# Money and Credit

## Performance of Monetary and Credit Policy in FY20

4.1 The monetary policy stance and monetary programme for FY20 was drawn-up with the dual objectives of maintaining price stability and supporting inclusive, equitable, and environmentally sustainable economic growth. Monetary policy stance and monetary programmes for FY20 were cautiously accommodative for all growth support needs with the target of attaining GDP growth rate at 8.2 percent alongside containing CPI-based annual average inflation within the targeted ceiling of 5.5 percent.

4.2 Until February of FY20, the domestic economy of Bangladesh upheld its precise path of moderating inflation and accelerating real GDP growth supported by the broad based economic activities. The emergence of novel corona virus pandemic in the late December 2019 confounds the world to an incomprehensible halt. With the confirmation of the COVID-19 outbreak locally spread in March 2020, a serious impediment created on the achievement of the key objectives of FY20 monetary policy - keeping annual CPI average inflation within target ceiling and attaining real GDP growth at the desired rate. As a result, annual average CPI based inflation stood at 5.7 percent in FY20, slightly up from target ceiling of FY20 and actual inflation of 5.5 percent in FY19. The annual average non-food inflation, particularly relating to health care and medical expenses, and disruption of supply chains due to corona virus pandemic were largely responsible for this higher inflation. The real GDP growth also tumbled which has been provisionally estimated at 5.2 percent for FY20, significantly lower than the target as well as actual growth (8.2 percent) recorded in FY19. The real GDP growth declined in FY20 due to both supply and demand side factors owing to long and sustained worldwide lockdowns caused by COVID-19 pandemic. In the supply side, the economic activities, particularly in the manufacturing and service sectors remarkably declined in FY20. Similarly, both the domestic and external demand declined sharply as reflected in the growth of imports (-8.6 percent) and exports (-16.9 percent) in FY20.

**Table 4.1 Programme and Actual Monetary and Credit Development**

(In billion BDT)

| Particulars | End June 2019 | End June 2020 | |
|---|---|---|---|
| | Actual | Programme | Actual |
| 1. Net foreign assets | 2704.5 | 2818.2 | 2980.8 |
| | (2.1) | (4.2) | (10.2) |
| 2. Net domestic assets (a+b) | 9483.7 | 10954.5 | 10750.3 |
| | (+12.3) | (+15.5) | (+13.4) |
| a) Domestic Credit (i+ii) | 11387.1 | 13365.9 | 12943.1 |
| | (+12.4) | (+17.4) | (+13.7) |
| i) Credit to the public sector[1] | 1284.5 | 1768.2 | 1970.4 |
| | (21.7) | (+37.7) | (53.4) |
| ii) Credit to private sector | 10102.6 | 11597.7 | 10972.7 |
| | (+11.3) | (+14.8) | (+8.6) |
| b) Other items (net) | -1903.4 | -2411.4 | -2192.7 |
| 3. Narrow money (i+ii) | 2725.0 | - | 3276.4 |
| | (+7.2) | | (+20.2) |
| i) Currency outside banks | 1542.9 | - | 1921.1 |
| | (+9.5) | | (+24.5) |
| ii) Demand deposits[2] | 1182.2 | - | 1355.3 |
| | (+4.4) | | (+14.6) |
| 4. Time Deposits | 9463.2 | - | 10454.7 |
| | (+10.7) | | (+10.5) |
| 5. Broad money (1+2) or (3+4) | 12188.2 | 13772.7 | 13731.1 |
| | (+9.9) | (+13.0) | (+12.7) |

Figures in the parentheses indicate y-o-y percentage changes.
[1] This includes net credit to government and government lending fund has been treated as deposit in calculating claims on government (net).
[2] Demand deposits of monetary authority are excluded.
Source: MPD and SD, BB.

## Box 4.1 Transformation to Interest Rate-based Monetary Policy Framework

With the rapid developments in theory of monetary policy, the practice of monetary policy framework has greatly been evolved since the early 1990s. Meanwhile many central banks around the globe especially in the industrialized/developed countries have transformed their long-existed monetary policy framework mostly from the Quantity Theory based monetary aggregate targeting regime to interest rate or inflation targeting regime depending on their own status of economic and financial developments. Likewise other central banks around the world, Bangladesh Bank (BB) has its own institutional arrangement under which monetary policy decisions are made and executed. BB's current monetary policy framework is essentially a monetary aggregate targeting based on the ideology that broad money (M2) is largely determined by reserve money (RM) through money multiplier. Under this framework, broad money (M2) is considered as intermediate target and reserve money consisting of currency outside banks plus cash in tills and cash balances of the deposit money banks (DMBs) with Bangladesh Bank as operating target.

