of 57.74% from AFN 7.70 billion in the first quarter of 1398 to AFN 3.25 billion in the quarter under review, and a remarkable increase of 263.4% in miscellaneous revenue from AFN 6.11 billion in the first quarter of the last year to AFN 22.19 billion in the quarter under review.

Non Tax Revenue:

One of the initial component of domestic revenues is tax revenues that represents a notable increase of 70% from AFN 16.18 billion in the first quarter of FY 1398 to AFN 27.59 billion in the first quarter of FY 1399. This is as a result of vital increase in income tax from capital property, fixed taxes and services and a notable change in miscellaneous return.

Figure 5.8: Comparison of Major Components of Total Non-Tax Revenue for first quarter of FY 1398 & FY 1399



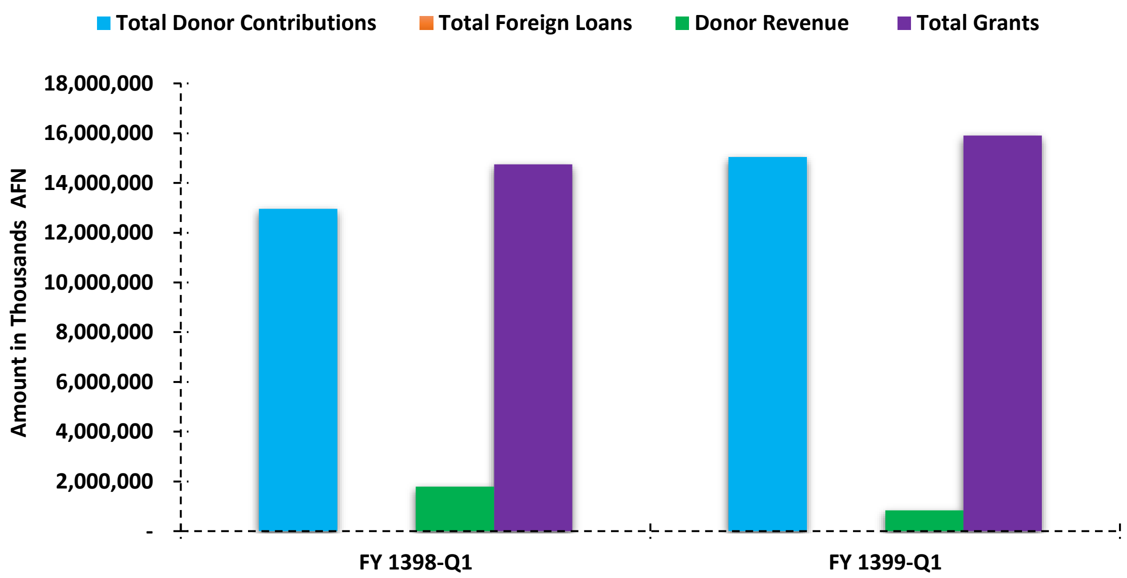
Source: MoF Financial Statement/MPD Staff Calculation

The main contributors of the non-tax revenues were retirement contributions that decreased to 0 (zero), sales of goods and services decreased from AFN 2.48 billion in the first quarter of FY 1398 to AFN 1.13 billion in the first quarter of FY 1399 which showed 54.48% decrease, similarly administrative fees decreased from AFN 6 billion in the first quarter of the last year to AFN 3.81 billion in the quarter under review which signified 36.56% decline, however miscellaneous revenue increased from AFN 6.11 billion in the first quarter of FY 1398 to AFN 22.19 billion in the first quarter of FY 1399.

5.3.2. Grants

The donor contribution comprises an important part of the national budget, meantime donor grants finance major expenditure items in both operating and development budget, likewise, the 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 total domestic expenditure and it should be financed by total domestic revenue where recently it is financed partially by external sources, foreign loans and rest by domestic revenue.

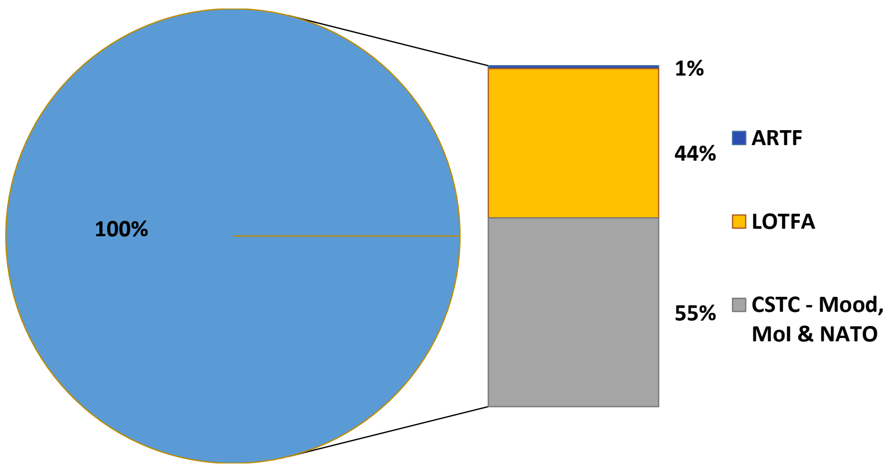
Figure 5.9: Total Annual Grants Analysis for first quarter of FY 1398 & FY 1399



Source: MoF Financial Statement/MPD Staff Calculation

The total development and operating grants represents significant increase of AFN 1.97 billion from AFN 14.75 billion in first quarter of FY 1398 to AFN 16.72 billion in the quarter under review which clearly indicates a mild increase to the same period of previous year.

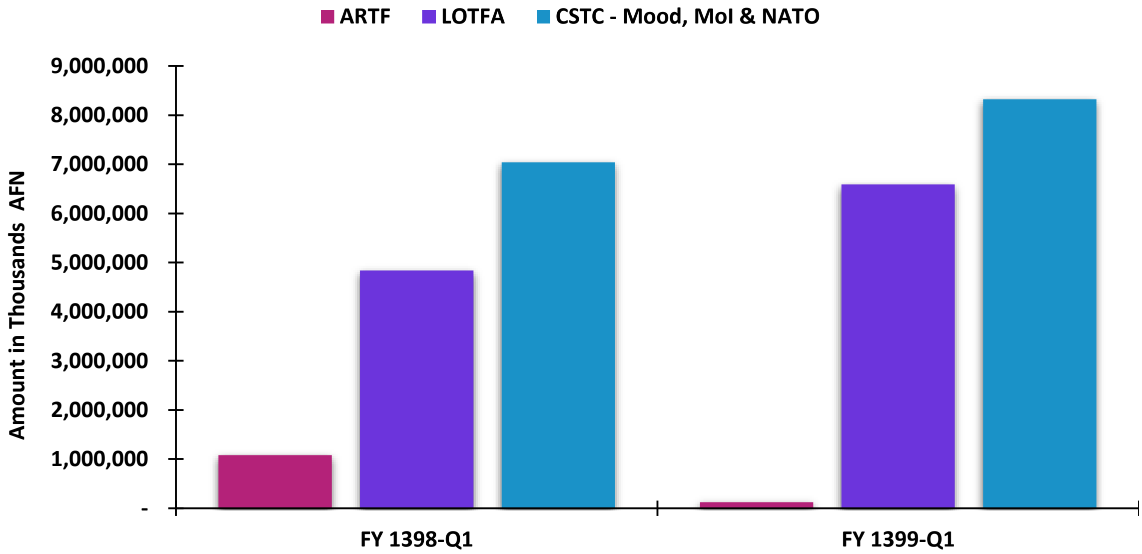
Figure 5.10: Components of Donor Contribution for first quarter of FY 1399



Source: MoF Financial Statement/MPD Staff Calculation

The main donor contributors to operating and development expenditures were grants from ARTF that declined 88% from AFN 1.08 billion in the first quarter of FY 1398 to AFN 0.13 billion in the first quarter of FY 1399 and CSTC-A (MoD, MoI & NATO) contributed AFN 7.04 billion in the first quarter of the last year compared to AFN 8.32 billion in the quarter under review that showed 18% increase. LOTFA contributed AFN 6.59 billion in the quarter under review compared to AFN 4.84 billion in the same quarter of the previous year that showed 36% increase.

