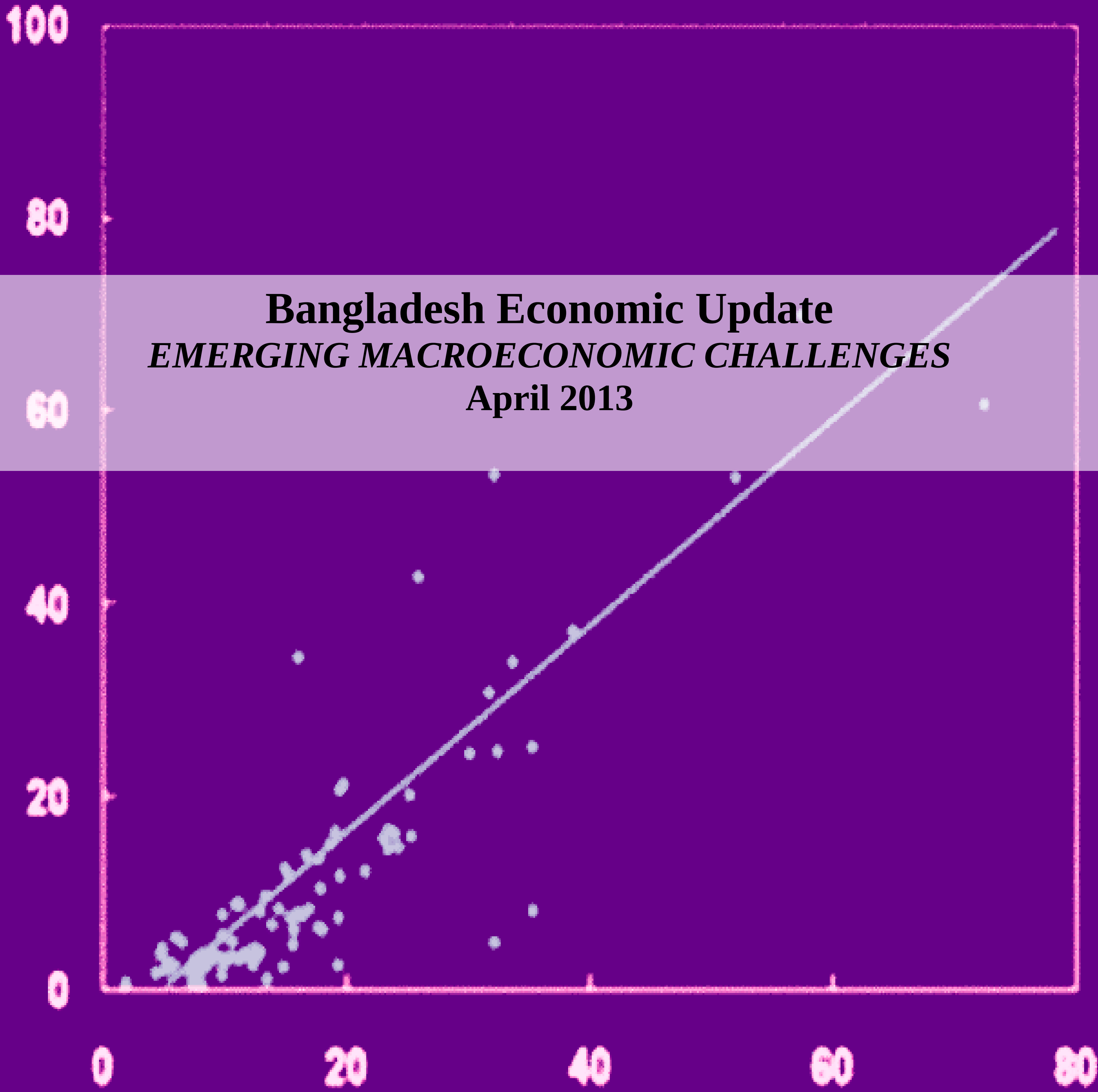

Bangladesh Economic Update

EMERGING MACROECONOMIC CHALLENGES

April 2013

উন্নয়ন অন্বেষণ
Unnayan Onneshan
The Innovators
centre for research and action on development

Bangladesh Economic Update
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Economic Policy Unit
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1. INTRODUCTION

The current issue of the Bangladesh Economic Update examines the macroeconomic challenges emerging in FY 2012-13, with an analysis on the elapsed four fiscal years under the current government by looking at the indicators mentioned at the Medium Term Macroeconomic Framework (MTMF).

The Update discusses the growth in Gross Domestic Product (GDP) and makes a projection based upon observable trends in the economy vis-à-vis the government target of 7.2 percent for the current fiscal. In doing so, it investigates into trend in saving and investment as well as effectiveness of monetary and fiscal policies of the government.

The Update discusses the growth in Gross Domestic Product (GDP) and makes a projection based upon observable trends in the economy vis-à-vis the government target of 7.2 percent for the current fiscal

It also focuses on the fiscal balances including revenue income of the government, budget deficit, deficit financing and the implementation status of the Annual Development Programme (ADP).

In understanding the macroeconomic developments, it is pertinent to comprehend the dynamics observed in the external balances including current account balance, capital account balance and overall financial balances.

There is continuity of jitters around money and capital markets, with concomitant implications emanating out of monetary policy. In MTMF, there is increasing target of rate of growth in investment but decreasing target of all kinds of money supply and credit, which is adopted for controlling inflation.

The penultimate section deliberates on the witnessed outcome in the real sector to understand as to how sectors such as agriculture, industry and services contribute to the achievement of the targeted GDP.

Finally, the impacts of IMF reforms have also been examined as the country has contracted to a three year reform programme under the Extended Credit Facility (ECF).

The impacts of IMF reforms have also been examined as the country has contracted to a three year reform programme under the Extended Credit Facility

2. THE GROWTH SCENARIO

Unnayan Onneshan projects that in FY 2012-13, the rate of growth in GDP might stand at 5.75 percent[1] whereas the targeted rate of growth of the government is 7.2 percent. The government in previous occasions has also not been able to achieve the targets. According to MTMF 08-11, the average target growth was 6.9 percent whereas the achieved rate was 5.87 percent on average. The targeted rate of growth might not be achieved due to several reasons including increasing saving investment gap, lack of farsightedness, rigidities and weaknesses of monetary and fiscal policies of the government and non-availabilities of adequate infrastructural services (detailed discussions in the following sections).

Unnayan Onneshan projects that in FY 2012-13, the rate of growth in GDP might stand at 5.75 percent whereas the targeted rate of growth of the government is 7.2 percent.

The government has continuously revised the MTMF projections of growth. This has been done at least four times (Table 1). Even the repeated changes of the target have not been achieved. In FY 2011-12, the rate of growth in GDP was 6.32 percent against the targeted 7 percent. In FY 2010-11, the rate of growth was 6.1 percent whereas this rate was 5.8 percent in FY 2009-10. In the first fiscal year of the ruling government in FY 2008-09, the projection of MTMF in growth was 6.5 but actually 5.7 percent growth was achieved, lower than 6.2 percent of FY 2007-08.

There has been deceleration in the ratio of growth in total investment to GDP during FY 2008-09 to FY 2011-12.The growth has been led by consumption. In the FY 2011-12, the share of consumption in GDP has slightly increased and reached at 80.63 percent from 79.69 percent in FY 2007-08.

