Monetary policy stance: how effective is it?

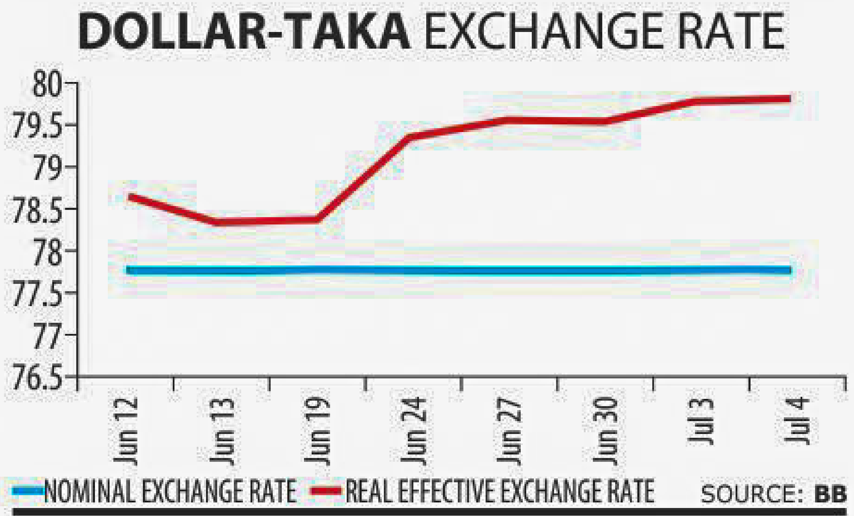
MONZUR HOSSAIN

BANGLADESH Bank declared its monetary policy stance on July 25 for the first half of fiscal 2013-14. It has been made clear in the monetary policy statement that there is no big change in the current stance compared to the last one, i.e. tight monetary policy will continue. The authority does not see any reason for quantitative easing as they feel that inflation target needs to be brought down further from 7.5 percent to 7 percent. The MPS claims that bringing down inflation to 7.5 percent is a great success of the monetary policy stance. The current monetary policy stance is to curb inflation as well as to maintain growth momentum. In the context of this claim, this article makes a critical review of the current monetary stance.

Inflation: In the last few years, Bangladesh saw a surge in inflation due to global commodity price volatility and financial crisis. However, since 2011, the inflation rate started falling and the trend continues for headline inflation. Inflation in Bangladesh is mainly influenced by food inflation. Due to good harvest and favourable agriculture condition, food prices have been declining for the last few years, which have contributed to the fall in inflation. In the contrary, non-food inflation, which is also known as core inflation, was on a rising trend. Monetary policy usually targets core inflation. Then what was the impact of tight monetary policy stance? Since in Bangladesh, food inflation is not largely contingent on monetary policy, and non-food inflation does not follow food inflation pattern, the role of monetary policy on inflation management appears to be ambiguous. Though there might have some positive role of monetary policy in curbing core inflation slightly, the net effect is not significant.

Private credit and aggregate demand: The impact of current tight monetary policy can be seen in squeezing private sector credit growth and aggregate demand. Private sector credit growth declines from 18.2 percent in April 2012 to 11.4 percent in June 2013. The reasons for such retreat, as identified in the MPS, are the political uncertainties and banks' stringent credit policy. This statement warrants further clarification; however, it is missing in the MPS. First, what was the private sector credit growth during other episodes of political uncertainties, particularly in the cases of previous governments? Bangladesh Bank statistics show that private sector credit growth was 18.2 percent in 2005-06 (end of BNP government), 16.87 percent in 2000-01 (end of Awami League govt), and 19.18 percent in 1995-96 (end of BNP govt). The private sector credit growth was much higher than the current level even in the political uncertainties in previous cases. Thus, the statement in the MPS is not true. Second, why do banks pursue a stringent lending policy as long as they are profit-making organisations? Higher repo and reverse repo rates, strict instruction to maintain lending-deposit ratio (usually it should be 0.85, but in reality it was brought down to 0.74) and the overall high lending rates compel banks to pursue stringent lending policy. This is the result of the current tight monetary policy stance. Thus, tight monetary policy is responsible for low private sector credit growth.

