The SLR as a Monetary Policy Instrument in Bangladesh

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Abstract

The statutory liquidity requirement (SLR), as a monetary policy instrument, has experienced infrequent changes in Bangladesh. Past evidence shows that reduction in SLR produced positive impact on bank credit and investment especially prior to the 1990s. In recent times, changes in SLR and cash reserve requirement (CRR) helped to reduce inflation to some extent in some years. Since the 1990s, Bangladesh Bank has used open market operations (OMOs), more frequently rather than changes in the Bank Rate and SLR as instruments of monetary policy in line with its market oriented approach. In this context, it should be noted that lately Bangladesh depends mostly on the money market as the channel for monetary transmission rather than changes in reserve requirements. The CRR and SLR for scheduled banks are used only in situations of drastic imbalance resulting from major shocks. The effectiveness of SLR in bringing about desired outcomes, however, depends on appropriate adjustments of other indirect monetary policy instruments such as repo and reverse repo rates.

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The SLR as a Monetary Policy Instrument in Bangladesh

The Statutory Liquidity Requirement (SLR) is one of the quantitative and powerful tools of monetary control of the central banks.[2] Changes in SLR can have a marked effect on money and credit situation of a country. If the central bank raises average reserve requirement of the commercial banks, this would create a reserve deficiency or decrease in available reserve of depository institutions. If the banks are unable to secure new reserves, they would be forced to contract both earnings and deposits which would result in a decline in the availability of credit and increase the market interest rates. The reverse would happen if the central bank lowers its reserve requirements.

The Bangladesh Bank is responsible for formulating and implementing monetary policy in the country on the basis of the Bangladesh Bank Order 1972. It provides the Bangladesh Bank with the responsibility of achieving both monetary stability (domestic price and exchange rate stability) and economic growth. The instruments that are used to control money supply and credit can be broadly classified into direct and indirect ones. Typically, direct instruments include cash reserve (CRR) and/or statutory liquidity ratios (SLR), directed credit, and administered interest rates. The indirect instruments generally operate through repurchase (repo) and reverse repo and outright transactions in government securities (open market operations).

Throughout the 1970s and 1980s, selective and quantitative control measures were widely used in Bangladesh to provide adequate credit to state owned enterprises (SOEs) and other priority sectors to achieve economic reconstruction and other development objectives. The banks were provided concessionary loans under refinance facility to lend to priority sectors like agriculture, small scale industries, housing, and export sectors. In order to create an efficient banking system in Bangladesh, a National Commission on Money, Banking, and Credit was appointed by the government to identify problems and suggest remedies. On the basis of the Commission's report, the World Bank conducted an in-depth study of the financial sector and suggested reforms to ensure safety, soundness, and efficiency of the banking sector. Based on these recommendations, the government started to implement a number of institutional and policy reform/liberalization measures since 1989/90.[3] These included: (i) decontrol of deposit and lending rates to make them flexible to meet market needs with a view to improving allocation of resources; (ii) replacement of direct credit control with indirect monetary instruments; (iii) autonomy of self-regulation by banks/financial institutions; (iv) strengthening bank supervision by the central bank; (v) establishment of appropriate accounting policies including loan classification and improvement of capital; (vi) strengthening the legal framework of debt recovery and regulations affecting financial institutions.

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[2]In terms of section 33(1) of the Bank Company Act 1991 the Statutory Liquidity Requirement (SLR) is the minimum (in percentage of total time and demand liabilities, i.e., TDTL) that a scheduled bank has to maintain in liquid assets (i.e., SLR) and a prescribed proportion of cash reserve daily of total demand and time liabilities (excluding inter-bank deposits) with the Bangladesh Bank (i.e., CRR). Specialized banks are exempted while banks guided by Islamic laws are required to keep reserve at concessional rate. In Bangladesh, SLR include (cash in till, balances with Sonali Bank Limited as agent of BB;Taka and foreign currency balances with the BB, unencumbered approved securities). Source: Department of Off-Site Supervision, BB.

