

THE EFFECTIVENESS OF THE CHANNELS OF MONETARY POLICY TRANSMISSION OF BANGLADESH: A PATH ANALYSIS APPROACH

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Abstract

This paper examines the effectiveness of four major monetary policy transmission channels in the post reform period of Bangladesh using quarterly data from fiscal year 1998 to 2013. There have been a few empirical analyses on the monetary policy transmission channels of Bangladesh. Majority of those applied VAR or standard VAR model to evaluate the strength of those channels of effecting real output level. Nonetheless SVAR/VAR model suffers from serious shortfall as any theory of monetary transmission mechanism assumes the existence of some degree of friction (i.e., stickiness) and VAR model doesn't resolve this problem. In our investigation we applied "Path Analysis" to examine simultaneous impact of all the channels of monetary policy. The paper finds that, monetary policy works in the desired direction in affecting both output and price level. Credit channel and exchange rate channel of monetary policy transmission seem to be quite strong. We also found asset price channel is also has very prospective in influencing output and price level in Bangladesh. Our analysis exemplifies interest rate channel has very weak influence or no influence on output and price level in Bangladesh.

Keywords: Path analysis, SME, Monetary policy, Price level, Exchange rate, Credit, Lending rate, Stock price

JEL classification codes: C6, E3, E4, E5, E6