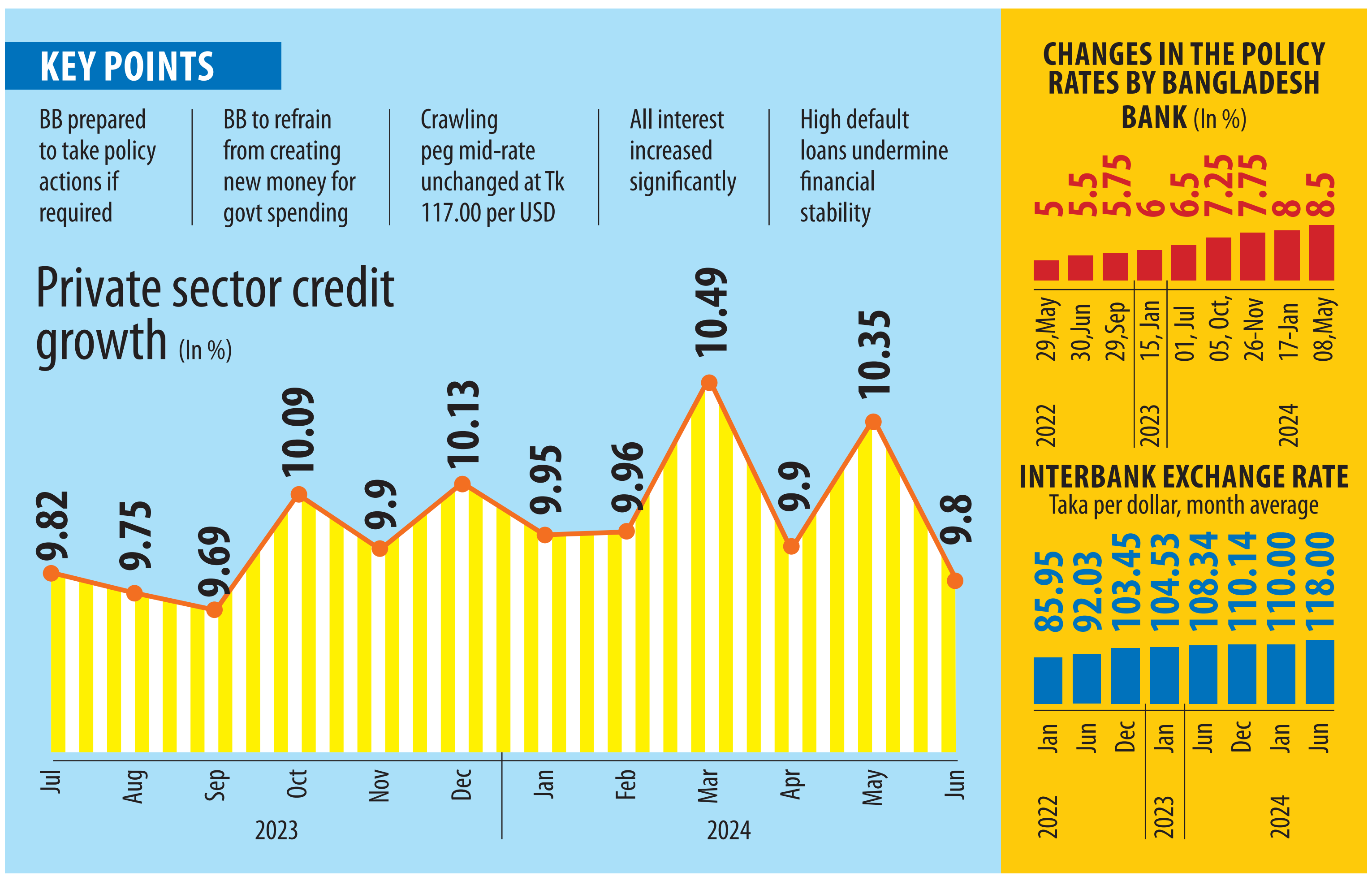
Star BUSINESS

Import and sale of reconditioned vehicles have increased in Bangladesh despite suffering from high inflationary pressure and foreign currency crisis.

Story on B4

BB keeps key policy rate unchanged but signals further tightening

Inflation can't be curbed without raising the repo rate, say economists



Govt borrowing from banks to increase

FAHMIDA KHATUN

Broadly, the policy measure to control inflation remains the same in the Monetary Policy Statement (MPS) of the Bangladesh Bank for July-December 2024.

