Monetary Policy Statement

January-June 2024

Bangladesh Bank

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Bangladesh Bank

www.bb.org.bd

Acronyms and Abbreviations

ABB	Association of Bankers, Bangladesh
ALS	Assured Liquidity Support
AMC	Asset Management Company
App	Appreciation
AD	Authorised Dealer
BAFEDA	Bangladesh Foreign Exchange Dealer's Association
BB	Bangladesh Bank
BBLC	Back-to-Back Letter of Credit
BBS	Bangladesh Bureau of Statistics
BFIU	Bangladesh Financial Intelligence Unit
BDT	Bangladesh Taka
BL	Bad and Loss
BoP	Balance of Payments
BPM6	Balance of Payments and International Investment Position Manual, 6th. edition
BPS	Basis Points
BSEC	Bangladesh Securities and Exchange Commission
CAB	Current Account Balance
C&F	Clearing and Forwarding
CDBL	Central Depository Bangladesh Limited
CMSME	Cottage, Micro, Small and Medium Enterprise
COVID	Coronavirus Disease
CPI	Consumer Price Index
CRR	Cash Reserve Ratio
DBU	Domestic Banking Units
Dep	Depreciation
DSE	Dhaka Stock Exchange
DSEX	Dhaka Stock Exchange Broad Index
EDF	Export Development Fund
ERQ	Export Retention Quota
FY	Fiscal Year
FC	Foreign Currency
FDI	Foreign Direct Investment
FID	Financial Institutions Department
GCC	Gulf Cooperation Council
GDP	Gross Domestic Product
GIR	Gross International Reserves
GTF	Green Transformation Fund
H1	First Half
H2	Second Half
IBLF	Islamic Banks Liquidity Facility
ID	Identification
IDFR	International Day of Family Remittances
IDTP	Interoperable Digital Transaction Platform
IFC	International Finance Corporation
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund

IRC	Interest Rate Corridor
IT	Information Technology
LC	Letter of Credit
L.H.S	Left Hand Side
M2	Broad Money
MFS	Mobile Financial Service
MLS	Mudarabah Liquidity Support
MoF	Ministry of Finance
MoUs	Memorandum of Understandings
MPS	Monetary Policy Statement
NBFI	Non-Bank Financial Institution
NEER	Nominal Effective Exchange Rate
NFA	Net Foreign Asset
NPL	Non-Performing Loan
NRB	Non-Resident Bangladeshis
NSCs	National Savings Certificates
OBOs	Offshore Banking Operations
ODA	Official Development Assistance
PCA	Prompt Corrective Action
PCBs	Private Commercial Banks
PFI	Private Finance Initiative
PLC	Private Limited Company
PoP	Period over Period
p-to-p	Point to Point
PSPs	Payment Service Providers
QR	Quick Response
RBS	Risk-Based Supervision
REER	Real Effective Exchange Rate
RFCD	Resident Foreign Currency Deposit
R.H.S	Right Hand Side
RM	Reserve Money
RMG	Ready-Made Garments
SDF	Standing Deposit Facility
SLF	Standing Lending Facility
SLR	Statutory Liquidity Ratio
SMART	Six-months Moving Average Rate of Treasury bills
SOCBs	State-Owned Commercial Banks
TB	Treasury Bills
UK	United Kingdom
UPS	Universal Pension Scheme
US	United States
USD	US Dollar
WEO	World Economic Outlook
Y-o-Y	Year over Year

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Executive Summary

As Bangladesh's economy navigates through the latter half of Fiscal Year 2024, Bangladesh Bank (BB) finds itself at a critical juncture, facing a multifaceted economic landscape. Internally, the economy is striving to restore the stability of the exchange rate and manage the inflationary pressures while dealing with the lingering issue of high non-performing loans. The increasing costs of essential imports and the strain on the country's foreign exchange reserves add complexity to the domestic economic challenges.

Globally, geopolitical tensions and trade uncertainties continue to roil commodity markets, exacerbated by growing rivalries among vital global powers. This international turmoil impacts Bangladesh's economy through disrupted supply chains and altered trade dynamics. In response, BB's policy strategy involves a nuanced approach: tightening monetary controls to rein in inflation while ensuring sufficient liquidity to nurture growth sectors. Additionally, reinforcing the balance of payments and wisely managing the foreign exchange reserves is pivotal.

This MPS delineates a strategy designed to navigate these diverse challenges, aiming to preserve the resilience of Bangladesh's economic trajectory amidst these internal and external pressures. Notably, despite a recent moderation in core inflation (excluding food and fuel), the headline Consumer Price Index (CPI) based inflation remains high. Monetary and credit aggregates, including broad and reserve money and public and private sector credit, have aligned with BB's projections in the first half of FY24. Considering these factors and BB's policy priorities, maintaining a tighter monetary stance in the latter half of FY24 seems prudent. This approach is intended to control inflation and stabilize expectations while ensuring adequate funding for the more productive sectors to foster desired growth.

Global and domestic macroeconomic conditions and projections have been comprehensively analyzed in shaping BB's monetary and credit policy. Crucially, BB has incorporated various perspectives and expert insights garnered from a series of monetary policy consultation meetings. This inclusive process enriches its policy-making with diverse viewpoints and specialized knowledge. In light of the prevailing economic conditions and after thorough deliberations, the monetary policy committee has decided to adjust the policy rates in the following manner:

> *The policy rate will be increased by 25 basis points to 8.00 percent from 7.75 percent. Additionally, to refine liquidity management, the Standing Lending Facility (SLF) rate will be reduced by 25 basis points to 9.50 percent from 9.75 percent, and the Standing Deposit Facility (SDF) rate will be increased by 75 basis points to 6.50 percent from 5.75 percent, reducing the policy rate corridor from ± 200 basis points to ± 150 basis points.*

Since mid-2022, the Bangladesh Taka has been depreciating against the US dollar, a trend primarily attributed to a balance of payments deficit leading to a significant reduction in foreign exchange reserves over the year. This weakening of the Taka has been a contributing factor to domestic inflation, as the cost of imports has risen. In response to these challenges, there is an increasing call for a gradual shift towards a market-based exchange rate system. This transition is advocated to stabilize the exchange rate and prevent further depletion of the country's foreign exchange reserves.

> *In this regard, BB is contemplating the implementation of a crawling peg system, which would be linked to a carefully selected basket of currencies and operate within a predefined exchange rate corridor. This strategy is aimed at tempering unusual fluctuations in the currency's value. By setting a competitive equilibrium exchange rate at the midpoint of this corridor, BB would establish a stable benchmark while retaining the flexibility to intervene in the market as necessary to maintain the currency within the designated boundaries.*

BB's policy efforts, combined with the anticipated global decline in energy and commodity prices and a promising outlook for internal production, support BB's expectation that average general inflation will align with the government's revised 7.50 percent target by June FY24. Introducing a crawling peg exchange rate management system is expected to reduce market volatility and enhance foreign exchange stability significantly.

For the second half of FY24, Bangladesh Bank's strategic directives are centered on upholding a vigilant, hawkish approach to monetary policy until inflation rates are effectively reined into a desired level. Concurrently, the BB is evaluating the potential of implementing a crawling peg exchange rate system. This system would serve as a transitional arrangement, paving the way towards a fully flexible exchange rate regime in the future. Additionally, a significant focus is being placed on enhancing the management of non-performing loans. This involves adopting more robust governance practices and deploying efficacious strategies through a targeted roadmap for NPL resolution.

Despite the ongoing challenges, Bangladesh's economic outlook for the end of FY24 remains positive, with expectations of robust real GDP growth targeted at 6.5 percent and moderated inflation aimed at 7.5 percent. With the concerted efforts of Bangladesh Bank, the government, and other stakeholders, stability in the foreign exchange market and improvements in corporate governance and non-performing loans management are also anticipated.

Monetary Policy Statement: H2FY24

1. Foreword

One of the primary mandates of Bangladesh Bank (BB), the central bank of Bangladesh, is to craft and execute its Monetary Policy. This policy aims to stabilize and uphold the internal and external value of the Taka (BDT) while concurrently fostering investment, employment opportunities, and overall economic growth. Since 2006, BB has been formally formulating and implementing its monetary policy by publishing Monetary Policy Statements (MPS). This release of MPS for the second half of FY24 (H2FY24) aims to secure and maintain Taka's value, anchoring inflation expectations among economic stakeholders. The strategy also includes targeted interventions to spur desired investment, employment, and economic growth.

The current edition of BB's biannual Monetary Policy Statement (MPS) outlines the monetary policy approach for H2FY24, drawing insights from the actual performance in the first half of FY24 (H1FY24). This comprehensive analysis encompasses prevailing macroeconomic conditions, forecasts for global and domestic landscapes, monetary and credit projections, and insights from consultations with diverse stakeholders. These stakeholders encompass a spectrum of voices, including former and current policymakers, economists from think tanks and academia, respected personnel from the business and financial sectors, economic journalists, and inputs received via the BB website. BB also conducts deliberations involving its executives and esteemed members of its Board of Directors.

The invaluable feedback, suggestions, and directives gathered through these consultations with stakeholders, BB's executives, external members of the monetary policy committee and learned members of its Board of Directors have significantly enriched the formulation of this monetary policy stance and shaped monetary and credit projections for H2FY24. Moreover, considering essential background information and rationale, a thorough assessment of the preceding monetary policy stance has been diligently conducted before framing the strategy and projections for H2FY24.

2. Monetary Policy Outcomes in H1FY24

BB released its Monetary Policy Statement (MPS) for H1FY24 in June 2023, shifting toward a contractionary monetary policy stance and implementing a structural change within its monetary policy framework. Traditionally, BB had favored a monetary targeting framework for its monetary policy approach. However, considering the economy's evolving complexity, the financial system's dynamic nature, the emergence of new financial instruments, efficient liquidity management, and integration into the global financial market, BB transitioned to an interest rate targeting framework, discarding the monetary targeting framework.

The new monetary policy introduced four significant reforms: (i) the implementation of a policy interest rate corridor, (ii) the establishment of a reference interest rate for lending, (iii) the unification of the exchange rate, and (iv) a revised methodology for calculating gross international reserves, aligning with the 6th Balance of Payment and International Investment Position Manual (BPM6). One of the primary objectives of the monetary policy for H1FY24 was to curb inflation and maintain it within the targeted level outlined in the national budget for FY24.

Confronted with persistently high inflation, BB implemented several policy measures during H1FY24 to alleviate the inflationary pressure. These initiatives encompassed a cumulative 175 basis points increase in policy rates from July to December 2023, the removal of the lending rate cap, replaced with a competitive market-based reference rate (SMART) accompanied by a margin, and ceased lending to the government by creating money. These actions aimed to elevate borrowing costs, restrict money and credit expansion, and anchor inflation expectations. Consequently, money supply and private sector credit growth rates moderated between July and November 2023. Additionally, BB continued foreign currency sales, which functioned as automatic quantitative tightening measures in the money market, significantly absorbing liquidity from the system.

While the inflationary pressure slightly eased to 9.41% (point to point) by the end of December 2023 compared to the previous month, it remained considerably higher than the desired level. Bangladesh's economy couldn't capitalize on the recent global commodity price decline due to substantial domestic currency depreciation, negating the potential advantages of lower international prices. BB also extended comprehensive support for supply enhancement activities to combat inflation, offering refinancing and pre-financing lines of low-cost credit for agriculture, CMSMEs (Cottage, Micro, Small, and Medium Enterprises), import substitution, and export-oriented industries.

During the first half of FY24, Bangladesh Bank (BB) took several strategic measures to address persistent external sector pressure. These actions aimed to balance demand and supply side factors, encompassing a range of impactful steps. To manage these pressures, BB allowed a noticeable depreciation of the Bangladesh Taka (BDT) in line with market forces. Additionally, it conducted significant sales of foreign currencies, amounting to USD 6.74 billion by December 2023, to ease the strain on the exchange rate. Efforts were made to discourage less-necessary & luxury imports while enhancing monitoring and price verification of all imports. Furthermore, BB strengthened oversight of foreign exchange dealings by banks and money changers, reducing cash foreign currency holdings by the latter. The bank also implemented measures such as increasing interest rates on loans from the Export Development Fund (EDF), streamlining remittance repatriation and cash incentive distribution processes, and establishing agreements with foreign exchange houses.

Innovative steps were taken, including permitting mobile financial services in remittance collection and distribution and waiving remittance transaction fees by local banks. The Non-Resident Bangladeshi (NRB) investment procedure was liberalized, allowing FC accounts to be opened with a passport instead of a National ID. Moreover, BB raised interest rates on non-resident foreign currency deposits and enforced a 180-day limit for export proceeds repatriation, among other adjustments to export retention quotas and banks' net open positions.

