Bangladesh Economic Update

Inflation, Unemployment and Growth Trajectory

October, 2010

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

Bangladesh Economic Update
Volume.1. No 4, October 2010

Acknowledgement:
The Bangladesh Economic Update is an output of the Economic Policy Unit of the Unnayan Onneshan, a multidisciplinary research centre based in Dhaka, Bangladesh. The report is prepared by a team, led by Rashed Al Mahmud Titumir and comprising Kashfi Rayan and Shah Md. Zabir, and edited by A. Z. M. Saleh.

For orders and request please contact:

Unnayan Onneshan-The Innovators
House: 16/2, Indira Road, Farmgate, Dhaka-1205, Bangladesh.
Tell: + (880-2) 815 82 74, 911 06 36; Fax: + (880-2) 815 91 35
E-mail: info@unnayan.org; Web: www.unnayan.org

Inflation, Unemployment and Growth Trajectory

Inflation is on a rising trend and unemployment rate is also increasing in recent years which imply that the strategies and policies of the government to achieve 8 percent GDP growth rate by FY 2014-15 need re-working to address these problems for bringing the economy on track to achieve the target.

That is why, the fourth issue of Unnayan Onneshan Economic Update focuses on these three important variables. These are analysed through impact of increased inflation and unemployment vis-a-vis the targeted GDP growth, inflation and unemployment in Bangladesh and the possible sources of high inflation in recent months. This issue also highlights the trade situation of the country.

1. Growth-Inflation-Unemployment Situation

With the vision to establish Bangladesh as a middle-income country by 2021, the present government has targeted to achieve 8 percent GDP growth rate by Fiscal Year (FY) 2014-15 as stipulated in the Medium Term Macroeconomic Framework of 2011-2015. However, the aim of the government is seriously threatened by rising inflation and the government has not been able to contain it within the targets it has set. Even in the last fiscal year, the government anticipated inflation to remain within 6.5 percent but it reached to 7.31 percent at end of the year.

Inflation can affect the macroeconomic situation of a country by creating uncertainty in investment projects in terms of future profitability, reducing export competitiveness through making it more expensive, and distorting borrowing and lending situation etc. Thus, high inflation associated with high price variability can lead to different negative externalities in an economy and a large effect on the economy’s efficiency.

Increased inflation along with unemployment seriously hampers the income distribution aspects of a country. Average rise in the price of necessary goods along with unavailability of work deteriorates the standard of living of mass people, creating imbalance in economy and life of people.

1.1 Growth-Inflation Trade-off

Numerous studies state that inflation has negative effect on output growth. These studies mainly focused on the nonlinearities and threshold effects of inflation on growth. Some findings of some of these studies are presented below:

- A nonlinear relationship between inflation and economic growth has been found in the studies of Sarel (1996), Andres & Hernando (1997) and Ghosh & Phillips (1998), Andres & Hernando (1997). These studies find a significant negative effect of inflation on economic growth. They also state that there exists a nonlinear relationship. Their main policy message is that a reduction in inflation by 1 percent could raise output in the range of between 0.5 and 2.5 percent.

- Atish Ghosh and Steven Phillips in the *IMF Staff Papers Vol. 45, No. 4 (1998)* state that the negative inflation-growth relationship is evident in both the time and cross-section dimensions of the data, and that it is quite robust. Their main policy message is that even lowering of moderate inflation rates can yield gains in GDP growth of up to 0.8-0.9 percentage.

- Joao Ricardo Faria and Francisco Galrao Carneiro (2001) analyzed the data for Brazil and finds that inflation does not impact growth in the long-run, but in the short-run there exists a significant negative effect from inflation on output.

- Robert J. Barro (1995) in his empirical analysis in a NBER Working Paper shows that if a number of the country characteristics are held constant, the regression results indicate that the effects from an increase in average inflation by 10 percentage points per year are a reduction of the growth rate of real per capita GDP by 0.2-0.3 percentage points per year, and a decrease in the ratio of investment to GDP by 0.4-0.6 percentage points.

As a result, the findings of these studies hold consistent with traditional Keynesian theory, Stockman's neoclassical model and some endogenous growth theories, which imply that higher inflation is negatively correlated to growth.

Due to negative effect of inflation in Bangladesh, gap between growth rate and the actual growth rate is increasing

This finding is reflected in the planned development growth rate and the actual growth rate gap. Due to negative effect of inflation in Bangladesh, gap between growth rate and the actual growth rate is increasing (Table 1). Thus, the finding is applicable for Bangladesh.

Table 1: Summarised Version of Planned Development Effort

Plan	Target of GDP growth rate	Achieved GDP growth rate	Average inflation
The Fourth Five Year Plan 1990-95	5	4.15	5.24 (FY 91 to FY 96)
The Fifth Five Year Plan 1997-2002	7	5.21	5.19 (FY 97 to 2002)
The Medium Term Monitory Framework 2011-2015	8 (by FY 2015)	---	6.87 (FY 2003 to FY 2010)

Source: Bangladesh Economic Review, 2010.

The gap between the targeted GDP growth rate and the achieved GDP growth in the last twenty years show that increase in average inflation may be one of the major reasons behind this gap.

The inflation rate of Bangladesh in the last five years, starting from FY 2004-05 is above 6 percent and if the trends continuous like this, the aim of the government to achieve 8 percent growth rate of GDP by FY 2015, may be hindered by the increasing rate of inflation and increased price variability.

