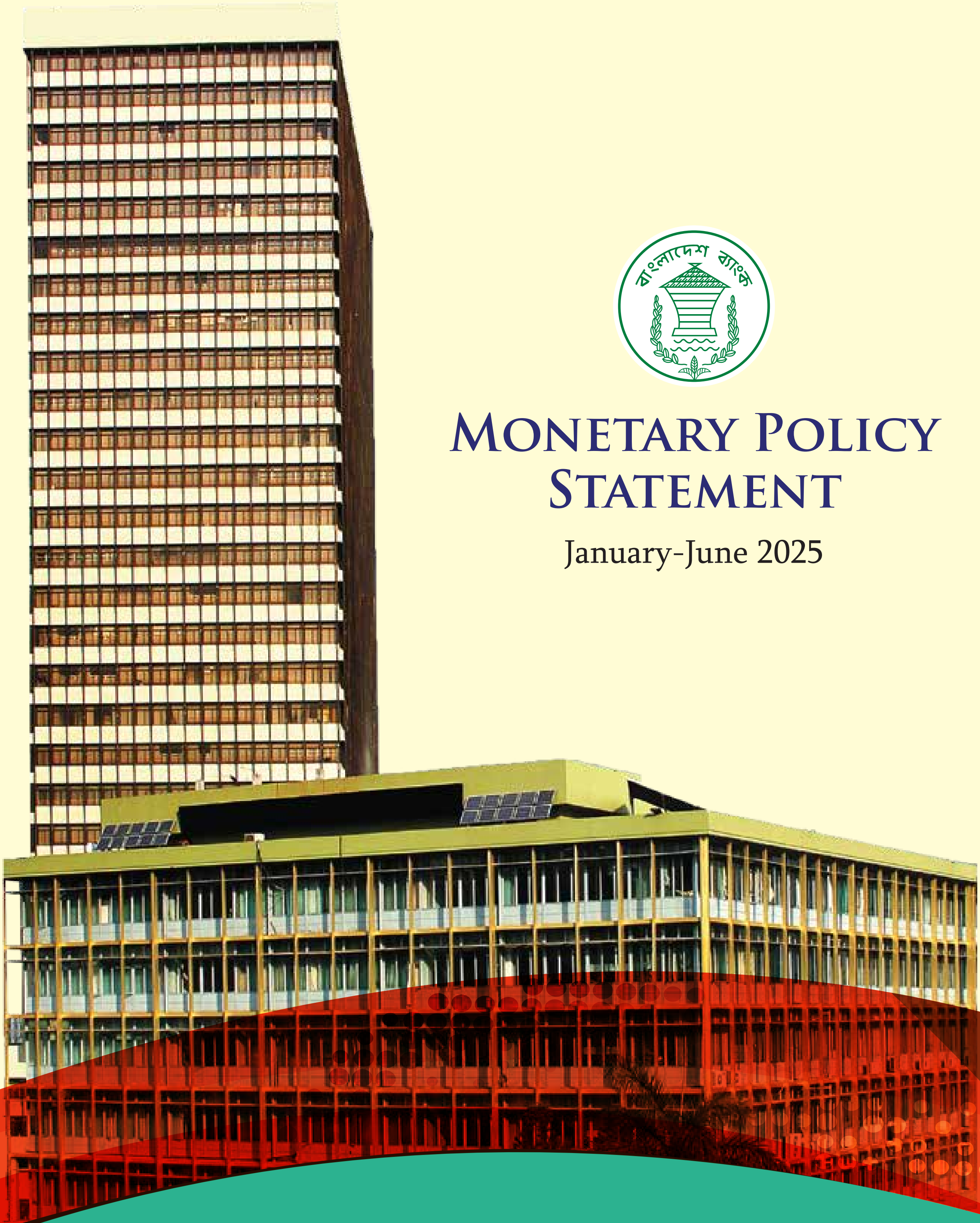

MONETARY POLICY STATEMENT

January-June 2025

Bangladesh Bank

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Monetary Policy Statement

January-June 2025

Bangladesh Bank

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Acronyms and Abbreviations

Act.	Actual
AD	Authorised Dealer
ADP	Annual Development Programme
ALS	Assured Liquidity Support
ALS	Assured Liquidity Support
AM	Ante Meridiem
AQR	Asset Quality Reviews
BB	Bangladesh Bank
BBS	Bangladesh Bureau of Statistics
BDT	Bangladesh Taka
BoP	Balance of Payments
BSEC	Bangladesh Securities and Exchange Commission
BSRTF	Banking Sector Reform Taskforce
CAB	Current Account Balance
CPI	Consumer Price Index
DPS	Deposit Pension Scheme
DSEX	Dhaka Stock Exchange
ECL	Expected Credit Loss
EDF	Export Development Fund
FDI	Foreign Direct Investment
FDR	Fixed Deposit Receipt
FY	Fiscal Year
GDP	Gross Domestic Product
GoB	Government of Bangladesh
H1	First Half
H2	Second Half
IBLF	Islamic Banks Liquidity Facility
IFRS	International Financial Reporting Standard
IMF	International Monetary Fund
IRC	Interest Rate Corridor
L.H.S	Left Hand Side
LC	Letter of Credit
M2	Broad Money
MFS	Mobile Financial Service
MLS	Mudarabah Liquidity Support
MLT	Medium and Long-Term
MPS	Monetary Policy Statement
MSMEs	Micro, Small, and Medium Enterprises
NBFIs	Non-Bank Financial Institutions
NEER	Nominal Effective Exchange Rate
NFA	Net Foreign Asset
NPL	Non-Performing Loan
NSCs	National Savings Certificates
OMOs	Open Market Operations
P	Provisional
PM	Post Meridiem

PMI	Purchasing Managers' Index
Proj.	Projection
Q2	Second Quarter
R.H.S	Right Hand Side
RBS	Risk-Based Supervision
REER	Real Effective Exchange Rate
RFCD	Resident Foreign Currency Deposit
RM	Reserve Money
RMG	Ready-Made Garments
RMP	Reserve Maintenance Period
RR	Reference Exchange Rate
SDF	Standing Deposit Facility
SLF	Standing Lending Facility
SLS	Special Liquidity Support
SME	Small and Medium Enterprise
SOFR	Secured Overnight Financing Rate
TK.	Taka
UBOs	Ultimate Beneficial Owners
UK	United Kingdom
US	United States
USA	United States of America
USD	US Dollar
WEO	World Economic Outlook

Table of Contents

Executive Summary

On 5 August 2024, a student-led mass uprising ousted an authoritarian regime, paving the way for significant political transformation and extensive economic and legal reforms in Bangladesh. As the country enters a new era, it presents opportunities for much-needed reforms in the financial sector that can support the revival of the economy. In this context, Bangladesh Bank (BB) has initiated essential reforms to address long-standing structural problems in the banking sector and rebuild trust in the sector. The key focus areas of the reforms include restoring macro-economic stability by addressing the inherited external and domestic sector imbalances and restoring price stability by lowering inflation.

Accordingly, BB has developed clear, forward-looking strategies and has started implementing robust reform measures to tackle economic and financial challenges. As part of its implementation strategy, three task forces have been established with the following objectives: (i) conducting a comprehensive asset quality review of banks' assets to lay the groundwork for a thorough banking sector reform program; (ii) enhancing the capacity and efficiency of BB with focus on effective enforcement of regulations and ensuring good governance in the banking system; and (iii) aggressively pursuing the recovery of stolen assets both domestically and internationally.

This edition of BB's half-yearly Monetary Policy Statement (MPS) primarily explains the monetary policy stance for the second half of FY25. It considers political and economic conditions, global and domestic market trends for the first half of FY25. The main goals are to contain inflation, stabilize the foreign exchange market while building foreign exchange reserves of BB, and address the rapidly rising non-performing loans in banks and financial institutions.

Regarding the global economy, various multilateral organizations project global growth will remain steady at approximately 3.2 percent for both 2024 and 2025, which could aid Bangladesh's recovery in exports and remittances. Additionally, global inflation is expected to continue its downward trend toward central bank targets, likely easing the issue of imported inflation. However, several downside risks persist, including potential escalations in various regional conflicts, a resurgence in financial market volatility that could adversely affect sovereign debt markets, and an increase in protectionist trade measures.

Despite various monetary and fiscal tightening measures, inflation remained persistently high, staying above 10 percent for an extended period. However, the positive impact of these policies is beginning to show, as the point-to-point inflation rate eased in December 2024 and again in January 2025, dropping to 9.94 percent in January from 11.38 percent in November, mainly due to a decline in food inflation. With BB's firm policy stance and close collaboration with key stakeholders, inflation is expected to decline further in the near future, making the target range of 7-8 percent achievable.

In the first half of FY25, the growth rate of money supply was subdued, with private sector credit growth decelerating to 7.3 percent in December 2024, marking the lowest growth rate since October 2021. Given the global and domestic realities, BB remains committed to a tight monetary policy stance for the second half of FY25.

> *In light of the recent inflation results, the central bank has decided to maintain the policy rate unchanged at 10.0 percent. The Standing Lending Facility (SLF) rate will remain at 11.5 percent, while the Standing Deposit Facility (SDF) rate will stay at 8.5 percent, establishing a policy rate corridor of ± 150 basis points.*

Given the current inflation landscape, BB anticipates a decrease in inflation in the coming months. This outlook is supported by actions already taken by the monetary and fiscal authorities, continued stability in the exchange rate, ongoing global commodity price moderation, and anticipated output expansion in agricultural products like 'boro' rice and other agricultural products. BB will continuously monitor inflation trends and adjust interest rates and liquidity measures as necessary.

BB has been implementing a crawling peg exchange rate mechanism to enhance both flexibility and stability of the rate in the foreign exchange market. This framework is designed to ensure stability of the exchange rate while preparing for an eventual transition to a more flexible exchange rate system in the near future. BB has already stopped intervening in the exchange market by completely halting the sales of foreign exchange in the interbank market to support exchange rate stability. BB has established a methodology for calculating the Foreign Exchange Spot Reference Exchange Rate (RR) which is prepared and published twice per day. Prudent exchange rate management under the current system is anticipated to strengthen remittance inflows, stimulate export activities, and augment foreign exchange reserves.