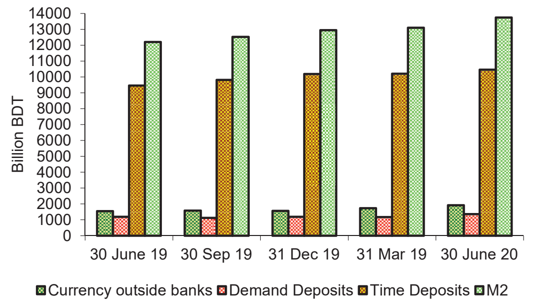
To reach its reserve money target, Bangladesh Bank controls liquidity in the market on a day-to-day basis using various indirect monetary policy tools such as auctions based repo and reverse repo operations, buying and selling of Bangladesh Bank bills including government's debt instruments comprising of various treasury bills and bonds. If required, BB sporadically uses its available direct monetary policy instruments such as change in cash reserve ratio (CRR) and or the statutory liquidity ratio (SLR) depending on the macroeconomic situation and liquidity position of banks. Bangladesh Bank also intervenes in foreign exchange market to reduce undue volatility in the exchange rate of Taka against other currencies and for maintaining export competitiveness. In addition, Bangladesh Bank uses refinancing lines and mandatory credit quotas to steer credit allocation in priority sectors of the economy, as well as a variety of regulatory measures to promote financial inclusion, inclusive growth and environmental stability.

Bangladesh has experienced a significant transformation from its agrarian based to an outward-oriented industry and service sectors based economy during the last three decades or more. With the implementation of structural adjustment policies and gradual opening of external sector, Bangladesh economy has consistently exhibited a strong real GDP growth performance in the recent years and is now proceeding towards a middle-income country status where controlling monetary aggregates by using reserve money may appear to be tricky and thus transmit of monetary policy decisions in the real sectors of the economy may be inadequate. Therefore, BB is proceeding with preparatory work for adopting a policy interest rates focused monetary policy regime in which policy interest rates exert direct impact on prices in the financial and real sectors, rather than indirectly through a monetary aggregate (broad money) as in the policy regime now in use. The intended regime is expected to quicken and heighten efficiency in transmission of intentions of monetary policy. The process of shifting current monetary policy regime may be initiated by introducing flexible monetary targeting (FMT) for gradually transformation to an interest rate targeting framework. The IMF SARTTAC is currently extending technical assistance in BB's ongoing preparatory work for transformation towards inflation targeting framework.

4.3 Although the achievements of prime objectives were slightly lower than the targets, the monetary policy stance and programme executed in FY20 were largely successful in narrowing the current account deficit of BoP from USD 5.1 billion in FY19 to USD 4.9 billion in FY20 which help to excel up the growth of net foreign assets of the banking system. Most of the monetary and credit aggregates also remained consistent with the programmed paths in FY20. Broad money (M2) growth (12.7 percent) remained very close to the target ceiling of 13.0 percent. Although credit to public sector experienced an elevated growth path as compared to its programme, domestic credit growth remained well below the programme ceiling.

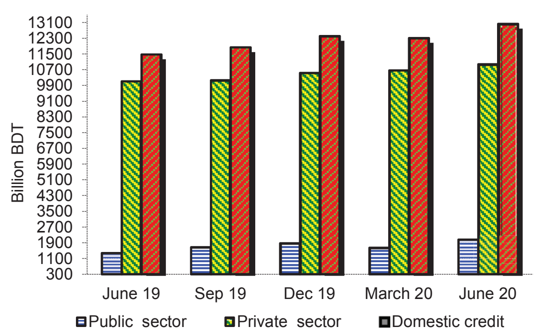
4.4 Favourable policy measures undertaken by government as well as Bangladesh Bank to boost remittance inflows, slow and steady depreciation of BDT, strict monitoring on compliance with macro prudential advance-deposit ratios and lower internal and external demand worked together well to moderate import demand and workers' remittance inflows and, thereby, contributes to reduce the current account deficit. The Government's 2.0 percent cash incentive programme and BB's initiatives of easing money transfer process along with the policy of gradual depreciation of BDT against the USD played pivotal role in augmenting remittance inflows (10.9 percent growth) in FY20. Supported by larger inflows from remittances and significant amount of surplus in financial account balance emerged from medium, long-term loans and FDI inflows, foreign exchange reserve reached to a record high of USD 36.4 billion at the end of June 2020. BB's policy measures including reducing CRR and repo rate along with providing enhanced repo and refinance facilities to banks with timely

**Chart 4.1 Movements in the Components of Broad Money (M2)**




Source: MPD and SD, BB.

**Chart 4.2 Movements in Domestic Credit and its Components**




Source: MPD and SD, BB.

intervention in the foreign exchange market helped maintain stability in both the inter-bank local currency and foreign exchange and as such BDT-USD exchange rate (month end) depreciated only by 0.5 percent at the end of June 2020. The comfortable level of foreign exchange reserve as well as stability in the exchange rate is now instilling the confidence of foreign investors on the strength and stability of the growing Bangladesh economy.