[3] Report of the Financial Sector Reform Program (unpublished), Bangladesh Bank, 1990

A recent survey on monetary policy instruments in 48 developing, emerging, and developed countries observes that majority of the countries rely on money market operations for monetary policy implementation and direct instruments of monetary policy are no longer used (Buzeneca and Maino 2007). It is argued that poor performance in terms of monetary control may have acted as the contributing factor behind the abandonment of direct instruments in many of these countries. Alexander et al. (1995) depict many problems that have often been identified when direct instruments are used, including decreasing effectiveness of the instruments arising from evasion as the financial market develops and economic agents learn how to circumvent them, increasing inefficiency in resource allocation, potential inequity during implementation, and lack of credible enforcement.

In this regard, it is observed that "...*reserve requirements could also lead to disintermediation if the spread between lending and deposit rates widens as a result of its heavy use and may disrupt banks' asset/liability management. Furthermore, the imposition of statutory liquidity requirements, which obliges financial institutions to hold a certain percentage of their liabilities in the form of government securities, may also create market distortions, such as (a) constraining commercial banks' asset management, (b) distorting the pricing of government securities in the financial markets, (c) causing disintermediation and generating a loss of effectiveness to control monetary aggregates, and (d) suppressing secondary markets. Thereby, the use of the rule based instruments (e.g. SLR) in some developing countries could slow down market development considerably, which is a key institutional constraint for market-based monetary policy operations. In addition, the heavy use of the rules-based instruments may have also affected the design of the lending facility in the developing countries, causing these countries to differ from the best practices in the more advanced economies..*" (Buzeneca and Maino 2007). In this back drop this note examines the use of monetary policy instruments particularly SLR as a policy tool in Bangladesh.

The SLR was first introduced in the US in 1933 empowering the Board of Governors of the Federal Reserve System to change the member banks reserve requirements in order to control money supply and ensure soundness of the depository institutions. The central banks of all countries are empowered now to use SLR to control money and credit of the banking system. However, SLR is not free from limitations since the ratio can be altered only by law so that it cannot be used to make small adjustments in credit supply through frequent use.

It is argued that the central bank should look at both money and credit aggregates when judging a policy's impact since when both money and credit grow strongly then it is logical to think that the economy is growing strongly. However, if money and credit grow at similar rates then the central bank needs to watch credit growth rather than money growth due to its closer link with aggregate spending. It is sometimes difficult to distinguish between transmission through the money channel and credit channel following an expansionary monetary policy because bank reserves increases in both cases which in turn increases bank liabilities (deposits) and bank assets (through loan and securities). Therefore, the ultimate impact on economic activity is not easy to identify whether it is due to money channel or credit channel, or both. Under the traditional monetary view, following an expansionary monetary policy, bank reserves will increase; interest rate will fall, which will stimulate consumption and investment decisions by households and firms. This reflects adjustments in the liabilities side of the banking sector balance sheet.

According to the credit view, following an expansionary monetary policy, bank reserves will increase as well. If there is no close substitute, an increase in bank reserves will be reflected in increase in bank credit, which is an asset side of the balance sheet. This may have independent effects on economic activity. However, if there is a close substitute of bank credit, borrowers will switch from other close substitute assets (e.g., commercial paper, Treasury bill) to bank credit which will in turn increase bank credit and economic activity.

A persistent feature of the financial sector in Bangladesh is that the commercial banks suffer substantially from default loans. This is partly due to information problems in the form of moral hazard, adverse selection, or monitoring cost of commercial banks in selecting borrowers. Other factors include lack of legal action against defaulters due to various reasons and the government's policy of granting loan forgiveness discouraging the borrowers not to repay loans on time. Therefore, there is a possibility that default culture of the borrowers may force commercial banks in Bangladesh toward credit rationing and thus prevent the interest rate from falling following an expansionary monetary policy. As a result, bank credit, deposits and economic activity may remain unchanged or even may fall leading to insensitivity of policy through credit channel as well. A higher interest rate raises the cost of finance and reduces the borrowers' access in the loan market, which in turn reduces investment, employment and production levels (Walsh 1994). Jaffee and Russel (1976) find that higher interest rates, due to uncertainty, may attract more risky borrowers and drive low risky borrowers away. In this backdrop, change in SLR, particularly cash reserve requirement (CRR), may be a useful policy instrument to affect economic activity.

Adjustment of SLR in Bangladesh

In Bangladesh, the direct credit control policy was abandoned in the early 1990s and Bangladesh Bank (BB) has been using open market operation (OMO), repo and reverse repo as indirect monetary policy instruments to control money supply and credit. Since then, SLR has infrequently been adjusted to increase supply of fund to reduce interest rate differential and increase investment and economic activity in Bangladesh.