Notwithstanding the progress reported, Bangladesh economy is poised to encounter substantial hurdles in the second half of FY25 as it grapples with the pressing need to curb inflation, stabilize the exchange rate, rebuild foreign exchange reserves, and restore public confidence in the banking system. The landscape is further complicated by the growing concern of non-performing loans (NPLs), sluggish economic activity, and a slowdown in deposit and credit growth, all of which present formidable challenges for the banking sector. In response to these mounting issues, the government and BB have embarked on a series of ambitious reform initiatives designed to avert any potential crisis in the banking system and pave the way for long-term economic stability. The success of these ongoing initiatives will hinge on their effective implementation, along with forthcoming measures that aim to develop comprehensive solutions for distressed banks in line with the findings of the Asset Quality Review (AQR). Through these efforts, BB seeks to restore sound governance practices and enhance stakeholder confidence in the banking system, thereby fostering a more resilient and trustworthy financial environment for future growth.

Monetary Policy Statement: H2FY25

1. Foreword

In July 2024, Bangladesh underwent a historic political transformation characterized by a student-led movement resonating deeply with a wide spectrum of the populace. This movement successfully fostered an environment of dialogue and collaboration, culminating in the formation of a new Interim Government in August 2024, with the endorsement of major political parties. Bangladesh Bank (BB) under the guidance of the interim administration has promptly prioritized the essential financial sector reforms to address longstanding structural problems. Key focus areas include restoring macroeconomic stability, preventing a potential banking system run, initiating legal and policy reforms to resolve the banking sector problems, strengthening the operations of BB, and recovery of the assets stolen from the banking system.

As the country enters a new era, BB is seizing the opportunity to implement essential reforms in the financial sector. The interim government is decisively driving significant changes in macroeconomic management and taking definitive steps to restore trust in the banking sector. BB has outlined clear and forward-looking strategies emphasizing its commitment to maintaining low and stable inflation while ensuring sustained economic growth and financial stability.

BB has been implementing a robust set of measures to address economic and financial challenges. The measures include the establishment of three task forces with the clear objectives of (i) strengthening the banking system by conducting asset quality review of bank assets, and paving the way for a comprehensive resolution of banking sector problems; (ii) strengthening the operations of BB through internal restructuring and capacity building; and (iii) aggressively pursuing the recovery of stolen assets both at home and abroad.

The Monetary Policy Statement (MPS) for the second half of FY25 primarily aims to address the ongoing inflationary challenges while stabilizing the foreign exchange market amid alarming non-performing loans in the banks and non-bank financial institutions. This MPS reflects BB's strategic monetary policy direction for the second half of FY25, based on the outcomes observed during the first half of the current fiscal year.

In light of the macroeconomic developments in the first half of FY25 and the evolving political landscape in Bangladesh, BB has actively sought feedbacks from a wide range of stakeholders. This consultation process included input from BB senior executives, members of the Monetary Policy Committee, and the Board of Directors. Additionally, insights from policymakers, economic analysts, think-tanks, and private sector leaders were gathered through stakeholders' consultations.

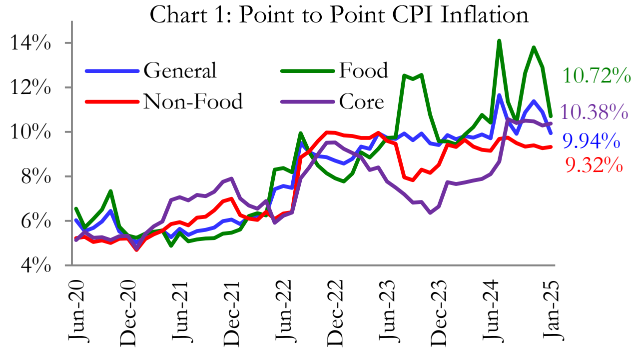
Historically, stakeholder consultations had primarily taken place in Dhaka. However, to enhance the inclusivity of the feedback process, BB has initiated a stakeholder meeting in Chattogram for the first time. This outreach aims to gather insights from regional stakeholders, ensuring that the MPS reflects different perspectives and considerations.

2. Monetary Policy Outcomes and Macroeconomic Developments in H1FY25

2.1 Price Developments

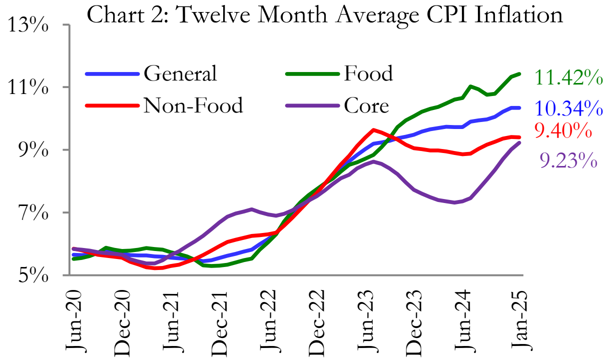
Headline inflation and its components — food and non-food inflation — have remained persistently high for an extended period (Charts 1 & 2). Since May 2022, headline inflation has risen steadily, reaching 9.33 percent in March 2023 and staying above 9 percent ever since. In July 2024, inflation peaked at 11.66 percent, the highest level recorded since September 2011. While food inflation has remained volatile and exhibited a similar upward trend, non-food inflation has remained relatively stable.

Chart 1: Point to Point CPI Inflation



Source: Bangladesh Bureau of Statistics (BBS)

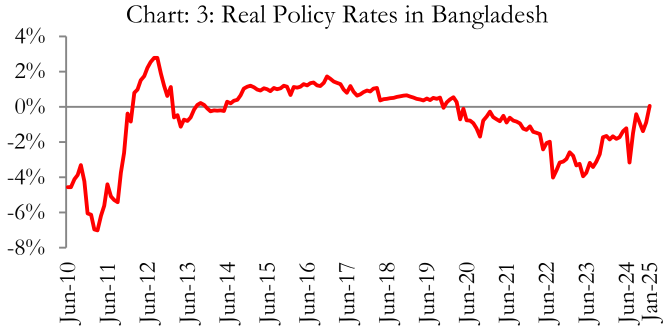
Chart 2: Twelve Month Average CPI Inflation



Source: Bangladesh Bureau of Statistics (BBS)

The persistently high inflation observed recently can be attributed to several critical factors. Historical data regarding real policy rates indicate that monetary policy has remained excessively accommodative since 2020, as demonstrated by the consistently negative real policy rate. Furthermore, the implementation of a lending rate cap at 9 percent since April 2020, which remained in effect until May 2024, has undermined effective monetary policy operations in Bangladesh.

Chart: 3: Real Policy Rates in Bangladesh

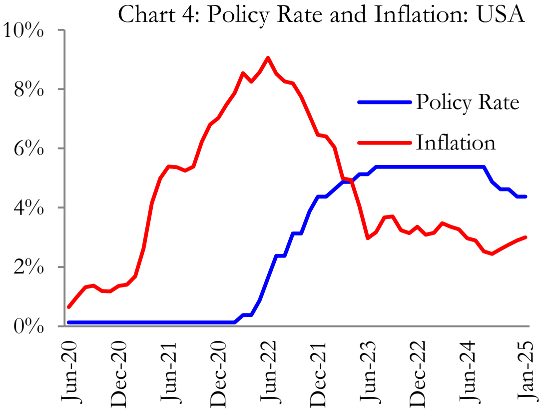


Source: Bangladesh Bank

In contrast to the prompt and decisive actions undertaken by both advanced and emerging economies—which swiftly raised their policy rates and completed their tightening measures within a year—Bangladesh's policy response has been characterized by delays and inadequate adjustments. This lack of urgency has exacerbated the inflationary pressures confronting the nation.

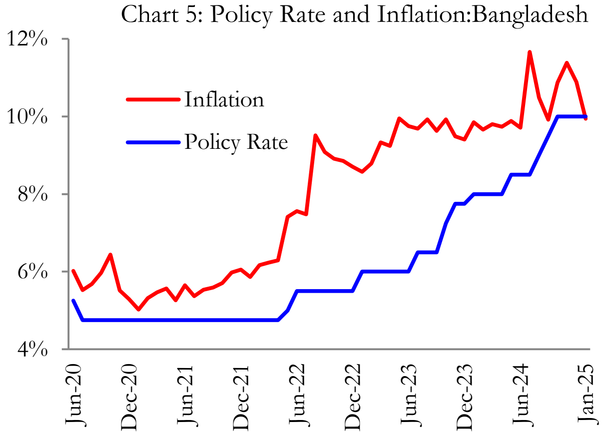
Another important contributor to the ongoing inflation was the rapid depreciation of Bangladesh Taka against the U.S. dollar, which escalated sharply in 2022. By the end of 2024, the Taka has depreciated by more than 30 percent, contributing to the surge in inflation through the pass-through effect of the exchange rate depreciation. Even as global commodity prices began to stabilize after 2023, domestic prices continued to increase, primarily due to the detrimental effects of the domestic currency's significant depreciation. The developments underscored the urgent necessity for robust and timely monetary policy response to restore macroeconomic stability. The 1.5 percentage point increase in the policy rate implemented by BB during August-October 2024 was a manifestation of that policy shift by the interim government.

Chart 4: Policy Rate and Inflation: USA



Source: Federal Reserve Board, USA

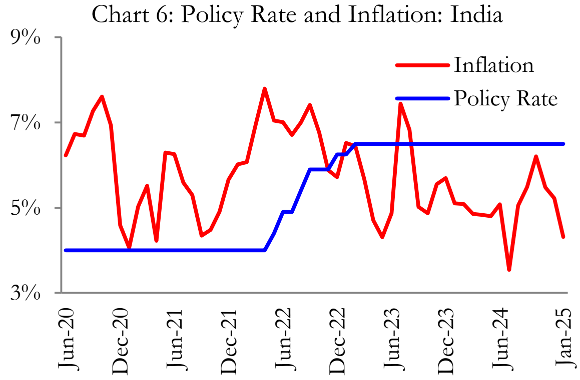
Chart 5: Policy Rate and Inflation:Bangladesh



Source: Bangladesh Bank

Furthermore, persistent supply chain disruptions and inefficiencies have intensified the inflationary pressures. The initial spike in inflation, as happened across the globe, was primarily triggered by supply chain disruptions stemming from the COVID-19 pandemic and the geopolitical turmoil and energy shock associated with the Russia-Ukraine conflict. Additionally, the effects of the exchange rate depreciation and the consequent energy price adjustments, market imperfections, and disruptions from the twin floods in August and September 2024 have further worsened the inflation situation.