Table 01: Projection of MTMF and actual rate of growth

Component	MTMF	2008-09	2009-10	2010-11	2011-12	2012-13	2012-14	2014-15
GDP Growth	MTMF 08-11	6.5	7.0	7.2				
	MTMF 09-12		5.5	6.0	6.5			
	MTMF 12-16			6.7	7.0	7.2	7.6	8
	MTMF 13-17				7.0	7.2	7.6	8
Actual Growth in GDP		5.7	5.8	6.1	6.32			

Source: Bangladesh Bank and Finance Division, Ministry of Finance, Bangladesh, 2013

[1] The results of the statistics is shown in the Appendix A

2.1 Savings and Investment

The gap between savings and investment has increased at a high rate over the time and contributes in non-achievement of the targeted level of growth in GDP. A two-way process has depressed the translation of saving into investment. The lack of matching infrastructure development by the government and the private sector due to lack of farsightedness in operating fiscal policy on the one hand and increase in cost of loanable funds due to contractionary monetary policy on the other, have suppressed investment demand. The fiscal space for infrastructure has been contracted due to increased expenditure in quick and rental power plants, heightened payment on the account of principal and interest due to mounting public borrowing (again due to quick and rental power plants) and its spiral effects on the capacity for the government to invest. At the policy level, the government's much vaunted and trusted instrument of public-private partnerships did not bring measureable progress in setting up infrastructure. The monetary policy has remained restrictive, with a prevalence of a high rate of interest, on the one hand and the high borrowing by the government has also crowded out private investment on the other.

The rate of national saving has remained approximately constant in the period of this government and has been able to fulfill the target of MTMF, though the rate of growth has slowed down

The rate of national saving has remained approximately constant in the period of this government and has been able to fulfill the target of MTMF, though the rate of growth has slowed down. The average rate of growth in national saving as percentage of GDP was 0.32 during the last four years.

In FY 2011-12, the investment was provisionally estimated to be 25.45 percent of the GDP. In case of investment, the government could not achieve the target of MTMF.

In case of investment, in FY 2001-02, the rate of total investment was 23.15 percent of GDP in which the shares of public and private sector were 6.37 and 16.78 percent respectively. The rate of national investment gradually picked up at 24.65 percent of GDP in FY 2005-06 but in FY 2006-07, this rate declined at 24.46 percent. In FY 2008-09, the rate of national investment further declined at 24.18 percent. In FY 2009-10, the investment slightly increased and reached at 25 percent of the GDP, but later, in FY 2010-11, this investment fell down further at 24.4 percent of the GDP. Finally, in FY 2011-12, the investment was provisionally estimated to be 25.45 percent of the GDP. In case of investment, the government could not achieve the target of MTMF.

Table 02: Actual investment and national savings of MTMF

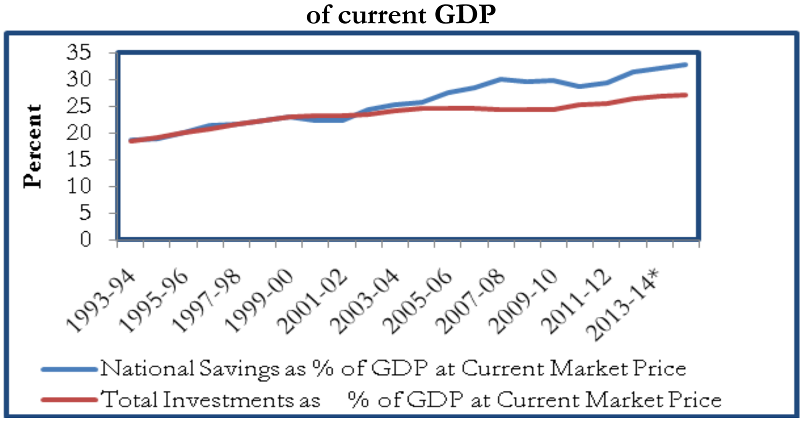
Component	MTMF	2008-09	2009-10	2010-11	2011-12	2012-13	2012-14	2014-15
Gross Investment (as percentage of GDP)	MTMF 08-11	24.4	26.3	27				
	MTMF 09-12		23.6	24.3	25.2			
	MTMF 12-16			26.5	28.8	29.6	31.0	32.5
	MTMF 13-17				25.9	26.6	28.1	29.6
Actual Investment		24.18	25.0	24.4	25.45*			
Actual National Savings		29.6	30.02	28.78	29.40*			
National Savings (as percentage of GDP)	MTMF 12-16			28.3	29.8	30.4	31.1	32.8
	MTMF 13-17				26.3	26.8	28.2	29.6

Source: Bangladesh Bank and Finance Division, Ministry of Finance, Bangladesh, 2013

The saving-investment gap might reach at 5.14, 5.47 and 5.81 percent of the nominal GDP in FY 2012-13, FY 2013-14 and FY 2014-15 successively.

Considering the same business scenario, the national savings might be 31.51, 32.18 and 32.86 percent of the nominal GDP in FY 2012-13, FY 2013-14 and FY 2014-15 successively. The total investment might be 26.37, 26.71 and 27.05 percent of the nominal GDP in FY 2012-13, FY 2013-14 and FY 2014-15 successively.[2]

Figure 01: National savings and total investment as percentage of current GDP



Source: Bangladesh Bank, 2013

The savings-investment gap has increased sharply and may continue further, if the existing policies continue. The saving-investment gap might reach at 5.14, 5.47 and 5.81 percent of the nominal GDP in FY 2012-13, FY 2013-14 and FY 2014-15 successively.

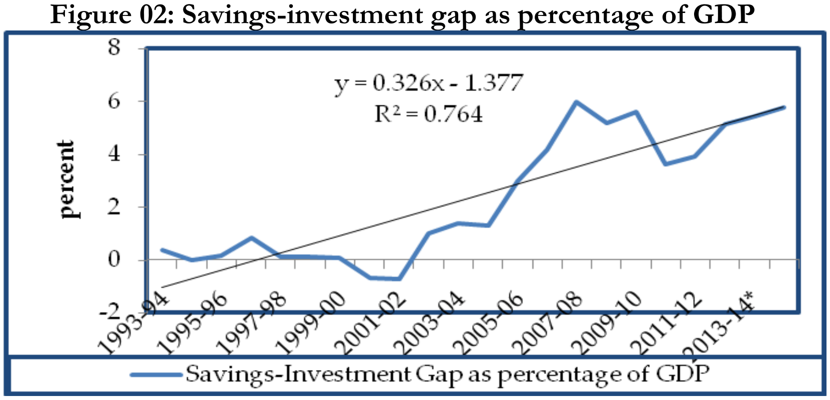
[2] The details of the projection procedure has been shown in Appendix: B

The MTMF targets no gap between saving and investment in FY 2014-15 and will reach at 29.6 percent of the GDP

The contractionary monetary policy through high rate of interest not only reduces the private investment but also fails to attract foreign investment. The depreciation in rate of exchange over the time is also assumed as a factor in relatively low attainment of foreign investment. Though recently Taka seems to be strong against dollar because of lower aggregate demand due to falling investment and a higher growth of remittances, yet this phenomenon may be seen as a short-term one. The political contestation is also perceived as another reason for declined foreign investment.

The MTMF targets no gap between saving and investment in FY 2014-15 and will reach at 29.6 percent of the GDP. An econometric exercise, however, does not support such estimation.[3]

Figure 02: Savings-investment gap as percentage of GDP



Source: Author's calculation based on data of Bangladesh Bank, 2013

Achievement of 7.2 percent economic growth in 2012-13 requires an investment of USD 2460 billion while the investment was USD 2327 billion in the previous year (FY2011-12), which achieved higher growth of 6.32 percent than the projected growth of the current year.

