

## CHAPTER II

### LITERATURE REVIEW

#### 2.1 Overview of Bangladesh Economy

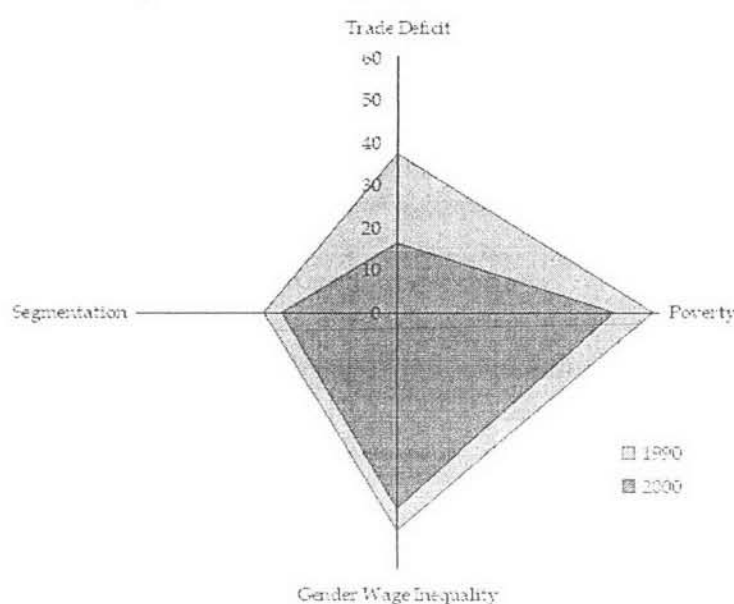
Despite sustained domestic and international efforts to improve economic and demographic prospects, Bangladesh remains a poor, overpopulated, and inefficiently-governed nation. Although more than half of GDP is generated through the service sector, nearly two-thirds of Bangladeshis are employed in the agriculture sector, with rice as the single-most-important product (Bangladesh Economic Review, 2006). Major impediments to growth include frequent cyclones and floods, inefficient state-owned enterprises, inadequate port facilities, a rapidly growing labor force that cannot be absorbed by agriculture, delays in exploiting energy resources (natural gas), insufficient power supplies, and slow implementation of economic reforms. Reform is stalled in many instances by political infighting and corruption at all levels of government. Progress also has been blocked by opposition from the bureaucracy, public sector unions, and other vested interest groups. On an encouraging note, growth has been a steady 5-6% for the past several years (Bangladesh Statistical Yearbook, 2004).

Bangladesh is an economy firmly in transition, with the manufacturing and services sector increasing in importance as a share of GDP, and agriculture declining. In 1980, agriculture accounted for 56 percent of GDP, manufacturing 13 percent and services 31 percent. By 2003, agriculture had declined, falling to 22 percent of GDP, while manufacturing and services had risen to a little over 27 percent and 52 percent, respectively (BBS, 2004).

To examine the real pulse of a macro economy at a glance is plainly impossible. However, Greater Access to Trade Expansion (2005) published by USAID has used a very impressive technique named 'Development Diamond'

depicting in Figure 2.1, which can track some of the economic indicators by mapping poverty, labor market segmentation, trade, and wage rate indicators for Bangladesh over a 10 year period.<sup>4</sup> While improvements in all indicators are visible, trade and poverty rates register greater improvements than do the indicators of labor market segmentation. This suggests that gender inequality within the labor market remains, demanding greater reactions to ensure poor women benefit from economic and trade expansion activities.

**Figure 2.1: Development Diamond, in percent**



Source: Greater Access to Trade Expansion (GATE), 'Bangladesh: An Economic Snapshot', USAID, January 2005

As there is no hard and fast rule to measure the performance of an economy, the thesis has attempted to explain the prevailing status of Bangladesh based on 8 major goals included in Millennium Development Goals (MDGs).<sup>5</sup>

<sup>4</sup> The trade deficit is measured as  $(X-M)/(X+M)$ , and gender wage inequality as the average gender wage gap as a percentage of male wages  $(W_m - W_f)/W_m$ .

<sup>5</sup> In order to achieve some targeted progress in poverty, education, health, gender equality, sustainable environment and strengthening inter country co-ordination for development, the Millennium Development Goals (MDGs) have been adopted by the United Nations, which contain a set of development activities agreed upon during a series of global conferences over the preceding decade. After review and editing by the United Nations Secretariat, IMF, OECD and The World Bank, the objectives were published in September 2001 as a set of 8 major goals accompanied by 18 targets and 48 indicators for measuring progress towards the goals.