Chart 6: Policy Rate and Inflation: India



Source: Reserve Bank of India

In January 2025, BB conducted an insightful study on price determination and efficiency of the supply chain for essential agricultural products. The findings revealed that, although domestic value/market chain is generally quite efficient, proactive measures—such as robust monitoring and oversight of commodity stocks, timely imports before shortages occur, accurate and timely prediction of supply-demand gaps, and rationalization of import duties—could be pivotal in stabilizing prices for staple items like rice, wheat, edible oil, potato, and onion.

2.2 Expected Inflation in Near Future

The overall inflation rate has declined by around 1.5 percentage points in the most recent two-month period in response to the demand and supply side measures put in place in recent months. On the demand side policies include: allowing the determination of interest rates by market forces; the three-step increase in the policy rate; a sizable reduction of the fiscal deficit, despite revenue shortfall, through substantial expenditure cuts. The supply side policies include: increased availability of foreign exchange and stabilization of the exchange rate; ensuring availability of agriculture and power sector related imports; elimination of taxes and duties on essential food imports; and abolishing margin requirements on all essentials imports.

Against this background, BB expects that the current high rate of inflation will come down to within a 7-8 percent range by end-June 2025. This forecast is anchored in a series of compelling factors that reflect a robust and adaptive economic landscape. The current stance of monetary policy remains reasonably tight, designed to keep Taka attractive as an asset, maintain exchange rate stability, and thereby curtail inflationary pressures. This deliberate multi-dimensional approach should serve as the cornerstone for our inflation reduction strategy. Historical and cross-country experience reveals a consistent pattern: inflation typically recedes in 6-12 months following sustained increases in policy rates, providing valuable insights into the likely trajectory of inflation and reinforcing confidence in this timeline. Generally, within 6-12 months the real policy rates turned positive in other countries and, thereafter, remained positive, with inflation falling steadily. In the case of Bangladesh, we also observed that the real policy rate has turned slightly positive in January 2025 for the first time in recent months. BB expects the policy rate to become more positive in the coming months, with a further decline in inflation.

BB also anticipates the exchange rates to remain stable, bolstered by significant improvements in the balance of payments (BoP). This stability translates to reduced volatility in domestic commodity prices and contributes to overall economic resilience. BB is optimistic about the continued strengthening of the BoP, driven by the ongoing surge in inflow of remittances and promising prospects for export receipts, which will further support efforts to maintain price stability.

Discontinuing the devolvement facility for the Government is a strategic decision aimed at mitigating the inflationary effects associated with the injection of high-powered money. This move reinforces the Government’s commitment to sound economic principles. In tandem, a concerted effort to harmonize fiscal and monetary policies has enhanced the effectiveness of macroeconomic management, ensuring that both frameworks work synergistically to combat inflation and create conditions for stimulating growth.

Additionally, the government's strategic initiative to cut unnecessary expenditures is expected to fortify macroeconomic management, allowing for a more efficient allocation of resources and fostering long-term economic stability. The implementation of extensive measures to improve supply chains includes slashing tariffs on essential commodities, adjusting the Letter of Credit (LC) margins for critical goods—particularly in anticipation of the holy month of Ramadan—expanding open market sale operations, and facilitating the required imports of fertilizers to support agricultural production. Necessary stocks of fertilizer are now in place to ensure more acreage under 'boro' cultivation. These initiatives are crucial for ensuring an increased supply of agricultural outputs, including rice, potato and onion, which are vital for food security and price stability.

Finally, the outlook for global commodity prices remains on a downward stable trajectory, acting as a buffer against domestic inflationary pressures and further supporting the objective of maintaining price stability. Through these strategic actions and favorable conditions, BB is confidently steering toward its inflation target, setting the stage for a healthier and more resilient economy. Historical experience reveals a consistent pattern: inflation typically starts receding in 6-12 months following an increase in policy rates and reaches the envisaged target ranges within 12-18 months. This historical lens provides valuable insights into the likely trajectory of inflation, reinforcing our faith in the projected timeline.

2.3 Growth

The post-pandemic economic recovery has been sluggish in Bangladesh, with real GDP growth of 4.22 percent in FY24. This slowdown had occurred alongside sustained high inflation in the domestic market, reflecting the challenges stemming from the Russia-Ukraine war, global uncertainty, and mediocre growth coupled with rising inflation in key trading partners and remittance sources. This growth performance has been influenced by several factors, including adjustments to the exchange rate that resulted in depreciation, lower import demand, a tight monetary policy, and efforts to maintain fiscal discipline. However, the student-led mass uprising in the summer of 2024, followed by a change in government, significantly impacted on economic activity, leading to consumer and investor uncertainty. This uncertainty manifested as a mere 1.81 percent real GDP growth in the first quarter of FY25, down from 3.91 percent in the last quarter of FY24.

The industrial sector, which historically grows faster than other sectors, shows some potential for recovery despite sluggish private credit growth and a rising unemployment rate. Conversely, the agriculture sector has suffered significant losses due to severe floods. The output losses during the public uprising, combined with disruptions in the domestic supply chain, pose challenges for the service sector as well. Weakened aggregate demand resulting from fiscal austerity, elevated uncertainty, and a tighter policy mix could further hinder the recovery of lost growth momentum.

However, the domestic market may begin to show the effects of adaptation to the depreciated exchange rate of Bangladesh Taka (BDT) over the last two fiscal years. As flexibility increases in the foreign exchange market, the external sector is performing better, as indicated by the recent surge in workers' remittances, strong export performance, and rebounding import demand. The large-scale manufacturing output, a key component of GDP, exhibited 1.95 percent growth during July-October of FY25. The Purchasing Managers' Index (PMI), on the other hand, indicated an expansion in economic activity in Q2 of FY25, rising to 61.7 in December 2024, compared to 47.7 in September 2024. This upward trend in the PMI across various sectors during the second quarter of FY25 points to increased economic activity in agriculture, industry, and services despite challenges such as political instability, labor unrest, and economic headwinds.

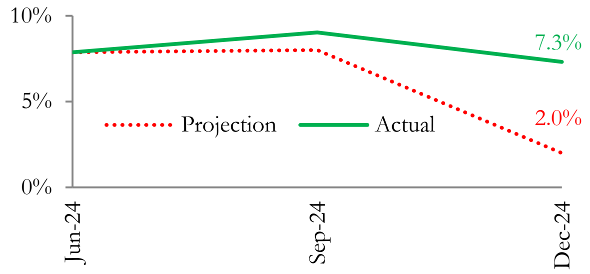
The International Monetary Fund (IMF) projects global growth to remain mediocre at 3.3 percent for 2024 and 2025, which may pose additional challenges for Bangladesh's economic recovery efforts. Although there has been a recent decline in global commodity prices, new spikes are emerging due to rising shipping costs, intensified protectionist policies, and increasing geo-economic fragmentation alongside geopolitical tensions. On a positive note, most advanced economies have paused their aggressive monetary tightening that characterized the post-pandemic years, leading to lower inflation expectations in the near to medium term.

The growth outlook for the second half of FY25 for Bangladesh does not appear optimistic due to the existing challenges. However, remittances from workers abroad, strong growth in Ready-Made Garment (RMG) exports, and increased private demand from the two upcoming religious festivals are expected to provide support. Additionally, it will be hard to regain growth momentum in the near term since the government is focusing on improving fiscal discipline, and the central bank is working to control inflation. As a result, economic growth may remain sluggish at around the 4.0-5.0 percent range in FY25. Growth should bounce back to 6.0 percent or above in FY26 as the political situation stabilizes, uncertainty decreases, and policies become more proactive. Despite the modest slowdown in economic activity, the projected growth should be viewed as remarkable, given the numerous challenges facing the economy.

2.4 Monetary Aggregates

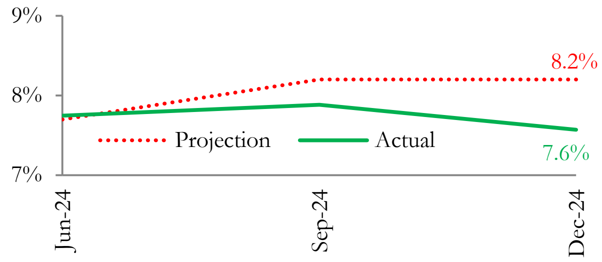
Broad money (M2), witnessed a year-on-year growth of 7.6 percent in December 2024 against the projected growth of 8.2 percent. The slower broad money expansion compared with the projected growth path, is attributable to the negative growth in the net foreign assets (NFA). The NFA of the banking system during H1FY25 experienced a decline of 15.7 percent compared to the projected growth of 2.7 percent for December 2024. The deficit in the overall balance of payments (BoP), despite a virtual balance position in the current account and a surplus in the financial account is attributable to repayment of external payment arrears accumulated in recent years. Reserve Money (RM), another information variable of monetary policy, experienced a robust growth of 7.3 percent (year-over-year) by the end of December 2024. The growth of RM exceeded the projected trajectory for December 2024 due to the strong growth in the net domestic assets (NDA) of BB. The positive growth of NDA was mainly driven by BB's significant liquidity supports to some banks to meet their daily liquidity needs. The positive growth of the NDA of BB partially offset the negative growth of Bangladesh Bank's Net Foreign Assets (NFA). Although Bangladesh Bank stopped sale of dollars to commercial banks since August 2024, the negative growth of the NFA of BB was mainly attributable to debt service payments associated with the public sector debt and lower than expected inflow of foreign financing for budget financing.

Chart 7: Reserve Money (RM) Growth



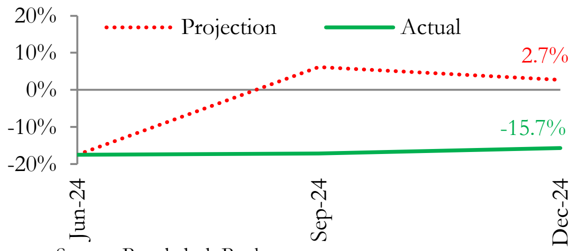
Source: Bangladesh Bank.