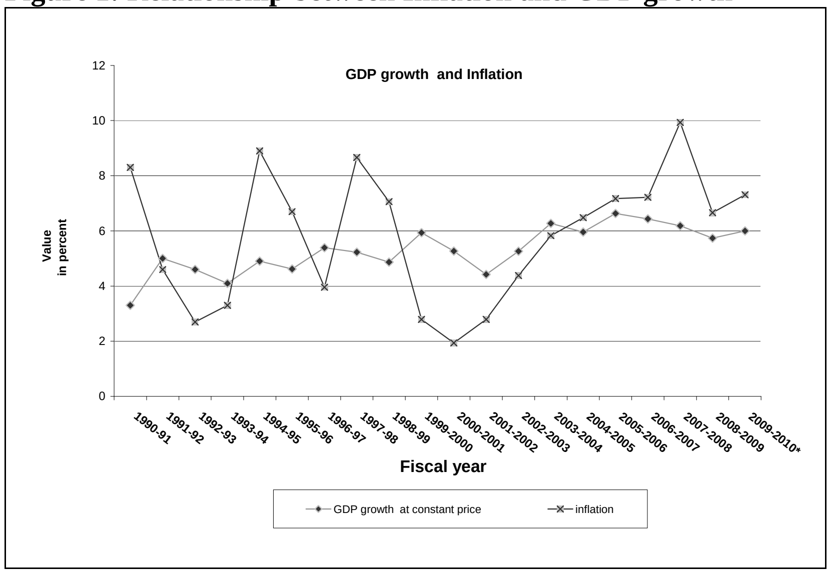
The gap between the targeted GDP growth rate and the achieved GDP growth in the last twenty years show that increase in average inflation may be one of the major reasons behind this gap (Table 1). During the last five fifth year plan though the government wanted to achieve a 7 percent growth in GDP, only 5.1 percent growth was achieved. The inflation rate of Bangladesh in the last five years, starting from FY 2004-05 is above 6 percent and if the trends continuous like this, the aim of the government to achieve 8 percent growth rate of GDP by FY 2015, may be hindered by the increasing rate of inflation and increased price variability.

The rate of inflation has been very fluctuating in the fiscal years of 90s till FY 2002-03 (Figure 1). Then it started rising continuously and after FY 2004-05 it has maintained a level more than 6 percent per year and with an average of 7.5 percent inflation in the last six years. However, from FY 2005-06 the GDP growth also started declining and it reached its lowest point in FY 2008-09 in the last seven years because the average inflation rate increased to 9.93 percent in the

The data of recent years show that increase in inflation reduces the GDP growth rate but the magnitude of reduction is still unknown in case of Bangladesh owing to lack of systematic research.

previous year FY 2007-08. Therefore, the data of recent years show that increase in inflation reduces the GDP growth rate but the magnitude of reduction is still unknown in case of Bangladesh owing to lack of systematic research.

Figure 1: Relationship between Inflation and GDP growth



Source: Bangladesh Economic Review, 2010

The government must take two-fold strategies: (i) reduce the rate of inflation from current level, (ii) maintain inflation within the grip to reach the output target. The inflation target and actual inflation mismatch can create distortions in expected inflation and hamper investment, which has a direct impact on output production.

As a consequence, the government must take two-fold strategies: (i) reduce the rate of inflation from current level, (ii) maintain inflation within the grip to reach the output target. The inflation target and actual inflation mismatch can create distortions in expected inflation and hamper investment, which has a direct impact on output production. As, inflation in the recent years are increasing and if cannot be stabilized at a certain level, it can hamper the target to achieve 8 percent growth rate of GDP by the FY 2015.

Inflation in the recent years are increasing and if cannot be stabilized at a certain level, it can hamper the target to achieve 8 percent growth rate of GDP by the FY 2015.

1.2 Inflation-Unemployment: Two-Way Trap

Inflation and Unemployment are the two closely watched indicators for evaluating the macroeconomic performance of a country. There exists a negative association between the inflation rate and the unemployment rate according to the articulation of A.W. Philips. It shows that if inflation is low, unemployment rate is high and if inflation is high, unemployment rate should be low. This relationship is known as "The Philips Curve". Later Samuelson and Solow also supported that, the policymakers face a trade-off between inflation and unemployment and the Philips curve illustrates that trade-off. But the data of Bangladesh in recent years depict a different picture than the findings of Philips.

The data of Bangladesh in recent years depict a different picture than the findings of Philips.

In Bangladesh rate of unemployment is increasing along with increasing rate of inflation from FY 2005-06 and thus the relationship between inflation and unemployment has become positive. Thus, the economy of Bangladesh is heading towards a two-way trap; as high inflation is creating income erosion and increasing unemployment rate is preventing access of general people into income source. On an average, workers are losing Tk. 384.04 per month of their nominal earnings due to the effects of inflation in 2009 (till June) [Bangladesh Economic Update September, 2010, Unnayan Onneshan].

Decreasing scope of employment is triggering the poverty situation and creating inequality. Therefore, poor people are faced with a twin pressure of loss of income and scope of getting employed.

Table 2: Inflation and Unemployment rate

Surveys	Inflation in corresponding years (%)	Unemployment rate (%)	average inflation (5 years)
LFS,1990-91	8.3	1.9	8.3
LFS,1995-96	6.7	2.57	5.24
LFS,1999-2000	2.79	4.3	5.62
LFS,2002-03	4.38	4.3	3.04
LFS,2005-06	7.17	4.3	6.49
MES,2009	7.31	5.1	7.94

Source: Bangladesh Economic Review, 2010, Bangladesh Bureau of Statistics and author's calculation of average inflation based on the data.