3. FISCAL BALANCE

3.1 Revenue Income

The acceleration rate of collection on revenue income of the government is not satisfactory and achieving the target might not be possible, primarily due to fall in tax-revenue income from the large enterprises like banking sector.

[3] The detailed regression results are shown in Appendix: C

One of the most important reasons of budget deficit is subsidy payment of quick rental system which is only based on very short run basis irrespective to long run sustainability

The present trend of increasing budget deficits, however, occurs due to mismanagement of the government. One of the most important reasons of this deficit is subsidy payment of quick rental system which is only based on very short run basis irrespective to long run sustainability. To meet the unsustainable deficit of the budget, the government has increased borrowing from banking sector at a significant rate which reduces the profitability of financial sector as well as makes the crowding out effect.

From July to November in FY 2012-13, the total collection of NBR and non NBR revenue were Tk. 37, 388 crore and Tk. 1512 crore respectively which were Tk. 32,034 and Tk.1328 crore respectively in the corresponding period of FY 2011-12. The observed rate of growth during the aforementioned period is 16.71 percent which is lower than the targeted rate of growth of 21.42 percent for the current year. To achieve the target, however, might not be possible, primarily due to fall in tax-revenue income from the large enterprises like banking sector. The falling rate of economic growth of this fiscal year also hampers the acceleration process of the tax revenue growth through falling actual outputs below its potential level.

The first five months (July-November) of current FY 2012-13 witnessed continuity in overall deficit balance which stood at 0.31 percent of GDP and -0.83 percent over the same period of FY 2011-12

During the FY 2012-13, the total revenue collection of the government is targeted at Tk. 1,39,670 crore against Tk. 1,14,885 crore of the revised estimate of FY 2011-12, about 21.57 percent higher than the previous fiscal year. The target of NBR for FY 2012-13 is Tk. 1,12,259 crore against Tk. 92,370 crore of FY 2011-12, an increase by 21.53 percent.

3.2 Budget Deficit

The first five months (July-November) of current FY 2012-13 witnessed continuity in overall deficit balance which stood at 0.31 percent of GDP and -0.83 percent over the same period of FY 2011-12 (Integrated Budgeting and Accounting System (IBAS), Finance Division).[4]

The present trend of deficits occurs due to lack of farsightedness on the part of the government. One of the most important reasons of this deficit is subsidy payment on account of quick rental system, which has received high degree of criticism, particularly for its loss caused to the exchequer as well as its long run non-sustainability.

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[4] http://www.mof.gov.bd/en/budget/mfr/mfr_november_2012.pdf

Accordingly, in FY 2012-13, the overall budget deficit is targeted at Tk. 52,068 crore which is 5 percent of the GDP and is 12.38 percent higher than that of the previous year. In FY 2007-08, the deficit reached at the peak but after that, deficit has turned around to five percent.

Table 03: Budget deficit

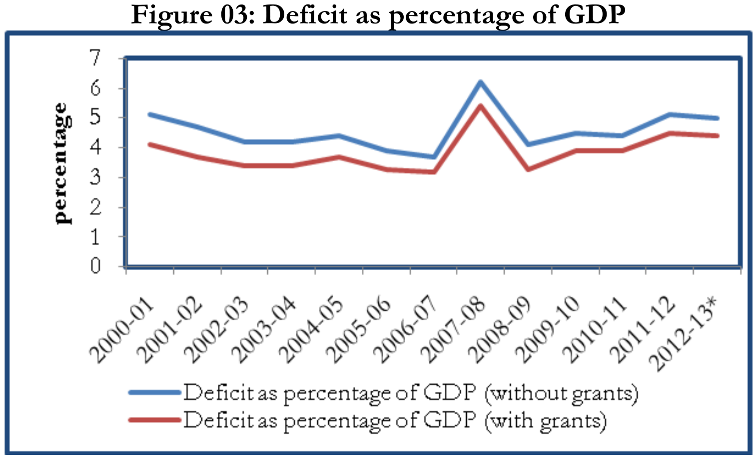
	MTMF	2008 -09	2009 -10	2010 -11	2011-12	2012 -13	2012 -14	2014 -15
Budget Deficit (as percent age of GDP)	MTMF 08-11	5	4.4	4				
	MTMF 09-12		5	4.8	4.7			
	MTMF 12-16			4.3	5.0	5	5	5
	MTMF 13-17				5.1	5	4.7	4.6
Actual Budget Deficit		4.1	4.5	4.4	5.1			

Source: Bangladesh Bank and Finance Division, Ministry of Finance, Bangladesh, 2013

One of the prime tasks of the fiscal policy of the government is to continue endeavoring for narrowing the gap between expenditure and income in order to offset the budget deficit or to maintain it at a tolerable level

One of the prime tasks of the fiscal policy of the government is to continue endeavoring for narrowing the gap between expenditure and income in order to offset the budget deficit or to maintain it at a tolerable level. Over the past few years, the overall budget deficit registers an increasing trend that puts serious pressures on the total debt of the country. MTMFs (taken in last four fiscal years) have planned to accommodate around five percent of the fiscal deficit.

Figure 03: Deficit as percentage of GDP



Source: Finance Division, Ministry of Finance, Bangladesh, 2013

The major problem with the current deficit is its inability to augment multiplier effect and capital formation and hence fails to contribute in generating growth. Moreover, the unprecedented government borrowings projected for FY 2012-13 may dry up the liquidity, crowd out private investment and force the rate of interest to go up at a high level. A liquidity crisis is already there in the economy along with the huge borrowing from the central bank. The growth of Bangladesh economy is consumption lead. The higher level rate in interest also forces down the consumption and consequently, the consumption lead growth may witness a decline.

The higher level rate in interest also forces down the consumption and consequently, the consumption lead growth may witness a decline

3.3 Internal Debt and External Debt

The accumulation in domestic debt derives mainly from three sources: Bangladesh Bank, Deposit Money Banks (DMBs), and Non-banks including National Savings Directorate (NSD). The government of Bangladesh mainly borrows both from Bangladesh Bank and the commercial ones.

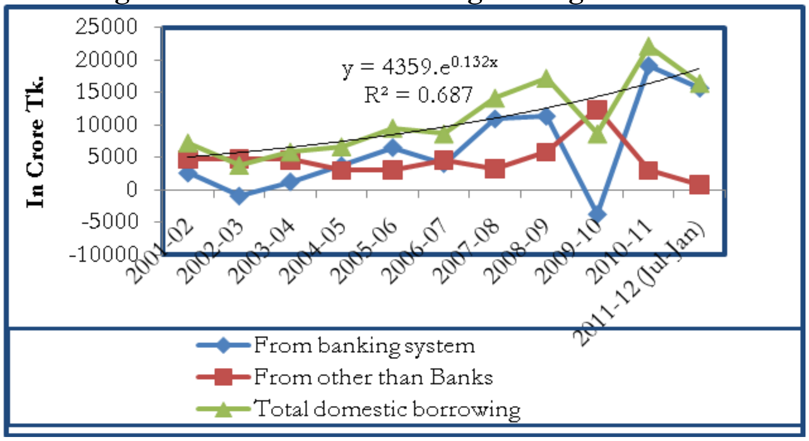
From July-February of FY 2012-13, the government has borrowed net Tk. 8,053.77 crore from domestic sources. For this, the borrowing from banking sector and non banking sector stood at Tk. 6433.90 crore and Tk. 1,619.87 crore respectively.

From July-February of FY 2012-13, the government has borrowed net Tk. 8,053.77 crore from domestic sources. For this, the borrowing from banking sector and non banking sector stood at Tk. 6433.90 crore and Tk. 1,619.87 crore respectively

The government targeted Tk. 33,484 crore as net borrowing from domestic sources in the budget of FY 2012-13. From this target, the net target to borrow from banks and non banking sector were Tk. 23,000 crore and Tk. 10,484 crore respectively.