Chart 8: Broad Money (M2) Growth



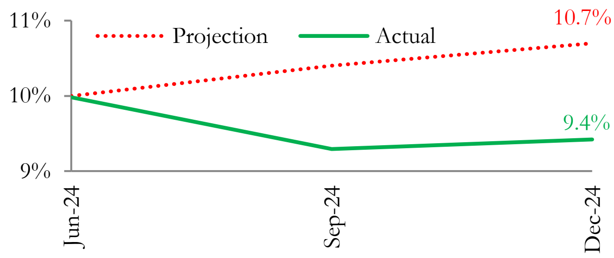
Source: Bangladesh Bank.

Chart 9: Net Foreign Assets (NFA) Growth



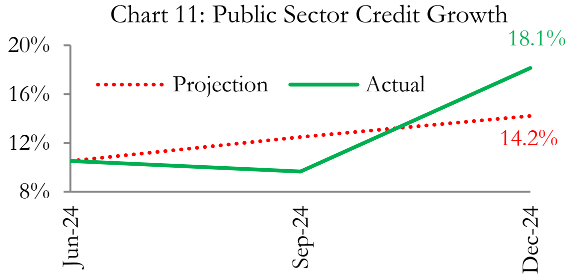
Source: Bangladesh Bank.

Chart 10: Domestic Credit Growth



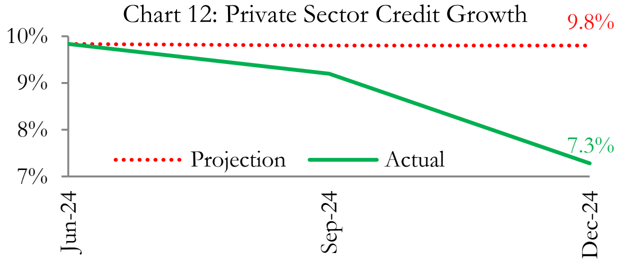
Source: Bangladesh Bank.

Chart 11: Public Sector Credit Growth



Source: Bangladesh Bank.

Chart 12: Private Sector Credit Growth



Source: Bangladesh Bank.

Credit extended to the private and public sectors showed mixed trends during the first half of the fiscal year 2025 (H1FY25). Private sector credit growth has been decreasing since November 2022, reaching a growth rate of 7.3 percent in December 2024. This ongoing deceleration of private sector credit suggests that the slowdown is not the result of policy rate hikes but rather a combination of several other factors. These factors include: slower deposit growth and increased government borrowing from commercial banks, crowding out private sector credit. Deposit growth decelerated to 7.4 percent in December 2024 from 14.3 percent in March 2021, contributing primarily to the slowdown in overall credit expansion.

Despite the slower deposit growth, public sector credit growth of 18.1 percent in December 2024, surpassed the projected growth rate of 14.2 percent. This significant increase is attributed to higher credit demand from the government, attempting to meet its spending needs amidst revenue collection falling significantly below target. Overall, domestic credit growth exceeded the projected trajectory for December 2024, largely driven by the robust increase in public sector credit, thereby crowding out the availability of credit for the private sector.

According to the latest data, the government's net credit from the banking system during the July-December period of FY25 reached Tk. 14,642.54 crore, which accounts for 14.79 percent of the revised target of Tk. 99,000 crore borrowing from the banking system. It is noteworthy that, during this timeframe, the government borrowed a net amount of Tk. 69,056.1 crore from scheduled banks while making a net repayment of Tk. 54,413.6 crore to BB.

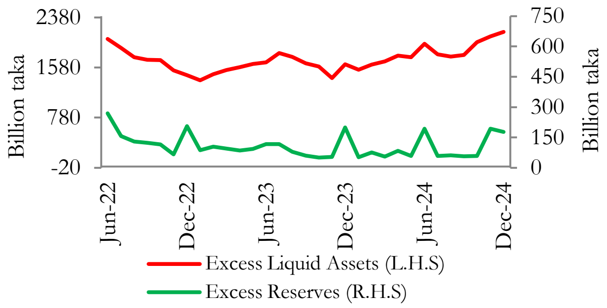
With BB halting its devolvement, the government's net credit now heavily depends on scheduled banks. Furthermore, government borrowing from National Savings Certificates (NSCs) during July-November of FY25 saw a decline of Tk. 15,588.6 crore, compared with a decline of Tk. 5,539.0 crore recorded during the same period in FY24. This drop indicates that repayments surpassed new sales, suggesting a partial redemption of NSCs and a diversion of non-bank savings to other sources. Additionally, net foreign financing amounted to Tk. 5,540.0 crore during the July-November period of FY25, reflecting a decrease of Tk. 11,086.0 crore compared to the same period in the previous fiscal year.

2.5 Liquidity and Interest Rate

The banking sector in Bangladesh has been facing some liquidity crunch since June 2021, which has continued throughout the first half of the fiscal year 2025. This tight liquidity situation is due to several factors, including sale of foreign exchange in the interbank market by BB out of its reserves in support of the exchange rate of Taka, slow loan recovery, a high volume of non-performing loans (NPLs), sluggish deposit growth despite rising and attractive interest rates on deposits, and increased cash holding by the public stemming from a lack of confidence in the banking sector due to widespread irregularities and scams, particularly involving some Shariah-based banks. Additionally, the implementation of contractionary monetary policy to control inflation has further limited the liquidity in the banking sector.

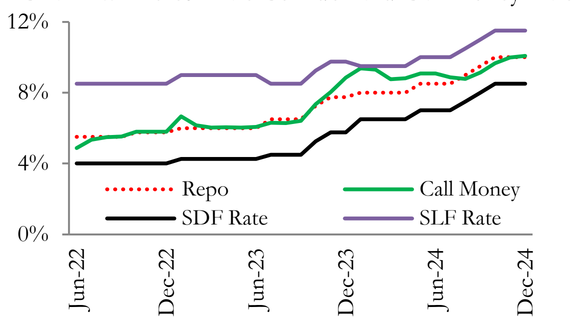
In response to the declining liquidity, the Bangladesh Bank has taken several measures to relieve the pressure on the banking sector during H1FY25. These measures include: (i) granting unrestricted access to the Standing Lending Facility (SLF) and facilitating full allotment of repo facilities for banks and non-banks; (ii) allowing liquidity-deficient banks to borrow from the inter-bank money market with BB guarantee; (iii) providing special liquidity support to certain banks facing operational difficulties. However, to mop up a part of the liquidity injections to cash-strapped banks, BB has issued 30- and 90-day Bangladesh Bank Bills (BB Bills). The changes in the liquidity situation are illustrated in Chart 13.

Chart 13: Movement of Excess Liquid Assets



Source: Bangladesh Bank

Chart 14: Interest Rate Corridor and Call Money Rate



Source: Bangladesh Bank

The combined effects of contractionary monetary policy and the tight liquidity environment in the money market have led to a significant rise in interest rates. The weighted average call money rate increased by almost one percentage point to 10.07 percent over six-month period to December 2024 (as shown in Chart 14). The interbank repo rate rose from 8.56 percent in June 2024 to 10.18 percent in December 2024. Furthermore, the substantial increase in the policy interest rate has been reflected in the lending and deposit rates. (Chart 15 and 16). However, much of the rise in the lending rate originated at the time when the lending rate cap was removed (in May 2024), well before the start of policy rate increases which began in August 2024.

Chart 15: Developments of Deposit rates

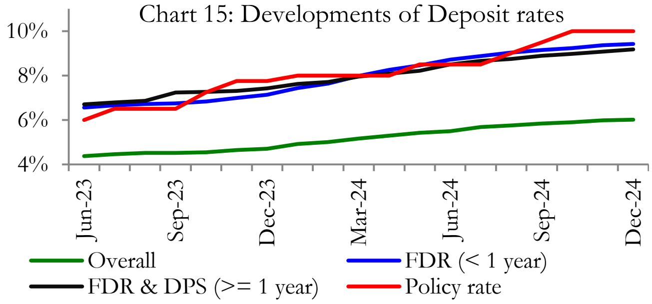
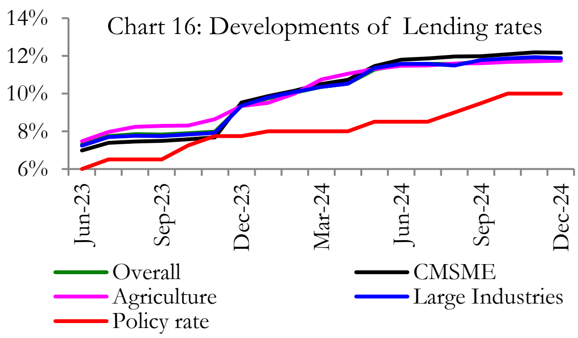


Chart 16: Developments of Lending rates

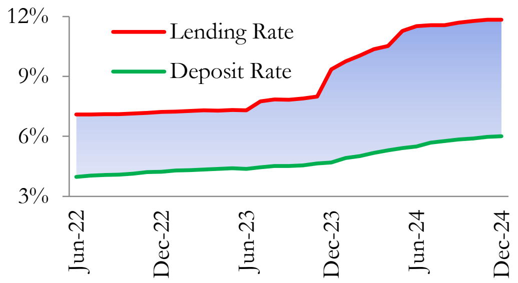


BB has consistently extended various forms of liquidity support to ensure healthy liquidity conditions. This includes the provision of full allotment for repo facilities, Assured Liquidity Support (ALS), and standard and special repo facilities for conventional banks and non-bank financial institutions. For Shariah-compliant Islamic banks, BB has implemented Mudarabah Liquidity Support (MLS), the Islamic Banks Liquidity Facility (IBLF), and Special Liquidity Support (SLS).

At the end of H1FY25, the outstanding liquidity reached TK. 1,17,533 crore, an increase from TK 91,806 crore at the end of H2FY24. Additionally, BB has guaranteed BDT 11,100 crore via its credit guarantee scheme to facilitate interbank transactions to assist the banks facing liquidity constraints, with BDT 7,350 crore utilized under this scheme by December 2024. Furthermore, special liquidity support amounting to TK. 23,500 crore had been allocated to banks encountering challenges in their daily operational liquidity.

