



Monetary Policy Update

Bangladesh Bank Decreased Policy Rates by 50 basis point at Jan-July 16 Semi-Annual MPS

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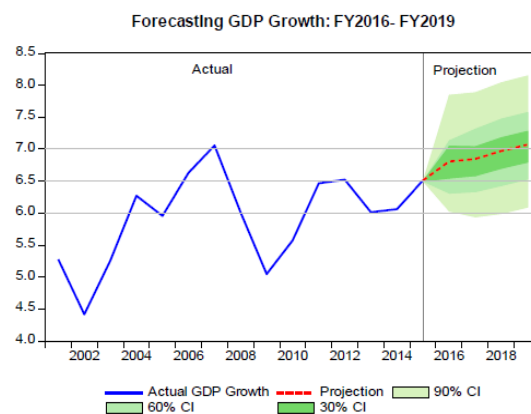
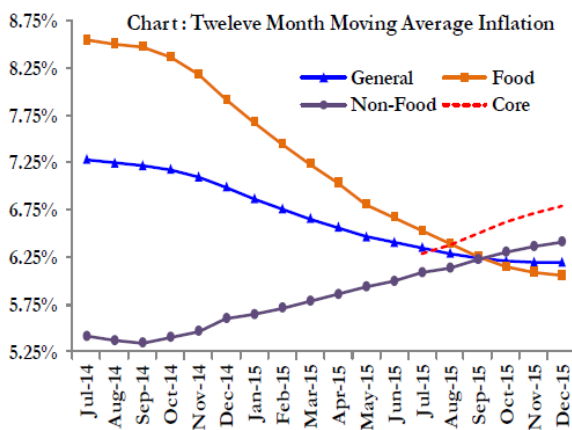
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- Bangladesh Bank finally cut official interest rates by 50 bp with the benchmark repo and reverse repo rates falling to 6.75% and 4.75% respectively.
- The response in the markets was relatively muted although this can be explained by the fact that the cut was already leaked in the newspapers before the official release of the MPS report.
- Moreover, official market interest rates have already fallen sharply in recent months so to a large extent the cut in official rates was a lagged adjustment to market reality.
- The fall in market interest rates was driven by the excess liquidity in the financial system which in turn reflects relatively disappointing recovery in private sector credit growth which was 13.7% in November, below BB official target of 15%.
- It may be that the debt overhang both in terms of margin loans in the stock market and NPLs in the real estate sector as well as with commodity trading houses is depressing demand and the failure to respond to the decline in market interest rates.
- The next major focus as far as BB policy is concerned is exchange rates. We understand that BB has set up an internal committee to explore the case for a devaluation of the taka.
- Although reserve growth has been robust and the BOP situation healthy, the twin threats of the collapse in oil prices slowing remittance growth and weakness in China depressing exchange rates of RMG export competitors such as Vietnam and Indonesia suggest it would be prudent for Bangladesh to allow a modest 5% depreciation of the Taka versus USD exchange rate taking the BDT/USD rate to 81-82.
- We have an end-2016 DSEX target of 5500 with a risk to the upside. In response primarily to the decline in interest rates that will reduce the attractiveness of alternatives to holding equities.



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