LightCastle Partners

Bangladesh Economic Update 2022

Navigating Through Global Headwinds

About LightCastle Partners

At LightCastle, we take a data-driven approach to create opportunities for growth and impact. We consult and collaborate with development partners, public sector and private organizations to promote inclusive economic growth that positively changes the lives of people at scale.

Till date, we have consulted for **150+** development partners & private organizations on **250+** projects, collaborated with **650+** SMEs & startups, mobilized USD **150** million+ in investments and supported **40+** accelerator/ incubator programs across Bangladesh. LightCastle also hosts the largest market and industry datasets in Bangladesh across **30+** industries.

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September, 2022

Table of Acronyms

ADB	Asian Development Bank
BASIS	Bangladesh Association of Software and Information Services
BB	Bangladesh Bank
BBS	Bangladesh Bureau of Statistics
BCF	Billion Cubic Feet
BD	Bangladesh
BDT	Bangladesh Taka
BGMEA	Bangladesh Garment Manufacturers and Exporters Association
BMET	Bureau of Manpower Employment and Training
BoP	Balance of Payment
BPC	Bangladesh Petroleum Corporation
BPDB	Bangladesh Power Development Board
CEBR	Centre for Economics and Business Research
CPD	Centre for Policy Dialogue
CPI	Consumer Price Index
CY	Calendar Year
DAE	Department of Agricultural Extension
DCCI	Dhaka Chamber of Commerce and Industry
DPC	Development Policy Credit
EPB	Export Promotion Bureau
ERD	Economic Relations Division
EU	European Union
FCA	Financial Conduct Authority
FDI	Foreign Direct Investment
FY	Fiscal Year
GCC	Gulf Cooperation Council
GCI	Global Competitiveness Index
GDP	Gross Domestic Product
GM	General Manager
GNI	Gross National Income
GRID	Green Resilient and Inclusive Development
HAI	Human Asset Index
ICT	Information and Communication Technology
IDA	International Development Association
IDB	Islamic Development Bank
IFPRI	International Food Policy Research Institute
ILO	International Labour Organization
IMF	International Monetary Fund
IT	Information Technology
ITES	Information Technology Enabled Services
ITFC	Islamic Trade Finance Corporation
JICA	Japan International Cooperation Agency
KG	Kilogram
KM	Kilometres
LC	Letter of Credit
LDC	Least Developing Country
LMIC	Lower Middle-Income Countries
LNG	Liquefied Natural Gas

MIT	Massachusetts Institute of Technology
mmBtu	Metric Million British Thermal Unit
MMcfd	Million Cubic Feet Per Day
MTOE	Mega Tonnes of Oil Equivalent
MW	Megawatts
NBFI	Non-Banking Financial Institution
NBR	National Board of Revenue
OEC	Observatory of Economic Complexity
OMS	Open Market Sales
OPEC	Organization of the Petroleum Exporting Countries
P	Provisional
Pc	Percentage
PET	Polyethylene Terephthalate
PSMP	Power System Master Plan
RE	Renewable Energy
RMG	Readymade Garments
SEZ	Special Economic Zone
SWIFT	Society for Worldwide Interbank Financial Telecommunication
TCB	Trading Corporation of Bangladesh
Tcf	Trillion Cubic Feet
TIN	Taxpayer Identification Number
UAE	United Arab Emirates
UK	United Kingdom
US	United States
USD	United States Dollar
USGS	United States Geological Survey
VAT	Value Added Tax
WB	World Bank

Snapshot Bangladesh

Real GDP Growth:
6.40% per annum
(2022)
Projected Real GDP:
6.70% per annum (2023)
Source: World Bank

GDP (Current, USD)
USD 416 Billion
(2021)
Source: World Bank Open Data

Per Capita Income:
USD 2,824
(FY 2022)
Source: Bangladesh Bureau of Statistics

Food
8.37%

Inflation
7.56%
(June 2022)

Non-Food
6.33%

Source: Bangladesh Bureau of Statistics

Export (f.o.b)
USD 52 billion
(FY 2022)

Trade Balance
USD -32 billion
(FY 2022)

Import (f.o.b)
USD 84 billion
(FY 2022)

Remittance Inflow:
USD 21.0 billion
(FY 2022)

Net FDI Inflow:
USD 2.9 billion
(CY 2022)

Current Account Balance
USD -18.7 billion
(FY 2022)

Foreign Exchange Reserve:
USD 38.95 billion
(As of Aug, 2022)

Population:
165 million
(Census 2022)

Population Density:
1,119 per sq. km
(Census 2022)

Mobile Phone Users:
55.9%
(Census 2022)

Median Age:
27.6 years
(2022)

Literacy Rate:
74.7%
(Census 2022)

Total Budget Expenditure:
USD 64.3 billion
(FY 2023)

Total Debt as Percentage of GDP:
38.0%
(FY 2021)

Power Generation:
25,284 MW
(Installed Capacity) (2022)

Total Net Domestic Borrowing:
USD 90.6 billion
(FY 2022)

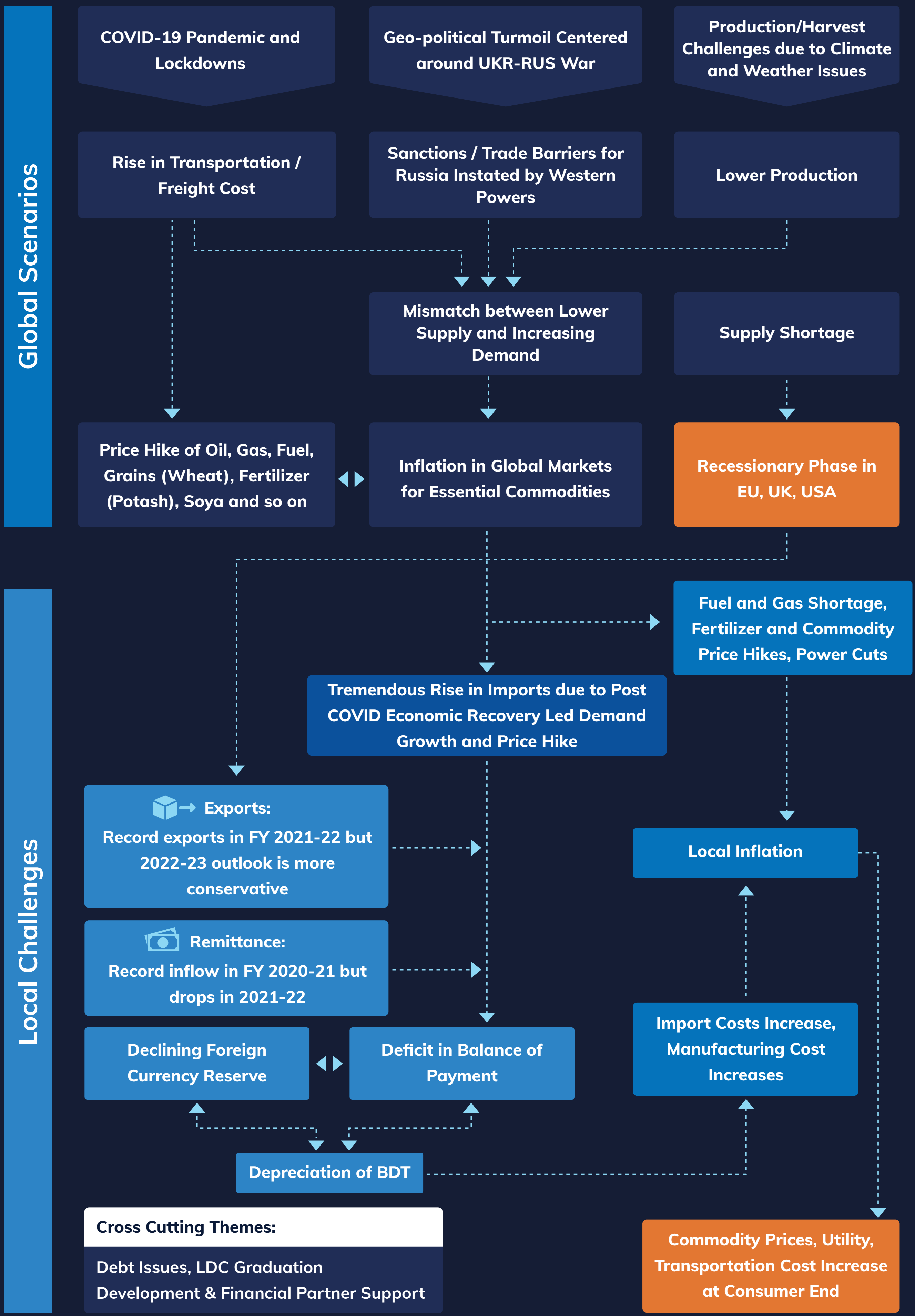
Interest Rate on Deposits:
4.01%
(Jan 2022)

Interest Rate on Advances:
7.13%
(Jan 2022)

Source: International Monetary Fund (IMF), World Bank, Bangladesh Bureau of Statistics (BBS), Bangladesh Bank

Note: Decimal points has been rounded up

Conceptual Framework Depicting Interplay of Global and Local Factors



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Preamble

The global economy has been undergoing turbulent times over the last couple of years, spearheaded by the pandemic induced slowdown in 2020 and the resulting supply chain disruptions wrought about by travel restrictions and lockdowns. While the pandemic has receded—facilitated by the invention, mass production and distribution of vaccines in record time—a number of geopolitical challenges have disrupted economic recovery. The advent of the Ukraine-Russia war has swiveled the global commodities market as a result of the sanctions imposed on Russia by the Western economies. Russia's importance as a global supplier of fossil fuel (USD 211 billion), fertilizers (USD 12.5 billion), precious minerals (USD 31.6 billion), Iron & Steel (USD 28.9 billion), and cereals (USD 9.1 billion) has resulted in severe supply side shocks and skyrocketing commodities prices. While the commodity prices have receded over the last few months, mainly due to recessionary bouts across the EU and the US, prices have remained well above the pre-war levels. Another structural shift witnessed over the last few years has been the confrontational stance between China and the US; initially manifested in the form of a trade war. The latest impasse over the visit of a senior US elected official to Taiwan has led to assertive response from China and the possibility of an armed conflict over Taiwan cannot be ruled out in the medium term. Economists are predicting a gradual reversal of trade liberalization as the geopolitical fault lines are increasingly becoming more pronounced, leading to de-globalization.

The aforementioned shocks have contributed to a global slowdown reflected in the growth projections of the multilateral development agencies. According to the World Bank, the global economy is expected to grow by 2.9% in 2022, a downward revision from the 4.1% growth estimated at the beginning of the year and significantly lower than the 5.7% growth experienced in 2021. Bangladesh's economy has been hit hard by the global turmoil considering its dependence on international trade. As Bangladesh is a net importer of essential commodities like oil, natural gas, fertilizer, wheat, soybean and cotton; international price hikes have led to external shocks culminating in current account deficit of USD 18.7 billion in FY 2021-22. The lopsided international trade numbers led to dollar shortages and the government was forced to stand aside and let the currency depreciate to BDT 106 (BDT 115/kerb market) against each USD. Alongside, the government recently hiked fuel prices in an effort to reduce subsidies, which had a knock on effect on inflationary trends.

Bangladesh's growth trajectory has been augmented by infrastructure development, which can potentially bolster growth in the upcoming years. However, the high cost of developing these projects is a matter of concern, especially owing to repeated extension of project deadlines and corresponding revision of budgets. Since most of these projects are financed by external debt, with the graduation from LDC, cost of funding is expected to increase and soft loans will increasingly become harder to avail. As of March 2022, the external debt to GDP ratio stood at 27%, which is lower than IMF's risk threshold of 70%. However, the debt repayment burden is expected to double within the next three years according to ERD's calculations and is expected to reach USD 4.02 billion in 2025, from current repayment burden of USD 2.4 billion. The tax collection rate hasn't kept up with the growing economy, generating less than 10% of GDP, significantly lower than regional peers.

In order to continue the growth momentum, policymakers need to undertake a series of policy reforms and reduce red tapism, mainly aiming to facilitate ease of doing business. International investors will have to be wooed to enter the country, which will not only create new jobs but facilitate technology transfer and help the country transition toward an innovation led economy. The demographic dividend the country is experiencing will cease to exist within the next couple of decades and the government has to facilitate employment opportunities for 2.2 million workforce entering the job market per year. Large scale investment in education will also be required for improving the overall skill-set of the working population and contribute to growing human capital.

The pandemic and the war led commodity price hikes have led to winners and losers across the economy. A notable percentage of the economically vulnerable population has slid back to poverty and a comprehensive social safety net arrangements and livelihood projects have to be implemented by the government and development agencies in order to reduce inequality. Growth in the manufacturing sector will also create employment opportunities for unskilled and semi-skilled workers leading to inclusive growth. The coming few years will be monumental as Bangladesh finally transitions out from the LDC status in 2026, but fresh challenges will emerge as the country will cease to benefit from various trade benefits accrued to LDCs. The country's overdependence on the apparel sector for export earnings might prove to be a major hurdle for sustaining growth in the next 10 years, and the government will have to provide policy support and facilitate investments for diversifying the export basket.

Although the current scenario at the global level is translating into local economic challenges, Bangladesh is currently in a position to tackle all the challenges with great confidence and proactive efforts. The promising GDP growth over the previous years is a sign of Bangladesh's resilience. As a testament to this, during the pandemic years, Bangladesh performed well in comparison to its South Asian peers in terms of year-on-year GDP growth rate. The nation's efforts on transportation infrastructure, energy generation capacity, economic zones, suitable policies for the manufacturing industries along with broader industrialization, digitization of financial and government services, and accommodating political landscape both within and out of the nation's border have placed Bangladesh in a stronger position than ever before. Consequently, in recent times, export-driven industries hit new records in FY 22 and are going strong in seeking new avenues for expansion. Remittance worker flow is also witnessing greater positive response. Local industries are quickly scaling up and acquiring larger shares of the markets; such as consumer goods, construction materials, electronic products, and various markets. With the right economic, fiscal, and monetary directions the nation can utilize its existing capabilities to continue its advancements and then focus on nurturing future potential through diversification and specialization.

** Values in Bangladeshi Taka converted to United States Dollar as per inter-bank exchange rate reported by Bangladesh Bank on the 18th of September, 2022 standing at **BDT 105.5** for every USD 1 throughout this white paper

Chapter 1

Contemporary Macro-Economic Situation of Bangladesh

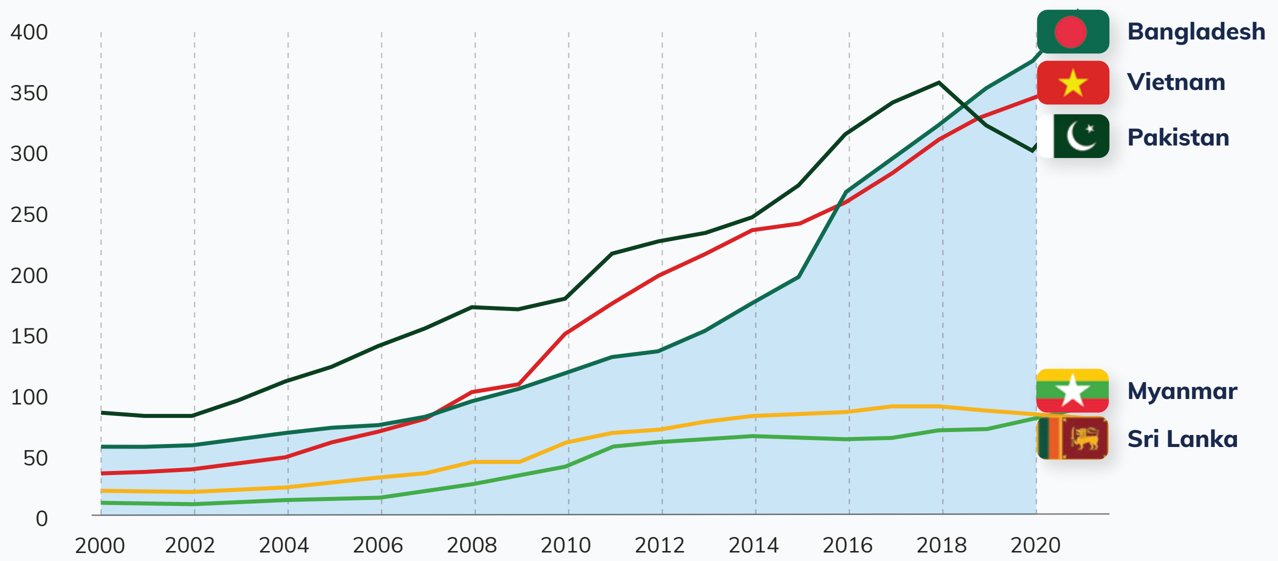
Contemporary Macro-Economic Situation of Bangladesh

1.1 Bangladesh's Economy has Flourished in the Recent Past

In 2021, Bangladesh celebrated 50 years of independence highlighting achievements in areas relating to connectivity, industrialization, digitization, urbanization and socio-political stability. For the last few decades, the nation has been progressing towards economic advancements. Such systemic progression has been possible due to the nation's perseverance, resilience, and growth mind-set. Prioritizing strategic policies, infrastructure development, and digitization over the decades has helped Bangladesh to utilize its economic potential such as demographic dividend, export competitiveness, remittance inflow, technology adoption and greater supply chain integration. These potentials ultimately have resulted in commendable growth over the past decade. The Gross Domestic Product (GDP) from 2012 to 2021 has almost tripled. Per capita income as of FY 2021 – 22 stands at USD 2,824.[1]

The United Kingdom's Centre for Economics and Business Research (CEBR) expects Bangladesh's economy to become the 28th largest in 2030 and the 25th largest in 2035 globally. The nation is also projected to have real GDP growth above 6% year on year according to International Monetary Fund's (IMF) latest world economic outlook in 2022.