These policy initiatives resulted in significant shifts within the money market. The volume and weighted average interest rates in the money market experienced notable increases. The weighted average call money rate surged to 8.84 percent by December 2023, up from 6.06 percent in June 2023. Similarly, the interbank average repo rate climbed to 8.06 percent by December 2023, compared to 6.16 percent in June 2023. Moreover, lending and deposit rates for various financial transactions notably rose in H1FY24 while effectively containing the interbank call money rate within the Interest Rate Corridor (IRC).

In response to measures undertaken globally to mitigate higher inflation, there appeared to be a contraction in global demand, as indicated by growth projections from various agencies. Despite this, export earnings, a pivotal indicator of external demand, saw a marginal increase of 0.84 percent (Period over Period, PoP) during July-December of FY24, contrasting with the 10.58 percent rise in the same period the previous year. This growth occurred amidst ongoing uncertainties in the global economy, supported by policy measures enacted by monetary and fiscal authorities. However, customs-based imports, a crucial gauge of internal demand, experienced a significant decline of 21.02 percent (PoP) during July-November of FY24 compared to a 4.35 percent rise in the same period of the previous fiscal year.

The decrease in imports might be attributed to discourage imports of less-necessary and luxury goods, reinforce monitoring mechanisms by BB concerning justified prices for opening Letters of Credit (LCs), alongside a notable depreciation of the Bangladesh Taka. This combined impact likely contributed to the negative import growth during this period. Moreover, consumer credit, another critical indicator of internal demand, saw slower growth of 15.99 percent (Year over Year, YoY) in September 2023 compared to the 26.65 percent increase recorded in the same month of the previous year.

Throughout H1FY24, domestic commodity prices witnessed a substantial increase compared to the corresponding period of the previous fiscal year. The inflation surge was initially triggered by supply chain disruptions due to the COVID-19 pandemic and the Russia-Ukraine conflict. Later, in 2022, while global commodity prices started to decline, the significant deficits in Bangladesh's current account balance and overall balance of payments led to a sizeable depreciation of the Bangladesh Taka. Despite the recent global commodity price decline, Bangladesh's economy couldn't benefit due to the significant domestic currency depreciation, offsetting potential advantages from lower international prices. This depreciation subsequently raised import prices, contributing to inflationary pressures. Additionally, second round effects from adjustments in energy prices and imperfections in the commodity market further compounded high inflation.

Based on the available Consumer Price Index (CPI) data, the point-to-point inflation rate showed a moderate decline, reaching 9.41 percent in December 2023 compared to 9.74 percent in June 2023. However, the CPI-based average headline inflation rose to 9.48 percent in December 2023 from 9.02 percent in June 2023, primarily due to higher inflation rates in the most recent months were considered in this count. Among the components contributing to headline inflation, the prominence of food inflation outweighed non-food inflation during July-December of FY24. Furthermore, core inflation (excluding food and fuel), an important indicator closely linked to monetary policy, continued to show a declining tendency, averaging 7.72 percent in December 2023 compared to 8.53 percent in June 2023.

Regarding the monetary landscape, the broad money (M2), a key indicator monitored by monetary policy, grew by 8.8 percent by the end of December 2023, falling below the projected growth for December 2023. This subdued M2 growth was primarily influenced by a decrease in the net foreign assets (NFA) of the banking system during H1FY24, which declined by 21.8 percent in December 2023 compared to the anticipated 16.8 percent decline in December 2023, mainly due to a deficit in the overall balance of payments (BoP), particularly in the financial account balance despite a surplus in the current account balance.

The Reserve Money (RM) experienced a decrease of 2.0 percent (year-over-year) by the end of December 2023. However, RM growth fell below the projected trajectory in H1FY24 due to the negative growth of Bangladesh Bank's Net Foreign Assets (NFA), which saw substantial negative growth due to significant foreign currency sales to banks to meet excess demand for USD. Throughout H1FY24, the banking sector encountered a situation of tightened excess cash reserves due to commercial banks' purchases of USD from Bangladesh Bank to satisfy heightened demand for foreign currency and increased investments in T-bills and T-bonds driven by attractive high-return opportunities.

In summary, most monetary and credit aggregates were aligned with the anticipated trajectory during H1FY24. Table 1 and Charts 1-6 exhibit the actual growth paths of major monetary and credit aggregates compared to the projection set for FY24, initially announced in June 2023.

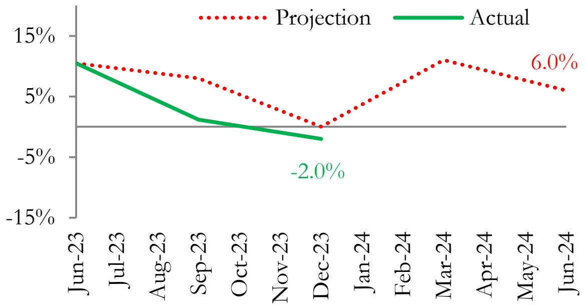
Table 1: Developments of Monetary Aggregates

(YoY % change)

Item	Jun-23	Sept-23	Dec-23		Jun-24
	Actual	Actual	Projection	Actual P	Projection @
Broad money	**10.5**	**9.0**	**9.5**	**8.8**	**10.0**
Net Foreign Assets*	-23.4	-23.7	-16.8	-21.8	4.7
Net Domestic Assets	21.3	17.9	15.9	16.2	11.1
Domestic Credit	15.3	12.7	15.9	11.7	15.4
Credit to the public sector	35.8	25.9	37.9	18.0	31.0
Credit to the private sector	10.6	9.7	10.9	10.2	11.0
Reserve money	**10.5**	**1.2**	**0.0**	**-2.0**	**6.0**
Money multiplier	4.93	5.46	5.07	5.14	5.11

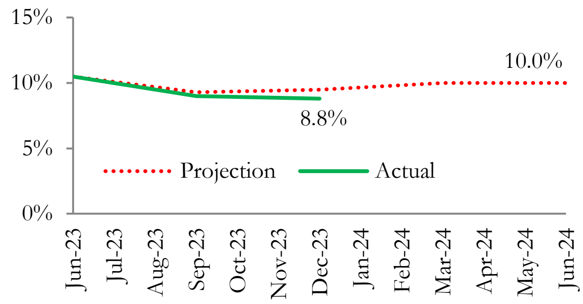
Source: Bangladesh Bank. *Calculated using the constant exchange rates of end June 2023. @ Announced in June 2023. P= Provisional

Chart 1: Reserve Money (RM) Growth



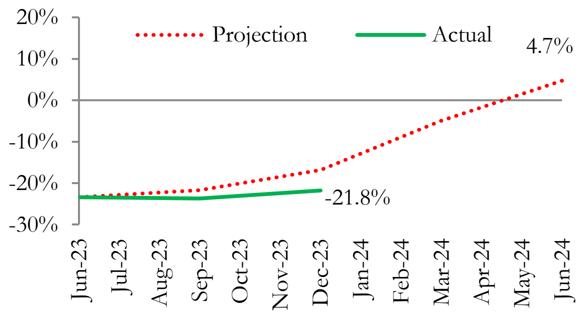
Source: Bangladesh Bank.

Chart 2: Broad Money (M2) Growth



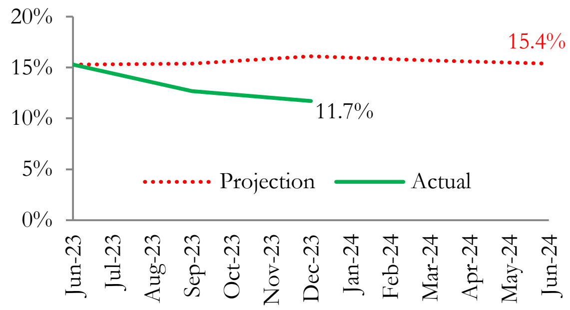
Source: Bangladesh Bank.

Chart 3: Net Foreign Assets (NFA) Growth



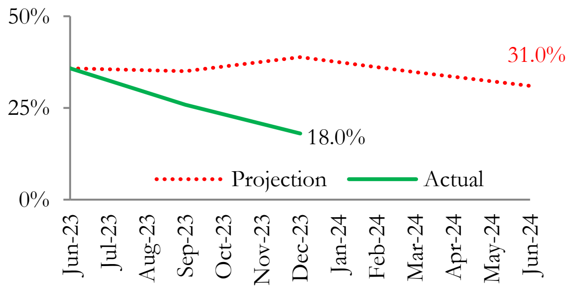
Source: Bangladesh Bank.

Chart 4: Domestic Credit Growth



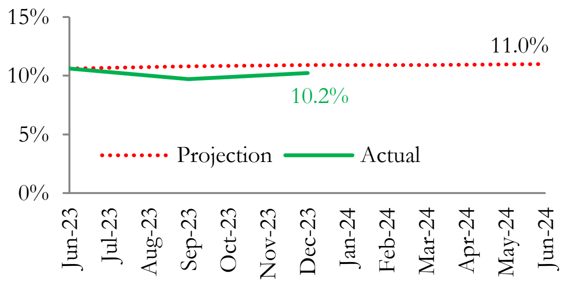
Source: Bangladesh Bank.

Chart 5: Public Sector Credit Growth



Source: Bangladesh Bank.

Chart 6: Private Sector Credit Growth

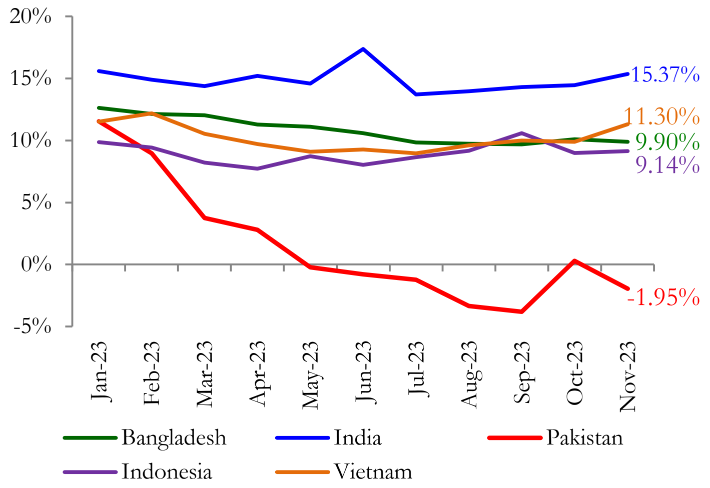


Source: Bangladesh Bank.

During H1FY24, private and public sector credit growth, indicative of the national investment landscape, displayed moderate trajectories. In December 2023, private sector credit expanded by 10.2 percent, slightly lower than the anticipated growth of 10.9 percent by December 2023 (Chart 6). This subdued growth might be attributed to reduced interest from private sector investors, stemming from higher borrowing costs, ongoing global and domestic economic uncertainties, liquidity constraints within the banking sector, and the pursuit of a contractionary monetary policy. Similarly, public sector credit grew 18.0 percent in December 2023, significantly lagging behind the projected growth of 37.9 percent for December 2023 (Chart 5). The noticeable decline in public sector credit growth within the banking system could be traced to diminished credit demand from the government, aligning with the government's selective spending on priority projects as part of austerity measures. Domestic credit movements remained under the projected trajectory for December of FY24, primarily due to sluggish private-sector credit growth coupled with lower expansion in public-sector credit (Chart 4).

However, from a cross-country perspective, Bangladesh's private sector credit growth, which is a critical indicator of private investment at the national level, exhibited a commendable performance compared to other emerging and developing Asian economies, except for India (Chart 7). This comparison underlines Bangladesh's relatively favorable trajectory of private sector credit growth, emphasizing its resilience and stability amidst the dynamics of the broader Asian economic landscape.

Chart 7: Cross-country Comparison of Private Sector Credit Growth



Source: Respective Central Banks' Websites.

Furthermore, large-scale manufacturing output, a key component of Gross Domestic Product (GDP), demonstrated robust growth, surging to 15.29 percent during July-September of FY24 compared to 6.24 percent in the corresponding period of the preceding fiscal year. This notable upswing in manufacturing output portrays a positive sign for the economy, suggesting a potential driver for GDP growth during this fiscal year.

During July-November of FY24, the outstanding value of NSCs witnessed a decline by Tk. 3,859 crore, a notable contrast to the Tk. 1616 crore decrease recorded during the same period in FY23. This decrease suggests that repayments exceeded sales, indicating a partial redemption of NSCs through alternative sources. However, net foreign financing totaled Tk. 12,218 crore during July-November of FY24, reflecting a decrease from Tk. 17,578 crore recorded in the corresponding period of the previous fiscal year.