## Money and Credit Situation

4.5 To pursue the growth supportive monetary policy stance and to attain the inflation target, the growth of major anchor variables of the monetary and credit policy and programme viz. broad money (M2), reserve money and domestic credit were set to be within 13.0 percent, 12.0 percent and 17.4 percent respectively for FY20. Broad money actually grew closely to the programme level of 12.7 percent against the targeted 13.0 percent. Although credit to public sector as well as actual NFA growth outpaced the programme path, NDA remained well below the programmed level due mainly to slow growth of credit to private sector, which also helped keep broad money within the programmed level. The growth in private sector credit experienced a moderating trend throughout the whole fiscal year (FY20) initially due to the banks' adherence towards quality lending which was further aggravated by the outbreak of corona virus. Therefore, private sector credit grew by 8.6 percent against the targeted growth of 14.8 percent in FY20. The public sector credit including net credit to the government significantly grew by 53.4 percent against the programmed growth of 37.7 due mainly to slow growth of NBR revenue collection, subdued sale of national saving certificates while the government spending followed an increasing trend for the implementation of massive stimulus package to mitigate the blow of corona virus pandemic. However, domestic credit grew moderately by 13.7 percent against the targeted 17.4 percent due to slow pace in credit to private sector, the leading contributing sector to the domestic credit. The monetary and credit programme vis-à-vis their actual outcome and development of the major components of broad money are presented in Table 4.1 and Charts 4.1 and 4.2 respectively.

### Reserve Money developments

4.6 Bangladesh Bank uses reserve money (RM) as an operating target to modulate liquidity consistent with the overall monetary projection as well as keeping broad money (M2) in line with the target path to attain the price stability. Bangladesh Bank's own instruments along with government's treasury bills and bonds are used to track RM for maintaining M2 growth within the projected level.

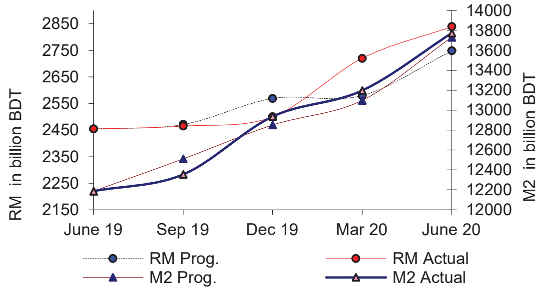
**Table 4.2 Programmed and Actual Growth of Reserve Money and its Components**

(in Billion BDT)

| Particulars | End June 2019 | End June 2020 | |
|---|---|---|---|
| | Actual | Programme | Actual |
| Net foreign assets[1/@] | 2458.8 | - | 2697.3 |
| Net foreign assets[2/@] | 2439.4 | 2474.0 | 2704.8 |
| Net domestic assets[1/] | -4.8 | - | 141.3 |
| Net domestic assets[2/] | -14.6 | 274.5 | 133.9 |
| Domestic Credit | 335.0 | 382.4 | 498.3 |
| | (41.4) | (+14.1) | (48.7) |
| Credit to the public sector[3/] | 281.5 | 328.9 | 430.4 |
| | (55.1) | (+16.8) | (52.9) |
| Credit to deposit money banks[4/] | 53.5 | 53.5 | 67.9 |
| | -(3.4) | (+0.0) | (27.0) |
| Other items (net) | -320.4 | -107.9 | -364.4 |
| Reserve money | 2454.0 | 2748.5 | 2838.6 |
| | (+5.3) | (+12.0) | (+15.7) |
| Currency issued | 1703.9 | 2020.9 | 2080.9 |
| | (+10.0) | (+18.6) | (+22.1) |
| Deposits of banks with BB[5/] | 750.1 | 727.6 | 757.7 |
| | -(3.9) | (-3.0) | (1.0) |
| Money multiplier | 4.97 | 5.01 | 4.84 |

Note: Figures in the parentheses indicate y-o-y percentage changes.
[1/] Calculated from monetary survey using end of period exchange rates.
[2/] Calculated using constant exchange rates of end June 2019.
[3/] Govt. lending fund is treated as deposit in calculating net credit to Govt.
[4/] Considers only loans and advances to DMBs.
[5/] Excluding foreign currency clearing account balance and non-bank deposits.
[@] Excluding foreign currency clearing account balance and offshore bank account.
Source: MPD and SD, BB.