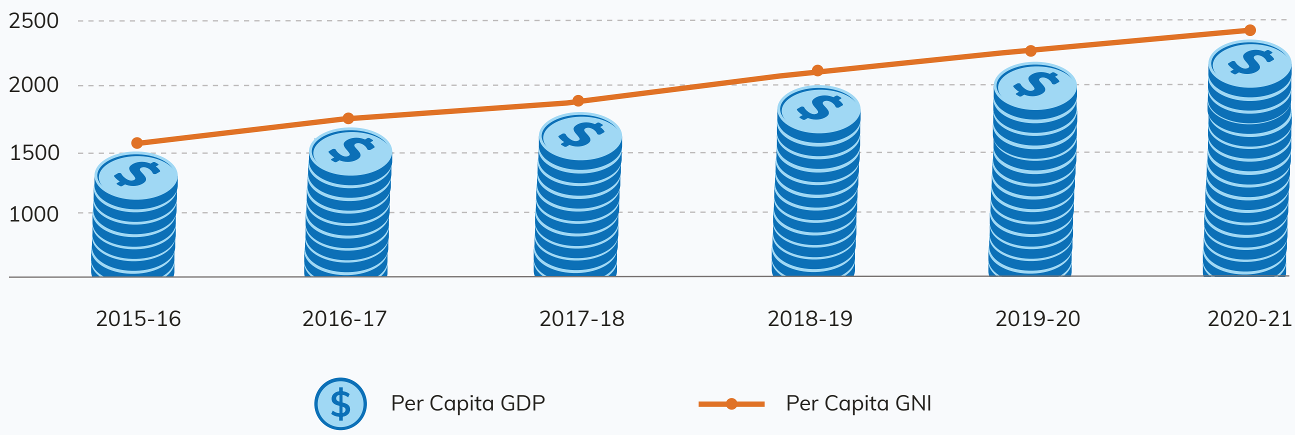
Cross Country GDP Comparison (2000 to 2020)
(USD Billion)



Source: World Bank Open Data

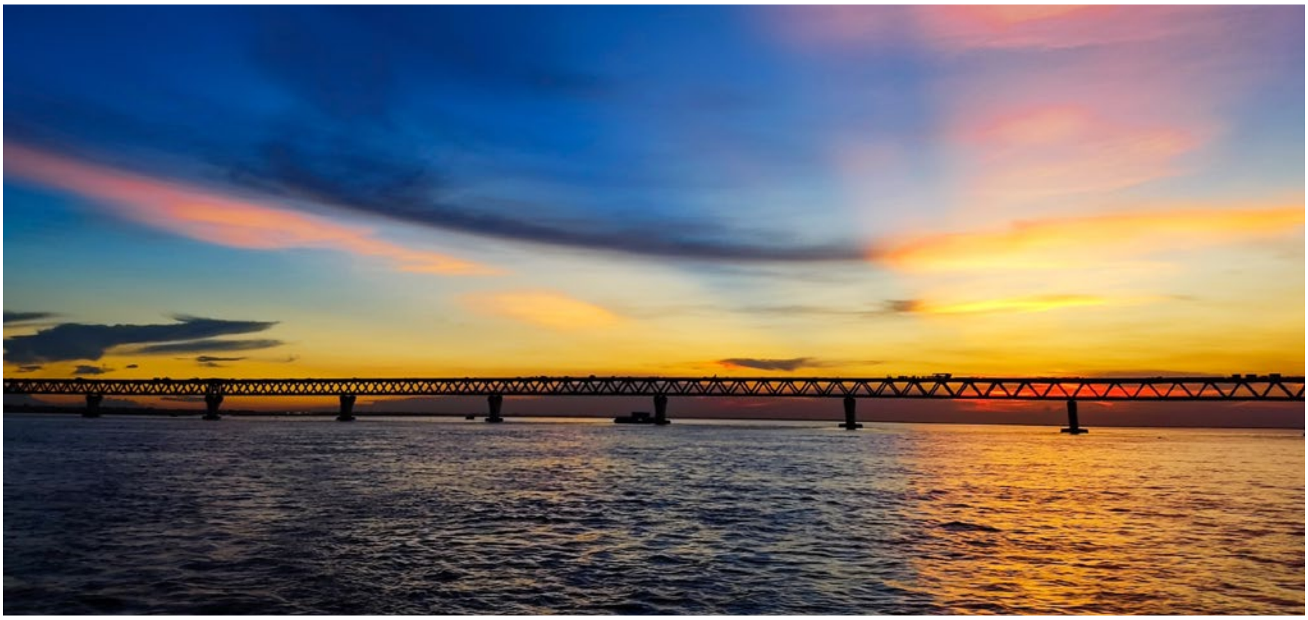
1. Bangladesh Bureau of Statistics

Per Capita GDP and GNI Trend of Bangladesh
(USD)

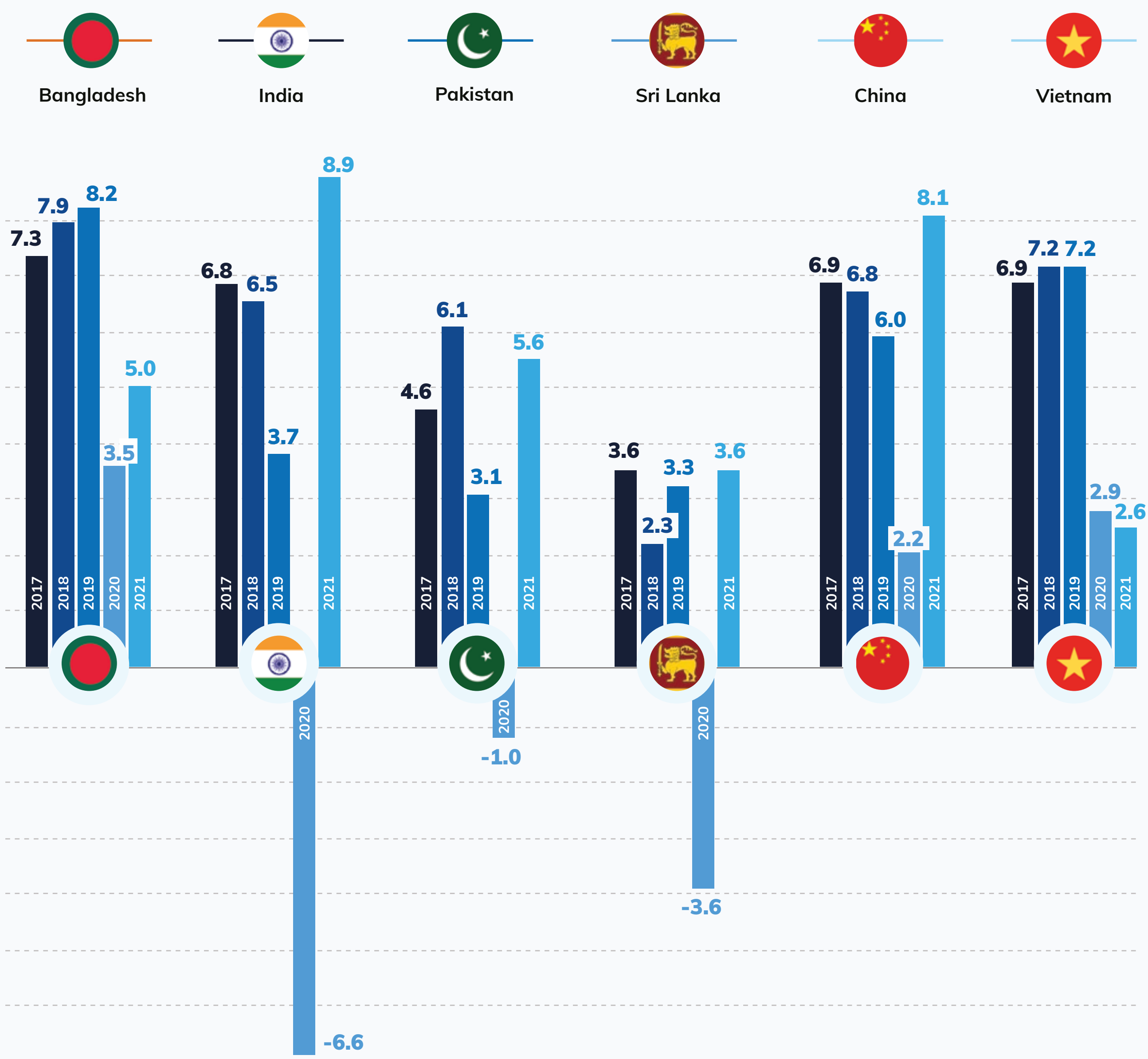


Source: World Bank Open Data

Even during the COVID-19 pandemic years, Bangladesh has been a major growth outperformer among its peers and South Asian neighbours with the highest growth rate in 2020. This performance can be attributed to the stable demand in global apparel market and Bangladesh's Readymade Garments sector adapting quickly to COVID-19 related changes. In addition, the remittance inflow also increased due to workers returning back to Bangladesh after lay-offs. Upon the subsidence of the pandemic, the country was on its way to recovering with rigor.



Comparative Analysis of Annual Percentage Change in Real GDP of Bangladesh with Peers



Source: IMF, 2022

The country also fulfilled all the Least Developing Country (LDC) graduation criteria for the first time in 2018 and a second time in 2021. Although with a revised target of 2026 from 2024 due to the economic turbulence caused by the COVID-19 pandemic, Bangladesh is on its way to graduating to the middle-income status.

1.2 Bangladesh is Now More Sensitive to the Changes in Global Economy

Alongside the achievements, the economic landscape of the country has also transformed. The shift towards industrialization, urbanization, and technology adoption has led the country's economy to become more dynamic and diversified. In the latest trend analysis, it is observed that both exports and imports are on the rise.

Compared to the previous decades, the export basket has diversified with the addition of consumer durables, mobile phones, active pharmaceutical ingredients, software, frozen fish, marine vessels, and agricultural products. New countries are also being added to the list of export destinations.

On the other hand, Bangladesh is witnessing a rise in consumerism leading to higher imports. The raw materials for most of the industries including the influential RMG sector have to be imported along with LNG and fuel oil for transportation and power sectors. Thus, the country is now highly integrated into the global supply chain for both imports and exports.

Thus, Bangladesh's internal economic condition has become extremely sensitive to external economic scenario. With the shift in demand-supply dynamics for commodities globally, Bangladesh's sector leaders are having to make strategic shifts accordingly. For example, due to the chip shortage induced by pandemic led lockdowns, Bangladesh's smartphone and electronics manufacturers had to shift production and prices accordingly. The profit margins across the RMG sector have been highly dependent on the global supply of cotton. Fuel and natural gas prices have been readjusted in tune with changes in the global market, leading to higher cost of production. A similar pattern has also been seen across the agriculture, chemical, and transportation sectors.

1.3 Bangladesh's Near-Term Prospects Unnerved by Global Economic Turbulences

Being connected to the global economy is a sign of Bangladesh's progress as a mature economy. However, the country's dependence on imports overshadows export growth causing balance of payment imbalances. Hence, being connected to global trade also requires a healthy balance of foreign reserves. The various mega projects underway in collaboration and partnership with major economies would bring 'debt servicing' into the development equation as well. Due to such dependence on and integration into the global economy, any kind of turbulence at the global level impacts Bangladesh directly and pervasively. Thus, the current economic struggle on the global stage is being resonated within Bangladesh's economy. More importantly, multiple challenges have developed simultaneously in recent months. Since many of the major economic indicators are under pressure at the same time, the situation has become even harder to control. In fact, some of the weaker points of our economy have surfaced as major challenges to be dealt with. A summary of how global issues are having a local impact is given in the next page.

Global Issue →	Local Impact
COVID lockdowns in source countries for raw materials	Hindered supply posed trouble for sectors in Bangladesh, particularly consumer durables and apparel
Lockdowns in destination countries for labor force	Remittance earners returning home due to lockdown led economic slowdown
Slowed COVID recovery in developed countries	Potential fall in export orders. Orders increased in some sector e.g., apparel due to pent up demand
Russia banned from the Society for Worldwide Interbank Financial Telecommunication (SWIFT) system due to Ukraine Russia War	Trade with Russia and infrastructure funded and developed by Russia halted
Global oil and gas supply shortage and price hike	Bangladesh having to buy oil and gas at a higher price leading to a price hike in the energy and transportation sector
Ban on Russia-produced cereals, fertilizer, feed and edible oils	Price hikes from other suppliers and potential food shortage
Inflation and recession-like phase in major economies	Rise in import bills and fall in export orders leading to balance of payment deficit and pressure on foreign reserves
Currency strengthening by United States (US), European Union (EU), United Kingdom (UK), and other major economies and currency market volatility	Depleting foreign reserve and depreciation of Bangladeshi Taka
The rising cost of debt and investment	Debt financing through internal sources and seeking loans from international financing sources

The infographic above shows how the different global issues are having an adverse effect on the local context of Bangladesh. Since the beginning of 2022, the global economy has been battered by a cascade of challenges. These challenges are interconnected and have multiplying effects on different angles of the economic cogs.

With a slowed recovery from the COVID slump, the world witnessed another major conflict in the form of the Ukraine-Russian war. The war had a polarising effect on geopolitical stances among nations. Russia has been banned from the SWIFT system and trading with Russia became politically challenging. This created crises for natural gas, oil, and commodities leading to a global price hike. With the dislocated supply chain and crisis for necessary commodities, developed western countries went for a conservative approach for strengthening their currencies through tightening monetary policy.

As a result, Bangladesh witnessed a rise in commodity prices. The prices for gas, fuel, oil, wheat, soya bean, and fertilizer went up due to global shortages. This had a domino effect on the overall economy of Bangladesh: prices of everything else started to rise as the cost of production, transportation and services increased. Thus, the cost of inflation is being passed on to the shoulders of the consumers.

On the other hand, the rising import bill had tremendous pressure on the forex reserves as the global currency market became extremely volatile. The Central Bank of Bangladesh tried to cushion some of the impacts but later resorted to devaluating the Bangladeshi currency. The cost of each dollar peaked at an unprecedented level of almost BDT 120 in the kerb market in August.[2] The rate fluctuated in the following months, reaching the official rate of BDT 105. In mid-September, Bangladesh Bank allowed floating exchange rate for US dollar.

The government is trying to keep a balance, yet the situation is made complicated by the simultaneous rise of several interconnected challenges. Tackling inflation is proving difficult due to the supply shortage of several necessary commodities at the global level. At the same time, the depleting forex reserves and the USD supply shortage in the global market are responsible for currency devaluation. This in turn increases the cost of imports and raises inflation in the local market. Bangladesh is trying to pull its demand for imports to tackle inflation. Power cuts, banning foreign trips for government officials, reducing open hours for shops, introducing day-light saving time, prioritizing most crucial megaprojects, deprioritizing others have been some of the major initiatives of the government.

However, the government is compelled to raise the prices of gas, fuel, and electricity and is unable to control the price hike of commodities. The currency would take time to stabilize. Moreover, the servicing solutions for domestic and foreign debt are still in the process while debt is on the rise.

These are the major concerns of Bangladesh, and the near-term strategies will be devised based on a focus to tackle all these challenges. The rigorous strategies and countermeasures will ultimately impact the bottom lines of various industries, and people's living standards and determine the path for our growth journey.

2. Dollar price jumps to Tk 119 in kerb market, The Daily Star, August 2022

Chapter 2

The External Turbulences Moulding Bangladesh's Economic Prospects

The External Turbulences Moulding Bangladesh's Economic Prospects

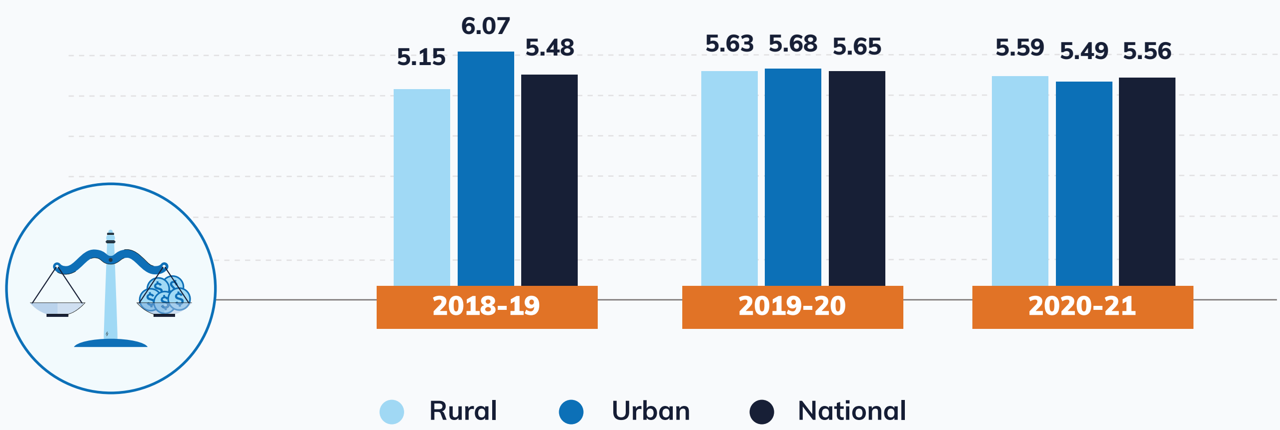
2.1 A Storm of Events Leading to Record Global and Local Inflation

Globally, the demand started picking up after the second wave of the pandemic. However, the global supply chain disruptions continued to hamper supply of imported raw materials. Added to this burden is the Ukraine-Russia war which increased energy prices and obstructed major trading channels, particularly in Europe. This global context had a domino effect on the local inflationary trend. The subsequent currency devaluation also provided upward pressure on prices of imported goods.

Worldwide, May 2022 saw a 65% increase in oil prices, a 114% increase in urea fertilizer prices, a 29% increase in soybean oil prices, an 85% increase in wheat prices, and a 13% increase in sugar prices compared to May 2021.[3] Lesser agricultural outputs compared to previous years in the South American regions also fueled commodity shortage in the global market. Energy prices also witnessed a 50% hike. The US is undergoing an inflationary phase projected at 9.1%, which is the highest in 40 years, while recession looms in European Union according to the Economist Intelligence Unit.[4]

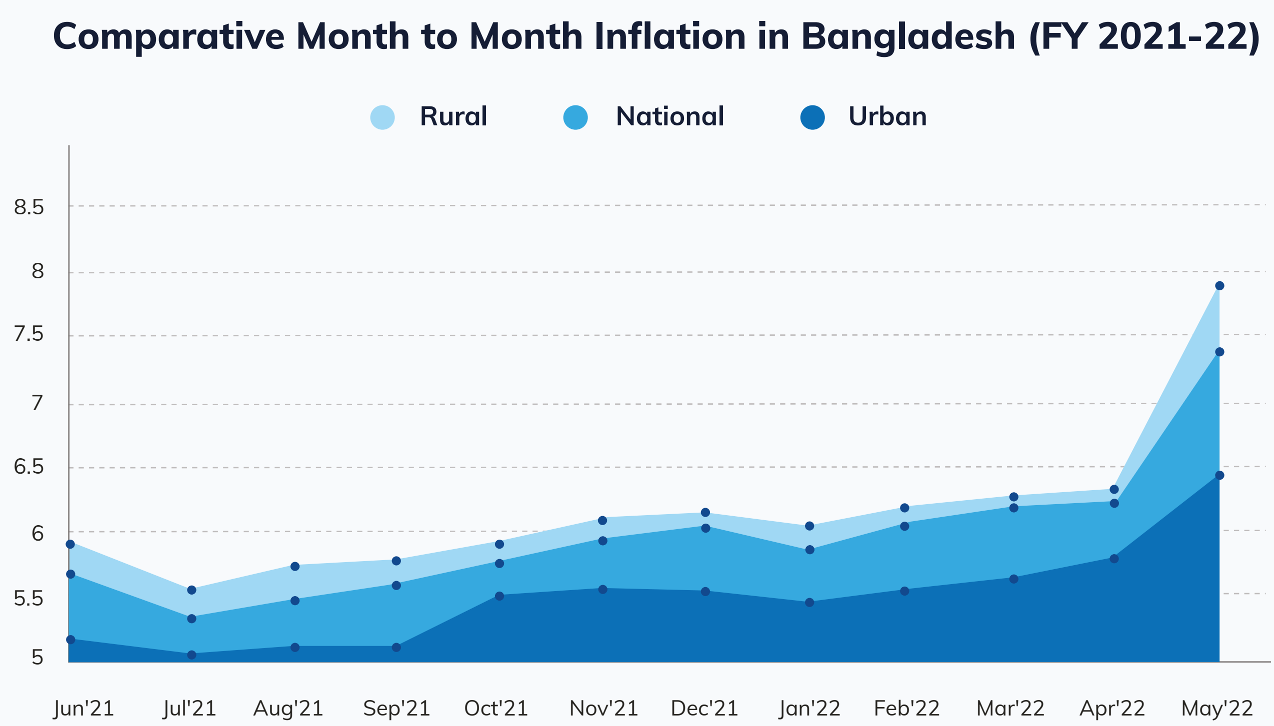
The latest inflation figures from the Bangladesh Bureau of Statistics (BBS) showed that in June 2022, inflation reached 7.56% which is the highest in the last nine years. The food inflation for June was 8.37% and the non-food inflation rate was 6.33%. Also, inflation is almost equivalent in urban and rural regions.[5] This increases the cumulative inflation figure for the financial year 2022 to 6.15%, overshooting the government's target by 85%.