3. Global and Local Contexts of Monetary Policy for H2FY24

3.1 Global Context: Growth, Inflation and Trade Environment

As per the IMF's most recent World Economic Outlook released in October 2023, the global GDP is forecasted to decline, dropping from 3.5 percent in 2022 to 3.0 percent in 2023 and further diminishing to 2.9 percent in 2024. It is anticipated that this trajectory will persist below the historical average of the last two decades. The GDP growth rate of advanced economies is expected to decelerate from 2.6 percent in 2022 to 1.5 percent in 2023 and 1.4 percent in 2024. This trend mirrors robust growth momentum in the United States but indicates a weaker-than-expected expansion in the euro area.
For emerging market and developing economies, a marginal slowdown from 4.1 percent in 2022 to 4.0 percent in both 2023 and 2024 is foreseen, primarily due to China's ongoing property sector crisis. However, in South Asia, Bangladesh and India are poised to maintain GDP growth rates surpassing 6.0 percent in 2023 and 2024, as indicated in Table 1.

Table 2: Overview of Global Economic Growth as of October 2023 WEO

(YoY % change)

Region	Growth				Difference from April 2023 WEO Projection	
	Actual		Projection			
	2021	2022	2023	2024	2023	2024
World	6.3	3.5	3.0	2.9	0.2	-0.1
Advanced Economies	5.6	2.6	1.5	1.4	0.2	0.0
USA	5.9	2.1	2.1	1.5	0.5	0.4
Euro Area	5.6	3.3	0.7	1.2	-0.1	-0.2
Other Advanced Economies	5.5	2.6	1.8	2.2	0.0	0.0
Emerging Market and Developing Economies	6.9	4.1	4.0	4.0	0.1	-0.2
China	8.4	3.0	5.0	4.2	-0.2	-0.3
Indonesia	3.7	5.3	5.0	5.0	0.0	-0.1
Vietnam	2.6	8.0	4.7	5.8	-1.1	-1.1
South Asia						
Bangladesh	6.9	7.1	6.0	6.0	0.5	-0.5
India	9.1	7.2	6.3	6.3	0.4	0.0
Pakistan	5.8	6.1	-0.5	2.5	-1.0	-1.0
Sri Lanka	3.5	-7.8	-	-	-	-

Source: World Economic Outlook, October 2023, International Monetary Fund.

The economic landscape in Asia and the Pacific region confronts various challenges, including shifts in global demand from goods to services, a transition from foreign sources to domestic manufacturers, and synchronized tightening of monetary policies. Despite the initial upward momentum in economic growth witnessed in the first half of 2023, the Asia-Pacific region is experiencing a slowdown. This deceleration is notably observed as China's post-pandemic reopening loses momentum due to subdued investment, partly influenced by weakened external demand.

Nevertheless, the region's economic activity, contributing significantly to approximately two-thirds of global growth in 2023, remains broadly on course. According to the Regional Economic Outlook for Asia and the Pacific released in October 2023, growth in the region is anticipated to reach 4.6 percent in

2023, surpassing the 3.9 percent growth seen in 2022. However, this growth trajectory is expected to ease to 4.2 percent in 2024.

Table 3: Global Inflation as of October 2023 WEO

Region	Actual		Projection		Difference from the April 2023 WEO update	
	2021	2022	2023	2024	2023	2024
World	4.7	8.7	6.9	5.8	-0.1	0.9
Advanced Economies	3.1	7.3	4.6	3.0	-0.1	0.4
Emerging Market and Developing Economies	5.9	9.8	8.5	7.8	-0.1	1.3

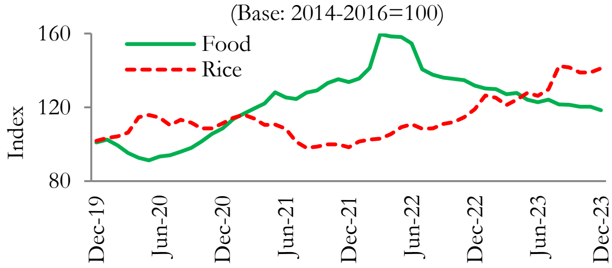
Source: World Economic Outlook, October 2023, International Monetary Fund.

Since mid-2022, global headline inflation has been gradually decreasing, primarily attributed to declining fuel and energy prices, along with the implementation of hawkish monetary policies in both advanced and emerging market economies. Projections indicate a decline in headline inflation from 8.7 percent in 2022 to 6.9 percent in 2023 and further down to 5.8 percent in 2024, as outlined in Table 3. However, these projected rates for 2023 and 2024 signal that inflation levels remain elevated compared to earlier forecasts.

Advanced economies are anticipated to experience a reduction in inflation, from 7.3 percent in 2022 to 4.6 percent in 2023, driven by decreased commodity prices and the impact of monetary policy tightening. Conversely, emerging market and developing economies may sustain relatively higher inflation rates, although a decline is projected from 9.8 percent in 2022 to 8.5 percent in 2023 and further to 7.8 percent in 2024. The pace of disinflation appears more noticeable in advanced economies, reflecting their robust monetary policy frameworks, effective communications, and lower susceptibility to shocks in commodity prices and exchange rates.

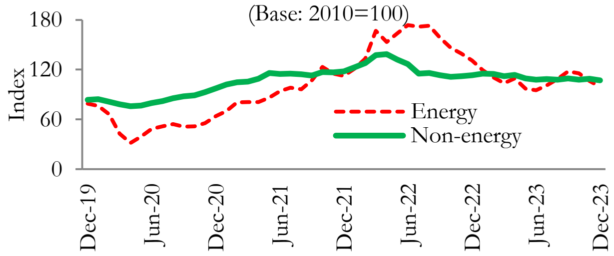
The IMF forecasts that inflation will likely surpass targets in most countries in 2024. However, it is anticipated to approach targets by 2025 as global commodity prices trend downward and oil prices decrease. Regarding price indices, the global food price index has shown a consistent decline since July 2022, except for the rice price index, which has been rising since early 2022 and continued with some fluctuations until November 2023 (Charts 8). The energy price index has followed a downward trajectory with occasional volatility in recent months. Conversely, the price index for non-energy commodities exhibited a relatively stable trend until November 2023 (Chart 9).

Chart 8: Global Food and Rice Price Indices
(Base: 2014-2016=100)



Source: Food and Agriculture Organisation.

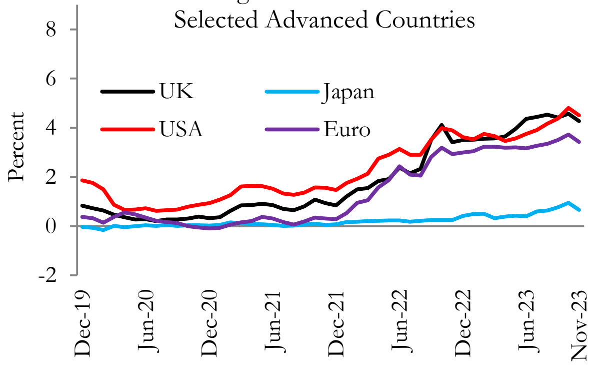
Chart 9: Commodity Price Indices
(Base: 2010=100)



Source: World Bank

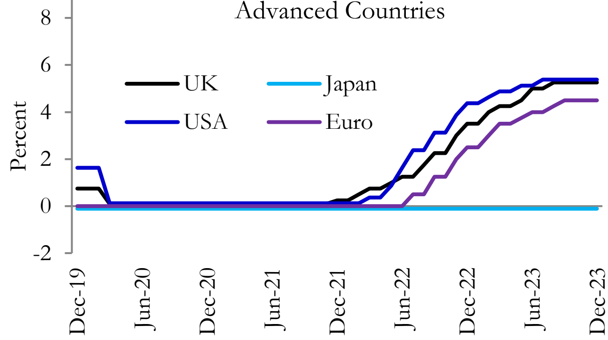
Following the aftermath of the pandemic, long-term interest rates have been consistently climbing in most advanced countries. This upward trend peaked in October 2023, indicating central banks' proactive measures towards tightening policies due to concerns about enduring inflationary pressures (Chart 10). Notably, the Bank of Japan increased the upper limit of the 10-year Japanese government bond from 0.5 percent to 1 percent, facilitating unlimited purchases to reinforce the sustainability of monetary easing. Conversely, countries like the US, UK, and Eurozone initiated policy rate hikes in early 2022, responding to the growing inflationary pressures (Chart 11). In comparison, among Bangladesh's peer countries, there exists a varied trend: India, Pakistan, and Indonesia have upheld elevated policy interest rates, while Vietnam and China recently experienced a slight decrease (Chart 12 & Chart 13).

Chart 10: Long-Term Interest Rates of Some Selected Advanced Countries



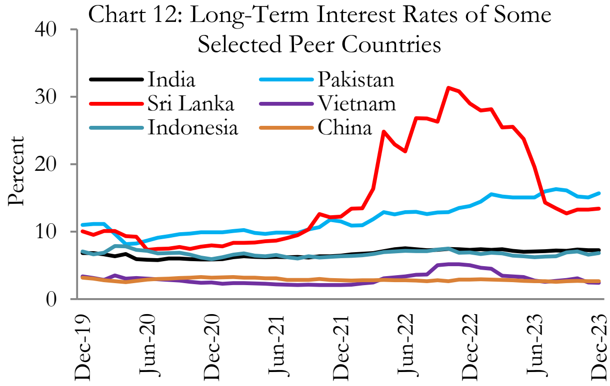
Source: Organization for Economic Co-operation and Development

Chart 11: Policy Rates of Some Selected Advanced Countries



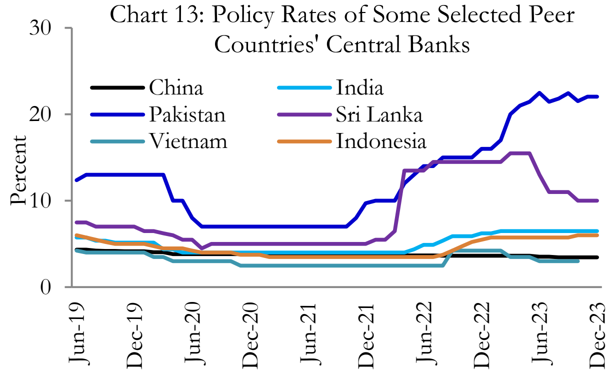
Source: Bank for International Settlements

Chart 12: Long-Term Interest Rates of Some Selected Peer Countries



Source: Organization for Economic Co-operation and Development

Chart 13: Policy Rates of Some Selected Peer Countries' Central Banks



Source: Bank for International Settlements

3.2 Local Context

3.2.1 Growth and Inflation

Bangladesh's economy has showcased robust resilience and impressive growth in recent years, achieving a real GDP growth of 6.94 percent in FY21 and 7.10 percent in FY22. This growth trajectory was underpinned by strong internal and external demand, complemented by growth-supportive monetary and fiscal policies. The post-pandemic recovery saw substantial progress, notably in the industrial and service sectors. In contrast, the agriculture sector made significant contributions with increased production, buoyed by favorable weather conditions and successful crop harvests. However, according to provisional estimates by BBS, the growth momentum slightly tapered off to 6.11 percent in FY23. This was amidst domestic price levels outpacing wage growth and persistent depreciation pressure on the Bangladesh Taka (BDT).

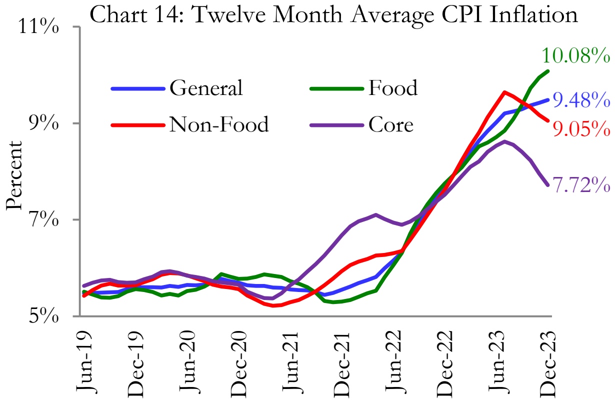
Projections indicate challenges ahead due to lower-than-expected growth forecasts for key trading partners and remittance sources, notably India, the Middle East, and the Euro Area. These could compound existing headwinds stemming from global macroeconomic uncertainties. Looking ahead to the remaining six months of FY24, substantial support from growing industrial output, steady services, agriculture sectors, and increased private demand is expected, along with positive impacts from major religious festivals in the latter half of the fiscal year.

Despite recent moderation in global commodity prices and stabilization in Russia-Ukraine war-related supply chain disruptions, concerns persist regarding price stability. Ongoing monetary tightening in major economies, coupled with global uncertainties and slower growth prospects, pose challenges to the global economic recovery. However, Bangladesh's economy anticipates support from resilient domestic demand, steady growth in Ready-Made Garments (RMG) exports, and consistent inflows of remittances from wage earners, bolstering its growth outlook. Projections suggest that the economy is poised to maintain a robust growth rate of around 6.5 percent in FY24, supported by both domestic and international agencies' forecasts alongside BB's in-house assessments.