In May 2024, the Bangladesh Bank hiked the policy rate by 50 basis points to make it 8.5 percent. This was a continuation of earlier attempts to increase policy rates.

For example, in January 2024, the policy rate was increased from 7.75 percent to 8 percent. The central bank increases policy rates to hike the interest rates in the commercial banks. This was a welcome move as the interest rate cap on lending and deposit rates during April 2020- June 2023 was a wrong policy tool to contain inflationary pressure.

Following a lot of discussions, the Bangladesh Bank's next attempt to introduce a reference lending rate - the six-month moving average rate of treasury bills (SMART) was also a total failure in bringing down inflation.

On top of that, the Bangladesh bank printed money that further increased inflationary pressure on the people. Even after the policy rate hike in May 2024, the inflation rate is over 9 percent. So, the effectiveness of the increased policy rate is yet to be observed.

The Bangladesh Bank has opted to use policy rates as a tool to control inflation much later than other central banks in the world, including developing countries such as India. As a result, the central banks of those countries have successfully curtailed the inflation rate. Though the policy rate has not been changed, Bangladesh Bank has to remain open to further increases in policy rates to curb inflation.

Some changes have been made in the monetary and credit projection for fiscal year (FY) 2025. Though credit growth to the private sector remains the same at 9.8 per cent, credit to the public sector will grow by 14.2 percent till December 2024 and by 17.8 percent by June 2025.

This implies that the government borrowing from the banking sector will increase. The reliance of the government on bank borrowing risks crowding out of the private sector. If commercial banks are under pressure to provide loans to

READ MORE ON B3

MD MEHEDI HASAN

Despite suggestions for a policy rate hike from the International Monetary Fund (IMF) and economists, the central bank of Bangladesh has kept unchanged the major tool of its monetary policy at 8.5 percent although inflation is running high.

The Bangladesh Bank yesterday unveiled the monetary policy statement (MPS) for July-December of 2024-25. It said that the current tightening monetary policy stance would be maintained, and it will help ease the inflationary pressure.

"However, BB remains prepared to take necessary policy actions if required," it said.

"The major policy reforms that the central bank took on May 8 came into effect, and we see the outcome to tackle economic challenges, including higher inflation and the forex crisis," Md Habibur Rahman, a deputy governor, told The Daily Star.

Also the head of the monetary policy department of the central bank, Rahman said as the previous policy stance is producing expected outcome, the policy rate and the crawling peg exchange rate system have not been changed.

In May, the banking watchdog took three bold measures in line with the IMF's $4.7 billion loan programme. It allowed banks to fix the interest rate, brought flexibility to the exchange rate by introducing the crawling peg system, and hiked the policy rate by 50 basis points to 8.5 percent, the ninth straight increase in the span of less than two years.

Yesterday, the BB said that the economy has begun to respond to these policies.

It, however, said while the upward trend in inflation has moderated recently, it remains stubbornly high owing to food price inflation. The BB aims to bring down inflation to 6.5 percent at the end of FY25.

Annual inflation rose to 9.73 percent in 2023-24, the highest since 2011-12, overshooting the government's target of containing it to 7.5 percent, according to the Bangladesh Bureau of Statistics (BBS). This was the second year in a row, inflation in the country stayed above 9 percent.

On the other hand, most countries, including the US, India and even cash-strapped Sri Lanka, have succeeded in bringing down inflation from their record levels.

As a result, inflation control has remained a top priority for the BB.

The BB has maintained a contractionary monetary policy for over a year, significantly increasing the policy rate and avoiding new high-powered money issuance for government spending.

Ahsan H Mansur, executive director of the Policy Research Institute of Bangladesh, thinks that the central bank was on the right

READ MORE ON B3

Not much beyond lip service

ZAHID HUSSAIN

In their Monetary Policy Statement (MPS) for the first half of FY25, Bangladesh Bank (BB) has stuck to the policy stance already in place. There is no further tightening, no specific measures to enhance liquidity management and transition to a flexible market-based exchange rate regime from the "crawling peg". The MPS recognises the deep stress in the financial sector and provides a long list of legislative measures already passed and regulatory plans announced without committing to a timebound and results-oriented path of action.

Let's begin with the central question to gauge what more this MPS could have done to increase the potency of monetary policy in restoring macro-financial stability.