Comparative Inflation of Bangladesh from FY 2019 to FY 2021



Source: Consumer Price Index (CPI), Inflation Rate and Wage Rate Index (WRI) in Bangladesh, BBS, July 2022

3. Volume: 3, The Cost & Management, The Institute of Cost and Management Accountants of Bangladesh (ICMAB) (May-June, 2022)
4. US inflation shows signs of peaking, Economist Intelligence Unit (August, 2022)
5. Consumer Price Index (CPI), Inflation Rate and Wage Rate Index (WRI) in Bangladesh, BBS, July 2022



Source: Consumer Price Index (CPI), Inflation Rate and Wage Rate Index (WRI) in Bangladesh, BBS, July 2022

2.1.1 Supply Chain Dislocations from Ukraine-Russia War Have Destabilized the Global Market Leading to Inflation in Bangladesh

The Russia-Ukraine war has disrupted trade flows of high-linkage essentials including fuel, fertilizer, and grain due to disruptions in export, sanctions, and the banning of Russia from the SWIFT payment system. Such trade disruptions and dislocations have increased the prices of commodities at the global market level. This, in turn, fuelled the inflation in Bangladesh. Energy, power, transportation, agriculture, among other sectors were highly and directly impacted.

2.1.2 Agricultural Import Challenges Make Food Security Costly

The cost of agricultural products had risen since the beginning of the Ukraine-Russia war, especially for wheat, since Russia and Ukraine jointly export up to 30%[6] of the world's wheat, about 75%[7] of sunflower oil supply, and corn up to 19%.

These adjustments raised the prices of staple goods, which might make Russian export interruptions profitable for other commodity exporters. As the top two producers of wheat are Russia and Ukraine, the cost of a tonne of wheat in January 2022 was USD 334.50 and in March it increased to USD 353.[8] This has raised the import prices of wheat in Bangladesh.

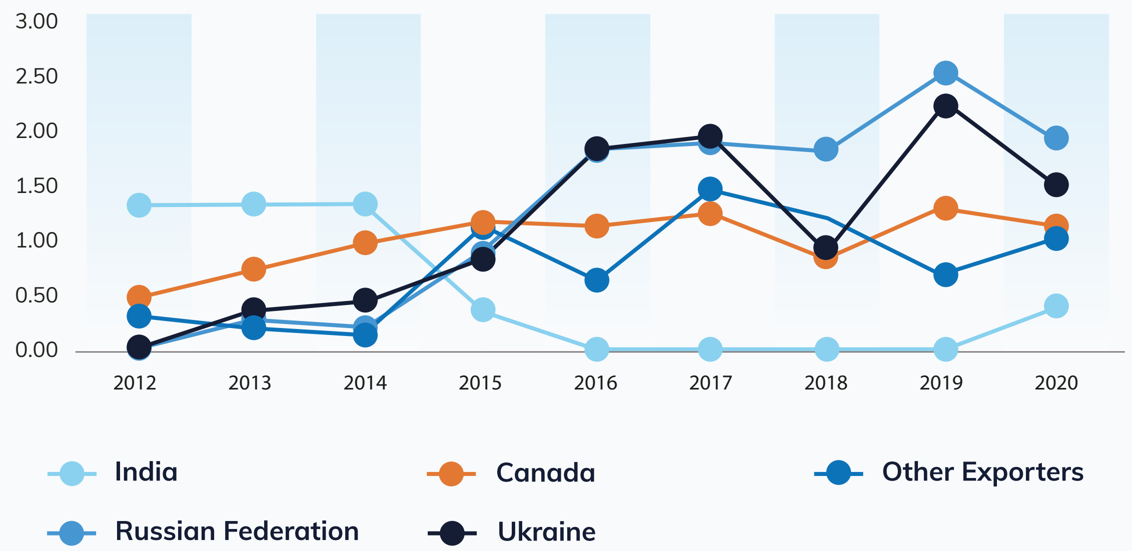
Bangladesh produces 0.2–0.3 million tons of edible oil out of a total consumption of 3 million tonnes.[9] Hence, the remaining 92% of the oil has to be imported. The majority of edible oil comes from

6. Wheat Production by Country 2022 Ranking (2022)
7. Ripple effects from Russia-Ukraine war test global economies, MIT Management (2022)
8. Wheat (Commodity), Markets Insider
9. Edible Oil & Fat Consumption Trend in Bangladesh, Council of Palm Oil Producing Countries (CPOPC) (August, 2021)

Argentina and soybean seeds from Brazil. Although Bangladesh buys just a little amount of oil seeds from Russia and Ukraine, the global price increase has influenced the domestic market. The price of soybean oil increased from USD 1,460 per tonne in January 2022 to USD 1,598[10] the following month, in global market.

Furthermore, barley and fertilizer are also among the key commodities that Ukraine-Russia produce and export. Prices for both the items and their derivatives have risen because of their absence from the global market. Additionally, Russia (20% of global market share) and Belarus (17.6% of global market share) are the second and third largest producers of potash, which is used in fertilizer.[11] The conflict has prevented potash from these countries to be exported. Although the United States does not have a direct ban against Russian fertilizer trading, the global market is persistently in a volatile state.

Country Specific Wheat Import Trend in Bangladesh (2012 to 2020)
(Million Metric Tonne)



Source: COMTRADE

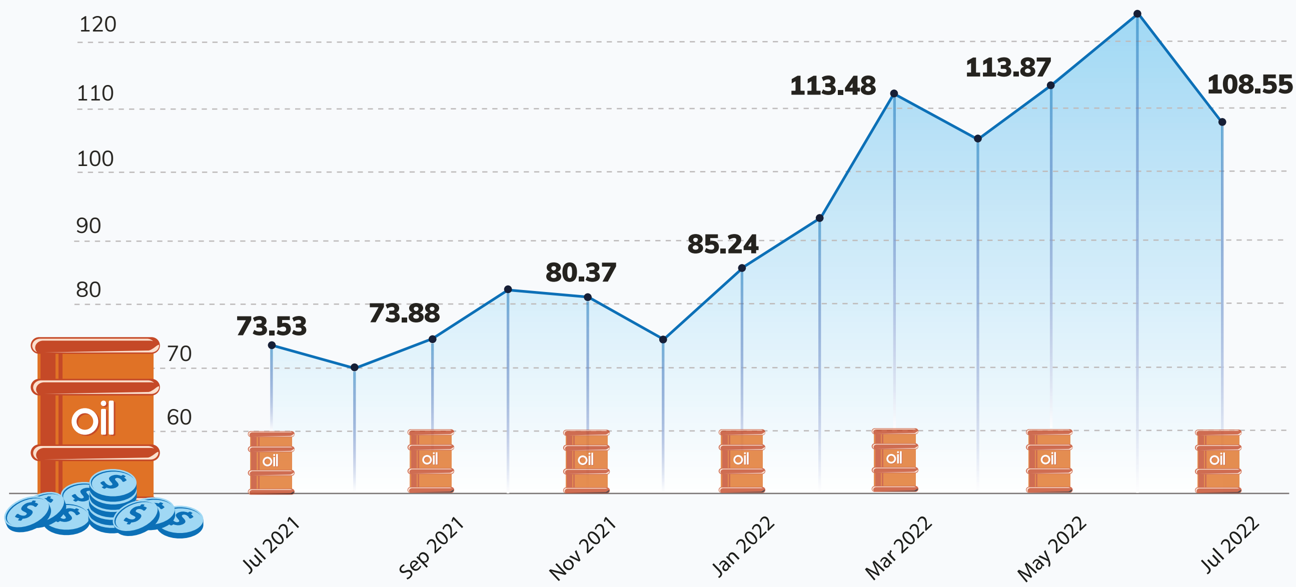
10. How the war in Ukraine threatens Bangladesh's food security, International Food Policy Research Institute (2022)
11. Potash Facts, Government of Canada

2.1.3 Oil and Gas Price Volatility

During the COVID-19 pandemic, oil and gas sector globally saw major shocks from the demand side. Lock downs all across the globe resulted in staggering drops in demand. Soon after the lockdowns have been withdrawn, the demand increased sharply. At the same time, the Middle Eastern suppliers were not increasing supplies to counterbalance supply deficit, despite repeated pleas from the US and EU. As a result, crude oil price increased to USD 100 a barrel in March and then gradually reaching up to USD 120 in between the following months.[12]

In October 2021, Bangladesh bought LNG at record prices of USD 36.95 per mmBtu from Gunvor, even though in March of the same year, the price of LNG was only USD 7 per mmBtu. At the end of last year, the price of LNG soared to near USD 50 per mmBtu internationally, causing Bangladesh to halt its LNG imports. After the beginning of the Ukraine-Russia conflict, Russian natural gas supply to the Europe has been partially curtailed, leading EU countries to desperately seek alternate sources of energy, inflating the price even more. Bangladesh's capacity to import from various sources is also limited due to the lack of infrastructure to refine petroleum products. Currently we have only one refinery with limited capacity to refine light crude oil, making Bangladesh miss out on discounted Russian crude oil in recent months.

OPEC Basket Price from July 2021 to July 2022
(USD Per Barrel)



2023 Forecasts

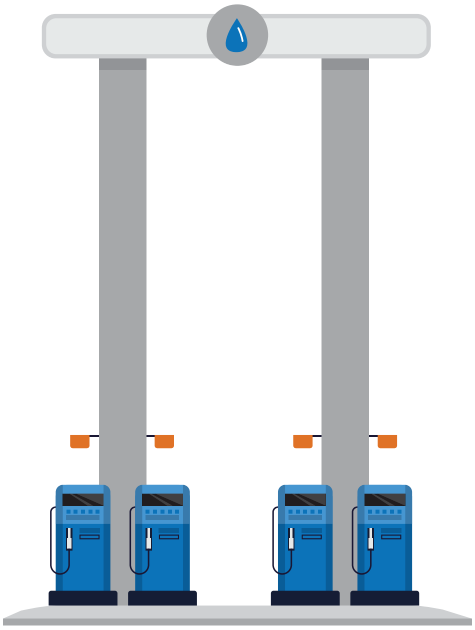
Global Demand to rise by **2.7%**	Oil Demand to rise, but slower than **2022**	OPEC expects **30.1** million Barrel Per Day in 2023 to balance markets	Assumes no further escalation in current situations

OPEC Basket Price: Weighted average of prices for petroleum blends produced by OPEC members

Source: OPEC Basket Price

12. Why Is the Price of Oil Rising?, Forbes Advisor (August, 2022)

Changes in Prices of Petroleum Products in Bangladesh after BPC Revision (As of 6th August)



	New Price	Previous Price	
Diesel	114 BDT	80 BDT	42.5% RISE
Kerosene	114 BDT	80 BDT	42.5% RISE
Petrol	130 BDT	86 BDT	51.1% RISE
Octane	135 BDT	89 BDT	51.7% RISE

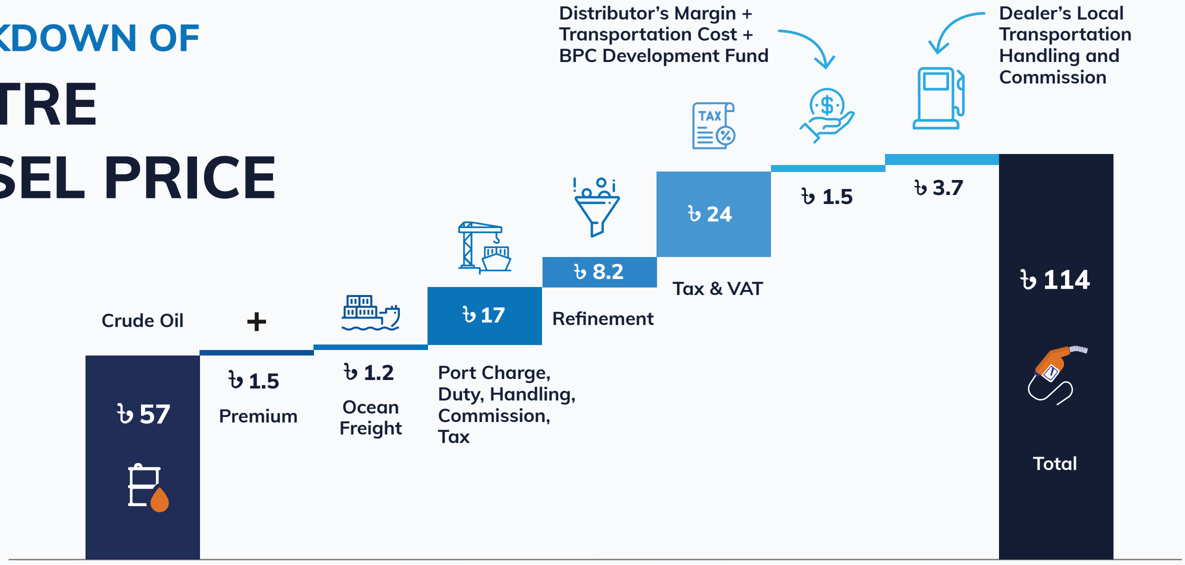
* Price Per Litre

Source: Energy and Mineral Resources Division, Ministry of Power (August, 2022)

Breakdown of Diesel Price in Bangladesh after BPC Revision (As of 6th August)

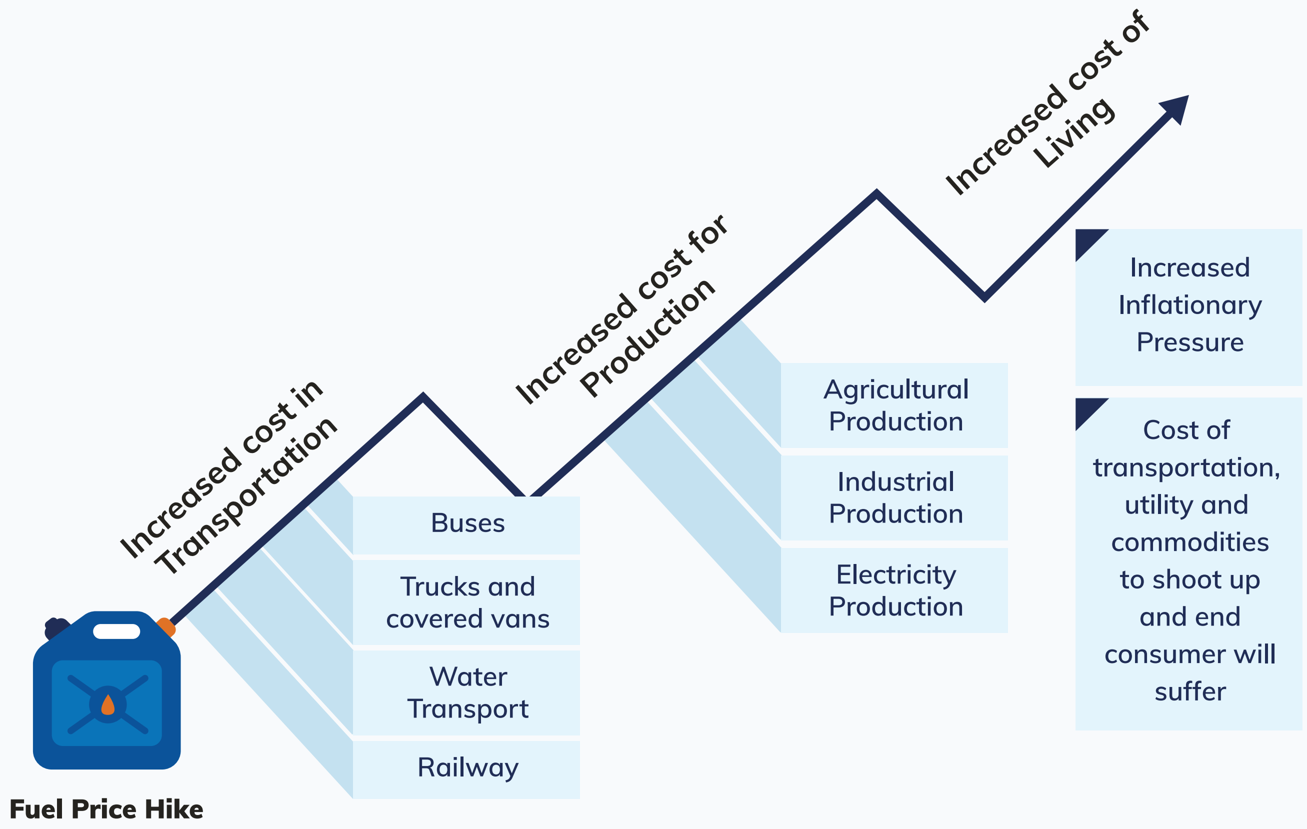
BREAKDOWN OF

1 LITRE DIESEL PRICE



Source: Graphic Stories, Finpresso

Impact of Hike in Fuel Prices



Source: A fiscal space and correct policy measures could have prevented the arbitrary hike of the fuel price, Centre for Policy Dialogue (CPD) (August, 2022)

From a local perspective, we are largely dependent on imported sources of fuel mix. Although Bangladesh is not directly dependent on Russian oil, the Russian-Ukraine war has significantly distorted the market, leading to higher import bills. The economy has taken a big hit due to a sudden spike in the domestic oil prices. Similarly, the cost for urea fertilizer has been increased to BDT 22 from BDT 16[13] to align prices with those at the international market. This shows how the agriculture sector would be adversely impacted by higher irrigation costs.

13. Press Release by Md Kamrul Islam Bhuiyan, Senior Information Office of the Ministry of Agriculture

2.2 Trade Deficit is Rising Despite Export Growth and Balance of Payment has Become a Major Concern

The rising import payment costs due to global inflation and supply chain disruption, coupled with a 40.27%[14] growth in imports (From April'21 to April 22) has widened the trade deficit. The trade deficit stood at USD 27.5 billion (Jul-Apr, FY 2022), a 53%[15] increase compared to the year before. The deficit stands at a historical high, expanding by almost two and a half times since 2016. This deficit trend is expected to continue and bubble beyond USD 33 billion[16] in the outgoing fiscal year with expectations of a slower deficit growth in the future once prices settle down.