The global trend of elevated prices has seen some moderation primarily attributed to improved supply conditions and stabilized food and energy prices (as depicted in Chart 8 and Chart 9). However, Bangladesh's economy has yet to experience an equal adjustment primarily due to domestic price rigidity, market imperfections marked by oligopolistic behaviors in certain commodities, and significant depreciation of the domestic currency, counteracting the potential advantages of reduced global prices.

In Bangladesh, Consumer Price Index (CPI)-based inflation surged notably, particularly following the subsequent upward adjustments in fuel and energy prices, during the first quarter of FY23. Chart 14 illustrates the 12-month average headline inflation trend alongside its components—food and non-food inflation—since June 2019. Starting from October 2021, there has been a steady escalation in the 12-month average CPI inflation, recording 6.15 percent at the end of FY22. The average headline inflation continued its ascent throughout FY23 and the initial half of FY24, culminating at 9.02 percent in June 2023 and further increasing to 9.48 percent by December 2023.

Chart 14: Twelve Month Average CPI Inflation



Source: Bangladesh Bureau of Statistics (BBS)

The inflexible nature of internal price adjustments, coupled with the persistent depreciation of the domestic currency, might impede a decline in domestic inflation despite recent reductions in international market prices. The inflationary strains and significant price surges observed in various essential goods during FY23 and the initial half of FY24 are likely to contribute to sustained inflationary expectations in the latter half of FY24. Elevated land and construction materials prices have driven up asset prices, further exacerbating inflation risk. While cost-push factors primarily influence inflation in Bangladesh, BB prioritizes measures to curb inflationary pressures. This includes the continuation of tighter monetary policies and strengthened interventions on the supply side, aligning with the objectives outlined in the national budget for FY24. It is anticipated that an improved supply-side scenario, coupled with a stringent monetary policy and support from fiscal measures, will result in a decline in the inflation rate, stabilizing it at an acceptable level by the conclusion of FY24.

BB's strategic policy initiatives to ease external sector pressures and establish a unified exchange rate regime under a crawling peg system aim to mitigate downward pressure on the Bangladesh Taka (BDT). This strategy seeks to minimize the pass-through effects of BDT depreciation and contain inflation throughout FY24. Additionally, the benefits stemming from BB's policy-tightening measures throughout the fiscal year are expected to play a pivotal role in curbing inflationary pressures. Considering these factors collectively, achieving the revised target of 7.50 percent inflation by the end of FY24 appears feasible.

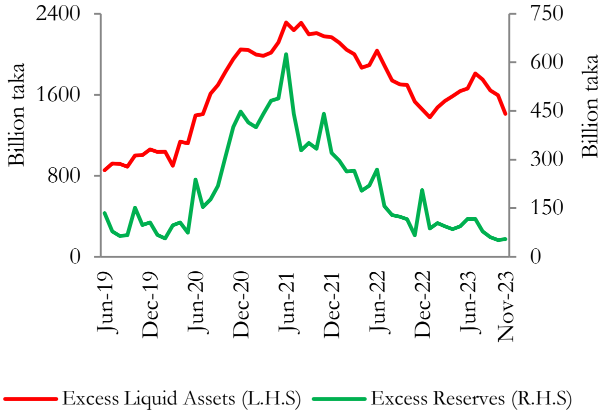
3.2.2 Liquidity and Interest Rate

Amidst a backdrop of monetary policies leaning towards contraction and consistent intervention in the foreign exchange market by BB, the banking sector in Bangladesh finds itself navigating through tight liquidity conditions. This strain is evident in the diminishing levels of excess cash reserves and liquid assets, as highlighted in Chart 15.

The effects of this contractionary stance became apparent as borrowing from banks became more expensive. Simultaneously, BB's active involvement in the foreign exchange market, involving substantial USD sales that absorbed a significant chunk of local currency liquidity, intensified the pressure on liquidity levels. Adding to this, a notably high currency-deposit ratio has further contributed to the tight liquidity scenario in the money market. The resulting dry liquidity situation within the banking sector has triggered a steady surge in interest rates across the board. The weighted average call money rate witnessed a striking ascent, climbing from 6.06 percent in June 2023 to 8.84 percent by December 2023, as depicted in Chart 16.

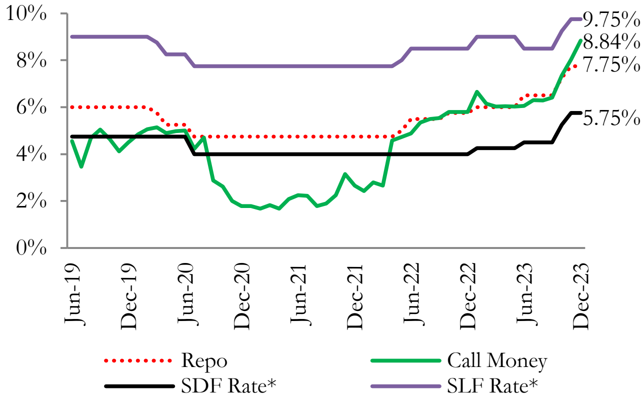
The movement observed in the call money rate aligns with BB's recent implementation of an interest rate corridor as part of its monetary policy statement. This initiative allows the interbank call money rate to fluctuate within the confines of the policy rate corridor, shaping the dynamics of lending and borrowing within the sector.

Chart 15: Movement of Excess Liquid Assets



Source: Bangladesh Bank

Chart 16: Movement of Call Money and Policy Rates



Source: Bangladesh Bank, * Before 01July 2023, SDF was Reverse Repo and SLF was Special Repo .

In its commitment to uphold liquidity stability within the financial sector, BB has been unwaveringly proactive in providing continuous support. BB has extended its assistance to conventional banks and non-bank financial institutions through various instruments, including repo facilities, assured liquidity support (ALS), and standing lending facilities. Recognizing the diverse landscape, BB has tailored its support, introducing Mudarabah Liquidity Support (MLS) and Islamic Banks Liquidity Facility (IBLF) explicitly aimed at Shariah-based Islamic banks. This specialized approach ensures comprehensive support across the banking spectrum.

Furthermore, BB's ongoing efforts extend to refinancing and pre-financing facilities tailored to foster growth in pivotal sectors like agriculture and CMSMEs (Cottage, Micro, Small, and Medium Enterprises). These strategic measures have a dual focus: fostering sufficient liquidity while concurrently nurturing employment opportunities and stimulating output-generating activities. Such initiatives underscore BB's proactive role in sustaining a dynamic and supportive financial environment in Bangladesh.

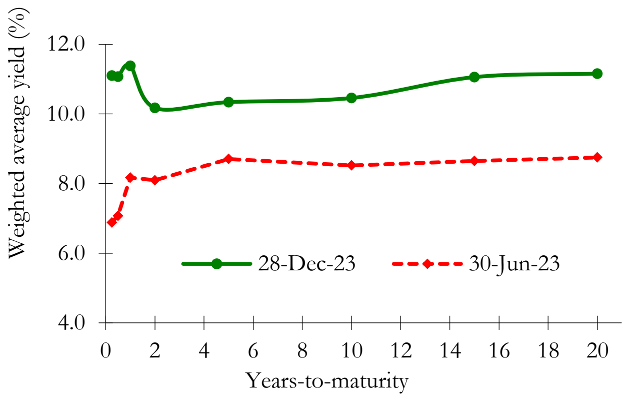
Table 4: Interest Rate Structure of the Banking Sector

Category	FY22 (Jun-22)	FY23 (Jun-23)	FY24 (Nov-23)
Advance Rate (%)			
Large Industries (Lowest-Highest)	3.06-8.80	3.22-9.00	3.88-10.81
Agricultural Credit (lowest-Highest)	3.71-8.48	3.04-8.43	4.85-9.98
SME (Lowest-Highest)	3.12-8.98	3.02-8.99	3.41-10.93
Deposit rate (%)			
Less than One year (Highest)	7.52	7.58	8.92
One year and above (Highest)	8.55	8.68	9.07

Source: Banking Statistics Division, Statistics Department
Note-1: For advance, Weighted Average Interest Rates below 3% are excluded, considering loans disbursed under different schemes (eg-EDF, Refinance)
Note-2: For deposits, lower interest rates are provided mainly by foreign banks

Given the constrained liquidity scenario in the local currency market, there have been discernible upticks in the interest rates of various financial products, notably in weighted average nominal lending and deposit rates, as well as interest rates on short and long-term government securities (as illustrated in Table 4 and Chart 17). The weighted average nominal lending rate experienced a noticeable climb, surging from 7.31 percent in June 2023 to 7.99 percent by November 2023. Similarly, the weighted average nominal deposit rate demonstrated an upward shift, reaching 4.64 percent in November 2023 from 4.38 percent in June 2023.

Chart 17: Yields on Government Securities



Source: Bangladesh Bank

In July 2023, the implementation of SMART as a benchmark for banks' lending rates marked a significant shift. This benchmark rate surged from 7.10 percent in July 2023 to 8.14 percent by December 2023. This surge can be attributed to increased government borrowings from commercial banks via T-bills and T-bonds, accompanied by the discontinuation of devolvement amidst BB's observed contractionary policy stance. It's important to note that there has been a recent uptick in the margin added to the reference rate, determining the maximum lending rate.

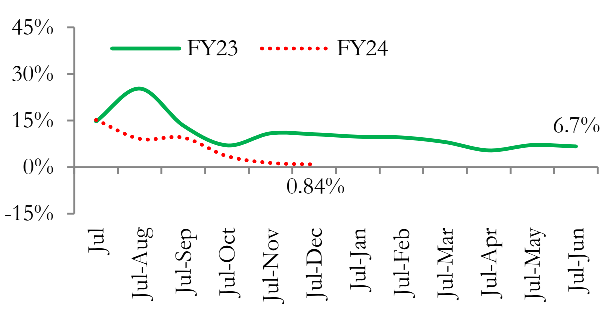
BB's recent initiatives, embracing a hawkish monetary policy stance, transitioning towards an interest rate targeting framework, and introducing competitive reference interest rates, are expected to influence real interest rates pivotally. The concerted effort aims to steer these rates into positive territory by mitigating inflationary pressures and elevating nominal interest rates.

3.3. Overview of External Sector Developments and Outlook

Bangladesh's external sector has grappled with significant challenges since late FY22. These challenges have emerged from heightened pressure on the balance of payments (BoP), declining foreign exchange reserves, noticeable currency depreciation, and global monetary tightening. These complexities have been further compounded by elevated global economic uncertainties stemming from ongoing geoeconomic tensions and geopolitical conflicts. However, a significant and positive shift was observed in the current account balance (CAB) from July to October 2023. This transformation—from a substantial deficit to a surplus—was primarily propelled by resilient exports, vigilant control over import prices, currency depreciation, and consistent inflows of remittances. Despite these encouraging advancements, an unprecedented deficit persisted in the financial account, contributing to an overall deficit in the BoP.

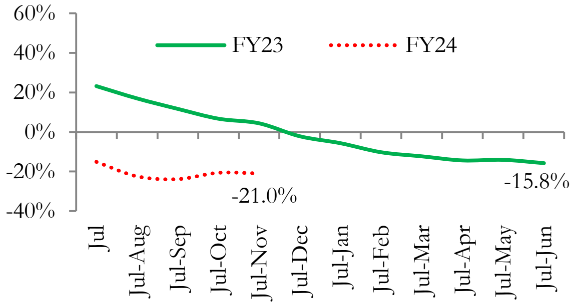
Amidst global uncertainties and tightening monetary policies in advanced economies, Bangladesh's exports showcased resilience, marking a moderate growth of 1.30 percent to USD 22.23 billion during July-November 2023 (as depicted in Chart 18). While the global economic landscape faced challenges, the country's export growth, predominantly led by the ready-made garments (RMG) sector accounting for 85 percent of total exports, exhibited a 2.75 percent surge during this period. Although recent data indicates a slight moderation, with overall export growth at 0.84 percent during July-December 2023, compared to a higher growth of 10.58 percent in the same period of FY23, Bangladesh's export sector continues to demonstrate resilience and stability amidst evolving global conditions.

