

Money and Credit

Stance of Monetary and Credit Policy

4.1 Bangladesh Bank pursued cautious but growth-supportive, inclusive and investment friendly monetary policy stances in FY16 with a view to achieving desired economic growth and maintaining inflation at a moderate level. Monetary and credit policies and programmes were designed to contain average inflation at 6.2 percent and attain output growth of 7.0 percent as per aspiration of FY16 national budget. Available data indicate attainment of key objectives of monetary and credit programmes and policies for FY16. Though broad money (M2) growth surpassed the target ceiling a bit due mainly to an extraordinary growth in net foreign assets, overall domestic credit growth remained below the target ceiling in FY16. Though government's net borrowing from the banking system ended up with an upbeat at the end of FY16; it was in a downward trend in entire period of the fiscal year which created an extra-space for the private sector and as such private sector credit grew robustly at 16.6 percent overshooting the targeted ceiling of 14.8 percent at the end of June 2016.

4.2 Strong private sector credit growth, stability in macroeconomic management along with the uninterrupted supply of gas and

Table 4.1 Money and credit situation

	(billion Taka)		
	End June 2015	End June 2016	
	Actual	Programme	Actual
1. Net foreign assets	1885.6	2094.6	2316.6
	(+21.3)	(+11.1)	(+22.8)
2. Net domestic assets (a+b)	5985.6	6957.3	6841.8
	(+9.9)	(+16.2)	(+14.3)
a) Domestic credit (i+ii)	6950.3	8025.7	7954.0
	(+10.1)	(+15.5)	(+14.4)
i) Credit to public sector ^{1/}	1204.3	1429.3	1243.9
	(-2.5)	(+18.7)	(+3.3)
ii) Credit to private sector	5746.0	6596.4	6710.1
	(+13.2)	(+14.8)	(+16.8)
b) Other items (net)	-964.7	-1068.4	-1112.2
3. Narrow money (i+ii)	1603.2		2118.3
	(+13.5)		(+32.1)
i) Currency outside banks	879.4	-	1220.7
	(+14.3)	-	(+38.8)
ii) Demand deposits ^{2/}	723.8		897.6
	(+12.5)	-	(+24.0)
4. Time deposits	6268.0		7039.5
	(+12.1)		(+12.3)
5. Broad money* (1+2) or (3+4)	7871.2	9051.9	9157.8
	(+12.4)	(+15.0)	(+16.3)

* According to monetary programme definition.

¹ "Government lending fund" is treated as deposit in calculating claims on Government (net).

² Demand deposits of monetary authority are excluded.

Note: Figures in the parentheses indicate y-o-y percentage changes.

Source: Monetary Policy Department, Bangladesh Bank.

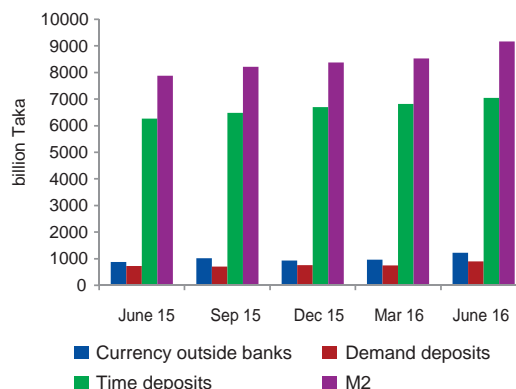
electricity throughout the year contributed to achieve 7.1 percent real GDP growth in FY16 and lifted up the country from the 6 percent GDP growth trajectory. Annual average CPI inflation contained at 5.9 percent, well below the targeted level of 6.2 percent even though the pass through of global oil price decline to consumer prices was belated and minimal. Government's domestic borrowing using the costly instrument of high yield non-bank NSD instruments was non-inflationary nearly entire FY16, though afflicting banks with a liquidity glut and Bangladesh Bank with a high sterilisation cost burden.