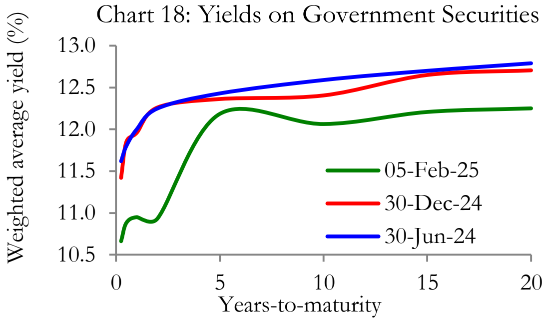
The liquidity landscape has shown improvement due to BB's comprehensive liquidity interventions. As of December 2024, banks' excess liquid assets rose to TK. 2,15,002.2 crore from TK. 1,95,824.5 crore in June 2024. Meanwhile, excess reserves slightly decreased to TK. 17,675.3 crore by the end of December from TK. 19,329.0 crore in June 2024. Notably, despite the ample liquidity provision by BB during H1FY25, the excess liquid assets for Islamic banks fell to TK. 8971.2 crore at the end of December 2024, down from TK. 11,603.1 crore in June 2024. Furthermore, the excess reserves for these banks decreased to TK. 5,508.3 crore at the end of December, compared to TK. 6,901.6 crore in June.

Chart 17: Development in Nominal Interest Rates Spread



Source: Bangladesh Bank

Chart 18: Yields on Government Securities



Source: Bangladesh Bank

In the context of a tight liquidity situation in the local market, there was an increase in the nominal interest rate spread (see Chart 17). Specifically, the weighted average nominal lending rate rose from 11.52 percent in June 2024 to 11.84 percent in December 2024. At the same time, the weighted average nominal deposit rate also experienced an increase, reaching 6.01 percent in December 2024, up from 5.49 percent in June 2024. Notably, long-term interest rates are now lower than short-term interest rates (refer to Table 1), indicating that inflation expectations for the future are comparatively lower.

Table 1: Interest Rate Structure of the Banking Sector (%)

Category	FY23 (Jun-23)	FY24 (Jun-24)	FY25 (Dec-24)
Advance Rates (%)			
Large Industries	7.23	11.58	11.88
SME	6.99	11.80	12.17
Agricultural Credit	7.48	11.48	11.74
Deposit Rates (%)			
Less than one year (FDR)	6.56	8.72	9.42
1 to 3 year (FDR)	6.71	8.39	9.41
3 year and above (FDR & DPS)	7.62	8.60	8.90

Source: Statistics Department, Bangladesh Bank.

Yields on the government securities in December 2024 were lower than those of the end June 2024. The yield curve shows the interest rates (yields) on government securities for a particular day against their maturities of 91-day, 182-day, 364-day, 2-year, 5-year, 10-year, 15-year, and 20-year. Chart 18 represented the lower interest rates of T-bills and T-bonds, which stemmed from higher investment demand from banks, non-banks, and individuals. The downward shift of the yield curve by more than 150 basis points between December 2024 and January 2025 at the short end is particularly noteworthy.

2.6 External Sector Developments

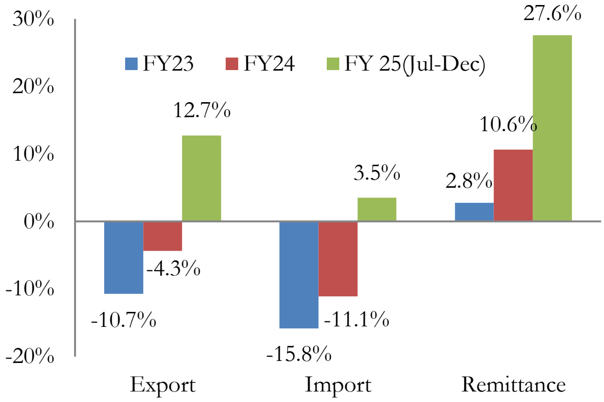
The external sector experienced a notable turnaround in the first half of the fiscal year 2025 (H1FY25), supported by ongoing domestic monetary tightening, fiscal consolidation, exchange rate adjustments, strong remittance inflows, robust export growth, and a downward revision of policy rates in most advanced and emerging market economies, particularly the USA. This improvement in the external position was evident in the narrowing balance of payments (BoP) deficit, the recovery of foreign exchange reserves, and stabilization of the exchange rate.

According to the latest available data, the external current and financial account balances witnessed remarkable improvements, both turning to surplus positions compared with large deficits recorded earlier. Driven by a surge in remittance inflows and strong export growth, the current account balance (CAB) registered a surplus of USD 33 million in H1FY25 – an improvement over a deficit of USD 3.5 billion in the corresponding period of the preceding fiscal year. Notwithstanding the surplus in the current and financial accounts, due to large repayments of past arrears accumulated in the past, the overall BoP recorded a small deficit of USD 384 million in the first half of FY25, compared with a much higher overall deficit of USD 3.5 billion in the corresponding period last year.

Exports increased by 12.7 percent (year-on-year)—despite the output losses due to the July uprising and subsequent labor unrests—to USD 24.5 billion from July to December 2024, up from USD 21.8 billion in the first half of FY24. As usual, exports were largely concentrated in ready-made garments (RMG), which expanded by 12.3 percent in this timeframe.

Despite a significant depreciation of the exchange rate, tight foreign exchange liquidity conditions, and higher borrowing costs due to the strict monetary policy, overall imports showed a remarkable turnaround in H1FY25, especially in December 2024. This acceleration in import was mainly driven by strong demand for RMG-related inputs, relaxation of import restrictions, stable global commodity prices, and increased import demand ahead of Ramadan. Following a sharp downturn of 11.1 percent in FY24, imports rebounded strongly, with a 23.3 percent growth in December 2024 (year-on-year), contributing to an overall 3.5 percent growth in H1FY25. This growth in imports was broad-based.

Chart 19: Growth of Export, Import, and Remittance Inflows in FY25

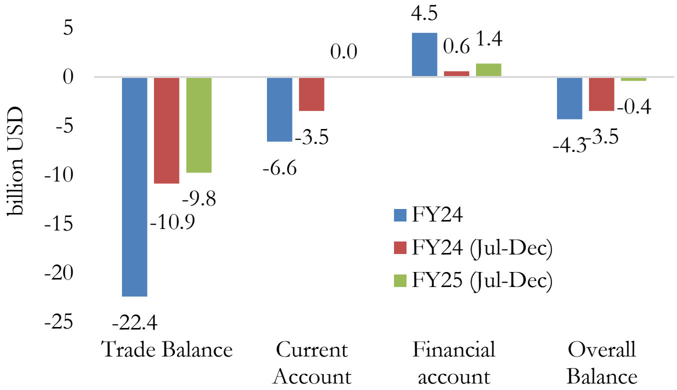


Source: Bangladesh Bank

A resurgence in remittance inflows through official channels, supported by a competitive exchange rate, government cash incentives, accessible agent banking, and mobile financial services (MFS), along with vigilant monitoring of over and under-invoicing has helped reduce pressure on the BoP. Remittance inflows surged by 27.6 percent during July to December of FY25, compared to a growth of only 2.9 percent during the same period of FY24 (Chart 19).

Similarly, a rise in inflows of medium to long-term (MLT) loans, mainly in the form of budget supports, despite a significant decrease in trade credit, led the financial account to a surplus of USD 1.4 billion in H1FY25. This was a notable improvement over a modest surplus of USD 604 million in H1FY24 (Chart 20). Improvements in the current and financial accounts have contributed to an overall reduction in the BoP deficit. The overall BoP deficit decreased to USD 384 million in H1FY25, down from the deficit of USD 3.5 billion in H1FY 24 (Chart 20). Much of the overall deficit, however, is attributable to the reduction of payments arrears in the amount of more than USD 2.0 billion accumulated before August 2024.

Chart 20: Balance of Payment



Source: Bangladesh Bank

Looking ahead, the potential for further improvement in the current account balance (CAB) is not intended due to the relaxation of import restrictions and an expected increase in imports from the anticipated recovery of economic growth. The outturn of the overall BoP will depend largely on developments in the financial account. The financial account is anticipated to regain momentum with an expected increase in FDI inflows and foreign assistance, including budget support and development project aid. However, this outlook is fraught with uncertainties and risks that lean toward the downside. Risks to sustaining remittance growth in the near future may arise from a concentrated overseas labor market, a decrease in overseas employment in the first half of FY25, and temporary bans on recruitments in specific labor markets. Political uncertainty and labor unrest in industrial areas could also negatively impact FDI and export prospects.

2.7 Movements of Exchange Rate and Foreign Exchange Reserve

Following a significant depreciation in FY24, pressure on the exchange rate has largely subsided, thanks to an improved BoP in H1FY25. To stabilize the BoP, safeguard foreign exchange reserves, and invigorate the foreign exchange market, BB has permitted greater flexibility in the exchange rate and has refrained from intervening in the interbank foreign exchange market. As a result, BB's foreign exchange reserves rebounded impressively to USD 21.4 billion by the end of December 2024, bolstered in part by foreign assistance.

The improvement in the BoP has effectively diminished pressure on the exchange rate. The nominal exchange rate of the BDT against the USD stood at 120 by the end of December 2024, reflecting only a slight depreciation of 1.7 percent in H1FY25, following a more substantial 8.2 percent drop in FY24. Additionally, the nominal effective exchange rate (NEER) showed a modest depreciation of 0.7 percent in H1FY25. In contrast, the real effective exchange rate (REER) index increased to 103, marking a noteworthy appreciation of 4.4 percent due to higher inflation rates in Bangladesh compared to its major trading partners. Consequently, the nominal exchange rate of the BDT against the USD was allowed to depreciate by 1.6 percent to BDT 122 per USD 1.0 at the beginning of January 2025, driven by market dynamics.

