Independent Review of

iRBD

Bangladesh's Development

বাংলাদেশের উন্নয়নের স্বাধীন পর্যালোচনা

State of the Bangladesh Economy in FY2021-22

Third Reading

Dhaka: 05 June 2022

CENTRE FOR POLICY DIALOGUE

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The CPD IRBD 2022 Team alone remains responsible for the analyses, interpretations and conclusions presented in this report.

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1. Introduction

Introduction

- Bangladesh economy is facing several challenges in the backdrop of global political and economic crises.
- In the context of high inflationary pressure, deficits in trade and current account, exchange rate volatility, and pressure on foreign exchange reserve, macroeconomic management will be more challenging than ever before.
- This will require prudent fiscal and monetary policies which will meet the demand for higher subsidies and incentives in a few critical areas, enhance domestic resource mobilisation, rationalise public expenditure to avoid unnecessary expenditures without dampening domestic demand, encourage private investment and ensure social protection to the poor.

Introduction

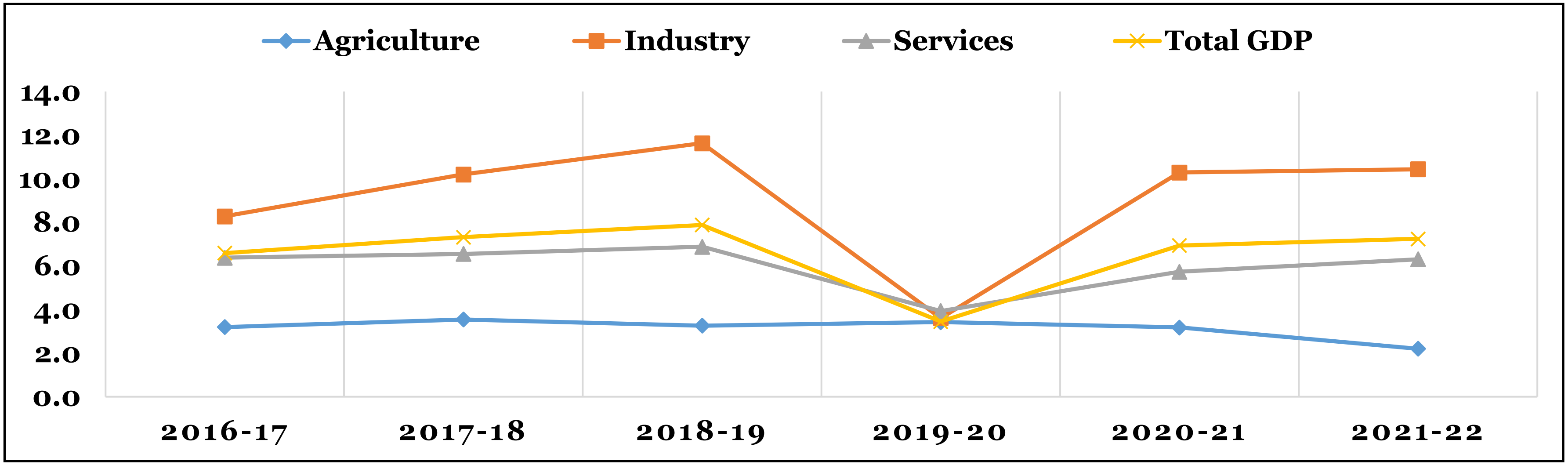
- Given that the current crisis will continue to prevail in the coming months, the Centre for Policy Dialogue (CPD) emphasises both immediate and medium-term measures to address the challenges.
- Taking cognisance of the ongoing challenges, the third reading of the Independent Review of Bangladesh's Development (IRBD) by CPD focuses on five (5) areas:
  1) Economic growth
  2) Public finance
  3) Inflation
  4) Monetary and banking sector
  5) External sector

2. Economic Growth

Economic Growth

- BBS has predicted sustained strong recovery in FY22.
  - According to the provisional estimates of BBS, GDP growth rate is expected to reach 7.2% - exactly same as the programmed figure of the budget for FY22!
  - Industry sector is expected to carry out the strong growth (10.4%)
  - Curiously, Agriculture sector to attain the lowest growth in last six years (2.2%) – even below the pandemic year of FY20.

GDP Growth (%)



Economic Growth

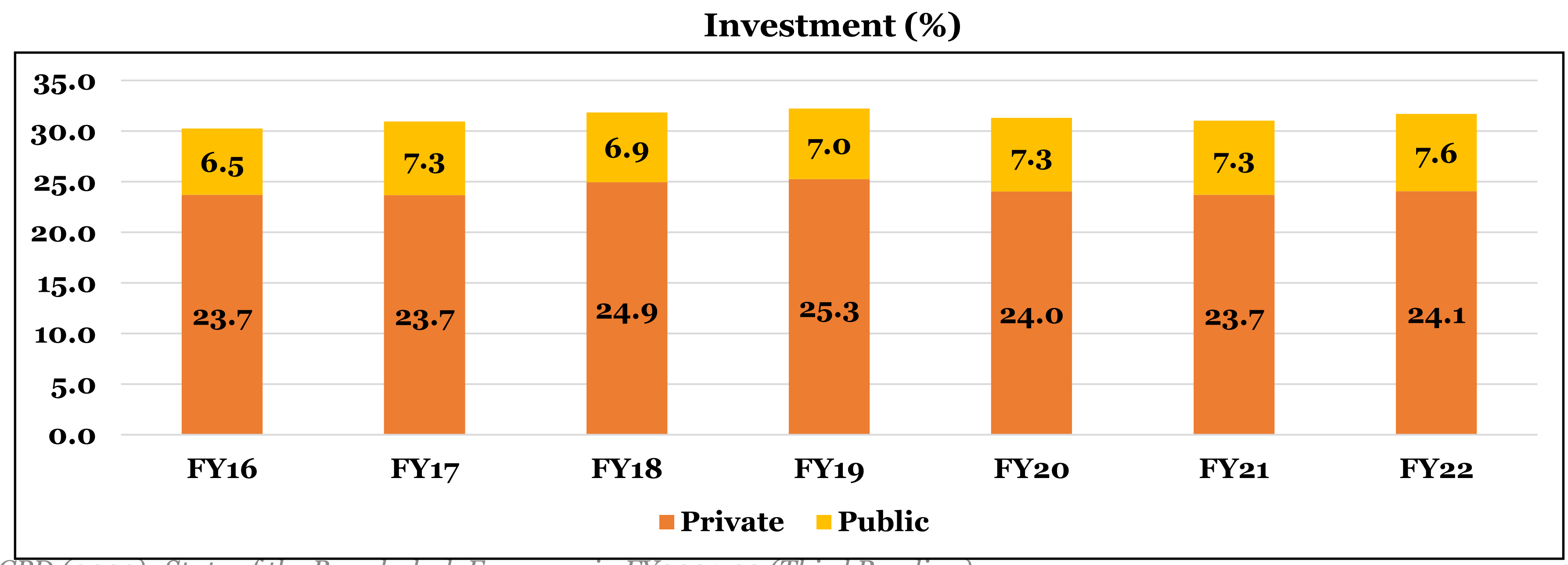
- A decomposition analysis of the provisional estimates of GDP growth indicates that Industry sector, more precisely the manufacturing sector, is expected to contribute to the attained growth.
- Within the manufacturing sector, the large industry sub-sector is expected to lead with its largest contribution in last six years (for which the GDP estimates are available according to the new base year).
- On a comparative scale, the contribution of Small, Medium and Micro Industry is expected to be weakened.

Contribution to GDP Growth (percentage points)

Sector	FY17	FY18	FY19	FY20	FY21	FY22
Agriculture	**0.4**	**0.5**	**0.4**	**0.4**	**0.4**	**0.3**
Industry	**2.6**	**3.2**	**3.8**	**1.2**	**3.5**	**3.6**
Manufacturing	1.4	2.1	2.6	0.4	2.5	2.8
a) Large Industry	*0.5*	*1.2*	*1.4*	*0.0*	*1.2*	*1.5*
b) Small, Medium and Micro Industry	*0.6*	*0.7*	*0.7*	*0.2*	*0.9*	*0.8*
c) Cottage Industry	*0.3*	*0.3*	*0.5*	*0.1*	*0.4*	*0.5*
Services	**3.3**	**3.3**	**3.5**	**2.0**	**2.9**	**3.1**
Total GDP Growth (%)	**6.6**	**7.3**	**7.9**	**3.4**	**6.9**	**7.2**

Economic Growth

- The higher GDP growth is expected to be attained with a higher Investment-GDP ratio.
- Private investment-GDP ratio is expected to increase marginally to 24.1% in FY22 compared to 23.1% in FY21 – a 0.4 percentage points rise.
- Private consumption-GDP ratio is expected to rise faster - by 1.8 percentage points – from 68.8% in FY22 from 67.0% in FY21.

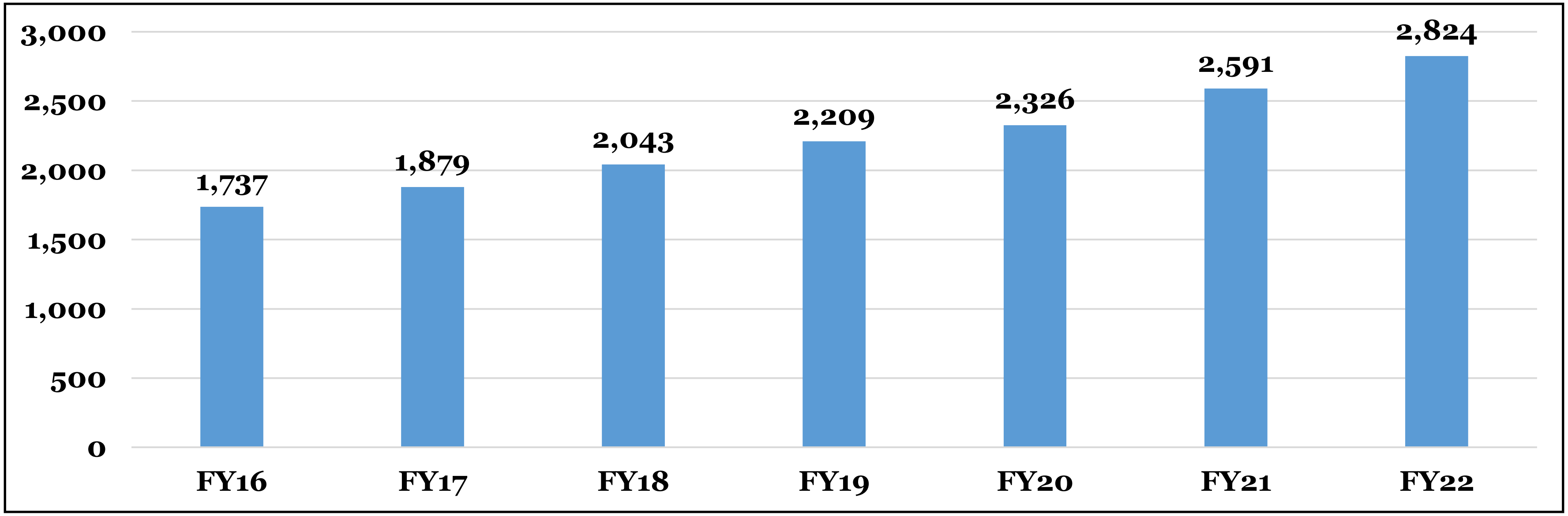


CPD (2022): State of the Bangladesh Economy in FY2021-22 (Third Reading)

Economic Growth

- ❑ Per capita income, in terms of current USD, is expected to continue rally and reach $2,824 by the end of FY22.
- ❑ However, this would mean the growth of per capita income (current USD) would decline to 9% in FY22 compared to 11.4% in FY21.

Per capita Income (current USD)

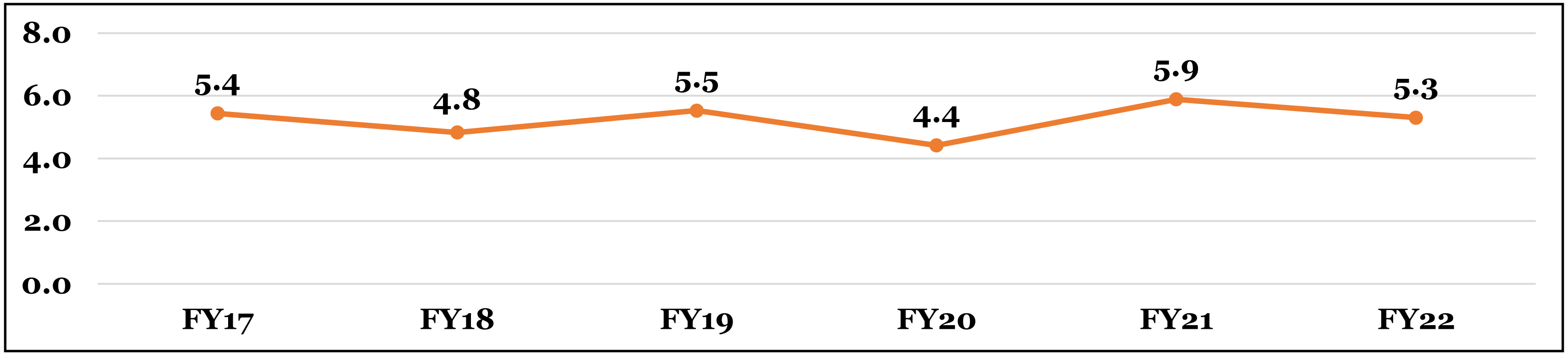


Economic Growth

- The estimates of GDP has been under scrutiny for past several years due to its apparent disjuncture with several other key macroeconomic and development correlates.
- Indeed, more than half of the provisional GDP estimates are not based on credible real time data.
- At a turbulent time for economy, in view of the unprecedented impact of the COVID-19 pandemic, lack of real time data weakens realistic estimates of GDP in a country.
- The provisional estimates of GDP in FY22 are likely to carried out with mostly data for the first six months and may have not captured the faltering macroeconomic developments in second half of FY22.
- For example, the exchange rate assumed for estimating per capita income (current USD) for FY22 is BDT 85.52 per USD.
- It is highly likely to depreciate when the final estimates will be prepared.