Figure 1: Trends in SLR, CRR and Bank Rate
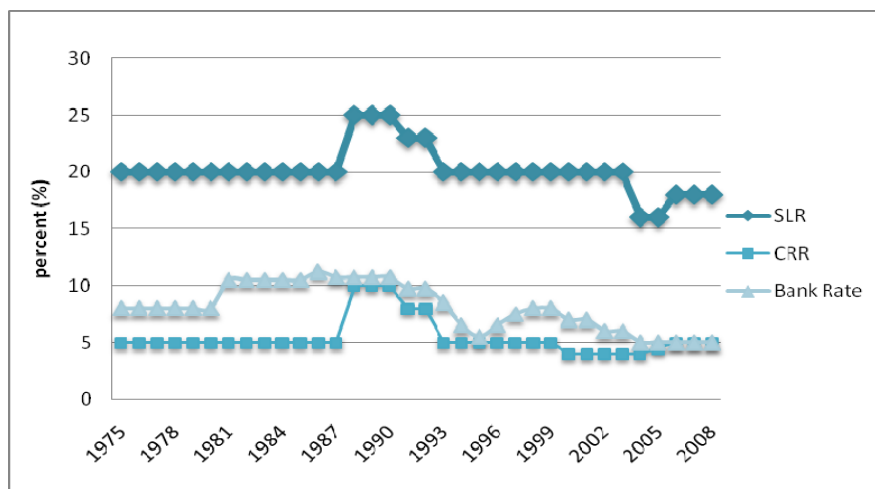
Source: Annual Reports, BB

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Figure 1 shows the movements of SLR, CRR and the Bank Rate since 1975. Banks were required until mid 1980s to maintain 5 percent of their total demand and time deposit liabilities as CRR and 20 percent of total liabilities as SLR. In October 1987, the SLR was raised to 25 percent of which CRR was raised to 10 percent which continued until 1990. Thereafter the SLR of the scheduled banks was gradually reduced to 24 percent (01 April 1991); 23 percent (25 April 1991); 22 percent (05 December 1991); 21 percent (01 April 1992); 20 percent (28 May 1992); and 16 percent (08 November 2003) of total demand and time liabilities. The CRR was also adjusted to 9 percent, 8 percent, 7 percent, 6 percent, and 4 percent respectively during the period mentioned above. However, in the face of upward pressure on inflation, the monetary policy stance changed significantly in September 2004. The Bangladesh Bank responded by tightening the monetary policy and revised CRR for the scheduled banks from 4 percent to 4.5 percent of their demand and time liabilities effective from 01 March 2005 increasing further to 5 percent on 01 October 2005. The SLR was raised to 18 percent from 16 percent effective from 01 October 2005.

Table 1: The SLR and Actual Liquidity of Scheduled Banks on 04/12/2008

(In billion Taka)

| Bank Group | Required liquidity (SLR) | Cash in tills+ bal. with Sonali Bank | Tk. bal. with BB | | | F.C. bal. with BB | Unencum. approved securities | Total liquidity | Excess liquidity |
			CRR	Excess reserves	Total				
1	2	3	4	5	6=(4+5)	7	8	9	10=9-2
1. State-owned banks	128.40	7.76	35.80	1.71	37.51	0.02	172.16	217.45	89.05
(18% of TDTL									
2. Private banks	222.83	18.05	69.65	6.88	76.53	22.08	158.17	274.83	52.00
a) Other than Islami banks	188.06	14.60	52.28	2.34	54.62	13.99	144.96	227.31	39.25
(18% of TDTL)									
b) Islami banks	34.77	3.45	17.37	4.54	21.92	8.09	13.20	47.52	12.75
(10% of TDTL)									
3. Foreign banks	40.33	2.93	11.20	0.29	11.50	19.99	38.32	72.73	32.41
(18% of TDTL)									
4. Specialised banks	6.77	1.18	6.47	0.49	6.96	0.95	7.39	8.06	1.29
5. Total (1+2+3+4)	398.32	29.91	123.12	9.38	132.49	43.05	376.03	573.07	174.75

TDTL= Total Demand and Time Liabilities, * BASIC Bank is allowed to maintain SLR at 18 percent. However, BSB, BKB, RAKUB and BSRS are exempted from maintaining SLR but maintained liquidity at 5 percent as CRR*.
Source: Department of Off-Site Supervision, Bangladesh Bank.