2.8 Capital and Bond Market

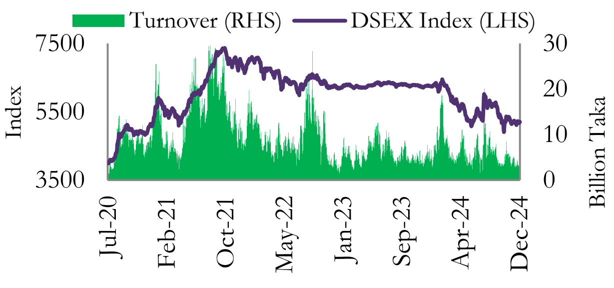
In the first half of FY25, Bangladesh's capital market experienced a tumultuous period characterized by a relentless downtrend, primarily fueled by a decline in investor confidence. The landscape grew increasingly complex following a political upheaval sparked by student-led uprisings, which prompted sweeping changes within the Bangladesh Securities and Exchange Commission (BSEC).

The newly appointed leadership at BSEC has responded with a series of assertive measures, including imposing significant fines on individuals and entities found guilty of market misconduct. In addition, they have established multiple investigative committees tasked with uncovering the underlying causes of market instability and identifying those responsible for undermining its integrity.

Beyond punitive actions, the BSEC has also formed a specialized task force with a focused mission: revitalizing the capital market, restoring investor trust, and upholding the principles of good governance. This multifaceted approach aims to stabilize the current market conditions and foster a more robust and resilient financial ecosystem that can inspire renewed confidence among investors.

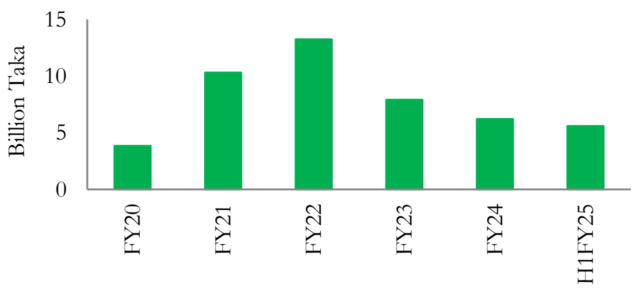
The DSEX, the benchmark index for the capital market, experienced a notable decline of 2.3 percent, falling to 5205 points by the end of December 2024, a drop from 5328 points at the end of June 2024 (Chart 21). Additionally, the average daily turnover reflected a substantial downturn, plummeting by 10.0 percent to BDT 560 crore in the first half of FY25, compared to BDT 622 crore during FY24. This decline signals a waning interest and reduced participation from investors in the market (Chart 22).

Chart 21: DSEX Index and Turnover



Source: Dhaka Stock Exchange.

Chart 22: DSE Daily Average Turnover



Source: Dhaka Stock Exchange.

3. Global Macroeconomic Development in H1FY25 and outlook for H2FY25

According to the World Economic Outlook released by the IMF in October 2024 and updated in January 2025, global GDP growth, which was 3.3 percent in 2023, is projected to decline slightly to 3.2 percent in 2024 before increasing again to 3.3 percent in 2025. This growth was anticipated to be constrained by several factors, including high borrowing costs, reduced fiscal support, structural challenges, demographic shifts, sluggish productivity growth, the prolonged Russia-Ukraine conflict, and rising geopolitical and geo-economic tensions.

For advanced economies, GDP growth was 1.7 percent in 2023 and is expected to remain steady at this level in 2024, with a modest increase to 1.9 percent in 2025. This growth will be driven by strong momentum in the United States, bolstered by robust consumption, nonresidential investment, improved export performance, and strong domestic demand in the euro area.

Emerging markets and developing economies are expected to slow down, with growth projected to decrease from 4.4 percent in 2023 to 4.2 percent in 2024 and 2025. This slowdown is primarily attributed to ongoing weaknesses in China's real estate sector, low consumer confidence, and the fading of pent-up demand in India that had built up during the pandemic. However, in South Asia, India is predicted to sustain robust GDP growth, exceeding 6.0 percent by 2025. Conversely, Bangladesh's growth forecast has been downgraded due to the continued impact of political unrest experienced during July and August of 2024, as detailed in Table 2.

Table 2: Overview of Global Economic Growth

(YoY % change)

Region	Growth			
	Actual		Projection	
	2022	2023	2024	2025
World	**3.6**	**3.3**	**3.2**	**3.3**
Advanced Economies	2.9	1.7	1.7	1.9
USA	2.5	2.9	2.8	2.7
Euro Area	3.3	0.4	0.8	1.0
Other Advanced Economies	3.3	1.9	2.0	2.1
Emerging Market and Developing Economies	4.0	4.4	4.2	4.2
China	3.0	5.2	4.8	4.6
Indonesia	5.3	5.0	5.0	5.1
Vietnam	8.1	5.0	6.1	6.1
South Asia				
Bangladesh	7.1	5.8	5.4	4.5
India	7.0	8.2	6.5	6.5
Pakistan	6.2	-0.2	2.4	3.2

Source: World Economic Outlook, October 2024 and updated in January 2025, International Monetary Fund.

In Asia and the Pacific, inflation has decreased and remains significantly lower than in other regions. This improvement is mainly due to effective monetary tightening, temporary price controls, and subsidies, which have alleviated the impact of commodity price fluctuations. By the end of 2023, inflation in most emerging economies had already met policy targets, and other economies in this region are expected to reach these targets by 2025.

Projections suggest that inflation will continue to decline, dropping from 6.7 percent in 2023 to 5.8 percent in 2024 and further to 4.2 percent in 2025. In advanced economies, inflation is expected to decrease from 4.6 percent in 2023 to 2.6 percent in 2024 and 2.0 percent in 2025 due to falling commodity prices and the impact of stricter monetary policies. In contrast, inflation in emerging markets and developing economies is anticipated to remain relatively high at 7.9 percent in 2024 before easing to 5.9 percent in 2025, as shown in Table 3.

Table 3: Global Inflation

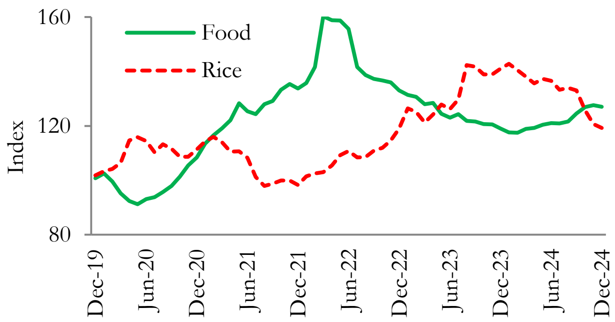
(in percent)

Region	Actual		Projection	
	2022	2023	2024	2025
World	8.7	6.7	5.8	4.2
Advanced Economies	7.3	4.6	2.6	2.0
Emerging Market and Developing Economies	9.6	8.1	7.9	5.9

Source: World Economic Outlook, October 2024 and updated in January 2025, International Monetary Fund.

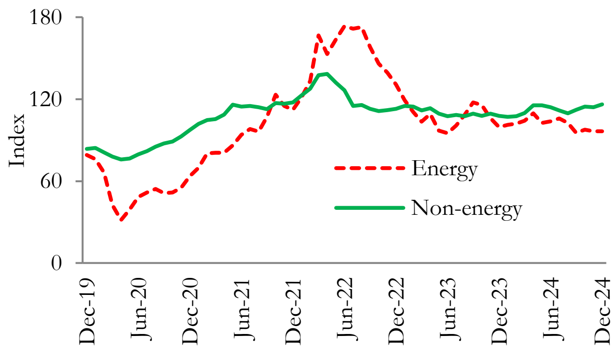
The International Monetary Fund (IMF) expects inflation to approach its targets by 2025 as global commodity and fuel prices decline. The global food price index has decreased since July 2022 and is projected to fall by 4.5 percent in 2025, driven by record global grain production. The rice price index, which has been rising since early 2022, stabilized as of January 2024 but is trending downward due to India's bumper production and resumption of rice exports (Chart 23). The energy price index has generally declined, with occasional volatility, while the non-energy commodity price index remained stable until November 2024 (Chart 24).

Chart 23: Global Food and Rice Price Indices
(Base: 2014-2016=100)



Source: Food and Agriculture Organisation.

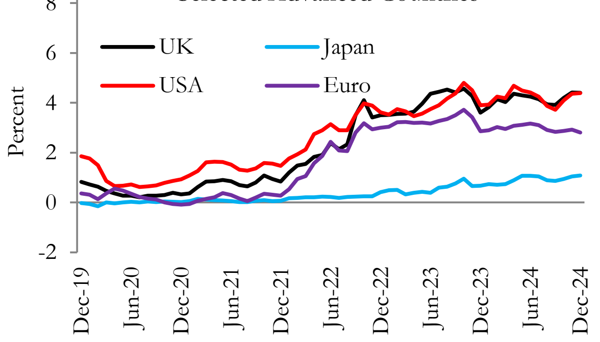
Chart 24: Global Commodity Price Indices
(Base: 2010=100)



Source: World Bank.

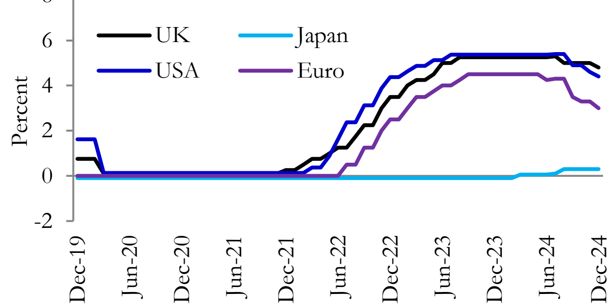
Long-term interest rates have been rising in most advanced economies since the pandemic, peaking in October 2023 due to central banks' tightening policies to control inflation. Rates showed mixed trends until September 2024 and began rising again in October 2024 (Chart 25). Except for Japan, the US, UK, and the Eurozone raised policy rates from early 2022 to August 2023. Inflation had reached policy targets in most industrial countries, and central banks paused or revoked in their tight monetary policy stance in recent months. After periods of pauses, the central banks started to cut the policy rate gradually until December 2024, except for Japan (Chart 26).