4.3 Partly due to subdued price levels in global commodity markets, import growth in FY16 remained slow and lagging in absorbing the inflows from workers' remittances and growing exports and foreign direct investment (FDI), Bangladesh Bank had to keep buying the market surpluses of USD inflows to ease appreciation pressures on Taka. The consequent foreign exchange reserve growth is bolstering confidence of foreign investors on the strength and stability of the Bangladesh economy.

Money and Credit Situation

4.4 Following the growth supportive stance, broad money (M2) growth was programmed at 15.0 percent where growth in net foreign assets and net domestic assets were projected at 11.1 percent and 16.2 percent respectively. Broad Money (M2) grew by 16.3 percent in FY16 against 15.0 percent targeted and 12.4 percent actual growth in FY15. Broad money growth above the targeted level can be attributed to buoyant growth in net foreign assets (NFA). Growth in NFA stood at 22.8 percent against the targeted growth of 11.1 percent for FY16. Higher growth in NFA above the target is the outcome of higher export growth along with moderate import growth. Domestic credit grew by 14.4 percent against the targeted growth of 15.5 percent for FY16 and actual 10.1 percent growth in FY15. Domestic credit grew lower than the targeted level due to lower public sector credit growth. Growth in public sector credit stood at 3.3 percent against the targeted 18.7 percent in FY16,

Chart 4.1 Components of broad money (M2)



Source: Monetary Policy Department, Bangladesh Bank.

Table 4.2 Reserve money

Particulars	(billion Taka)		
	End June 2015	End June 2016	
	Actual	Programme	Actual
Net foreign assets ¹ @	1695.1	-	2117.7
Net foreign assets ² @	1688.4	1865.8	2102.4
Net domestic assets ¹	-215.2	-	-191.7
Net domestic assets ²	-208.5	-174.2	-176.3
Domestic Credit	143.6	157.5	231.4
	(-8.4)	(+9.7)	(+61.1)
Credit to the public sector ³	95.4	105.4	187.7
	(-6.7)	(+10.5)	(+96.7)
Credit to deposit money banks ⁴	48.2	52.1	43.8
	(-11.6)	(+8.1)	(-9.3)
Other items (net)	-352.2	-331.7	-407.8
Reserve money	1479.9	1691.6	1926.0
	(+14.3)	(+14.3)	(+30.1)
Currency issued	981.5	1127.5	1323.1
	(+14.8)	(+14.9)	(+34.8)
Deposits of banks with BB ⁵	498.4	564.0	603.0
	(+13.3)	(+13.2)	(+21.0)
Money multiplier	5.32	5.35	4.76

@ Excluding foreign currency clearing account balance and offshore bank account.

¹ Calculated from monetary survey using end of period exchange rates.

² Calculated using constant exchange rates of end June 2015.

³ Government lending fund is treated as deposit in calculating net credit to Government.

⁴ Considers only loans and advances to DMBs.

⁵ Excluding foreign currency clearing account balance and non-bank deposits.

Note: Figures in the parentheses indicate y-o-y percentage changes.

Source: Monetary Policy Department, Bangladesh Bank.

while public sector credit growth was negative 2.5 percent in FY15.

4.5 An unusually high receipt of the government borrowing originated from net

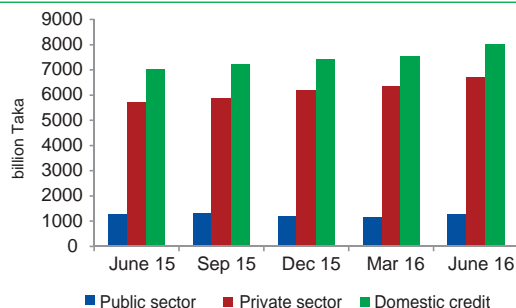
selling of national saving certificates and supernatural profit earnings by the state-owned Bangladesh Petroleum Corporation (BPC) owing to a drop in global oil prices contributed to subdued growth in public sector credit. However, credit to the private sector recorded at 16.8 percent in FY16 against the targeted growth of 14.8 percent for FY16 and actual 13.2 percent growth in FY15. BB's revised policy rates, access of foreign financing facilities at lower interest rate, subdued lending rates as well as political stability have contributed to an increase in private sector credit growth in FY16. Thus net domestic assets (NDA) in the banking system registered 14.3 percent growth in FY16 against the targeted 16.2 percent growth, while it was 9.9 percent in FY15. The monetary program vis-à-vis actual outcomes and the component of broad money are presented in Table 4.1 and Chart 4.1 respectively.