**Chart 4.3 Programmes and Actual Developments of M2 and RM**



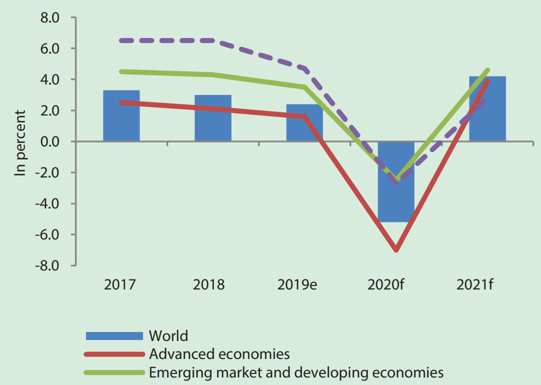

Source: MPD and SD, BB.

## Box 4.2 Policy Measures of Bangladesh Bank in Addressing Economic Fallout due to COVID-19

The outbreak of COVID-19 has created a large-scale socio-economic impact on countries around the globe. According to World Bank's Global Economic Prospects, June 2020 global GDP was expected to contract by 5.2 percent during 2020 and the pandemic is likely to have adverse effect over the coming years. This seanario can be seen from the chart; all types of economies are expected to experience slump in 2020 and recover by 2021.

COVID-19 also shook up the Bangladesh economy, GDP recorded 5.24 percent growth in FY20, which was much lower than our budgetary target of 8.20 percent. Export declined by 16.93 percent at the end of FY20 while import decreased by 8.56 percent. Domestic consumption, private investment etc. suffered setback due to lower demand and prolonged lockdown. To deal with the economic fallout due to COVID-19 Bangladesh has announced a series of stimulus packages amounting close to BDT 1.11 trillion (about 4 percent of GDP 2019), consisting of both fiscal and monetary measures. Most of the packages are composed of bank loans using bank's own capital with some support by Bangladesh Bank's refinancing schemes. With a large part of the package channeled through the banking system, banks are faced with rising demand for bank lending. To contain the negative fallout from the COVID-19 outbreak, the focus of Bangladesh Bank (BB) is to ensure that there is adequate liquidity in the financial system to support the operations of banks.

**Chart: Real GDP growth forecast**




f= forecasted
Source: World Bank

BB used its full range of tools to support the economy through the challenging time include reduction of the repo rate in two steps by 75 basis points (bps) to 5.25 percent and the cash reserve requirement (CRR) by 150 bps to 3.5 percent on a daily basis and to 4 percent on a bi-weekly average basis. CRR was cut to 1.5 percent (daily basis) and 2.0 percent (bi-weekly basis) for offshore banking operation and 1.0 percent (daily basis) and 1.5 percent (bi-weekly basis) for Non-bank Financial Institutions (NBFIs). BB expanded provision of the repo facility with a 360-day tenor special repo to support exporters, farmers and to facilitate the implementation of the government stimulus packages.BB initiates outright purchase of treasury bonds and bills from the secondary market at the market rate from banks and non-bank financial institutions after these institutions meet the statutory liquidity ratio (SLR). As some banks and financial institutions act as primary dealer of such securities, this will help ease their liquidity.

BB raised the advance/investment-deposit ratio (ADR/IDR) by 2.0 percentage points, increasing ADR to 87 percent for the conventional banks, and IDR to 92 percent for the Shariah-based Islamic banks.

Besides, BB announced a number of refinance scheme to support the flow of credit to the households and businesses. These facilities include :

**Interest payment subsidies for working capital :** Government introduced interest payment subsidies for working capital loans by banks to businesses: (i) BDT 330 billion loans to COVID-19 impacted industries and service sector firms and (ii) BDT 200 billion loans to Cottage, Micro, Small and Medium Enterprises (CMSMEs). In this connection, BB has launched two revolving refinance schemes of BDT 150 billion for (i) and BDT 100 billion for (ii) to ensure adequate liquidity of banks.

Injection of fund into EDF: Facilitation of exports by enhancing the size of BB's Export Development Fund by USD 1.5 billion to USD 5.0 billion with lower interest rates.

Pre-shipment credit refinance scheme: BDT 50 billion refinance schemes by BB to provide short-term working capital for raw materials, manufacturing, insurance and freight based on evidence of an export commitment;

Low-income professionals, farmers, and marginal/ micro-businessmen : BDT 50 billion refinancing scheme to support the working capital of small and medium farmers; and BDT 30 billion scheme to assist the COVID-19 affected low-income professionals, farmers, and marginal/ micro-businessmen.

Working capital for agricultural businesses: Introduced stimulus package of BDT 50 billion for working capital of small and medium farmers (working capital dependent agricultural business excluding crop industries e.g. horticulture, fish firm, poultry, dairy, animal husbandry).The affected customers will be able to avail up to 20 percent extra of the existing loan facilities. BB will charge only 1 percent from banks and the banks will charge 4 percent from the customers. The loan will be repayable within 18 months including 6 months grace period. BB also asked all banks to form Quick Response Team (QRT) consisting of senior officials at the headquarters so that the QRT can take quick decisions to counter issues arising from COVID-19 pandemic. For the crop sector, BB advised banks to provide agricultural loan at 4% from banks' own funds whereas BB will reimburse banks with 5% interest as subsidy.