Table 1 shows the overall liquidity position of the scheduled banks on 04 December 2008. Cash in tills and the excess cash reserves with BB (totaling around 7 percent of total liquidity) are held by banks to meet immediate cash withdrawal needs of customers while the cash reserve requirement (CRR) component of the Taka balances with BB is mandatory deposit not divertible to other uses which earn no remuneration. Foreign currency balances in clearing accounts with BB are held for settlement of external transactions. The liquidity in excess of SLR, are held in approved securities which are zero risk rated earning assets being issued or guaranteed by the government.

Figure-2 shows the movements of total liquidity composition wise during September, 2005 to December 2008. It is evident from Figure-2 that banks are inclined to holding securities because those securities earn assets while cash or other deposits are non-remunerated. It could be mentioned here that Bangladesh bank increased SLR from 16 to 18 percent on October 1, 2005 which enabled banks to hold more securities thereafter.

Figure 2: Composition of Liquidity
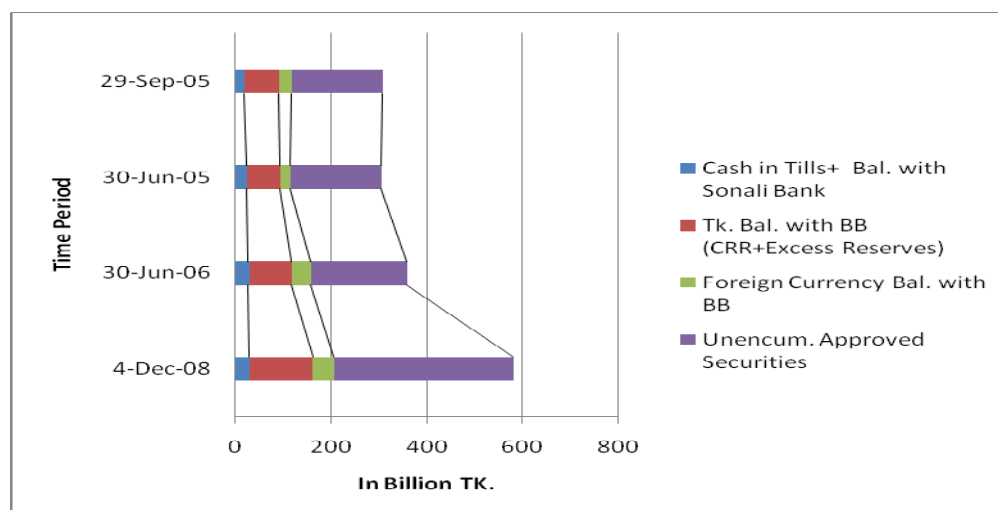
Source: Department of Off-Site Supervision, Bangladesh Bank.

Table 2: Changes of SLR, CRR and Bank Rate and Impact on Interest Rates

(percent)

Year (end June)	SLR	CRR	Bank Rate	Weighted avg. deposit rate	Weighted avg. lending rate	Interest rate differen tial	12 month avg. inflation (Base: 1995-96=100)	Real deposit rate	Real lending rate
1997	20	5	7.5	6.67	13.69	7.02	3.96	2.71	9.73
1998	20	5	8	7.07	14.02	6.95	8.66	-1.59	5.36
1999	20	5	8	7.28	14.16	6.88	7.06	0.22	7.10
2000	20	4	7	7.21	13.86	6.65	2.79	4.42	11.07
2001	20	4	7	7.03	13.75	6.72	1.94	5.09	11.81
2002	20	4	6	6.74	13.16	6.42	2.79	3.95	10.37
2003	20	4	6	6.29	12.78	6.49	4.38	1.91	8.40
2004	16	4	5	5.65	11.01	5.36	5.83	-0.18	5.18
2005	16	4.5	5	5.62	10.93	5.31	6.49	-0.87	4.44
2006	18	5	5	6.68	12.06	5.38	7.16	-0.48	4.90
2007	18	5	5	6.85	12.78	5.93	7.20	-0.35	5.58
2008	18	5	5	6.95	12.29	5.34	9.94	-2.99	2.35

Note: SLR includes CRR.
Source: *Economic Trends* and Research Department, BB.