Chart 25 : Long-Term Interest Rates of Some Selected Advanced Countries



Source: Organization for Economic Co-operation and Development

Chart 26: Policy Rates of Some Selected Advanced Countries



Source: Bank for International Settlements

4. Forward-Looking Policy Initiatives

4.1 Upholding Good Governance

Bangladesh Bank has embarked on an ambitious journey to enact transformative measures to reinforce good governance within the banking sector, enhancing transparency, and ensuring accountability for financial stability. A significant aspect of these initiatives involves restructuring the Boards of Directors of eleven banks, a move that was crucial to bolstering oversight and fostering a culture of compliance, accountability, and transparency.

To facilitate more robust governance, BB has initiated regular face-to-face meetings with the banks' boards, focusing on critical issues such as liquidity management and the effective recovery of loans. This hands-on engagement strategy is designed to sharpen strategic direction and enhance decision-making processes, ultimately leading to more impactful solutions to the challenges that pervade the sector.

In a noteworthy step toward greater transparency in banking ownership, BB issued an important circular on 1 December 2024. This document introduced comprehensive guidelines on identifying the Ultimate Beneficial Owners (UBOs) and mandated the disclosure of ownership structures within banks. These guidelines require financial institutions to submit detailed ownership information in standardized reporting formats, thereby promoting clarity and accountability in bank ownership.

4.2 Banking Sector Reforms in Bangladesh

Bangladesh Bank has established three specialized task forces to further address the structural problems within the banking sector and undertaken necessary structural reforms. The first task force is dedicated to implementing comprehensive banking sector reforms, strongly emphasizing improving governance and risk management practices. The second task force aims to strengthen BB's capacity and restructure its operations with a view to enforcing the banking regulations and improving compliance. The third task force is focused on recovering stolen assets and managing the non-performing assets of banks by establishing an asset management company.

The first taskforce, called the Banking Sector Reform Taskforce (BSRTF), aims to assess banks' financial health, mitigate risks, and recommend reforms to strengthen governance and resilience within the sector. A central component of this reform initiative is the systematic implementation of Asset Quality Reviews (AQR) across the banking landscape. To facilitate this process, special regulations have been enacted permitting the engagement of foreign consulting firms.

BB has advocated introducing two pivotal laws in the legislative arena: the Bank Resolution Act and the Deposit Insurance Act (Amendment). These pieces of legislation are designed to establish a robust framework for resolving, restructuring, or liquidating the underperforming banks, directly informed by the outcomes of the AQRs. Concurrently, BB is drafting guidelines and circulars intended to delineate the procedures for deploying various bank resolution mechanisms. Additionally, the amendment of Bangladesh Bank Order 1972 and the formulation of the Distressed Asset Management Act are underway.

A pivotal initiative aims to combat money laundering and curb illicit capital flight by demonstrating our unwavering commitment to financial integrity. An inter-agency task force, spearheaded by the Governor of Bangladesh Bank, has been established to reclaim and manage laundered assets with precision and resolve. This task force works diligently alongside key authorities to identify and investigate assets unlawfully removed from the country, expertly navigate the legal complexities, and initiate proactive repatriation efforts.

To date, a number of specialized Joint Investigation Teams—comprising dedicated members from the Anti-Corruption Commission (ACC), the Criminal Investigation Department (CID) of the Bangladesh Police, the National Board of Revenue (NBR) on tax related fraud, and Bangladesh Financial Intelligence Unit (BFIU)—have strategically prioritized cases involving distinct groups and individuals. BFIU plays a crucial role in coordinating these investigations, while the Attorney General’s Office provides the much-needed legal support to strengthen our joint efforts.

In addition, the task force is actively collaborating with esteemed international organizations, including the World Bank’s StAR Initiative, the U.S. Department of Justice (USDoJ), the International Anti-Corruption Coordination Centre (IACCC) of the UK government, and the International Centre for Asset Recovery (ICAR). This global network enhances our capabilities and fosters collaborative efforts to recover stolen assets on an unprecedented scale. Together, we are committed to safeguarding our nation’s financial future and ensuring justice for the perpetrators.

A noteworthy advancement in BB's supervisory approach is the implementation of a Risk-Based Supervision (RBS) framework. Following the successful completion of a pilot program with three banks in April 2024, the initiative progressed to a second phase that involved 20 banks undergoing preliminary risk assessments. To further bolster the banking sector's resilience, BB concentrates on recovery planning for certain struggling banks, including establishing frameworks tailored for recovery and resolution. BB has also released updated stress testing guidelines to enhance risk management practices across the sector. These guidelines encompass conventional risk categories—such as credit, market, operational, and liquidity risks—and have also integrated climate risk stress testing to address potential vulnerabilities arising from natural disasters.

4.3 Roadmap to Managing Non-Performing Loans (NPLs)

It is important to note that several banks are facing a significant liquidity crisis, worsened by rising non-performing loans (NPLs), slow deposit growth, and weak loan recovery. To help stabilize their liquidity situations, BB is allowing struggling banks to borrow from the inter-bank market under central bank guarantees. However, the increasing demand for funds has led BB to provide some of these banks with temporary liquidity support, while measures have been taken to absorb excess liquidity from the banking system by using BB bills to avoid long-term financial imbalances.

The surge in NPLs will likely to exceed 30 percent of total outstanding loans, raising serious concerns for the banking industry. Contributing factors include systemic weaknesses, regulatory gaps, and exploitative practices such as money laundering and illicit capital flight. In response, BB has introduced comprehensive guidelines aligned with international best practices for loan classification, provisioning, and recovery. BB is committed to enforcing strict regulations consistent with international best practices to improve governance. Strengthening regulatory oversight and effectively implementing these reforms will be crucial for restoring stability, resilience, and public trust in the country's banking sector.

The management and recovery of Non-Performing Loans (NPLs) are paramount priorities for BB in its efforts to ensure the financial stability and resilience of the banking sector. The BB has emphasized the necessity for solid credit risk management policies and tools that comply with Basel III requirements. Accordingly, the Expected Credit Loss (ECL) methodology-based provisioning system is scheduled for implementation in 2027, in alignment with the International Financial Reporting Standard (IFRS 9). This ECL model incorporates historical data, current economic conditions, and future forecasts, thus enabling banks to engage in proactive credit risk management and mitigate the accumulation of NPLs.

In the context of recovering defaulted loans, particularly those in legal proceedings within the Artha Rin Adalat and higher courts, BB has issued a policy directive highlighting the essential role of commercial banks' legal departments. This directive underscores the need for these departments to expedite the resolution of such cases to enhance overall banking efficiency and effectiveness in managing credit risk.

4.4 Enhancing Financial Inclusion and Cashless Society

Bangladesh Bank has set an ambitious goal of achieving 75 percent cashless transactions by 2027 as part of its initiative to foster a cashless society while implementing the National Financial Inclusion Strategy for the country. To this end, BB is proactively advancing several key initiatives. One significant development is facilitating digital lending by creating a customer digital credit score. The bank has issued guidelines for establishing private credit bureaus and invited applications from eligible private entities. This digital credit scoring system will support embedded lending solutions, including microloans and revenue-based financing.

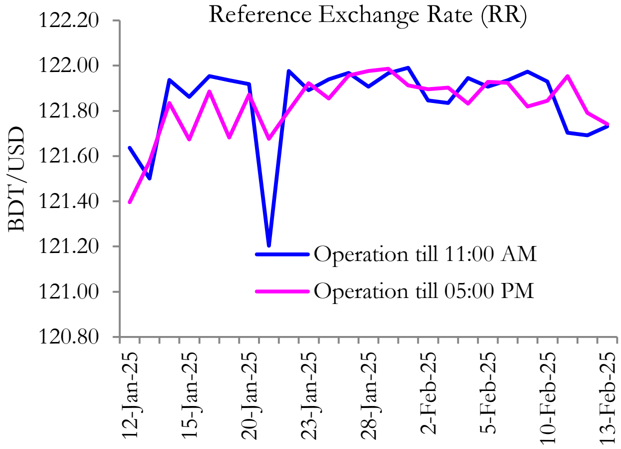
BB is also exploring implementing an open banking framework that would integrate fintech companies, traditional banks including agent banking, and mobile financial services (MFS) across digital platforms. This initiative will streamline the lending process, allowing customers, particularly micro, small, and medium enterprises (MSMEs), to apply for loans, submit necessary documentation, and monitor approval status efficiently. This approach aims to ensure smooth disbursement and repayment processes at minimal cost.

In addition, BB is focused on enhancing regulatory frameworks by adapting to emerging fintech products and services. The bank has drafted the 'E-Money Regulations' to create a secure and competitive environment for digital transactions. This legal framework will govern the issuance, utilization, and management of e-money. Moreover, BB has developed the 'Escrow Model' to bolster customer protection in online e-commerce transactions, with a view to promoting a safe and trustworthy digital financial ecosystem.

4.5 Towards Market-Oriented Exchange Rate and Build-up of Foreign Exchange Reserve

Increasing exchange rate flexibility is crucial for enhancing resilience against external shocks, safeguarding reserve buffers, and facilitating BB's move towards a more modern and proactive monetary policy. In May 2024, the BB introduced a crawling peg exchange rate regime as an interim solution before fully transitioning to a market-determined flexible exchange rate system. This crawling peg approach balances stability and flexibility within specified limits. Prior to this change, the BB had made significant adjustments to the Bangladeshi Taka (BDT) vis-à-vis the US Dollar (USD), reflecting a considerable depreciation to bring it closer to market-clearing levels and in line with the underlying Real Effective Exchange Rate (REER) levels. The central rate was adjusted twice since August 2024, and the exchange rate band was widened in August 2024 to 2.5 percent (from 1.0 percent earlier).

Chart 27: Foreign Exchange Market Spot Reference Exchange Rate (RR)



Source: FRTMD, Bangladesh Bank

On 31 December 2024, BB further advanced its efforts by issuing a circular that allows authorized dealers to buy and sell foreign currency at freely negotiable rates within the band, thereby enhancing exchange rate flexibility. BB has also begun publishing the Foreign Exchange Market Spot

Reference Exchange Rate (RR) since 12 January 2025 to support the effective functioning of the foreign exchange market. This rate, which represents a weighted average of freely quoted exchange rates within the band based on market transactions involving customers and dealers, is published twice daily: in the morning for transactions before 11:00 AM and at 6:00 PM for all day's transactions (Chart 27). BB also intends to develop an auction-based Foreign Exchange Intervention Strategy in preparation for the future exchange rate framework to ensure a consistent approach to foreign exchange interventions—an essential element in modernizing monetary and exchange rate policies. Under this strategy, interventions will occur exclusively in the spot market through buying or selling of USD.