- The deflators used for estimating GDP figures also appear to be problematic.
- According to BBS, in FY22, growth of personal consumption expenditure price index (which may be considered as a proxy for consumer price index) increased by only 5.3% - which is lower than FY21.
- With the prevailing high level of increases in prices of essential commodities, such background numbers used for estimating GDP creates doubt regarding the credibility of the GDP figures.

Changes in personal consumption expenditure price index (%)



CPD (2022): State of the Bangladesh Economy in FY2021-22 (Third Reading)

Economic Growth

- Over the years, GDP growth rate has emerged as the centre of attention of economic policy discourse in Bangladesh and often appears to be a sacrosanct issue.
- Regrettably, GDP estimates have apparently become the sole measure of the development of the country for many key policymakers.
- CPD has always emphasised that qualitative and distributive aspects of GDP growth are no less important than mere growth figures.
- In view of the recovery of disadvantaged population groups of the country from the impact of the pandemic who are currently suffering from the significant rise of prices of essential commodities and the prevailing concerns as regards macroeconomic instability, it is high time to refocus the policy attention to protect purchasing power of the low and limited income groups, maintain macroeconomic stability and prioritise sustainable development targets beyond GDP growth.

3. Public Finance

Revenue Mobilisation

- Following the trend of first six months of FY22, it has now become obvious that the annual targets of revenue mobilisation will not be attained.
  - As per MoF data, total revenue mobilisation growth improved by a small margin (15.3% during Jul-Dec FY22 compared to 12.5% during Jul-Dec FY21).
- Tax revenue (26.7% growth against the annual target of 28.2%) collection has missed the target during the first half of FY22.
  - Data discrepancy makes the actual scenario difficult to gauge - while MoF data shows a 27.5% growth in NBR tax collection during Jul-Dec FY22, NBR data shows a 16.8% growth during the same period!

Growth scenario of components of revenue mobilisation (%)

Component	BFY21	AFY21	BFY22	AFY21 (Jul-Dec)	AFY22 (Jul-Dec)	Required Jan-Jun FY22
a. Tax revenue	**55.4**	**21.5**	**28.2**	**5.7**	**26.7**	**29.4**
a.1 NBR tax	52.8	22.1	25.1	6.6	27.5	23.3
a.2 Non-NBR tax	152.3	-0.5	170.5	-17.5	-3.2	350.9
b. Non-tax revenue	**-24.9**	**33.9**	**-26.9**	**58.5**	**-36.4**	**-19.9**
Total revenue (a+b)	**42.2**	**23.6**	**18.4**	**12.5**	**15.3**	**20.6**

Source: Calculated from MoF data

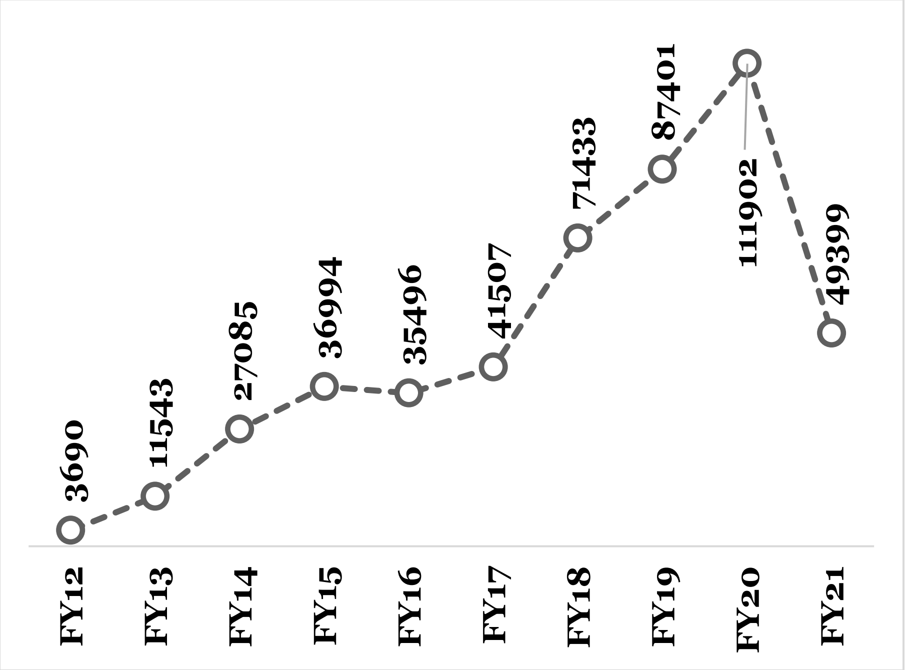
Revenue Mobilisation

- Latest data from NBR shows that, during Jul-Apr FY22, tax collected by NBR increased by 15.3% - well below the annual target of 25.1%.
- Revenue mobilisation from non-tax sources exhibits a negative required growth (as per MoF data) during the second half of FY22, despite attaining a negative growth during the first half of the FY!
  - It is thanks to two factors: i) targeted revenue collection from non-tax sources in FY22 being less than the actual collection in FY21, and ii) the massive amount of non-tax revenue mobilised during the second half of FY21 - thanks to the withdrawal of 'idle' funds from state-owned enterprises.
  - The impressive performance in terms of non-tax revenue mobilisation is unlikely to be repeated in FY22.

Revenue Shortfall

- ❑ Revenue shortfall (i.e., the discrepancy between revenue mobilisation target and actual attainment) has been a recurring phenomenon.
  - ➢ Over the recent years, failure to collect income tax at the targeted level has been the key source of revenue shortfall.
  - ➢ Low VAT collection (at domestic level) has become a rising concern.
  - ➢ The sudden decline in FY21 can be attributed to – (a) conservative target setting in view of COVID-19 and (b) the unprecedent amount of revenue generated from non-tax sources - owing to mobilisation of 'idle' funds from state owned entities.

Actual revenue shortfall (in Crore Tk.)



Source: Calculated from MoF data

- ❑ If the ongoing trend in revenue mobilisation is maintained, the revenue shortfall in FY22 is expected to reach approximately Tk. 30,000 crore.

Public Expenditure

- Regrettably, the repeated incidence of inability to utilise planned budgetary allocation continues in FY22.
- Total expenditure posted a meagre growth of 1.4% during Jul-Dec of FY22 compared to the corresponding period of FY21.
  - Largely driven by ADP expenditure (6.7%).
  - Substantially lower than the revenue mobilisation growth of 15.3%.
- ADP, as well as operational expenditure, will need to grow by 51.1% and 43.8% respectively, over the remaining six months of FY22 to reach the public expenditure targets.
- The lower expenditure growth, coupled with higher revenue generation growth, resulted in a budget surplus of Tk. 1,130 crore during the first half of FY22 – an undesirable situation in the present context.

Growth of public expenditure components (%)

Component	Target FY21	Actual FY21	Target FY22	Jul-Dec FY22	Required growth Jan-Jun FY22
Total expenditure	35.2	9.3	31.4	1.4	46.8
ADP expenditure	32.0	2.8	41.1	6.7	51.1
Non-ADP expenditure	37.0	13.2	26.3	-0.2	43.8

Source: Calculated from MoF data

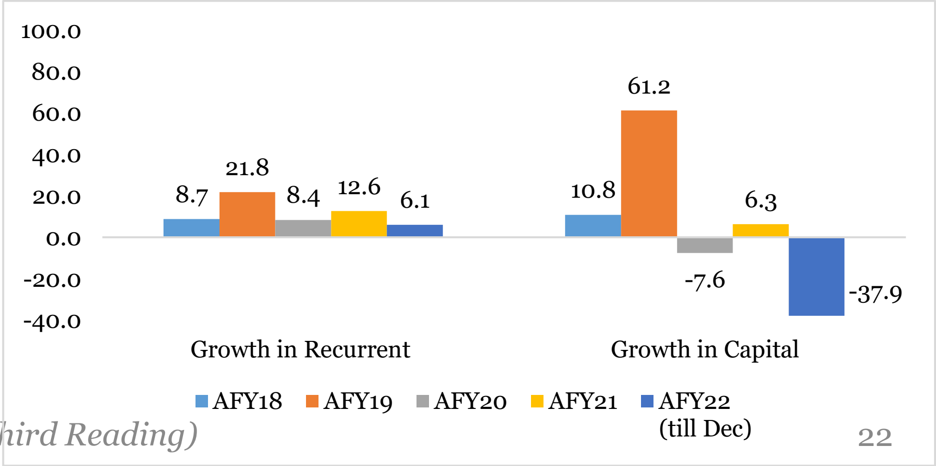
Annual Development Programme

- ADP expenditure, against allocation in FY22, is higher compared to FY21 according to IMED data.
  - 50.5% of original ADP was spent during Jul-Apr of FY22 –higher compared to FY21 (48.7%) for the corresponding period.
- ADP expenditure was primarily driven by GoB fund utilisation.
  - GoB find utilisation during the first ten months (52.8%) was the second highest in the last five years.
  - Regrettably, project aid utilisation (47.0%) was the lowest in the last five years – a worrisome development.
- Among the top 10 agencies with a cumulative share of 76% in FY22 ADP, four key ministries performed below the average during Jul-Apr FY22.
  - These include Ministry of Science and Technology (47.0%), Health Services Division (30.5%), Secondary and Higher Education Division (36.9%) and Bridges Division (29.3%).
    - The performance of Health Services Division is particularly worrisome given the pandemic scenario.

Operating Expenditure

- Operating expenditure, which comprises operating recurrent expenditure and capital expenditure, did not experience major compositional change over the last several years.
  - Over 90% of this expenditure goes to recurrent expenditure – includes allocation for wages and salaries and administrative expenses, repairs and maintenance, interest on foreign and domestic loans, current grants, social assistance benefits in cash and in-kind, employment-related social benefits in cash and incentives.
- Capital expenditure (share is less than 10%) observed more ups and downs in the recent past.
  - Capital expenditure includes acquisition of assets and land such as allocation of buildings and structures, machinery and equipment, weapons systems, goods for resale, and land.
- During FY22 (up to December) capital expenditure was 37.9% lower than the same period of the previous year – lower disbursement of funds owing to fiscal pressure??

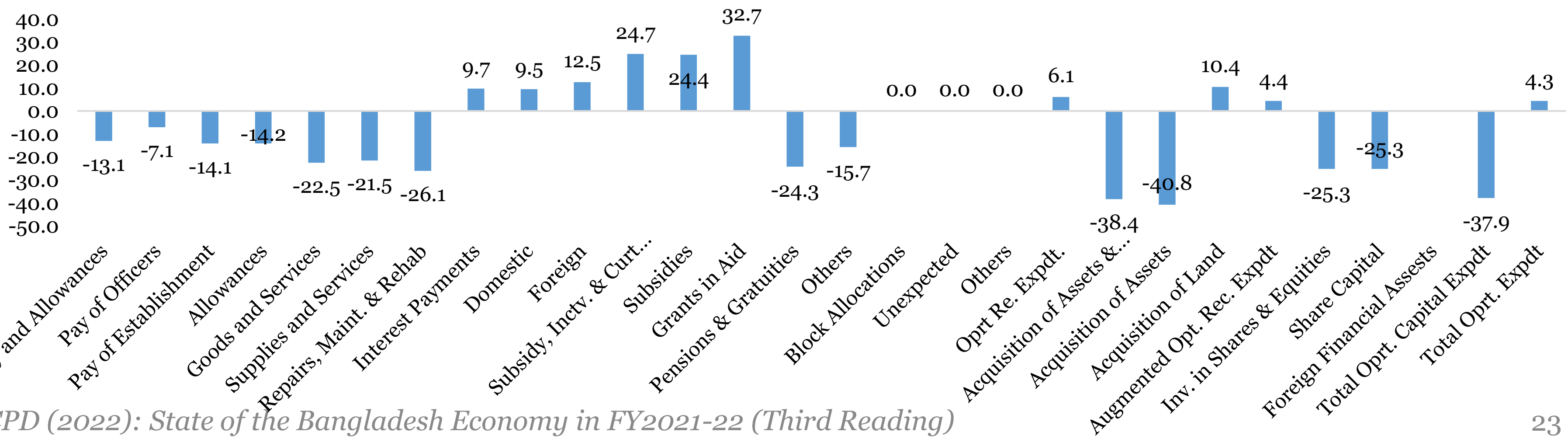
Figure: Growth in operating recurrent and capital expenditure



Operating Expenditure

- During FY22 (up to Dec), the moderate growth of total operating expenditure (4.3%) is largely driven by high growth in expenses for a few recurrent expenditures.
  - These include high growth in grants in aid (32.7%), subsidies (24.4%), domestic debt (9.5%) and foreign debt (12.5%) and interest payment (9.7%).
- A part of this rise in expenditure is related to meeting time-specific demands
  - High price of commodities and petroleum contributed to higher disbursement of subsidies against the budget allocation.
  - Easing the conditionalities in using grants for the COVID-19 pandemic caused higher growth in grants in aid.

