BRAC EPL STOCK BROKERAGE LTD

BRAC EPL Research
research@bracepl.com

# No Major Change in the Monetary Policy for Jul-Dec 2018

Macroeconomic Report
July 31, 2018

Bangladesh Bank (BB) published Monetary Policy Statement (MPS) for the first half of FY18 on 31 July 2018. The inflation and growth target remain in a similar range, indicating policy continuation without any surprise in this MPS. The repo and reverse repo rates will remain unchanged at 6.0% and 4.75% respectively for Jul-Dec 2018.

## Monetary Policy Statement for Jul-Dec 2018: Key Figures

| *Figures in Percentage* | Targets in Dec 2017 | Actual in FY 2018* | Targets in Jul 2018 |
|---|---|---|---|
| **GDP Growth Rate** | 7.40 | 7.65 | 7.5 — 7.7 |
| **Inflation** | 5.50 | 5.78 | 5.4 — 5.8 |
| **Repo Rate** | 6.00 | 6.00 | 6.00 |
| **Reverse Repo Rate** | 4.75 | 4.75 | 4.75 |
| **Broad Money Growth Rate** | 13.30 | 9.20 | 10.20 |
| **Domestic Credit Growth Rate** | 15.80 | 14.60 | 15.90 |
| **Private Sector Credit Growth Rate** | 16.80 | 16.95 | 16.80 |
| **Public Sector Credit Growth Rate** | 12.10 | -2.50 | 8.60 |

**as of Jun 2018, Source: Bangladesh Bank*

## Inflation Projection Slightly Increases to 5.80%

### Results in FY 2018 & Proposed Policy

- Current 12-months average inflation stood at 5.78% as of June 2018, slightly above the target rate 5.5%.
- Central Bank projects average inflation to be 5.4% — 5.8% for Jul-Dec 2018.

| *Figures in Percentage* | Actual Inflation | Target Inflation |
|---|---|---|
| **2H2013** | 7.70 | 7.50 |
| **1H2014** | 7.53 | 6.0 — 6.5 |
| **2H2014** | 7.35 | 6.0 — 6.5 |
| **1H2015** | 6.99 | NA |
| **2H2015** | 6.40 | 6.50 |
| **1H2016** | 6.19 | 6.20 |
| **2H2016** | 5.92 | 6.07 |
| **1H2017** | 5.52 | 5.80 |
| **2H2017** | 5.44 | 5.80 |
| **1H2018** | 5.78 | 5.50 |
| **2H2018** | NA | 5.4 — 5.80 |

*Source: Monetary Policy Statement, Jul 2018*

### Analyst Notes

The flood-related domestic shocks in FY 2018, along with higher global commodity prices were reflected in a slight uptick in the average inflation. The trend of global high commodity prices, accompanied by a deteriorating BDT exchange rate against USD, is expected to continue in FY 2019. Therefore, we assume that the average inflation in FY 2019 is likely to be 50-75 basis points higher than Bangladesh Bank's projection. Any major external or domestic shock will edge the inflation even higher.

| *Breakdown of Inflation* | Actual Inflation (%)* | Trend |
|---|---|---|
| **General Inflation** | 5.78 | Downwards |
| **Food Inflation** | 7.10 | Downwards |
| **Non — Food Inflation** | 3.70 | Upwards |
| **Core Inflation^** | 3.80 | Upwards |

**as of Jun 2018, ^excludes food, oil and commodity prices, Source: MPS*

## Bangladesh Bank Assumes GDP Growth Rate between 7.5% — 7.7%

### Results in FY 2018 & Proposed Policy

- Real GDP increased by 7.65% in FY 2018, mainly driven by strong remittance inflows and domestic consumption.
- Bangladesh Bank projects GDP growth to be 7.5% — 7.7% in FY 2019.

### Analyst Notes

BB's projection of GDP growth rate for 2019 is 40 — 120 bps higher than those of many international bodies. Political unrest due to the upcoming national election in 2018 and escalation of global trade conflicts can further deteriorate the projected GDP growth rate in FY 2019.