Table-2 shows the movements of SLR, CRR, Bank Rate, interest rate, inflation, and the real rate of return since 1997. With a view to facilitating better management of the scheduled banks with

ample liquidity as well as to avoid widening of interest rate spread, a policy of downward adjustment of SLR was followed under the Financial Sector Reform Program (FSRP). It may be noted here that SLR and CRR are generally revised downward to increase funds with the scheduled banks for productive purposes and for boosting the confidence of the customers in respect to soundness of the banking system. Thus the decline of SLR and CRR was expected to create a favorable impact on the banks to expand credit. Table 1 shows that the downward adjustment of SLR and the Bank Rate in 2004 resulted in reducing the gap between lending and deposit rates which mostly continued until 2008.

Table 3 shows that the downward adjustment in SLR resulted in increases in scheduled banks' deposits, credit, investment, and liquidity position except in 2007 and 2008. In 2005, SLR and CRR were adjusted upward in the face of uptrend in inflation which resulted in increased excess liquidity due to its supply driven nature.

Year (end June)	SLR (percent)	Deposit (in billion Tk.)	Credit (in billion Tk.)	Investment (in billion Tk.)	Total required liquidity (in billion Tk.)	Total actual liquidity (in billion Tk.)	Total excess liquidity (in billion Tk.)
1990	23	204.81	190.42	22.08	46.86	48.10	1.24
1991	23	230.78	212.58	25.45	51.61	55.67	4.06
1992	20	265.61	216.06	49.12	51.99	61.26	9.27
1993	20	297.45	232.94	55.76	58.08	66.31	8.23
1994	20	339.37	240.43	59.16	66.06	91.01	21.97
1995	20	391.27	324.34	78.71	74.55	102.48	27.94
1996	20	419.33	368.65	78.19	81.14	96.78	15.64
1997	20	466.36	409.68	82.39	89.92	109.86	19.94
1998	20	518.88	464.02	90.19	99.52	122.35	22.83
1999	20	592.32	525.78	104.39	106.96	144.22	37.27
200	20	702.02	579.17	129.28	124.96	178.39	53.44
2001	20	816.04	670.91	139.40	144.13	189.04	44.91
2002	20	920.06	759.54	144.59	162.40	228.28	65.87
2003	20	1065.74	845.72	187.74	183.85	266.56	79.71
2004	16	1212.87	950.04	178.52	169.35	286.90	117.54
2005	16	1425.86	1114.71	206.43	197.17	286.90	89.72
2006	18	1689.89	126.48	188.87	255.56	351.47	95.91
2007	18	1969.56	1484.30	244.96	305.62	448.41	142.79
2008	18	2316.79	1830.73	391.59	353.93	483.82	129.88

Table 3: SLR and Scheduled Banks' Deposit, Credit and Liquidity Position

Source: *Economic Trends* and Research Department, BB

From Table 3, it is seen that because of downward adjustment of SLR and Bank Rate, the volume of excess liquidity steadily increased during the period from 1990 to 2008 (except for 1996 and 2001). Bank credit also increased to Tk 1,830.7 billion in 2008 which was Tk. 204.0

billion in 1990. Bank investment increased to Tk.391.6 billion from Tk.22.1 billion over the same period.

Table 4: Impact of SLR through the Lending Channel

(Percent)