Reserve Money Developments

4.6 Reserve money (RM) has been used as an operating target to modulate liquidity consistent with the overall monetary projection. The weekly auctions of Government treasury bills and bonds usually influence the level of RM, while repo and reverse repo operations are applied for smoothing the money market.

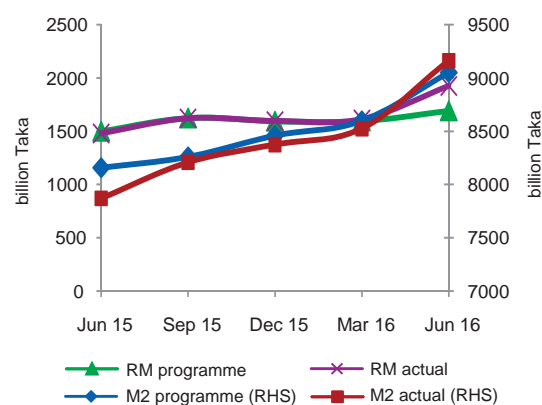
4.7 In line with the projected broad money growth, the monetary programme set a 14.3 percent growth of RM for FY16 but the actual growth was 30.1 percent. Reserve money growth was unprecedentedly higher than the

Chart 4.2 Domestic credit and its components



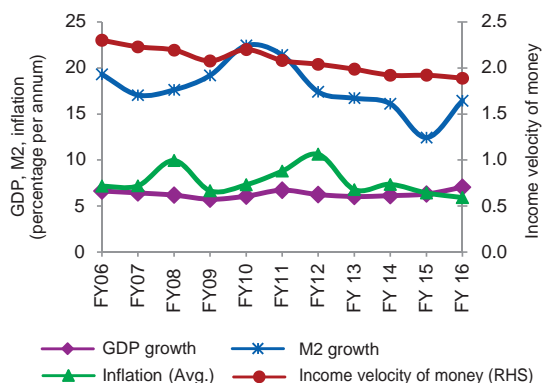
Source: Monetary Policy Department, Bangladesh Bank.

Chart 4.3 Programmes and actual developments of M2 and RM in FY16



Source: Monetary Policy Department, Bangladesh Bank.

Chart 4.4 Movement of GDP growth, M2 growth, rate of inflation and income velocity of money



Source: Monetary Policy Department, Bangladesh Bank.

target due to Bangladesh Bank's absorption of excessive flow of foreign currency from the banking system. Bangladesh Bank bought USD 4131 million from the foreign exchange market in FY16 to maintain external competitiveness of Taka against the US dollar. As a result, net foreign assets of Bangladesh Bank increased by Taka 236.6 billion and stood at Taka 2102.4 billion in FY16 against the programmed level of Taka 1865.8 billion.

4.8 On the other hand, net domestic assets stood negative at Taka 176.3 billion against the programmed level of negative Taka 174.2 billion. Domestic credit of BB registered 61.1 percent growth associated with its components where public sector credit recorded 96.7 percent growth against the programmed growth of 10.5 percent. BB's credit to the deposit money banks stood at Taka 43.8 billion in FY16 against the targeted amount of Taka 52.1 billion in FY16. Actual and programmed growth of RM during FY16 can be seen in Table 4.2.

4.9 Money multiplier decreased to 4.76 in FY16 as compared to 5.35 in FY15. Reserve-deposit ratio increased to 0.089 in FY16 from 0.086 in FY15 and currency-deposit ratio also increased to 0.154 in FY16 as compared to 0.126 in FY15. Changes in both reserve-deposit and currency-deposit ratios led to decrease in money multiplier. Movement of domestic credit and its components in FY16 are shown at Chart 4.2.