DOLLAR-TAKA EXCHANGE RATE



Excess liquidity in the banking sector: At present, the banking sector is sitting with around Tk 72,000 crore of idle money. The banks are trapped in a liquidity overhang. Since there is no signal to the market from the monetary authority for quantitative easing, it is difficult for the banks to go for aggressive lending by lowering the lending rates. The prevailing deposit rates are 12.5 percent or more in the market, which is even higher in some cases due to unhealthy competition among banks for maintaining lending-deposit ratio. The situation is expected to deteriorate with the entrance of new banks. So, there is no option for the banks other than sitting with idle money. This will ultimately be reflected in banks' low profitability. If this situation continues, the banking sector will be in deep trouble in near future. The MPS could not provide any guideline for the banks on how to handle excess liquidity.

Is this a liquidity trap? The current situation is the reflection of a lack of effective demand. The effective demand is the one that matches supply and demand, bringing equilibrium in the situation. Here money supply falls short of meeting the demand for the investment of the economy. As Say's Law suggests, supply creates its own demand, which was forgotten. The lack of demand for investments coupled with a drop in velocity of money is an indication of a decrease in the aggregate demand, while the MPS claims that aggregate demand increases. Velocity of money for the last three years has been below the long-term average of 2 indicating somewhat "unwillingness to spend". It is obvious that banks are now in a liquidity trap. It is the central bank's duty to help banks come out of this trap; however, the current MPS has failed to do so.

Exchange rate policy: This is another area of concern, which was not given due importance in the MPS. It has been admitted in the MPS that Bangladesh loses price competitiveness slightly due to the appreciation of real effective exchange rate (REER). In my view, the current exchange rate management will deteriorate the situation further. There are inconsistencies in exchange rate management and monetary policy stance. Sluggish investment due to tight monetary policy decreases imports (investment), so does the demand for dollars. On the other hand, the dollar buying spree continues to stabilise the exchange rate. Excessive buying of dollars ($ 5 billion in 2011-12) is also causing liquidity overhang and creating a room for losing export competitiveness as figure shows that current exchange rate management creates no room for gaining competitiveness. Maintaining an overvalued exchange rate, as like as the current one, is not always helpful for the economy as well as for exports. While depreciated exchange rate might bring some gain for remitters and exporters, it has downside risk of fuelling inflation. This is another reason for the rising trend of non-food inflation. Thus, the policy should be aimed at maintaining a near-equilibrium rate, and for this reason, the market trend needs to be followed steadily. No such pragmatic exchange rate policy prescription is seen in the MPS.

To conclude, at the time of sluggish investment and falling GDP (gross domestic product) growth, it was expected that there would be a signal for quantitative easing in the MPS when inflation is in control. This is the right time for moving towards accommodative monetary policies; however, unfortunately, the current monetary policy failed to project this. The current tight monetary policy will ultimately take toll on the long-term growth prospects of the economy.

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Indian row over poverty and policy extends to Harvard and Columbia

REUTERS, *New Delhi*

INDIAN government figures showing that poverty has been cut by a third since 2004 has set off a row between the country's main political parties on whether the data is accurate, and a slanging match between two of the world's best-known economists on the implications for policy.

The debate boils down to what path India should take in coming years as slower growth puts further poverty reduction at risk in the world's second-most populous nation.

The opposition Bharatiya Janata Party (BJP) backs growth-oriented reforms that would include a curb on public spending, while the ruling Congress party believes subsidies and a range of social welfare projects have lifted millions out of penury.

Neither of these parties has a commanding lead in opinion polls ahead of general elections due by next May, so they will be competing fiercely for the votes of the poor.

India's Planning Commission said last week that 138 million people - more than the combined population of Britain, Spain and Australia - had climbed out of poverty between fiscal 2004/05 (March-April) and 2011/12. That left the official number of poor among a population of 1.2 billion at 269 million.

"The reduction of the poverty level across the country is a clear manifestation and endorsement of the pro-poor policies and the policy of inclusiveness of the UPA regime," said Bhakta Charan Das, a spokesman of Congress and its United Progressive Alliance (UPA) coalition that has been in power since 2004.

Critics say the numbers have been massaged to look good and any gains are pitiful compared to countries like China or Indonesia.

Congress party policies, which include guaranteed employment for 100 days a year and plans to provide subsidised grain to 800 million people, are also a huge financial drain. India's budget deficit is already around 5 percent of GDP and is seen as a major contributor in drooping investor sentiment.