Figure: Growth in recurrent expenditure by economic classification in FY22 (till Dec) over FY21 (till Dec)



Operating Expenditure

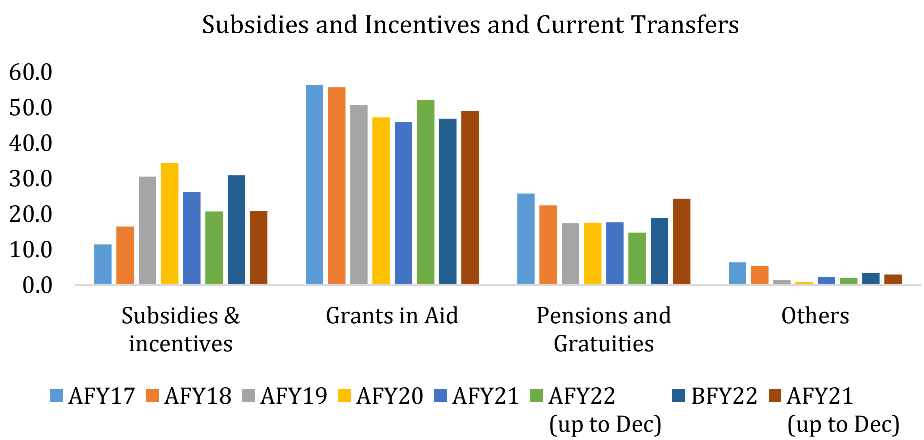
- Rise in some of the operating expenditures indicates a structural change in the expenditures owing to rising disbursement for payment of domestic and foreign debt and related interest payments.
  - Such expenditures are likely to rise in the future as well.
- It is interesting to examine the reasons behind a reduction in some of the important recurrent and capital expenditures.
  - These include recurrent expenditures such as payment of allowances, pay for officers, establishments, and supplies of goods.
  - These also include capital expenditure such as the acquisition of assets, investment shares, and share in the capital – CPD earlier suggested reducing some of the capital expenditure which have little element of 'investment' rather those are de facto 'liabilities'.

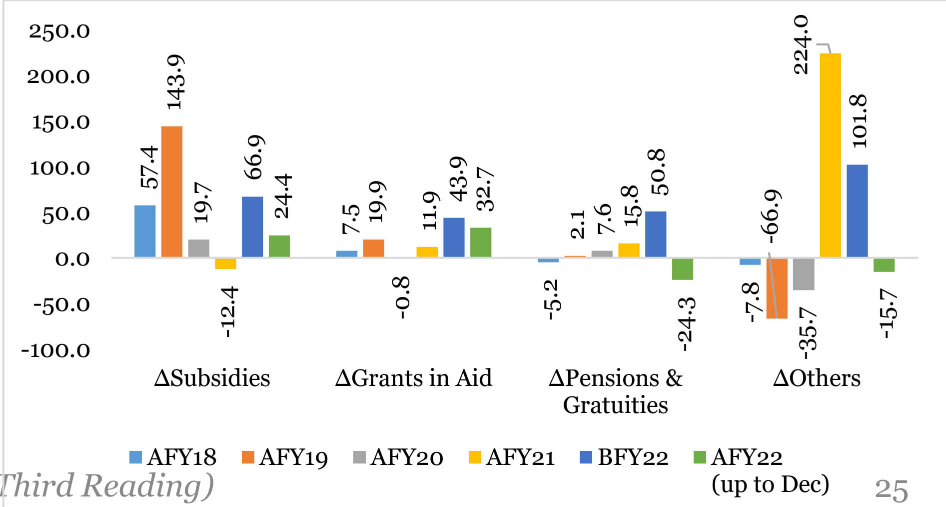
Independent Review of Bangladesh's Development (IRBD)

Operating Expenditure

- ❑ Subsidies, incentives, and current transfers related expenditure have increased by 24.7% in FY22 (till Dec) compared to the same period of the previous year.
  - ➢ This growth is largely driven by higher growth in subsidies (24.4%), and grants in aid (32.7%). Pensions & gratuities reduced by 24.3%.
  - ➢ Higher subsidy requirement (against the projected allocation in FY22 budget) for supplying energy and power as well as fertiliser at administered price is the main reason for the rise in subsidy.
- ❑ Subsidy management will be a major challenge in the upcoming fiscal year in order to stabilise the operating expenditure.

Figure: Subsidies and Incentives: Share and Y-o-Y Growth

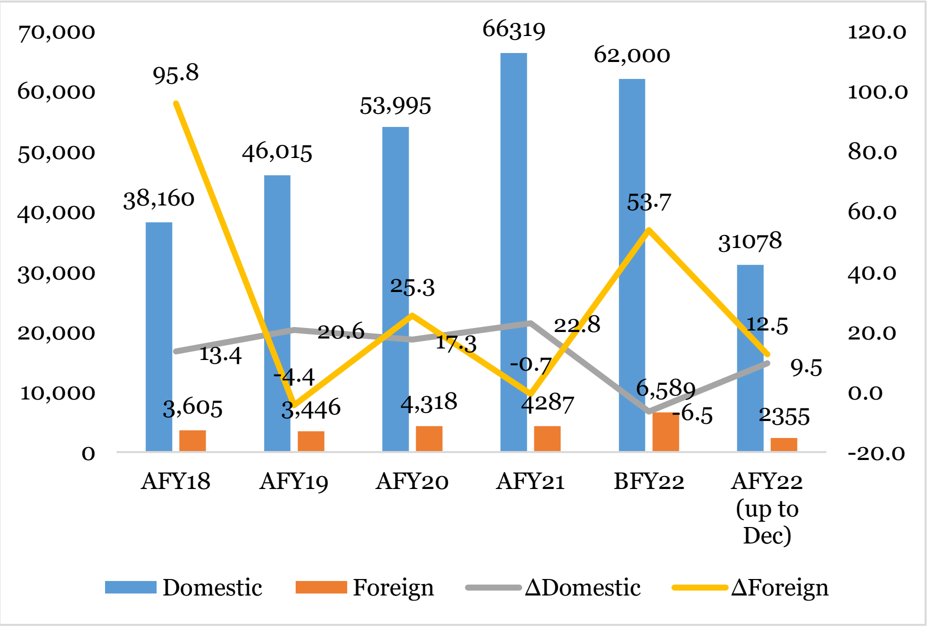




Operating Expenditure

- Interest payment comprises a major share of recurrent operating expenditure (about one-fifth in FY22 budget) - during FY22 (up to Dec) its share reached to 29%.
- Interest payment particularly against domestic debt has increasingly become a major recurrent operating expenditure - increased by 9.7% during Jul-Dec FY22.
  - Growth of interest payment of foreign loans though not consistent in nature, is likely to rise further in the coming years because of the increasing use of non-concessional loans.
- In terms of sectoral distribution, expenditure for general public services (GPS) and interest payment (IP) comprise over 50% of total operating expenditure - share has been increasing over the years.
  - In FY17, the total share of GPS and IP was almost 35% which has been increased up to 46% in BFY22.
  - Is there any revisiting of GPS expenditure required?

Figure: Interest payments: Amount & Y-O-Y Growth



Budget Deficit

- Surprisingly, as of December FY22, the overall budget balance excluding grants entered into a surplus of Tk. 1,130 crore.
  - The deficit that prevailed in the corresponding period of FY21 was Tk. 17,872 crore.
  - It is important to find out the reasons behind budget surplus during the interim period.

Table: Budget deficit (in crore Tk.)

Particulars	AFY21	BFY22	AFY21 (up to Dec)	AFY22 (up to Dec)
Overall Deficit (Including Grants)	-128424	-211191	-17872	1142
(In percent of GDP)	-3.6	-6.1	-0.51	0.03
Overall Deficit (Excluding Grants)	-130741	-214681	-17897	1130
(In percent of GDP)	-3.7	-6.2	-0.51	0.03

Deficit Financing

- The major financing source for the budget deficit is domestic borrowing - although the share has decreased in the recent years.
  - Compared to the previous year, domestic borrowing situation has improved (till December FY22, net Tk. 10,002 crore has been paid).
- Over the years, foreign borrowing has been increasing in financing the deficit.
  - Financing from foreign borrowing has increased by 30% in FY22 (up to December) compared to the corresponding periods of the previous year.
- Borrowing from banks is rising, especially for long-term debt (net) financing
  - Financing from the national savings schemes has decreased by 36% during FY22 (up to December) given surplus available in hand.

Table: Budget deficit financing

Year	Foreign Borrowing- Net	Domestic Borrowing	National Savings Schemes (Net)	Total Financing
AFY2017	11,603	55,985	51,806	67,588
AFY2018	25,621	78,815	46,289	104436
AFY2019	31,289	106845	50,357	138134
AFY2020	41,610	1,08,049	15,139	1,49,659
AFY21	45463	82088	43040	0
BFY2022	97,738	1,13,453	32,000	2,11,191
AFY21 (up to Dec'20)	6795	11077	20995	17872
AFY22 (up to Dec'21)	8852	-10002	13479	-1150

CPD (2022): State of the Bangladesh Economy in FY2021-22 (Third Reading)

Major Highlights

- Revenue shortfall may reach approximately Tk. 30,000 crore in FY22. The revenue targets for FY23 should be set taking this into cognisance.
- Operating expenditure owing to subsidies and interest payments is expected to rise in the later half of FY22 and the upward trend is likely to continue in FY23.
- The budget surplus at the end of the first half of FY22 is not at all desirable, particularly when the economy is about to turn around from the COVID-19 induced shocks and ensuring utilisation of budgetary allocations is of paramount importance.

4. High Prices and Low Wages: A Time for Struggle and Compromise

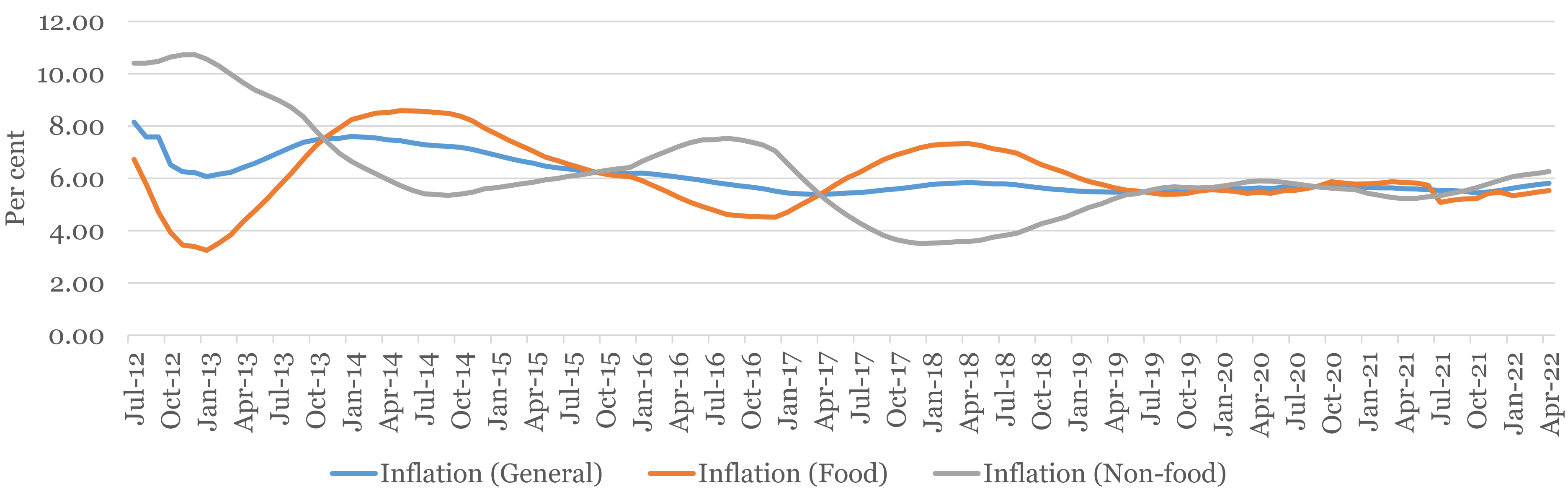
Prices of Essentials: Is the Only Way 'Up'?

- The struggle of the poor and low-income group that began with the outbreak of Covid-19 in early 2020 is now worsened by the **unabated rise in the prices of essentials**.
- These people are still grappling with their limited budgets as the pressure of price hikes continues to mount.
- This is affecting the economic recovery process as **a large section of people are still struggling to stay afloat**.
- Though the current price hike is mainly due to high import cost, domestic factors, such as market distortion by a few dominant players, are also responsible

CPI Inflation Trends Hide the Rapidly Rising Prices

- ❑ The 12-month average food and non-food inflation rates have fluctuated in a cyclical pattern over the past ten years
  - ➢ Increases in food inflation were generally accompanied by decreases in non-food inflation, so the overall general inflation rate has remained largely stable in the short-term
  - ➢ In the long-term, the overall general inflation rate has experienced a slight decline

Figure: 12-month average inflation rate from July 2012-April 2022



Source: Monthly Economic Trends, Bangladesh Bank

CPI Consumption Basket: Does it Reflect Consumption Pattern?