Chart 18: Cumulative Exports Growth



Source: Export Promotion Bureau

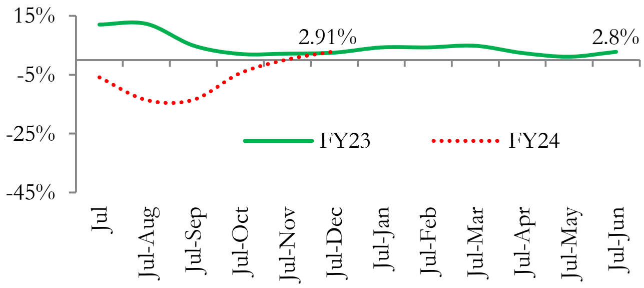
Chart 19: Cumulative Imports Growth



Source: National Board of Revenue

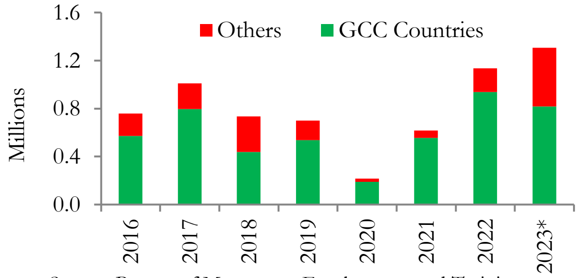
The import landscape underwent a remarkable shift, marking a substantial decline of 21.02 percent to USD 27.76 billion (c&f) during July-November 2023. This dip, fueled by multiple catalysts like falling global commodity prices, strategic policies discouraging less-essential and luxurious imports, vigilant monitoring of import prices, domestic interest rate hikes, and BDT depreciation, starkly contrasts the 4.35 percent increase seen in the same period of the previous fiscal year (Chart 19). This import decline and consistent export growth reshaped the trade scenario, slashing the trade deficit to USD 4.76 billion during July-November 2023 from a hefty USD 11.82 billion in the same period of the previous fiscal year. Despite rising service and primary income deficits, sound remittance inflows flipped the current account into a surplus of USD 579 million, a stark reversal from the USD 4.49 billion deficit recorded in the same FY23 period. The wage earners remittances have seen a 2.91 percent growth during July-December 2023, aided by various policy support measures and a substantial BDT depreciation. Moreover, the robust 40.46 percent growth in overseas employment during July-November 2023 hints at a promising trajectory for future remittance inflows.

Chart 20: Cumulative Remittance Growth



Source: Bangladesh Bank

Chart 21: Overseas Employment



Source: Bureau of Manpower, Employment and Training.
* Up to December 2023.

Despite a current account surplus, the pressure on the Balance of Payments (BoP) persisted, notably as the financial account transitioned into a deficit of USD 5.40 billion during July-November 2023, in contrast to a surplus of USD 1.26 billion in the same period of the previous year. This shift towards a financial account deficit stemmed primarily from several factors, including a slowdown in private foreign borrowings amid global interest rate hikes and economic uncertainties. Additionally, this deficit contributed to faster repayment of short-term private foreign borrowings, intended to avoid additional costs linked to rising base interest rates. Moreover, a significant trade credit deficit emerged due to delayed repatriation of certain export earnings. The overall balance of the BoP depicted a deficit of USD 4.90 billion during July-November 2023, compared to a deficit of USD 6.00 billion in the corresponding period of the previous fiscal year. This underscores the complex dynamics at play, with efforts needed to address the nuanced challenges in the financial account.

Table 5: Balance of Payments Highlights

(Million USD)

Major Items	FY22 Actual	FY23 Actual	FY24 Projection
Trade balance	-33,250	-17,163	-10,197
Services	-3,987	-4,384	-7,275
Primary income	-2,726	-3,407	-5,617
Secondary income	21,767	22,289	22,756
of which: workers' remittances	21,032	21,611	22,043
Current account balance	**-18,196**	**-2,665**	**-332**
Capital accounts	610	475	150
Financial accounts	**16,691**	**-2,078**	**200**
Errors and omissions	-5,761	-3,954	-622
Overall balance	**-6,656**	**-8,222**	**-604**
Memorandum items:			
Exports growth (adjusted as per BPM6, percent)	33.4	6.3	4.0
Imports growth (percent)	35.9	-15.8	-7.0
Remittances growth (percent)	-15.1	2.8	2.0
Gross international reserves (GIR)	41,827	31,203	29,000

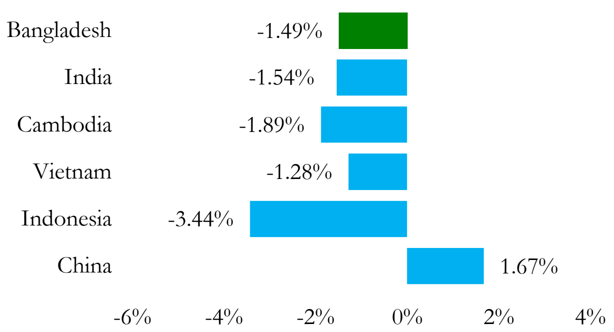
Source: Bangladesh Bank

Looking ahead, there's an optimistic outlook for easing pressure on the Balance of Payments (BoP) in the remainder of FY24. Foreseeably, a manageable Current Account Balance (CAB) and anticipated improvements in the financial account are expected to play a pivotal role. The ongoing trend of reduced imports, evident in declining fresh LC openings and anticipated enhancements in remittance inflows, signifies a promising trajectory for the current account in FY24. Moreover, efforts to mitigate the deficit in the financial account are expected to yield positive results, with potential reductions in trade credit deficits, a slower pace of short-term external borrowing repayments, and increased inflows of FDI, ODA, and PFI. Overall, this expected shift hints at a more balanced and resilient BoP scenario in the upcoming months of FY24.

3.4. Movements of Exchange Rate and Foreign Exchange Reserve

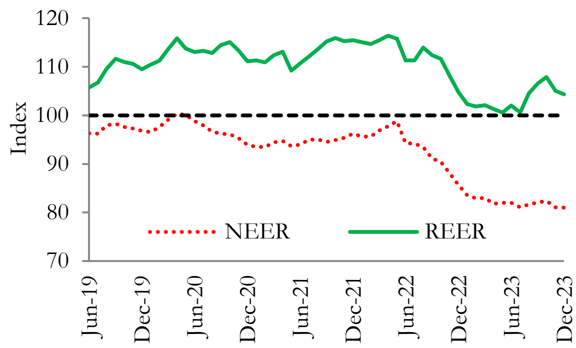
The Balance of Payments (BoP) encountered a substantial deficit, compounded by tightened monetary conditions in major advanced economies and escalating geopolitical tensions. These factors collectively exerted significant downward pressure on the Bangladesh Taka (BDT). To mitigate disruptive fluctuations in the foreign exchange market, the Bangladesh Bank (BB) opted for a gradual approach, allowing market forces to determine the exchange rate. Simultaneously, BB intervened in the foreign exchange market through net sales. During July-December 2023, BB's net sale of foreign currency amounted to USD 5.69 billion, contributing to a decline in the nation's foreign exchange reserves. By 31 December 2023, the gross official foreign exchange reserves decreased to USD 21.87 billion (BPM6) from the previous USD 24.75 billion recorded at the end of June 2023. In a strategic move, BB has already initiated the unification of exchange rates, adopting the prevailing interbank exchange rate announced by the Bangladesh Foreign Exchange Dealers' Association (BAFEDA) for foreign exchange transactions.

Chart 22: App(+)/Dep(-) of Domestic Currency against USD during July- December 23



Sources: Respective Central Banks' Websites.

Chart 23: Effective Exchange Rate Indices (Base: 2015-16=100)



Source: Bangladesh Bank

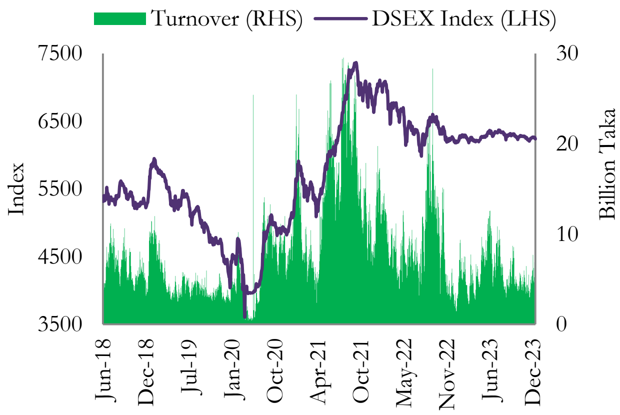
Amid sustained Balance of Payments (BoP) deficits, notable adjustments were witnessed in the exchange rate of the Bangladesh Taka (BDT) against the US Dollar (USD) in FY23, reflecting a depreciation of 13.8 percent. Subsequently, in July-December 2023, the BDT experienced an additional depreciation of 1.49 percent against the USD, reaching Tk. 110.00/USD at the end of December 2023 from Tk. 108.36/USD at the end of June 2023. Chart 22 provides an overview of the exchange rate adjustments, showcasing the movement of domestic currencies against the USD across various countries. Moreover, despite a remarkable decrease in the Nominal Effective Exchange Rate (NEER) index, the Real Effective Exchange Rate (REER) indicated an appreciation of 3.71 percent during July-December 2023. The REER index reached approximately 104, primarily due to higher inflation rates in Bangladesh compared to its trade partners (as depicted in Chart 23). This suggests an inclination toward the current Bangladesh Taka (BDT) being somewhat overvalued against the US Dollar (USD). However, this condition is expected to improve with an anticipated reduction in Bangladesh's relative price indices to its trading partners.

To mitigate exchange rate instability and allow more flexibility, BB plans to implement a crawling peg system with a specified band based on a basket of currencies as an interim measure before transitioning towards a free-floating exchange rate regime. These measures are part of BB's proactive steps to ensure stability and resilience in the foreign exchange market, fostering confidence and adaptability amid challenging global economic dynamics.

3.5 Capital Market

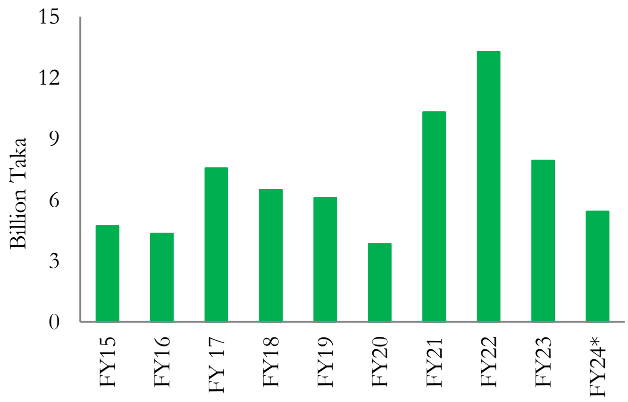
In the first half of FY24, Bangladesh's capital market underwent notable fluctuations mainly due to economic challenges, including high inflation, exchange rate pressures, and economic uncertainties at home and abroad.

Chart 24: DSEX Index and Turnover



Source: Dhaka Stock Exchange

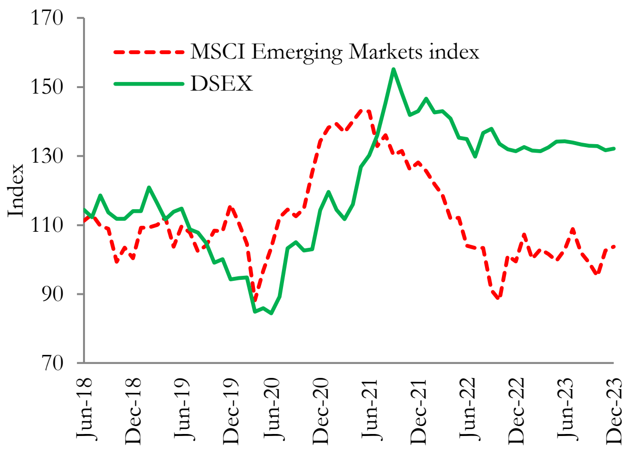
Chart 25: DSE Daily AverageTurnover



Source: Dhaka Stock Exchange * Up to 26 December 2023

The DSEX, serving as the benchmark index of the stock market, experienced a slight increase of 0.64 percent, settling at 6,246.50 points at the end of December 2023 compared to 6,206.81 points at the end of December 2022. However, between June 2023 and December 2023, the DSEX index witnessed a modest decline of 1.5 percent (Chart 24). The crucial indicator of capital market liquidity, the daily average turnover, notably dropped by 44.80 percent, down to BDT 543 crore by the end of December 2023 from BDT 983 crore in December 2022 (Chart 25). This decline in turnover volume during the first half of FY24 is attributed to investors' cautious approach. Notably, the insurance sector dominated with the highest turnover share at 25.4 percent during H1FY24, up to October 2023. Additionally, the DSE market capitalization marginally increased, reaching BDT 7,80,849 crore by the end of December 2023 compared to BDT 7,72,078 crore as of June 2022.

Chart 26: Synchronization of DSE with Global Markets
(Base: Jan 2015=100)



Sources: Dhaka Stock Exchange and www.msci.com

4. Recent Policy Review

4.1 Exchange Rate Stability

Bangladesh Bank (BB) has been actively pursuing exchange rate stability amid increasing pressures on the exchange rate since mid-2022. To counteract this trend, BB has implemented various measures. Besides allowing a significant depreciation of the Bangladesh Taka (BDT) and infusing a substantial amount of foreign exchange into the local market, BB has made concerted efforts to augment inflows and curtail unnecessary outflows of foreign exchange, aiming to stabilize the foreign exchange market.