Figure 5.11: Comparison of Donor Contributions for first quarter of FY 1398 & FY 1399



Source: MoF Financial Statement/MPD Staff Calculation

5.4. EXPENDITURE:

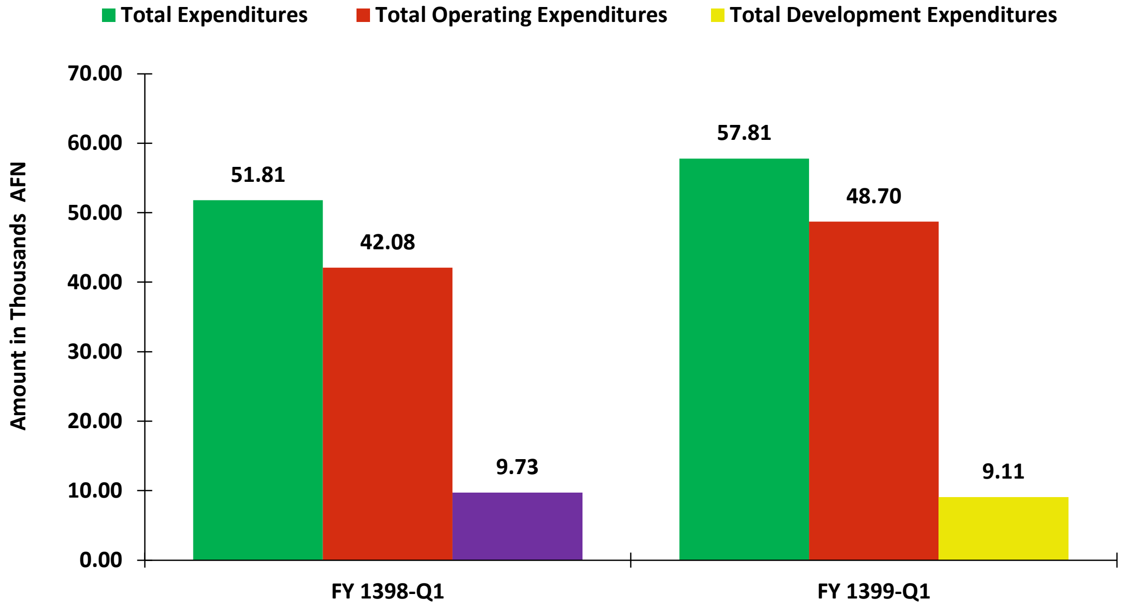
The core expenditures are classified into development and operating expenditures which are allocated in eight different sectors such as security, governance, education, health, agriculture, social protection, infrastructure, and economic governance, moreover, the sector wise expenditure is provided for both operating and development budget, while, increased expenditure on infrastructure, economic governance, and agriculture sectors are in line with the ANPDF priority.

Furthermore, total core expenditure presented 11.57% increase from AFN 51.81 billion in the first quarter of FY 1398 to AFN 57.81 billion in the quarter under review which indicated AFN 6 billion increase in overall development and operating expenditure, and this was as a result of increase in employee expenditures, grants contribution, pensions and capital expenditure.

In addition, operating expenditure indicates increase of 15.73% from AFN 42.08 billion in the first quarter of FY 1398 to AFN 48.70 billion in the first quarter of FY 1399. Meanwhile, development expenditure shows 6.43% decrease from AFN 9.73 billion in the first quarter of FY 1398 to AFN 9.11 billion in the quarter under review which indicates AFN 0.63 billion decrease in development expenditure.

To compare with the same period of last year, it shows a high increase in overall expenditure by increase in annual approved development budget as well as increase in core annual expenditure.

Figure 5.12: Comparison of Total Expenditures for first quarter of FY 1398 & FY 1399



Source: MoF Financial Statement/MPD Staff Calculation

6

Banking Systems Performance

6

BANKING SYSTEM PERFORMANCE

The overall banking system performance chapter presents an overview of the financial trends on Q-o-Q. The financial statistics table accompanying graphs on key financial indicators with the source data are provided below each graph and table.

The banking sector in Afghanistan consists of 12 duly-licensed and permitted banking organizations: 3re-licensed state owned banks, 6[4] private full-fledged commercial banks, 1[5] private full-fledged Islamic bank and 2 branches of foreign banks. The performance of the banking sector in the first quarter of 2020 is described below followed by analysis of the Islamic banking sector[6] in the given period.

As of end of March 2020 (Hoot 1398) the main banking sector data demonstrated a decreasing trend as compared to December 2019. Total assets, loans, deposits, equity capital and profitability decreased, owing to settlement, repayment and less OD utilization, revocation of license of a bank, deposit withdrawals and losses. Liquidity remained adequate but the banking sector still beleaguered with the low asset quality.

6.1. TOTAL ASSETS

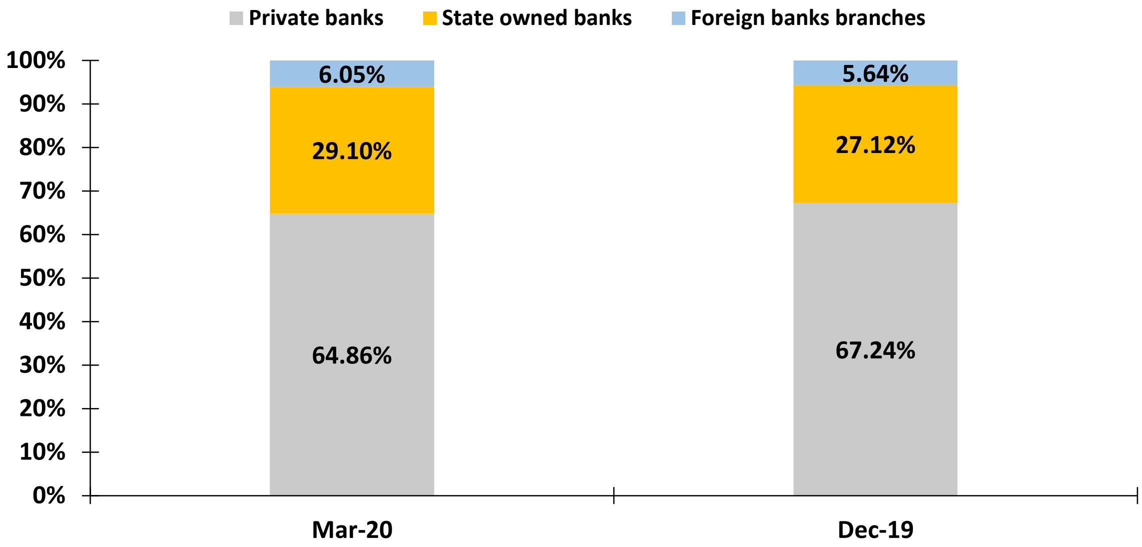
Concerning the growth, the total assets of the banking sector witnessed 9.07% Q-o-Q decline, amounting AFN 284.669 billion, against AFN 31[i]3.069 billion in Dec,2019. The above mentioned decrease in the total assets was mainly contributed by deposit withdrawals (dominant in customer demand and saving deposits), while other contributing factors included revocation of license of a bank and losses. Disaggregated analysis of total assets shows that top decreasing items were cash in vault and claims on DAB and interbank claims.

The most important components of the system's total asset portfolio were cash in vault and claims on DAB (38.29%), net interbank claims (27.70%), net loans (12.47%), investments (10.65%), net other assets (5.7%) and fixed assets making 3.37% of the total assets, while the share of the repossessed assets and intangible assets were negligible.

The share of private bank in the system's total asset is reported to be 64.86% of total banking sector assets (Islamic bank makes 6.90% of sector total assets); state-owned banks with 29.10% share are at the second place while branches of foreign banks have 6.05% shares in the system's total asset.

