Some thoughts on Bangladesh Bank's next monetary policy statement

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The next monetary policy statement (MPS) of the Bangladesh Bank (BB) will be announced at a time when the economy is in a deep recession, unemployment is high, millions of people and households have become poor overnight, and the infection level is still on the rise.

Economic activity has resumed but seriously handicapped by very low domestic and foreign demand and there is no end in sight for the flattening of the infection curve.

People (jobless workers) and entrepreneurs look to the government for help in pulling them out of the gut.

Various countries have undertaken massive fiscal and monetary interventions to pull their economies out of this devastating situation.

We also must acknowledge that as long as the elephant is in the room, i.e., coronavirus caseload is on the rise, private sector investment will not come back.

Businesses will not be able to operate with full capacity and economic activities will be limited to a sub-optimal level -- well below the 2019 level in real terms (except for agriculture).

Fundamentally, what I would like to underscore is that the BB should not expect that the economy will be rebounding strongly, like after pushing a reset button beginning on July 1.

The central bank should not lose its credibility by projecting that economy will be growing at 8.2 per cent in real terms.

No country in the world can achieve this lofty goal in 2020 amid a pandemic.

At the same time, the MPS must clearly state that the BB would be following an expansionary monetary policy (MP) -- by expanding its balance sheet -- and accommodate the genuine credit needs of the economy in support of economic recovery.

HOW THE MONETARY POLICY SHOULD RESPOND TO THE CURRENT PANDEMIC SITUATION

The huge logjam created by any crisis of this proportion must be cleared with enough injection of liquidity for the wheels of the economy to start turning again.

How much liquidity will be needed will be extremely difficult to predict.

However, the BB should err on the side of injecting a little too much instead of injecting too little under current circumstances.

Close monitoring of the liquidity situation of banks, large enterprises and SMEs will be important in this regard.

In particular, the BB should look at how much credit has been extended to enterprises, including and excluding the unrealised interest accrual that has been capitalised into the outstanding loans by the banks.

The capitalisation of accrued interest will continue to grow fast as borrowers would not be able to service their debt properly and will continue to be protected by the BB regulations without impairment of their loan quality.

How much additional financing has gone to the enterprises of different types should be looked at continuously.

WHAT SHOULD BE THE APPROPRIATE MIX BETWEEN MONETARY AND FISCAL POLICIES IN THE CURRENT BANGLADESH CONTEXT

The policy response to the pandemic has been asymmetric in terms of the mix between fiscal and monetary policies.

While the BB is going to inject liquidity to the tune of Tk 74,000 crore, budget support for creating domestic demand and support for workers' jobs and livelihood have remained modest.

Total budget subsidy embedded within the economic stimulus package was estimated to be only about Tk 3,000 crore and possibly another Tk 2,000 crore out of the interest held in the suspense account.

Unfortunately, the budget does not have domestic resources to provide a significant amount of income or livelihood support without making the already announced deficit even larger.

In my view, this is not a normal year and there was no reason for the fiscal deficit to be limited to 6 per cent of GDP.

It could certainly go up to 8-9 per cent for one year to boost up domestic demand and provide employment and livelihood support.

SHOULD WE BE CONCERNED ABOUT INFLATIONARY PRESSURE UNDER CURRENT CIRCUMSTANCES?

Generally, we would not expect significant inflationary pressure under the current deflationary situation.

Thus, non-food inflation is expected to decelerate in the coming months as house rent, wage costs and THE cost of many services are expected to decline or at best remain unchanged.

In contrast, food inflation as always will continue to be supply-driven and the government has to remain vigilant about accurate production and supply situation.

Rice price has increased in recent months contributing to the spike in food inflation last month.

There is no reason for the current boro paddy price to be at or above Tk 1,100 per maund in various districts even before the flood.

This is an indication of a potentially tight supply situation that may also get aggravated by the loss of entire Aus crop due to the ongoing flood.