In the budget of FY 2012-13, Tk. 96,064 crore has been estimated as total borrowing from the banking sector including both short run debt and long term debt against Tk. 80, 194 crore of the revised budget of FY 2011-12. In FY 2010-11, the government borrowed 4.43 times higher from banking sectors (in comparison of FY 2001-02 indicating a sharp crowding out effect, which has dampened private investment). Previously, government borrowed an amount of Tk. 2,534.9 crore from banking sector whereas Tk. 4,711.47 crore has been borrowed from non-banking sectors in FY 2001-02. The government has become more dependent on banking sectors than non-banking ones for domestic financing over the time.

Figure: 04: Domestic borrowing of the government

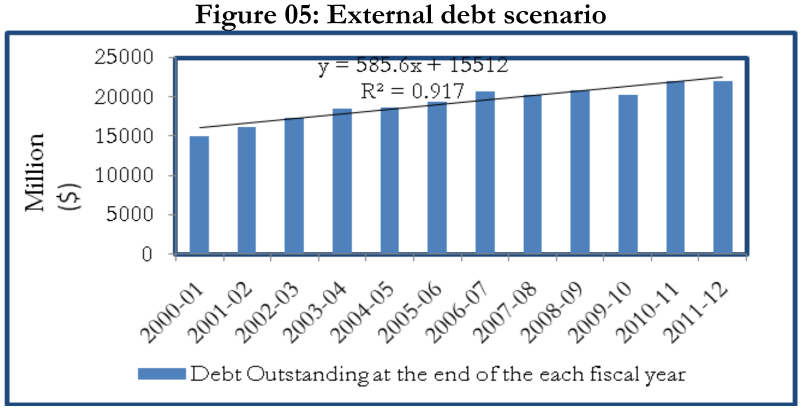


Source: Economic Relations Division (ERD), Ministry of Finance, 2013

The increasing external debt, together with the expiry of grace periods and unfavourable exchange rate movements, has resulted in increased external debt service

In FY 2011-12, total external debt totals at USD 22095.2 million from USD 65 million in FY 1972-73. Over the time, the amount of external debt has been increasing at a higher rate and therefore in FY 1989-90, the amount reached at USD 1,069 million, incurring a growth of additional USD 55 million each year.

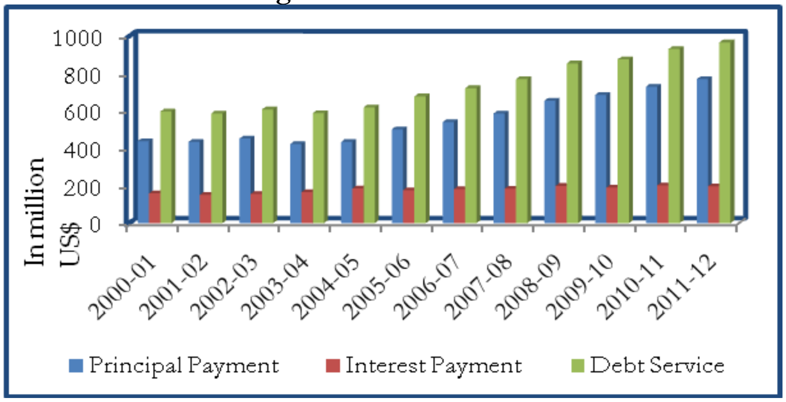
Figure 05: External debt scenario



Source: Economic Relations Division (ERD), Ministry of Finance, 213

The increasing external debt, together with the expiry of grace periods and unfavourable exchange rate movements, has resulted in increased external debt service. The principal and interest payment in FY 2011-12 were USD 769.9 million and USD196.6 million respectively, and the total payment was USD 966.5 million. In FY 1973-74, the principal and interest payment were USD 9 million each. The both principal and interest payment have risen at a much higher rate during the 90s. In FY 2001-02, the principal and interest payments were USD 435 million and USD 151 million respectively, amounting the total payment to USD 586 million

Figure 06: Debt service



Source: Economic Relations Division (ERD), Ministry of Finance, 2013

3.4 Annual Development Programme (ADP)

Only 44 percent of ADP was implemented from July, 2012 to February, 2013 of the current fiscal year compared to that of 38 percent at the same period of FY 2011-12

The implementation status of ADP in the first eight months (July, 2012 – February, 2013) of the current fiscal year is not very satisfactory. Only 44 percent of ADP was implemented from July, 2012 to February, 2013 of the current fiscal year compared to that of 38 percent at the same period of FY 2011-12. The sluggish pace of the implementation has led the government to revise the size of ADP at the end of each fiscal year which tends to continue this year as well. In FY 2012-13, the estimated ADP allocation is Tk. 55, 000 crore which was Tk. 46, 000 crore in FY 2011-12 and stood at Tk. 41, 080 crore as revised. Due to the lack of financial ability, the implication of ADP is not fully utilized.[5] There are, however, newspaper reports about the revised ADP standing higher (Tk. 57,120 crore) than from the original size of Tk. 55,000 crore. [6] According to such reports, the planning commission finds out the inclusion of the development budgets of the autonomous bodies as responsible for such increase; whereas others suggest the government has increased it to distribute resources in the election year.

Instead of lower capacity of implementation, a large amount of targeted ADP in every year is very ambitious and myopic. The allocation of ADP is continuously increasing over the last twenty years except FY 2008-09. Implementation of ADP, however, is much lower than its target. The question remains whether such politically motivated investment tantamount to

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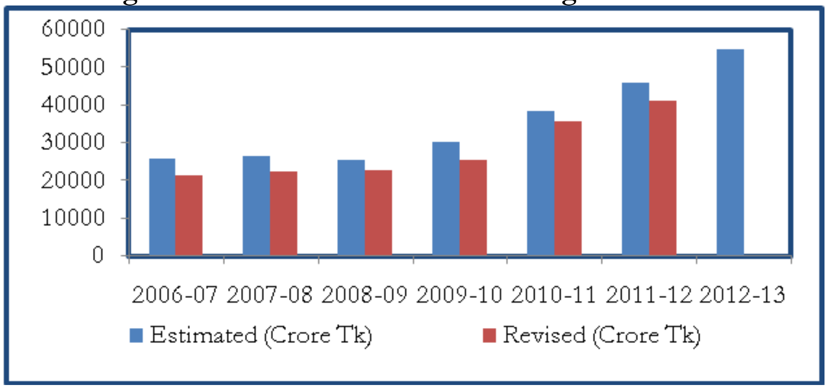
[5] http://www.mof.gov.bd/en/budget/adp/adp_february13.pdf]

[6] http://newagebd.com/detail.php?date=2013-04-17&nid=46297#.UXUI5CspY5g

bad investment at the cost of inability to create a multiplier effect.

Figure 07: Estimated and revised budget for ADP



Source: Implementation Monitoring and Evaluation Division (IMED), Ministry of Planning, 2013

4. EXTERNAL BALANCE

The current trade balance in the first eight months (July-February) of FY2012-13 was provisionally estimated with a deficit of USD 4707 million which was USD 6384 million during the corresponding period of FY 2011-12

The current trade balance in the first eight months (July-February) of FY2012-13 was provisionally estimated with a deficit of USD 4707 million which was USD 6384 million during the corresponding period of FY 2011-12. During the same period, there seems a positive trend in current account balance due to higher rate of remittance flow. The capital account estimated provisionally has decreased from USD 331 million in FY 2011-12 (July-February) to USD 301 million in FY 2012-13(July-February). The overall balance has provisionally accounted a surplus of USD 3506 million against the deficit USD 516 million over the change in same time horizon. This occurrence is seen as a result of the accumulated loan received from the private sectors and reduction in import.