BB has introduced several policy initiatives to encourage individuals and investors to retain their foreign currencies in banks and utilize formal channels for remitting their foreign exchange earnings. Notably, BB has permitted domestic commercial banks' offshore banking operations (OBOs) to offer an interest/profit rate markup over a benchmark rate for term deposits in foreign currency to eligible customers, including individuals and entities residing outside Bangladesh, non-resident Bangladeshi nationals, persons of Bangladeshi origin, foreign nationals, companies/firms registered and operating abroad, and foreign institutional investors.

BB has expanded its scope and authorized all approved foreign exchange dealers in Bangladesh to open and maintain Resident Foreign Currency Deposit (RFCD) accounts for resident Bangladeshis who return from foreign travel with foreign currency. Unlike the previous restriction on specific currencies, these accounts now accept deposits in any approved foreign currency. These accounts offer a 1.5 percent interest or profit markup over the benchmark rate of respective currencies for deposits held for at least one month. Account holders also have the provision of international cards, including a maximum of two supplementary international cards (debit/credit/prepaid) for their dependents, and the flexibility to convert balances into Taka as needed.

BB has introduced measures to boost foreign direct investment (FDI) by allowing AD banks to open temporary foreign currency accounts with a one-year tenure in the name of foreign investors' proposed companies from their opening dates. Foreign currency can be retained in these temporary accounts and used for outward payments for capital expenditure or converted into Taka. These accounts are expected to attract more foreign investors, as they can retain funds in foreign currency accounts for one year, allowing flexibility in managing capital.

Moreover, BB has revised the foreign currency retention limits for exporters maintaining foreign currency accounts with shipment proceeds. Effective 24 September 2023, the new retention limits from realized export proceeds—Exporter Retention Quota (ERQ)—stand at 7.5 percent, 30 percent, and 35 percent for different categories. These revised limits mark a decrease from the previous percentages of 15 percent, 60 percent, and 70 percent, respectively, aiming to boost foreign currency liquidity in the foreign exchange market. Also, BB has extended the facility of borrowing from offshore banking operations (OBOs) by domestic banking units (DBUs) till 30 June 2024 to continue the flexibility for external transactions. DBUs may receive funds from any OBOs up to 40 percent of their regulatory capital to settle permissible payment obligations.

BB has intensified its oversight of import prices to enhance transparency and regulate foreign currency utilization in import-related transactions. The focus is verifying whether these prices align with the costs of goods/commodities in the country of origin and international markets, aiming to curb over-invoicing practices. BB allowed the retention facility of the value-added portion for 30 days for exporters and eligible local suppliers engaged in producing goods against bulk imports and local content to meet their subsequent foreign currency requirements. This facility extends to local suppliers producing intermediate goods through the Back-to-Back Letter of Credit (BBLC) by importing input contents. Exporters can use their retention facility for LC payments to other banks within 30 days, and any remaining unused value-added portions can be encashed after this period.

In efforts to bring order to the foreign exchange market, BB has directed banks to apply prevailing exchange rates for encashment, preventing exporters from taking advantage of higher rates due to delayed encashment. Furthermore, BB has imposed limits for Ads to apply forward premiums, capping them at SMART plus 5 percent per annum with declared spot rates, facilitating forward sales for import payments only for a maximum of 3 (three) months. Also, BB specified that the premium must be adjusted according to the actual duration for early settlement of the forward contract. Given the global context of the discontinuation of LIBOR and the upward trend of the interest rate, BB revised the pricing terms of USD and EURO financing for eligible borrowers under the Green Transformation Fund (GTF) and fixed the rate at 5 percent per annum effective from 1 July 2023. Additional measures have been implemented to reduce foreign currency cash holdings by money changers and to combat illegal money changers and Mobile Financial Service (MFS) providers, aiming to mitigate unauthorized transactions and activities associated with hundi.

4.2 Foreign Exchange Reserve

Bangladesh's foreign exchange reserves have faced significant challenges recently due to various external sector pressures. These pressures include a range of factors, such as increased trade deficits with heightened demand for imports, fluctuations in global commodity prices, a surge in import payments, and widened financial account deficit amid economic uncertainties in the global market. The country's foreign exchange reserves are crucial as they buffer against external shocks, help maintain stability in the currency exchange rate, and support international trade and payment obligations. Maintaining adequate foreign exchange reserves is vital due to its reliance on imports for various commodities, including fuel, essential goods, and raw materials for industries like textiles and garments. Moreover, global economic fluctuations, geopolitical tensions, and other external uncertainties can impact remittance inflows, export revenues, and foreign investment, further affecting the stability of foreign exchange reserves.

Bangladesh has been actively managing these challenges with strategic foresight. Although under strain, the reserves remain a crucial safeguard against external shocks. They play a pivotal role in ensuring stability in currency exchange rates, supporting international trade, and fulfilling payment obligations. Efforts to diversify export markets, enhance export competitiveness, attract more remittances and foreign investments, and strengthen trade balances can stabilize and bolster the country's foreign exchange reserves.

With a series of demand management strategies and supply-side interventions implemented by BB, there has been a remarkable improvement in mitigating the current account deficit, providing much-needed relief in reserve management. Despite this progress, the growing deficit in the financial account of the BoP presents challenges in stabilizing foreign exchange reserves. However, the recent disbursement of loans by several development partners has contributed positively to rebuilding the foreign exchange reserves.

As of 31 December 2023, total international reserves were USD 27.13 billion, which amounted to USD 21.87 billion as per BPM6 excluding other foreign currency assets like the export development fund (EDF). This reserve covers 4 (four) months of imports equivalent, exceeding the internationally recognized benchmark level by one month. This reflects a rise from the USD 19.30 billion reported at the end of November 2023 but contrasts with the USD 24.75 billion recorded at the end of June 2023.

4.3 Enhancing the Remittance Inflows

Enhancing workers' remittances goes beyond merely improving the current account balance and strengthening international reserves; it plays a pivotal role in driving the rural economy of Bangladesh. The government and the Bangladesh Bank have implemented comprehensive policy measures to amplify the influx of remittances. These encompass the following noteworthy initiatives:

a) **Dual Incentive Scheme**: In addition to the existing 2.5 percent incentives provided by the government, banks now offer an additional incentive (up to 2.5 percent) on the market-determined exchange rate for any amount transferred as remittances through official channels.

b) **Increased Remittance Limits**: The maximum limit for remittances to individual Mobile Financial Service (MFS) accounts has been doubled, rising from Taka 1,25,000.00 (including incentives) to Taka 2,50,000.00 (excluding incentives) to liberalize the remittance transfer.

c) **Expanded Remittance Channels**: BB has granted licensed Payment Service Providers (PSPs) the authority to repatriate wage earners' remittances, extending the remittance landscape beyond banks and mobile financial services. These PSPs establish arrangements with foreign counterparts to receive foreign currency, ultimately crediting the equivalent Taka value to the wage earners' PSP accounts.

d) **Streamlined Banking Regulations**: Local banks are no longer required to obtain prior permission from BB to establish drawing arrangements with foreign exchange houses. This regulatory streamlining aims to improve the efficiency of remittance services.

e) **Efficient Remittance Disbursement**: BB has issued instructions to banks, mandating remittance disbursement to beneficiaries within two days without imposing additional fees. This directive aims to streamline the process, making it easy, hassle-free, time-efficient, and cost-effective for recipients.

f) **Fair Pricing for Remittances**: BB is actively working to ensure that wage earners who remit their hard-earned foreign income receive a fair price, underlining their commitment to safeguarding the interests of remitters.

g) **Promotion of Official Channels**: Foreign embassies of Bangladesh annually celebrate the 'International Day of Family Remittances (IDFR)' to raise awareness among wage earner remitters about the advantages of transferring their remittances through official channels.

h) **Combating Unofficial Channels**: Collaborative efforts involving the Bangladesh Financial Intelligence Unit (BFIU) and other law enforcement agencies are underway to identify individuals engaged in Hundi activities and curb unofficial remittance channels.

i) **'PROBASH' Pension Scheme**: The government introduced a special pension scheme named 'PROBASH' for expatriate Bangladeshis as part of the recently introduced universal pension scheme. This initiative serves as an incentive for inward remittance and long-term financial security for expatriates.

j) **Tax remission on IT freelancers:** BB clarified that freelancers do not have to pay tax at source on remittance from IT freelancing jobs.

These multifaceted initiatives reflect a proactive approach, highlighting the determination to harness the full potential of inward remittances. They support foreign exchange reserves and contribute significantly to economic growth and development. As we look ahead, the Bangladesh Bank remains unwavering in its commitment to creating a conducive environment that further enhances remittance inflows and benefits the nation and its hardworking expatriate community.

4.4 Anchoring Inflation

Focusing on curbing inflation, BB has implemented crucial strategies to stabilize the economy. To address demand-side pressures, BB increased the overnight policy rate to 7.75 percent, ceasing lending to the government, and conducted US dollar sales, tightening liquidity in local markets. Additionally, initiatives to ease supply-side constraints involve funding schemes for pivotal sectors like agriculture, CMSMEs, and import-substituting industries. Transitioning to an interest rate targeting framework on 1 July 2023, BB introduced an Interest Rate Corridor (IRC), stepping away from the previous reserve money targeting. BB has enacted measures to contain unnecessary forex outflows and crack down on invoicing inconsistencies to counter inflation from exchange rate fluctuations. Necessary policy measures that are taken to control inflation are highlighted below:

Increasing Policy Rate: BB gradually adjusted the policy rate upward by 175 basis points (bps) from 6.00 percent to 7.75 percent, with a standing lending facility rate of 9.75 percent during July-December 2023. This move was designed to elevate borrowing costs, thus curbing excessive monetary expansion. The standing deposit facility rate, mirrored by the reverse repo rate, also rose from 4.50 percent to 5.75 percent, in line with the policy rate adjustment.

Removing Remaining Lending Restrictions: BB introduced the 'Six Months Moving Average Rate of Treasury Bill (SMART)' as a reference lending rate. Starting in July 2023 with an added margin of 300 basis points (bps) for banks' lending, this margin subsequently increased by 75 bps in two stages. The intention behind this adjustment was to enhance credit allocation efficiency in the banking sector, fostering a conducive lending environment for both businesses and individuals.

Removing Deposit Rate Floor: In tandem with the new policy framework, BB eliminated the interest rate floor on deposits. This step aimed to facilitate a more efficient transmission of the policy rate and encourage higher real interest rates for the public, thus aiding effective demand management to control inflation.

Quantitative Tightening: BB addressed external sector pressures by mitigating potential inflation risks due to the steep depreciation of the BDT. BB effectively managed likely inflationary pressures stemming from the demand side by withdrawing local currency from the market through the net infusion of approximately USD 5.0 billion into the local market during July-December 2023 of the current fiscal year.

Exchange Rate Unification: Bangladesh Bank diligently implemented a unified and market-driven exchange rate regime to tackle challenges posed by external factors. This initiative aimed to enhance stability in the exchange rate, thereby contributing to improved inflation management. The unified market-driven exchange rate regime prioritizes transparency and efficiency in foreign exchange transactions, aligning with economic growth goals and trade facilitation while maintaining stability in the BDT-USD exchange rate.

Halting the Devolvement Process of Lending to the Government: BB ceased lending to the government through devolvement, a practice known to have a multiplier effect on money supply and, thereby, inflation. This measure was instituted to rein in inflationary pressures.

Sector-focused funding initiatives: Various projects and schemes were continued by BB to ensure adequate funding to vital sectors such as agriculture, Cottage, Micro, Small, and Medium Enterprises

(CMSMEs), and industries focused on import substitution. These efforts aimed to alleviate supply-side constraints contributing to inflation.

Guided by the above range of tactical policy interventions, the proactive measures undertaken by BB are positioned to influence addressing inflationary pressures in the near term substantially. The orchestrated steps encompassing interest rate modifications, regulatory changes in lending and deposit systems, strategic quantitative tightening, unified exchange rate strategies, and prudent lending policies are expected to be pivotal in steering the economy toward stability and effectively anchoring inflation.

4.5 Financial Sector Stability

Ensuring sound governance and transparency in the banking sector is critical for fostering a robust and resilient financial system. Recent milestones in the latter half of 2023, notably the Bank Company (Amended) Act of 2023 and the introduction of the Financial Company Act of 2023 signal a concerted effort to fortify discipline and stability within a dynamically evolving regulatory financial landscape. Bangladesh Bank has embarked on significant initiatives to enhance financial inclusivity, digital transformation, and sustainable finance within the banking industry. Moreover, BB has implemented regulatory measures addressing legal compliance in loan recovery and streamlined supervisory requirements for financial sector oversight.

In a proactive endeavor to fortify supervision over commercial banks and NBFIs, BB has curated a roster of accredited Chartered Accountant Firms, mandating banks and NBFIs to appoint these firms for various regulatory audits, risk assessments, and internal control systems. Concurrently, BB has charted a roadmap for the banking sector's adoption of IFRS9, setting an example by publishing its financial statements compliant with IFRS.