The BB has set a maximum allowable spread of one Taka between buying and selling rates for foreign currencies to eliminate discriminatory currency practices and streamline operations. Additionally, ADs must display daily exchange rates on digital screens and prominently on their websites, ensuring transparency and accessibility for customers.

4.6 Streamlining Open Market Operations (OMOs)

Bangladesh Bank has implemented several key initiatives to optimize the functionality and efficiency of Open Market Operations (OMOs) within the interest rate targeting framework. Starting in July 2024, the bank transitioned from daily repo auctions to a bi-weekly auction schedule. Additionally, as of November 2024, BB introduced a weekly repo auction complemented by overnight fine-tuning OMOs at the conclusion of the Reserve Maintenance Period (RMP).

These adjustments are designed to encourage commercial banks to bolster their liquidity management capabilities while promoting a more dynamic and robust money market. Looking ahead, BB plans to modernize liquidity management in the banking system by adopting a single instrument at a uniform repo rate. This strategy aims to eliminate the multiplicity of instruments and disparate interest rates currently present in the money market. These measures will enable banks and non-bank financial institutions (NBFIs) to manage their liquidity positions effectively.

5. Monetary Policy Stance and Monetary & Credit Projections for H2FY25

5.1 Monetary Policy Stance for H2FY25

The global economy has demonstrated notable resilience over the past two years, despite the tightening of monetary policies implemented across the globe. Projections for global growth remain steady at approximately 3.2 percent for both 2024 and 2025, with expectations for inflation to continue its downward trajectory towards central bank targets (WEO, January 2025). However, several downside risks to inflation persist, including potential escalations in regional conflicts, prolonged tightening of monetary policies, a resurgence of financial market volatility, and inadequate fiscal consolidation in the industrial countries, which could adversely impact sovereign debt markets. Additionally, increasing protectionist trade measures worldwide remains a significant concern.

Bangladesh economy faces significant macroeconomic challenges characterized by persistently high inflation, decelerating GDP growth, exchange rate volatility, stagnant private investment, rising public debt, and alarmingly high levels of non-performing loans. BB is currently engaged in a comprehensive analysis of these global and domestic macroeconomic developments to guide its monetary policy stance and credit policy for the second half of FY25 while ensuring alignment with the government's objective of achieving a GDP growth target of 4-5 percent and maintaining inflation within the 7-8 percent range by end-FY25.

Despite some progress on the inflation front due to the various fiscal and monetary tightening measures implemented by the Government of Bangladesh (GoB) and BB, inflation still remains high at 9.94 percent. While the stance of monetary needs to remain on the tighter side, it is important to note that in the first half of FY25, the growth rate of money supply decelerated further, with private sector credit growth declining to only 7.3 percent in December 2024, marking the lowest growth rate since October 2021. Moreover, liquidity within the banking system remains constrained, with interest rates remaining high across all categories. As a result, any further adjustments to the policy rate risk exacerbating borrowing costs and potentially stifling private sector investment.

Against this background, despite the recent moderation, inflation continues to exceed the target level for end-June 2025. Therefore, BB remains steadfast in its commitment to a tight monetary policy stance for the second half of FY25.

> *Given this position, the BB has opted to maintain the policy repo rate steady at 10.0 percent. The Standing Lending Facility (SLF) and the Standing Deposit Facility (SDF) rates will also remain unchanged at 11.5 percent and 8.5 percent, respectively, with a policy rate corridor of ± 150 basis points.*

BB will persistently monitor inflation dynamics, recalibrate interest rates, and adjust liquidity measures as required. Given the current trajectory of global commodity and energy prices landscape, BB projects a steady reduction in inflation in the coming months. This expectation is bolstered by strategic fiscal and monetary synergies, through coordinated monetary-fiscal mix, a stable exchange rate, an anticipated robust 'boro' paddy harvest, and a burgeoning supply of winter-season vegetables.

BB implemented a reference-centric exchange rate mechanism on 12 January 2025 to enhance flexibility and stability within the foreign exchange market. This framework aims to facilitate the effective operation of the existing crawling peg exchange rate system while laying the groundwork for a transition to a more flexible exchange rate framework in the near future. When the overall macroeconomic environment becomes more stable, and foreign exchange reserve position improves further, BB plans to implement an intervention strategy, establish a sizable intervention fund, and move to a market-based freely determined exchange rate system. BB has also established a methodology for calculating the Foreign Exchange Spot Reference Exchange Rate (RR). This rate is defined as a weighted average of freely quoted exchange rates from market transactions involving customers and other dealers, representing a crucial step toward achieving a fully flexible exchange rate system. Prudent exchange rate management under this new system is anticipated to bolster remittance inflows, enhance foreign exchange reserves, and stimulate export activity.

The banking sector in Bangladesh has historically grappled with significant challenges, primarily stemming from loan defaults, financial irregularities, weak governance frameworks, and diminished public confidence resulting from pervasive scandals. The interim government is committed to firmly restoring discipline and rebuilding public trust in the banking system. Policy responses have begun to show improvements in FY25, particularly for the banks facing liquidity constrains. The effective implementation of ongoing initiatives, coupled with forthcoming measures and the development of robust resolutions for distressed banks based on AQR findings, will position BB to restore good governance practices and bolster stakeholder confidence in the banking system.

5.2 Monetary and Credit Projections for H2FY25

Table 4 details the semi-annual trends in broad money, its principal components, and reserve money, along with the projections for H2FY25. Within the interest rate targeting framework, explicit prioritization of monetary and credit projections is not required; however, it is crucial to synchronize the interest rate target in a manner that fosters price stability and preserves financial stability.

Control over reserve money and broad money expansion will be executed by establishing a target for the policy interest rate and managing liquidity through an interest rate corridor. This strategy aims to maintain the interbank call money rate in proximity to the policy rate, specifically within the defined policy rate corridor (Chart 14). Moreover, existing monetary policy tools will be employed to fine-tune liquidity levels, subsequently influencing the dynamics of reserve money and broad money. Fluctuations in reserve money and broad money will yield significant insights regarding their anticipated effects on inflation and broader economic activities.

Table 4: Revised Monetary and Credit Projections for FY25

(YoY % change)

Item	Actual			Projection
	Jun-24	Sep-24	Dec-24	Jun-25
Broad money	**7.7**	**7.9**	**7.6**	**8.4**
Net Foreign Assets*	-17.1	-17.2	-15.7	7.7
Net Domestic Assets	13.5	12.9	11.9	8.5
Domestic Credit	10.0	9.3	9.4	12.0
Credit to the public sector	10.5	9.7	18.1	19.8
Credit to the private sector	9.8	9.2	7.3	9.8
Reserve money	**7.9**	**9.0**	**7.3**	**1.0**
Money multiplier	4.92	5.40	5.15	5.28

Source: Bangladesh Bank. Note: *Calculated using the constant exchange rates of end June 2024.

The broad money growth projection for June 2025 is set at 8.4 percent, aligning with the revised GDP growth and inflation targets along with anticipated changes in money velocity. Given the government's adjusted borrowing parameters, public sector credit expansion is expected to hit 17.5 percent by June 2025. In contrast, private sector credit growth is estimated at 9.8 percent, reflecting in part the crowding out of the private sector credit through government borrowing and the somewhat subdued deposit growth in the banking system. Overall, domestic credit growth is projected at 11.5 percent for FY25, considering the dynamics of both public and private sector credit. In terms of the banking system's net foreign assets growth in H2 FY25, a positive increase of 7.7 percent is anticipated. This projection underpins expectations of a modest overall balance of payments surplus, driven by inflows from official multilateral development partners, sustained growth in export revenues, and remittance inflows.

6. Near-term Macroeconomic Issues and Challenges

The Bangladesh economy is undergoing a major transformation, and it will take some time for the positive impacts of various government actions to materialize fully. The current interim government's massive economic reform efforts are expected to benefit the economy in the medium to long-term. Strong domestic political support for financial sector reforms and commensurate support from international development partners, underpin the prospects for further momentum to economic recovery. These considerations notwithstanding, the near-term challenges continue to be: bringing down inflation further, maintaining exchange rate stability, sustaining the rebuilding of foreign exchange reserves, and restoring confidence in the banking system. Global economic uncertainties, coupled with domestic political uncertainties, create complex macroeconomic challenges requiring vigilance and proactive policy responses.

In FY25, economic growth is anticipated to decelerate due to output losses resulting from sudden floods in some districts of the country, labor unrests in some industrial belts, gas supply scarcity slowing industrial production, slow implementation and right-sizing of the Annual Development Programme (ADP), and disruptions in economic activities during the student-led protests. However, a rebound in domestic demand is expected, supported by higher remittance inflows along with continued rise in exports and imports.

Inflation in Bangladesh still remains above comfortable levels, despite recent improvements. Delayed and inadequate policy responses in earlier periods had contributed to this elevated inflationary outcome. Additionally, the contraction of aggregate supply due to agricultural production losses and disruptions in supply chains caused by the twin floods in August and September 2024 may have further exacerbated the inflation situation. However, a decline in global prices, a moderation of geopolitical tensions, stability in the exchange rate, and recent significant increases in policy rates should help alleviate domestic inflationary pressures in the coming months.

The recent uptick in remittances and export figures indicates a more favorable outlook for the external sector. Future export potentials may arise from the "China plus one" strategy and the imposition of additional tariffs by the US on Chinese exports could lead to diversification in sourcing by the US companies, leading in higher Bangladeshi ready-made garment (RMG) exports. Moreover, the anticipated disbursement of additional concessional loans and technical assistance from foreign governments as well as international financial institutions, will likely enhance domestic financial stability and support institutional restructuring, thereby reinforcing overall domestic macroeconomic stability.

The banking sector continues to face numerous challenges, including rising non-performing loans (NPLs), tighter liquidity conditions, and slowing deposit and credit growth. BB has set up task forces dedicated to managing and implanting banking sector reforms. The stressed banks are under close surveillance, and future actions will be determined based on the outcomes and consistent with the forthcoming Bank Resolution Act.

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