The Labour Force Survey (LFS) conducted by Bangladesh Bureau of Statistics (BBS) after every five years presents the unemployment situation of the country. In LFS 1990-91 unemployment rate was 1.9 percent and inflation in that year was 8.3 percent and after that in LFS 1995-96 unemployment increased to 2.57 percent but inflation in that year was lower than before with 6.7 percent rate and the average inflation of these five years also was low. Therefore, it supported the findings of the Philips curve. However, according to the Monitoring of Employment Survey -2009 (MES), the unemployment rate reached to 5.1 percent, the highest in the last twenty years and average five-year inflation rate was also highest in the last twenty years with a rate of 7.31 percent.

Thus, in Bangladesh rate of unemployment is increasing along with increasing rate of inflation from FY 2005-06 and thus the relationship between inflation and unemployment has become positive. Thus, the economy of Bangladesh is heading towards a two-way trap; as high inflation is creating income erosion and increasing unemployment rate is preventing access of general people into income source. On an average, workers are losing Tk. 384.04 per month of their nominal earnings due to the effects of inflation in 2009 (till June) [Bangladesh Economic Update September, 2010, Unnayan Onneshan]. Simultaneously, decreasing scope of employment is triggering the poverty situation and creating inequality. Therefore, poor people are faced with a twin pressure of loss of income and scope of getting employed.

1.3 Unemployment and Output Relation: Another Two-Way Trap

Current estimates of the relationship between the output gap and employment predict that a one percent increase in the unemployment rate will correspond to about 2-percentage point reduction.

The economy of Bangladesh is heading into another two-way trap. With the decline in rate of growth, both poverty and inequality are increasing rapidly. Therefore, unemployment can hamper the production of gross output. Arthur Okun explained the connection between fluctuations in the unemployment rate and fluctuations in the economy's production. He shows that as the economy pulls out of a recession, output increases by a greater percentage than the rise in employment. And as the economy goes into a recession, output decreases by a greater percentage than the reduction in employment. This result is called "Okun's Law". Current estimates of the relationship between the output gap and employment predict that a one percent increase in the unemployment rate will correspond to about 2-percentage point reduction (Stiglitz and Walsh, 2005)

Though, the magnitude of this relationship in case of Bangladesh has not been calculated yet, because the natural rate of unemployment in developing countries is hard to determine. Still, it can be said that the unemployment gap can affect output gap in the long-run in Bangladesh. In this update, the natural rate of unemployment has been set as 4.3 percent based upon BBS' different LFS and this unemployment rate existed for more than eight years in recent times.

Here, the cost of cyclical unemployment is measured by the output that could have been produced if natural rate of unemployment had been maintained.

As the unemployment rate in 2009 is stated at 5.1 percent, the increment in unemployment rate is measured from 4.3 percent on the GDP growth target of the Government in the Medium Term Macroeconomic Framework 2011-2015.

Step1:

Cyclical Unemployment is the difference between the actual unemployment rate and the rate estimated to correspond to full employment or natural rate of unemployment.

In case of Bangladesh:

Natural rate of Unemployment = 4.3%
Actual unemployment rate (MES, 2009) = 5.1%
Cyclical unemployment = (5.1- 4.3) %
= 0.8 % point

**Output gap is the percentage deviation between actual real GDP and potential real GDP.*

Step 2:

So the lost of output is roughly 0.8 × 2=1.6 percent of real GDP in case of Bangladesh.

Okun's Law states that the percentage gap between actual output and full-employment output is about twice the level of cyclical unemployment. So the lost of output is roughly 0.8 × 2=1.6 percent of real GDP in case of Bangladesh.

Step 3:

Therefore, the effect of increase of unemployed population from 2.1 million in LFS 2005-06 to 2.7 million in MES 2009 will affect the GDP growth rate.

Table 3: Projection of Future Output lost due to increase in Unemployment

Fiscal Years	GDP growth rate at constant price	GDP at constant price Base Year 1995-96 (in billion taka)	The Value of output lost through Okun's law (in billion taka)
2010-11*	6.7	3847.7087	61.56
2011-12*	7.2	4124.74373	66.00
2012-13*	7.6	4438.22425	71.01
2013-14*	8	4793.28219	76.69
2014-15*	8	5176.74476	82.83
Total		22380.7036	358.09

Source: Authors calculation based on B.B.S data from Bangladesh Economic Review, 2010 and MTMF projection from, Ministry of finance

A total amount of output worth Tk.22380.7036 billion at constant price of 1995-96 will have to be produced within the country by the 2014-15, as unemployment has increased to 5.1 percent in the recent years.