Table: Food expenditure as a share of income (in per cent)

	National	Rural	Urban
2000	42	48	32
2005	45	50	36
2010	53	57	45
2016	46	52	37

Table: Food expenditure as a share of consumption expenditure (in per cent)

	National	Rural	Urban
2000	55	59	45
2005	54	59	45
2010	55	59	48
2016	48	50	43

Table: Weights used for food in calculation of CPI (base year 2005)

	National	Rural	Urban
2000			
2005	56	61	47
2010	56	61	47
2016	56	61	47

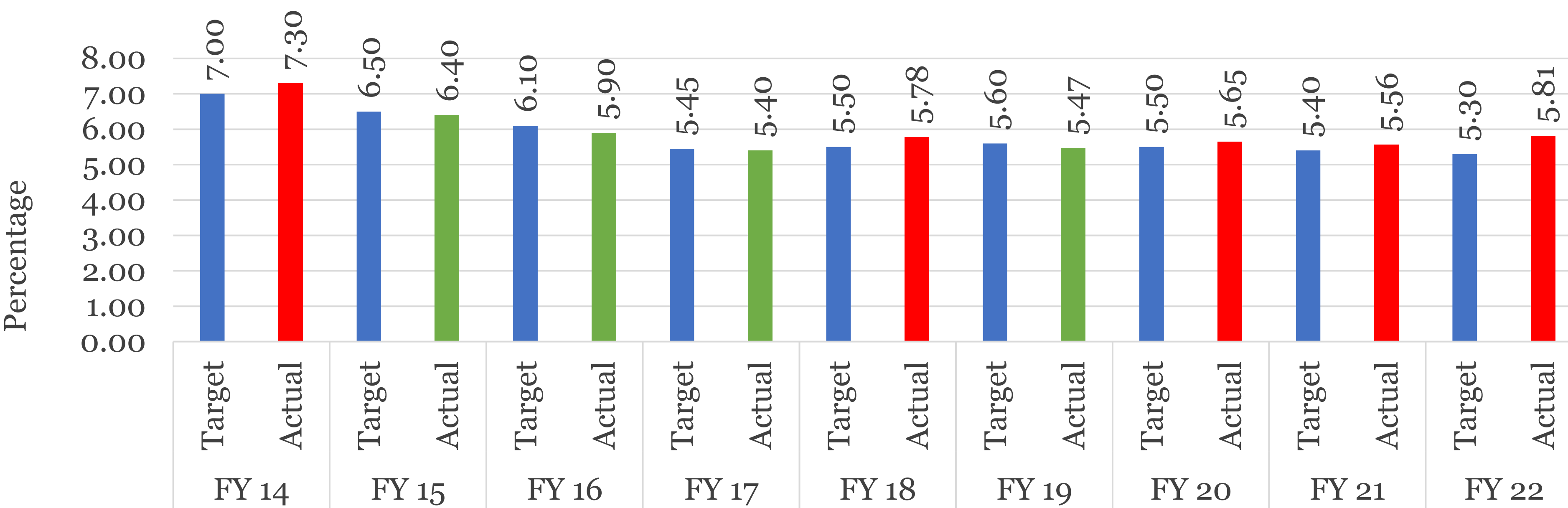
- **Engel's law** states that *as income increases, people spend a smaller proportion of their total income on food*
  - In Bangladesh, *nominal* household income increased by 7.86% per year on average and *real* household income increased by 0.16% per year on average between 2010 and 2016
    - *food expenditure as a share of income* **decreased** from **53%** in **2010** to **46%** in **2016**
    - *food expenditure as a share of total consumption expenditure* **decreased** from **55%** in **2010** to **48%** in **2016**
- However, the *weights used for food in the calculation of CPI are significantly higher than share of food expenditure in either income or consumption expenditure*
- **Thus, the consumption basket used for calculating overall general inflation was created in 2005 and does not reflect the current consumption pattern of consumers or the actual prices in the market in 2022**

Source: BBS

Inflation Targets Vs. Actual Inflation

- Inflation during the COVID-19 pandemic exceeded the monetary policy targets set in FY20, FY21 and FY22
- Due to problematic calculations of the CPI, actual inflation did not exceed inflation targets of the monetary policy by a large margin
- Prior to the pandemic years, **inflation targets were met** in FY15, FY16, FY17 and FY19, although in reality the cost of living kept rising

Figure: Inflation - Monetary Policy Targets vs. Actual



Source: Bangladesh Bank

High Incidence of Tax on Some Imported Essential Food Items

- CPD's analysis shows that **at least 29 imported essential food items currently face a high incidence of tax**
- High inflation has revealed the inherent weakness in the government's domestic resource mobilisation approach which is largely dependent on revenue collection from indirect taxes
  - The government has recently been obliged to withdraw VAT on soyabean oil in a bid to prevent the price of soyabean oil from increasing further
  - It is likely that if inflation continues at the present rate, the government may be compelled to withdraw other indirect taxes on essential items as well
- Thus, fiscal policy which is highly dependent on indirect taxes propagates economic inequality in society and forces the government to trade-off revenue generation in the face of high inflation

High Incidence of Tax on Some Imported Essential Food Items

DESCRIPTION	CD	SD	VAT	AIT	AT	RD	EXD	TTI
Fresh or chilled, other cuts of bovine meat with bone	25	20	0	5	0	3	0	58.6
Fresh or chilled boneless bovine meat, wrapped/canned up to 2.5 kg	25	20	15	5	5	3	0	89.3
Fresh or chilled other cuts of meat of sheep,with bone	25	20	0	5	0	3	0	58.6
Frozen cuts and offal of chicken, wrapped/canned up to 2.5 kg	25	20	15	5	5	3	0	89.3
Fish (ruhi, katla, pangash, karp & alike), excluding wrapped/canned up to 2.5kg	25	20	0	5	0	3	0	58.6
Hilsha fish (excluding wrapped/canned up to 2.5 kg)	25	20	15	5	5	3	0	89.3
Milk & cream of greater than 1% but less than or equal to 6% fat, not concentrated or sweetened, wrapped/canned up to 2.5 kg	25	0	15	5	5	3	0	58.6
Milk & cream in powder forms less than or equal to 1.5% fat, concentrated or sweetened, in retail packing up to 2.5kg	25	20	15	5	5	3	0	89.3
Milk and cream in solid forms of less than or equal to 1.5% fat imported by VAT registration milk and milk product	10	0	15	5	5	0	0	37.0
Milk and cream in powder excluding powder, granules or other solid from and imported VAT registered companies	10	0	15	5	5	0	0	37.0
Milk and cream in powder excluding Powder, granules or other solid from and imported VAT registered companies	10	0	15	5	5	0	0	37.0
Tomatoes, fresh	25	20	0	5	0	3	0	58.6
Onions, fresh or chilled	5	0	0	0	0	5	0	10.0

Source: Operative Tariff Schedule, National Board of Revenue

High Incidence of Tax on Some Imported Essential Food Items

DESCRIPTION	CD	SD	VAT	AIT	AT	RD	EXD	TTI
Garlic, fresh or chilled	5	0	0	2	0	0	0	7.0
Dates, fresh	0	0	0	5	5	0	0	10.0
Pepper, neither crushed nor ground	25	20	0	5	0	3	0	58.6
Cardamoms: Neither crushed or ground, excluding wrapped/canned up to 2.5 Kg	25	20	0	5	0	3	0	58.6
Seeds of Cumin: Neither crushed or ground, excluding wrapped/canned up to 2.5 Kg	25	20	0	5	0	3	0	58.6
Ginger: Neither crushed or ground, excluding wrapped/canned up to 2.5 Kg	5	0	0	5	0	0	0	10.0
Turmeric (Curcuma)	5	0	0	5	0	0	0	10.0
Other maize, excluding wrapped/canned up to 2.5 kg	0	0	0	2	0	0	0	2.0
Husked (brown) rice	15	0	0	5	5	0	0	25.8
Semi-milled or wholly milled rice	15	0	0	5	5	0	0	25.8
Maize (corn) starch	15	0	15	5	5	20	0	67.0
Crude palm oil imported by VAT registered edible oil refinery industries	10	0	15	0	5	0	0	32.0
Palm oil (excluding crude) & its fractions, not else specified, including refined palm oil	0	0	15	0	5	0	0	20.0
Refined palm kernel/Babassu oil & fractions, not chemically modified	25	0	15	5	5	0	0	55.0
Salt (other than pure sodium chloride) solution, salt boulder for crushing & salt in bulk	25	20	15	5	5	3	0	89.3
Sugars, pure (excluding glucose, etc); sugar ethers and salts, etc.	10	0	15	5	5	0	0	37.0

Source: Operative Tariff Schedule, National Board of Revenue

High Price of Internet Creating Digital Divide

- The Bangladesh Telecommunication Regulatory Commission (BTRC) declared its ***"One Country, One Rate"*** policy with the stated objectives of providing affordable broadband internet and reducing the digital divide
- Unfortunately, it appears that **most internet service providers (ISPs) are currently not abiding by the BTRC mandated prices**, especially for the internet packages of higher speeds
- Additionally, **there are wide variations in the prices of broadband internet across the country** which is completely contradictory with the "One Country, One Rate" policy of the BTRC
- The Bangladesh Competition Commission, should file lawsuits under Bangladesh Competition Law 2012, clause 15(2)(a), against all ISPs which are violating BTRC's mandate by colluding within themselves and charging abnormally high prices

Internet Service Providers Charging More Than BTRC Mandated Price for Broadband Internet

Broadband price recommendation by BTRC (One Country, One Rate)		
Speed, in Mbps	**Price per month, in BDT**	**Price per Mbps , in BDT**
5	500	100
7.5	675	90
10	800	80
15	1050	70
20	1200	60
30	1500	50
40	1600	40
60	**1800**	**30**

Average price of 60 Mbps broadband internet in Bangladesh		
City	**Price per month, in BDT**	**Price per Mbps, in BDT**
Barisal	**2,150**	**36**
Chittagong	**2,578**	**43**
Dhaka	**2,293**	**38**
Khulna	**5,333**	**89**
Mymensingh	**2,200**	**37**
Rajshahi	**2,293**	**38**
Rangpur	**5,000**	**83**
Sylhet	**2,000**	**33**
National	**2,610**	**44**

Source: BTRC and Numbeo

Price of Basic Food Items Beyond the Grasp of Ordinary Citizens

- Assuming that each person consumes the average amount of food, as indicated by the Bangladesh Urban Socioeconomic Assessment Survey 2019 conducted by the Bangladesh Bureau of Statistics (BBS), **the average monthly cost of a basket of 20 common food items (“*regular diet*”) for a household of 4 persons in Dhaka city was BDT 21,358 , as of 30 May 2022**
- Assuming that a household lives on a “*compromised diet*”, and never consumes fish, mutton, beef, or chicken, the average monthly cost of food for a household of 4 persons in Dhaka city was **BDT 8,016**, as of 30 May 2022

Average Monthly Food Expenditure in Dhaka City in May 2022, in BDT

Item	Average daily consumption per person, in kg or litre (as of 2019)	Average price in Dhaka city, in BDT (of 30 May 2022)	Average monthly expense per person	Average monthly expense per household of 4 persons
Rice (Pijam)	0.3403	53	541	2,164
Loose unprocessed flour (aata)	0.0774	47	109	437
Lentils (Musoor daal, big granules)	0.0189	108	61	243
Soyabean oil (loose)	0.0286	186	160	638
Onion (local)	0.0193	38	22	88
Garlic (local)	0.0128	100	38	153
Ginger (local)	0.0128	120	46	184
Chilli (dry chilli, local)	0.0100	195	58	233
Turmeric (local)	0.0124	235	87	349
Fish (Rui)	0.0798	300	718	2,872
Beef	0.0527	665	1,051	4,205
Mutton	0.0424	975	1,241	4,964
Chicken (broiler)	0.0723	150	325	1,301
Milk (liquid)	0.0844	81	204	816
Milk (powder, cheapest brand)	0.0142	625	267	1,067
Eggs	0.0199	205	122	489
Potato	0.0772	28	64	257
Bananas	0.0532	103	165	660
Sugar	0.0207	79	49	196
Salt	0.0104	33	10	41
Total monthly expenditure on food (“*regular diet*”)			**5,339**	**21,358**
Total monthly expenditure on food, excluding fish, beef, mutton, and chicken (“*compromised diet*”)			**2,004**	**8,016**

Source: BBS , TCB and Numbeo

High Non-food Prices Putting Huge Burden On Households

- Apart from the high price of basic food items, the high price of non-food items were putting a huge burden on households
- Crowd-sourced data shows that maintaining even a modest standard of living was becoming prohibitively expensive for households in Dhaka
- In the absence of support from the government, **out-of-pocket expenditure on health for a household of 4 persons was equivalent to BDT 2,625 per month** in 2019, at purchasing power parity
- It is apprehended that many households are at risk of falling below the poverty line due to out-of-pocket expenditure on health