The high paddy price, like in 2017/18, may give us a nasty surprise.

The government should go easy on domestic procurement and encourage the private sector to import 1-2 million tonnes of rice from India in the next 1-2 months through reduction of customs duty.

We want farmers to get fair prices, which should be about Tk 900-1,000 per maund of paddy.

On other supplies like fish, poultry, beef, fruits and vegetables, the issue is an efficient transport system and restoration of marketing chains amid the expanding coronavirus caseload.

The bottom line is that, if the government can keep rice price stable and lower than what it is now and help improve domestic transportation and marketing bottlenecks, there should be no upsurge in inflationary pressure.

WHAT SHOULD BE THE STANCE ON THE EXCHANGE RATE AND RESERVE MANAGEMENT?

On the exchange rate, the government has for long been following the policy of maintaining the nominal exchange rate virtually unchanged against the dollar. This did not help the export sectors including garment.

The government had to provide various budgetary incentives to partially compensate for this loss of competitiveness. The sooner we get out of this convoluted arrangement, the better it is for the budget and the export sector.

Recently, with the influx of remittance and a sharp decline in imports due to collapsed domestic economic activity, there has been an excess supply of dollar in the interbank market. This is not an unusual phenomenon.

India is also experiencing a surge in reserve build-up due to a collapse in domestic demand and negative growth (-5 per cent to -9 per cent).

I fear that the Bangladesh economy is also going through a contraction (negative growth) though official data is not reflecting that.

India has massively built up foreign exchange reserves as their trade deficit has declined to a historic low. We are seeing a similar picture in Bangladesh.

The BB should take this opportunity to build up reserves at a fast pace -- perhaps and if possible -- by one billion dollars per month until the economy comes out of the guts.

India is accumulating at the rate of $12-15 billion a month. The consequent injection of liquidity would help increase deposit growth in the banking system and help expand credit to both the private and public sectors.

As regards the prime minister's desire to use dollars for financing development budget, as you know very well, the budget does not need dollar -- it needs taka to finance its projects and other operations.

The government can borrow from the banking system, including also from the BB (which will amount to the creation of high-powered money) in taka to finance its development programme.

If it needs to import anything it can open letters of credit in taka and the BB and banks can provide the necessary foreign exchange.

The government budget does not have any use for foreign currency -- what it needs is taka. The government must make efforts to increase the National Board of Revenue's collection by undertaking forceful and correct reforms -- not bad reforms by listening to the vested groups.

The BB can, however, propose to establish a Sovereign Infrastructure Fund by diverting $5 billion or so to promote public-private partnership investment in major infrastructure projects.

The finance ministry and the BB worked out such a scheme in 2017, but for some unknown reasons, despite cabinet approval, it did not see the light of the day.

That proposal may be presented to the PM for reconsideration to promote $40-$50 billion worth of PPP infrastructure investment in the country.

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My personal feeling is that inflows of remittance will nosedive after a few months once the transfer of savings by the returning workers is completed

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FTA with Bhutan within a month: Munshi

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Bangladesh will sign a free trade agreement (FTA) with Bhutan within the next one month in a bid to increase bilateral trade with the landlocked country in the Eastern Himalayas, Commerce Minister Tipu Munshi said yesterday.

"After that, FTAs will be signed with several other countries in phases. Already, negotiations with those countries, including Indonesia, have come a long way," said Munshi.

The commerce minister made these comments while addressing a virtual workshop styled, 'Covid-19 and international trade issue: policy options for promoting Bangladesh's exports', organised by the Economic Reporters Forum (ERF) in association with RAPID Bangladesh and Asia Foundation.

Trade between Bangladesh and Bhutan that amounted to $26.52 million in fiscal 2012-13 reached $57.90 million in fiscal 2018-19, according to data from the commerce ministry of Bangladesh.