Table 04: Balance of payments **In million USD**

Item	2004-05	2005-06	2006-07	2008-09	2008-09	2009-10	2010-11	2011-12
Trade Balance	-3297	-2889	-3458	-5330	-4710	-5155	-7744	-7928
Current Account Balance	-557	824	952	702	2416	3724	885	1704
Overall Balance	67	338	1493	331	2058	2865	-656	494

Source: Statistics Division, Bangladesh Bank, 2013

The country is mainly dependent on import than export and hence, the balance of payments will get into a crisis because of the outflow of finance. The burden of external repayment depreciates the Taka and consequently, increases the cost of import. As a result, the inflation is rising and creating excessive pressure on balance of payments (BOP).

In FY 2012-13, total remittance inflow is USD 12843 million which was USD 11650.32 million in previous FY 2010-11

Over the years, the flow of remittance in Bangladesh is increasing in volume, but the rate of growth in remittance decreased since FY 2008-09 except the last fiscal year. In FY 2012-13, total remittance inflow is USD 12843 million which was USD 11650.32 million in previous FY 2010-11. Over the last decade, the total remittances inflow has increased about six times which mainly helps to make a positive current account balance.

5. MONEY MARKET, MONETARY POLICY AND CAPITAL MARKET

5.1 Money Market and Monetary Policy

In each and every target of MTMF, there is a decreasing trend on the percentage change in broad money and the change in broad money supply always exceeds the target levels at a decreasing rate

There is a mismatch between the target of MTMF in case of percentage change in broad money and actual change in broad money. In each and every target of MTMF, there is a decreasing trend on the percentage change in broad money and the change in broad money supply always exceeds the target levels at a decreasing rate.

In FY 2011-12, the growth of board money was 17.39 percent against the targeted level of MTMF 12-16 as 15.8 percent whereas this fiscal year, domestic credit and credit in private sector also exceeded its target a little bit. During FY 2008-09, the growth of broad money reached at 19.2 percent from 17.6 percent in FY 2007-08. In FY 2009-10, the growth of broad money slightly increased and reached at 22.4 percent. In FY 2010-11 and FY 2011-12, the growth of broad money was successively 21.34 and 17.39 percent, indicating a result of contractionary monetary policy. The target of MTMF in domestic credit and credit in private sectors were based on contractionary mode. The actual figure, however, showed that from FY 2008-09 to FY 2010-11 an increasing growth of credit was prevailing in this sector and stated to fall down further in FY 2011-12.

Table 05: Domestic credit, credit in private sector and broad money

Component	MTMF	2008-09	2009-10	2010-11	2011-12	2012-13	2012-14	2014-15
Domestic Credit (percentage change)	MTMF 08-11	18	18.2	17.9				
	MTMF 09-12		19.2	18.8	18.4			
	MTMF 12-16			17.7	19.2	19.5	19.5	19.2
	MTMF 13-17				19.1	18	17.1	16.7
Actual Change of DC		15.9	17.6	27.42	19.53			
Credit in private sector (percentage change)	MTMF 08-11	17	19	19				
	MTMF 09-12		18.3	18.5	18.5			
	MTMF 12-16			18	18	18	18.5	18.5
	MTMF 13-17				16	16	16	16
Actual Change		14.6	24.2	25.83	19.72			
Broad Money (M2) (Percentage change)	MTMF 08-11	16.9	15.8	15.3				
	MTMF 09-12		16.3	16.2	16			
	MTMF 12-16			16	15.8	15.8	15.7	15.5
	MTMF 13-17				17	16	15.5	15.5
Actual Change		19.2	22.4	21.34	17.39			

Source: Bangladesh Bank and Finance Division, Ministry of Finance, Bangladesh, 2013

Unnayan Onneshan (UO) has shown that no statistically significant relationship and inflation could explain the growth of GDP in the short run, though there a statistically significant long-run positive relationship between the two variables exist

The recent tightened monetary policy has been taken to control monetary expansion and hence to reduce the board money in the near future. The growth of board money and domestic credit is supposed to decline over three succeeding years, indicating high rate of interest in those years. For this, investment will be negatively affected and consequently, it will hamper the real economic rate of growth. The credit to the private sector is projected to remain constant over the same time. The government mainly takes the contractionary monetary policy aiming the reduction of rate of inflation.

A recent study of Unnayan Onneshan (UO) has shown that no statistically significant relationship and inflation could explain the growth of GDP in the short run, though there a statistically

The suggested tools to influence the growth of money stocks, identified in the MPS are the restrictions of broad money growth path which is adjusted through cash reserve ratio (CRR), statutory liquidity requirements (SLR) and restriction in the capital accounts

significant long-run positive relationship between the two variables exist [7]. The results of the empirical analyses have major policy implications, particularly, in articulating monetary policy. The evidence suggests that emphasis in the short run has to be concentrated on understanding the level of price, the sources of inflation and its relationship with other complementary policies affecting growth and employment, as opposed to concentrate on inflation targeting approach. Though in last three years, the government took the contradictory monetary policy, the reason of the sky rocketing rate of inflation was hidden in wrong policy mixture and misidentification of the source of inflation.

The suggested tools to influence the growth of money stocks, identified in the MPS are the restrictions of broad money growth path which is adjusted through cash reserve ratio (CRR), statutory liquidity requirements (SLR) and restriction in the capital accounts.

Table 06: Changes in money supply over the time (In million Tk.)

Components	Jan, 2013	Jan, 2012	Jun, 2011	Jun, 2010	Jun, 2009	Percentage Changes of Jan 2013 over Jan 2012	Percentage Changes of June 2011 over		Percentage Changes of Jun, 2010 over Jun, 2009
							Jun 2010	Jun 2009	
Money Supply (M 1)	1138380	1097214	10,31,011	8,79,884	6,64,268	3.75	17.18	55.21	32.45
Money Supply (M 2)	5624768	5171095	44,05,200	36,30,312	29,64,998	8.77	21.34	48.57	22.43

Note: January-Jan; June-Jun
Source: Author's calculation based on Statistics Department of Bangladesh Bank, 2013

On the basis of components of money supply, there seems a declined trend in growth of money supply in case of both M1 and M2. The percentage change of M1 of January 2013 over January 2012 is 3.75 percent and percentage change in M2 is 8.77 percent over the same period. The percentage change of M1 of June 2011 over June 2010 was 17.18 percent and

[7] http://www.unnayan.org/reports/meu/Aug_12/MEU_Aug_2012.pdf

percentage change in M2 was 21.34 percent over the same time period. From June 2010 to June 2011, the percentage change in M1 and M2 were 17.18 and 21.34 respectively against 19.12 and 17.59 from June 2009 to June 2010. The domestic debt financing increases the amount of M1 and M2, which directly influence the increase in price level.

5.2 Rate of Interest

The policy application of IMF results in high rate of interest which adversely affects the level of investment as well

The policy application of IMF results in high rate of interest which adversely affects the level of investment as well. The rate of weighted interest on advances of all banks was 13.8 percent on year closing day of 2012 whereas this rate was much higher in the private banks (14.69 percent). During the same time, the spread between the rate of deposit and the rate of lending averaged at 5.33 percent, pointing on the gap between the levels of investment and savings in the economy.