### 2.1.1 Goal I: To Eradicate Extreme Poverty and Hunger

Under the first and foremost goal, i.e. to eradicate extreme poverty and hunger, Table 2.1 has presented the percentage of total population living below poverty line. The data shows that the trend of poverty is downward sloping, where urban poverty is more spreading and hence a threat to the overall development of Bangladesh.

Table 2.1: Poverty Head Count Ratio by DCI<sup>6</sup> Method 1981- 82 to 2000

Survey	% of population below poverty line		
	National	Rural	Urban
2004	40.9	40.1	43.6
2000	44.3	42.3	52.5
1995-96	47.5	47.1	49.7
1991-92	47.5	47.6	46.7
1988-89	47.8	47.8	47.6
*1985-86	55.6	54.7	62.6
*1983-84	62.6	61.9	67.7
*1981-82	71.0	73.0	68.0

Sources: BBS, HIES various years, PMS 2004

\*Poverty estimates were based on 2200 k.cal and for other years 2122 k.cal;

Another way to measure poverty situation is the proportion of income in the lowest and highest quintile that has been presented in Table 2.2. It is observed that the ratio of income of highest quintile to lowest quintile was stable from 1981-82 to 1991-92. It ranges from 6.0 to 7.0. However, in 1995-96 it increased to 8.8 and increased

<sup>6</sup> In the DCI method, the caloric threshold of 2122 k. cal. is used for determining the poverty line. It does not take into account either the income of the households or the price of the food items. Therefore, this method is a crude measure where only food intake in terms of calorie is used for poverty estimation. There is an argument that DCI method estimates "undernourishment" not poverty as it does not take care of other welfare issues. However, the estimate is easy to understand because of the simplicity and transparency of the standard used.

further to 11.0 in 2000. Perhaps, this is the outcome of market friendly economic policies of the government.

**Table 2.2: Proportion of Income in the Lowest and Highest Quintile**

Survey year	Lowest Quintile	Highest Quintile	Ratio of highest quintile to lowest quintile
1981-82	6.64	45.32	6.8
1983-84	7.20	43.38	6.0
1985-86	6.99	46.04	6.0
1988-89	6.64	46.20	7.0
1991-92	6.52	44.87	6.9
1995-96	5.71	50.08	8.8
2000	4.97	55.0	11.0
2004 (PMS)	4.70	52.0	11.1

Source: BBS, HIES and PMS

### 2.1.2 Goal II: To Achieve Universal Primary Education

The primary school enrolment rate is defined by the ratio of the children aged 6-10 years enrolled in the primary school to the total number of children in the same age group. The primary school enrolment rate increased from 69.8% in 1993 to 83.0% in 2000 with some annual fluctuation. It is interesting to note that enrolment rate for girls was higher than that for boys in 1995 and onward. This is a result of that to government scholarship program for primary school.

**Table 2.3: Primary School Net Enrolment Rate**

Sex of Children	Enrolment rate							
	2003	2000	1999	1997	1996	1995	1994	1993
Both sex	83	81.8	78.3	81.5	78.8	82.0	81.3	69.8
Male	81	80.7	76.9	80.0	78.5	81.7	81.5	70.2
Female	84	82.8	79.7	82.9	79.1	82.2	81.0	69.3

Sources: BBS, National Report on follow up to the World Summit for Children and MICS

### 2.1.3 Goal III: To Promote Gender Equality and Empower Women

Gender equality is a core development issue, which needs to be addressed properly. Employed population by sex in 2002-2003 has been presented in Table 2.4. It is observed that of the total employed population of 44.3 million, 34.5 million were male and 9.8 million were female. The proportion of male and female employed population is 77.9 % and 22.1% respectively. Relatively higher proportion of women is employed in services sector, followed sequentially by agriculture and industry.