[4] Since Arian Bank license is revoked, it is no more included in the banking sector
[5] In the banking sector bulletin Islamic bank is part of private banks
[6] The Islamic banking sector consists of one bank and six windows

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



Source: Banking Supervision Department, DAB

Table 6.1: Banking Sector Asset Composition

Banking Sector Asset Composition				
	Amount in million AFN			
	Dec-19	Mar-20	Growth	% total assets
Cash in vault & Claims on DAB	131,392	109,008	-17.04%	38.3%
Interbank claims	83,338	78,844	-5.39%	27.7%
Investment	31,743	30,325	-4.47%	10.7%
Net loans	36,127	35,508	-1.71%	12.5%
REPOSSESSED ASSETS	1,087	1,018	-6.39%	0.4%
UNCONSOLIDATED INVESTMENTS	3,105	3,078	-0.88%	1.1%
Net Other Assets	15,555	16,353	5.13%	5.7%
INTANGIBLE ASSETS	971	939	-3.25%	0.3%
PREMISES AND OTHER FIXED ASSETS	9,751	9,597	-1.58%	3.4%
TOTAL ASSETS	313,069	284,669	-9.07%	100.0%

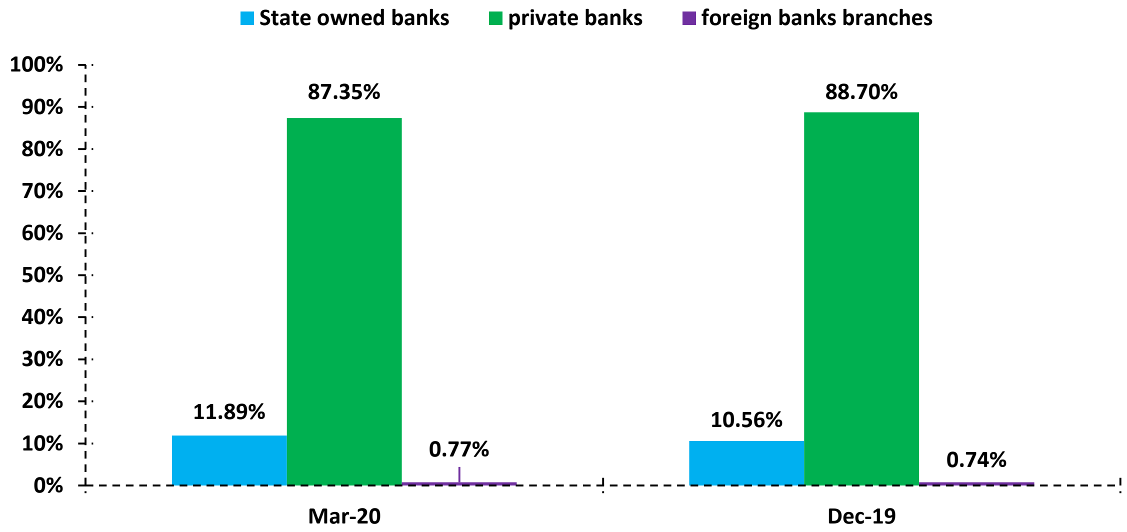
Source: Banking Supervision Department, DAB

6.1.1. Gross Loans

The gross loan portfolio of the banking sector recorded Q-o-Q decrease of 1.28%, currently stands at AFN 40.624 billion, constituting 14.3% of the total assets, whereas it was AFN 41.150 billion in Dec, 2019 comprising 13.14% of the total assets.

The decrease in total gross loans is mainly attributed to revocation of license of a bank, settlement of loans, repayment and less OD utilization. Share of the gross loans portfolio among banking group is shown in below graph.

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



Source: Banking Supervision Department, DAB

- **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. As per the assets classification and provisioning regulation banks are required to make specific provision on non-standard assets, while general reserves on standard assets is optional, in order to mitigate their credit risk.

By the end of Mar,2020, total provision cover of the system was 12.6% of total gross loans as opposed to 12.2% recorded as of end of Dec, 2019.

- **Distribution of Credit**

Breakup of gross loans across the various sectors indicates that some sectors are receiving greater credit while others witnessing a contraction. The Province wide and sector wide distribution of the banking sector's loan portfolio as of Mar, 2020 are given in the tables below .

The designation of Loans geographically and institutionally is not properly diversified, but it is expected that with time the distribution of loans will improve. It is desirable that all banks take active part in lending, so as to diversify lending services in country.

Table 6.2: Medium, Small and Micro Loans in the banking sector

Item amount in million AFN			
	Mar,2020	Dec, 2019	As % of TGL
Medium Loans	1,359	1,234	3.3
Small Loans	801	902	2.0
Micro Loans	4,640	4,540	11.4

Source: Banking Supervision Department, DAB

Table 6.3: Designation of Loans in different sectors of the economy

No	Sectors	As % of Total Loans
1	**Commercial Real Estate and Construction**	7.27
	Construction and Buildings	7.27
2	**Infrastructure Projects**	8.73
	Power	0.10
	Road and Railway	2.69
	Dames	0.37
	Mines	0.48
	Other infrastructure projects	5.09
3	**Manufacturing and Industry**	9.76
	Manufacturing &Products of Metal wood plastic rubber leather paper	4.38
	Manufacturing handmade and machine products	3.41
	Cement and Construction Materials	1.97
4	**Trade**	43.91
	Textile	1.95
	Wholesale	5.90
	Machineries	0.39
	Petroleum and Lubricants	11.98
	Spare parts	1.75
	Electronics	2.76
	Comment and other construction Material	3.93
	Food Items	8.31
	All other Items	4.03
	Retail trading	2.91
5	**Service**	23.89
	Education	0.09
	Hotel and Restaurant	2.34
	Telecommunication	6.90
	Ground Transportation	4.88
	Air Transportation	0.90
	Health and Hygienic	1.65
	Media, Advertisements, Printer	1.92
	All other Services	5.22
6	**Agriculture, Livestock and farms**	3.82
	Agriculture	3.31
	Livestock and farming	0.51
7	**Consumer Loans**	2.62
	Total	**100**

Source: Banking Supervision Department-DAB

- ### Classification of Loans

Banks should strengthen credit risk management measures to significantly reduce the high level of NPLs. 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.

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.

Table 6.4: Classification of Loans

	Amount in million AFN			
	Mar,2020	Dec,2019	As % of total gross loans	% growth
Non-performing loans (doubtful and loss)	6,095	5,956	15.00	2
Adversely Classified Loans(substandard, doubtful, Loss)	8,009	7,366	19.71	9
Loans classified Watch	4,484	5,542	11.04	-19
Loans Charged-off	18	17	0.05	10

Source: Banking Supervision Department, DAB

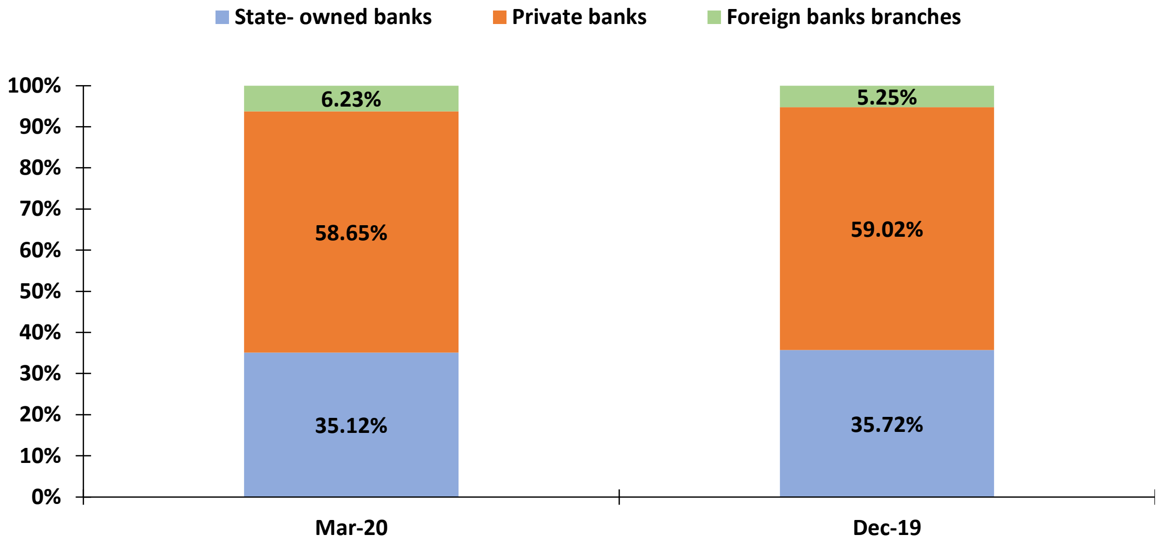
The overall quality of loans in the banking sector is a concern as the NPLs are making 15% of the sector gross loan portfolio and 20.24% of the regulatory capital. Meanwhile, other classes are on increasing path as well, which could affect the profitability and capital position of the banking sector if the trend continues. Out of 15% NPLs, 12.97% (86.41% of total NPLs and 17.5% of total reg. capital) is attributed to four banks. These banks hold 66.70% of the system's gross loans and 50.64% of system's regulatory capital.