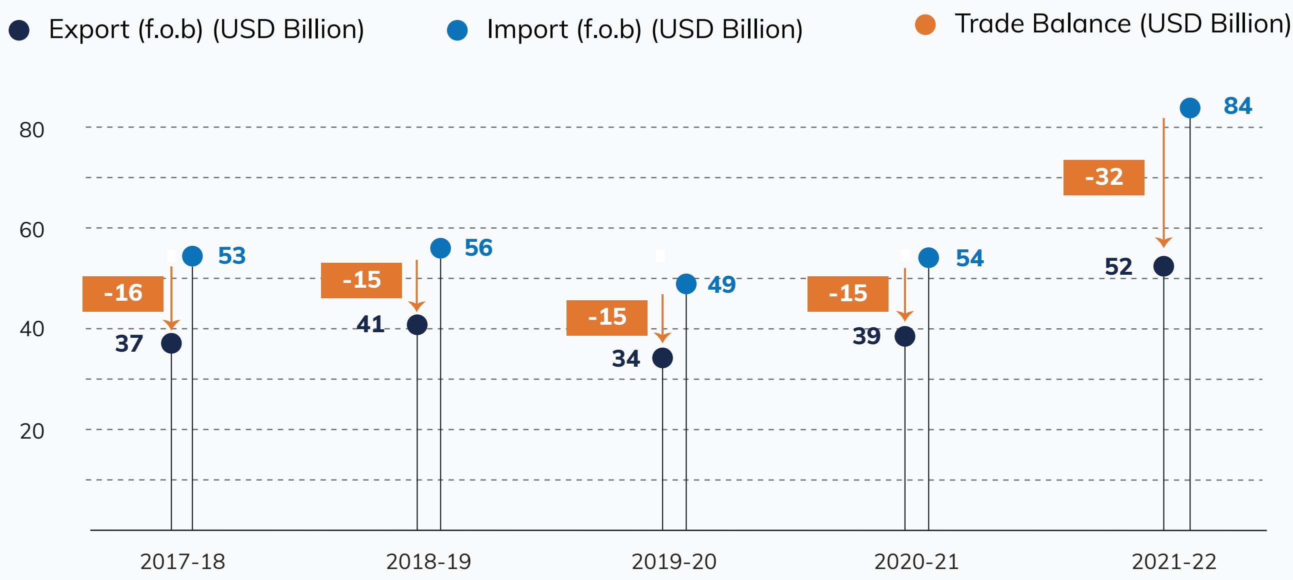
If imports keep rising faster than exports, the rising deficit will have to be accounted for through Bangladesh's foreign exchange reserve and the deficit will lead to further currency depreciation.

At the same time, the foreign reserve needs to cover import bills for at least 4-5 months, which needs to be retained through austerity measures, some already put in place by the Government of Bangladesh.

As of 2021, import payments amounted to USD 83 billion[17], a comparative look between the period Jul 21-Apr'22 versus Jul'20-Apr'21 shows 50.17% increases in between, according to the World Bank.

Taking a deeper dive into the components behind this growth, a catalyst comes in the form of the reopening of economies, the time before which saw anomalies in trade due to a reduction in imports and a better (yet small) outlook for export.

Trade Statistics of Bangladesh from FY 2018 to FY 2022

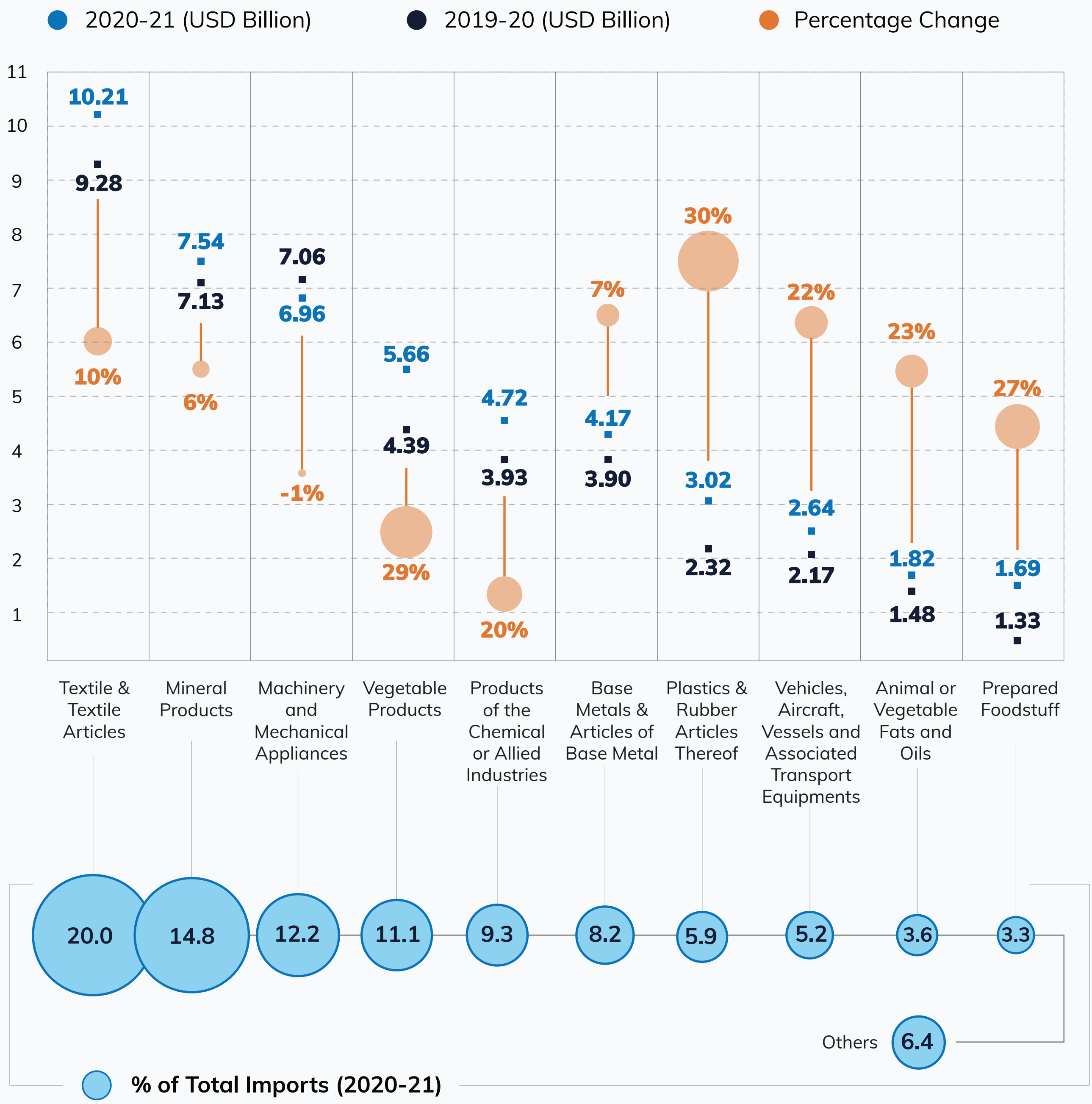


Source: Monthly Economic Trend, Bangladesh Bank
** F.O.B indicates Free On Board*

14. Monthly Economic Trends, Bangladesh Bank (April, 2022)
15. Bangladesh Bank
16. Monetary Policy for FY 2023, Bangladesh Bank
17. Import Data, Bangladesh Bank (July, 2022)

Bangladesh's main import basket according to Bangladesh Bank's statistics for 2020-21 consists of the ones given in the following figure:

Top 10 Import Basket Components of Bangladesh by Total Share
(USD Billion)

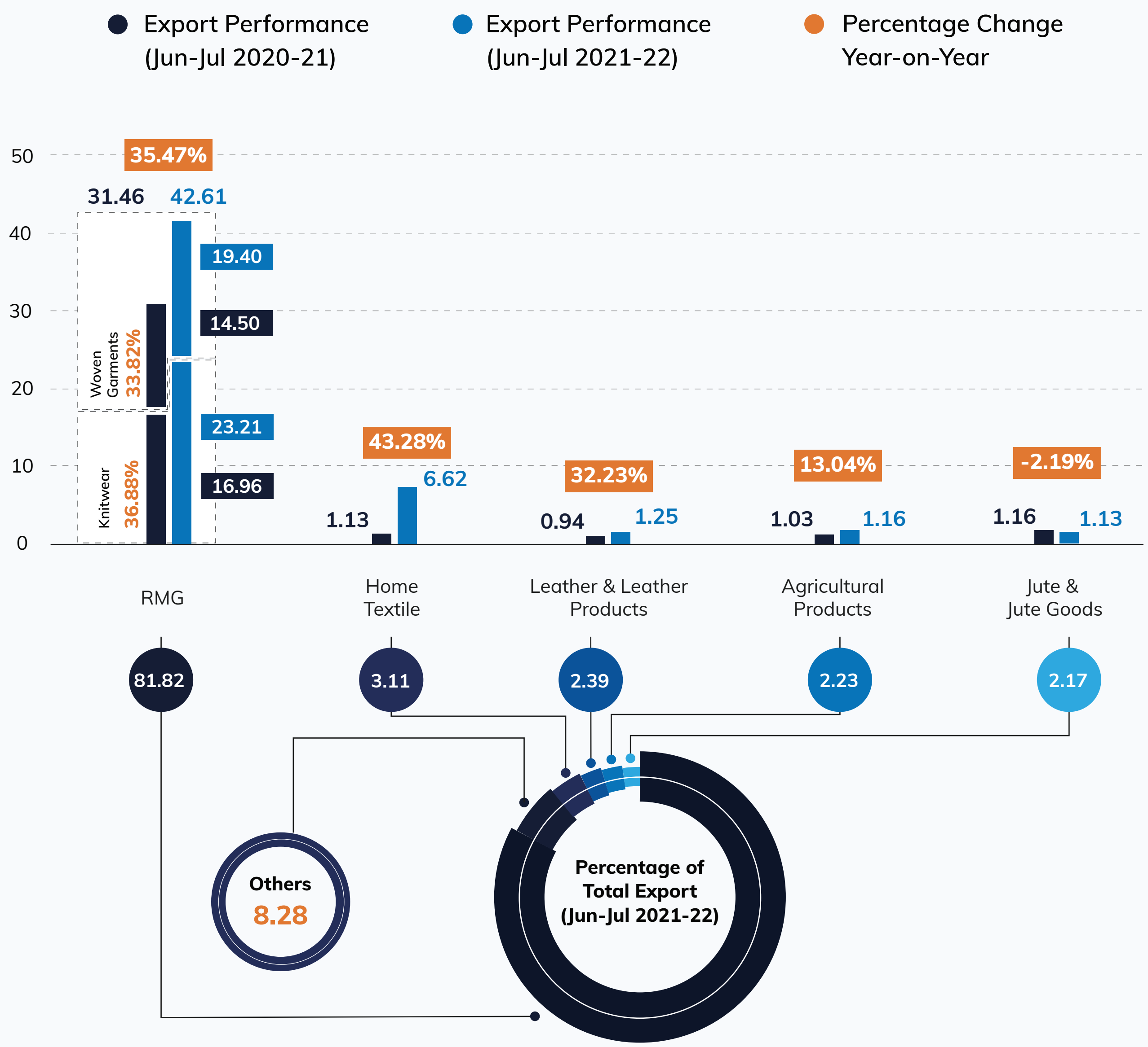


Source: BB Annual Report 2020-21, Bangladesh Bank

The counterbalance to imports comes through export, but even with record export shipments and a growth of over 34% in FY 2022 from the year before, it is a long way off from narrowing the trade deficit.

The export receipts for the fiscal year stood at around USD 52 billion[18] and components can be summarized through the following figure:

Bangladesh's Top 5 Sectors by Share of Total Export (USD Billion)



Source: BB Annual Report 2020-21, Bangladesh Bank

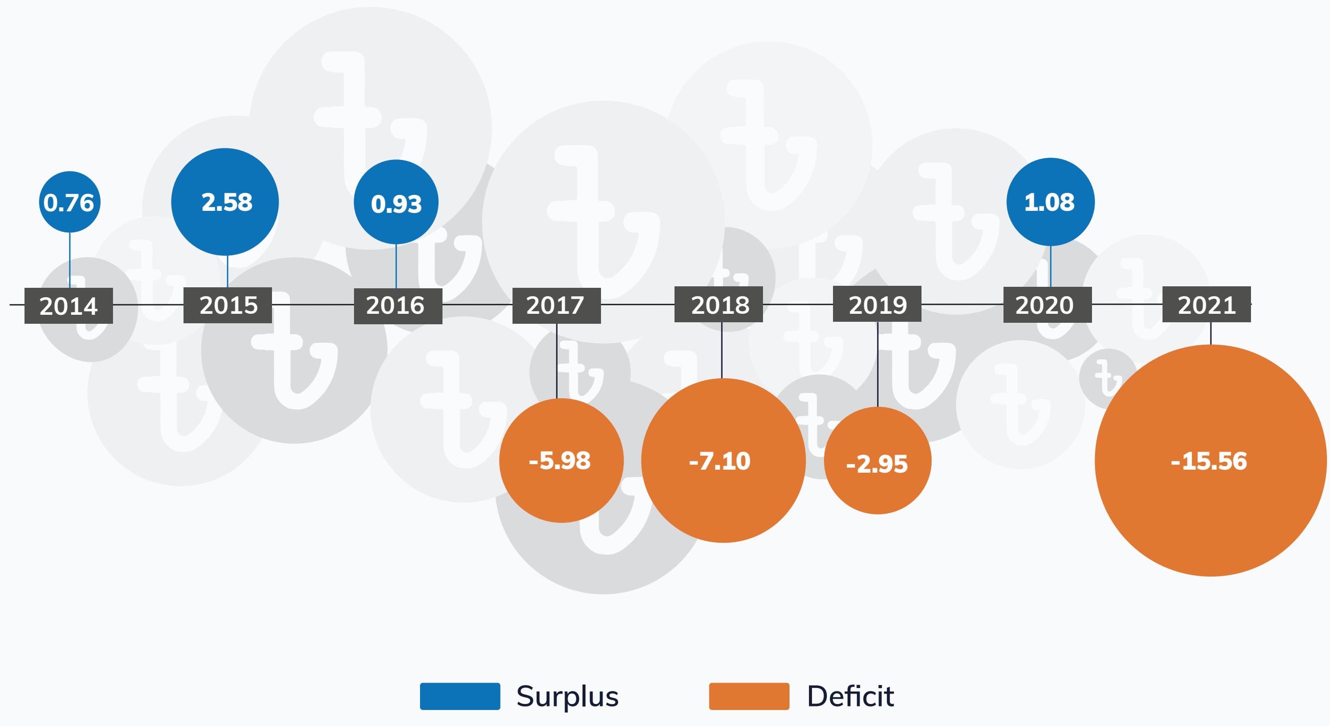
18. Export Promotion Bureau (EPB) (July, 2022)

This significance in contribution from the RMG sector resembles two sides of a coin; the export basket for Bangladesh is highly concentrated with over 80%[19] shares from the sector, meaning the performance is highly dependent. This need for a diversified basket has been an impending issue, but export data for FY 2022 showed positive contribution as USD 8 billion in export was raked in from sectors other than RMG.[19]

That being said, the net trade is just one component of the Current Account, which itself stood at a deficit of about USD 15 billion (Revised Provision, Jul-Apr FY 2022).[20] The components behind this deficit for the current account are the following: rising imports over export, a fall in remittance, and increased demand for USD.

Historic trends indicate Bangladesh has achieved 14 years of current account surplus and 28 years of the deficit between 1980 to 2021, and usually a deficit in the current account indicates import dependence, low savings, and high personal consumption rates as a percentage of disposable income.[21] In recent times, the huge deficit indicates to high levels of import dependence.

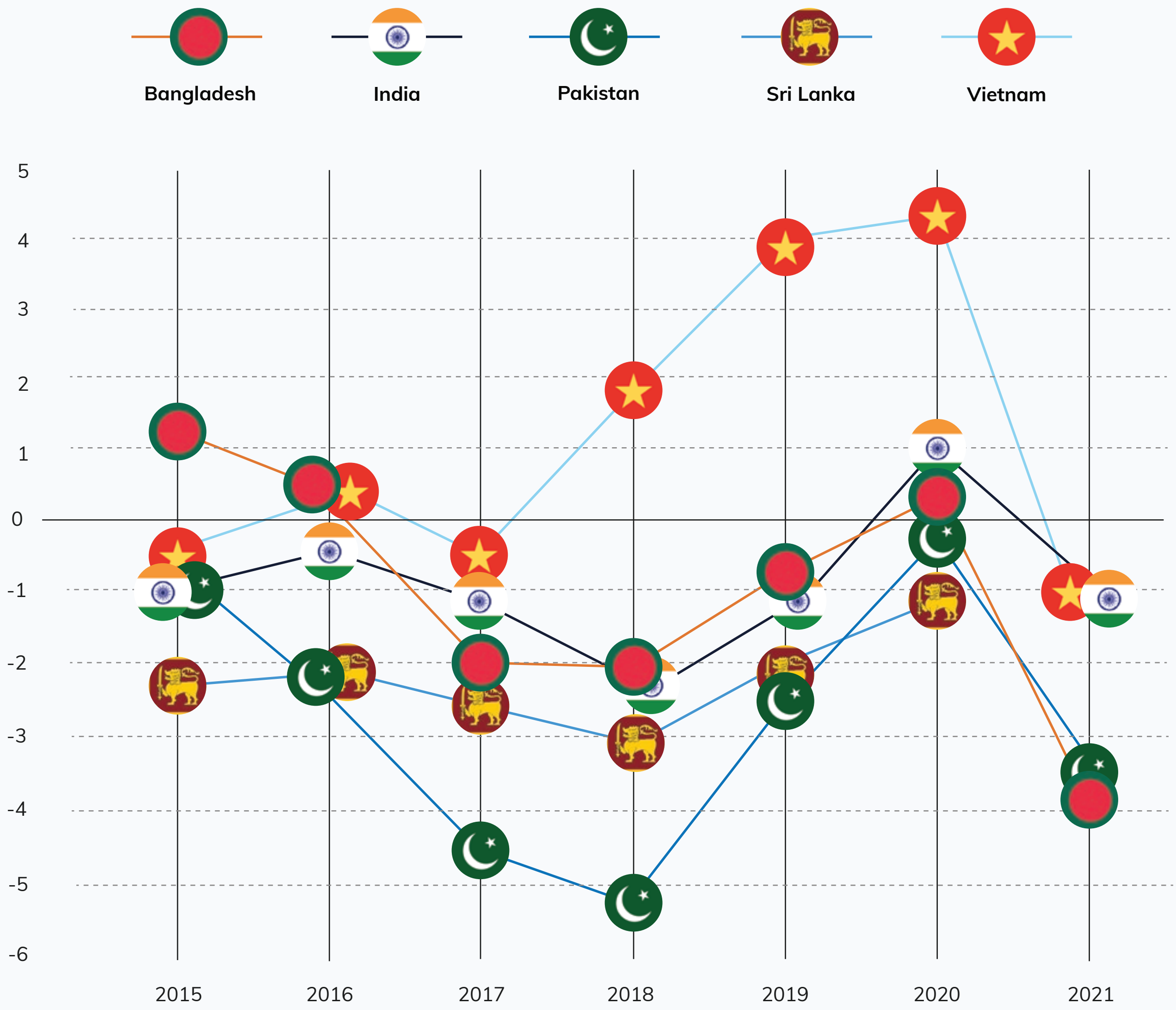
Current Account Balance of Bangladesh in the Last 8 Calendar Years
(USD Billion)



Source: World Bank Open Data

19. Export Promotion Bureau (EPB) (July, 2022)
20. Balance of payments [Monthly Data], Bangladesh Bank
21. Dr. Muhammad Mahmood, Policy Research Institute (July, 2022)

Cross-Country Current Account Balance as Percentage of GDP



Source: World Bank Open Data
Data on Sri Lanka is not included for the latest term

This phenomenon of rising import costs and skewed balances of payment is not unique to Bangladesh, rather a global one and the natural response to tackling rising costs comes in the form of monetary and fiscal tightening, like increasing interest rates. The result of this is expected to make borrowing on all levels costlier and this is also true for Bangladesh. Given Bangladesh's dependence on foreign aid, the gap due to costs will come out of the development prospect for the country, either through higher revenue from the public or by forgoing continued progressive growth.