Global trade and commerce have suffered greatly due to the ongoing coronavirus pandemic and Bangladesh is no exception even though the country's economy has moved forward based on its strong foundations, he said.

However, once the Covid-19 crisis comes to an end, Bangladesh's economy will recover in time, the minister added.

"Therefore, better days wait for us ahead," Munshi said, adding that the time has come to take advantage of new global trade opportunities brought about by the coronavirus fallouts.

"We have to work together to take advantage of this opportunity. Soon there will be a lot of changes and competition in the international market," the commerce minister said.

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Govt will go to great lengths for more Japanese investment

Says PM's adviser as over 200 participants join webinar to drive up investment from the Asian economic giant

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The government has assured that potential investors from Japan will be given full cooperation in a bid to drive up the number of investments made in Bangladesh from businesses of the island nation.

"The strength and stability of our economy and our strong political leadership is undoubted. We are very grateful to be considered as a possible destination for further Japanese investments," said Salman F Rahman, the prime minister's private industry and investment affairs adviser.

Rahman made these remarks while addressing a virtual discussion styled, 'Dialogue to drive Japanese investments in Bangladesh' jointly organised by the Prime Minister's Office, the International Finance Corporation (IFC) and Japan International Cooperation Agency (JICA) on Wednesday.

Over 200 participants from Japan's private sector joined the webinar, aimed at attracting investments from the island nation.

During the event, Rahman urged Japanese businesses to take advantage of Bangladesh's high corporate profitability, business-friendly policies, massive domestic market and strategic access to key markets across the world.

While addressing the event, Ito Naoki, the Japanese ambassador to Bangladesh, asked investors from his country to explore the diverse investment opportunities available here.

Bangladesh's economic landscape will transform in a few years with adequate support from the Japanese government, Naoki said.

The ambassador also mentioned Japan's cooperation in the Bay of Bengal Industrial Growth Belt initiative, the Mass Rapid Transit project and the expansion of Dhaka's Hazrat Shahjalal International Airport.

"The Moheshkhali-Matarbari Integrated Infrastructure Development Initiative (MIDI), an energy hub, will be a game changer for Bangladesh," he added.

Naoki also reiterated Japan's commitment towards Bangladesh's development in select sectors such as agriculture, healthcare and human resource development.

"The Japanese government has a menu for cooperation. We will leverage that as much as possible," he said.

Bangladesh Investment Development Authority's (BIDA) Executive Chairman Md Sirazul Islam highlighted the profitability of the country's domestic market as found by JETRO's survey on Asian and Oceania for two years in a row.

"Bangladesh currently has over 300 Japanese companies. In a 2019 survey, it was found that 70.3 per cent of Japanese companies are willing to expand their operations in Bangladesh, which remains the highest proportion in Asia and Oceania," he said.

The BIDA chief discussed the various initiatives being taken to improve the country's business climate through Ease of Doing Business reforms and the expansion of an online One Stop Service.

"BIDA's online and interoperable One Stop Service already provides 18 e-payment enabled services of three agencies and will provide 34 more services of 15 government agencies within the year.

"With the PMO's guidance, we are preparing an attractive package for investors," Islam added.

The BIDA executive chairman also mentioned various measures taken by the government to simplify dividend and profit repatriation.

Foreign companies can now access working capital loans from parent companies.

"And at present, we are working to further liberalise the investment regime for foreign businesses," Islam said.

On Tuesday, Bangladesh Bank announced that all banks and non-banking institutions can now extend financial support to foreign companies against their overseas guarantees. Likewise, the bill-of-entry process was also simplified through automation.

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OBSERVATIONS

- Japanese businesses can take advantage of Bangladesh's massive domestic market
- Diverse investment opportunities available in Bangladesh
- Bangladesh should update policies for foreign investors
- Govt to simplify dividend and profit repatriation
- Bangladesh will be new frontier for Japanese investment
- Bangladesh is a gateway to South Asia due to strategic location