BB has modernized its sustainable finance policy to advance green banking and climate-conscious finance, encompassing a revised spectrum of green products, including gender-focused initiatives and adherence to environmental regulations and climate strategies. Financial institutions will undergo sustainability ratings, and BB plans to publish a roster of top-rated institutions on its website annually.

BB's core ambition of augmenting financial depth is underscored by pursuing a higher M2/GDP ratio, signifying an advanced and resilient financial landscape akin to peer nations. Initiatives encompassing financial inclusion, digitalization, eco-friendly financing, and diversification into long-term financial instruments like bonds and stocks are pivotal in this pursuit. Additionally, BB's authorization of bancassurance, commencing on 12 December 2023, enables commercial banks to act as corporate agents of insurance companies, leveraging their extensive networks to augment insurance penetration in Bangladesh. This move aims to bolster confidence and increase insurance participation among consumers.

This holistic approach by Bangladesh Bank, encapsulating regulatory advancements, sustainable finance reforms, and strategic directives, not only underlines its commitment to strengthening the banking sector but also underscores its dedication to fostering a resilient and inclusive financial landscape. These proactive measures are poised to pave the way for Bangladesh's financial ecosystem's robust and sustainable future, ensuring stability, growth, and accessibility for all stakeholders involved.

4.6 Enhancing Financial Inclusion and Cashless Society

Over the past decade, Bangladesh has made remarkable progress in fostering financial inclusion through mobile financial services (MFS), agent, sub-branch, and branchless banking, providing formal financial avenues to the unbanked and micro-entrepreneurs. The interoperability among MFS providers has significantly driven the growth of digital payments, propelling the nation's journey toward greater financial inclusion. In line with the government's 'Smart Bangladesh Vision,' Bangladesh Bank has initiated the 'Cashless Bangladesh' program to accomplish seventy-five percent cashless transactions by 2027. Initiatives like Binimoy, QR Code transactions, Digital Bank, and TakaPay have been introduced to integrate the unbanked and marginalized population into the formal banking system.

The evolution of MFS has expanded its scope beyond basic transactions to encompass a comprehensive range of services, including savings, loans, insurance, and remittances. This expansion has empowered individuals and small businesses, significantly contributing to poverty reduction and economic empowerment. BB's decision to permit individuals aged 14-18 to open MFS accounts aims to integrate more users into the regulated payment systems. Additionally, the collaboration between MFS providers and the Universal Pension Scheme (UPS), charging a unified service fee of BDT 0.7 for every BDT 100 deposit, showcases BB's commitment to expanding financial access.

On 16 July 2023, BB augmented the revolving refinance fund for 'digital microcredit' from BDT 100 crore to BDT 500 crore, extending financial inclusion to marginalized individuals in digital transactions. BB provides this fund at a 1.0 percent interest rate to banks, enabling digital modes like Internet banking, mobile apps, mobile financial services, and e-wallets for the marginalized population.

The introduction of the 'TakaPay' national card scheme on 1 November 2023 is a significant leap towards a cashless society. Collaborating with selected banks such as Brac Bank PLC, The City Bank Ltd, and Sonali Bank PLC, the TakaPay card aims to facilitate secure local payments through the National Payment Switch, reducing reliance on international card networks and foreign exchange expenses.

The introduction of digital banks approved on 22 October 2023 signifies a transformative shift in the banking industry. These banks facilitated through mobile apps and online banking, eliminating traditional paperwork and aligning operations with regulatory frameworks, contributing to the momentum of a cashless payment system.

The 'Bangla QR' code, launched on 6 January 2021 and enhanced on 18 January 2023, is a collaborative effort between banks, mobile financial services, and international payment gateways, fostering an inclusive and convenient digital payment landscape. Additionally, BB's measures to ease the opening of 'Individual Retail Accounts' with minimal documentation benefit micro-entrepreneurs, traders, and service providers. Contactless payment systems using near-field communication-enabled cards streamline transactions, enhancing user convenience, operational efficiency, and security.

The launch of the Interoperable Digital Transactions Platform (IDTP), 'Binimay,' on 13 November 2022, links various payment system partners, providing customers unified access to multiple digital payment services through a single interface. BB's Guidelines for Merchant Acquiring and Escrow Services, introduced on 26 September 2023, enhance consumer protection in the e-commerce sector, encouraging the adoption of digital payment methods by online retailers. These initiatives signify Bangladesh's steadfast commitment to embracing a digital future and fostering financial inclusion for all.

4.7 Strengthening Capital Market

Bangladesh's capital market regulatory body, the Bangladesh Securities Exchange Commission (BSEC), in collaboration with the Bangladesh Bank (BB) and other relevant government entities, has consistently spearheaded initiatives to foster a robust capital and bond market within the country. The government's ongoing mega projects and private investments in energy, power, and transportation sectors have underscored the necessity for a well-developed capital market.

In a concerted effort, BB, BSEC, and the Central Depository Bangladesh Limited (CDBL) jointly introduced secondary trading of government treasury bonds in the capital market in October 2022. This move received an overwhelmingly positive response from investors. Presently, 238 treasury bonds are actively traded in the capital market, and several other bonds are in the pipeline for listing. Additionally, on 4 December 2023, BB released guidelines for the mark-to-market-based revaluation of treasury bills and bonds held by banks, aiming to establish an efficient secondary market for government securities.

Moreover, Islamic Shariah-compliant 'Sukuk' bonds have become a regular trading instrument in the capital market, offering investment opportunities for Shariah-compliant banks, financial institutions, companies, and Islamic branches and windows of conventional banks. Collaborative efforts between the government of Bangladesh, BB, and the International Finance Corporation (IFC) are ongoing to develop a local currency bond market.

To overcome prevailing economic challenges, BB has taken several key initiatives to invigorate the capital and bond market. Notably, on 4 August 2022, BB allowed banks and non-bank financial institutions (NBFIs) to calculate their capital market exposure based on the investment cost instead of market prices for their held securities. This initiative bolstered the investment capacity of banks and NBFIs in the capital market. Furthermore, BB updated its guidelines on bank investment portfolios to stimulate bond market growth and expand investment avenues for banks on 31 August 2023. Under the revised guidelines, bonds, debentures, and Islamic Shariah-compliant securities are exempted from banks' market exposure limits in line with the Bank Company (Amendment) Act 2023.

To encourage diversification of portfolio risks, BSEC extended the investment duration for securities market intermediaries in listed debt securities and treasury bonds until March 2024 from the previous deadline of June 2023. These intermediaries must now invest a minimum of 3.0 percent of their portfolios in listed debt securities and a minimum of 1.0 percent in listed treasury bonds. Moreover, BSEC outlined specific roles and responsibilities for independent directors of listed securities or companies on 18 October 2023. These directors are mandated to prioritize good governance, sustainability, and the company's overall well-being within the regulatory boundaries set by BSEC or other relevant regulators. Independent directors are exempted from providing guarantees for company loans or liabilities and are restricted from signing mortgage or security documents unless specifically required.

5. Forward-looking Policy Initiatives

5.1 Upholding Good Governance

To secure good governance within the financial sector, the Bank Company Act, 1991 (amended up to 2023) aims to enhance governance structures by limiting the maximum number of directors from the same family to three, down from four. This significant legislation empowers BB with the authority to dismiss the board of directors of any bank, including state-owned banks. Previously, the central bank could solely suggest or inform the finance ministry about any unethical activities by a director in state-owned banks. However, under the amended Bank Company Act, if the chairperson, director, or chief executive of a bank company is found engaged in harmful activities like fund misuse, money laundering, terrorist activities, or any offense related to the bank's interests, BB is authorized to issue a written order for their removal. Additionally, this amendment grants the central bank the power to take necessary actions, such as forced amalgamation or restructuring, if a bank company fails to implement a revival or restructuring plan effectively and its higher authorities are involved in any misconduct.

In alignment with this, the Finance Company Act, 2023, introduced on 13 November 2023, seeks to reinforce the governance of non-bank financial institutions (NBFIs). The act prohibits individuals or family members from owning more than 15 percent of an NBFI's shares and limits the number of directors from the same family to two.

BB introduced the Prompt Corrective Action (PCA) framework on 5 December 2023, designed to enable timely regulatory and supervisory intervention to uphold financial stability and public trust in the financial system. This framework takes a proactive approach to address a bank's issues early before they become severe, aiming to restore the bank to a normal state within a reasonable timeframe. BB will direct the concerned bank to execute a schedule of corrective actions based on selected parameter indicators like capital ratios, non-performing loans, and corporate governance.

Furthermore, BB has integrated risk-based supervision (RBS) into its five-year strategic plan to be implemented by 2025. This supervisory framework, established through a pilot program assessing three banks, including one Islamic bank, aims to formulate guidance notes encompassing a comprehensive set of objective and qualitative indicators for risk assessment, enhancing accuracy, credibility, comparability, and consistency in risk evaluation.

These recent regulatory strides signify that banks and financial institutions will face closer scrutiny and supervision in credit and institutional management, fostering financial stability, discipline, and strong governance. BB's proactive measures and vigilant systems in addressing potential issues in the banking sector are instrumental in averting potential crises within the industry.

5.2 Roadmap to Managing Non-Performing Loans (NPLs)

The high incidence of non-performing loans (NPLs) in Bangladesh's financial sector, significantly attributed to a prevalent willful default culture, requires immediate and focused attention. Addressing this, the recently amended Bank Company Act and Finance Company Act have opened up new avenues for action. Notably, the recent amendments of the Bank Company Act, 1991, targets explicitly willful loan defaulters – individuals who avoid repaying loans despite having the means to obtain loans through falsified information, misuse the funds, or illegally transfer mortgaged assets. Bangladesh Bank plays a pivotal role in this process, guiding banks in identifying these defaulters and compiling comprehensive lists. Once identified, these defaulters will be restricted from accessing new loan facilities. BB can propose further punitive measures, including travel bans and restrictions on holding significant positions in financial institutions for up to five years post-clearance.

To enhance the accuracy of collateral valuations, BB now requires commercial banks to use third-party evaluation firms, specifically from a BB-approved list, for appraising mortgaged assets. This regulatory measure aims to prevent inflated valuations that often lead to loan defaults, thereby safeguarding the interests of lenders. BB also emphasizes the need for legal adherence in loan recoveries, mandating banks to ensure borrowers and guarantors fully understand and acknowledge the loan terms.

BB has taken significant steps to improve transparency in loan reporting, aligning with international best practices. It now includes detailed data on banks' rescheduled loans alongside NPLs in its annual financial stability report. This approach provides a clearer insight into the distressed assets within the banking sector. BB aims to reduce the NPL ratio to below 10 percent for state-owned commercial banks (SOCBs) and 5 percent for private commercial banks (PCBs) by 2026, aiming for an overall gross NPL ratio limit of 8 percent.

In managing loans and advances more effectively, BB has introduced self-rescheduling for banks and the possibility of writing off loans classified as Bad and Loss (BL) after three consecutive years. This initiative is a strategic move to enhance NPL management. BB has also instituted a new monitoring system from the beginning of FY23, involving Memorandums of Understanding (MoUs) with several domestic private commercial banks. These MoUs focus on reducing NPL levels, addressing bank performance issues, and promoting good governance, with BB regularly monitoring compliance and progress. Besides, the recently issued PCA circular and the amended Finance Company Act will help proactively address the asset quality of banks and non-bank financial institutions. With due consultation and consent of the BB Board, the roadmap will be implemented at a faster pace.

Additionally, a committee formed by the Financial Institutions Department (FID) of the Ministry of Finance (MoF) and BB is making headway in creating the necessary legal framework and operational groundwork for establishing a privately-owned "Asset Management Company (AMC)." This initiative marks a significant step towards more effective management of distressed assets in the financial sector.

5.3 Towards Market-oriented Exchange Rate and Build-up of Foreign Exchange Reserves

Like many other economies, Bangladesh acknowledges the significance of a market-oriented exchange rate system. This system underscores efforts to bolster economic resilience, trade competitiveness, and financial stability in a globalized context. It allows the nation to closely align its currency's value with its economic fundamentals, supporting sustainable growth and development. Reflecting this, the Bangladesh Bank transitioned from using an official rate to the prevailing interbank exchange rate, as announced by the Bangladesh Foreign Exchange Dealers' Association (BAFEDA) and Association of Bankers, Bangladesh Limited (ABB), effectively eliminating the complexity of multiple exchange rates for exports, imports, and remittances from September 2023. This move toward a market-determined unified exchange rate ensures greater exchange rate flexibility despite gaps between informal and formal market rates. However, a suitable rate is anticipated to gradually close these gaps, bolstering external balance and international reserves in the future, thereby reinforcing exchange rate stability.