BB also announced some foreign trade related initiatives to facilitate trade. Previously, bullet repayment was possible for raw material import by industrial units for their own use under supplier's/ buyer's credit regardless of shiptment value. Moreover, bullet repayment was possible for import amounting to USD 0.50 million or equivalent with usance period between six months to one year. Now, BB also announced that bullet payment will be permissible for other usance imports besides specified import transaction under supplier's/ buyer's credit.

In addition, BB has taken measures to defer non-performing loan classification, waive credit card fees and interests, suspend loan interest payments, impose restrictions on bank dividend payments, extend tenures of trade instruments, and ensure access to financial services. The recent BB initiative regarding formation of a credit guarantee scheme to support cottage, micro and small enterprises that lack adequate assets to pledge for bank loans is noteworthy.

With all these policy measures, BB provides a bridge by stepping in and supporting lending throughout the economy so that the COVID-19 pandemic related challenges could be recovered fast.

4.7 In line with the projected broad money growth, monetary programme is set at 12.0 percent growth of RM for FY20 while actual growth stood at 15.7 percent. Actual growth of reserve money surpasses the target due mainly to increase in net foreign assets (NFA) as well as hefty growth of credit to public sector including government. Owing to slow pace of import accompanied by strong inflows of remittances, medium and long-term loan, NFA of Bangladesh Bank increased by BDT 265.4 billion in FY20 against the programmed increase of BDT 34.6 billion. On the other hand, net domestic asset (NDA) of Bangladesh Bank increased by BDT 148.5 billion in FY20 against the programmed increase of BDT 289.1 billion. Domestic credit, the major component of NDA registered 48.7 percent growth in FY20, against the projected 14.1 percent growth for FY20. Domestic credit growth substantially increased due to increase in BB's credit to public sector along with credit to deposit money banks. BB's credit to public sector increased by BDT 148.9 billion or 52.9 percent as compared to the programmed increase of BDT 47.4 billion or 16.8 percent. BB's credit to deposit money banks also increased by BDT 14.4 billion and stood at BDT 67.9 billion at the end of June 2020 as compared to the programmed level of BDT 53.5 billion. Against the projected liability of BDT 107.9 billion, actual liability in other items (net) stood at BDT 364.4 billion at the end of June 2020. Reduction of liability in other items (net) as per the projection mainly hindrances by increasing liability in BB's capital account, government Islamic investment bond (GIIB) fund and unclassified liability. In spite of enhanced liability in other items (net), reserve money grew faster than programme level due to vigorous growth in domestic credit (DC) as well as increase in net foreign assets (NFA) of BB. Programmed and Actual growth of RM during FY20 can be seen in Table 4.2. Actual developments of M2 and RM against their respective programmed paths can also be seen in Chart 4.3.

4.8 Money multiplier decreased to 4.84 in FY20 as compared to 5.01 in FY19. Money multiplier is usually affected by the behavior of banks, individuals as well as central bank due to change in reserve-deposit ratio and currency-deposit ratio. Reserve-deposit ratio decreased to 0.077 in FY20 from 0.086 in FY19, while currency-deposit ratio increased to 0.163 in FY20 as compared to 0.145 in FY19. A rapid growth of currency holdings by the public due to the pandemic situation of corona virus led to increase in currency deposit ratio and decrease in reserve-deposit ratio which interactively contributed to decrease the size of money multiplier in FY20.

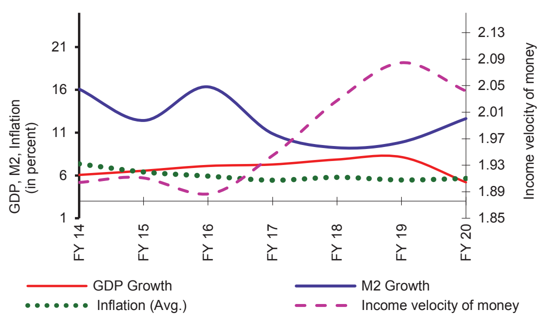
**Table 4.3 Income Velocity of Money**

(Billion BDT)

| Year | GDP at current market prices | Broad Money ($M^2$) | Income velocity of money |
|---|---|---|---|
| FY 14 | 13436.74 | 7006.24 | 1.92 (-3.52) |
| FY 15 | 15158.02 | 7876.14 | 1.92 (0.0) |
| FY 16 | 17328.64 | 9163.78 | 1.89 (-1.56) |
| FY 17 | 19758.15 | 10160.76 | 1.94 (2.65) |
| FY 18 | 22504.79 | 11099.81 | 2.03 (4.64) |
| FY 19 | 25424.83 | 12196.12 | 2.08 (2.46) |
| FY 20 | 27963.78 | 13737.35 | 2.04 (-1.92) |

Note: Figures in parentheses indicate percentage changes over previous fiscal year.
Source: MPD and SD, BB, and BBS.