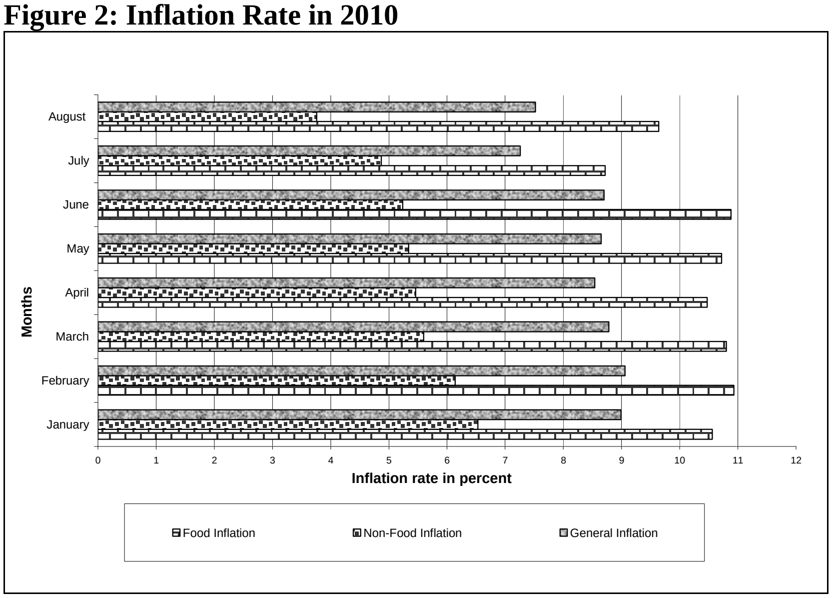
To achieve 8 percent GDP growth, a total amount of output worth Tk.22380.7036 billion at constant price of 1995-96 will have to be produced within the country by the 2014-15, as unemployment has increased to 5.1 percent in the recent years. Therefore, if rate of unemployment cannot be reduced to 4.3%, the target of the government to achieve the GDP growth rate of 8 percent may be hindered because a total of Tk. 358 billion of output would be less produced between FY 2011 to FY 2015 due to higher rate of unemployment. As a consequence of rising unemployment, the loss of output might be Tk. 119.36 billion per annum, on average, in the upcoming five years.

2. Inflation Situation of the Country

If rate of unemployment cannot be reduced to 4.3%, the target of the government to achieve the GDP growth rate of 8 percent may be hindered because a total of Tk. 358 billion of output would be less produced between FY 2011 to FY 2015 due to higher rate of unemployment. As a consequence of rising unemployment, the loss of output might be Tk. 119.36 billion per annum, on average, in the upcoming five years.

Inflation in recent months and for couple of years seems to exceed the expectations. The average rate of general inflation in the present calendar year 2010 is 8.44 percent, with the non-food inflation close to 5.37 percent and food inflation 10.34 percent.

Figure 2: Inflation Rate in 2010



Source: National Accounts Reports by B.B.S

The general inflation rate was above 8.5 percent until the middle of 2010, because both the non-food inflation and food inflation were high (Figure 2). Non-food inflation was above 5 percent and food inflation was above 10 percent during this period. However, in July-August, the average inflation declined close to 7 percent because non-food items inflation reduced to 4.87 percent and then to 3.76 percent. Nevertheless, the general inflation tends to rise in the upcoming months because food-inflation has started to increase again.

The lowest inflation was in the month of July, 2010 at 7.26 percent when both the food inflation and non-food inflation reduced. However, as international price of imported food items are increasing, general inflation may increase further as food inflation would be harder to control.

2.1 Effect of Inflation

Reduction in output growth and increase in food inflation are affecting the price of average food basket of general people and insecurity in job market, resulting in deterioration of the poverty situation of the country. International Food Policy Research Institute (IFPRI) recently published the Global Hunger Index in which Bangladesh finds its place in one of the lowest rank among the South Asian countries.

Table 4: Global Hunger Index 2010

Rank	Country	1990	2010
39	Srilanka	21.1	14.5
52	Pakistan	24.7	19.1
56	Nepal	27.5	20
67	India	31.7	24.1
68	Bangladesh	35.8	24.2

Source: http://www.ifpri.org/publication/2010-global-hunger-index

Global Hunger Index Explanation:

- Score ≥ 30.0 ,extremely alarming
- 20.0 to 29.9 ,alarming
- 10 to 19.9 ,serious problem
- 5.0 to 9.9 ,moderate hunger
- < 5 ,low huger

Bangladesh is in the alarming position with 24.2 score. The increased average inflation is making the situation worse. Not only a vast amount of population is in hunger but also children are the worst victims of this situation.

Twenty-nine countries still have levels of hunger that are “extremely alarming” or “alarming’ in the Global Hunger Index, 2010. Bangladesh is in the alarming position with 24.2 score. The increased average inflation is making the situation worse. Not only a vast amount of population is in hunger but also children are the worst victims of this situation. 54 out of every 1,000 children do not survive to their fifth birthday. Thus to ensure food security the government must also ensure adequate supply of food along with a favourable price which will allow the people to meet their food demand.

2.2 Sources of Inflation

Bangladesh is a net food importing country. Thus if the price of the food-items increase in the international market and necessary stock of food is not adequate, the prices in the domestic market rises.

According to the latest available data, the international Food and Agriculture Organisation made a Food Price index.

Table 5: FAO Food Price Index in 2010

Months	Food Price Index	Cereals Price Index	Oils Price Index	Sugar Price Index
January, 2010	174.01	170.28	168.78	375.53
February, 2010	170.13	164.21	169.23	360.82
March, 2010	162.76	157.76	174.81	264.82
April, 2010	164.58	154.83	173.51	233.42
May, 2010	164.39	155.11	170.39	215.72
June, 2010	162.58	151.20	168.39	224.94
July, 2010	166.73	163.33	174.41	247.36
August, 2010	176.90	185.25	192.38	262.70
September, 2010	188.22	208.37	195.26	315.52

Source: http://www.fao.org/worldfoodsituation/FoodPricesIndex/en

The growth rate of Food Price Index was 2.55 percent in July, it increased by 6.10 percent in August and in September it increased by 6.40 percent.

The index is showing that, food price Index started to decline from March 2010 to June 2010 than the starting period of this year. But it started to increase from July, 2010. The growth rate of Food Price Index was 2.55 percent in July, it increased by 6.10 percent in August and in September it increased by 6.40 percent. The cereals, oil and sugar price index are following the same trend and thus an upward trend can be seen in the international food market in recent months.