Average Monthly Non-food Expenditure in Dhaka City in May 2022, in BDT

Category	Item	Average monthly expense
Rent	Apartment with 1 bedroom outside of city centre	7,274
Rent	Apartment with 1 bedroom in city centre	11,909
Rent	Apartment with 3 bedrooms outside of city centre	18,667
Rent	Apartment with 3 bedrooms in city centre	32,568
Utilities	Basic electricity, heating, cooling, water, and garbage for a 915 square foot apartment	3,789
Health	Out-of-pocket expenditure on health for a household of 4 persons	2,625
Hygiene	100 gram bar of bathing soap, 100 gram of handwashing soap, 100 gram tube of toothpaste, 1 kilogram of detergent powder, 125 gram dishwashing soap bar, 1 roll of toilet paper, 1 litre toilet cleaner, 180 mililitre bottle of shampoo, 5 regular sanitary napkins	752
Education	Preschool or kindergarten, full day, private, monthly for one child	6,818
Transportation	1 two-way trip of average length within city on each weekday (22 days per months) using public transport	1,760
Mobile phone	5 minute local voice call daily using prepaid mobile phone, and paying regular tariff without any discount or plan	192
Internet	5 Mbps broadband internet connection	500

Source: Numbeo, World Bank

The High Cost of Living in Dhaka

- **The average cost of living on a "regular" diet** for one household of 4 persons living in an apartment with one bedroom outside of city centre in Dhaka in May 2022 would be approximately **BDT 42,548**
- **The average cost of living on a "compromised" diet** for one household of 4 persons living in an apartment with one bedroom outside of city centre in Dhaka in May 2022 would be approximately **BDT 29,206**

CPD (2022): State of the Bangladesh Economy in FY2021-22 (Third Reading)

Average Cost of Living on a *"Regular"* Diet for 1 Household of 4 Persons in Dhaka in May'22

	Type of housing			
Broad expense category	**Apartment with one bedroom outside of city centre**	**Apartment with one bedroom in city centre**	**Apartment with three bedrooms outside of city centre**	**Apartment with three bedrooms in city centre**
Rent	7,274	11,909	18,667	32,568
Utilities	1,263	1,263	3,792	3,791
Food	21,358	21,358	21,358	21,358
Health	2,625	2,625	2,625	2,625
Hygiene	752	752	752	752
Education	6,818	6,818	6,818	6,818
Transportation	1,760	1,760	1,760	1,760
Mobile phone	192	192	192	192
Internet	500	500	500	500
Total	**42,548**	**47,182**	**56,469**	**70,369**

Source: BBS, TCB, Numbeo, World Bank

Average Cost of Living on a *"Compromised"* Diet for 1 Household of 4 Persons in Dhaka in May'22

	Type of housing			
Broad expense category	**Apartment with one bedroom outside of city centre**	**Apartment with one bedroom in city centre**	**Apartment with three bedrooms outside of city centre**	**Apartment with three bedrooms in city centre**
Rent	7,274	11,909	18,667	32,568
Utilities	1,263	1,263	3,792	3,791
Food	8,016	8,016	8,016	8,016
Health	2,625	2,625	2,625	2,625
Hygiene	752	752	752	752
Education	6,818	6,818	6,818	6,818
Transportation	1,760	1,760	1,760	1,760
Mobile phone	192	192	192	192
Internet	500	500	500	500
Total	**29,206**	**33,841**	**43,127**	**57,027**

Note: i) Compromised diet refers to food without fish, beef, mutton, & chicken

Source: BBS, TCB, Numbeo, World Bank

IRBD — Independent Review of Bangladesh's Development

Workers on Minimum Wage Unable to Afford Basic Food

- **Assuming a 5% annual increment of the basic salary since latest year of wage review, the minimum wage in 2022 for workers in all industries would not be sufficient for affording a "regular diet" for a household of 4 persons**
- Assuming a 5% annual increment of the basic salary since latest year of wage review, the minimum wage in 2022 for workers in the shrimp industry, fish and trawler industry, hotels and restaurants industry, soap and cosmetics industry, tailoring factories, cotton textile industries, bakery, biscuit and confectionery industry, automobile workshop industry, and leather and footwear industry would not be sufficient for affording a "compromised diet" for a household of 4 persons
- Thus, high inflation is directly threatening the food security of workers earning a minimum wage
- **Hence, it is urgent to revisit and revise the minimum wages of workers in all industries immediately**

Minimum Wage in Different Industries and Ability to Afford Average Monthly Cost of Food

Name of Industry	Job Rank	Minimum wage in 2022, assuming a 5 per cent annual increment since latest year of wage review	Ability to afford average monthly cost of food for a household of 4 persons	
			Consuming a ***compromised*** diet without fish, beef, mutton, & chicken (BDT 8,016)	Consuming a ***regular*** diet (BDT 21,358)
Shrimp	Worker	5,616	✗	✗
Shrimp	Employee	6,389	✗	✗
Fishing & Trawler Boat Industry	Worker	6,584	✗	✗
Hotels & Restaurants	Worker	4,304	✗	✗
Hotels & Restaurants	Employee	4,304	✗	✗
Soap & Cosmetics	Worker	6,496	✗	✗
Soap & Cosmetics	Employee	6,496	✗	✗
Pharmaceuticals	Worker	9,293	✓	✗
Pharmaceuticals	Employee	9,826	✓	✗
Tea Packaging	Worker	8,240	✓	✗
Tea Packaging	Employee	9,498	✓	✗

Source: Minimum Wage Board, BBS, TCB, and Numbeo

Minimum Wage in Different Industries and Ability to Afford Average Monthly Cost of Food

Name of Industry	Job Rank	Minimum wage in 2022, assuming a 5 per cent annual increment since latest year of wage review	Ability to afford average monthly cost of food for a household of 4 persons	
			Consuming a *compromised* diet without fish, beef, mutton, & chicken (BDT 8,016)	Consuming a *regular* diet (BDT 21,358)
Ship Breaking	Worker	17,724	✓	✗
Ship Breaking	Employee	16,695	✓	✗
Tannery	Worker	14,309	✓	✗
Tannery	Employee	14,309	✓	✗
Tailoring Factory	Worker	5,497	✗	✗
Cotton Textile Industries	Worker	6,486	✗	✗
Cotton Textile Industries	Employee	6,486	✗	✗
Bakery, Biscuit & Confectionery	Worker	6,716	✗	✗
Bakery, Biscuit & Confectionery	Employee	7,362	✗	✗
Automobile Workshop	Worker	6,673	✗	✗
Automobile Workshop	Employee	8,612	✓	✗

Source: Minimum Wage Board, BBS, TCB, and Numbeo

Minimum Wage in Different Industries and Ability to Afford Average Monthly Cost of Food

Name of Industry	Job Rank	Minimum wage in 2022, assuming a 5 per cent annual increment since latest year of wage review	Ability to afford average monthly cost of food for a household of 4 persons	
			Consuming a ***compromised*** diet without fish, beef, mutton, & chicken (BDT 8,016)	Consuming a ***regular*** diet (BDT 21,358)
Aluminium & Enamel	Worker	9,778	✓	✗
Aluminium & Enamel	Employee	9,778	✓	✗
Garments	Worker	8,884	✓	✗
Garments	Employee	9,312	✓	✗
Glass & Silicate	Worker	9,288	✓	✗
Glass & Silicate	Employee	9,288	✓	✗
Plastic	Worker	8,513	✓	✗
Plastic	Employee	8,513	✓	✗
Re-rolling Mills	Worker	11,255	✓	✗
Re-rolling Mills	Employee	13,018	✓	✗
Private Road Vehicles	Worker	10,766	✓	✗
Private Road Vehicles	Employee	8,513	✓	✗
Rice Mills	Worker	8,287	✓	✗
Rice Mills	Employee	8,287	✓	✗
Leather & Footwear Factory	Worker	7,459	✗	✗
Leather & Footwear Factory	Employee	8,981	✓	✗
Construction & Timber	Worker	16,830	✓	✗

Source: Minimum Wage Board, BBS, TCB, and Numbeo

Workers and Employees on Average Wage Unable to Afford the Basic Cost of Living

- **Assuming a 5% annual increment of the gross salary since 2017, the average wage in 2022 for workers and employees in all industries would not be sufficient for affording average monthly cost of living for 1 household of 4 persons living in an apartment with 1 bedroom outside city centre and consuming a "regular diet" in Dhaka**
- Assuming a 5% annual increment of the gross salary since 2017, the average wage in 2022 for workers and employees involved in most forms of economic activities would not be sufficient for affording average monthly cost of living for 1 household of 4 persons living in an apartment with 1 bedroom outside city centre and consuming a "compromised diet" in Dhaka
- **Thus, it is clear that a 5% increment hardly makes any difference to workers and employees, given that most prices are increasing in double digit growth rates**

Average Monthly Earnings of Workers and Ability to Afford Average Monthly Cost of Living

		Ability to afford average monthly cost of living for a household of 4 persons in an apartment with 1 bedroom outside city centre	
Economic activity	**Average monthly earnings of workers in 2022, assuming 5% annual increment of gross salary from 2017**	**Consuming a *compromised* diet without fish, beef, mutton, & chicken (BDT 29,206)**	**Consuming a *regular* diet (BDT 42,548)**
Agriculture; forestry and fishing	9,804	✗	✗
Mining and quarrying	11,440	✗	✗
Manufacturing	14,407	✗	✗
Electricity; gas, steam and air conditioning supply	31,889	✓	✗
Water supply; sewerage, waste management and remediation activities	18,895	✗	✗
Construction	11,582	✗	✗
Wholesale and retail trade; repair of motor vehicles and motorcycles	14,405	✗	✗
Transportation and storage	14,154	✗	✗
Accommodation and food service activities	13,106	✗	✗
Information and communication	25,845	✗	✗
Financial and insurance activities	35,018	✓	✗
Real estate activities	29,250	✓	✗

Source: BBS, TCB, Numbeo, World Bank

Independent Review of Bangladesh's Development (IRBD)

Average Monthly Earnings of Workers and Ability to Afford Average Monthly Cost of Living

Economic activity	Average monthly earnings of workers in 2022, assuming 5% annual increment of gross salary from 2017	Ability to afford average monthly cost of living for a household of 4 persons in an apartment with 1 bedroom outside city centre: Consuming a ***compromised*** diet without fish, beef, mutton, & chicken (BDT 29,206)	Ability to afford average monthly cost of living for a household of 4 persons in an apartment with 1 bedroom outside city centre: Consuming a ***regular*** diet (BDT 42,548)
Professional, scientific & technical activities	26,657	✗	✗
Administrative & support service activities	19,398	✗	✗
Public administration & defence; compulsory social security	28,389	✗	✗
Education	23,785	✗	✗
Human health & social work activities	25,486	✗	✗
Arts, entertainment & recreation	20,010	✗	✗
Other service activities	15,853	✗	✗
Activities of households as employers; undifferentiated goods- & services-producing activities of households for own use	9,799	✗	✗
Activities of extraterritorial organisations & bodies	27,054	✗	✗
Not elsewhere classified	11,200	✗	✗
Total	**15,075**	✗	✗

Source: BBS, TCB, Numbeo, World Bank

Those Who Are Unaffected by Inflation

- ❑ While workers on minimum wages are unable to afford food, and workers on average wages are unable to afford high cost of living, **the number of super-rich individuals and corporations is on the rise in Bangladesh**.
- ❑ The number of bank accounts worth greater than BDT 50 crore, and the amount of money held in such accounts, has increased substantially, indicating that *capitalists and their corporations have been largely unaffected by rising prices*.