**Table 2.4: Employed Persons 15 Years and Over by Broad Economic Sector and Sex, 2002-2003**

Broad economic sector	Both Sexes		Male		Female	
	No million	%	No. million	%	No. million	%
Total	44.3	100.0	34.5	77.9	9.8	22.1
Agriculture	22.9	100.0	17.2	75.0	5.8	25.0
Non-agriculture:	21.4	100.0	17.3	80.8	4.1	19.2
Industry	15.3	100.0	13.1	85.6	2.3	14.4
Services	6.1	100.0	4.2	68.9	1.8	31.1

Source: BBS, LFS 2002-2003

### 2.1.4 Goal IV: To Reduce Child Mortality

Infant Mortality Rate (IMR) is an important indicator for assessment of the overall health and sanitation condition of an economy. It is observed in Table 2.5 that infant mortality rate decreased largely over the period. In 1991, it was 92 per thousand live births, which reduced to 53 in 2003. In the rural area, it was 94 in 1991 that reduced to 57 in 2001, and in urban area, it reduced from 69 to 40 during the period.

**Table 2.5: Infant Mortality Rate 1991 and 2001**

Year	Sex	National	Rural	Urban
2003	Both Sexes	53	57	40
	Male	55	58	42
	Female	51	55	37
1991	Both Sexes	92	94	69
	Male	95	98	72
	Female	90	95	65

Source: BBS, Report on SVRS, June 2003

### 2.1.5 Goal V: To Improve Maternal Health

Maternal mortality rate<sup>7</sup> is still high in Bangladesh. It may be mentioned that the definition of maternal mortality has been changed in the recent years as per decision of 10th revision of International Classification of Diseases (ICD).

<sup>7</sup> Maternal mortality rate is defined by number of deaths of women due to pregnancy related causes per 100,000 live births. Bangladesh Bureau of Statistics uses 1,000 live births as the denominator.

**Table 2.6: Maternal Mortality Rate per 1000 Live Births, 2000-2003**

<b>Year</b>	<b>National</b>	<b>Rural</b>	<b>Urban</b>
2000	3.18	3.29	2.61
2001	3.15	3.26	2.58
2002	3.91	4.17	2.73
2003	3.76	4.02	2.70

Source: BBS, SVRS

### **2.1.6 Goal VI: To Combat HIV/AIDS, Malaria and other Diseases**

Human Immune Deficiency Virus (HIV) and Acquired Immune Deficiency Syndrome (AIDS) are of growing concern in the field of health and economic development. In Bangladesh, it is observed that only 30.8% of ever-married women and 50.2% of the currently married men ever heard of the HIV/AIDS. Furthermore, 40.8% of men said that avoiding sex with prostitutes could help avoid AIDS, but for ever married women the highest 18.2% mentioned about other sources followed by sex with the prostitute. Condom as a measure for avoiding AIDS was supported by 17.9% currently married men and 15.5% ever married women.

### **2.1.7 Goal VII: To Ensure Environmental Sustainability**

The water quality of major rivers indicates that Bangladesh is still below the danger level in case of existence of some harmful elements in the river water (Directorate of Environment, 2001). From the perspective of air quality system, it is observed in Dhaka city that in case of suspended particulate matter (SPM) the condition is alarming (i.e., it already exceeded the limit). However, for NO<sub>2</sub> it is still within the limit. Besides, in case of SO<sub>2</sub> the condition is frustrating (Directorate of Environment, 2001).. On the contrary, the proportion of land area covered by forest in the country stands at 17.50% in 2002-2003. It was 12.81% in 1990-91. Finally yet

importantly, access to safe drinking water has improved tremendously in Bangladesh. According to the latest BBS data, 97.4% households have access to safe drinking water, which was 89% in 1990.

### **2.1.8 Goal VIII: To Develop a Global Partnership for Development**

Bangladesh is a member of the United Nations and committed to uphold the policies of the UN. Bangladesh has made significant contributions in UN peace keeping mission in different war ravaged countries. As a Muslim country, Bangladesh has friendly relations with all brotherly Muslim countries. It is a potential member of OIC and working for peace and progress of the Muslim Ummah. Bangladesh has also made positive contribution to non-alignment movement and participated in the last conference held in Malaysia.

Bangladesh has also excellent relations with various UN agencies such as UNDP, UNFPA, UNICEF, FAO, WFP, ILO and UNHCR. They contribute to the development of Bangladesh in many ways. These agencies are also working closely with GOB for achieving MDGs. The UN agencies took specific responsibility on monitoring, evaluation of MDGs. Bangladesh has also excellent relation with European countries, and the European Union is contributing to various development activities of Bangladesh. The other developed countries like the US, UK, Japan, Australia, Canada, New Zealand are also participating in different developmental activities of Bangladesh.