Income Velocity of Money

4.10 The income velocity of money decreased to 1.89 in FY16 from 1.92 in FY15

Table 4.3 Income velocity of money

(billion Taka)			
Year	GDP at current market prices	Broad Money (M2) (end June position)	Income velocity of money
FY10	7975.39	3630.31	2.20
FY11	9158.29	4405.20	(-7.56) 2.08
FY12	10552.04	5171.10	(-5.45) 2.04
FY13	11989.23	6035.06	(-1.92) 1.99
FY14	13436.74	7006.24	(-2.45) 1.93
FY15	15158.02	7871.20	(-3.02) 1.92
FY16	17328.64	9163.78	(-0.52) 1.89 (-1.56)

Note: Figures in parentheses indicate percentage changes over previous fiscal year.

Source: Monetary Policy Department, Bangladesh Bank.

Table 4.4 Bank credit*

(billion Taka)			
Outstanding as of	Advances	Bills	Total
30 June 15	5528.69	200.30	5728.99
	(96.50)	(3.50)	
30 Sep 15	5640.51	216.12	5856.63
	(96.31)	(3.69)	
31 Dec 15	5975.22	198.43	6173.65
	(96.79)	(3.21)	
31 Mar 16	6126.64	215.03	6341.67
	(96.61)	(3.39)	
30 June 16	6421.16	233.60	6654.76
	(96.49)	(3.51)	

* Excluding foreign bills and interbank credit.

Note: Figure in parentheses indicate percentage shares of total bank credit.

Source: Monetary Policy Department, Bangladesh Bank.

Table 4.5 Bank deposits*

(billion Taka)				
Balances as of	Demand deposits	Time deposits	Govt. deposits	Total deposits
30 June 15	723.84	6268.00	471.17	7463.00
30 Sep 15	699.16	6488.04	463.30	7650.50
31 Dec 15	752.28	6697.95	519.16	7969.40
31 Mar 16	743.04	6816.88	521.94	8081.86
30 June 16	897.59	7039.47	558.75	8495.81

* Excluding interbank and restricted deposits.

Source: Monetary Policy Department, Bangladesh Bank.

(Table 4.3). The rate of decrease in FY16 was 1.56 percent as against 0.52 percent decline in FY15. Income velocity of money was on a declining trend over the past several years indicating increased speed of transaction as a result of some other factors, which includes rapid commercial bank branch expansion and financial inclusion drives in the financial system. Movement of GDP growth, M2 growth, inflation and income velocity of money during FY06-FY16 are shown in Chart 4.4.

Bank Credit

4.11 Outstanding bank credit (excluding foreign bills and interbank items) during FY16 rose by Taka 925.77 billion or 16.16 percent to Taka 6654.76 billion as against an increase of 13.50 percent in FY15. The rise in the bank credit during FY16 was driven by both the increase in bills and advances.

4.12 Advances increased by Taka 892.47 billion or 16.14 percent in FY16, as against an increase of 13.90 percent in FY15. Bills purchased and discounted increased by Taka 33.30 billion or 16.62 percent in FY16 as compared to the increase of 3.52 percent in FY15. The quarterly position of bank credit and its components are given at Table 4.4.

Bank Deposits

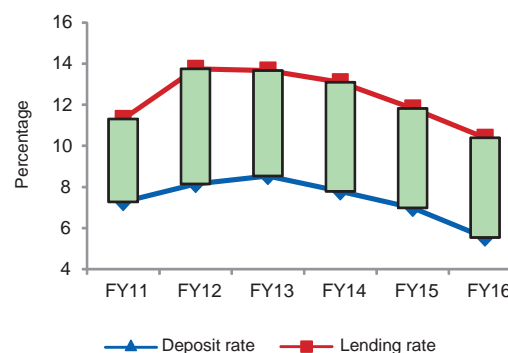
4.13 Bank deposits (excluding interbank items) increased by Taka 1032.81 billion or 13.84 percent to Taka 8495.81 billion during FY16 against 12.64 percent increase in FY15. The rise in total bank deposits was shared by all kinds of deposits. Time deposits increased