Figure: Number of accounts worth greater than BDT 50 crore

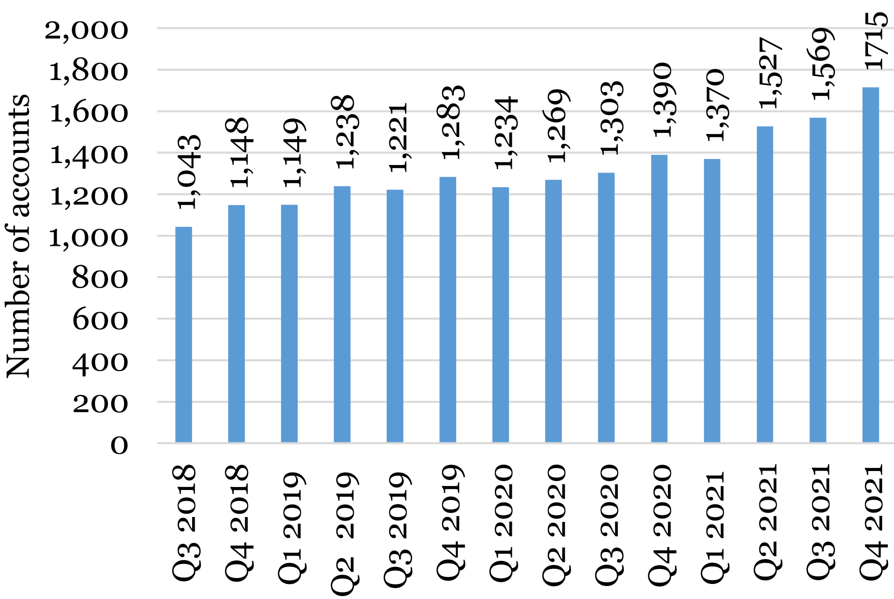
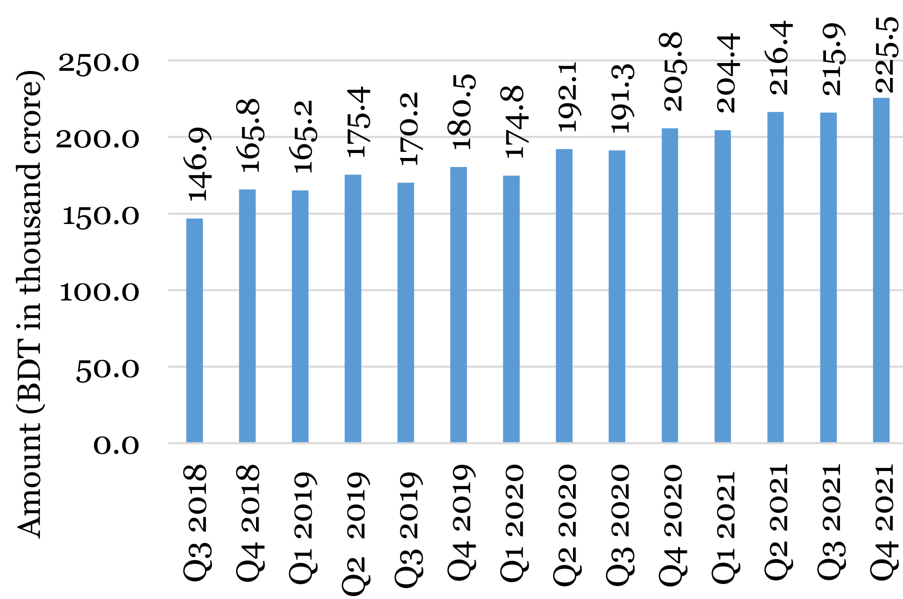


Figure: Amount of money held in accounts worth greater than BDT 50 crore



Source: Bangladesh Bank

Policy Recommendations

- **A new consumption basket should be formulated for calculating CPI inflation**, based on rigorous research as regards consumer behaviour and expenditure patterns. All targets, projections, and plans in the monetary policy and the 8th Five Year Plan should be revised in accordance with this new consumption basket for CPI and new base year for inflation.
- **The National Board of Revenue (NBR) should immediately consider removing the advance income tax (AIT), advance tax (AT) and regulatory duty (RD) on all imported essential food items.**
- The role of the Bangladesh Competition Commission needs to be strengthened, particularly in the case of the essential consumer goods market.
  - The Commission should develop a database, regularly monitor the dominant market players' operations, examine the market control and manipulation (if any), and take proper measures.
- **The Bangladesh Competition Commission should adopt a strong stance against cartels and a zero tolerance policy towards collusive practices.**
- The Competition Act 2012 should be revised to directly address monopolies and include specific anti-trust clauses, along with concrete penalties for violators.
- Efficient market management through close monitoring and supervision will be critical to keep the commodity prices under control.

Policy Recommendations

- **The Minimum Wage Board should consider increasing the minimum wages in all industries** so that workers earning minimum wages may at least afford basic food
- **Private sector corporations should consider a higher salary increment in 2022**, given that a 5% increment of salary in the face of double digit price hikes is compelling workers to seriously compromise their standard of living
- The volume of sale of essential commodities through the open market system (OMS) should be increased
- **Distribution of these commodities must be managed effectively and without any corruption**, so that the eligible people have access to these items at low prices
- The government should provide direct cash support to the poor, enhance social protection for low-income families, and extend stimulus to the small businesses for their survival during difficult times

Policy Recommendations

- The government should prepare for maintaining adequate food stock not only through better agricultural production, but also through importing food.
- There is a need for actual demand estimation of rice and other food items in the country.
- During a crisis, food-exporting countries would not export food without meeting their domestic demands first. If they decided to export, the prices would be exorbitant. Therefore, planning the production and import of food should be done early on.
- **Inflationary pressure will hamper a sustainable and inclusive pandemic recovery, since the real purchasing power of many people will decline, causing further inequality.**

5. Monetary and Banking Sector

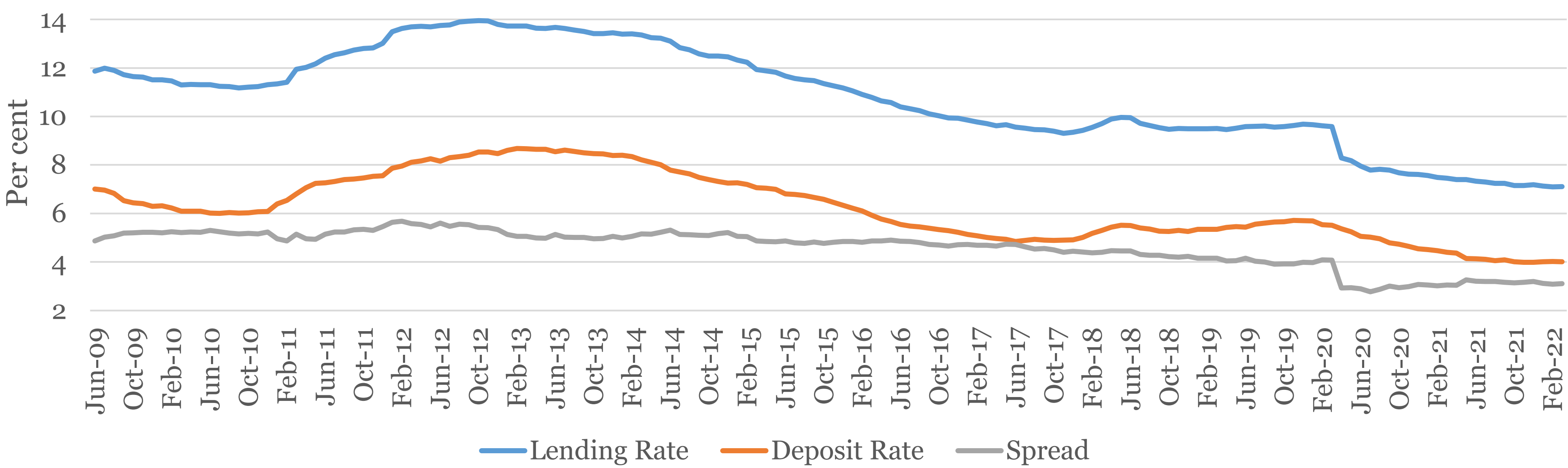
Introduction

- *A strong financial sector is key to higher economic growth*. The banking sector, which is the dominant sub-sector within the financial sector, has traditionally been contributing to Bangladesh's private investment, trade, commerce, and employment generation.
- However, due to lack of reforms, the banking sector is facing severe challenges, including **high loan defaults**, **low profitability**, and **poor management**.
- The COVID-19 pandemic is apprehended to intensify these pre-existing challenges, including higher non-performing loans (NPLs)
- However, due to longstanding moratorium on loan classification during the pandemic, the currently available data may be under-estimating the actual level of NPL in the banking sector.
- Since the highest share of COVID-19 related liquidity support has been offered to large industries, there are apprehensions that there could be ingenuine borrowers who were not actually affected by the pandemic
- This section presents the performance of the banking sector through a set of banking and monetary indicators.

Interest Rate Spread

- Excess liquidity in the banking system has led to a fall in the interest rates, which were already quite low even prior to 2020.
- During the pandemic, the weighted average lending rate in all scheduled banks has come down sharply and the weighted average borrowing rate in all scheduled banks has also declined.
- As a result, the interest rate spread has come down, adding to the woes of the commercial banks.

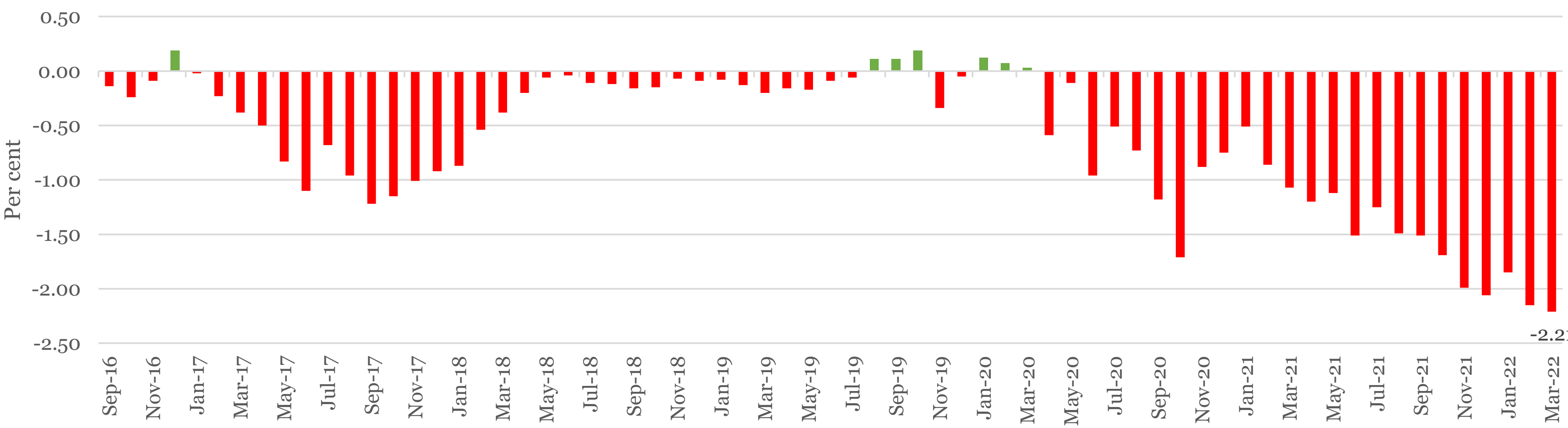
Interest rate spread



Negative Real Interest Rate on Bank Deposits

- Excess liquidity in the banking system has led to a fall in the interest rates, which were already quite low even prior to 2020.
- The *real deposit rate*, calculated as the weighted average of the monthly deposit rate of all scheduled banks adjusted with the point-to-point monthly consumer price index inflation, fell from 0.03 per cent in March 2020 to -2.21 per cent in March 2022
- The **negative real interest rate on bank deposits** means that value of the savings of ordinary people was being depleted away during the pandemic and during high inflation—a time when they needed to utilise their savings the most.

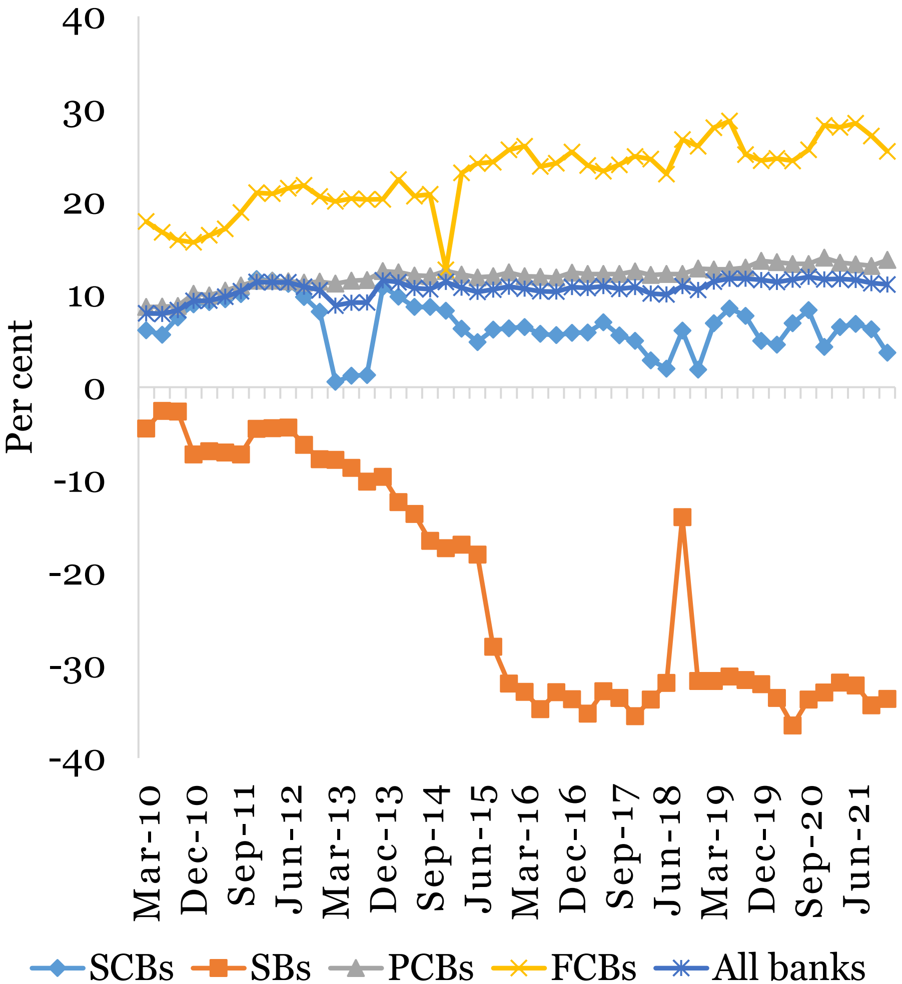
Figure: Real deposit rate in banks (in per cent)



Capital Inadequacy of Banks

- Bangladesh Bank's Guidelines on Risk Based Capital Adequacy state that banks must maintain a minimum total capital ratio of 10% (or minimum total capital plus capital conservation buffer of 12.5%) by 2019, in line with BASEL III.
  - However, the SCBs have failed to maintain minimum requirements of capital adequacy.
  - On the other hand, the SBs have remained critically under-capitalised.
- **Without reducing NPLs, capital adequacy cannot be improved** since higher levels of NPLs lead to increased provisioning requirements, which results in capital shortfall.