Bangladesh has also pursued an increasingly liberalized policy in the external sector over the last two decades. The liberalization of industrial policies began in the late 1980s with the removal of import controls, which resulted in the elimination of very high implicit tariffs that had characterized earlier trade regime. New rounds of trade reforms were undertaken in the early 1990s. The objective was to achieve further liberalization by reducing import tariffs to significantly lower and uniform



levels. Overall, the policy reforms have included widespread trade liberalization as well as market determined exchange rate.

## **2.2 Inter-temporal Macroeconomic Trends of Bangladesh**

Empirically, there are dozens of macroeconomic indicators that are used to feel the nation's economic pulse. Hence, it is very difficult to make a short list of fundamental macroeconomic variables that can cover the basic scenario of the economy. In this context, Robert J. Gordon (1990)<sup>8</sup> has specified six macroeconomic issues including unemployment rate, inflation rate, productivity of labor, interest rate, government budget deficit, and foreign trade deficit. Here, it is to point out that Gross National Product (GNP) is the most widely used measure of visualizing macroeconomic environment. That is why, it is loyal to include GNP in any short lists of basic macroeconomic indicators. Therefore, the thesis at this stage has attempted to show the general inter-temporal trends of 6 macroeconomic indicators (i.e. excluding the productivity of labor due to unavailability of data) that are given below.

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<sup>8</sup>For more clarification, see Gordon Robert, 1990, "Macroeconomics," Fifth Edition, Harper Collins Publishers:2.

Figure 2.2: Gross National Product at Constant Prices

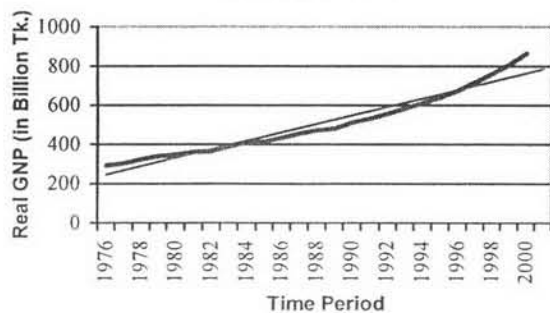


Figure 2.3: Rate of Unemployment (%)

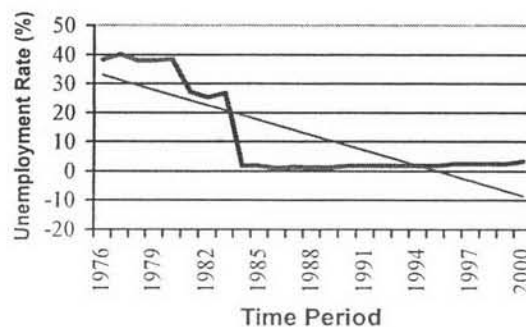


Figure 2.4: Inflation, Consumer Prices (annual %)

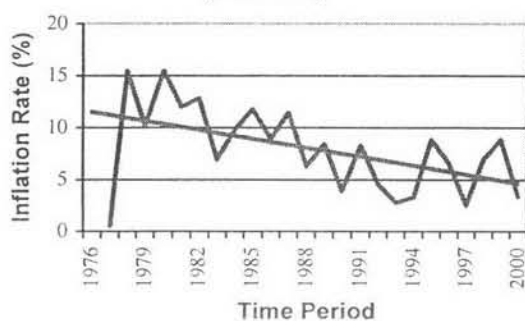


Figure 2.5: Interest Rate Spread of Bangladesh Economy

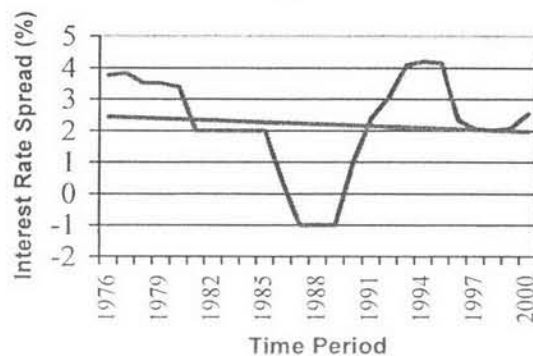
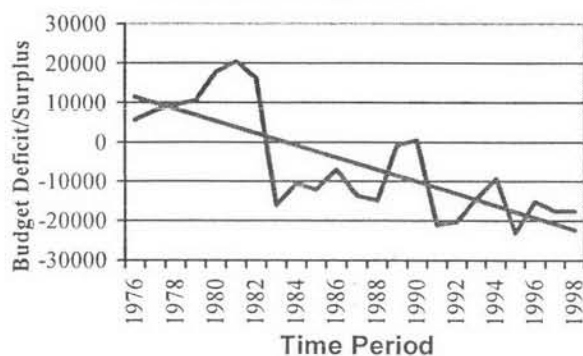