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




Source: MPD and SD, BB, and BBS.

## Income Velocity of Money

4.9 The income velocity of money slightly decreased to 2.04 in FY20 from 2.08 in FY19 (Table 4.3). The income velocity of money decreased after a continued increasing trend for the previous three consecutive years, reflecting M2 growth was faster than the growth of nominal income indicating slow pace of economic activities in spite of BB's expansionary monetary policy measures taken to boost up the economy. As a result, the change of income velocity of broad money declined by 1.92 percent in FY20 against 2.46 percent increase in FY19. The magnitudes of income velocity of money and their changes during FY14-FY20 are shown in Table 4.3. Movements of the growth of GDP at current market prices, broad money (M2) growth, annual average inflation and income velocity of money during FY14-FY20 are shown in Chart 4.4.

## Bank Credit

4.10 Outstanding bank credit (excluding foreign bills and inter-bank items) in FY20 rose by BDT 898.26 billion or 8.95 percent to BDT 10940.07 billion against the increase of 11.64 percent in FY19. The rise in the bank credit occurred due to increasing of advances by banks while bills purchased and discounted by banks slightly decreased in FY20. Advances increased by BDT 964.39 billion or 9.91 percent in FY20 against the increase of 11.74 percent in FY19. Bills purchased and discounted decreased by BDT 66.13 billion or 21.63 percent in FY20 against the increase of 8.40 percent in FY19. The quarterly position of bank credit and its components are given in Table 4.4.

**Table 4.4 Quarterly Position of Bank Credit***

(In billion BDT)

| Outstanding as of | Advances | Bills | Total Credit |
|---|---|---|---|
| 30 June19 | 9736.14<br>(96.96) | 305.68<br>(3.04) | 10041.81 |
| 30 Sep 19 | 9818.47<br>(97.10) | 293.60<br>(2.90) | 10112.07 |
| 31 Dec 19 | 10230.64<br>(97.24) | 290.29<br>(2.76) | 10520.93 |
| 31 Mar 20 | 10400.98<br>(97.62) | 253.63<br>(2.38) | 10654.61 |
| 30 June20 | 10700.53<br>(97.81) | 239.55<br>(2.19) | 10940.07 |

Figure in parentheses indicate percentage shares of total bank credit.
*Excluding foreign bills and inter bank credit.
Source: MPD and SD, BB.

**Table 4.5 Quarterly Positions of Bank Deposit***

(In billion BDT)

| Balances as of | Demand deposits | Time deposits | Govt. deposits | Total deposits |
|---|---|---|---|---|
| 30 June19 | 1182.18 | 9463.18 | 827.79 | 11473.15 |
| 30 Sep 19 | 1121.79 | 9810.61 | 769.29 | 11701.69 |
| 31 Dec 19 | 1184.83 | 10184.97 | 849.84 | 12219.64 |
| 31 Mar 20 | 1167.04 | 10197.14 | 846.43 | 12210.60 |
| 30 June20 | 1355.28 | 10454.71 | 880.99 | 12690.99 |

*Excluding inter bank and restricted deposits.
Source: MPD and SD, BB.

## Bank Deposits

4.11 Bank deposits (excluding inter-bank items) increased by BDT 1217.84 billion or 10.61 percent to BDT 12690.99 billion during FY20 against 9.89 percent increase in FY19. The rise in total bank deposits was shared by all kinds of deposits. Demand deposits increased by BDT 173.11 billion or 14.64 percent to BDT 1355.28 billion in FY20 against 4.42 percent increase in FY19. Time deposits increased by BDT 991.53 billion or 10.48 percent to BDT 10454.71 billion in FY20 against 10.67 percent increase in FY19. Government deposits increased by BDT 53.2 billion or 6.43 percent to BDT 880.99 billion in FY20 against 9.2 percent increase in FY19. Quarterly position of bank deposits has been shown in Table 4.5.

### Credit/Deposit Ratio

4.12 The credit/deposit ratio of the scheduled banks excluding the specialized banks was 0.86 at the end of June 2020 which was 0.88 at the end of June 2019 (Table 4.7). Marginal decrease in credit to deposit ratio indicates that deposit growth was slightly faster than the credit growth.

### Scheduled Banks' Borrowing from BB

4.13 Scheduled banks' borrowings from the Bangladesh Bank sharply increased by BDT 149.30 billion or 42.21 percent in FY20 to BDT 503 billion at the end of June 2020 which increased by 9.40 percent in FY19. The switching over of the Government borrowing policy from non-bank sources to banking sources and an unusually high demand of cash withdrawals by the depositors due to pandemic situation of corona virus were responsible for this sharp increase of scheduled banks borrowing from the BB in FY20.