Group wise analysis shows that out of AFN 6.095 billion total NPLs, AFN 5.395 billion NPL is coming from private banks making 13.28% of the banking sector total gross loans (88.52% of banking sector total NPLs) and AFN700 million is attributed to one state-owned bank constituting 1.72% of the banking sector total gross loans (11.5% of banking sector total NPLs).

6.1.2. Interbank Claims

Gross Interbank Claims are the second largest among various asset categories, currently standing at AFN 78.96 billion, constituting 27.74% of total assets, decreased by 5.4% Q-o-Q basis, against AFN 83.466 billion in Dec,2019. It worth mentioning that, banks should not only appropriately measure risks associated with individual bank's but also country or countries in which they have placed funds.

Figure 6.3: Share of Interbank Claims among banking groups



Source: Banking Supervision Department, DAB

6.1.3. Investment

The net-investment[7] portfolio of the banking sector comprising of bonds, Gov. Securities, investment in associated companies; decreased by 4% in compare to Dec,2019, currently stands at AFN 30.325billion, constituting 10.65% of total assets, the increase mostly came from three banking institution. Major part of the sector's investment took place outside Afghanistan. The investment portfolio is attributed to four private 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 38.29% of the total assets, currently stands at AFN 109.008 billion decreased by 17% compared to Dec, 2019. The decrease was observed in correspondent account with DAB, Overnight deposit account with DAB and cash in vault. 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 decreased by 9.6% standing at AFN 250.787 billion against AFN 277.365 billion in Dec, 2019.The mentioned decrease in total liabilities was mainly contributed by deposit withdrawals (dominant in customer demand and saving deposits).

The majority of liabilities are made up of deposits (95.27%), followed by other Liabilities (2.78%) and borrowings in third place (1.94%).

6.2.1. Deposits

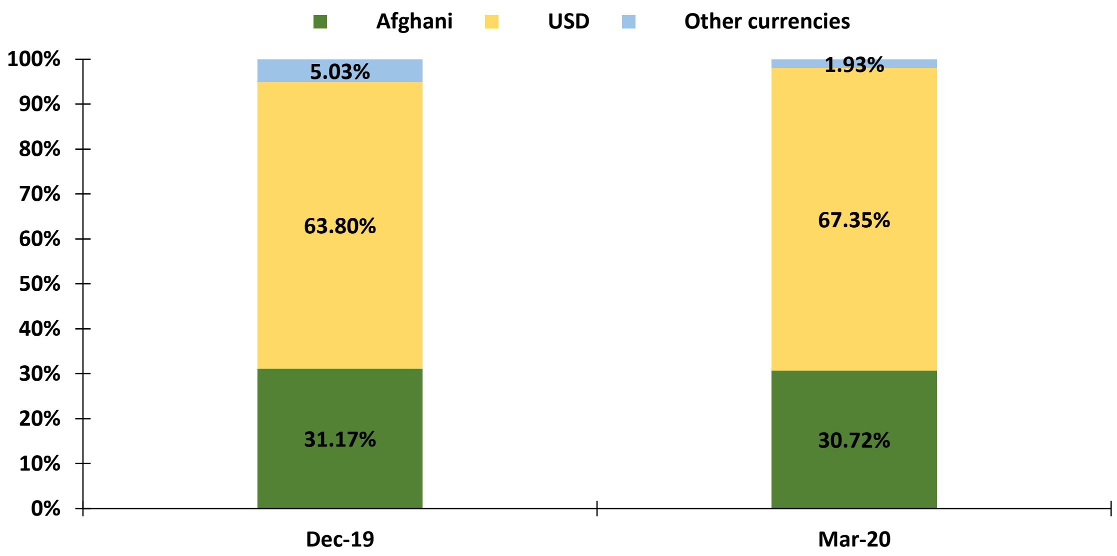
Total deposits comprising of customer and interbank deposits, the main source of funding and the major component of liabilities (95.27%), stand at AFN 238.937 billion decreased by 10.37% Q-o-Q basis, against AFN 266.576 billion in Dec, 2019.

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

Out of this, customer's deposits stand at AFN 234.753 billion making 98.25% of the total deposits decreased by 10.30% Q-o-Q basis. The decrease in total deposits mainly came from the customer demand and saving deposits.

AFN-denominated customer deposits of the banking sector are AFN 72.113 billion, or 30.7% of the total customer deposits, decreased by 11.6%, while the USD-denominated customer deposits of the banking sector stand at AFN 158.100 billion, or 67.35% of total customer deposits decreased by 5.31% attributed to withdrawals. Private Banks have the highest percentage share in total deposits of the sector, standing at 65.83% followed by state-owned banks with 28.30% share, while the share of the branches of foreign banks was 5.87%.

Figure 6.4: Currency Composition of Deposits



Source: Banking Supervision Department, DAB

Table 6.5: Breakdown of Deposits by Type for first quarter of FY 1399

Amount in Million AFN			
Item	Customer deposits	Interbank deposits	Total deposits
Demand	168,523.01	544.8	169,067.78
Time	16,609.95	3,632.8	20,242.78
Savings	49,619.59	6.6	49,626.15
Total	234,752.55	4,184.2	238,936.71

Source: Banking Supervision Department, DAB

6.3. CAPITAL

The banking sector is well capitalized, making 11.90% of total assets. The net equity position of the sector recorded at AFN 33.882 billion, decreased by 5% on Q-o-Q mainly attributed to revocation of license of a bank and loss. CAR of the sector recorded at 25.97% against 25.93% in Dec, 2019. Disaggregated analysis shows that the financial capital of all banks is above the regulatory limits and the regulatory capital ratio of all banks are above the set regulatory threshold (12% of the risk weighted assets). The Basel benchmark for capital to risk weighted is 8%.

6.4. LIQUIDITY

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

Overall all banking institutions are above the set minimum for the broad liquidity ratio **(15%)** and the Quick Liquidity Ratio **(20%)**. Broad liquidity ratio of the banking sector as a median stand at 56.09% against 55.89% in Dec, 2019.

6.5. FOREIGN EXCHANGE RISK

All banking institutions are within the set regulatory threshold for overall open FX position (± 40%) and on an individual currency (± 20%) basis except for four banks, which have violated the limits on overall, five banks on an individual currency basis USD long position and one bank in EURO long position.

6.6. PROFITABILITY

In terms of the profitability, on cumulative basis the banking sector recorded AFN 71.3 million net loss for the first three months of fiscal year 1399 against AFN 1,261 million net-profits recorded in last quarter of 2019, showing deterioration over the quarter, resulting in ROA[8] of -0.13% annualized as compared to 0.83% annualized in Dec 2019. The factors contributed towards the deterioration in the profitability of the banking sector were increase in credit provision, decrease in non-interest income and FX revaluation losses.

Group wise analysis reveals that Private Banks (PB) and Branches of foreign banks (BFB) ended with profit, whereas State-Owned Banks (SOB) ended with losses. Losses of the banking sector is mostly coming from State-Owned Banks standing at AFN 135 million, with annualized ROA of -0.99%, while private banks and branches of foreign banks were having profit of AFN 49 million and AFN 14.53 million, with annualized ROA of 1.44% and 0.13% in the period under review.

[8] ROA (Return On Assets)

6.7. ANALYSIS OF FINANCIAL CONDITION AND PERFORMANCEOF THE ISLAMIC BANKING SECTOR

6.7.1. Executive summary

The Islamic banking sector recorded a downward trend for its main financial indicators in the quarter under review, apparent from the decrease in total assets, which is mostly due to deposits downturn. The capital of four windows out of six windows is negative and the equity capital of one full-fledged bank is maintained at a healthy level attributed to rise in the profitability along with adequate level of liquidity position. However, gross financing has downward trend due to settlement of financing of a window and meanwhile investment has growth trend mainly due to issue of new investment.