Figure 2.6: Government Budget Deficit or Surplus[-] of Bangladesh



In Figure 2.2, it is observed that there is a positive trend of real GNP over the period 1976 to 2000. It is also envisaged that unemployment rate of Bangladesh is decreasing (in Figure 2.3) continuously from 1976 to 2000. However, it is witnessed that inflation rate of Bangladesh has an ups and down motion throughout the same period. Likewise, it is noticed that interest rate spreads<sup>9</sup> are changing randomly without following any specific trends. It is because the interest rates of Bangladesh are solely determined by the *Bangladesh Bank*<sup>10</sup>. The free market forces are not activated to determine the interest rate. Though it is strictly determined, it can influence on the other economic variables continuously. Hence, interest rate has been included as an exogenous variable in the model (more clarification is provided later). In Figure 2.6, it is clear that there exists a downward sloping inter-temporal trend in government budget deficit over the period 1976-2000.

### 2.3 Review of Bangladesh Macroeconomic Models

Empirical works on constructing macroeconometric models for Bangladesh economy can be traced back to the sixties when macro modeling as a professional academic activity was still in its infancy (Krishnamurty and Pandit, 1984).

Islam (1965) conducted one of the first studies on the macroeconomic model for the Pakistan economy, in which East Pakistan (the present Bangladesh) was treated as a region. The objectives of Islam's study were to formulate an econometric model of Pakistan, undertake statistical estimation, collect, organize, and process both published and unpublished data systematically. In his model, there were 50 equations of which 20 were behavioral equations, and 62 variables of which 12 were exogenous. However, no theory for such an exercise (statistical estimation) was presented. The model was highly aggregative and the specifications of the equations were simple. The simple nature of the equations was partly forced on the model by data limitations. Amongst serious omissions, the specification of the equation for agricultural output

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<sup>9</sup> Here, interest rate spread is the difference between lending rate and borrowing rate of commercial banks.

<sup>10</sup> Bangladesh Bank is the central bank of Bangladesh.

did not recognize the importance of weather conditions and the manufacturing output was not constrained by imported intermediate and raw materials.<sup>11</sup> Besides, the model contained only the real sector of the economy and thus the link between real and monetary sector was not considered.

Later in 1978, a paper prepared by the World Bank attempted to present a model of the Bangladesh economy, but until 1980, virtually any attempt confronted the serious problem of too few observations.

At the University of New Castle, Rashid (1981) developed a short-run macroeconometric model for Bangladesh economy. The primary objective of the model was to help the understanding of the workings of the economy. The model was also quite simple containing six sectors, viz., expenditures, production, monetary, government and foreign trade. There are only 8 behavioral equations in the model and 9 identities. The model, however, represents much realism by capturing both demand and supply constraints on the macroeconomic relationships. Like Islam (1965), Rashid's model is also highly aggregative and cannot explain some special features of the economy. For example, the random shocks in production (mainly in agriculture) created by weather conditions are not recognized. Moreover, the specification of the output equation with labor is of questionable relevance in a labor surplus economy. Further, the price determination process is not stressed in the model. Despite the absence of rigorous formulation of the model (e.g., no policy simulation was carried out, therefore, no definite conclusions about the policy implications of the model were presented), the author made some tentative conclusions based on the signs and magnitudes of estimated coefficients. It was actually the beginning of the attempt to quantify macro model for the Bangladesh economy.

Thereafter, Parikh (1983) constructed a macroeconometric model of the Bangladesh economy using the Keynesian approach of price rigidity with quantity rationing. The model also explicitly delineated the structure of the economy and

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<sup>11</sup> However, the price of manufactures was influenced by price of imported intermediates and raw materials.

interdependence between various sectors of the economy. Another feature of the model distinguished it from the model developed by Islam (1965), as Parikh included the weather factor. However, Parikh's model is confined to strict functional forms. It did not test the equations and therefore, no definite policy suggestions were offered.

Chowdhury (1986) first offered a theoretical framework vector autoregression (VAR) technique as an alternative approach to forecast the macroeconomic model in the context of the Bangladesh economy. However, the model was once again restricted into functional form and no estimation of the parameters was carried out.