### Scheduled Banks Balances with BB and their Cash in Tills

4.14 Balances of scheduled banks with Bangladesh Bank increased by BDT 7.58 billion or 1.00 percent in FY20 and stood at BDT 757.68 billion at the end of June 2020 which increased by 3.88 percent in FY19. Cash in tills of scheduled banks decreased by BDT 1.2 billion or 0.75 percent in FY20 and stood at BDT 159.8 billion at the end of June 2020 which increased by 14.81 percent in FY19.

### Cash Reserve Requirement (CRR)

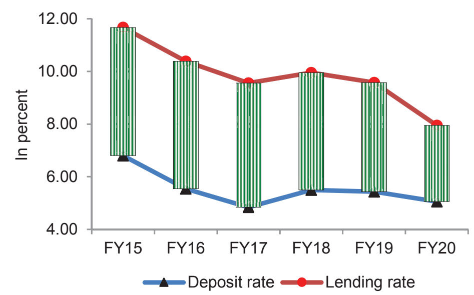
4.15 On the backdrop of economic downturn emerged from the COVID-19 pandemic, the Cash Reserve Requirement (CRR) for the scheduled banks with the Bangladesh Bank was reduced by 150 basis points in two parcels to 4.0 percent of their total demand and time liabilities to enhance adequate liquidity in the economy in FY20. It may be mentioned here that banks are required to maintain CRR at the rate of 4.0 percent on bi-weekly average basis provided that the CRR would not be less than 3.5 percent in any day with effect from 15 April, 2020.

**Table 4.6 Trends in Weighted Average Interest Rates of Scheduled Banks and their Spreads**

| Items | as of end June (percent) | | | | | |
|---|---|---|---|---|---|---|
| | FY15 | FY16 | FY17 | FY18 | FY19 | FY20 |
| Deposit rate | 6.80 | 5.54 | 4.84 | 5.50 | 5.43 | 5.06 |
| Lending rate | 11.67 | 10.39 | 9.56 | 9.95 | 9.58 | 7.95 |
| Spread | 4.87 | 4.85 | 4.72 | 4.45 | 4.15 | 2.89 |

Source: SD, BB.

**Chart 4.5 Trends in Weighted Average Interest Rates of Scheduled Banks**




Source: SD, BB.

**Table 4.7 Liquidity Indicators**

(In percent)

| As On | ADR | LCR | NSFR | Call Money Rate | Credit Deposti ratio |
|---|---|---|---|---|---|
| 30 Jun 2019 | 77.49 | 177.28 | 111.56 | 4.54 | 0.88 |
| 30 Sep 2019 | 76.58 | 187.79 | 112.70 | 5.02 | 0.86 |
| 31 Dec 2019 | 77.34 | 200.50 | 111.24 | 5.07 | 0.86 |
| 31 Mar 2020 | 77.77 | 192.55 | 109.75 | 5.17 | 0.87 |
| 30 Jun 2020 | 76.22 | 213.52 | 110.57 | 5.02 | 0.86 |

ADR and call money rate has shown in percentage.
Source: DOS, SD and MPD, BB.

## Statutory Liquidity Ratio (SLR)

4.16 According to the amendment of sub section (2) under section 33 of the Bank Company Act, 1991, it was 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, will not be less than 13.0 percent of their total demand and time liabilities, and (b) for the *shariah* based Islami banks- this rate shall not be less than 5.5 percent. This became effective on February 01, 2014 and remained unchanged in FY20.

## Bank Rate

4.17 After introduction of repo and reverse repo windows for banks on November 6, 2003; the use of bank rate became very much limited. However, BB has prudently been using bank rate mostly for providing refinance facilities to banks and penalizing them for any departure from maintenance of CRR as per set rules of BB. The bank rate remained unchanged at 5.00 percent in FY20.

## Interest Rates on Deposits and Lending

4.18 BB's efforts towards rationalization of market lending rate and enhancement of banks intermediation efficiency through reduction of spread between the deposit and lending rates continued in FY20. Both lending and deposit interest rates are seen to be following declining trends particularly towards the end of FY20. The gap between lending and deposit interest rates (interest rate spread), viewed as a measure of intermediation efficiency of banks, has also been markedly narrowed since April 2020 due mainly to BB's direction of rationalization of interest rates/profits on banks' lending and investment, with effective from 01 April 2020. Along with the reduction in the intermediation spread, both the deposits and advances have maintained growing trends in FY20 supported by the government's execution of discipline on the issuance of NSCs. Following BB's liquidity enhancing monetary policy measures as well as policy direction of interest rates/ profits on banks' lending interest rate spread (the gap between deposits and lending rates) remarkably narrowed down to 2.89 percent in FY20 from 4.15 in FY19. Table 4.6 and Chart 4.5 contain weighted average interest rates of scheduled banks on deposit and lending along with their spread during FY15 to FY20.