Table 07: Monthly weighted average rate of interest on deposits and advances (on 31.12.12)

Name of Banks	W. Avg. Deposits	W. Avg. Advances	Spread
State owned Banks	7.15	11.21	4.06
Specialized Banks	9.72	12.45	2.73
Foreign Banks	5.6	14.36	8.76
Private Banks	9.18	14.69	5.51
All Banks	8.47	13.8	5.33

Note: W. Avg. -Weighted Average

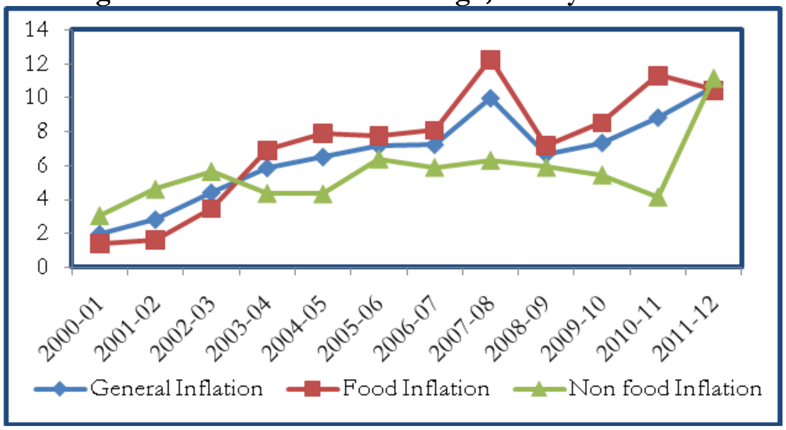
Source: Statistics Department, Bangladesh Bank, Head Office, 2013

5.3 Inflation

Inflation is dependent on fiscal policy actions related to financing, domestic public debt creation and other means of borrowing by government as well as the level of total revenue generated at any period

Inflation is not always evident everywhere as a monetary phenomenon. It is however, dependent on fiscal policy actions related to financing, domestic public debt creation and other means of borrowing by government as well as the level of total revenue generated at any period. Sometimes the public debt is financed through money creation, which directly causes the inflation to rise. There is always crowding out when the government finances through open market operation that brings about the investment to fall. As a result, actual output becomes less than the potential level. The positive relationship between total deficit financing, money supply and inflation imply that total deficit financing and money supply are the contributing factors to the upward variations in the CPI over the years.

Figure 08: Twelve-month average, Base year 1995-96



Source: Bangladesh Bureau of Statistics, 2013

Inflation has remained at high level, though dropped to 7.22 percent in October, FY 2012-13, from the peak of 10.62 percent in FY 2011-12 as a result of a significant level of food inflation

Inflation has remained at high level, though dropped to 7.22 percent in October, FY 2012-13, from the peak of 10.62 percent in FY 2011-12 as a result of a significant level of food inflation. Food inflation is seen to be more increasing than non-food inflation. During FY 2010-11, the food inflation rose to its peak (11.34 percent) while non-food inflation was quite low (4.15 percent). The scenario has changed in next year and in FY 2011-12, the food inflation has decreased slightly at 10.47 percent. On the other hand, non food inflation has increased significantly at 11.15 percent. (Base year FY 1995-96)

In March, 2013 point to point basis general inflation was 7.71 percent which was 6.76 percent over the corresponding previous year. In point to point basis, the food inflation has increased from 3.63 percent to 7.50 percent from March, 2012 to March 2013 whereas in the same time, non food inflation has decreased from 11.79 percent to 8.04 percent. (Base year FY 2005-06)

The recent rate of inflation has been published by Bangladesh Bureau of Statistics (BBS) only using 2005-06 as base year, making the comparison difficult.

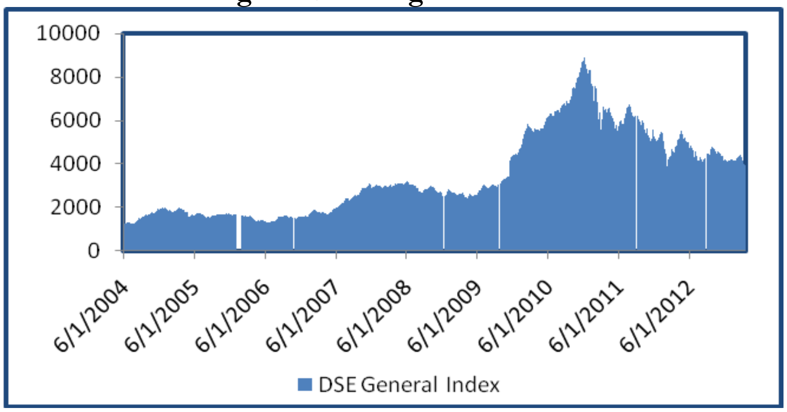
5.4 Capital Market

Unnayan Onneshan recently makes an attempt to understand the reasons for continuous fall in capital market (Bangladesh

Economic Update, March 2013)[8]. The main reasons for failing to revive confidence amongst the investors are non-implementation of commitments made to resuscitate the market, failure in taking actions against the individuals involved in the crash, lack of zero-tolerance in regulatory oversights etc. All these have manifested in inadequate supply of liquidity in the market. After the crush in the capital market in 2011, a continuous fall in turnover is observed, indicating over the time short in supply of liquidity in the capital market. In FY 2011-12, the turnover in DSE dropped to Tk.117145.07 crore from Tk.325879.77 crore in previous FY 2010-11, a rate of decrease by 65.05 percent.

The main reasons for failing to revive confidence amongst the investors of capital market are non-implementation of commitments made to resuscitate the market, failure in taking actions against the individuals involved in the crash, lack of zero-tolerance in regulatory oversights

Figure 09: DSE general index



Source: Dhaka Stock Exchange (DSE), 2013

Furthermore, Unnayan Onneshan discussed the reasons for crush in the market as well (Bangladesh Economic Update, October 20119). The major findings were individual wise manipulation in the market and the mounting growth in the size of the market, which did not reflect the ground realities of the economy. For example, GDP and the market capitalisation have not witnessed any significant correlation, indicating no match between the growth of the capital market and the growth in the real economy. The market capitalisation, however, exceeded the total investment of the economy. In FY 2009-10 and FY 2010-11, the market capitalisation and investment ratio were 134.29 and 116.13 percent respectively whereas this ratio remained between 10 and 35 percent during the period of 1995-96 to FY 2006-07.

The major findings were individual wise manipulation in the capital market and the mounting growth in the size of the market, which did not reflect the ground realities of the economy

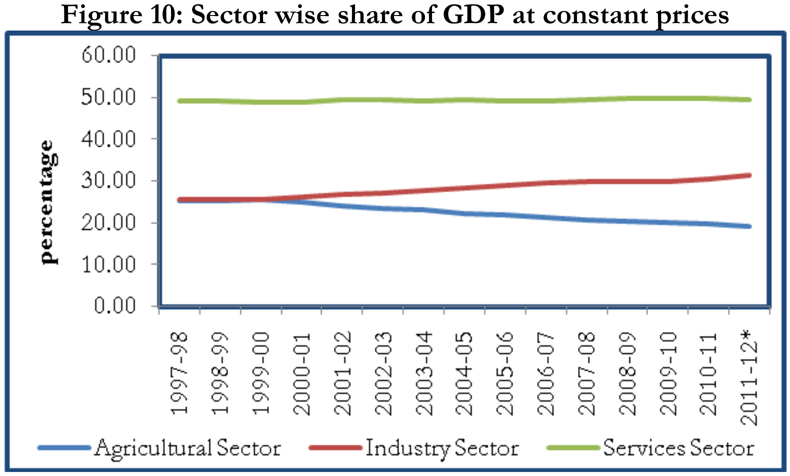
[8]http://www.unnayan.org/reports/meu/march_13/MEU_March_2013%20.pdf

[9] http://www.unnayan.org/reports/meu/oct_11/meu_Oct_2011.pdf

6. REAL SECTOR

In FY 2011-12, the share of agricultural, industrial and service sector in GDP was 19.29 percent, 31.26 percent and 49.45 percent respectively which were 20.01 percent, 30.38 percent and 49.60 percent respectively in FY 2010-11. This is a matter of concern that the contribution of crops and horticulture has decreased from 14.59 percent to 10.74 percent whereas the contribution of large and medium scale industries has decreased to 11.29 percent from 13.75 percent.

