Bangladesh Economic Update

Monetary Policy Statement (July-December, FY 2017-18): A Rapid Assessment

July, 2017

The Unnayan Onneshan (UO), an independent multidisciplinary think-tank, in its rapid assessment of recently announced monetary policy statement for the first half of the FY 2017-2018 cautions that targeted private sector credit growth may fail to boost private investment in absence of a business enabling environment. Rising food inflation may further challenge the effectiveness of the policy.

The UO in its July issue of Bangladesh Economic Update 2017 fears that without increasing the quality, mere growth in private sector credit by the targeted level – 16.3 percent for July-December of the current fiscal year compared to 16.5 percent for the January-June of the previous year – may prove ineffective in facilitating investment-led employment generation and economic expansion.

The think tank points out that private investment has remained stagnant and stood at 22.07 percent of GDP in FY 2014-15, 22.99 percent in FY 2015-16, and 23.01 percent in FY 2016-17 despite significant increase in domestic savings from 22.16 percent in FY 2014-15 to 26.06 percent in FY 2016-17.

From 16.1 percent in March 2017, private sector credit growth slightly increased to 16.2 percent in April, and then declined to 16 percent May 2017. Taking account of the recent trend, the research organization warns that the target of 16.3 percent growth in private sector credit for first half of the current fiscal year may remain unachieved causing stagnation in private investment to continue.

The think-tank evinces that the number of unemployed population increased at an annual rate of 5.29 percent during the period of 2000-2010 and increased from 1.70 million in 2000 to 2.60 million in 2010 while 10.6 million people were day laborers who did not have job security. In addition, 9.1 percent of the country's youth labor force is currently unemployed.

Referring to the recent rise in consumer price index (CPI) inflation, the research organization expresses concern over the "prudent and flexible" course sought by the central bank in dealing with inflationary pressure and predicts achievement of real growth in gross domestic product below the targeted 7.4 percent rate in the current fiscal year.

Taking note of the challenge facing the central bank in containing inflation in the first half of FY 2017-18, the think tank shows that general inflation increased from 5.47 percent in April'2017 to 5.94 percent in June'17, while food inflation increased from 6.94 percent to 7.51 percent during the same period of time. Moving average inflation also takes an upward trend in recent times.

Referring to weak performance of the external sector, the UO finds that the current account balance recorded a deficit of USD 1.76 billion during July-April 2017, whereas a surplus of USD 3.53 billion was observed during the same period of previous fiscal year. Current unsatisfactory performance of the sector is due to higher import growth (9 percent), lower export growth (1.7 percent), and slowdown in remittance inflows (-14.5 percent) during corresponding period of current fiscal year.

In regard to increased non-performing loan (NPL) vis-à-vis the total loan in the banking system, the think tank reiterates its concern about inefficiency in the banking sector and finds that the ratio of gross NPL to the total outstanding loans increased further from 9.2 percent at the end of December 2016 to 10.5 percent at the end of March 2017.

Referring to persistent deterioration in the financial portfolio of the state-owned banks due to monumental rise in writing off of loans, meteoric rise in the default loans and nose-dive in risk and capital adequacy ratio, the research organization cautions that the public in general has to pump their tax money to rescue the stripped nationalized commercial banks through recapitalization.

Calling for a cautious harmonization of fiscal and monetary policies that would cause both the money and fiscal multiplier to work in the economy and channel adequate resources for the expansion of productive capacities, the UO urges for creating a stable investment climate that would increase private investment leading to creation of employment opportunities and thus cause the national output to grow at the targeted rate.