Table 4.6 Weighted average interest rates* of scheduled banks

Items	as of end June (in percent)					
	FY11	FY12	FY13	FY14	FY15	FY16
Deposit rate	7.27	8.15	8.54	7.79	6.80	5.54
Lending rate	12.42	13.75	13.67	13.10	11.67	10.39
Spread	5.15	5.60	5.13	5.31	4.87	4.85

* Excluding interbank and restricted deposits.
Source: Monetary Policy Department, Bangladesh Bank.

Chart 4.5 Weighted average interest rates of scheduled banks



Source: Monetary Policy Department, Bangladesh Bank.

by Taka 771.47 billion or 12.31 percent and stood at Taka 7039.47 billion in FY16 against growth of 12.13 percent during FY15. Demand deposits increased by Taka 173.75 billion or 24.00 percent in FY16 to Taka 897.59 billion against 12.50 percent decrease in FY15. Government deposits increased by Taka 87.58 billion or 18.59 percent to Taka 558.75 billion in FY16 against 20.14 percent increase in FY15. Quarterly position of bank deposits in FY16 may be seen at Table 4.5

Credit/ Deposit Ratio

4.14 The credit/deposit ratio of the scheduled banks, excluding the specialised

banks was 0.78 at the end of June 2016 which was 0.77 at the end of June 2015. Increasing credit to deposit ratio indicates credit growth is higher than the deposit growth.

Scheduled banks' borrowing from Bangladesh Bank

4.15 Scheduled banks' borrowings from the Bangladesh Bank increased by Taka 135.64 billion or 281.21 percent to Taka 183.88 billion at the end of June 2016 against the decrease of 12.72 percent at the end of June 2015. It may be mentioned here that scheduled banks' borrowings from the Bangladesh Bank showed higher growth in FY16 as scheduled banks' borrowings from the Bangladesh Bank under Export Development Fund (EDF) are being shown under this head since January 2016.

Balances of Scheduled Banks with the BB and their Cash in Tills

4.16 Balances of scheduled banks with Bangladesh Bank increased by Taka 104.60 billion or 20.99 percent to Taka 602.99 billion at the end of June 2016 against the increase of 13.28 percent to Taka 498.39 billion at the end of June 2015. Cash in tills of scheduled banks increased by Taka 0.18 billion or 0.17 percent to Taka 102.31 billion at the end of June 2016 against the increase of 19.08 percent to Taka 102.13 billion as of end June 2015.

Cash Reserve Requirement (CRR)

4.17 The cash reserve requirement (CRR) for the scheduled banks with Bangladesh

Bank remained unchanged at 6.50 percent of their total demand and time liabilities in FY16. It may be noted that banks are required to maintain CRR at the rate of 6.50 percent on average on a bi-weekly basis provided that the CRR would not be less than 6.00 percent in any day with effective from 24 June 2014.

Statutory Liquidity Ratio (SLR)

4.18 According to the latest amendment (2013) of subsection (2) under section 33 of the Bank Company Act, 1991, it is decided that banks should have maintained SLR separately, (a) for the conventional banks the statutory liquid assets inside Bangladesh, which also includes excess reserves with Bangladesh Bank, shall not be less than 13.0 percent of their total demand and time liabilities, and (b) for the Shariah based Islamic banks, this rate shall not be less than 5.5 percent. This became effective on 1 February 2014 and is remained unchanged in FY16.