Chowdhury, Dao and Wahid (1995) analyzed the relationship between money, output, prices and the exchange rate for Bangladesh using a VAR model with quarterly data over 1974-92 periods. They found, among other things, monetary policy is significant in explaining output, and monetary policy and inflation jointly determine the exchange rate.

After that, Hossain (1995) has formulated a small macroeconomic model for Bangladesh to capture the macroeconomic linkages in the economy using quarterly data for the period 1974:2 to 1985:4. The main objective of the model was to explain the determination of inflation, economic growth, and the balance of payments. The model consisted of six block, viz., the fiscal sector, the monetary sector, the expenditure sector, the production sector, the external trade and payments sector, and wages and prices. In the fiscal sector, different types of nominal taxes are determined which together with exogenous government expenditures determine the budget deficit. The money supply is determined by reserve money and lagged money supply. Reserve money is determined by its various components- both domestic and external. Among the domestic components, Bangladesh Bank's credit to the government is related to government budget deficit and Bangladesh Bank's credit to scheduled banks is related to their total credit and their loan rate. Net foreign assets is determined through an identity in the external sector.

The nexus between output, government deficit, external sector, money supply and inflation are captured in the model. The model can be used to examine the effects of both domestic and external shocks on the economy. The model can also be used to analyze the effects of monetary, fiscal and exchange rate policies on the macroeconomy. Specification of the private expenditure equation is considered in the expenditure block. The private expenditure is modeled in the spirit of Monetary and New Cambridge schools, which consider private consumption and investment expenditure jointly. Private expenditure is determined by real permanent income, the stock of real money balances and the expected rate of inflation. Production is divided into agriculture, manufacturing, and services. Agricultural production is determined by planted acreage and per acre yield. The acreage response function is related to 4 quarter lagged wholesale agricultural price and yield. Yield per acre is determined by fertilizer and rainfall. The short-run variation in manufacturing production is not constrained by capital stock. It depends on real expenditure, real imported raw materials and capital goods, real bank credit and a dummy variable capturing effect of denationalization. Services sector output is determined by real expenditure and real bank credit. On the external front, exports of tea, fish and leather goods are determined under small country assumption but in the case jute and jute goods Bangladesh is believed to influence the world market price. The imports of major commodities are explained by real expenditures, relevant relative price variable and lagged imports. Government adjusts exchange rate based on the movement of relative price of traded and non-traded goods. The complete model consists of 113 equations-34 of which are behavioral- and has 46 exogenous variables. The model is made dynamic by including the lagged dependent variable. The causal structure of the model is as follows: an increase in budget deficit, caused by either increase in government expenditure or reduction in government revenue, increases reserve money, which increases money supply.<sup>12</sup> This, in turn, raises both the price level and imports by increasing real expenditure. Increases in expenditure and imports increase output and government revenue, which reduce the budget deficit and hence the stock of money.

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<sup>12</sup> Reserve money can also change because of changes in net foreign assets caused by changes in exports or imports.

However, this model did not consider the demand side of money market due to the unavailability of data. Although the model used by Hossain captures the linkages in different sectors of the economy, specifications of some of the equations might be problematic. In the fiscal sector, government expenditure is treated as an exogenous variable. The revenue-expenditure of the government has certain degree of automaticity and irreversibility so that it can be regarded as an endogenous variable. This also indicates the limitation of fiscal policy changes especially in the case of reduction of public expenditure. The modeling of private expenditure by aggregating consumption and investment expenditure has been done on the grounds of stability of the function. The lack of separate private investment function in the model misses the link between private investment and the financial sector. Separate treatment of private investment is needed especially in view of its growing importance in the economy. Further, the crowding out or complimentary effect of public expenditure cannot be assessed if private investment is not included in the model separately. Both manufacturing and services production are determined by demand variables and scarce factors of production. The logic of including both demand variables and factors of production on production function can be questioned.

A study carried out by Rahman and Shilpi (1996) at the Bangladesh Institute of Development Studies was an extension of an earlier work undertaken by Rahman (1990) under the South Asian Link Model Project sponsored by the Asian and Pacific Development Centre. The model comprises 42 equations of which 21 are behavioral equations and the rest are identities. The model consists of 5 blocks: viz., expenditure, fiscal, money and finance, trade, and aggregate supply. The model includes 32 exogenous variables and 20 dummy variables.