One particular way the Bangladesh government has financed deficits is through foreign aid. In the latest fiscal year, around USD 8.42 billion have been given as foreign aid mainly by Asian

Development Bank, the World Bank, Japan International Cooperation Agency (JICA), Russia, and China.[22] This figure is representative of the first eleven months of the fiscal year. This shows that Bangladesh is getting foreign aid due to its economic potential. However, this also brings about the headache of debt servicing and the timeline could not be more unpleasant.

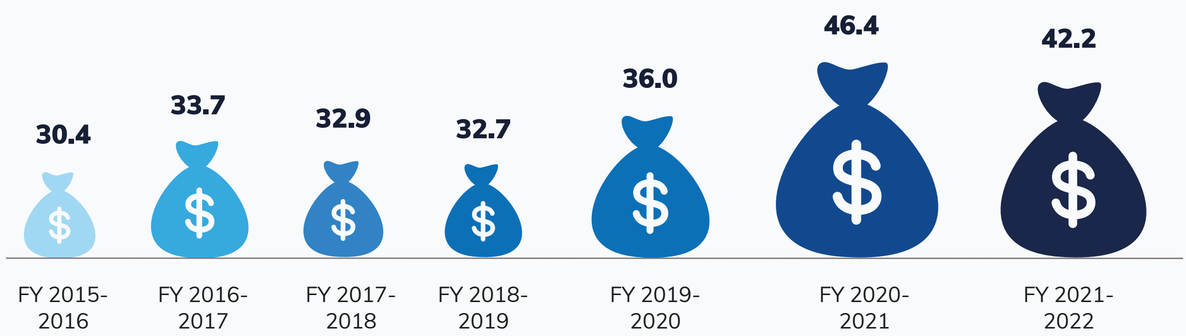
2.3 Foreign Reserve is Under Pressure and Under Guard

With the prevalent economic context, the foreign exchange reserve is the most critical shock absorber for Bangladesh. The ability to pay for the rising bill of imports and currency strength is directly dependent on the available foreign exchange reserve. However, the recent developments suggest that the central bank is taking measures to bolster the foreign reserve rather than utilizing the foreign reserve to stabilize the currency market.

In FY 2020-21, a spike in reserve was observed due to many remittance earners coming back to the country carrying their savings, amid plummeting labour demand due to the lockdown. On the other hand, there was a stagnation in imports during the pandemic period helping to increase the foreign reserve. Additionally, the informal channels to send remittances to Bangladesh closed down at the same time, forcing earnings to be diverted through formal channels.

However, the record USD 46.4 billion foreign reserve dwindled to USD 42.2 billion at the end of FY 2021-22[23] due to the unprecedented rise in imports. Bangladesh Bank had sold over 7.62 billion to the banks to stabilize the currency market.[24] As of July 2022, the foreign reserves dipped below the USD 40 billion mark at USD 39.6 billion.

Foreign Exchange Reserve of Bangladesh from FY 2016 to FY 2022
(USD Billion)



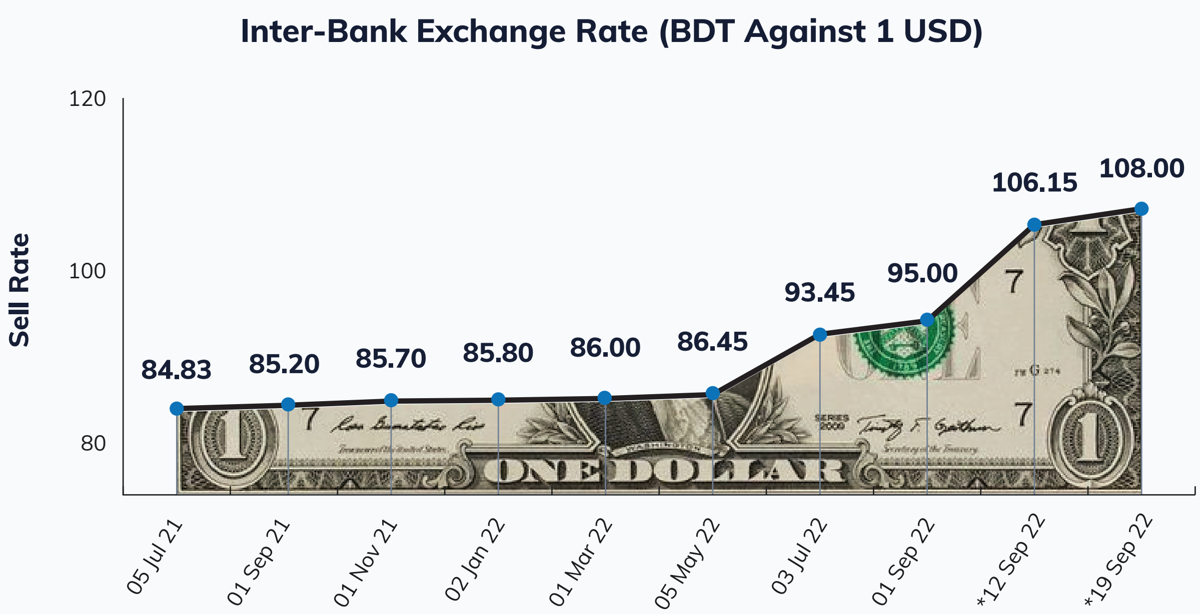
Source: Foreign Exchange Reserve, Economic Data, Bangladesh Bank

23. Foreign Exchange Reserve, Economic Data, Bangladesh Bank
24. Bangladesh Bank FY 2022

2.4 Currency Depreciation has Become an Unavoidable Burden on Bangladesh

The existing foreign exchange reserve poses tremendous pressure on the currency market. Due to the Ukraine-Russia war led turmoil, western economies started increasing interest rates to contain inflation. This resulted in money outflow from countries with lower interest rates to more developed markets having higher interest rates. Although Bangladesh had a healthy reserve in FY 2020-21 the central bank did not devalue the US Dollar against BDT then to maximize on the export earnings. Hence, Bangladesh is currently left without any cushion against the global foreign exchange market volatility.

As discussed in the previous section, the dwindling reserve compelled the central bank to devalue the currency. Since November 2021, Bangladesh Bank has allowed BDT to be devalued at least ten times till July 2022. In the kerb market, the rates reached up to BDT 100 for USD 1. Even some banks were forced to issue Letter of Credit (LC) for import at a rate higher than the rate fixed by the central bank. As of August, the kerb market rate hit the BDT 120 marks, while the official rate was BDT 25 less. As of September, 2022 the Bangladeshi currency has been allowed by the central bank to float against the US Dollar, with the value of each USD standing above BDT 105.



Source: Inter-Bank Exchange Rate, Bangladesh Bank

Note: All values taken at sell rate for the date, unless marked otherwise.

* Values represent highest inter-bank exchange rate

As Bangladesh is heavily dependent on imports, currency depreciation will significantly raise the cost of essential food items, energy (both household and commercial), and raw materials for manufacturers. Also, such increase in imports feed into the factors contributing to cost push inflation.

Another problem at hand is the 'Dollar Debt': government and private debt denominated in dollars. As most of the loans are financed in US Dollars and debt settled in US Dollars, any pending debt would have to be paid in US Dollars. Such debt servicing becomes costlier as BDT depreciates and the value of the USD rises in global markets.

2.5 The Saturated Banking Sector with Suffocating Interest Rate Cap

The banking sector has been suffering from excessive competition due to presence of a significantly large number of financial institutions, operating in a relatively smaller economy. Just to set the context, India having an economy size of USD 3.5 trillion only accommodates 21 commercial banks, while Bangladesh has 43 private commercial banks along with 9 foreign and 6 state owned commercial banks. Intense competition among banks lead to ill-judged lending decisions, which contribute to higher default rates. Some commercial banks suffer from lack of corporate governance as many lending decisions are made based on undue influence from the directors with vested interests, as opposed to adopting more objectives means to evaluate credit.

The recent setback in the banking sector has been the regulatory mandate imposed by the central bank on financial institutions, continuing to stipulate a lending cap of 9%. Although the central bank has pointed out its policy focus on facilitating liquidity and investments, such a strategy has its drawbacks. Coupled with other issues such as Non-performing Loans, rising external debt and increasing capital shortfall, the banking sector is getting entangled with myriad challenges.

2.5.1 Government's Fiscal Strategy Has Been Expansionary Leading to Private Sector Credit Growth and Inflation

The lending cap has adversely impacted depositors considering the higher inflation rates. Many depositors are losing money in real terms, encouraging them to spend more or find avenues for higher return, albeit at higher risk. To stem inflation, the central bank has been actively looking for ways to reduce money supply by changing the Cash Reserve Ratio and Statutory Liquidity Ratio requirements. Additionally, the central bank has raised its key interest rate, or repurchase agreement rate, by 50 basis points to 5.50%.[25] Unfortunately, this has an adverse effect on the banks as the interest rate for loans remains at 9% which in turn impacts the profitability of the banks.

In addition, despite recent macroeconomic pressure, Bangladesh's borrowing costs are still

25. Monetary Policy Statement, Bangladesh Bank (June, 2022)

low, which encourages borrowers to take higher credit. However, reduction of money supply and bleak economic outlook wrought about by the pandemic and international geopolitical turmoil have cautioned many investors. However, according to the central bank's statistics, the private sector credit rose to 13.95% in July 2022, compared to the previous fiscal year. The central bank has set the private credit growth target of 14.1% for the fiscal year of 2022-23.

2.5.2 Non Performing Loan (NPL) Build-Up Leading to Capital Short-Fall

According to the IMF, ballooning default loans have exposed Bangladesh's banking sector to higher risk category and their recent report estimated default loans to be over USD 11.84 billion[26], after the end of the fiscal year.

Amid higher credit demand in Bangladesh, the liquidity pressure in the banking sector is also on the rise. At the end of 2021, the banking industry had a capital shortage of more than USD 3.22 billion, highlighting the strain on the capital buffer as the Bangladesh Bank pulled out of policy relaxation due to an increase in defaulted loans. Basel III, an internationally endorsed set of standards created for banks, specifies that 10% of the capital must be maintained by the banks as the capital adequacy ratio. Twenty-three private commercial banks saw a decrease in capital adequacy ratio at the end of the previous year 2021. High default loans require maintaining a high provision, which puts pressure on the capital base of banks. Over the previous year, the provision gap tripled to USD 2.14 billion.

In addition, to address the country's ongoing financial crisis, Bangladesh recently formally requested a USD 4.5 billion loan from the Washington-based multilateral lender IMF. According to the finance minister, this is only a preventative measure by the government to tackle the current economic crisis. He also added Bangladesh's economy is not in dire straits just because the country is requesting an IMF loan. However, IMF did raise concerns regarding the low tax-GDP ratio, and Non Performing Loan (NPL) buildup in the banking system which is raising inequality.

The latest figures from the central bank show that the amount of Non Performing Loans (NPLs) increased to USD 9.79 billion as of December 31, 2021 from USD 8.41 billion the year before. On the other hand, the total amount of NPLs with the forty-three private commercial banks reached USD 4.88 billion as on December 31, 2021, from USD 3.83 billion on the same day of 2020. In an effort to ease the burden on the economy, the Bangladesh Bank on July 18 introduced a new loan rescheduling policy after nine years. To relieve pressure on firms, the new policy includes other time constraints and an extension of the grace period for loan payback. Defaulters will now be permitted to reschedule their NPLs four times, as opposed to the prior three times, all of which will encourage unscrupulous borrowings to default.

On top of that, Bangladesh Bank's repayment relaxation policy (Aug 26, 2021) stated, a 25% payment of dues for the month of January till December (2021) would result in the loans not being treated as substandard. While this is good for the borrower, it results in distorted cumulative default loan figures.

Some experts are supportive of more punitive actions on serial defaulters, while showing more leniency toward first time defaulters. The central bank has to ensure more oversight across the

26. As Reported by Bangladesh Bank Authorities

board of different commercial banks by including and empowering capable independent directors. Alongside, stricter actions have to be taken against directors with track record of unduly influencing lending decisions. Some experts have suggested shifting toxic assets from different banks to a government owned vehicle, which will indirectly support banks replenish their capital base.

Chapter 3

Measures to Keep the Economic Cogs Moving Smoothly

Measures to Keep the Economic Cogs Moving Smoothly

Inflation & Trade Deficit Measures Will Be Guiding the Government's Strategy

Over the last couple of months, we have seen the government take austerity measures to curb the import demand. There has been an increased import duty imposed on luxury products. Foreign trips of government officials have been cancelled. Open hours for shops and supermarkets across the nation have been curtailed to eight in the evening. Load shedding has been taking place regularly all across the country and factory closure has been enforced once per week.

Apart from the mentioned ones, the government needs to undertake a number of measures to stabilize the macroeconomic scenario and set the course for facilitating medium term growth trajectory. Some of the policy interventions which can be explored are included in the followings:

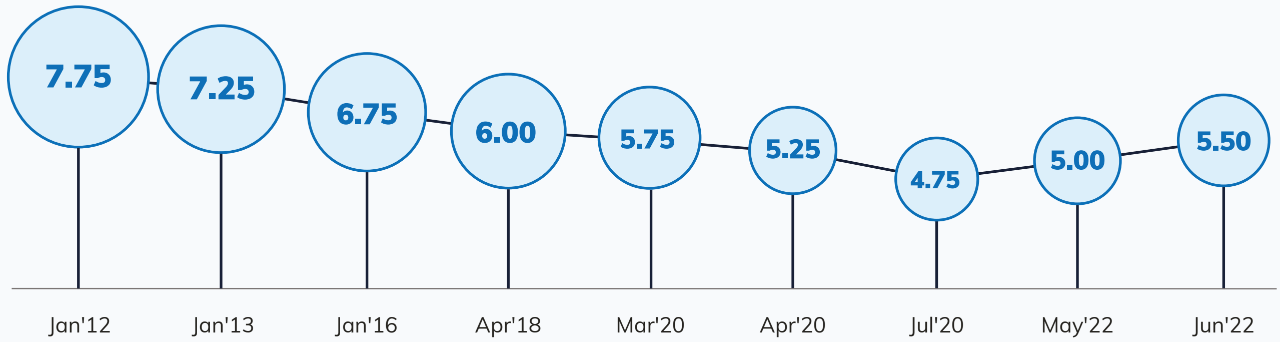
- Raising the interest rate to curb money supply to fight inflation
- Incentivize exports and promote FDI to replenish the foreign reserve
- Prioritize and formalize remittance
- Improving trade relations to prepare for Least Developed Country (LDC) graduation
- Focus on revenue collection for better debt-servicing

3.1 Raising the Interest Rate to Curb Money Supply to Fight Inflation

Major economies like the United States have undertaken tightening monetary policy for reining in inflation. In Bangladesh, the scenario is slightly different. The central bank has shown reluctance to increase interest rate as it will increase cost of borrowing for businesses. Hence, the central bank has focused on controlling money supply rather than raising interest rates.

In light of the global turbulence and rise of inflation, Bangladesh Bank (BB) resorted to increasing the policy rates in two steps. Currently, there is a 9% interest cap on lending rates and the repo rate stands at 5.5%, such increment has been viewed as insufficient to pull down aggregate demand and control inflation.