Figure 10: Sector wise share of GDP at constant prices



Source: Bangladesh Bureau of Statistics, Bangladesh Bank, Ministry of Finance, 2013

In FY 1990-91, the share of agricultural, industrial and service sector in GDP was 29.21 percent, 21.04 percent and 49.73 percent respectively.

Unnayan Onneshan makes an attempt to identify a number of major challenges in recent time the sector faces, besides long-running neglect of addressing the structural bottlenecks in the backdrop of policy makers' apathy of having strong and active industrial policy and the paradigmatic swing in favour of trade liberalization and export orientation (*Bangladesh Economic Update, February 2013*[10]).

Unnayan Onneshan makes an attempt to identify a number of major challenges in recent time the sector faces, besides long-running neglect of addressing the structural bottlenecks in the backdrop of policy makers' apathy of having strong and active industrial policy and the paradigmatic swing in favour of trade liberalization and export orientation

During this period, industrial sector has been facing obstacles because of shortages in power supply, inadequate inflow of FDI and most importantly, failure to endow the economy with

[10]http://www.unnayan.org/reports/meu/Feb_13/MEU%20FEB%202013.pdf

appropriate industrial policy, which could spur the economic growth.

7. LOAN FROM IMF AND ITS IMPLICATIONS

The major policies of IMF include fiscal management, monetary management as well as external balance management. Though the amount of IMF loan is not high compared to the size of the economy of Bangladesh, yet the policy suggestions have affected the economy.

To control the inflationary situation, the IMF suggested opting for contractionary monetary policy by the central bank, without adequate considerations on the reasons and the sources of the present inflation, whether it is demand-pull or cost-push

One of the important suggestions of IMF is to tight the fiscal policy and rearrangement of taxing system. The growth in GDP of this country is fully consumption based. Hence, increase of value added tax (VAT) without bringing reform towards progressive taxation regime hampers the consumption of the downtrodden and leaves a negative implication on the growth of GDP.

To control the inflationary situation, the IMF suggested opting for contractionary monetary policy by the central bank, without adequate considerations on the reasons and the sources of the present inflation, whether it is demand-pull or cost-push. Though change in the policy rate only demand inflation is affected, but supply-side induced inflation remains unabated. By this mechanism of increasing rate of interest, the level of investment has fallen and the rate of growth in GDP has started to decline, resulting into increased level of unemployment. A spike in the international prices of commodities and petroleum products has also contributed directly to the inflation.

The gap between savings and investment has increased at a high rate over the time and contributes in non-achievement of the targeted level of GDP growth

In case of international trade, the common suggestion of IMF is to make the rate of exchange flexible. A common problem with fully flexible rates of exchange in the developing economies is the high pass-through of the rate in exchange to inflation in these countries. The balance of payments (BOP) gets into a crisis owing to the outflow of finance. The burden of external repayment depreciates the Taka and hence, increases the cost of import. As a result, the inflation is rising and creating excessive pressure on BOP. To summarize, it is clear that the policies of IMF has affected the economy of Bangladesh negatively

8. CONCLUSION

The likelihood in this fiscal year is non-attainment of the achievement in targeted rate of growth combined with retention of high level of inflation and continuing shortfall in employment. According to the projection of Unnayan Onneshan, in FY 2012-13 the rate of growth in GDP might stand at 5.75 percent whereas the targeted rate of growth of the government is 7.2 percent. The government has also not been able to achieve the targets in previous occasions. According to MTMF 08-11, the average target growth was 6.9 percent whereas the achieved rate was 5.87 percent on average. In addition, the increasing savings-investments gap, wrong policy mix of fiscal and monetary policy suggested by IMF, inflationary outcome and instable political situation might not be able to reach in the desired growth in FY 2012-13.

The present trend of deficits occurs due to lack of foresight of the government. One of the most important reasons of this deficit is subsidy payment on account of quick rental system, which has received high degree of criticism

The gap between savings and investment has increased at a high rate over the time and contributes in non-achievement of the targeted level of GDP growth. The lack of matching infrastructure development by the government and the private sector due to lack of foresight in operating fiscal policy on the one hand and increase in the cost of loanable funds due to contractionary monetary policy on the other have suppressed investment demand.

As regards the revenue income, it might not be possible to achieve the target, primarily due to fall in tax-revenue income from the large enterprises like banking sector as well as political instability. The falling rate of economic growth of this current fiscal year also hampers the acceleration process of the tax revenue growth through falling actual outputs below its potential level.

During this period, industrial sector is also facing some obstacles due to shortages of power supply, inadequate inflow of FDI and most importantly, failure to endow the economy with appropriate industrial policy which could spur the economic growth

The present trend of deficits occurs due to lack of foresight of the government. One of the most important reasons of this deficit is subsidy payment on account of quick rental system, which has received high degree of criticism, particularly for its loss caused to the exchequer and its long run non-sustainability.

The sluggish pace of the implementation has led the government to revise the size of ADP at the end of each fiscal year which tends to continue this year as well. Due to the lack of financial ability, the implication of ADP is not fully utilized.

The country is mainly more dependent on import than export and hence, the balance of payments will get into a crisis because of the outflow of finance. The burden of external repayment depreciates the Taka and consequently, increases the cost of import. As a result, the inflation is rising and creating excessive pressure on balance of payments (BOP).

The growth of board money and domestic credit is supposed to decline over three subsequent years which is indicating high rate of interest in those years

The recent tightened monetary policy has been taken to control monetary expansion and hence to reduce the board money in the near future. The growth of board money and domestic credit is supposed to decline over three subsequent years which is indicating high rate of interest in those years.

The main reasons for the continuous fall in capital market are failing to revive confidence amongst investors owing to non-implementation of commitments made to resuscitate the market, failure in taking actions against the individuals involved in the crash, lack of zero-tolerance in regulatory oversights. All these reasons have manifested in inadequate supply of liquidity in the market.

During this period, industrial sector is also facing some obstacles due to shortages of power supply, inadequate inflow of FDI and most importantly, failure to endow the economy with appropriate industrial policy which could spur the economic growth.