The asset base of the sector during the first quarter of the year 2020, demonstrated 7.15% decline over the previous quarter standing at AFN 35.48 billion at the end of March, 2020 as compared to AFN 38.21 billion in the same preceding quarter (Dec, 2019). The decrease in total assets mostly originates from decrease in cash in vault and in financing.

Total gross financing and investment portfolio of the sector shows increase of 4% over the quarter, currently stands at AFN 13.18 billion. The increase in total gross financing and investment over the quarter is mainly due to the issue of new Sukuk investment during the quarter under review, the same time the Murabaha financing due to settlement has decreased over the period, it is worth to mention that the new Murabaha financing has taken place as well over the quarter. The percentage decrease of total gross financing portfolio of the sector is4% and vice versa the Sukuk investment shows 8% increase.

Deposits, the main source of funding in the Islamic banking sector witnessed 9.20% downturn over the quarter and currently stands at AFN 28.51 billion. The decrease in total deposits was due to decrease in the customers' demand and saving deposits. Time and saving deposits make 65.7% of overall deposits. Time deposits make 26.76% and saving deposits make 38.94% of total deposits. On the other hand, the depreciation rate of USD currency against AFN also has attributed in the decrease of total deposits of the sector. While the time deposits of the customers faced upturn for the current quarter.

There is no statutory requirement for Islamic Banking windows to maintain a separate limit of financial capital. The capital of one full-fledged bank stands above regulatory limit. The total capital of the sector increased by 2.48% over the last quarter (Dec, 2019) resulted from profit over the review quarter.

The financial capital of four windows out of six windows is negative; however, the regulatory capital ratio (CAR) of full-fledged bank has improved during the quarter under review stands at (16.1% of the risk weighted assets).

On a cumulative basis from (Jan to March 2020) the Islamic banking sector makes AFN 146.47 million net-profit against AFN 2.01 million net-losses in the same preceding quarter (Dec, 2019). Resulting in ROA of 3.7% annualized compared to that of

-0.01% and ROE 16.6% annualized compared -0.05% in Dec, 2019, respectively.

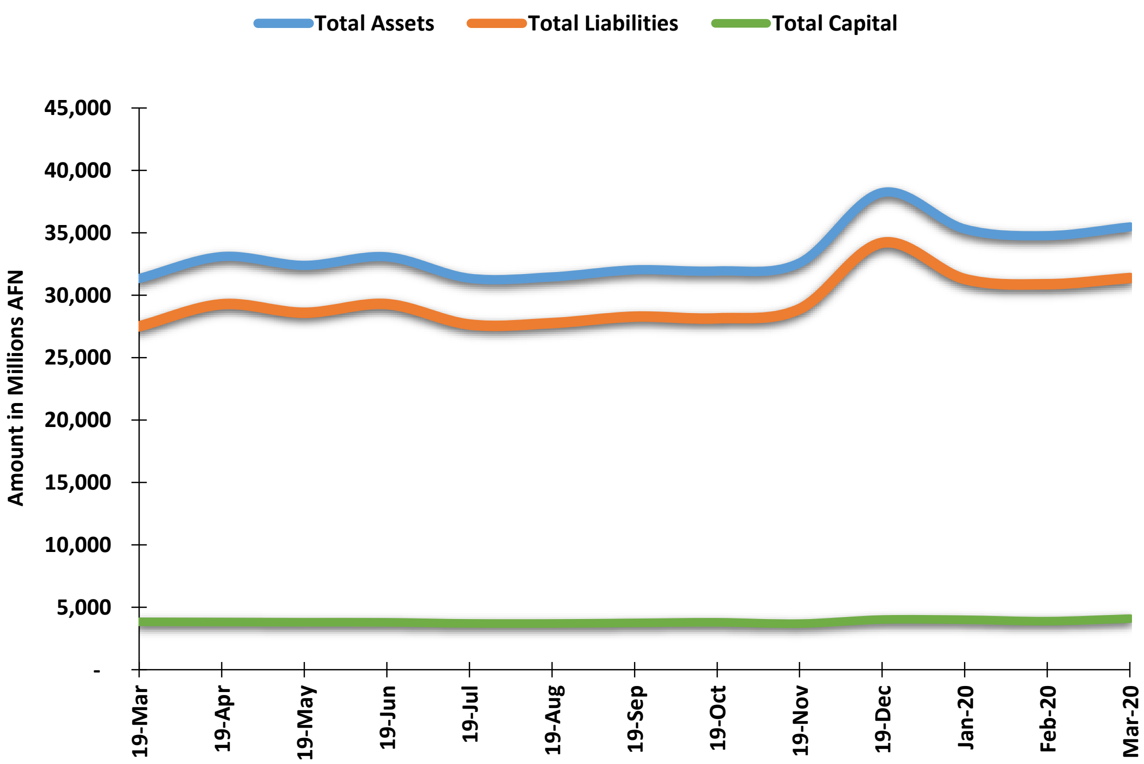
Liquidity and FX positions of windows are in accordance with the benchmarks set by the central bank (20% Quick and 15% Broad Liquidity Ratios and ± 40% for overall FX position and ± 20% on individual currency position) on overall and individual currency basis (USD long position). On the other hand, the full-fledged bank lies in violation of both FX limits set by Central Bank.

6.7.2. Total Assets

Assets base of the Islamic banking sector registered a downturn of 7.15% over the last quarter, standing at AFN 35.48 billion (USD 462.766 Million), against 19.28% growth in the same preceding quarter (Dec, 2019). The decrease in total assets was mostly due to decrease in deposit base. The analysis of total assets shows that most obvious decrease was recorded in cash in vault and in financing.

Looking at the decrease in total assets across the sector, the 72.22% decline taken place in full-fledged Islamic bank and meanwhile the assets of Islamic Banking Windows show decline of 27.77% as compared to last quarter. The percentage share of full-fledged bank in the sector's total asset is reported 55.35%; state-owned banks windows with 12.3% and while the four windows of private commercial banks have 32.35% shares in the sector's total assets. The trend of assets of the Islamic Banking Sector from March 2019 to March, 2020 is depicted in figure 6.5.

Figure 6.5: Currency Composition of Deposits



Source: IBFD, Islamic Banking and Finance Department, DAB

Table 6.6: Total Assets and Liabilities of Islamic Banking Sector (Amount in millions AFN)

	Qwas,1398 Dec, 2019	Hoot,1398 March, 2020	% of Total Assets/Liability	Quarterly Growth/Decline
Assets				
Cash in vault and claims on DAB	17,768.07	15,157.12	43%	-14.69%
Interbank claims	4,645.12	4,711.10	13.07%	1.42%
Financing Murabaha (Net)	4,111.42	3,954.16	11.14%	-4%
Investment (Sukuk and other)	7,761.42	8,376.37	23.61%	8%
Other Assets	2,799	2,671.20	7.53%	-5%
Fixed and Intangible Assets	776.61	755.54	2.03%	-5.7%
Total Assets	38,211.66	35,480.28		-7.15%
Liabilities + Capital				
Deposits	33,397.81	28,510.39	90.83%	-9.20%
Other liabilities	2,819.76	2,876.67	8.88%	4%
Total liabilities	34,217.75	31,387.06		-8%
Financial Capital	3,994.09	4,093.21		2.48%
Total Liabilities + Capital	38,211.66	35,840.28		-7.15%

Source: IBFD, Islamic Banking and Finance Department, DAB

The fluctuation in the assets of Islamic banking sector during the month of Dec and Jan 2019was mainly due to decline in demand deposits of the customers during the mentioned period. The components of the Islamic banking sector assets portfolio were cash in vault and claims on DAB without interest (43%), interbank claims (13%), net Murabaha financing (11%), investment (Sukuk and assets acquired for leasing) 24% and other assets make (10%) of the total assets.

• Gross Murabaha Financing and Investment (Sukuk)

Gross Murabaha financing and investments (Sukuks and others) of the Islamic banking sectors of Hoot 1398 (March, 2020) stands at AFN 13.189 billion (USD 172.031 million), constituting 37.17% of the total assets, depicted 4% or AFN 457.68 million increase since Qaws 1398 (Dec, 2019), whereas the gross Murabaha financing were AFN 5.196 billion (USD 67.77 million) or 13.60% of total assets and investment (Sukuk and other) were AFN 7.761 billion (USD 101.23million) constituting 20.31% of total assets.