"It is certainly an achievement," said Nobel laureate Amartya Sen of the reduction in poverty. "Is it a fantastic achievement? No, because the poverty line is low."

A Harvard University professor of economics and a confidant of Prime Minister Manmohan Singh, Sen is widely seen as a major influence on the Congress party's jobs and food programmes.

Jagdish Bhagwati, professor of economics and law at Columbia University, says Sen is an apologist for Congress and its brand of welfare spending at the cost of reforms.

"Sen is not simply wrong; he also poses a serious danger to economic policy in India," Bhagwati wrote in a newspaper column.

US tells Apple to cut ties with publishers in e-book scheme

AFP, *New York*

THE US Department of Justice said Friday that tech giant Apple must cut ties with the five publishers with which it was found guilty of running an e-book price-fixing scheme.

Last month, a US district court in New York found Apple guilty of conspiring with publishers to fix book prices for readers using its iPad and iPhone devices.

On Friday, Justice Department officials submitted to the court a plan for Apple to cut its existing ties to the publishers and to make it easier for its rivals to sell books on its platforms.

"Under the department's proposed order, Apple's illegal conduct will cease and Apple and its senior executives will be prevented from conspiring to thwart competition in the future," assistant attorney general Bill Baer said.

The proposed settlement would see Apple end its current agreements with five US-based publishers: Hachette Book Group, HarperCollins, Macmillan, Penguin and Simon & Schuster.

The tech firm would promise not to enter new contracts with the five to limit price competition in the next five years, and would allow other e-book retailers to link to their products from iPad and iPhone apps for two years.

Apple would also be ordered to pay the salary of an external monitor to confirm its compliance with anti-trust laws.

The Department of Justice lodged a civil antitrust lawsuit against Apple and the publishers in April last year.

It has since reached settlements with four of the publishers and has an agreement with Macmillan that is yet to be approved by the court.

Friday's proposition on Apple's settlement still has to be approved by a federal judge.

Under the existing settlements, the publishers agreed to end any agreements they have with retailers like Apple to prevent them from discounting titles sold through their platforms.

Through its devices and software, Apple allows readers to buy electronic versions of books online and download them to a personal digital library.

In this it competes with other retailers such as Amazon and Barnes & Noble, which sell e-books through online "apps" on mobile devices, using operating systems such as Microsoft's Windows or Google's Android.

The settlement would oblige Apple to allow retailers to "provide links from their e-book apps to their e-bookstores, allowing customers who purchase and read e-books on their iPads and iPhones easily to compare Apple's prices with those of its competitors."

New York Times sells Boston Globe

THE NEW YORK TIMES

THE New York Times Company said on Saturday that it had agreed to sell The Boston Globe and its other New England media properties to John W Henry, principal owner of the Boston Red Sox, returning the paper to local ownership after two decades in which it struggled to stem the decline in circulation and revenue.

Eileen Murphy, a Times spokeswoman, confirmed that Henry would pay $70 million for the paper. That would represent a staggering drop in value for the Globe, which The Times bought in 1993 for $1.1 billion, the highest price paid for an American newspaper. At the time, The Globe was one of the nation's most prestigious papers in a far more robust newspaper environment. But like other newspapers, it began to lose readers and advertisers to the Internet, and revenue plummeted. The Times Company has taken several write-downs related to the New England Media Group, and in February it said it was putting The Globe and other assets in the group up for sale.

For The Globe, the planned sale restores a Boston connection that prevailed for 120 years under the Taylor family, which owned the paper from 1873 until its sale 20 years ago. While not from Boston, Henry has for the last decade been active in local sports, and his Fenway Sports Group owns the Red Sox, Fenway Park and 80 percent of the New England Sports Network. It also owns the soccer club Liverpool FC in the English Premier League.

"This is a thriving, dynamic region that needs a strong, sustainable Boston Globe playing an integral role in the community's long-term future," Henry said in a statement about the sale. "In coming days there will be announcements concerning those joining me in this community commitment and effort."

In addition to The Globe, the sale includes BostonGlobe.com; Boston.com; The Worcester Telegram & Gazette; Telegram.com; the direct mail marketing company Globe Direct; and the company's 49 percent interest in Metro Boston, a free daily paper. Henry is buying the media group without partners through his acquisition company; under terms of the sale, he does not have to assume the Globe's pension liabilities.