Year (end June)	SLR	CRR	Bank Rate	Growth of bank credit	Growth of bank investment	GDP growth
1976	20	5	8	17.60	11.90	5.70
1977	20	5	8	25.30	29.10	2.70
1978	20	5	8	21.80	17.00	7.10
1979	20	5	8	28.80	22.10	4.80
1981	20	5	10.5	21.70	37.30	3.40
1982	20	5	10.5	33.10	11.30	1.20
1983	20	5	10.5	14.40	58.20	4.90
1984	20	5	10.5	36.70	46.00	5.40
1985	20	5	10.5	33.20	12.00	3.00
1986	20	5	11.25	22.00	10.10	4.30
1987	20	5	10.75	8.00	22.90	4.20
1988	25	10	10.75	18.20	-7.10	2.90
1989	25	10	10.75	19.10	10.80	2.50
1990	25	10	10.75	19.80	-5.90	6.60
1991	23	8	9.75	11.60	15.30	3.30
1992	23	8	9.75	1.60	93.00	5.00
1993	20	5	8.5	7.40	13.50	4.60
1994	20	5	6.5	3.70	6.10	4.10
1995	20	5	5.5	17.80	33.10	4.90
1996	20	5	6.5	18.10	-0.70	4.60
1997	20	5	7.5	11.40	5.40	5.40
1998	20	5	8	12.90	9.50	5.20
1999	20	5	8	12.90	15.70	4.90
2000	20	4	7	10.30	23.90	5.90
2001	20	4	7	16.50	7.80	5.27
2002	20	4	6	14.10	3.10	4.42
2003	20	4	6	13.50	10.80	5.26
2004	16	4	5	14.50	3.40	6.27
2005	16	4.5	5	17.33	15.64	5.96
2006	18	5	5	16.31	-8.51	6.63
2007	18	5	5	14.49	29.70	6.43
2008	18	5	5	23.34	59.86	6.21

Note: *SLR includes CRR.*
Source: *Economic Trends*, BB.

Evidence shows that the immediate effects of downward adjustment of SLR and the Bank Rate would be to enhance the cash flow of the money market in general and increase the output through both lending and cash flow channel.[4] The trends of relevant indicators are shown in Table 4 and Table 5.

Table 4 shows the growth of credit and investment was higher during the periods prior to 1987 compared with later years while Table 4 indicates that the reduction in SLR and the lending rate was generally associated with higher investment growth since 1991 (with a few exceptions) which in turn led to increased GDP growth implying that bank lending channel was more effective before 1987 while after 1990 Cash Flow Channel was more effective. It is also evidence from historical data that after 1993 Bangladesh bank kept unchanged SLR at 20 percent for ten years though CRR has been reduced by 100 basis points in 2000 to gear up economic activity by increasing available fund for lending.

Table 5: Impact of SLR through the Cash Flow Channel

(Percent)

Year (end June)	SLR	Growth of liquidity	Lending rate	Growth of bank investment	GDP growth
1991	23	15.74	14.99	15.25	3.30
1992	20	10.05	15.12	93.01	5.00
1993	20	8.24	14.39	13.53	4.60
1994	20	37.24	12.78	6.08	4.10
1995	20	12.61	12.22	33.05	4.90
1996	20	-5.56	13.41	-0.65	4.60
1997	20	13.51	13.69	5.37	5.40
1998	20	11.37	14.02	9.46	5.20
1999	20	17.88	14.16	15.74	4.90
200	20	23.69	13.86	23.85	5.90
2001	20	5.97	13.75	7.83	5.27
2002	20	20.75	13.16	3.72	4.42
2003	20	16.77	12.78	29.84	5.26
2004	16	7.63	11.01	-4.91	6.27
2005	16	0.00	10.93	15.64	5.96
2006	18	22.51	12.06	-8.51	6.63
2007	18	27.58	12.78	29.70	6.43
2008	18	7.90	12.29	59.86	6.21

Source: Economic Trends, BB.

[4] Lending channel: If SLR↓ ⇒ Bank lending ↑ ⇒ Bank investment ↑ that will↑ Y (output).
 Cash flow channel: If SLR↓ ⇒ Cash flow of bank ↑ ⇒ Interest rate ↓ ⇒ Bank investment ↑ that will ↑ Y (output).

Monetary Transmission through Money Market

Bangladesh Bank uses short term interest rates e.g., repo and reverse repo rates as indirect instruments of monetary policy which in turn affect long term rates (e.g., BGTB) and aggregate demand. The yield of long term bonds contains information on inflation expectations and thus can be used as an indicator of credibility of the central bank's commitment to low inflation. The repo and reverse repo operations are held regularly to inject liquidity and mop up excess liquidity respectively from the market to smooth money market operation and ensure liquidity management and bring stability in relation to reserve money targets. In this context, BB ensures careful use of repo and reverse repo operations along with regular auctions of treasury bills to influence the asset and liability sides of M2 which in turn impact economic activity and price levels in the real economy (MPS 2009).