The global situation may affect the future cereal import and also the food stock of Bangladesh.

Table 6: Cereal situation of Bangladesh (In lakh metric ton)

Particulars	**July - August, 2010**	**July - August, 2009**
1. Imports (Rice & Wheat)	6.03	1.31
2. Procurement (Rice & Wheat)	2.63	4.05
3. Distribution (Rice & Wheat)	1.20	2.04
4. Food Stock	7.77**	13.76**

Source: Bangladesh Food Situation Report, FPMU, Ministry of Food & Disaster Management, Govt. of the Peoples Republic of Bangladesh.
*=After 12% deduction for FY08, FY09 & FY10 and 10% for other years for seed, feed, waste etc.
** including transit stock

Stock of food grains (including transit stock) with the government stood lower at 7.77 lakh metric tons at the end of August, 2010 compared to 13.76 lakh metric tons at the end of August, 2009. The food stock is lowest after the FY 2007-08.

Import of food grains during July-August, 2010 stood higher at 6.03 lakh metric tons compared to 1.31 lakh metric tons in the same period of the previous year (Table 6). However, stock of food grains (including transit stock) with the government stood lower at 7.77 lakh metric tons at the end of August, 2010 compared to 13.76 lakh metric tons at the end of August, 2009. The food stock is lowest after the FY 2007-08.Thus, if the domestic production of rice could not be increased, further import demand of rice and wheat might be necessary to meet the domestic demand. As international price is increasing so it may add fuel to food inflation.

If the domestic production of rice could not be increased, further import demand of rice and wheat might be necessary to meet the domestic demand.

International price is increasing so it may add fuel to food inflation.

Table 7: Food Grain Situation of Bangladesh. (in lakh metric ton)

Year	Production Target	Actual Domestic Production (Gross)	Difference between target and actual Production	Total Food grain Import
FY 2004-05	300.49	261.33	39.16	33.74
FY 2005-06	275.7	272.65	3.05	25.62
FY 2006-07	322.66	280.49	42.17	24.2
FY 2007-08	336.33	297.74	38.59	34.57
FY 2008-09	343.32	321.66	21.66	30.13
FY 2009-10P	350.51	336.36	14.15	34.55
Average	321.50	295.04	26.46	30.47

Source: Bangladesh Food Situation Report, FPMU, Ministry of Food & Disaster Management, Govt. of the Peoples Republic of Bangladesh.

Since the price in the international market is increasing, the import bill in turn would be higher, resulting in higher food inflation.

The gap between production target and actual production is on average is 26.46 lakh metric ton during the last six years (Table 7). The total food grain import is also on the rise and on an average a total of 30.47 lakh metric ton food grain import is required for every year. Already during the first two months of the current fiscal year 6.03 lakh metric tons were imported. For the remaining year, another 24.44 lakh metric tons of food grain import would be needed. Since the price in the international market is increasing, the import bill in turn would be higher, resulting in higher food inflation.

2.3 Money Supply situation

The tenth issue of Bangladesh Bank (BB)'s half yearly Monetary Policy Statement (MPS) outlines the monetary policy stance for the second half of 2010, in which it decided to put a break on money supply growth. The suggested tools to influence the growth of money stocks, identified in the MPS, are: restriction of broad money growth path, adjustment in cash reserve ratio (CRR) and statutory liquidity requirements (SLR) and restriction in the capital accounts. All the banks were required to maintain five percent of their total demand and time liabilities to Bangladesh Bank as CRR and no less than 18.5 percent as SLR. But BB has raised the CRR and SLR for scheduled banks by one half percentage point from May2010 to restrain the expansion of monetary base. This analysis is focused on how such measures are impacting on containment of inflation.

According to MPS for the first half of FY11, the target is to reduce broad money base growth to 18.8 percent in June, 2010 from that of the previous year and to 15.2 percent in June 2011. The reduction target in case of the reserve money is 17.1 percent in June, 2010 from 25.2 percent in May, 2010. Thus, the plan is stabilize growth of reserve money at 13 percent at the end of FY 2011.

2.3.1 Reserve Money

The components of Reserve money are: i) currency outside banks ii) currency in tills of Deposit Money Banks (DMBs) and iii) deposits with Bangladesh Bank.

Table 8: Reserve Money Situation

Months	2008-2009 (taka in crore)	2009-10 (taka in crore)	Year -on-Year growth	Growth rate from previous month
July	52488.9	67709.5	29.0	-
August	52834.6	68530.6	29.7	1.21
September	59789.4	74601.5	24.8	8.86
October	54563.4	68772.3	26.0	-7.81
November	55151.1	73326.2	33.0	6.62
December	59938.2	70566.4	17.7	-3.76
January	58900	70793.4	20.2	0.32
February	58167.5	73119	25.7	3.29
March	59012.8	69553.2	17.9	-4.88
April	61882.5	70545.9	14.0	1.43
May	60942.4	75676.7	24.2	7.27
June	69390.1	81350	17.2	6.39

Source: Author's calculation based on data from Foreign Exchange Policy Department, Bangladesh Bank

The growth rate of the reserve money on a monthly basis is increasing in recent months.

At the start of FY 2010-11 the total reserve money balance was at 80857.3 crore, with 19.4 percent growth than that of the previous year. The growth rate of the reserve money on a monthly basis is increasing in recent months (Table 8). So to reduce the yearly growth rate by June 2011 from 19.4 percent to 13 percent will be tricky.