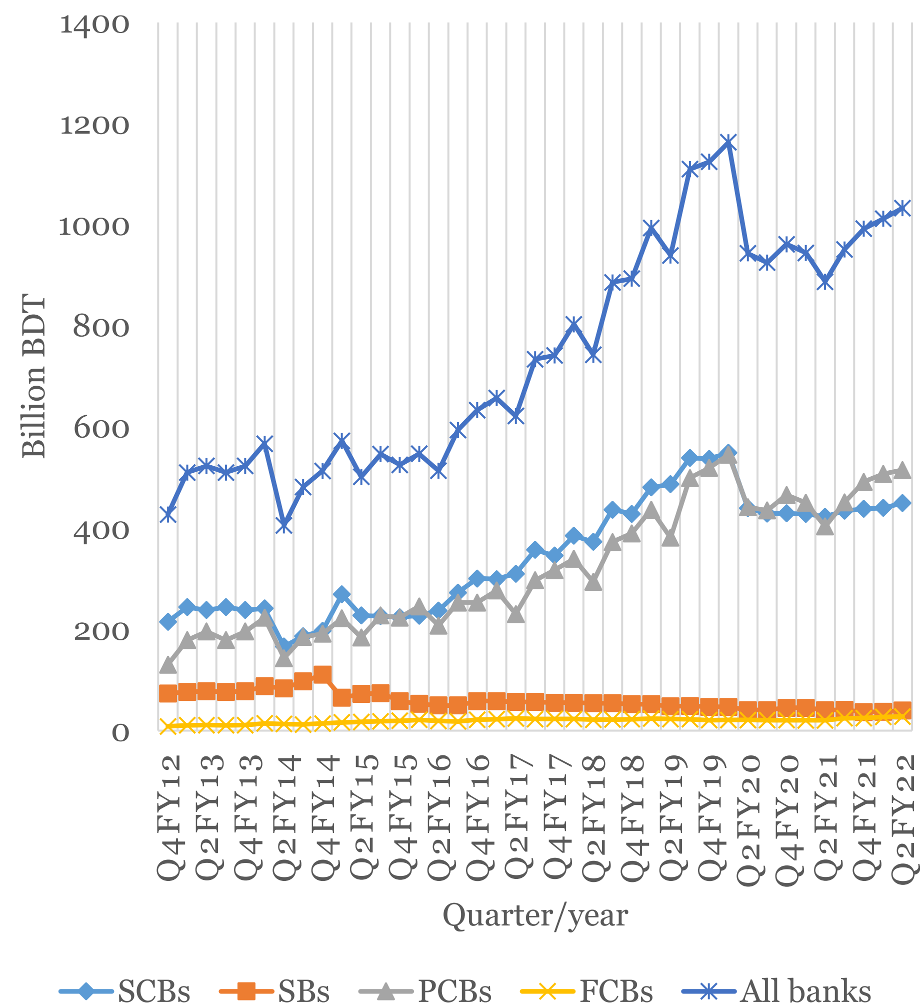
Figure: Capital to risk weighted asset ratios (in %)



Non-performing Loans (NPLs)

- Due to the longstanding moratorium on loan classification, the current level of non-performing loans (NPLs) in the banking sector is hardly indicative of the reality
- Nevertheless, it can be seen that the total volume of NPLs started rising from the third quarter of FY21
- It is apprehended that the actual volume of NPL in the banking sector is far greater than shown by the official numbers
- It is anticipated that NPL will rise further in the coming days, as loans under COVID-19 liquidity support packages were not provided in a transparent or accountable manner

Figure: Total classified loans (in billion BDT)



Huge Opportunity Cost of NPLs

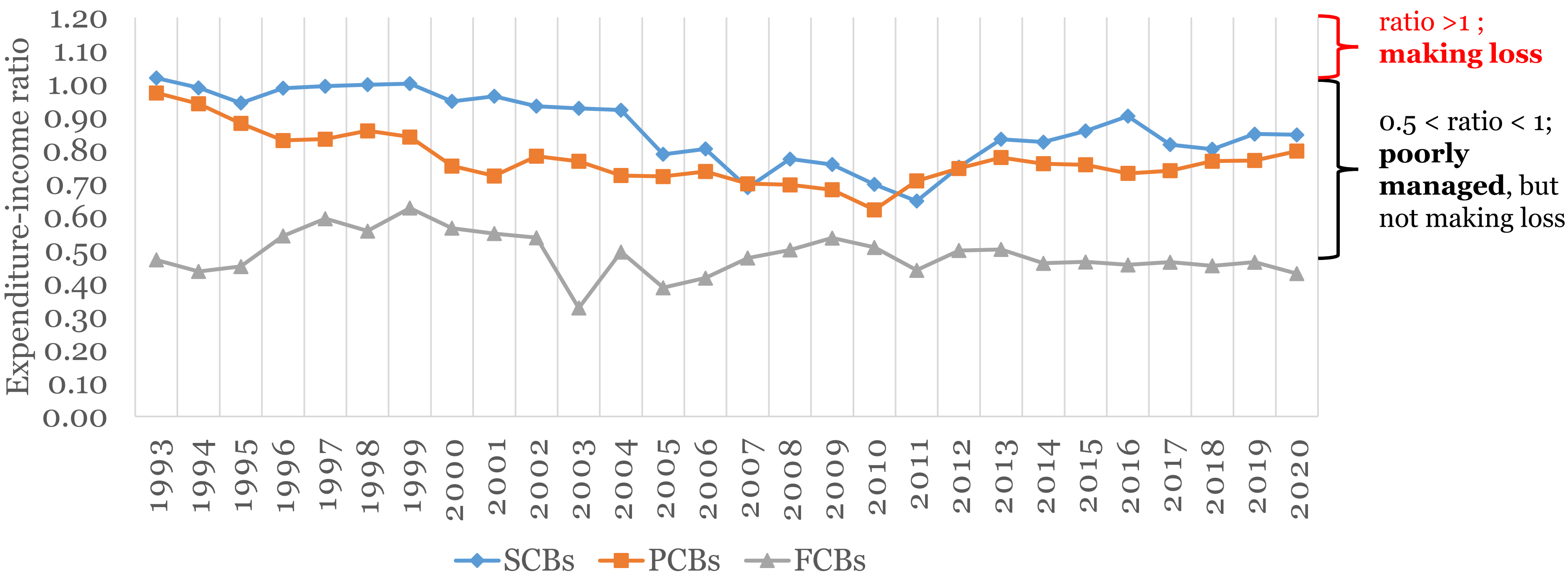
- Total volume of NPLs in the banking sector pandemic in the second quarter of FY22 was **BDT 1,03,274 crores**

What can Bangladesh do with **BDT 1,03,274 crores**?	➔	**Build 3 road bridges** like the **Padma Multipurpose Bridge** (Assuming cost is BDT 30,193 crores)
	➔	**Build 2 railway bridges** like the **Padma Bridge Rail Link** (Assuming cost is BDT 39,247 crores)
	➔	**Build 2 powerplants** like **Matarbari** 2x600 MW Ultra-Super Critical Coal-Fired Power Project (Assuming cost is BDT 35,984 crores)
	➔	**Build 4 metro rails** like the **Dhaka Mass Rapid Transit Development** Project (Metro Rail) (Assuming cost is BDT 23,490 crores)
	➔	**Build 5 railway lines** like the Single Line Dual Gauge Track from **Dohazari-Ramu-Cox's Bazar and from Ramu to Ghundum** (Assuming cost is BDT 18,034 crores)

Management of Commercial Banks

- During the years 1993 to 2019, the average expenditure-income ratio was 0.87 in SCBs and 0.77 in PCBs.
- This reveals poor management effectiveness of both SCBs and PCBs, even prior to the start of the pandemic.

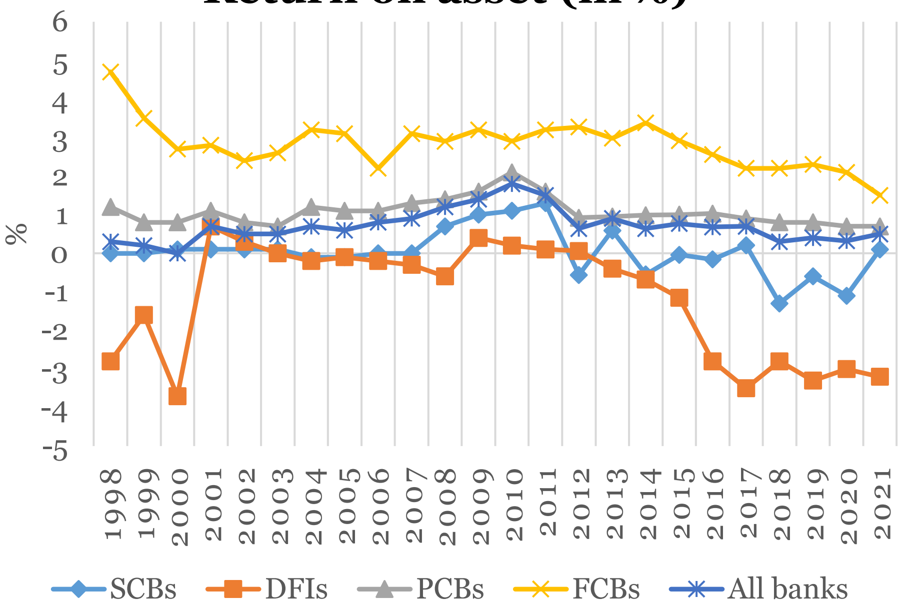
Figure: Expenditure-Income ratio (in %)



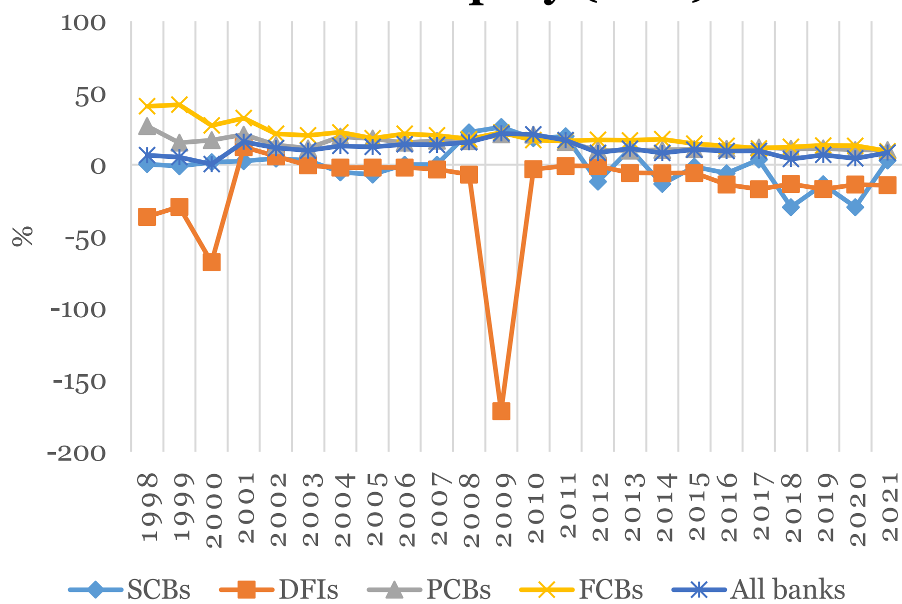
Profitability of Banks During the Pandemic

- PCBs experienced a **decline in profitability**, as their return on asset (ROA) fell from 0.80% in 2019 to 0.70% in 2021, and their return on equity (ROE) fell from 11.2% in 2019 to 10.1% in 2021.
- DFIs dug themselves into a deeper hole after the pandemic, as their return on asset and return on equity plummeted in 2020.
- FCBs saw their profitability fall in 2021, as both their ROA and ROE fell sharply.
- However, SCBs actually managed to improve their profitability in 2021.