The increase in Gross Murabaha financing and investments (Sukuks and others) has taken place in Sukuk investment but Murabaha financing due to settlement has decreased. Total Afghani denominated financing and investment recorded at AFN 3.84 billion (USD 50.12 million), which makes 29.14% of total Gross financing and investment or 10.83% of total assets. While the US Dollar denominated financing and investment are AFN 9.32 billion (USD 108.59 million), and make 70.86% of total gross financing and investment or 26.24% of total assets.

The decrease in total financing and investment portfolio is mainly due to settlement of Murabaha financing and of windows and depreciated rate of USD against AFN during the quarter under review, meanwhile investment securities (Sukuk) shows increase of AFN 614.95 million over the quarter. The increase in total gross investment is mainly attributed to new financing of Sukuk during the reviewed period.

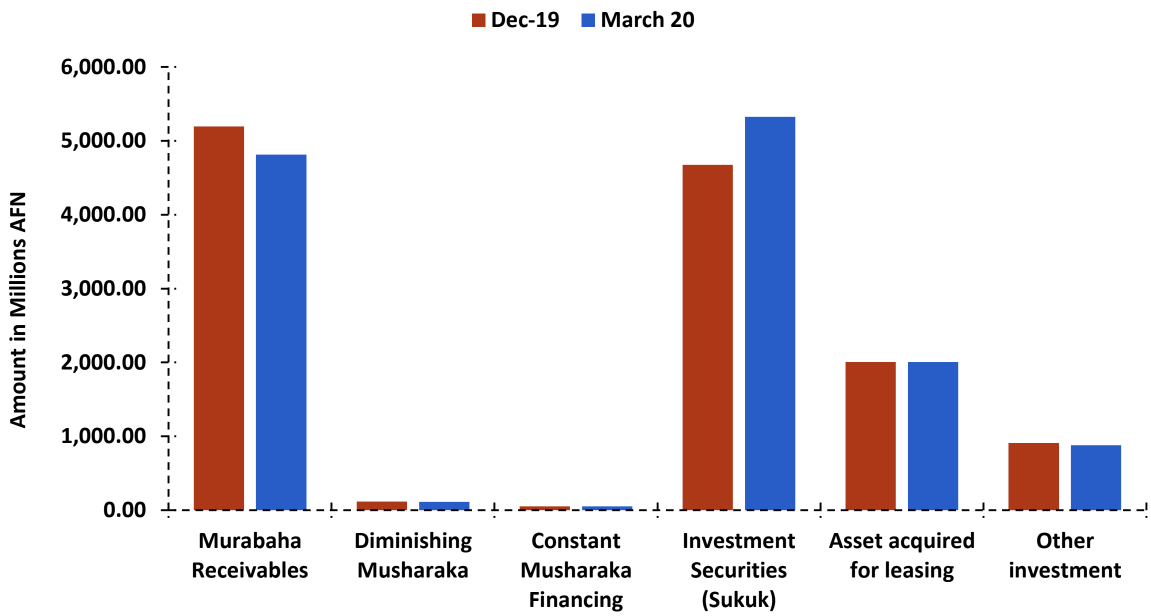
Table 6.7: Product wise Islamic Banking Sector Financing and investment (gross)

Amount in million AFN						
No	**Product**	**Dec-19**	**Mar-20**	**Difference in Amount**	**Difference in %**	**Products as % Gross Investment & Financing**
1	Murabaha Receivables	5,196.551	4,318.26	-383.28	-7.38%	36.49%
2	Diminishing Musharaka	115.83	110.03	(5.803)	-5%)	0.83%
3	Constant Musharaka Financing	53.01	51.29	(172)	-3%	0.38%
4	Investment Securities (Sukuk)	4,675.01	5,327.57	652.56.17	14%	40.49%
5	Asset acquired for leasing	2,007.48	2,007.48	0	0%	15.22%
6	Other investment	910.077	879.98	(30.09)	-3%	6.67%
	Grand Total	12,957.13	13,189.63	231.66	1.87%	100%

Source: IBFD, Islamic Banking and Finance Department, DAB

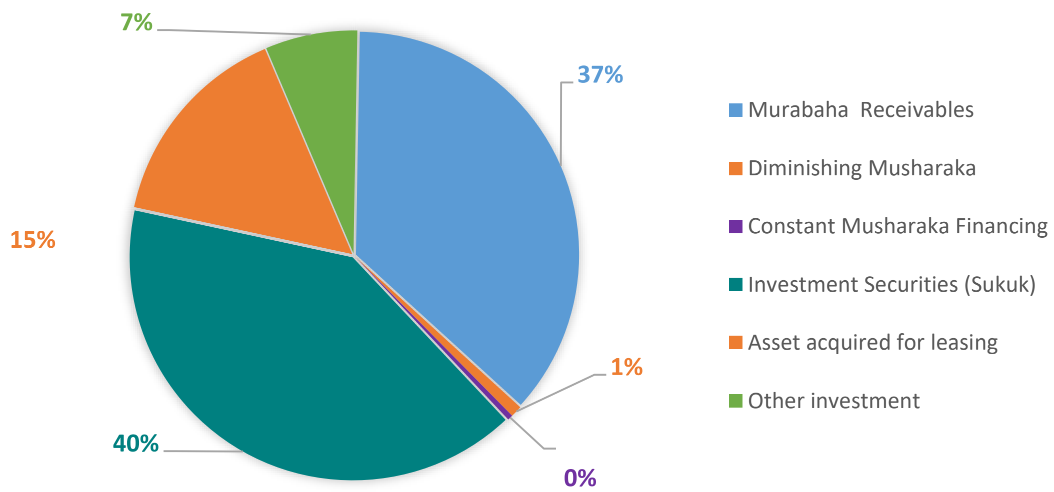
At the same time, settlement and installment of Murabaha financing have been collected during the quarter. The sect oral lending of Murabaha financing in Afghanistan is dominated by Islamic Banking window, constituting 84.30% of total gross Murabaha financing of the sector, while the share of fully fledged bank in total Murabaha financing is 15.69%, as well as the total investment securities in Sukuk of the sector which is invested out of the country is dominated 84.34% of total investment by fully fledged bank and remaining 15.65% followed by two Islamic banking windows of commercial banks.

Figure 6.6: Product wise Investment and Financing of the Islamic Banking Sector: comparison between Dec 2019 and March 2020



Source: IBFD, Islamic Banking and Finance Department, DAB

Figure 6.7: Product wise investment and financing as Percentage as per Mar, 2020



Source: IBFD, Islamic Banking and Finance Department, DAB

The breakup of total gross financing and investment of sector consists of Murabaha receivables AFN 4.813 billion that decreased by 7.38% and makes 36% of the gross financing and investment, Diminishing Musharaka amounted AFN 110.03 million or 0.83%, constant Musharaka amounted AFN 51.23 million, Sukuk investment amounted AFN 5.327 billion increased by AFN 652.56 million making 40.39% of total gross financing and investment and asset acquired for leasing amounting AFN 2.007 billion ,comprising 15.22% of the gross financing and investment and other investment amounted AFN 879.98 million making 6.67% of the gross financing and investment during the quarter under review (March, 2020). Increase in investment (Sukuk) portfolio was observed at one bank window and at full-fledged bank, and it is worth mentioning here that Islamic banking window of (NKB) has not financing and investment activities.