2.3.2 Broad Money

The Broad Money Supply includes i) currency notes and coins with the public, ii) demand deposit and iii) time deposit.

Table 9: Broad Money Situation

Months	2008-09 (taka in Crore)	2009-10 (taka in Crore)	Year - on-Year growth	Growth rate from previous months
July	251250.6	298095.4	18.6	-
August	254858.5	303606.4	19.1	1.8
September	266904.8	312056.9	16.9	2.8
October	263882.2	312579.4	18.5	0.2
November	268147.1	322999.4	20.5	3.3
December	271978.9	328192.3	20.7	1.6
January	272288.7	327990.7	20.5	-0.1
February	274310.3	334371.1	21.9	1.9
March	278313.3	337579.3	21.3	1.0
April	281902	343040.8	21.7	1.6
May	286515.9	352225.8	22.9	2.7
June	296499.9	363031.1	22.4	3.1

Source: Author's calculation based on data from Foreign Exchange Policy Department, Bangladesh Bank

Year-on-year growth target of reduction to 18.8 percent in June, 2010 was not achieved rather it reached to 22.4 percent.

The year- on- year growth which represents the growth rate of the corresponding months compared to previous year is escalating in case of broad money (Table 9). The monthly growth rate is also positive in recent months. That is why year-on-year growth target of reduction to 18.8 percent in June, 2010 was not achieved rather it reached to 22.4 percent. In July, 2010 the total volume of broad money was Tk. 364383.1 crore and it reached growth rate of 22.2 percent compared with that of the previous year. Since the central bank has not been able to decrease the rate of growth, it might prove to be difficult for the central bank to reach its target of 15.2 percent at the end of the current fiscal year.

It might prove to be difficult for the central bank to reach its target of 15.2 percent at the end of the current fiscal year.

The remittance inflow growth is declining on a monthly basis and it is following a negative rate during April- July 2010, though in August 2010, the inflow posted a positive growth of 3.1 percent due to Eid-Ul-Fitr. But the rate is declining because of some countries banned labour exports for few years (ex: Saudi Arab, Malaysia, Kuwait), new labour markets unavailability, return of workers from abroad (e.g. Saudi Arabia, Malaysia, Libya, Oman) and thus export of workers is declining. As a consequence, the remittance inflow might decrease.

The Central Bank can use this situation to reduce the liquidity but as the inflow in the last fiscal year and in this year is more than US $ 800 million per month. The demand of taka against this huge foreign currency is still large. The liquidity management is still blurred because the broad money growth is still above the target, thus the monetary policy to work properly all the tools should follow closely the target of the MPS declared by Central Bank. Otherwise, some discrepancy may arise.

The rate of inflation in the upcoming months may be higher because of increase in price in international markets and the maintenance of contraction in money supply may be difficult.

The rate of inflation in the upcoming months may be higher because of increase in price in international markets and the maintenance of contraction in money supply may be difficult.

The central bank has to devise instruments that address the sources of the inflation (i.e. supply side). Again, the government and the central bank need to harmonies the monetary and fiscal policies to address the food import demand, rise in the rate of unemployment and loss of opportunity of employment in abroad. This implies that the government has to come up with aggregate demand management policies that raise the purchasing power while the central bank keeps the inflation at tolerable limit which does not reduce the output growth.

The central bank has to devise instruments that address the sources of the inflation (i.e. supply side). Again, the government and the central bank need to harmonies the monetary and fiscal policies to address the food import demand, rise in the rate of unemployment and loss of opportunity of employment in abroad. This implies that the government has to come up with aggregate demand management policies that raise the purchasing power while the central bank keeps the inflation at tolerable limit which does not reduce the output growth.

3. Recent Trade Situation

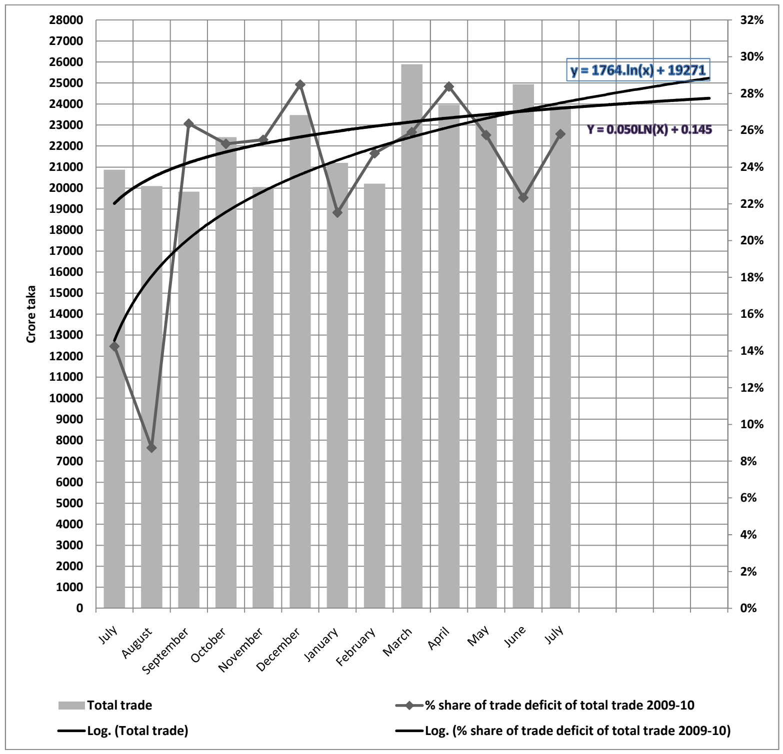
The trade deficit of FY 2009-10 is 1.438 percent higher than it was in FY 2008-09, to the tune of 4174.53 crore taka. The year started with a lower trade deficit of 14 percent in July 2009 but it ended up in July 2010 with a much higher trade deficit of 25.794 percent.