Following higher commodity prices particularly of food and fuel in the international market and production loss especially in the agriculture sector due to floods and the cyclone Sidr, the inflation rate (p-t-p) peaked in December 2007 at 11.59 percent before coming down to single digit at 7.20 percent in October 2008 and further to 6.12 percent in November 2008 (Figure 3). The response of BB was to raise CRR by 50 basis points in March 2005 followed by another 50 basis point hike in October 2005. The SLR was also raised by 200 basis points in October 2005. At the same time, repos and reverse repo rates were adjusted upward to mop up excess liquidity from the money market in order to contain inflation (Figure 4).

Figure 3: Recent Trend in CPI Inflation
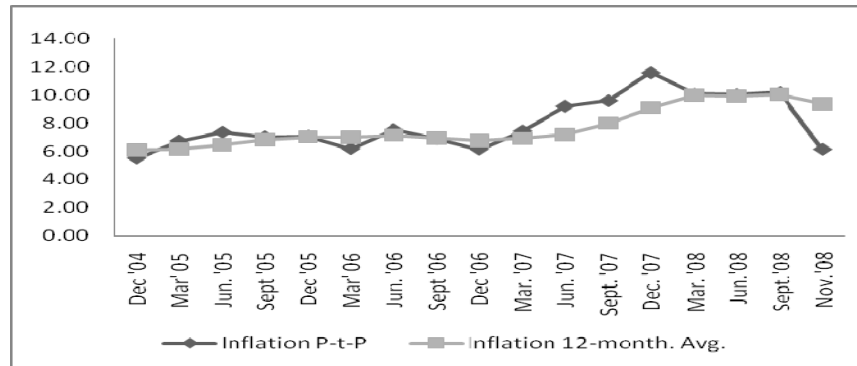
Source: Economic Trends, BB

Figure 4: Recent Changes in Repo and Reverse Repo Rates

Source: Monetary Policy Department, BB

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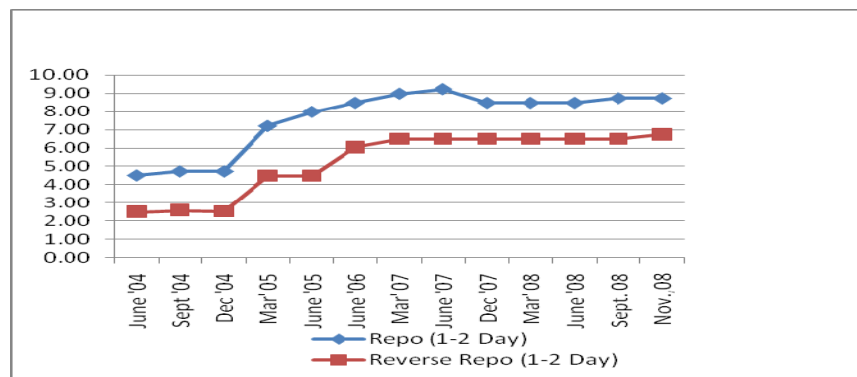
The rates of short term T. bills and long term bonds were also raised upward to avoid adverse consequences of inflation. Between March 2005 and November 2008, short term interest rates e.g., 91 day and 182 day T. bill rates increased by 2.46 and 2.34 percentage points respectively while both long term rates (5 year and 10 year BGTB) increased by 2.77 and 2.77 percentage points favoring containment of inflation and inflation expectations (Table 5). Recent data, however, show that short term interest rates increased more than the long term rates, reflecting the impact of BB's growth accommodating monetary policy stance and lower inflation expectations during the period (Table 6). On the other hand, BB's policy stance during the period emphasized on ensuring adequate credit flows to the economy's productive sectors to ease the supply situation due to damage caused by natural disasters. Figure 5 shows that the growth of broad money (M2) was higher than that of domestic credit (DC) during most of the period since July 2004 except during November 2006 to November 2007 when BB pursued cautiously restrained monetary policy due to higher episodes of inflation.

Table 5: Short Term T. Bill and Long Term BGTB Rates

(Percent)

	T. bill			BGTB	
	91 day	182 day	364 day	5 year	10 year
Mar 05	5.45	5.78	6.18	7.83	8.95
Nov 08	7.91	8.12	8.57	10.60	11.72
% point change	2.46	2.34	2.39	2.77	2.77

Source: Monetary Policy Department, BB.

