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Bangladesh
Economic Research

No major changes to MPS
Rate caps relaxed for consumer loans and deposits

- **Repo rate increased by 25bps:** Bangladesh Bank (BB) released its monetary policy for the second half of the fiscal year yesterday, and it seems to follow in the footsteps of the previous policy. The difficult macroeconomic conditions of accelerating inflation (+8.86% in Nov 2022) and high currency depreciation (Fig 4) have continued, and policy makers seems to be targeting inflation control which would essentially translate into a contractionary monetary policy. Accordingly, BB raised policy rates by 25bps; the repo rate will now be 6.00% and the reverse repo rate 4.25%.

- **Objective of policy rate hike to address rates mismatch:** Under the current regime of the lending rate cap, policy rate hike cannot have any impact on the real economy as the transmission mechanism is blocked off. Rather, we think the real objective of the hike was to address the growing gap between the 91-day T-bill rate and the policy rates, which left open a nice arbitrage opportunity (91-day yield was 7.45% in latest auction, compared to 5.94% in June 2022). Treasury rates have continued to push their way up as money market tightened further in the past few months (Fig 2), leaving policy makers in a tight spot amid rate caps.

- **No new commitments regarding rate caps:** While no changes were made to the lending rate cap, the relaxation on consumer loans and deposit floor were formally confirmed in this MPS. The rate on consumer loans can now vary up to 12%, and the deposit floor rate has been completely removed. While the other rate caps are here to stay for now, according to the MPS, the removal of the remaining lending rate cap will be considered under suitable economic conditions.

- **Exchange rate to conform to IMF rules:** As previously mentioned in media reporting, Bangladesh Bank has confirmed its plan to move towards a market-based, flexible and unified exchange rate regime by the end of this fiscal year. The various rates will be required to stay within a 2% variation. This is a significant change from the multiple rate regime that we had been experiencing.

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Table 1: Overview of target and actual growth rates (%)

Metric	Actual in December 22 (%)	Original target for June 23 (%)	Revised target for June 23 (%)
Inflation	8.7	-	7.5
Broad Money Growth	8.4	12.1	11.5
Domestic Credit Growth	15.1	18.2	18.5
Private Sector Credit Growth	12.8	14.1	14.1
Public Sector Credit Growth	26.6	36.0	37.7
Reserve Money Growth	17.4	9.0	14
Net Foreign Assets Growth	-22.6	-2.1	-11.9
Net Domestic Assets Growth	18.5	16.0	17.9

Figure 2: Credit growth exceeding money supply growth

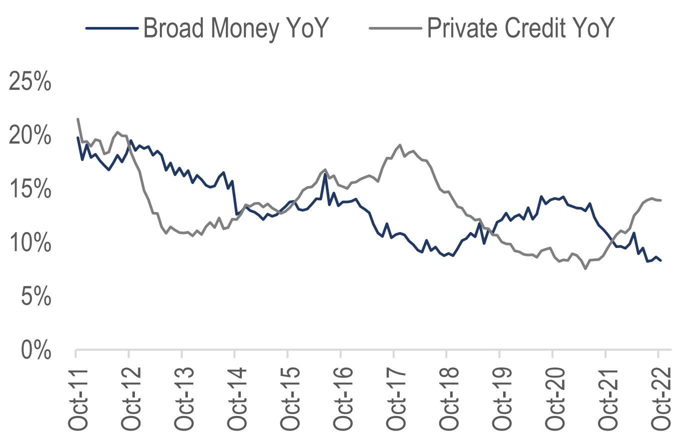


Figure 3: T-Bill yields continues to rise with liquidity on the decline

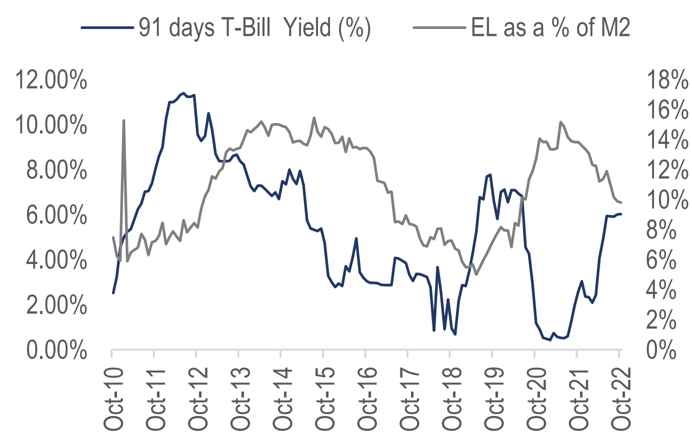


Figure 3: FX reserves falling due to external side shocks

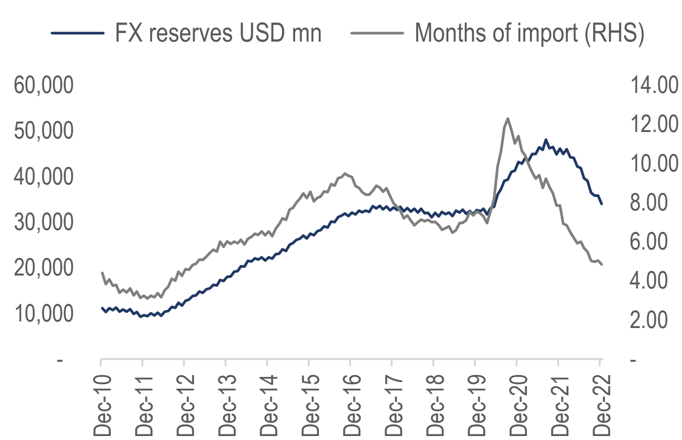
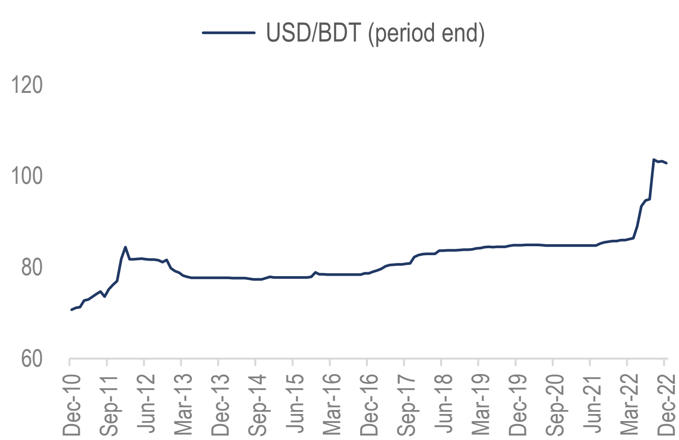


Figure 4 : Exchange rate faced steep depreciation in 1HFY23



Source: Bangladesh Bank

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