Therefore, basing on the log-linear trend line, the estimation of total trade deficit share is calculated till November 2010.

From July to November 2010, the total estimated sum of trade deficit would be 33518.19 crore take which is 61.728 percent higher than that of the same period of 2009.

From July to November 2010, the total estimated sum of trade deficit would be 33518.19 crore take which is 61.728 percent higher than that of the same period of 2009 (Table 10). Similarly, the estimated sum of trade for July to November 2010 would be 120345.3 crore taka which is 16.549 percent higher for the same months of 2009.

Figure 3: Forecasting about Trade deficit and Total trade till November 2010



Source: Statistics Department, Bangladesh Bank.

Table 10: Estimated statistics regarding the Total trade and Trade deficit till November 2010 (in crore taka)

Year 2010	June	July	August	September	October	November
Trade Deficit	5570	6174	6666.364	6783.903356	6894.621	6999.299
Percentage Share of trade deficit of total trade 2009-10	22.334%	25.794%	27.861%	28.209%	28.534%	28.839%
Total trade	24940	23936	23927.35	24049.08377	24162.96	24269.92

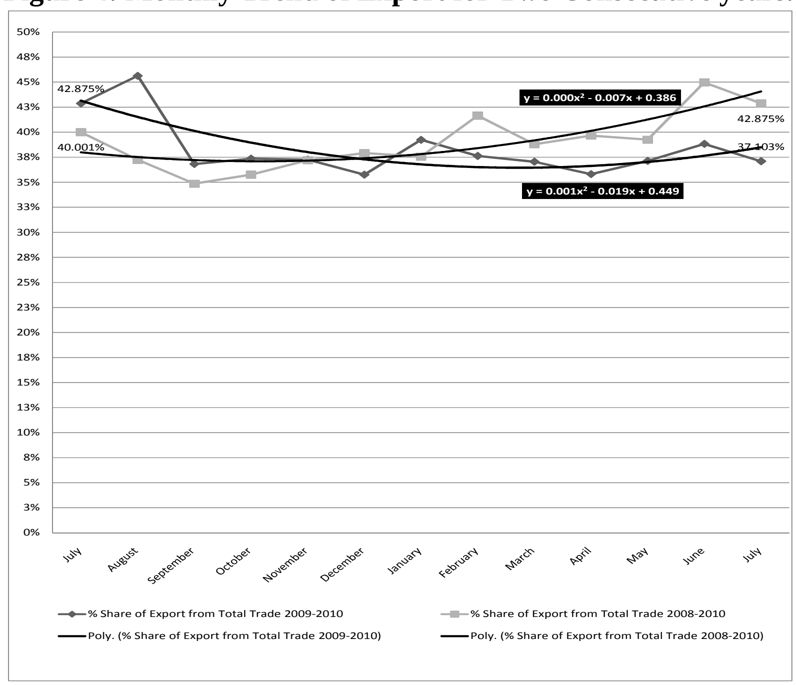
Source: Statistics Department, Bangladesh Bank.

3.1 Export

The monthly export share trends are shown for two consecutive fiscal years 2008-09 and 2009-10 (Figure 4). In FY 2008-09, the export share was 40.001 percent in July 2008 and ended up at a higher percentage of 42.87. However, in FY 2009-10, it started from 42.875 percent and ended at a lower percentage of 37.103. The polynomial trend lines are also supporting the motion trajectory of the line.

The average yearly export share of the total trade has dropped during these two years. It was 38.641 percent in FY 2008-09 and dropped to 38.345 percent in FY 2009-10. This means that the total export difference was -0.296 percent of total trade which further triggered a trade deficit of 859.3146 crore taka.

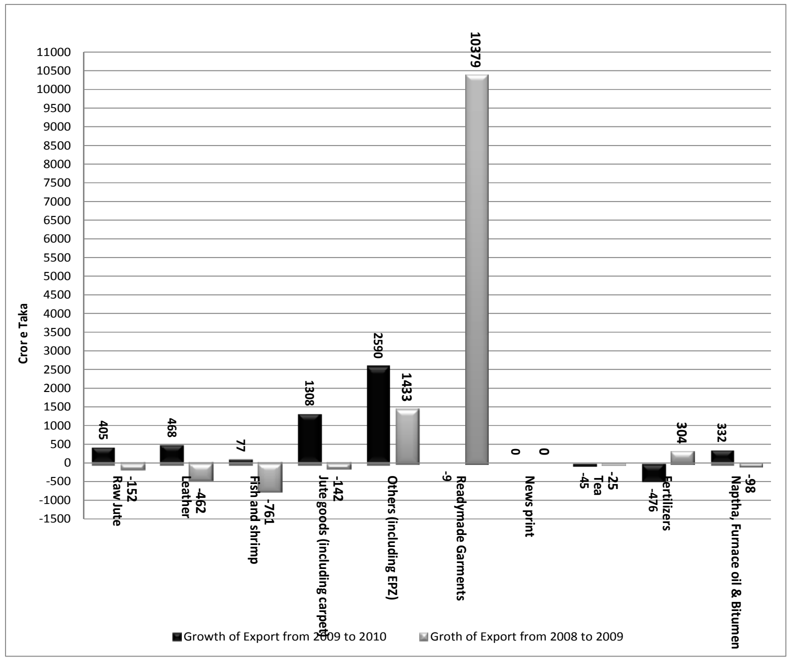
Figure 4: Monthly Trend of Export for Two Consecutive years.