Bank Rate

4.19 The bank rate remained unchanged at 5.0 percent in FY16 which became effective on 6 November 2003.

Interest Rates on Deposits and lending

4.20 The weighted average interest rates on deposits moved upward from FY11 to FY13. Deposit rates gradually declined from a pick of 8.54 percent in FY14 to 5.54 percent in FY16. Similarly, weighted average interest rates on lending also moved upward from

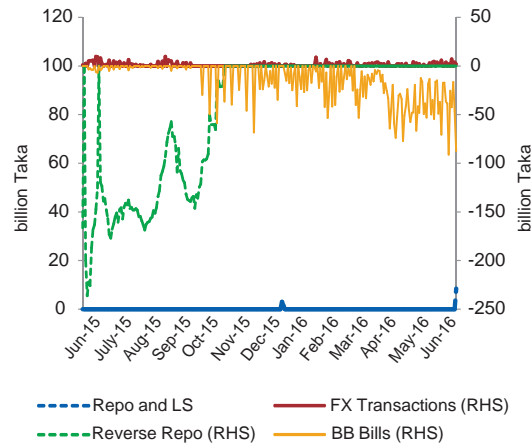
FY11 to FY12 and gradually declined from a peak of 13.75 percent in FY12 to 10.39 percent in FY16. Access of foreign financing facilities at lower interest rate, the subdued policy rate coupled with stringent loan practices by Bangladesh Bank contributed to decline in interest rates both on deposits and lending. The spreads between lending and deposit rates were above 5 percent from FY11 to FY14. The interest rate spread pulled down to 4.87 percent in FY15 and further marginally declined to 4.85 percent in FY16 following the declining trend of both lending and deposit rates. Table 4.6 and chart 4.5 contain weighted average interest rates of scheduled banks on deposits and lending along with the spread during FY11 to FY16.

Interest Rate and Liquidity Management

4.21 Borrowing and lending interest rates of banks were on a declining trend in FY16, aided by low interest foreign borrowing option kept open for input and capital equipment imports by manufacturing undertakings. Bangladesh Bank also reduced the repo and reverse repo rates by 50 basis points to 6.75 percent and 4.75 percent respectively on 14 January 2016 to align the policy rates with market rates and to stimulate investment. However, the market was still swamped with excess liquidity which induced to introduce 7-day and 14-day Bangladesh Bank Bills alongside the 30-day Bill in FY16 to effectively manage the market liquidity.

4.22 Effective transmission of monetary policy requires strengthening credit and debt

Chart 4.6 Liquidity management operations during FY16



Source: Monetary Policy Department, Bangladesh Bank.

markets. Towards enhancing effectiveness of the financial market instruments in order to smooth functioning of transmission channels for monetary policy, Bangladesh Bank's supervisory oversight on credit disbursement and loan recovery disciplines in banks and financial institutions has been intensified in FY16. In doing so, BB has given particular emphasis on risk management, internal audit and internal controls, accountability and transparency. Besides, firmly discouraging the abetting of habitual, willful repayment default; creating room for helping out recovery of genuine businesses distressed by circumstances beyond their control with realistic debt restructuring in line with international best practices. Furthermore, digital technology has been employed to investigate big financial transaction and loans in order to stop the repetition of banking irregularities.

Capital Market Situation

4.23 Bangladesh Bank's attention in support of capital market stability continued in FY16. Stock markets in Bangladesh have stabilized by now after the 2010 bubble creation and the subsequent collapse. Bangladesh Bank proactively lent hand in stabilizing the capital market, at the same time reining in banking sector's capital market exposures within global best practice norms linked to their capital bases.

4.24 The capital market in Bangladesh was mostly stable though currently somewhat anguishing from a lack of investors' confidence. The DSEX stood at 4507.6 at the end of June 2016 which is slightly lower than the level of 4583.1 in June 2015. The market capital to GDP ratio declined to 18.42 percent at the end of June 2016 from 21.45 percent of

end June 2015. The price earnings ratio of the DSE also declined to 14.61 in June 2016 from 15.90 in June 2015. Capital market authorities now needs to focus on further streamlining processes and bringing down costs in equity issuance, facilitating access of potential corporate to capital markets for raising finance.

4.25 It may be noted that the Government of Bangladesh has recently taken up an initiative of introducing long term pension savings schemes for general citizens, to be supervised by a new Pension Funds Regulator. Successful introduction of such initiative may help the financial and capital markets greatly in mobilizing long term savings for long term investments and restoring public confidence in a sustained mode.