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Appendix A

Real growth in GDP projected by UO:

Constant	Coefficient	R Square	Adjusted R Square	F Value
459472.000**	80454.800**	0.995	0.993	440.752**

*Note: *, ** and *** denote rejection of the hypothesis of unit root test at 10 percent, 5 percent and 1percent respectively.*

Saving- Investment Projection:

National Savings

Constant	Coefficient	R Square	Adjusted R Square	F Value
18.147***	0.668***	0.94	0.93	265.295***

*Note: *, ** and *** denote rejection of the hypothesis of unit root test at 10 percent, 5percent and 1percent respectively.*

Total Investment

Constant	Coefficient	R Square	Adjusted R Square	F Value
19.522***	0.342***	0.86	0.85	107.912***

*Note: *, ** and *** denote rejection of the hypothesis of unit root test at 10 percent, 5 percent and 1 percent respectively*

Growth- Investment Relationship:

Dependent Variable: Rate of Growth
Independent Variable: Investment

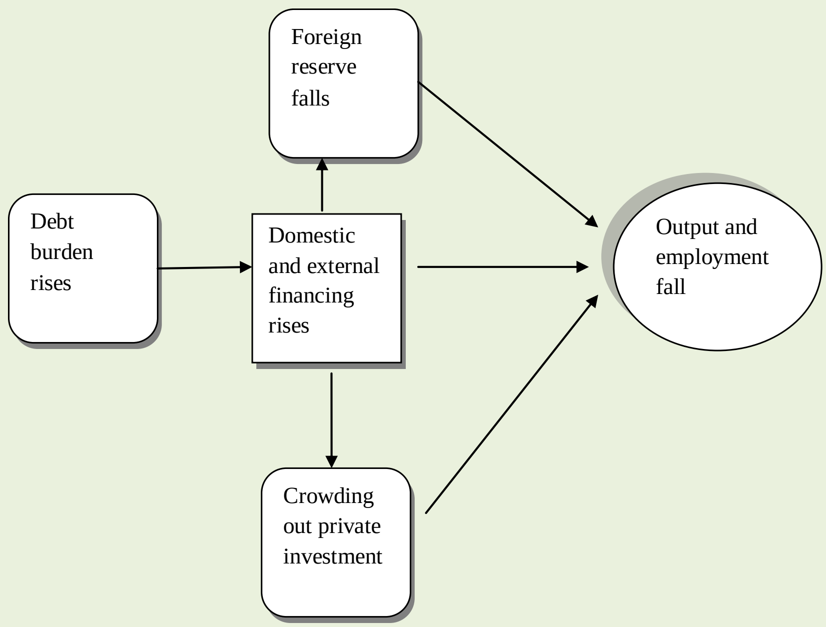
Constant	Coefficient	R Square	Adjusted R Square	F Value
4.540***	0.001***	0.55	0.52	24.496***

*Note: *, ** and *** denote rejection of the hypothesis of unit root test at 10 percent, 5 percent and 1 percent respectively*

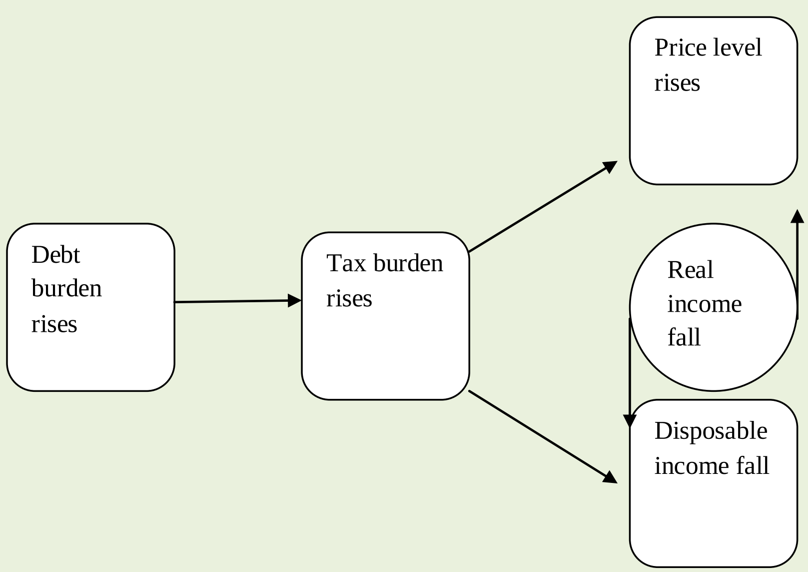
Appendix B
Impact of Debt Financing on Marginalised People

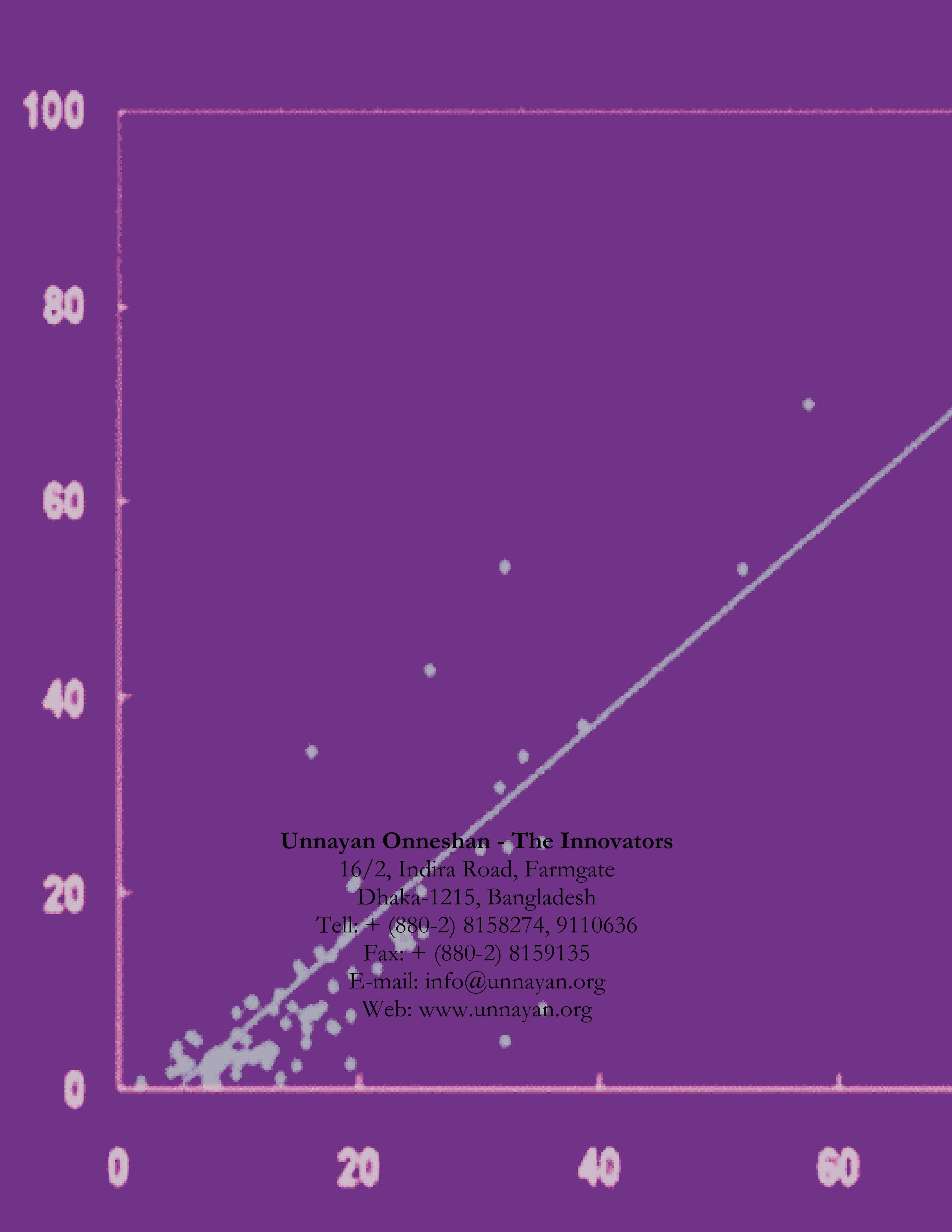
Impact of Debt Financing on Marginalized People

Through Fiscal Policy Effect:



Through Monetary Policy:





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