Real output in the model is determined from an aggregate production function, which includes accumulated capital stock and imported intermediates as the arguments. Capital stock is determined through a dynamic process in which lagged depreciated capital stock and current investment determines the current capital stock. Investment is divided into public investment and private investment. While public



investment is exogenous, private investment is endogenized in the model. Private investment is made to depend on lagged investment, current and lagged interest rate, lagged capital stock and current output. Imports of intermediates are influenced by real output and unit price of these imports. Imports of other types of goods, exports, exchange rate and capital account balance determine the overall balance of payments in the economy.

Nominal output in Rahman and Shilpi model is determined by real output and price, the latter being determined by output, import price and money supply. Nominal output influences direct and indirect taxes. Real taxes on income and wealth are deducted from real output to derive disposable income, which determines consumption. Budget deficit is determined by the difference between exogenous public expenditure and endogenous revenue. Deficit financing by the government provides the nexus between the monetary and fiscal sector of the economy. Government borrowing from the central bank increases the monetary base and affects the money supply.

Although the Rahman-Shilpi model captures important linkages in the economy, it has certain limitations. The model uses an aggregate production function to explain supply and therefore fails to recognize that the behavior of production may differ among sectors. The specification of the investment function lacks an appreciation of the availability of credit from banks at exogenously fixed interest rate as a constraint on investment. The estimation of the investment function experimented with different variables including change in bank credit to the private sector, which incidentally came up with a statistically significant coefficient. Further, the crowding out complementarity relationship between private and public investment is not known. In addition, the specification of the equations in the monetary sector does not seem to be well-built into the model. For example, the equations explaining the demand for demand deposits and time deposits are not integrated in the model. Besides, one can argue that separate specification of the demand for money, the supply of money and GDP deflator are not required. As the interest rate is not



determined in the model, the monetary sector is in equilibrium through changes in GDP deflator, in which case the demand for money function can be dropped from the model.

One fundamental problem associated with all the above-mentioned macroeconomic models is that estimated regression equations are based on the assumption that the time series data used in various equations are stationary. However, there is compelling evidence to suggest the non-stationarity of many macroeconomic time series in which case the use of OLS in estimating the relationship might result in inconsistent and inefficient results and might produce spurious relationship. Therefore, the recent econometric exercises with the time series data have emphasized the time series properties of the variables and have used, in the case of the presence of non-stationary data, cointegration techniques to overcome the problem of spurious relationship. As the integrating properties of the data used in the model have not been investigated in the previous studies, the estimated long-run relationships as reflected in various specifications may be called into questions.

More recently, Basher and Haque (2000) have developed a computerized simulated macroeconometric model for Bangladesh economy. Their model consisted of five important sectors of the Bangladesh economy: demand, fiscal, money and finance, trade and the supply side. It has also included remittance income as an endogenous factor in the model. The model was estimated using annual data from 1974 to 1997. The impact simulation was done from 1998 to 2000 while the simulation is live meaning that the model can include the latest available data to extend both the base simulation and ex ante simulation.

Finally, Hassan, Basher, Maroney, and Isik (2004) have developed a macroeconometric model for the Bangladesh economy using nine key macroeconomic variables employing annual data from 1974 to 2000. The methodology employed in this paper uses unit root and Johansen's cointegration tests followed by vector error correction model and variance decomposition to examine the

dynamic relationships among macroeconomic variables. In this paper, it has been shown that within the context of Bangladesh, monetary policy is more important than fiscal policy. As significant amount of development expenditure for Bangladesh comes from foreign donation, it is also argued that this aid must be channeled to productive activities so that it contributes to economic growth. The domestic export base has also to be widened and diversified.

Although, a number of researches have been conducted on macroeconomic models, most of them concentrated on some key variables and all of the models have been obsolete to apply in analyzing the concurrent macroeconomic environment of Bangladesh. Factually, the construction of macroeconometric model of an economy is an evolving process and a particular model cannot consider all aspects of the economy. The model presented in the thesis is built on the accumulated knowledge of the past models putting special emphasis on Hossain model (1995). The fundamental changes have been done in production function, private investment functions, export supply functions, money supply function, food grains and raw materials functions. The macroeconometric model in this paper includes six key blocks– production, expenditure, balance of payments, government, monetary, and price block. In the context of Bangladesh, supply-constraints have a major influence on the macroeconomy, though in some areas demand side factors also exert important influence. This research does not consider the demand side analysis of money market due to the absence of official data source.