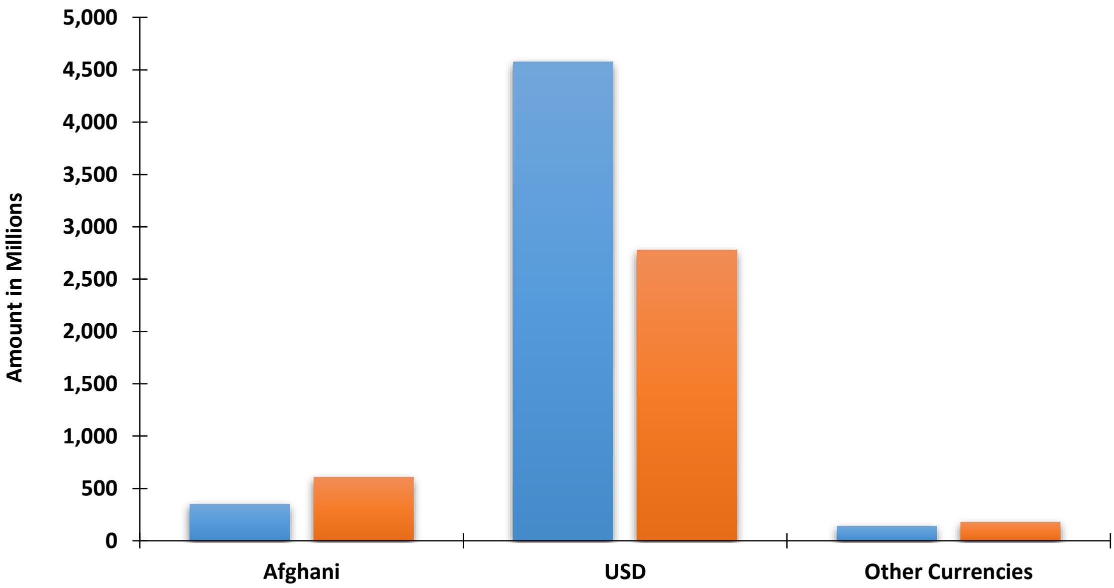
- **Financing & Investment Loss Reserve**

At the end of March, 2020 (Hoot 1398), total provision of Islamic Banking sector stands at AFN 950.505 million and shows a decrease of AFN 229 million as compared to previous quarter Dec 2019, the decrease amount reported wholly for Murabaha financing. The provision of the sector is comprised of AFN 859.09 million for Murabaha financing, AFN 72.61 million for interbank claims and AFN 18.79 million for account receivable. The provision for Murabaha financing that encompasses 17.84% of total gross financing of Islamic banking sector as against to 20.88% recorded in the previous quarter ending Dec, 2019.

- **Interbank Claims**

The Interbank Claims of the Islamic Banking Sector are the fourth largest among various asset categories, which at the end of first quarter March, 2020, stands at AFN 4.71 billion (USD 61.44 million) constituting 13.07% of total assets, and increased by AFN 65.97 million as compared to previous quarter. Interbank claims denominated by AFN 12.84%, USD 81.74% and other currencies 3.86%, see figure 6.8. Two out of six Islamic banking windows and one Islamic bank have interbank claims which consist of AFN 1.06 billion time deposits and AFN 3.57 billion demand deposits, the interbank claims used as commodity Murabaha and internal bank transferring and settlement transactions with their banks.

Figure 6.8: Interbank claims



Source: IBFD, Islamic Banking and Finance Department, DAB

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

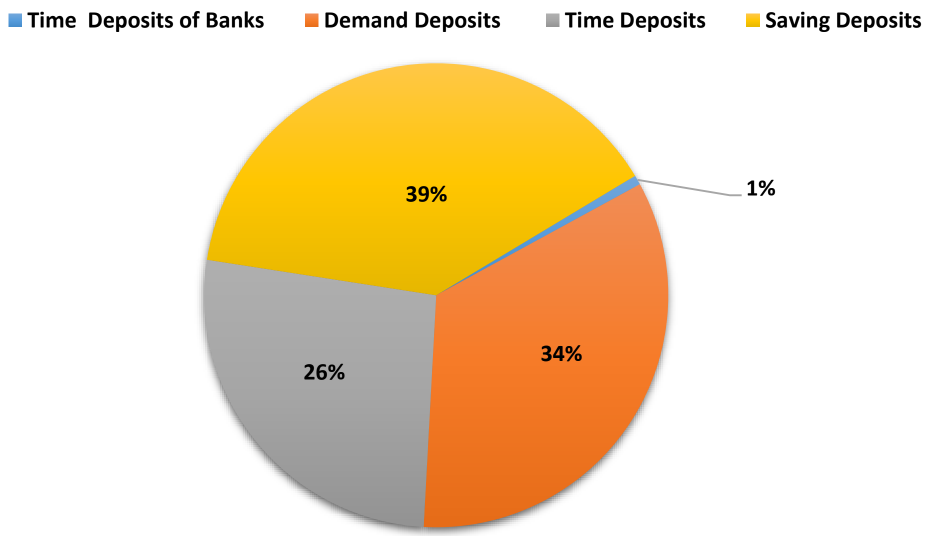
The Islamic Banking Sector's Cash in vault and claims on DAB at the end of march, 2020 stands at AFN 15.15 billion (USD 197.69 million) and decreased AFN 2.61 billion as compared to preceding quarter ended Dec, 2019. The cash in vault and claims on DAB is the largest item and makes 42.72% of total assets of the sector.

The decrease in Cash in vault and claims on DAB mainly showed in claims on DAB as well as in cash in vault. The reason of decrease in above item is mainly due to downturn in total deposits of sector over the quarter under review. Cash in vault and Claim on DAB consists of AFN 4.86 billion cash in vault, AFN 7.67 billion non-interest bearing current Account with DAB and AFN 2.61 billion Required Reserve Account with DAB.

6.7.3. Total Deposits

Deposits, the main source of funding and the major component of liabilities, stand at AFN 28.51 billion (USD 371.852 million), making 91.83% of total liabilities, decreased by 9.20% since Qaws 1398 (Dec, 2019), against AFN 31.39 billion (USD 409.51 million) with 20.08% growth in last quarter. The decrease in total deposits was mostly obvious in demand deposits of full-fledged bank, the decrease has taken place (AFN 2.58 billion or 89.77%) in demand deposits and (AFN 312.205 million or 10.83% decreases) in saving deposits of the customers during the reviewed period, while time deposits of customers showed increase of (AFN 17.75 million or 0.23%) over the last quarter.

Figure 6.9: Breakdown of Deposits as Per March, 2020



Source: IB FD, Islamic Banking & Finance Department, DAB

Furthermore, the decrease mostly occurred in AFN deposits, as well USD deposits registered decline in its position. AFN-denominated deposits of the sector are AFN 9.919 billion (USD 129.38 million), or 34.79% of the total deposits, decreased by 17.79%, while the USD-denominated deposits of the sector stand at AFN 18.59 billion (USD 242.47 million), or 65.61% of total deposits decreased by 4%. Full-fledged bank has the highest percentage share in total deposits of the sector, standing at 57.78% followed by Islamic banking windows with 42.22% share.

The total customers' deposits of the sector consist of AFN 9.64 billion of demand deposits, AFN 7.57 billion of time deposits and AFN 11.102 billion of saving deposits. As well as the demand deposits make 33.81%, time deposits 26.58% and saving deposits make 38.94% of the total deposits of the sector, and comprises of AFN 28.32 billion of customers' deposit and AFN 188.67 million of banks deposits. The deposits of banks make only 0.66% of total deposits of sector.

6.7.4. Liquidity

The liquidity position of all Islamic Banking Windows and full-fledged Islamic bank are above the set minimum for the broad liquidity ratio (15%) and the Quick Liquidity Ratio (20%). Broad liquidity ratio of the banking sector as a median stand at 53.94% points against 55.23% in the preceding period (Dec, 2019), showing a decrease of 1.29%. Since there is no Capital Market inside Afghanistan, the banking sector remained highly liquid.

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. For this reason, Islamic Bank and windows should maintain an asset liability committee (ALCO); one of its tasks is the liquidity management of the bank through gap analysis, stress testing, scenario analysis, cash flow analysis, etc. according to policies of the bank.