WHY HAS STABILITY REMAINED ELUSIVE?

Inflation has remained stubbornly close to double digits; foreign exchange reserves are significantly lower than they were a year ago; and financial sector woes appear to be seeking new lows all the time. What explains these performance shortfalls despite monetary tightening, exchange rate reforms and apparently streamlined financial regulation? The short answer is results elude when measures remain less than fully baked.

For most of the monetary tightening cycle that started in May 2022, the transmission of contraction remained confined within the banking system. It could not spillover at the retail level until July 2023 because of the 9 percent cap on retail lending rates. The SMART based retail rate policy subsequently allowed limited room for transmission. The door for transmission opened fully in principle only since May 2024 with the abolishing of SMART. Yet there are perceptions of invisible ceilings.

The tightening lacked consistency. BB has been financing the fiscal deficit indirectly by providing liquidity to banks against their holdings of government bills and bonds. Fiscal austerity has been limited at best. The large budget deficit counteracted monetary contraction by boosting aggregate demand. Tightening is also diluted by BB's so called "supply-side intervention policy" to enhance production and support employment generation.

READ MORE ON B3

Stocks drop amidst student movement

STAR BUSINESS REPORT

Stocks in Bangladesh fell for a second consecutive day yesterday as skittish investors sold off their shares in panic amidst a countrywide shutdown enforced by students demanding withdrawal of a quota system in government jobs.

As a result, the major index of Dhaka Stock Exchange (DSE), the DSEX, dropped 36.64 points, or 0.67 percent, from that on the day before to close at 5,446.50.

The two other indices of the DSE also ended lower.

The DSES index, representing the Shariah-compliant companies, slipped 10.43 points to finish at 1,191.43 while the DS30 index, comprising the blue-chip firms, dipped 8.10 points to settle at 1,953.27.

Chittagong Stock Exchange (CSE) also saw a similar trend with its all-share price index losing 50.45 points, 0.32 percent, to settle at 15,566.159.

Saiful Islam, president of the DSE Brokers Association of Bangladesh, said the drop in the index was a clear impact of the shutdown.

The uncertainties centring the student movement has been prolonged unexpectedly. So, its impact was evident on the stock market, he said.

Due to the movement, people could not move from one end of the capital to the other and many of them were stuck wherever they were. So, the presence of investors was low, he said.

On the other hand, people were worried over the law and order situation of the country. As a result, the day's turnover at the stock market was low, he added.

The day's turnover, meaning the total value of shares traded at the DSE, stood at Tk 371 crore, a decrease of 34.17 percent compared to the previous day's trading session. This was the lowest turnover in the last one month.

Block trades, meaning high-volume transactions in a

READ MORE ON B3

BB identifies risks to economic stability

STAR BUSINESS REPORT

The Bangladesh Bank has identified several macroeconomic challenges that are hurting the economy such as higher inflation and widening income inequality.

"Bangladesh faces several immediate macroeconomic issues that threaten its economic stability and growth," it said.

In its monetary policy statement released yesterday for the first half of the current fiscal year, the central bank said these challenges arise from domestic and international factors, creating a complex policy environment.

"Persistently high inflation erodes purchasing power and real incomes, exacerbating income inequalities."

The BB pinpointed some other challenges confronting the country, including the exchange rate volatility, fiscal constraints, and the financial sector instability.

In order to address these issues, the country requires a multifaceted approach involving a prudent monetary policy, effective fiscal management, and structural reforms, it said.

"By navigating these challenges carefully, Bangladesh can sustain economic growth and enhance resilience against external shocks."

Geopolitical tensions, such as the Russia-Ukraine conflict and the unrest in the Middle East, have disrupted global supply chains and driven up the prices for essential commodities like food and energy, hitting import-dependent nations like Bangladesh hard as foreign currency reserves have witnessed a significant depletion.

The BB has adopted a contractionary monetary policy to manage inflation, but balancing this with economic growth remains delicate.

The global economic outlook is positive, but uncertainties persist due to ongoing geopolitical tensions. Policy rate cuts in advanced economies could affect reverse capital flows and exchange rates.

Bangladesh's forex reserves fell from $41.7 billion in August 2021 to $21.79 billion on June 30. The taka has lost its value by about 35 percent against the US dollar in the past two years.