Revision of Policy Rate by Bangladesh Bank (In Percentage)

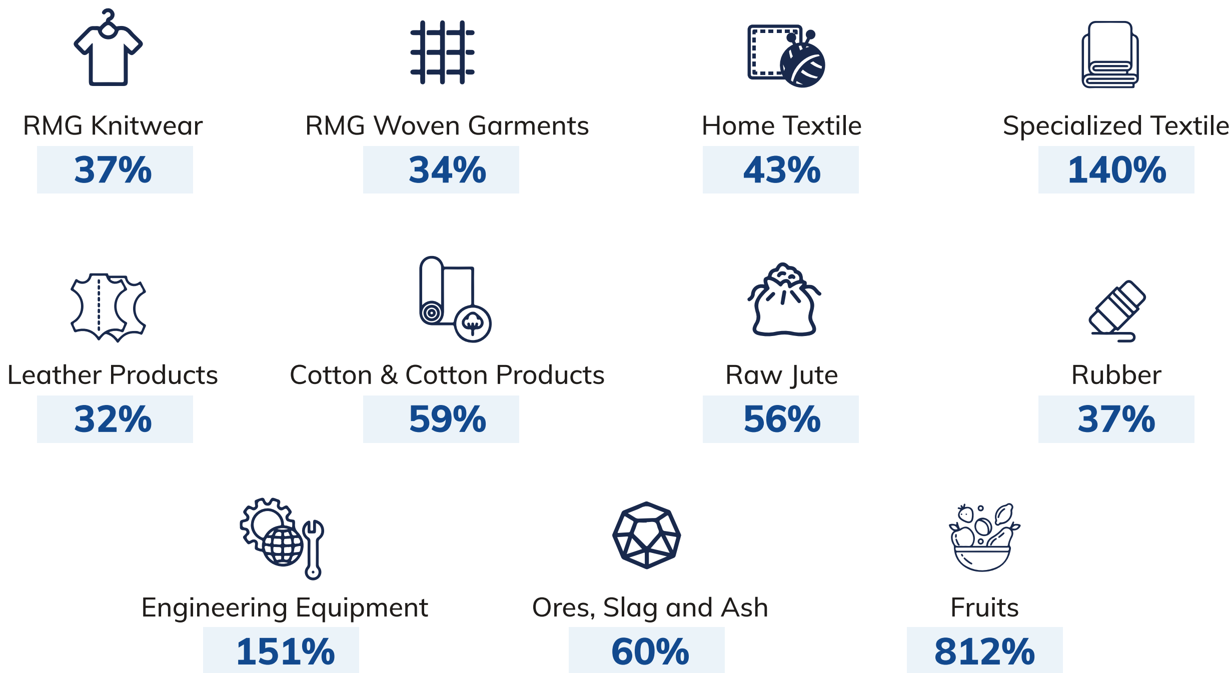


Source: Bangladesh Bank (May, 2022)

3.2 Incentivize Exports and Promote Foreign Direct Investment (FDI) to Replenish the Foreign Reserve

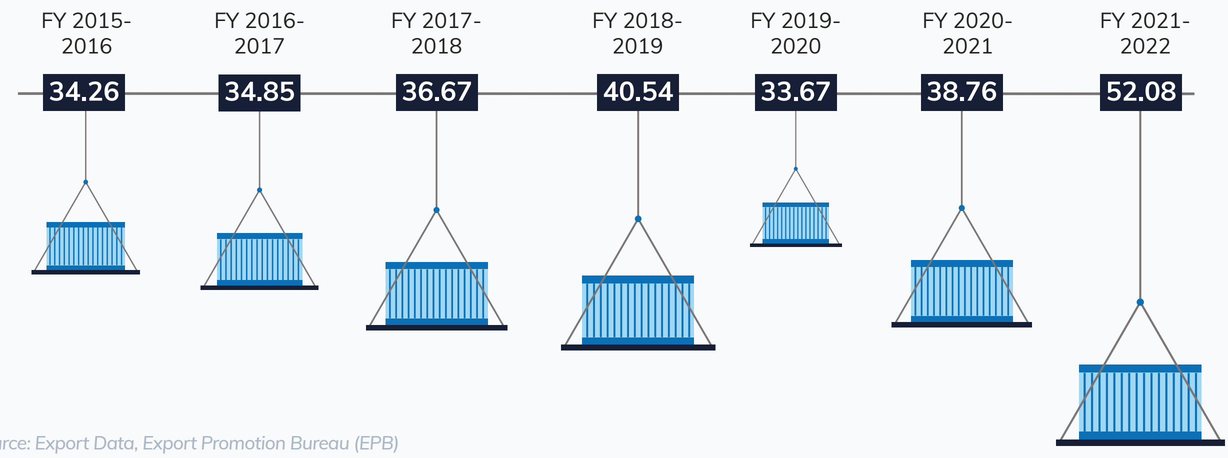
The major sources of foreign earnings: export, and remittances must be given utmost importance. In recent times, we have seen positive growth momentum for both these segments. In FY 2021-22, Bangladesh's export earnings crossed USD 50 billion for the first time in its history. This achievement is attributed to the quick rise in orders for apparel spearheaded by post-pandemic recovery in demand. Due to repeated lockdowns in China, large number of apparel orders have been shifted to other alternatives like Vietnam and Bangladesh.

Export Sectors and its Year-on-Year Growth (FY 2022)



Source: Export Data, Export Promotion Bureau (EPB)

Export Performance of Bangladesh
(USD Billion)



Source: Export Data, Export Promotion Bureau (EPB)

The national budget for FY 2022-23 has incentivized exports and import substitution through tax benefits. On the other hand, export opportunities to various markets are being explored through diplomatic channels through preferential trade agreements for various export items. New opportunities are opening up as negotiations with China and India are bearing promising results such as duty-free market access for 99% of Bangladeshi products.[27]

3.2.1 Export Earnings Compromised Due to Supply-Chain Disruptions

Despite the latest developments, Bangladesh's export is mostly confined to the apparel sector, accounting for over 80% of all exports in the latest fiscal year. An analysis of export destinations also shows that these exports are highly concentrated in the USA, UK, and EU markets.

Raw material prices in the global markets are also behaving erratically and putting pressure on the bottom line for the exporters. Energy prices have increased due to the rising oil and gas prices in the global market. Similarly, a trickle-down cost increment of transportation, freight and operations riddles the manufacturing landscape.

Bangladesh is also feeling the direct impact of the crisis between Russia and Ukraine since the country has commercial ties. New orders were cancelled as a result of the war and resulting sanctions on Russia, which caused numerous payments to be stopped and limiting shipments to Russia.

Bangladesh's exports to Russia have grown steadily each year for the past decade. Exports from Bangladesh to Russia increased from USD 133 million in the 2011–12 fiscal year to USD 665 million ten years later.[28]

Moreover, the war induced inflationary phase in US, UK, and EU market is leading to a potential decline in export volume to those destinations. Major merchants' and brands' outlets have a lot of unsold stock. Hence, companies are either

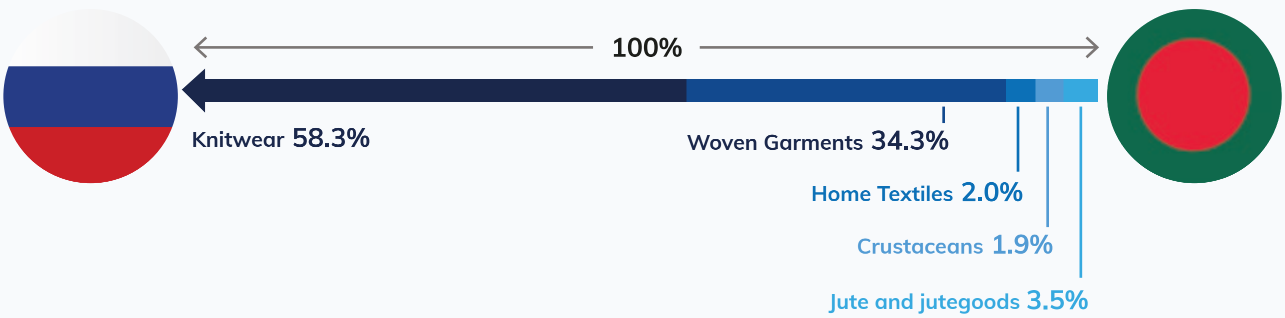
27. Foreign Minister AK Abdul Momen at a Press Briefing (August, 2022)
28. How the war in Ukraine threatens Bangladesh's food security, International Food Policy Research Institute (2022)

refraining from placing new purchases, requesting deferring payments, or requesting that suppliers delay supplies.

However, Bangladesh experienced stronger exports starting from September of the prior year, it persisted till April, 2022. This is due to the impact recessionary atmosphere prevailing in the EU, UK, and USA markets. As western customers tighten their pockets in response to soaring prices and the escalating unpredictability brought on by the Russia-Ukraine war, work orders to Bangladesh's clothing industry decreased by more than 20% between September-November.[29]

Similarly, from April to June period in 2022 saw a 20% decrease in orders compared to the previous year. Due to this, there have been reports of up to 30% of RMG capacity in Bangladesh not being utilized.

Breakdown of Exports to Russia in FY 2019-20



Source: Country Wise Export (Goods), Export Promotion Bureau (EPB)

29. Faruque Hassan, President, Bangladesh Garment Manufacturers and Exporters Association (BGMEA) (June, 2022)

Case Study

How the Current Budget Incentivizes Export Growth

The focus of the government for the current fiscal year is to shield businesses and consumers from inflation, while simultaneously investing in the diversification of export-oriented sectors to improve the balance of payment conditions. The proposed subsidy allocation of USD 7.84 billion (Increased by 1.7% from the previous budget) in the running budget is provisioned to aid sectors by controlling business input costs in the form of: USD 1.61 billion for electricity, USD 1.52 billion for fertilizers, and USD 1.64 billion for Liquefied Natural Gas (LNG).[30]

In light of the rising costs of the aforementioned commodities, these allocations are expected to shift the cost burden and help sustain the growth of local businesses without having to bear the adversities. The mentioned focus on food security was also aligned with the policy perspective which can be seen in the budgetary allocation for agriculture. USD 286 billion allocations for the use of 51,300 units of agro-machinery[31] followed by a focus on research and development in seed technology through best farming practices are highlights of the policy interventions.

The focus of policymakers went beyond facilitating the export-oriented sector and was also apparent for the growth prospect of local sectors. Some of the notable interventions come in the form of:

- Attention to green factories by further reducing taxes by 2%
- The textile industry enjoying reduced corporate tax rates of 15% till FY 2025-26
- The conditional tax cut of 2.5% for any local businesses that adopt banking channels for transaction (Currently 20% for listed companies and 27.5% for non-listed companies)
- Ability to amend input tax credit to receive tax rebates
- Reduction in penalty and increase in payable time for Value Added Tax (VAT) dispute cases
- Reduced VAT in wholesale trading
- VAT exemption on steep and Polyethylene Terephthalate (PET) chips
- Exemptions for local manufacturing of Active Pharmaceutical Ingredients
- Withdrawal of advance tax on imported raw material for polypropylene staple fiber
- The 10-year tax break for: fruit processing, vegetable processing, dairy and dairy products, and agriculture equipment

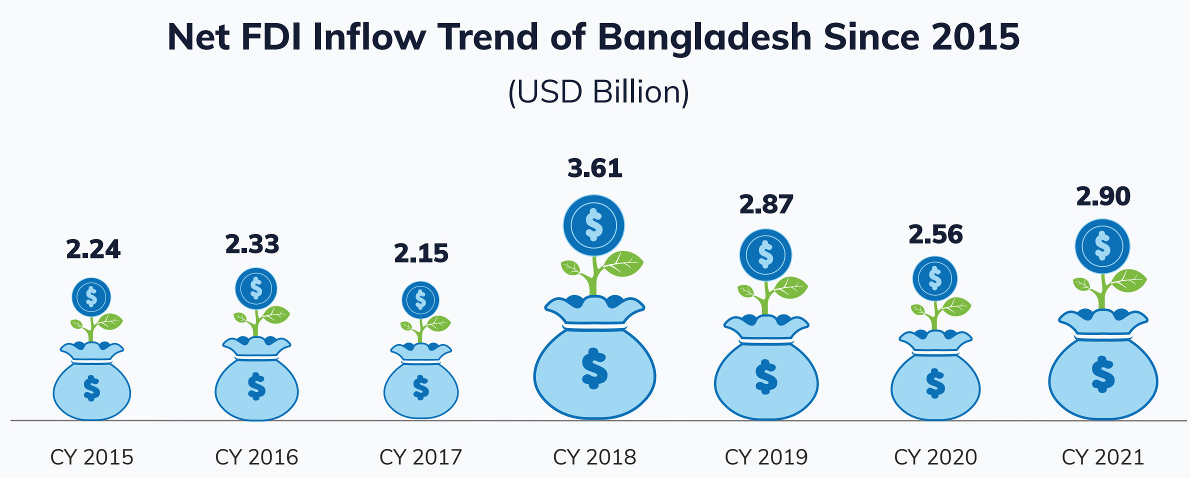
30. Bangladesh's National Budget 2022-23: Banking on Resilient Business Output during Global Challenges [Part 2], LightCastle Partners (June, 2022)
31. ASM Golam Hafeez, Professor, Bangladesh Agricultural University (At an interview with NewAge, June, 2022)

3.2.2 Interventions to Explore for Growth

Given the situation of the economy, particularly the need for foreign reserves, there is no alternative to focusing on exports. Expansion of exports in terms of depth and width is of the essence. Over the last couple of years, we have seen Bangladesh pursue bilateral trade agreements to bolster exports and some of the sectors got a foothold in new export destinations. At the onset of COVID recovery, there was robust growth in orders for the apparel sector. However, there has been a slump in export orders in the RMG sector. The current price hike of energy, fuel, transportation, and the depreciation of taka complicates the matter for the manufacturers.

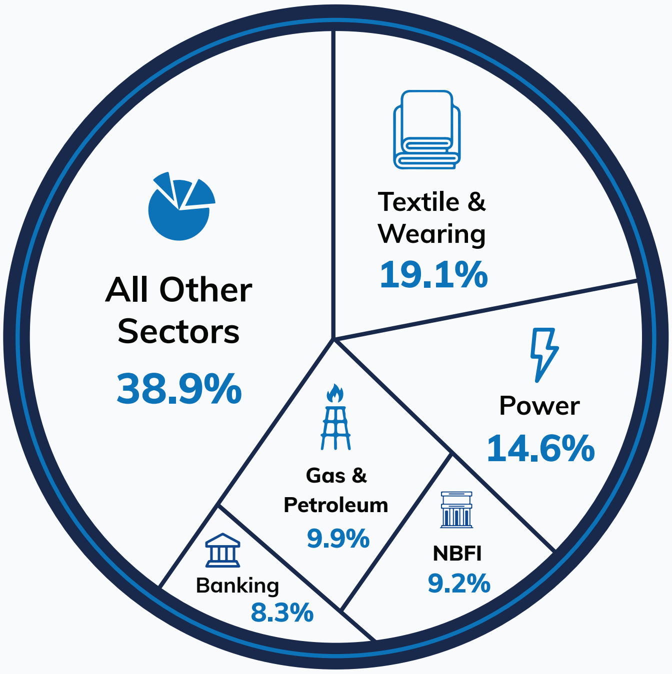
- Hence a focus on export diversification is a mandatory risk mitigation strategy for Bangladesh. Although we have seen the electronics or consumer durables industry pick up in exports there is ample room for export diversification.
- At the same time, export-oriented industries should be given continued priority in terms of energy, fuel, and transportation support in the form of service delivery or subsidies. Although there are major incentives in place in the budget proposed for the current fiscal year, some aspects can be revisited and prioritized to help out certain sectors.

Unlike exports and remittances, the FDI trend shows a very meagre growth rate over the last couple of decades. The slow pace of FDI growth in the recent past is attributable to investor reluctance due to the pandemic. On top of that, Bangladesh has an investment climate not conducive for setting up a business. The country ranked 105th on World Economic Forum's Global Competitiveness Index (GCI) 2019. The frustratingly long-time requirements for property title transfer, getting electric lines, and lack of a supporting ecosystem generally deters new investors.



Source: Foreign Direct Investment and External Debt (July-December 2021), Statistics Department, Bangladesh Bank

Share of Net FDI Inflow by Sectors (CY 2021)



Total FDI Inflow (CY 2021)
(USD Billion)

2.90

3.3 Prioritize and Formalize Remittance

Remittance inflow stood at just over USD 21 billion in FY 2021-22. In the previous fiscal year, the country registered its highest ever remittance flow of over USD 24.7 billion.[32] This major influx was attributed to the return of migrant workers who lost their jobs due to the pandemic, bringing with them all their savings. At the same time, informal remittance transfer channels were practically non-existent, making formal and banking channels the only option, leading to a higher transfer through formal channels.

In FY 2020-21, only 2,31,000 workers went abroad in search of jobs given the low employment opportunities due to the economic fallout of the pandemic. However, from January of FY 2022, 9,88,000 workers[33] have left for major destinations abroad in search of jobs. This shows a greater probability of higher remittance inflow in the current fiscal year. Another critical factor to get greater remittance is the devaluation of the Bangladeshi Taka against the US Dollar. As BDT gets devalued, and the 2.5% incentive for sending remittance is provisioned by the government, the gap between formal and informal channels will further diminish. As of mid september Bangladeshi currency value against US Dollar is allowed to float according to market dynamics. This narrowed gap will encourage more non-resident Bangladeshis to shift from the informal channels to the formal ones.

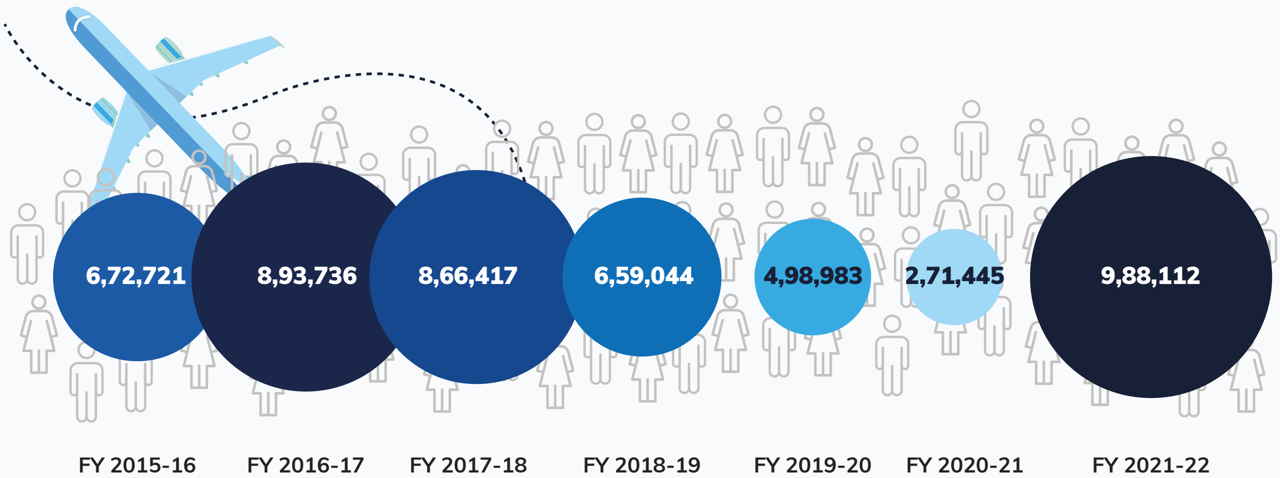
32. Monthly Data of Wage Earner's Remittance, Bangladesh Bank
33. Bureau of Manpower, Employment, and Training (BMET) (FY 2022)

Bangladesh's Remittance Inflow (FY 2013 to FY 2022)

(USD Billion)

Source: Monthly data of Wage earner's remittance, Bangladesh Bank

Bangladesh's Remittance Worker Outflow (FY 2016 to FY 2022)



Source: Bureau of Manpower, Employment, and Training (BMET)

Top 6 Destinations for Manpower Export (FY 2022)

	Total Migrant Workers		Total Migrant Workers
KSA	33%	Malaysia	7%
UAE	17%	Singapore	6%
Oman	11%	Qatar	6%

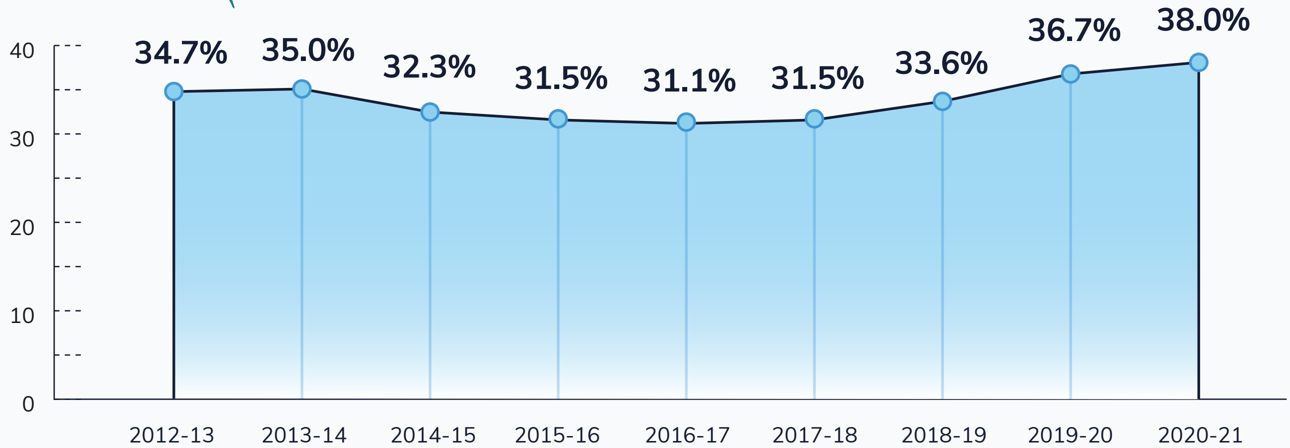
Source: Overseas Employment and Remittance, Bureau of Manpower Employment and Training

3.4 Improving Trade Relations to Prepare for Least Developed Country (LDC) Graduation

As the economy nears LDC graduation in 2026, the external cost of borrowing is expected to increase. Historical evidence shows the Asian Development Bank (ADB) decreasing the fund from its soft loan window year-on-year after Bangladesh's first announcement of graduating from a Low to Lower Middle-Income Countries (LMIC) in 2016.[34] Bangladesh's biggest bilateral donor, Japan, has also been observed to increase the interest rate from 0.01% to 0.1% in recent times.

