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Monetary Sector And National Development In Bangladesh

By

Nazimuddin Mostan
MONETARY SECTOR AND NATIONAL DEVELOPMENT
IN BANGLADESH.

- NAZIRUDDIN HOSEIN.

Rural economy of Bangladesh monetised to the present extent only after war of Liberation. Till the mid 70.5 36 percent of the whole economy were in pre-monetised state, where service and produces directly were being used by the producers themselves by passing the market and exchanging all these through money. So, it is natural that in late 80.5 econometric model builders of monetary expansion are of the opinion that rate of inflation in Bangladesh has not kept pace with the growth of money supply. They cited the example of 1980-85, when average annual growth rate of money supply was 26% compared with the average annual rate of change in the consumer price index of 11.4%.

It is better, to presume at this state, that, price movement in Bangladesh may be better explained by changes in real phenomena rather than by changes in the nominal money supply. Moreover, changes in the nominal supply of money have significant real effect in the longrun.

So, with the academicians we may also note that, inflation in Bangladesh is not a purely monetary phenomenon. Significant impact of nonmonetary factors on prices is there. Rate of inflation in the longrun is not equal to the rate of growth in the money supply. The length of time-lag during which money exerts an impact on prices presents an interesting departure from what generally thought of.

Following the war of Liberation monetary and credit policy of the Government supported the program for reconstruction. Money supply (\(M_1\)) increased by Tk. 120.75 cr in 1973-74. Impact was an increase in wholesale price index (\(WPI\)) by 59.8% in the following year, 1974-75. Next year, in 1974-75 money supply was reduced by 2.25 Cr. taka from that level of 1973-74. As a result \(WPI\) decreased to 9.9% in the following year, 1975-76. This trend has been observed although the decade with the
exception of the period from 1980-81 to 1983-84 where trend of money supply does not explain the cause of change in whole sale price index, i.e., behaviour of inflation.

From 1976-77 to 1979-80 the supply of additional money within the system was over tk. 200 crore every year. During the period from 1975-76 to 79-80 the supply of wage goods was more or less smooth which kept the trend of inflation within tolerable limit.

With gradual increase in supply of money and increase in aggregate demand through public development financing, borrowings of public sector Corporation, Credit expansion and Central Banks lending to the Government to support the losing public sector Corporation, there has been humble increases in G.D.P. and in supply of wage goods.

It was also a time when food for works programme was in full swing. There has been good years, when agricultural production increased continuously. All these factors kept the flow of supply of goods at a reasonable level which kept the rate of inflation at an average of below 10% per year which was lower than international average rate of inflation during the period. The movement of time deposit with banks offered an additional relief to public pressure. Since 1976-77 the level of time deposits has been on the continuous increase. It appeared that impact of an increase in Time Deposit has an instant impact on price. While supply of M affects the price level with time lag, the impact of the withdrawal of money from liquidity is simultaneous this liquidity pressure appeared again in the economy before the advent of the flood in 1988.

Though time deposit was functioning as 'Lever' yet it will appear that phenomenon of money supply and inflation are not quite well explained by money and banking statistics.
I-L does not explain the phenomenal increase in inflation equally throughout the post-independence period. It somehow explained the inflation quite well before 1975-76 and moderately during 76-77 to 79-80, but last 3 years from 81-82 to 83-84 are not explainable. Impact of public expenditure, wage earners money released against foreign exchange, cost aspect, relief and capital flight must have been the unexplained factor, to be taken into consideration, the case of savings, employment and Investment.

Credit creation and its management is the miracle of the monetary sector through which nations can achieve their cherished goal. In Daniel Webster's world, Credit has done more a thousand times more to enrich nations than all the mints of the world. It has excited labour, stimulated manufacturing, pushed commerce on every sea and brought every nation to ample.

Total credit delivered by different institutions for various purposes amounted to Taka 5020 crore in June, 1983 - recording a rise of 172% to over 1846 crore taka in June, 1979. It further rose to Taka 6073 crore taka in the end of 1984. In the financial year 1984-85 it expanded further 20.5% to 11000 crore taka.

Credit scenario in Bangladesh expanded enormously from agricultural credit to rural credit, small credit, loan to small scale and cottage industry, housing, transport, financing nontraditional export, jute finance, Industrial finance, to recent trend in consumer finance and rehabilitation finance.

Public sector, Central and Urban bias distribution of credit sustained the Governmental structure, though its financial institutions are thriving on over the savings and Investment of the private small savers and entrepreneurs. So investment in the public sector is the function of foreign aid and savings on the part of the government and people. Investment in private sector of Bangladesh is highly responsive to National Income. Income elasticity of private Investment in this economy is high. Role of National income in determining the volume of Investment is significant even at the highest level of confidence (upto 99%).
Investment in private sector of Bangladesh is less responsive to rate of interest. Rate of elasticity between rate of interest and investment is very low. This is a relevant result corresponding to inflationary situation in the country.

These facts and trends are characteristics of a developing economy where per capita income is low, shortage of capital is the crux of problematics, population problem creates imperatives of various dimensions. Our central bank—in a regional workshop on monetary management identified the following social aspects of such economies such as, political problem, population, unemployment, problem of domestic resource mobilisation, problems, in agriculture and industry, failure in the management of money and finance, and the external factors. Beyond money and through money these factors have their contribution positive and detrimental both in the economy of Bangladesh.

These factors still unresolved. As such the controversy about direct allocation versus allocation by price mechanism, balance versus unbalanced growth, Industry versus Agriculture, labour intensive versus capital intensive, import substitution versus export oriented growth, ways of income distribution yet not over.

Keeping these facts and facets in minds we may conclude by going through the paragraph drafted and documented by IBRD Staff about recent Bangladesh.

Monetary expansion brought under control over last eighteen months. In contrast with a growth of 42% in FY 84, broad money rose by 17% in FY86 and would have grown less had the balance of payment (net financial assets) not shown unexpected strength in the year. Broad M2 also rose by 17% in FY, largely due to the improvement in the Net foreign assets.

Demand management of the rate of inflation fell below 10% in FY 86. However in the first half of FY 87 inflation rose, led by higher food prices.

Good management of the monetary sector and bad intention in the management of public affairs creates problem, which can be seen in the headline in newspapers and also in the IBRD report, that stagnation of recovery at a part of four nationalised
commercial Banks, two DPI, and agricultural credit banks has been greatest threat to stability over last years.

...e must have to admit that instability in the monetary sector do create political instability in some occasion, yet when managed properly monetary sector creates favourable economic environment even for the authoritarian management.

In Bangladesh, money moves, still it is not prime mover.