Table 6.8: Key Financial Soundness Indicators of the Islamic banking sector as of march 2020

Ratio in %	(Dec, 2019)	(March,2020)
Liquid Assets to Total Assets	58.81%	55.99%
Liquid assets to short term liabilities	184%	206%
Foreign-Currency denominated funding to total funding	61.57%	65.21%
Foreign- Currency denominated financing to total financing	70.92%	70.86%
Return on Assets (ROA)	(0.01)	3.7
Return on Equity (ROE)	(0.05)	16.6

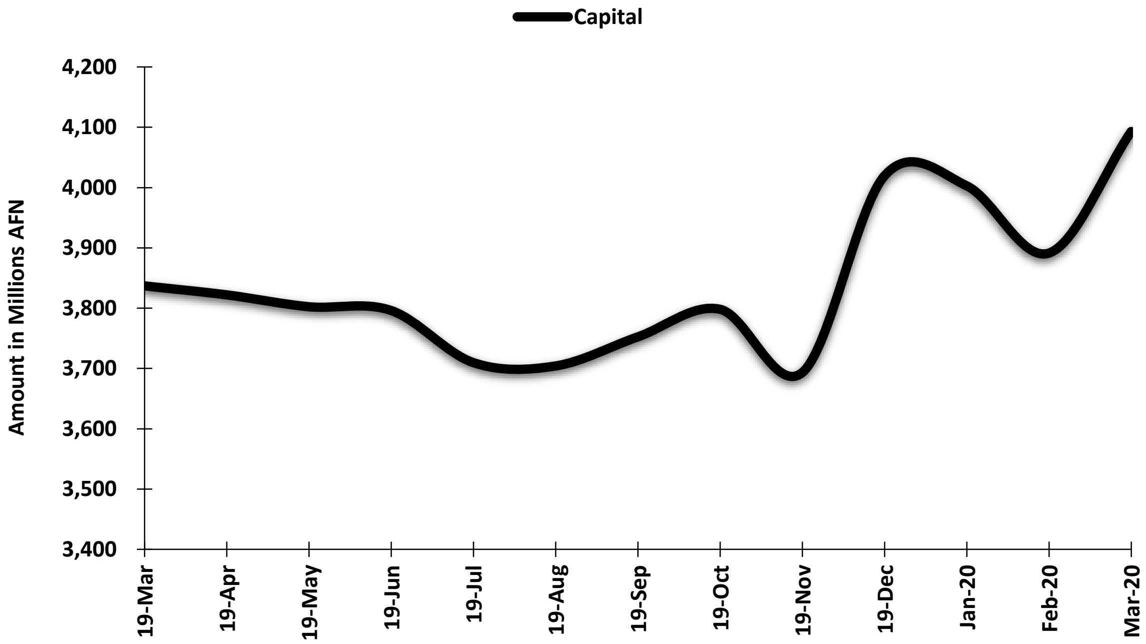
Source: IBFD, Islamic Banking & Finance Department, DAB

6.7.5. Capital

The capital of the sector stands at AFN 4.093 billion (USD 53.38 million), increased by 2.48% since previous period (Dec, 2019) when it was AFN 3.994 billion. The increase in the total equity capital is due to profit over the quarter. CAR of the Islamic Bank of Afghanistan remains above the regulatory limit.

The 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 current year. The trend of the sector financial capital as described above is given in the figure 6.10 above. One of commercial Banking windows has highest 71.53% share in total capital of sector and second fully fledged bank has 33.76% contributions in total capital of the sector.

Figure 6.10: Breakdown of Deposits as Per March, 2020



Source: IB FD, Islamic Banking & Finance Department, DAB

6.7.6. Profitability (Quarter–to–Quarter)

The Islamic banking sector earned AFN 146.47 million net profit in the current quarter (first quarter) ending March, 2020, against AFN 2.01 million net losses in last quarter. The increased in the profit of the sector in the current quarter is mainly due to reported AFN 370.42 million as reintegration of provisions by an Islamic Banking window and a full-fledged bank of the sector during the quarter under review. As well as the Islamic Banking Sector over the first quarter of the year 2020, reported AFN 183.97 million as FX revaluation gain and which shows AFN 82 million decreases as compared to last quarter.

The full-fledged bank reported AFN 4.66 million of net profit during the reviewed quarter. It is worth mentioning that the loss of one full-fledged bank in the current quarter before FX revaluation reported AFN 153.31 million, but due to FX revaluation gains AFN 157.98 million the loss of the bank has converted from AFN 153.31 million to AFN 4.66 million as net profit.

Table 6.9: Profit and Loss Schedule of the Islamic Banking Sector during quarter Mar 2020

Profit and loss Schedule (Amount in million AFN)			
Item	**Dec-19**	**March-20**	**Difference**
Profit income	137.67	152.76	15.09
Profit expense	44.730	55.513	10.783
Net profit income	92.940	97.254	4.314
Net Credit provisions	162.25	(163.3)	(325.55)
Other nonprofit income	127.48	84.08	(43.39)
Other nonprofit expense	359.55	342.15	(17.4)
Income (Loss) before FX revaluation and	(301.38)	2.49	303.87
FX revaluation Gain/loss	266.51	183.97	(82.54)
Tax	(32.85)	(39.99)	72.84
Net profit income/Loss after Tax	(2.011)	146.477	148..48

Source: IBFD, Islamic Banking & Finance Department, DAB

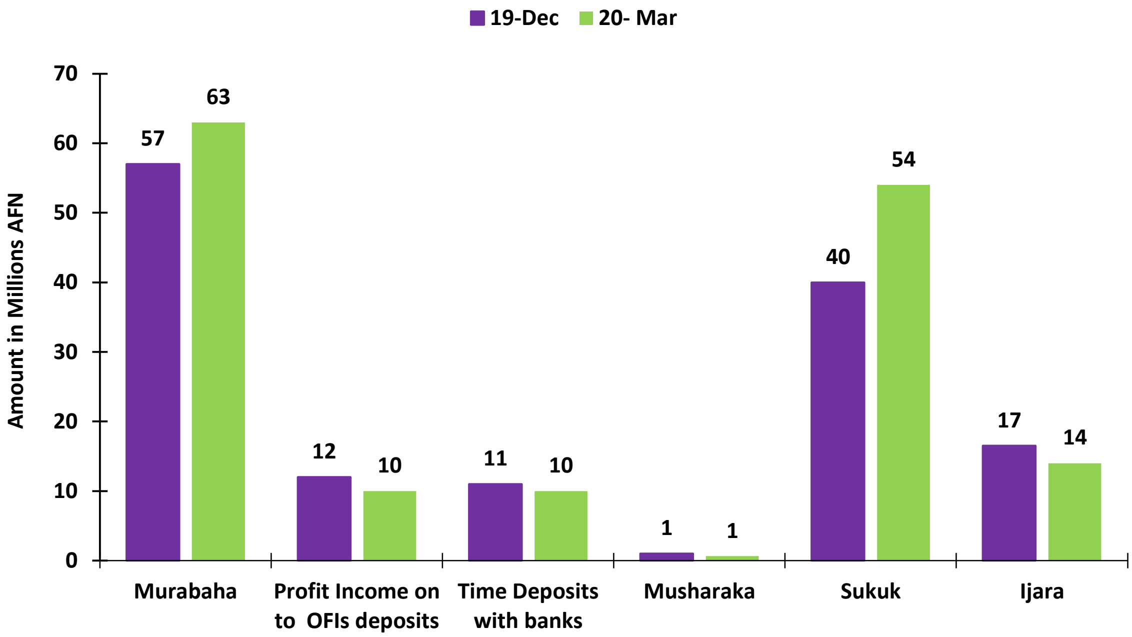
In general, the Islamic banking sector offering seven types of financial products. The returns from financing for the quarter under review are shown in table 6.10.

Table 6.10: Returns by Major Types of Shariah Compliant Products

Value of returns by major type of Shariah-compliant contract (Amount in million AFN)			
Product	**Dec-19**	**March-20**	**Difference**
Time Deposits with banks	11.215	10.206	(1.009)
Profit Income on to OFIs deposits	11.605	10.083	(1.522)
Murabaha	57.02	62.76	5.73
Diminishing Musharaka	1.103	0.635	(0.468)
Sukuk	40.211	54.802	13.99
Ijara	16.51	14.87	(1.63)
Total Profit Income	137.67	152.76	15.09

Source: IBFD, Islamic Banking & Finance Department, DAB

Figure 6.11: Return by Major Types of Shariah Complaint Products



Source: IBFD, Islamic Banking & Finance Department, DAB

Total number of employees, borrowers, depositors and of the Islamic banking sector as of March, 2020, all across the country are as follow:

Table 6.11: Number of employees, borrowers and depositors of the Islamic banking sector

Particulars	Numbers
Full-time Employees	1,030
Present Borrowers	2,579
Present Depositors	493,689

Source: IBFD, Islamic Banking & Finance Department, DAB

Contact:

Telephone : +93 (0) 20 2103930

E-mail : mp@dab.gov.af

Website : www.dab.gov.af




Monetary Policy Department
E-mail: mp@dab.gov.af
Tel: +93 210 3930