Total Debt as a Percentage of GDP

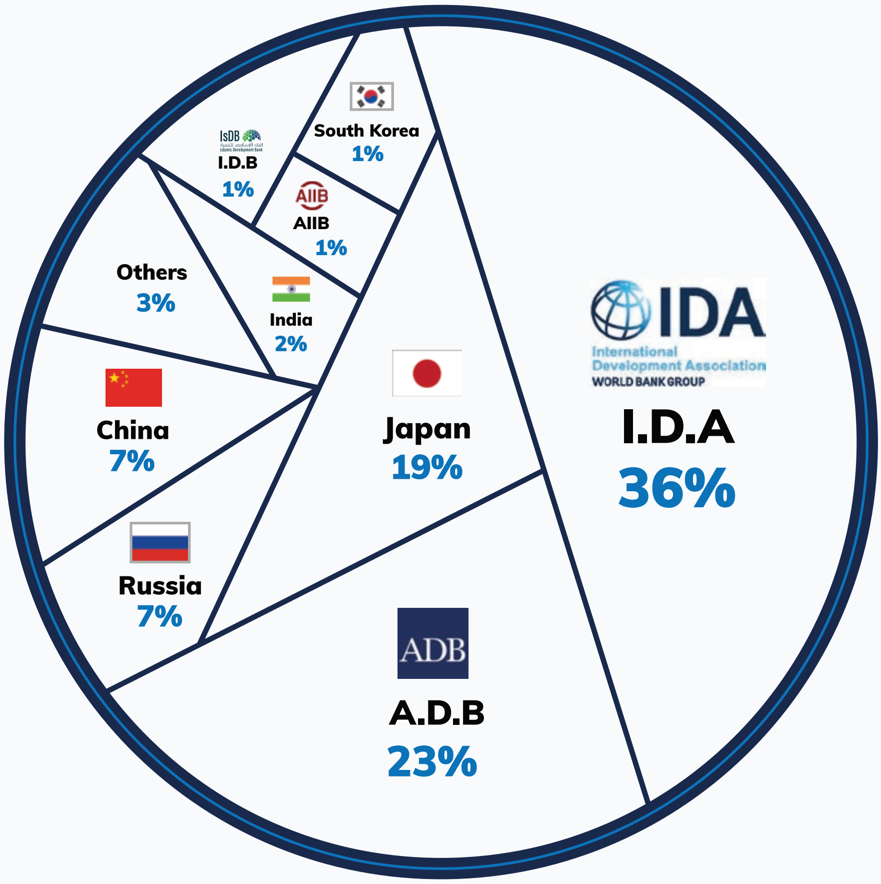
(FY 2013 to FY 2021)



Source: Ministry of Finance

34. The World Bank

Foreign Debt Composition of Bangladesh
(End of FY 2020-21)



Source: Ministry of Finance

3.5 Focus on Revenue Collection for Better Debt-Servicing

By the end of Fiscal Year 2021, the country's total debt stood at USD 131 billion, which was 44% of GDP. Broader estimates show that the debt has risen to 46% of GDP for FY 2022, and while this unusual rise has been observed since 2018 in the South Asian region[35], the adversities are expected to affect Bangladesh around FY 2024-25, when the grace period for a number of large loans expire. In recent years, the allocation of debt has also changed, shifting from predominantly domestic to external debt.

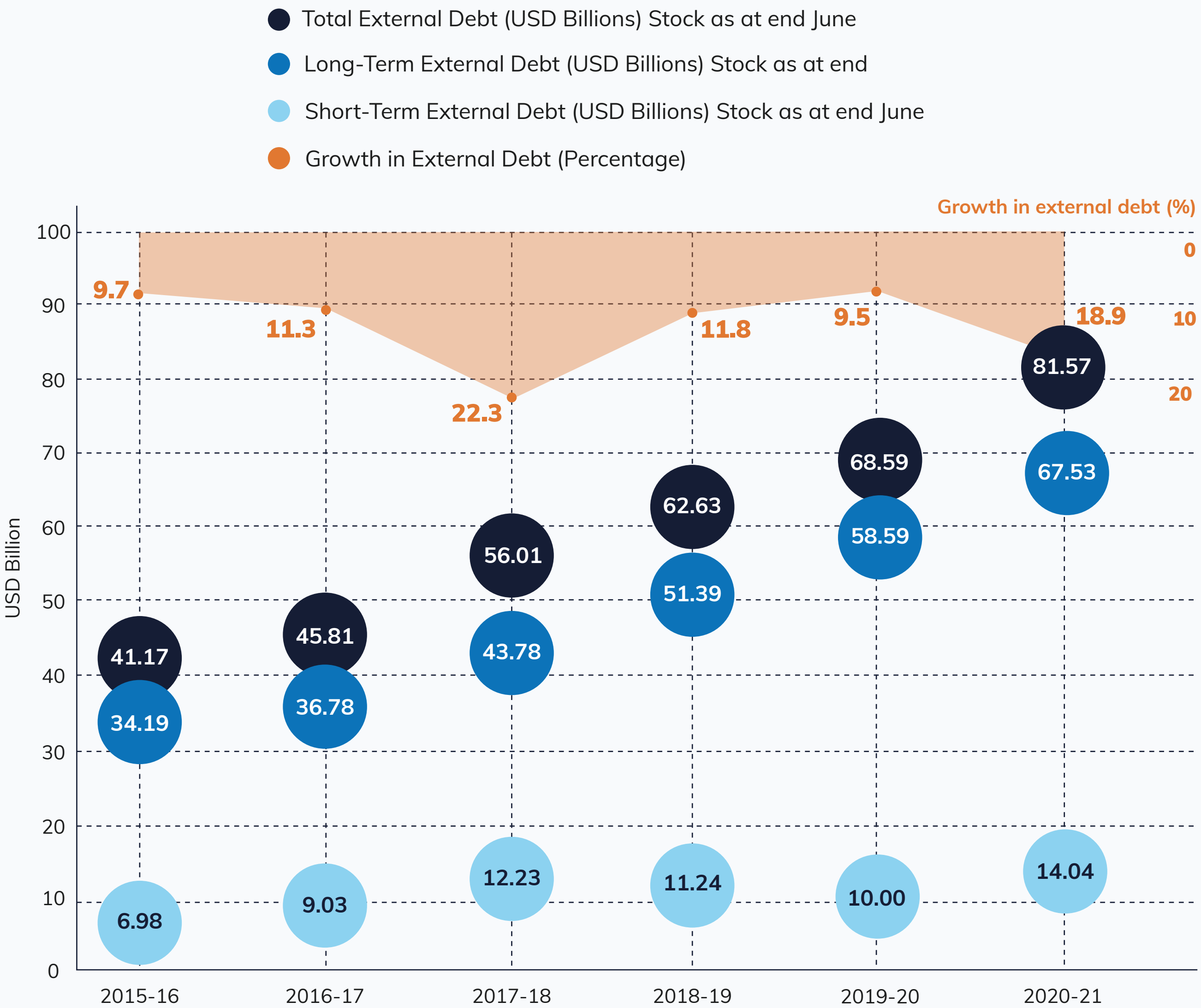
While these numbers themselves are not alarming, it is wise to consider that an increase in financing through external debt indicates an underlying amount of principal and interest payment, which will come out of the foreign exchange reserve due to international debts having to be paid in the currency it was received in.

This in turn puts pressure on the balance of payment. The external debt stock and its composition based on long or short-term debt have been shown in the next page.

35. Conversations on Public Debt in Bangladesh, Debapriya Bhattacharya, CPD Distinguished Fellow

External Debt Stock and Growth Rate of External Debt of Bangladesh

(FY 2016 to FY 2021)



Source: FIED Management Cell, Statistics Department, Bangladesh Bank

At the end of March 2022, the total external debt to GDP ratio stood at 27%[36] and a majority of this growth can be contributed to commercial borrowing, which can be broken down into the following:

Breakdown of Total External Debt to GDP Ratio

Private Sector Borrowing	Buyer's Credit	Foreign Letter of Credit
Increased By	Increased By	Increased By
USD 6.3 billion	**USD 4.0** billion	**USD 0.26** billion

Source: Bangladesh Bank and Economic Relations Division

36. Economic Data, Bangladesh Bank

In terms of the government's borrowing, more than 83% were collected from long-term concessional debts, meaning the short-term or even mid-term effects of these borrowings won't have an impact on the economy, as estimated by experts. However, increase in commercial borrowing, given its short-term nature, might impose eminent risk, especially as international borrowing becomes more expensive. Regardless, as mentioned, the borrowing statistics of a country is not an alarming figure, rather how this debt is serviced gives an outlook of the feasibility of utilizing these funds.

3.5.1 Debt Servicing Timeline and Least Developed Country (LDC) Graduation Will Bring Mixed Impact to the Economy in the Long Term

Considering the debt conditions, Bangladesh is still not in a position of risk. The 44% public debt to GDP is much lower than the IMF risk threshold of 70%[37] and the external debt service to revenue ratio stood at 10.2% (2020), which is also well below the threshold of 23%.

However, by FY 2025, the debt repayment is expected to double from USD 2.4 billion to USD 4.02 billion[38] as a number of large foreign loans reach maturity. Calculations by the Economic Relations Division (ERD) give a forecast as such:

Near Term Debt Servicing Forecast by ERD

Fiscal Year	Overall Debt Repayment (USD billion)	Principal Amount (USD billion)	Interest Amount (USD billion)
2024	3.28	2.3	0.98
2023	2.7	1.9	0.8

Source: FIED Management Cell, Statistics Department, Bangladesh Bank

A majority of these loans were secured through non-concessional loans from 2013 to 2021 and allocated to mobilize investments in megaprojects. A detailed list of projects are given in the next page.

In the short term, the budgetary allocation of fast-track projects are expected to significantly decrease once a few of the projects reach near completion, such as Chattogram-Cox's Bazar Rail Link project expected to be completed in FY 22-23, followed by Payra Seaport, Matarbari Deep Seaport, and Rampal Power Station. Contributions from completed projects are also expected to impact the economy, such as the Padma Bridge with its direct expected impact on the GDP by 1.3-2.0% per year.[39] Regardless, drive-through infrastructure development in Bangladesh is always met with deadline extensions and cost increases and the tendency to finance through foreign loans, especially at a time of reserve crunch will create added pressure on the debt servicing timeline.

37. Selim Jahan, Director, Human Development Report Office
38. Budget Preparation, Economic Relations Division (May, 2022)
39. Prof Mustafizur Rahman, Distinguished Fellow, Centre for Policy Dialogue (CPD)

Mega Project Debt Amount, Grace Period Details

TOP TWENTY MEGA PROJECTS IN BANGLADESH

Financial and Fiscal Issues

Amount of loans by End of Grace Period in USD Million

- There are a total of 40 loan packages and 5 grants for the 20 mega projects amounting to USD 32.26 billion
- 37 loan packages to kick-off repayment by 2030, amounting to USD 28.43 billion
- 7 loan packages out of 37 are semi and non-concessional owed to the Exim Bank of China and Russia, amounting to USD 17.78 billion
- The Russian loans are due for repayment in 2020 (1 loan) and 2026 (1 loan)
- The Chinese loans are due for repayment in 2021 (1 loan), 2024 (2 loans), 2025 (1 loan) and 2026 (1 loan)

Expiry Year of Grace Period	No. of Loans	Amount of Loans
2017	1	0.20
2018	1	0.03
2020	1	0.49
2021	2	0.70
2023	3	0.64
2024	5	5.16
2025	5	1.31
2026	6	14.07
2027	3	0.83
2028	4	1.73
2029	2	1.79
2030	4	2.78

Source: Dr Debapriya Bhattacharya, Distinguished Fellow of the Centre for Policy Dialogue (CPD) on a Media Conversation (July, 2022)

The USD 20 billion budget deficit expected for FY 2022-23 is one-third of the total allocation, which will be financed through public and foreign loans, out of which, 72.7% will be financed from the banking sector.[40] An aggressive drive by the government to finance the budget deficit is already underway with the concerned authorities approaching donor organizations in an attempt to close the gap. Current efforts by the government have seen potential from the following donors:

Expected Budgetary Deficit Financing Through Foreign Fund

	PROGRAM	Expected Amount (USD billion)
World Bank (WB)	Green Resilient and Inclusive Development (GRID) Policy Credit	0.5 - 0.75
World Bank (WB)	Recovery and Resilience Development Policy Credit (DPC)-II	0.25
Asian Development Bank	Budgetary Support	1.00

Source: Press Release, Ministry of Finance Official (June, 2022)

According to ERD, the budgetary support received by the government till May of FY 2022 stood at USD 1.13 billion, with foreign aid adding to a record USD 8.42 billion. The highest contributors to the aid are broken down:

Highest Contributors of Foreign Aid Received

During July-May of FY 2022

Asian Development Bank (ADB)
USD 2.08 billion

Japan International Cooperation Agency (JICA)
USD 1.78 billion

World Bank (WB)
USD 1.54 billion

Russia
USD 1.15 billion

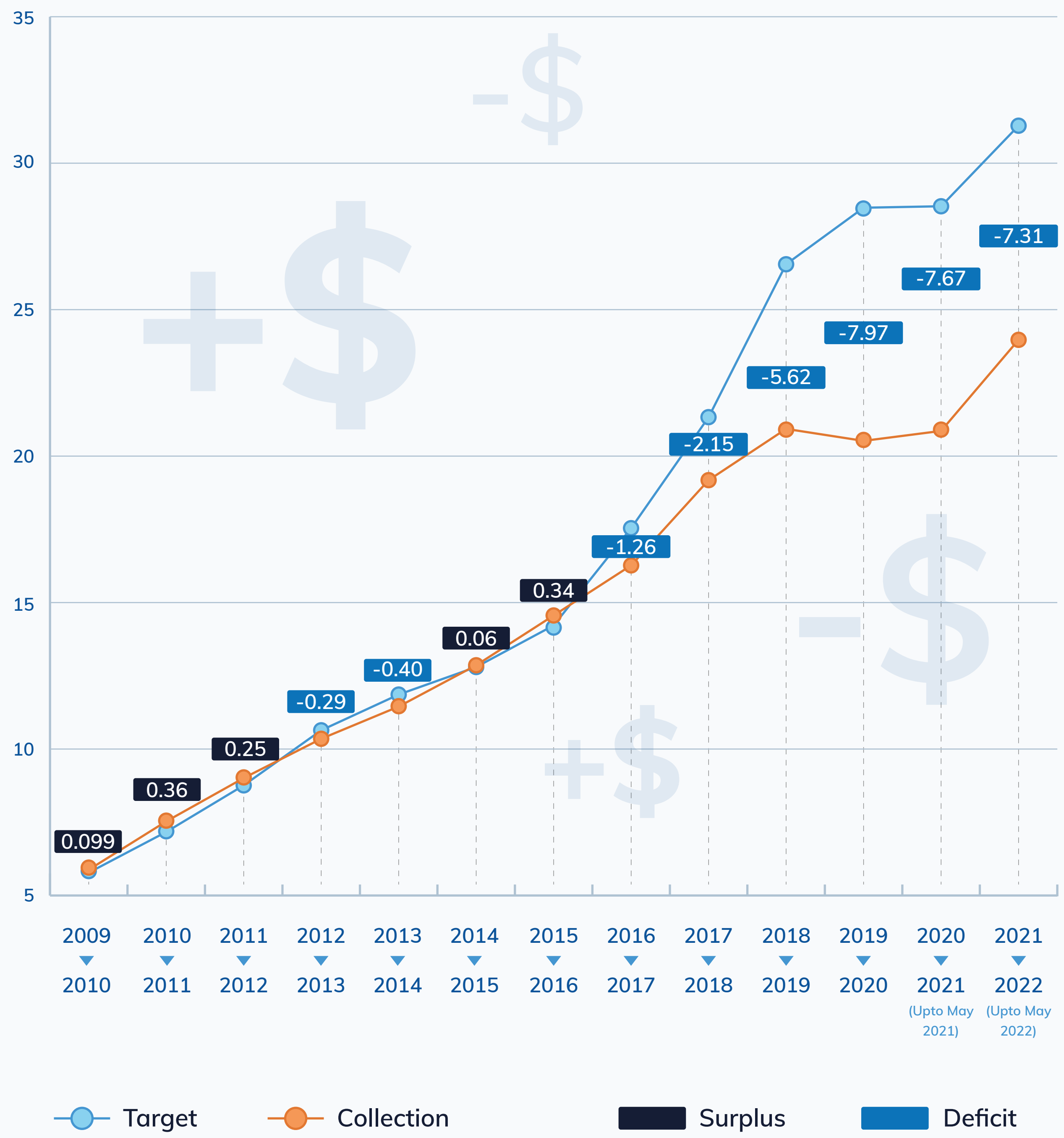
China
USD 0.80 billion

Source: Economic Relations Division (ERD) (June, 2022)

40. Bangladesh's National Budget 2022-23: Banking On Resilient Business Output During Global Challenges [Part 1], LightCastle Partners (June, 2022)

One way forward toward better debt servicing will be to shore up revenue collection, enabling the government to not only finance budget deficit, but also to finance infrastructure development projects by mobilizing internal funding, without relying on internal or external debt.