**Table 4.8 Excess Liquid Assets of Various bank-groups**

(in billion BDT)

| As On | State-owned Banks | Specialized Banks | Private Banks (Other than Islamic) | Islamic Banks | Foreign Banks | Total |
|---|---|---|---|---|---|---|
| 30-Jun-19 | 397.03 | 0.00 | 274.64 | 58.37 | 126.12 | 856.16 |
| 30-Sep-19 | 330.61 | 0.00 | 356.17 | 60.58 | 142.18 | 889.54 |
| 31-Dec-19 | 425.58 | 0.00 | 399.94 | 87.28 | 144.09 | 1056.89 |
| 31-Mar-20 | 368.18 | 0.00 | 340.26 | 61.63 | 129.30 | 899.37 |
| 30-Jun-20 | 546.73 | 0.00 | 556.85 | 93.52 | 198.68 | 1395.78 |

ADR and call money rate has shown in percentage.
Source: DOS and MPD, BB.

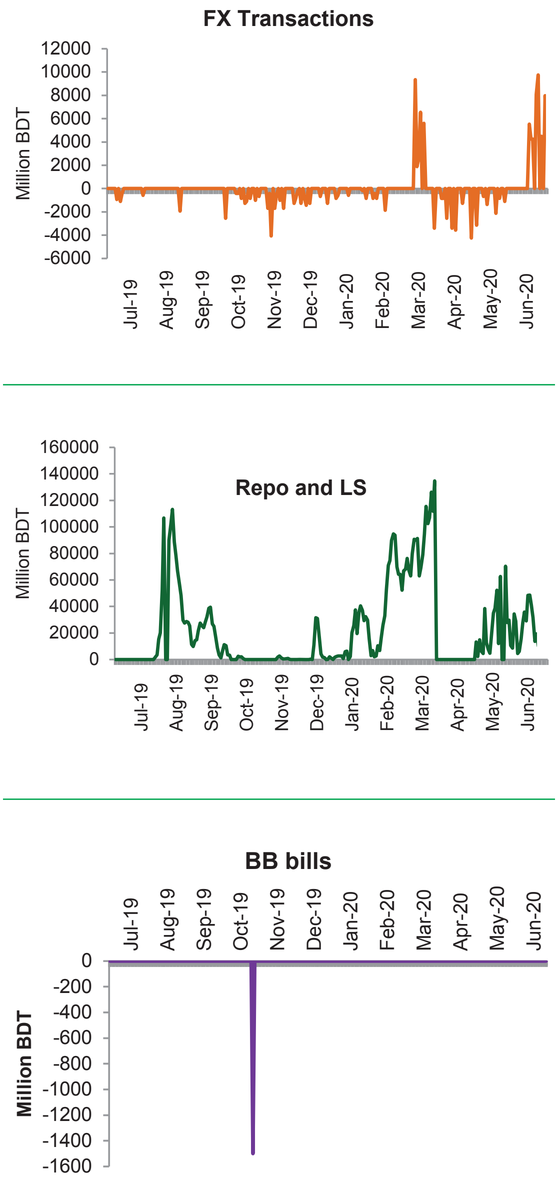
## Liquidity Management Framework

4.19 BB's current monetary policy regime is highly bonded with liquidity management especially for maintaining stability in call money rate, long-term interest rate as well as exchange rate and for promoting economic growth alongside maintaining price stability. Through controlling liquidity in the banking system by using various monetary policy instruments, BB tries to keep reserve money within the target path mostly for achieving price stability.

4.20 Lower than expected tax revenue generation and slow net sales of National Saving Certificate (NSC) forced the government to switch borrowing from non-bank to banks to meet up ADP related expenditure in FY20. As a result, credit demand in the banking system was high especially during the first half of FY20, thereby; surplus liquid assets (in excess of CRR and SLR) with banks remained at a reasonable level during that period. Moreover, in the backdrop of the COVID-19 outbreak, BB pursued various liquidity enhancing policy measures including reduction of CRR, purchase of government securities from banks and FIs, introduction of long-term repo facilities up to 360-day, along with the adoption of several refinance schemes facilitate to extend liquidity in the money market. As a result, excess liquid assets (in excess of CRR and SLR) of scheduled banks stood higher at BDT 1395.78 billion at the end of June 2020, though a lion share of this surplus liquidity holding by the banks remained in the form of government securities.

4.21 Alongside BB's ongoing expansionary policy measures, its drives of buying foreign currency from the market started during the last quarter of FY20 also helped restoring normalcy in both the money and foreign exchange markets, stabilizing the call money rate within the corridor of the repo and reverse repo rates and keeping the BDT-USD exchange rate competitive.

**Chart 4.6 Liquidity Management Operations During FY20**




Source: MPD, BB.