## Private Sector Credit Growth Target Remains at 16.8%

**Results in FY 2018 & Proposed Policy**

- In FY 2018, Broad money growth rate of 9.2% was well below the target rate of 13.3%.
- To improve liquidity conditions, Bangladesh Bank cut the repo rates by 75 bps and increased available repo tenures to 7, 14 & 28 days. BB also reduced the cash reserve ratio by 1 percentage points to 5.5%.
- Domestic credit remained slightly below the targets set in the last MPS despite a small stronger-than-expected growth of credit to the private sector.
- Target broad money growth rate, domestic credit growth rate and private sector credit growth rate is set at 10.2%, 15.9%, and 16.8% respectively for Dec 2018.

| *Sectorial Growth of Private Sector Credit* | Growth Rate (%)* | Trend |
|---|---|---|
| **Construction** | 18.00 | Upwards |
| **Industry** | 25.00 | Downwards |
| **Transport** | 26.00 | Upwards |
| **Consumer Finance** | 4.10 | Downwards |

**as of Jun 2018, Source: MPS*

**Analyst Notes**

Higher than planned sales of National Savings Certificate (NSC) in FY 2018 was the main reason for the low domestic credit growth as the government used the excess fund to pay off bank borrowings, T-bills, and T-bonds. The high-interest rate of NSCs is distorting the overall interest rate environment in Bangladesh. Even though BB recognizes the issue in this latest MPS, no detailed outline to solve this problem is yet to be announced.

Liquidity is mostly concentrated in state-owned banks whereas private banks are fighting for deposit growth. Even though bankers have successfully persuaded government to allow state-owned institutions to place 50% (previously 25%) of their deposits in private banks, we are yet to see significant movement of the deposit base. Moreover, the recent self-imposed rates of 6% deposit and 9% lending of the private banks makes the liquidity scenario overcomplicated.

## No Major Change in the Policy Rates

**Results in FY 2018 & Proposed Policy**

- Call money rate ranged between 2.0% to 4.5% in FY 2018.
- Lending rate increased to 9.96% as of May 2018.
- Deposit Rate increased to 5.51% as of May 2018.
- Faster increase in deposit rates tightened the spread by 27 bps in FY 2018.
- Non-performing loans edged up to 10.8% in March 2018.
- Repo rate and reverse repo rate remained at 6.0% and 4.75% respectively for Jul-Dec 2018.

**Analyst Notes**

Call money rate is down because of two reasons– first, banks acquired a handsome amount of deposit during Jan -Jun 2018 at an interest rate close to that of the government NSCs. Second, according to many bankers, BB put an unofficial indicative cap on call rate at ~4.0%. Whenever liquidity was tight and a bank had to borrow desperately, the lender bank would just offer a short-term loan at a rate higher than 4%. Call market was placid due to these reasons.

As a large proportion of non-performing loans (NPL) reduces the effectiveness of monetary policy in any country, the high NPL in Bangladesh is maladaptive to investment and growth. The stressed loan ratio (NPL + Rescheduled and Re-structured loans) reached 19.0% at the end of Dec 2017 although Gross NPL was 9.3%. There are 14 scheduled banks who have more than 20% stressed loans. Worst 5 and 10 banks held 47% and 67% of total stressed loans respectively at the end of Dec 2017. Among the worst 10 banks, six are State-owned and four are Privately-owned banks. We are yet to see any concrete plan by the central bank and the government regarding containing the NPL situation. Although we believe merger and acquisition is the credible way out of this mess, things will get worse before they get better. The next government will have to take some toiling decisions soon after election.

**BRAC EPL Research**
research@bracepl.com

## BB Vaguely Indicates to Decrease Interventions in Currency Markets

### Results in FY 2018 & Proposed Policy

- Current account deficit widened to 3.3% of GDP in FY 2018, primarily due to 25.0% increase in imports.
- Exports registered a growth of 6.0% in FY 2018.
- Remittances posted 17.3% growth in FY 2018.
- BB expects ~16.0% growth in remittance inflow and ~8.0% growth in exports, and import growth to moderate to ~12.0% in FY 2019.
- BDT exchange rate depreciated by ~4% in FY 2018.
- BB expects foreign exchange rate volatilities to subside.