The all-cash sale is expected to close in 30-60 days.

The Globe is not the only paper to sell for a heavily discounted price. In April 2012, Philadelphia's newspapers sold for $55 million after selling for $515 million in 2006. In October, The Tampa Tribune sold for $9.5 million. During recent talks about the sale of the Tribune Company's portfolio of newspapers, analysts estimated that the entire newspaper company, including The Los Angeles Times and The Chicago Tribune, was worth only $623 million.

For the Times Company, the New England Media Group was the last big asset in a portfolio it had been downsizing for several years. The acquisition of The Globe in 1993 was part of the company's strategy to solidify its grip on the eastern corridor advertising sector and to have a presence that stretched from Maine to the District of Columbia. At the time, in addition to its flagship New York newspaper, the Times Company owned 31 regional newspapers, 20 magazines, 5 television stations, 2 radio stations and other businesses. It also had a half-interest, with the Washington Post Company, in The International Herald Tribune.

But in recent years, the Times Company has been divesting itself of its noncore assets to focus on developing its primary brand, The New York Times. In 2012, the company sold its 16 regional newspapers. Last year, it sold the About Group to IAC/InterActiveCorp for $300 million. This year,

AFP

People walk by the New York Times office in New York. The premier US newspaper is selling the Boston Globe for a fraction of the $1.1 billion it paid for the newspaper in 1993.

The Times announced plans to expand its global presence by changing the name of The International Herald Tribune to The International New York Times and attracting a new global audience of readers to become subscribers.

The Globe attracted a range of prospective buyers. Among those who expressed interest were Douglas F Manchester, owner of the U-T San Diego; and a group led by Jack Griffin, the former chief executive of Time Inc., that included Ben and Steve Taylor, whose family sold The Globe to the Times Company.

This week, The Globe reported that Henry had offered to buy the paper after the sports investment group he had partnered with backed out. Henry worked with The Times over the last decade on its purchase of a stake in the Fenway Sports Group. In 2012, the Times Company sold its final stake in the group for $63 million.

Like most newspapers, The Globe has struggled to hold onto its readers and the print advertisers who fed its profits for decades. According to the Alliance for Audited Media, circulation at The Globe from Monday through Friday declined 38 percent in 2013 from 2003, to 245,572 from 402,423. Before the Times Company bought The Globe in 1993, The Globe had a weekday circulation of 506,996.

As circulation declined, so did advertising. According to the second-quarter earnings statement released by the Times Company on Thursday, advertising revenue for the New England Media Group dropped 9.5 percent, to $44.4 million, compared with the same quarter in 2012.

After the release of the company's earnings, John Janedis, a research analyst with UBS, said it was wise for the company to sell The Globe. He estimated that the paper was worth $150 million to $175 million on a cash flow basis without factoring in pension liabilities.

"The trends at The Globe have been a drag on the company," Janedis said. "The New York Times has performed a lot better over the past several years. To the extent that you can refocus on a paper with massive global appeal that has still a very strong core readership and then expand the product offerings, there's probably more long-term value creation there versus having The Times and The Globe long term in the same portfolio."

During the time that it was owned by the Times Company, The Globe won eight Pulitzer Prizes, including the 2003 public service award for its coverage of sexual abuse in the Catholic Church. Last November, The Washington Post hired away the paper's editor of a decade, Martin Baron, who had shepherded The Globe's coverage since shortly before the Sept. 11, 2001, attacks. In December, The Times announced that Brian McGrory, a longtime columnist and former metro editor, would succeed Baron. In the early days in his job, McGrory led the Globe staff through its coverage of the Boston Marathon bombing, which was picked up by news organisations around the world.

As many papers have struggled to remain relevant with younger readers who read more news online, The Globe made some strides at attracting younger audiences. Under the leadership of its publisher, Christopher M Mayer, The Globe invited technology start-up firms to use abandoned classified advertising space in its shrinking newsroom. It also turned empty space into community spaces where bands visiting the company's Internet station, RadioBDC, could perform. According to the latest earnings report, the number of digital subscribers grew nearly 70 percent to 39,000 in the second quarter compared with the year-earlier period.