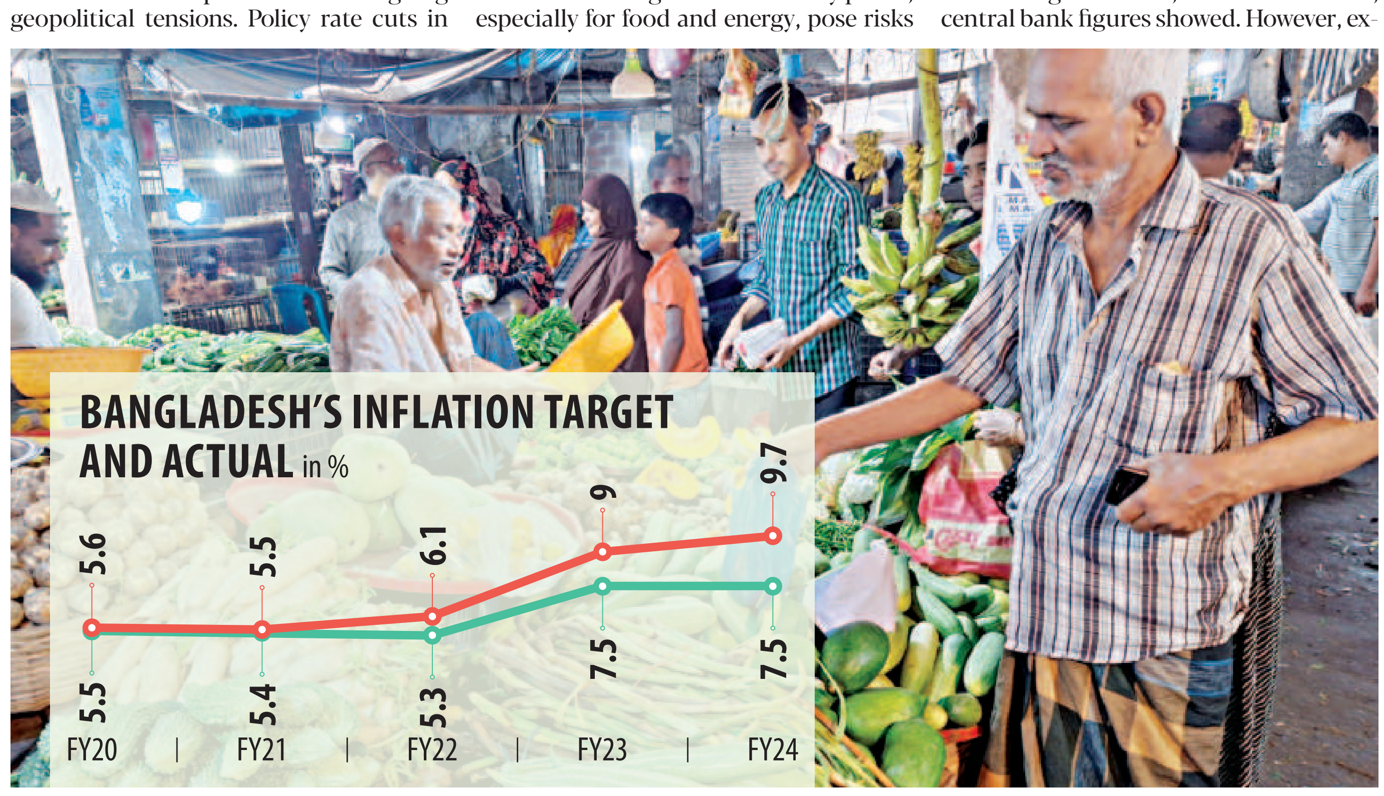
"Fluctuations in global commodity prices, especially for food and energy, pose risks due to Bangladesh's import dependence," the BB said.

According to the central bank, high non-performing loans (NPLs) undermine financial stability and limit credit availability for productive investments.

Default loans in the banking sector hit an all-time high of Tk 182,295 crore in March, central bank figures showed. However, experts say the figure would be much higher owing to under-reporting.

The BB is implementing measures to reduce NPLs and improve governance with-

READ MORE ON B3



Shoppers at a kitchen market in Notun Bazar area of Barishal city yesterday. Bangladesh concluded fiscal year 2023-24 in June with inflation at an average of 9.73 percent, the highest in 12 years, showcasing a worsening scenario for real income and a deterioration of living standards of low-income groups. PHOTO: TITU DAS