Bangladesh's Tax Collection Trend Against Targets
(USD Billion)



Source: Ministry of Finance and National Board of Revenue (NBR)

3.5.2 Bolstering Revenue Collection: The Need of the Time

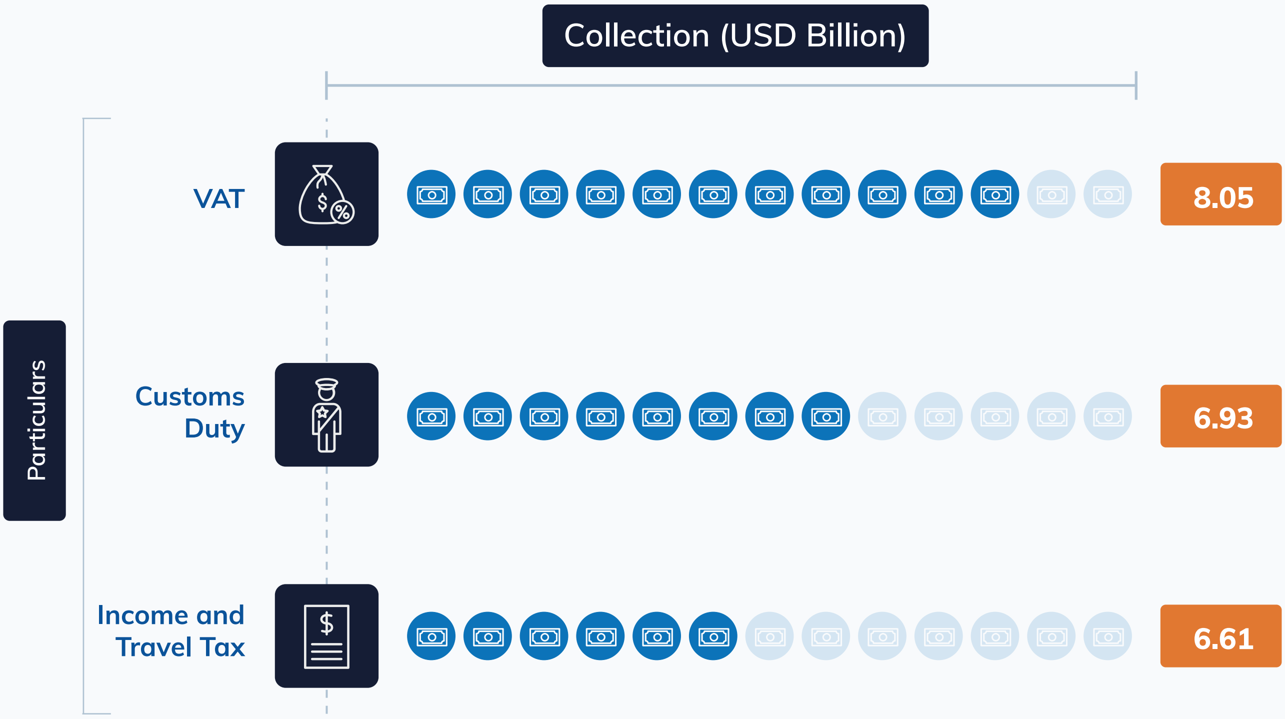
Bangladesh's historical revenue collection trend has mostly been underwhelming, most noticeable since FY 2012-13, due to overly optimistic goals set by the government but no structural reforms to back the strategy up. Looking at the current trend, total collection up till March of Fiscal Year 2021-22 fell short by 38%[41], a pressure that is a common scenario leading up to the fourth quarter of the fiscal year. This recurring scenario makes it difficult for respective authorities to determine the shortfalls and take effective actions in due time.

Component-Wise Revenue Collection (Target vs Actual)
(USD Billion)

Source: National Board of Revenue (NBR)

41. Revenue Collection, National Board of Revenue (NBR) (July-March, FY 2022)

Sector Wise Revenue Collection and Top Contributors (Jan-Mar'22)

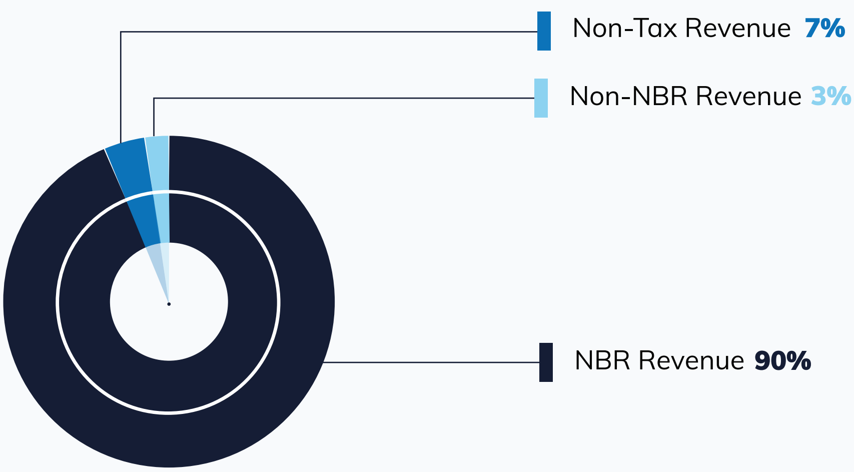


Source: Quarterly Analysis of Government's Revenue Receipts, Bangladesh Bank (Jan-Mar 2022)

Although the collection was below targets, the overall revenue grew by 15.21% from July-April compared to the same period of the last fiscal year.[42] The sector-wise revenue collection and its top contributors are summarized above.

Breaking down the components of revenue collection, National Board of Revenue (NBR) revenues make up 90% of the total collection followed by non-tax revenue and non-NBR revenue.

Share of Revenue Collection (Jan-Mar'22)



Source: Quarterly Analysis of Government's Revenue Receipts, Bangladesh Bank (Jan-Mar 2022)

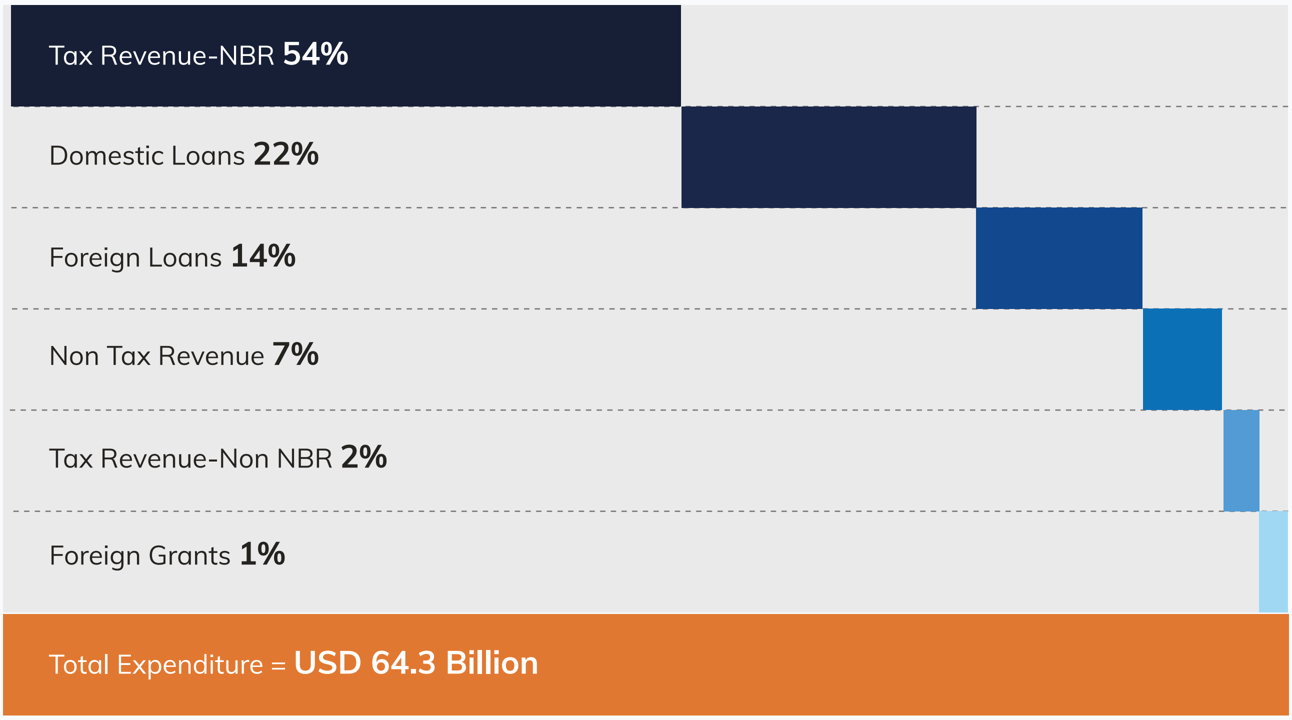
42. Quarterly Analysis of Government's Revenue Receipts, Bangladesh Bank (Jan-Mar 2022)

For the NBR Tax Revenue collection, direct taxes increased by 11.5% over the previous fiscal year, out of which 98.8% was accounted by income taxes. Travel taxes increased by 139.7% (this high percentage is due to changes in travel limitations). Additionally, indirect taxes also increased by 10%.

According to experts, higher revenue collection can be bolstered by bringing more individuals and businesses into the tax net, along with developing processes through digital transformation, in the process optimizing revenue collection.

The proposed collection strategy for the fiscal year 2023 can be summarized through the chart below.

Breakdown of Budget Finances for FY 2022-23



Source: Budget at a Glance (FY 2023), Ministry of Finance

Chapter 4

Conclusion

Conclusion

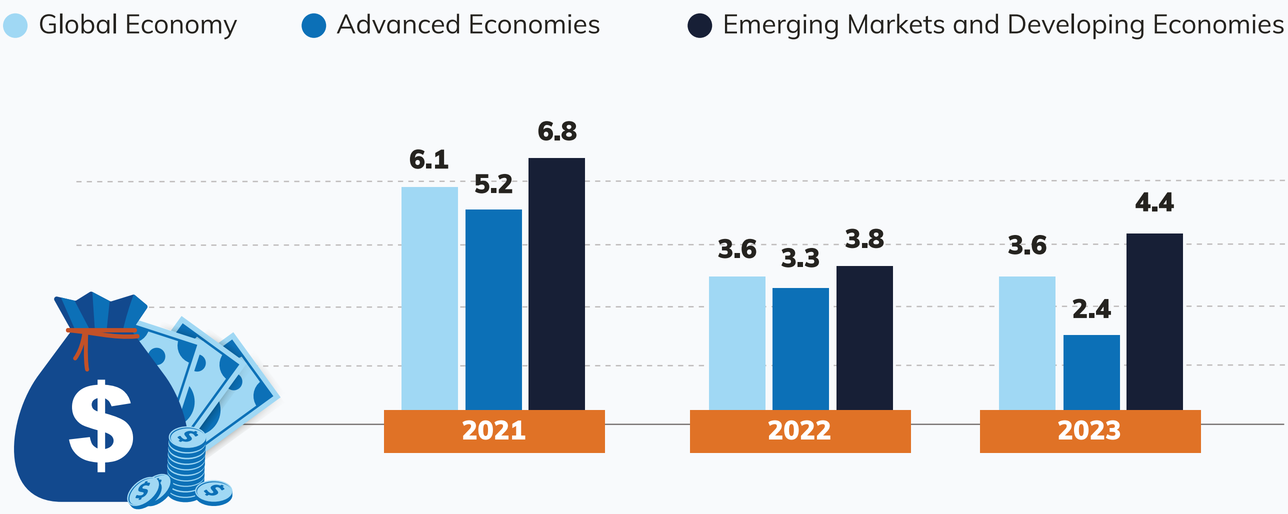
A Snippet of Global Outlook

While the global economy was just recovering from the COVID-19 pandemic, another humanitarian crisis unfolded and wreaked havoc in the world. Russia's invasion of Ukraine has sparked a supply chain nightmare, leading to a halt in the recovery of the global economy and undermining the stability throughout the region and beyond.

According to International Monetary Fund (IMF), the expected rate of global growth is 3.6% in 2022 and 2023 down from an estimated 6.1% in 2021.[43] This is lower than January's projection for 2022 and 2023 by 0.8 and 0.2 percentage points respectively before the war. Inflation projections for 2022 are 5.7% in advanced economies and 8.7% in emerging market and developing economies respectively which is 1.8 and 2.8 percent higher than the forecast in January.[43] These increases in inflation are a result of war-induced increases in commodity prices and continued supply chain difficulties. Point-to-point inflation was 5.64% in June 2021, but rose sharply to 7.56% in June 2022.

Global GDP Growth Projections

(In Percentage)



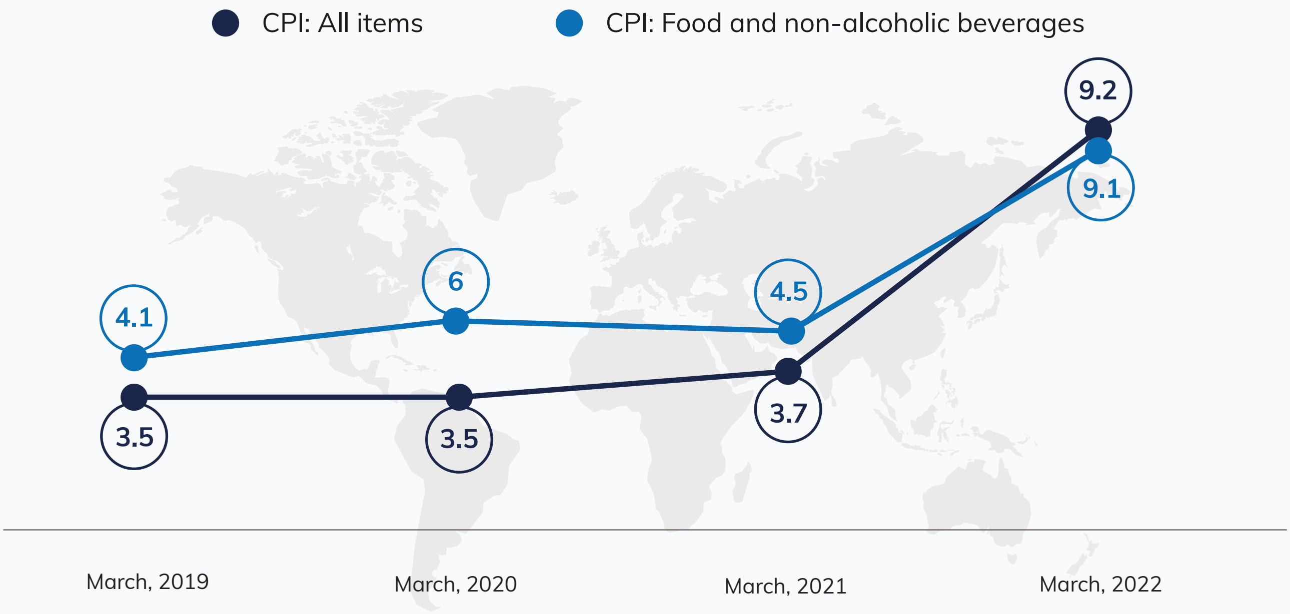
Source: *WAR SETS BACK THE GLOBAL RECOVERY*, International Monetary Fund (IMF)

43. World Economic Outlook, International Monetary Fund (IMF) (September, 2022)

China's continued struggle with lockdowns in key manufacturing hubs has also slowed the recovery of supply chains and fuelled inflation globally. Numerous key economies, the US in particular, have opted for contractionary monetary policies to curb inflation, a difficult policy trade-off when growth was particularly important globally to drive through the tail end of the pandemic. While inflation in the US touched 9.1%, the highest monthly rate since 1981, inflation in the Eurozone jumped to 8.9% in July, a record high for the currency club.[44] Due to rising commodity costs and supply-demand mismatches brought on by the COVID-19 pandemic, many countries had seen a spike in inflation even before the Russia-Ukraine conflict. In both advanced countries as well as developing nations, inflation is now expected to be higher than earlier projections.

According to International Labour Organization (ILO) STAT, the Consumer Price Index (CPI), which tracks global inflation, shows an increase in the annual rate of inflation to 9.2% in March 2022 from 7.5% in February 2022, 6.8% in January 2022, and 6.4% in December 2021.

Worldwide Annual Inflation Rate



Source: ILO estimates based on CPI data from ILOSTAT

Note: The annual, or 12-month, inflation rate, represents the percentage change of the CPI between a given month and the same month of the previous year. This rate is determined by the movements of prices of goods and services included in the CPI basket.

Production costs increased and competition decreased as a result of COVID-19-related limitations on the trans-border mobility of labor and interruptions in global supply networks. Due to the convergence of strong demand and ongoing supply difficulties, the recent price hikes brought on by the crisis in Ukraine have only served to exacerbate the already existing pricing pressure.

44. Inflation in the euro area, Eurostat (2022)

A Brave New Challenge for Bangladesh

As global economies face headwinds, national interventions are the most impactful tools to minimize the effects of the looming challenges. In the short and medium term, the depleting foreign reserve has to be made a priority and adequate steps in maintaining a healthy reserve have to be explored continuously. Bangladesh is already putting active efforts on this front. Additionally, the priority at the national level ought to tackle the rising cost of commodities and fuel, through implementing interventions that shelter the population from the economic burden and keep the economic activities undisturbed.

Disrupted supply chains as a result of the war have contributed to the increase in the cost of staple crops such as wheat, soybean, and other commodities. This poses the risk of hampering the crucial priorities by tipping the balance through higher costs. This in turn has increased the cost of our import bills and widened the trade deficit, chipping away the foreign exchange reserve and contributing to inflation.

Barriers of this magnitude, if continued might make it difficult to maintain the remaining reserves and cause an increase in the cost of everyday life. In the face of all this, the strategy to continue debt financing could have adverse effects if the balance between interest payment and meaningful output is not balanced.

For the way forward, Bangladesh is exploring new trade partnerships and bolstering the existing ones to supplement the lost trade aggravated by the war. Concerning the currency devaluation, the provision to allow US Dollar appreciate against Bangladeshi Taka has already been praised by prominent economists.

Different international financial partners such as IMF, ADB are willing to assist Bangladesh in this turbulent time and have already shown proactive approaches to that end. Different governments also view Bangladesh as a potential partner with sustained growth record. Moody's rating and Standard and Poor's credit rating also hails the country as stable and able to cater to risk in the short term. To all these partners and evaluators, Bangladesh's export growth and manufacturing landscape have not gone unnoticed. Finally, Bangladesh's 'Friendship towards all, malice towards none' strategy will definitely help in keeping a balanced supportive relationship with geo-political powers. All these factors are Bangladesh's cards to be played to tackle the ongoing challenges.

Despite the impending challenges, Bangladesh has significant growth potential in the coming decade due to a number of strategic advantages. Bangladesh's large working population and growing middle-and affluent-income class will provide the right impetus for incoming foreign investors to localize in Bangladesh. Many international investors are already planning to enter Bangladesh by investing in special economic zones. The ongoing US-China trade war will prove to be a boon as buyers and manufacturers are shifting from China to more cost competitive production destinations. Bangladesh is already experiencing the tailwind in terms of higher apparel export orders crossing the USD 50 billion mark in FY 2021-22. A depreciating currency and higher fossil fuel prices will improve export performance, while increasing remittances from the Gulf Cooperation Council (GCC) economies. Large scale investment in infrastructure will increase production efficiency, reduce lead time for distribution and improve growth prospects. All these would spearhead Bangladesh into the 24th largest economy in the world, according to the Economic Relations Department (ERD).

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