The Bangladesh Taka (BDT) against the USD maintains alignment with the market rate, supported by assessments using the Real Effective Exchange Rate (REER) Index and internal evaluations. While the BDT experienced a marginal depreciation from July to December 2023 compared to the same period the previous year, it currently stands at 110.00 per USD as of 31 December 2023. This positioning remains broadly competitive among peer countries, reflected by the relative magnitude of recent depreciation BDT vis-à-vis peer countries' currencies. In line with this, the BB is planning to implement a crawling peg arrangement, in the interim, based on a currency basket, initially featuring a band corridor, before moving to a free-floating exchange rate regime. This approach allows the exchange rate to move freely within the corridor while permitting intervention in foreign exchange markets to prevent rates from exceeding the set limits, aiming to mitigate unusual fluctuations.

Simultaneously, Bangladesh's current international reserves cover approximately four months of import payments, surpassing the standard benchmark of 3 months. This reserve position indicates the country's relatively stable financial stance. Moreover, forecasts suggest potential growth in international reserves in the latter half of FY24, driven by anticipated improvements in the current account balance and a reversal in the financial account deficit. Additionally, expected momentum in the ODA, FDI, PFI, and short-term borrowing from foreign sources are poised to improve the financial account, consequently enhancing the overall BoP position to help build international reserves. Prudent management of foreign exchange reserves serves as a protective buffer against potential external vulnerabilities, solidifying financial and economic stability.

5.4 Streamlining Open Market Operation

The Bangladesh Bank transitioned from its conventional monetary targeting framework to an interest rate targeting system in July 2023. Under this framework, the overnight repo rate is the policy rate, and the inter-bank call money market rate operates as the target rate. BB established an interest rate corridor (IRC) centered on the policy rate, wherein the standing lending facility (SLF) rate represents the upper limit, and the standing deposit facility (SDF) rate acts as the lower boundary. The goal is to maintain the call money rate in proximity to the policy rate by adjusting it in response to prevailing macroeconomic conditions.

BB opted to permit unrestricted access to SLF and SDF for banks and non-banking financial institutions as part of the new policy approach. This move aims to synchronize the call money rate with the policy rate, offering enhanced flexibility in monetary operations. To ensure seamless transmission of policy rates and optimize banks' liquidity management aligned with the reserve maintenance cycle, further refinement of open market operations is being contemplated for potential implementation in the foreseeable future.

6. Monetary Policy Stance and Monetary & Credit Projections for H2FY24

6.1 Monetary Policy Stance

In the context of current geo-economic and geopolitical tensions, the global economy is experiencing subdued growth. This slowdown is largely attributed to aggressive monetary policies responding to persistent inflationary pressures. Recent signs of inflation easing suggest that policy interest rates in major economies may have reached their zenith. There is a growing anticipation that the US Federal Reserve, the European Central Bank, and other central banks of major economies may soon consider reversing their rate-hiking trajectories. However, the timing of such shifts remains uncertain.

Similarly, Bangladesh's economy is grappling with significant macroeconomic headwinds, including heightened inflation, diminishing foreign exchange reserves, and exchange rate volatility exacerbated by a burgeoning balance of payments deficit. This situation is compounded by ongoing liquidity challenges and persistently high levels of non-performing loans. Conversely, Bangladesh stands out as one of the world's fastest-growing economies.

In response to these intricate economic landscapes, the Bangladesh Bank (BB) is poised to unveil its semi-annual monetary policy framework through this Monetary Policy Statement (MPS) for the second half of Fiscal Year 2024. This statement mainly focuses on alleviating inflationary pressures through demand-side management, complemented by strategic interventions in the economy's supply dynamics.

The Bangladesh Bank undertakes an exhaustive analysis of both global and domestic macroeconomic conditions and their short-term projections in shaping its monetary policy stance and credit policy for the second half of Fiscal Year 2024. This analysis is enriched by incorporating projections and insights from multilateral development partners, think tanks, and academic institutions, focusing on global growth trends, inflation, exchange rate fluctuations, and interest rate movements.

In addition to these global perspectives, BB meticulously evaluates recent developments across several domestic economic sectors. These include the real sector, inflation trends, the money market, the foreign exchange market, the capital market, monetary aggregates, the liquidity status of banks, and the structure of interest rates. Such a comprehensive approach is vital for an in-depth understanding of the current economic dynamics and future outlook. Moreover, the Bank emphasizes the feedback, opinions, suggestions, and recommendations obtained from experts during its monetary policy consultation meetings. This process of active engagement ensures that a diverse range of perspectives and expert knowledge is integrated into the policy-making process.

Further aligning with the government's economic objectives, BB's policies are crafted to support the revised target of achieving a 6.5 percent Gross Domestic Product (GDP) growth while keeping inflation within a maximum limit of 7.5 percent for the fiscal year 2024. This alignment underscores BB's commitment to synchronizing its monetary policy objectives with the broader economic goals of the nation.

According to the Commodity Market Outlook from October 2023, global energy prices are projected to marginally decline in 2024 due to reduced demand from advanced economies and China's moderate growth. However, the recent geopolitical tension in the Middle East could enhance energy prices, especially for oil. World food prices are also anticipated to decrease in 2024. Domestically, Bangladesh's annual average Consumer Price Index (CPI) inflation remains significantly above target, with export growth uncertain amidst weakening global demand. Nevertheless, with global energy and commodity prices expected to fall, the impact of imported inflation should be limited. Furthermore, liquidity in the banking system is tight due to BB's stringent monetary policy and significant foreign exchange sales to commercial banks, leading to de facto quantitative tightening. Monetary aggregates like broad money, reserve money, and credit to both public and private sectors grew slower than projected in the first half of FY24.

The headline Consumer Price Index (CPI) inflation, encompassing food and non-food categories, started to decline at a slower pace than anticipated, as there is a time lag associated with the transmission of monetary policy actions to the broader economy. Additionally, the anticipated inflation and forecasts from various international organizations suggest a rate higher than the targeted 7.5 percent for FY24. Consequently, increasing the policy interest rate is considered a viable strategy to curb inflation and stabilize inflation expectations. Given these factors and considering BB's current policy priority, maintaining a tight monetary policy in the latter half of FY24 appears prudent to control inflation and anchor inflation expectations while ensuring adequate funding to the productive sectors of the economy to support desired growth.

In light of the current economic conditions, Bangladesh Bank has resolved to adjust its policy rates following deliberations with its monetary policy committee members. Consequently, the policy rate will be increased by 25 basis points to 8.00 percent from 7.75 percent. To allow liquidity management more precisely and efficiently, the Standing Lending Facility (SLF) rate will be reduced by 25 basis points to 9.50 percent from 9.75 percent. Simultaneously, the Standing Deposit Facility (SDF) rate will see a markup of 75 basis points, moving to 6.50 percent from 5.75 percent, reducing the policy rate corridor from ± 200 basis points to ± 150 basis points.

The Bangladesh Taka (BDT) has been depreciating against the US dollar since mid-2022, primarily driven by an overall balance of payments (BoP) deficit. This depreciation has exerted pressure on the BDT/USD exchange rate, contributing to domestic inflation through increased costs of imports. In light of this, many stakeholders, including economists, have advocated for a gradual shift towards a market-based exchange rate system, implemented in phases. However, given the significant depreciation of the BDT over the last few months, economic fundamental driven exchange rate will help increase export earnings and remittances inflows as the current exchange rate of the BDT against the USD appears to be competitive, reflected through the NEER and REER-based index.

In response to these dynamics, Bangladesh Bank (BB) is contemplating the adoption of a 'crawling peg' system, tethered to a basket of currencies within a defined band corridor. This strategy aims to mitigate abrupt fluctuations in the exchange rate. A competitive and representative equilibrium rate is proposed to be established at the midpoint of this corridor, allowing the exchange rate flexibility within these bounds. Under this arrangement, BB would retain the option to intervene to prevent the exchange rate from breaching the established band limits.

The concerted policy efforts by BB to tackle inflation, combined with the anticipated decline in global energy and commodity prices and the promising outlook for the upcoming Aman and Boro paddy harvests, collectively reinforce the expectation that the average general inflation will align with the government's revised target of 7.50 percent by June FY24. Additionally, adopting a crawling peg arrangement in exchange rate management is poised to significantly reduce market volatility and enhance stability in the foreign exchange market.

6.2 Monetary and Credit Projections for H2FY24

The latest half-yearly trends in major monetary and credit aggregates, along with their revised projections for FY24, are detailed in Table 6. Since July 2023, the Bangladesh Bank has shifted its monetary policy framework from a monetary targeting regime to an interest rate targeting regime. As a result of this transition, while monetary and credit projections no longer serve as the primary focus, they remain crucial in aligning the interest rate targets with broader economic goals such as maintaining price stability, ensuring financial stability, and promoting desired economic growth.

Under this interest rate targeting framework, monetary aggregates like broad money and reserve money are treated as indicative targets that guide monetary policy. In this context, BB modulates reserve money and broad money by adjusting the policy rates and managing liquidity through various instruments. These include the cash reserve ratio (CRR), statutory liquidity ratio (SLR), open market operations (such as repo operations, Standing Lending Facility (SLF), Standing Deposit Facility (SDF), and BB bills), and a range of refinancing or pre-financing facilities. Additionally, specialized instruments like Mudarabah Liquidity Support (MLS) and Islamic Bank Liquidity Facility (IBLF) are employed to tailor liquidity management to the specific needs of the financial sector.

Table 6: Revised Monetary and Credit Projections for FY24

(YoY % change)

Item	Jun-23	Sept-23	Dec-23		Jun-24	
	Actual	Actual	Projection	Actual P	Prior Projection@	Revised Projection
Broad money	**10.5**	**9.0**	**9.5**	**8.8**	**10.0**	**9.7**
Net Foreign Assets*	-23.4	-23.7	-16.8	-21.8	4.7	-2.4
Net Domestic Assets	21.3	17.9	15.9	16.2	11.1	12.2
Domestic Credit	15.3	12.7	15.9	11.7	15.4	13.9
Credit to the public sector	35.8	25.9	37.9	18.0	31.0	27.8
Credit to the private sector	10.6	9.7	10.9	10.2	11.0	10.0
Reserve money	**10.5**	**1.2**	**0.0**	**-2.0**	**6.0**	**-1.0**
Money multiplier	4.93	5.46	5.07	5.14	5.11	5.46

Source: Bangladesh Bank.

Note: *Calculated using the estimated constant exchange rates of end June 2023. @ Announced in June 2023. P= Provisional

For FY24, the projected growth of broad money is set at 9.7 percent. This projection aligns with the revised Gross Domestic Product (GDP) growth target of 6.5 percent and an average inflation ceiling based on the Consumer Price Index (CPI) of 7.5 percent while also accounting for anticipated changes in the velocity of money. The projected growth in public sector credit is 27.8 percent, reflecting the government's selective expenditure on priority projects as part of its austerity policy measures, which are expected to reduce credit demand.

Private sector credit growth is forecast to remain steady at 10.0 percent. This projection is underpinned by BB's supply-side interventions, aimed at directing credit flow into more productive and employment-generating sectors. Considering these growth rates in both the public and private sectors, domestic credit growth is projected to grow by 13.9 percent by the end of June 2024. The banking system's Net Foreign

Assets (NFA) is projected to decrease by 2.4 percent for FY24. This is based on the anticipation of a modest overall balance of payments (BoP) deficit, despite expectations of moderate growth in exports and remittances, along with a negative growth in imports.

7. Near-term Macroeconomic Issues and Challenges

As Bangladesh navigates through a complex global economic landscape, its economy faces several near-term macroeconomic challenges. Foremost among these are the intensifying inflationary pressures fueled by disruptions in global supply chains and heightened commodity prices. Additionally, fluctuations in the value of the Bangladesh Taka, especially against the US dollar, are causing ripples through the economy, impacting everything from domestic inflation to trade balances and foreign exchange reserves. The financial sector, burdened with the enduring issue of non-performing loans, adds another layer of complexity, calling for decisive policy actions.

The central bank (BB) has adopted a contractionary monetary policy stance and implemented multiple measures aimed at curbing inflation. It's important to note that there is a time lag associated with the transmission of monetary policy actions to the broader economy. Despite these efforts, the recent upward trajectory of inflation has indeed been arrested, and a gradual decline has begun. However, it is noteworthy that given the global and domestic headwinds prevailing in the economy, this deceleration is occurring at a slower pace rate than initially anticipated.

BB is committed to taking all necessary policy measures until the point-to-point Consumer Price Index (CPI) based inflation rate reaches the target of 6.0 percent. Nevertheless, several challenges stand ahead, primarily in the near-term fiscal policy stance, non-economic factors, global fuel price dynamics amidst instability in the Middle East, and the prices of essential commodities in the international market. These factors collectively pose significant challenges in the ongoing battle to contain inflation.

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