### Analyst Notes

The high import growth in FY 2018 occurred due to the amalgamation of poor harvests and the initial development of some mega projects. As these one-off events are unlikely to materialize again in FY 2019, our expectation for import growth in FY 2019 is in line with that of Bangladesh Bank. However, despite the drop in import growth, the current account deficit is expected to be ~3.0% in Dec 2018. Bangladesh Bank vaguely indicates to cut its interventions in the currency market, and if actualized, we expect the BDT depreciation to accelerate in the second half of the year. We assume BDT to depreciate by ~3.0% in Jul-Dec of 2018, which puts the BDT-USD exchange rate in a 86.5 - 87.0 range at the end of the year.

BRAC EPL
STOCK BROKERAGE LTD

## IMPORTANT DISCLOSURES

**Analyst Certification:** Each research analyst and research associate who authored this document and whose name appears herein certifies that the recommendations and opinions expressed in the research report accurately reflect their personal views about any and all of the securities or issuers discussed therein that are within the coverage universe.

**Disclaimer**: Estimates and projections herein are our own and are based on assumptions that we believe to be reasonable. Information presented herein, while obtained from sources we believe to be reliable, is not guaranteed either as to accuracy or completeness. Neither the information nor any opinion expressed herein constitutes a solicitation of the purchase or sale of any security. As it acts for public companies from time to time, BRAC-EPL may have a relationship with the above mentioned company(s). This report is intended for distribution in only those jurisdictions in which BRAC-EPL is registered and any distribution outside those jurisdictions is strictly prohibited.

**Compensation of Analysts:** The compensation of research analysts is intended to reflect the value of the services they provide to the clients of BRAC-EPL. As with most other employees, the compensation of research analysts is impacted by the overall profitability of the firm, which may include revenues from corporate finance activities of the firm's Corporate Finance department. However, Research analysts' compensation is not directly related to specific corporate finance transaction.

**General Risk Factors:** BRAC-EPL will conduct a comprehensive risk assessment for each company under coverage at the time of initiating research coverage and also revisit this assessment when subsequent update reports are published or material company events occur. Following are some general risks that can impact future operational and financial performance: (1) Industry fundamentals with respect to customer demand or product / service pricing could change expected revenues and earnings; (2) Issues relating to major competitors or market shares or new product expectations could change investor attitudes; (3) Unforeseen developments with respect to the management, financial condition or accounting policies alter the prospective valuation; or (4) Interest rates, currency or major segments of the economy could alter investor confidence and investment prospects.


**BRAC EPL Stock Brokerage Limited**

**Research**

| | | | |
|---|---|---|---|
| Ayaz Mahmud, CFA | Deputy Head of Research | ayaz.mahmud@bracepl.com | 01708 805 221 |
| Md. Sakib Chowdhury | Research Analyst | sakib.chowdhury@bracepl.com | 01709 641 247 |
| S. M. Samiuzzaman | Research Analyst | sm.samiuzzaman@bracepl.com | 01708 805 224 |
| Sadman Sakib | Research Associate | sadman.sakib@bracepl.com | 01730 727 939 |
| Ahmed Zaki Khan | Research Associate | zaki.khan@bracepl.com | 01708 805 211 |
| Md. Rafiqul Islam | Research Associate | mrafiqulislam@bracepl.com | 01708 805 229 |

**International Trade and Sales**

| | | | |
|---|---|---|---|
| Ahsanur Rahman Bappi | Head of International Trade & Sales | bappi@bracepl.com | 01730 357 991 |

**BRAC EPL Research**
www.bracepl.com

Symphony, Plot No.: S.E.(F) – 9(3rd Floor), Road No.: 142
Gulshan Avenue, Dhaka – 1212
Phone: + (880)-2-9852446-50
Fax: + (880)-2-9852451-52
E-Mail: research@bracepl.com