Source: Statistics Department, Bangladesh Bank.

Export in raw jute sector has fallen by 152 crore taka from 2008 to 2009. The business improved by 405 crore taka in the next two years. leather, fish and shrimp and jute (including Jute goods) industries have also made some recovery from 2009 to 2010 despite the loss during 2008 and 2009. Jute goods export has increased the most by 1308 crore taka. On the other hand, export has decreased in readymade garments, tea and fertilizer industries while news print industry made no business whatsoever. However, export in readymade garments increased by 10379 crore taka during 2008 and volume of it decreased in the next two years by 9 Crore taka, this pheonomena has created a massive impact on the growth of export was 10476 crore taka between 2008 and 2009 while it was 4650 crore taka between 2009 and 2010. In order to ensure a rapid growth in the GDP, there is a need to increase export.

Figure 5: Comparative Growth of Export for Different Goods.

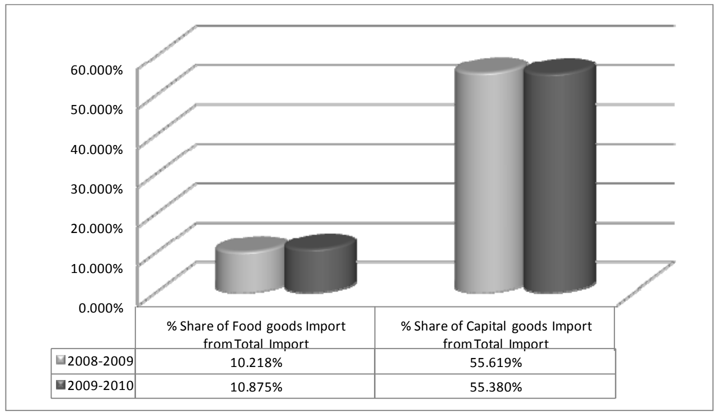


Source: Statistics Department, Bangladesh Bank.

During these two fiscal years, the import for food good items has increased from 10.218 percent to 10.875 percent. At the same time the import of capital goods has decreased from 55.619 percent in 2008-09 to 55.380 percent in FY 2009-10. This implies that in the FY 2009-10, the magnitude of import for capital good has decreased in comparison to the import of FY 2008-09 by 0.239 percent.

export growth. The gross 2009. Though,

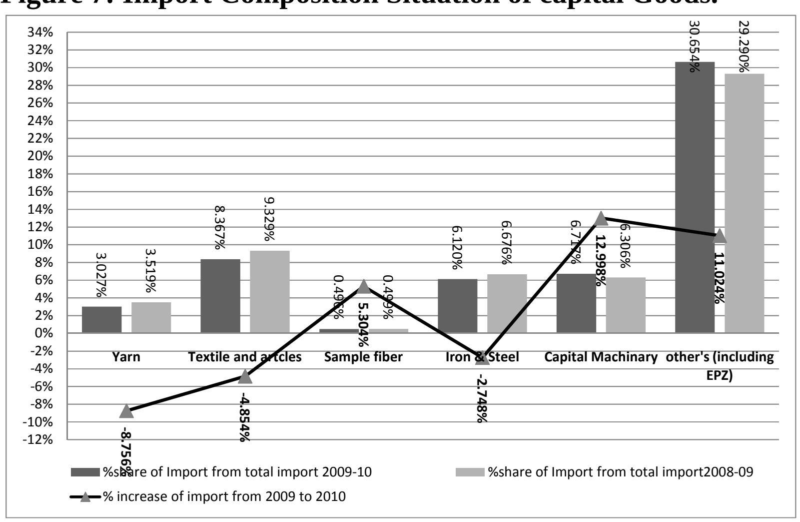
Figure 6: Comparison between Food goods and Capital goods for two different years.



Source: Statistics Department, Bangladesh Bank.

The import share for yarn, textile has decreased in FY 2009-10 compared to FY 2008-09. The decrease in import was 8.756 percent for yarn and 4.854 percent for textile. This reduction also explains negative growth of export in our readymade garment sector. The import of iron and steel has decreased by 2.748 percent in FY 2009-2010 compared to FY 2008-09 which may have a negative effect on the infrastructural development of the country. The volume of import for capital machinery has increased by 12.998 in FY 2009-10 percent from those of FY 2008-09.

Figure 7: Import Composition Situation of capital Goods.



Source: Statistics Department, Bangladesh Bank.

References

Andres J. and I. Hernando (1997). Does inflation harm Economic Growth? Evidence for the OECD, *Banco de Espana Working Paper 9706.*

Barro R. J. (1995). Inflation and Economic Growth, *NBER Working Paper 5326.*

Faria, J. R. and F. G. Carneiro. (2001). Does High Inflation Affect Growth in the Long and Short-run?, *Journal of Applied Economics Vol. IV, No.1*.

Ghosh, A. and S. Phillips. (1998). Warning: Inflation may be Harmful to your Growth, *IMF Staff Papers Vol. 45, No.4.*

Ghosh, A and S. Philips. (1998). Inflation, Disinflation, and Growth, *IMF Working Paper*.

Sarel, M. (1995). Non-Linear Effects of Inflation on Economic Growth, *IMF Working Paper No. WP/95/56.*

Joseph E. Stiglitz and Carl E. Walsh. (2005). *Economics fourth edition,* New York, London: W.W. Norton & Company. pp 503