

NRB issues repo to correct interest rate

Nepal Rastra Bank (NRB) – the central regulatory and monetary authority – today called for a repo auction worth Rs two billion, with a two-week maturity period, in a bid to mop up excess liquidity from the banking sector.

Banks have quoted five per cent interest rate, which is around two percentage points higher than the prevailing interbank borrowing rate. The financial instrument that has two-week maturity period has been issued to correct the interest rate, which plunged below three per cent yesterday.

The three per cent interest rate is lower bound, or floor, of the interest rate corridor for short-term instruments, like, interbank borrowing, treasury bills, among others.

The Monetary Policy 2017-18 has envisioned to keep the short-term interest rate in between three per cent and seven per cent for the stability of interest rates. Three per cent is lower bound and seven per cent is the upper bound of the interest rate corridor. The central bank mops up liquidity when the interest rate drops below three per cent and injects liquidity when the interest rate increases above five per cent, to keep the interest rate stable.

Narayan Prasad Paudel, executive director and spokesperson for NRB, said that excess liquidity in the market resulted in the interest rate dropping below the lower bound of the corridor. “Central bank has mopped up liquidity to keep the interest rate stable,” he said, adding, “Following the central bank’s intervention, the interbank borrowing rate stood at 3.0377 per cent today.”

The central bank has said that excess liquidity caused interest rate to drop in interbank borrowing.

Central bank has started implementing interest rate corridor in short-term interest rates and plans to gradually enforce it for long-term interest rates like in deposits and lending. “Once the short-term interest rate stabilises, we can expect the interest rate corridor to work on long-term interest rates like lending and deposits,” said Paudel.

However, the bankers have said that the market is not facing liquidity crunch and the BFIs are actually facing crisis of loanable funds. “Central bank is trying to keep its arguments up citing the liquidity scenario; however, the problem is being intensified as there is lack of fresh deposit sources,” one of the bankers told The Himalayan Times.

Banks can lend up to 80 per cent of the sum of their core capital and total deposits. From the remaining 20 per cent, they have to maintain six per cent as cash reserve ratio (CRR), around four to five per cent liquid cash in their vault and remaining 10 to 11 per cent can be invested in government securities.

“Banks are not facing pressure to maintain CRR, they are facing shortage of funds to lend as their lending capacity has already been saturated and majority of the banks have

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extended loans up to the permissible credit to core capital cum deposit (CCD) ratio,” said the banker, requesting anonymity.

There is slackness in potential source of deposits, as per bankers. “The government expenditure is slow, remittance growth is negative, so from where would the banks draw in fresh deposits?” the banker said, adding that the central bank could not even sort out the issue of demonetised Indian banknotes, which was supposed to come into the country.

Source: The Himalayan Times, 9th January 2018