Table 6: Short Term T. Bill and Long Term BGTB Rates

(Percent)

	T. bill				BGTB	
Period	28day	91 day	182 day	364 day	5 year	10 year
Jun 07	7.32	7.60	7.89	8.48	10.79	12.14
Jun 08	7.48	7.73	7.97	8.47	10.60	11.72
% point change	0.16	0.13	0.08	-0.01	-0.19	-0.42

Source: Monetary Policy Department, BB

Figure 5: Growth in M2 and Domestic Credit
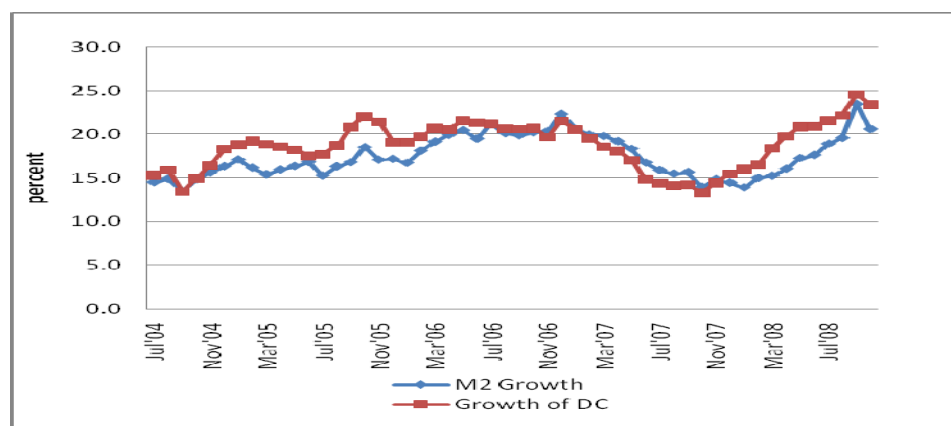
Source: Economic Trends, BB

CRR in Bangladesh and India

Like Bangladesh, SLR, CRR, OMO, and the Bank Rate are the prime monetary policy instruments in India as well as in Pakistan and Sri Lanka. Figure 6 shows the recent movements of CRR in India. The CRR started to increase since FY06 following rising global commodity prices which also fed rising inflation in India. The CRR reached a peak of 9.0 percent in September 2008 and was lowered to 6.5 percent on 17 October 2008. The CRR was reduced further to 5.50 percent on 14 November 2008. While India adjusted the CRR several times since FY06, Bangladesh changed CRR only twice during the period mainly due to the dominance of supply side factors in domestic inflation.

Figure 6: Movements in CRR in India
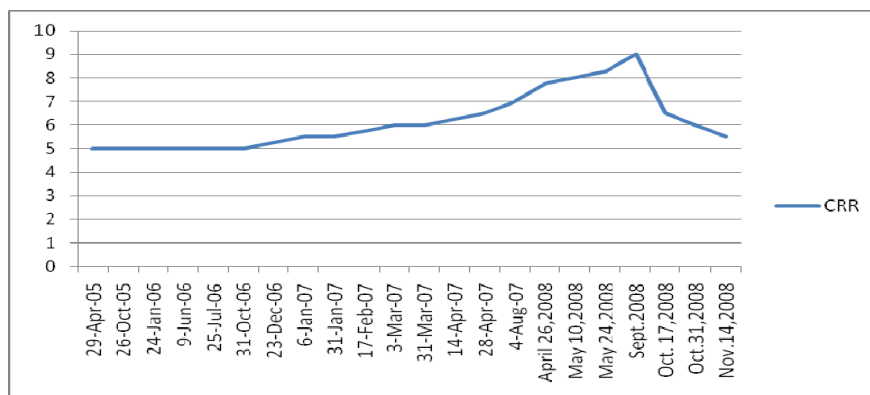
Conclusion

This policy note has examined the SLR as a monetary policy instrument in Bangladesh. Although the SLR experienced infrequent changes since the 1970s, evidence shows that the reduction in SLR produced positive impacts on bank credit and investment especially prior to the 1990s. After the FSRP that was initiated in 1990, the direct credit control policy was abandoned and since then Bangladesh Bank (BB) has been using OMOs as indirect monetary policy instruments to control money supply and credit in Bangladesh. In recent times, changes in SLR and CRR helped to reduce inflation to some extent in FY05 and FY06. The SLR also helps to reduce interest rate differentials which in turn help to increase investment and economic activity.

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