Return on asset (in %)



Return on equity (in %)

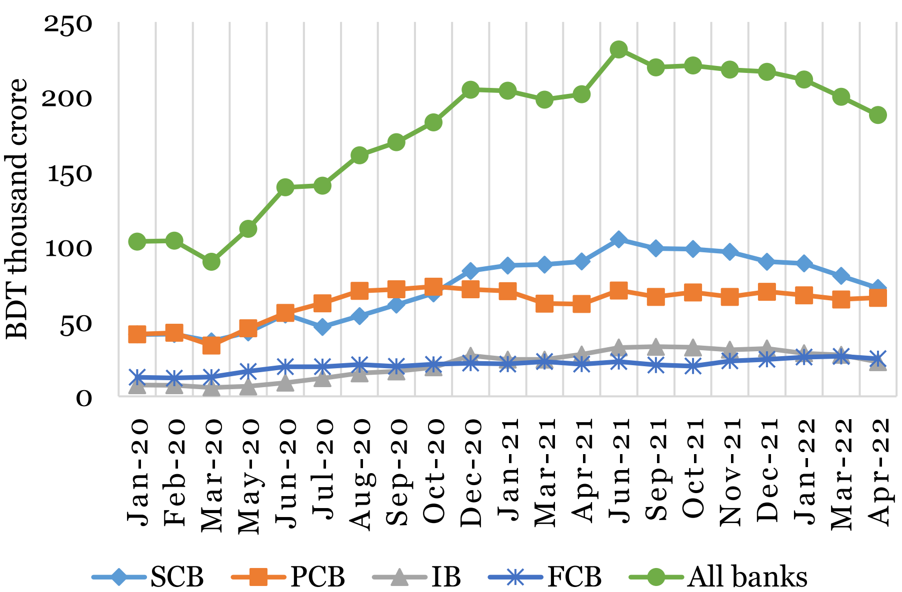


CPD (2022): State of the Bangladesh Economy in FY2021-22 (Third Reading)

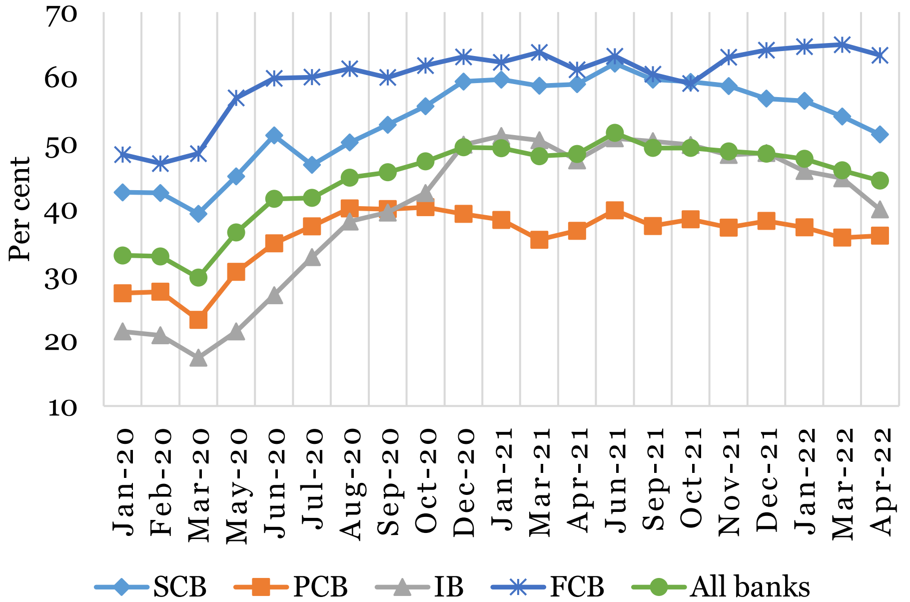
Excess Liquidity

- **Data from Bangladesh Bank shows that excess liquidity in the banking sector has nearly doubled from BDT 103 thousand crore in January 2020 to BDT 188 thousand crore in April 2022.**
- During the same period, excess liquidity has nearly doubled in SCBs and nearly tripled in IBs.
- Excess liquid assets comprised of 44% of the total liquid assets of the banking sector in April 2022.

Excess liquidity (BDT in thousand crore)



Excess liquidity (as % of total liquid assets)



Do Banks Perceive Risks on the Horizon?

- Banks have also increased their holdings of unencumbered approved securities, which are zero risk rated assets issued or guaranteed by the government
- Holdings of unencumbered approved securities of all banks increased from BDT 211 thousand crore, or 67% of total liquid assets, in January 2020, to BDT 312 thousand crore, or 74% of total liquid assets, in April 2022
- The decision of commercial banks to hold excess liquidity in the form of unencumbered approved securities instead of funds for lending shows that commercial **banks perceive that the yields on risk free unencumbered approved securities are better than the risk adjusted returns on interest-bearing loans that come with default risk.**
- *This indicates that commercial banks are hesitant to lend, as they probably that believe that economic activity is yet to pick up and so their loans may have a high probability of turning bad.*

Figure: Unencumbered approved securities (BDT in thousand crore)

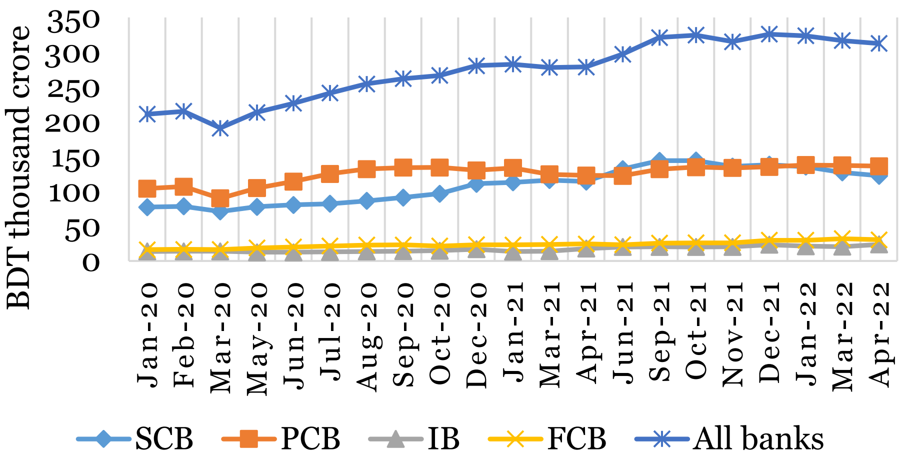
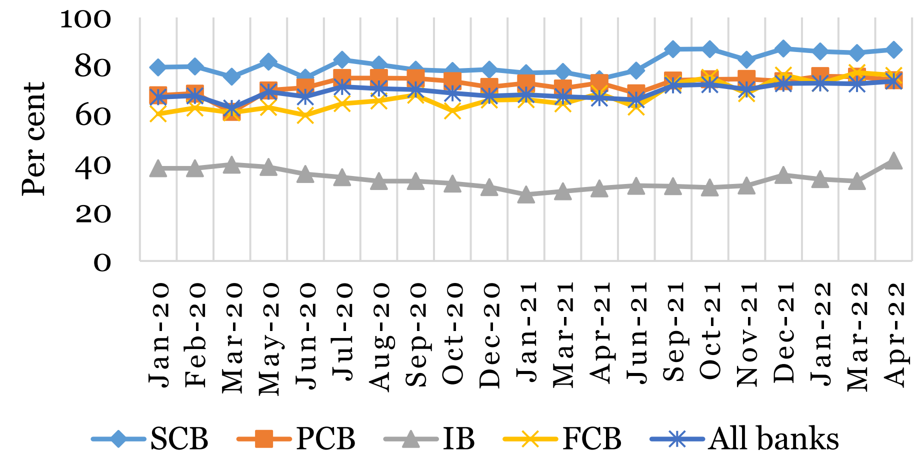
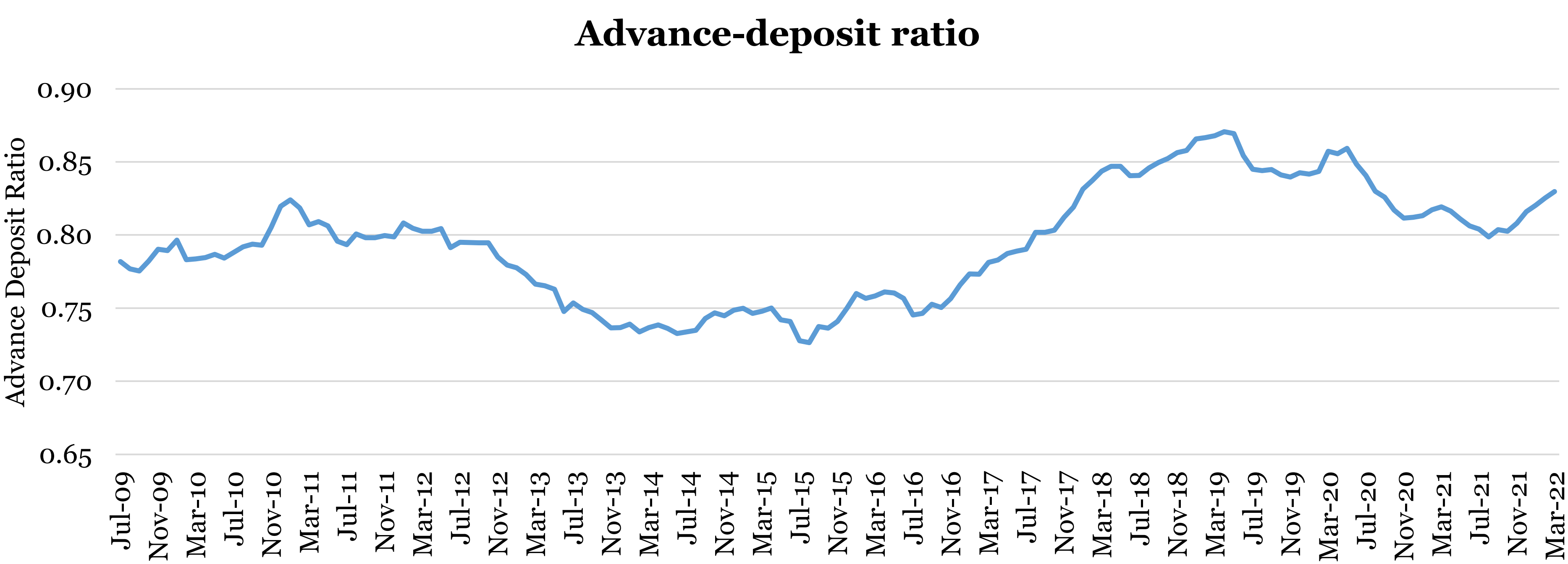


Figure: Unencumbered approved securities as a share of total liquid assets (in per cent)



Advance-deposit Ratio

- Excess liquidity is also a sign that the demand for loans is low, which is likely since the real economy is still experiencing the repercussions of the COVID-19 shock.
- The advance-deposit ratio of all banks fell to a low of 0.80 in August 2021.
- However, since then the advance-deposit ratio has increased slightly, indicating that **economic activity may be slowly picking up.**



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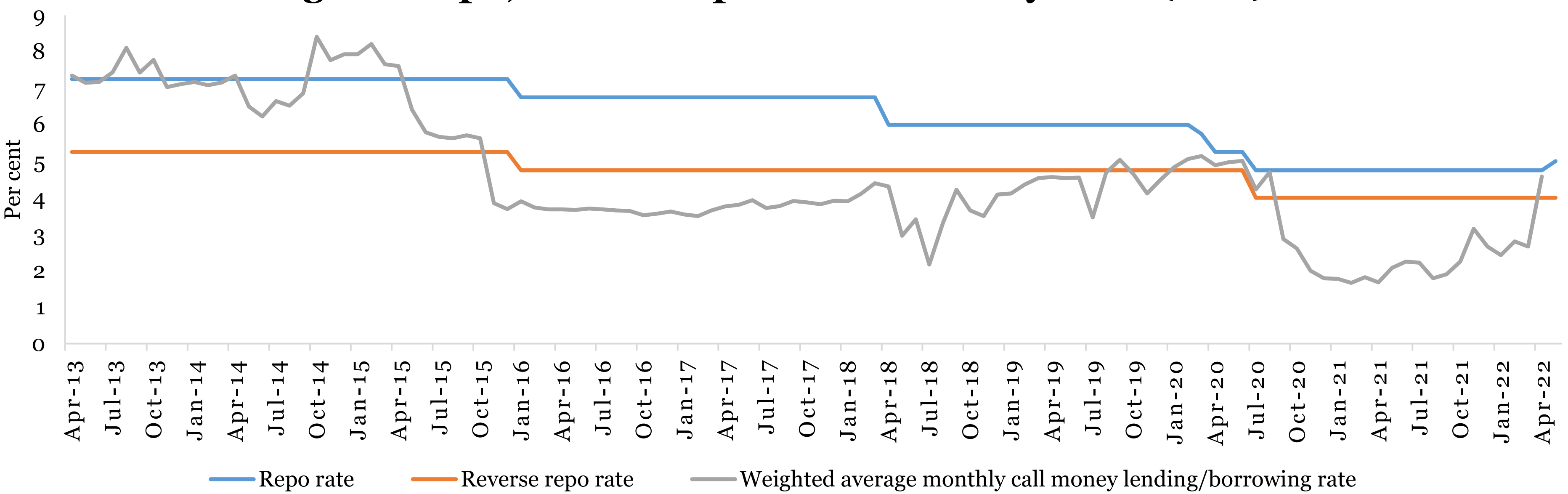
Increasing Trend of Call Money Rates

- The monthly average **call money market** borrowing and lending rates have both increased sharply from 2.66% in March 2022 to **4.58% in April 2022**.
- The increasing trend of call money rates implies that the demand for cash, particularly by under-capitalised banks, has been high.
- On 29 May 2022, the central bank the repo rate from 4.75% to 5%, whereas the **reverse repo rate remained at 4%**.
- Since the weighted average monthly call money rate in April 2022 exceeded the reverse repo rate, the effectiveness of monetary policy may be compromised.

Figure: Repo, reverse repo and call money rates (in %)



Excess Reserves

- Data from Bangladesh Bank shows that in 2020, **excess reserves of all banks increased** from BDT 6.74 thousand crore, or 2.15% of total liquid assets, in January 2020, to BDT 20.39 thousand crore, or **4.82% of total liquid assets, in April 2022**.
- *Since excess reserves represent un-invested cash, holding excess reserves is costly for banks.*
- However, excess reserves have been declining starting from June 2021 onwards.

Figure: Excess reserve (un-invested cash) (BDT in thousand crore)

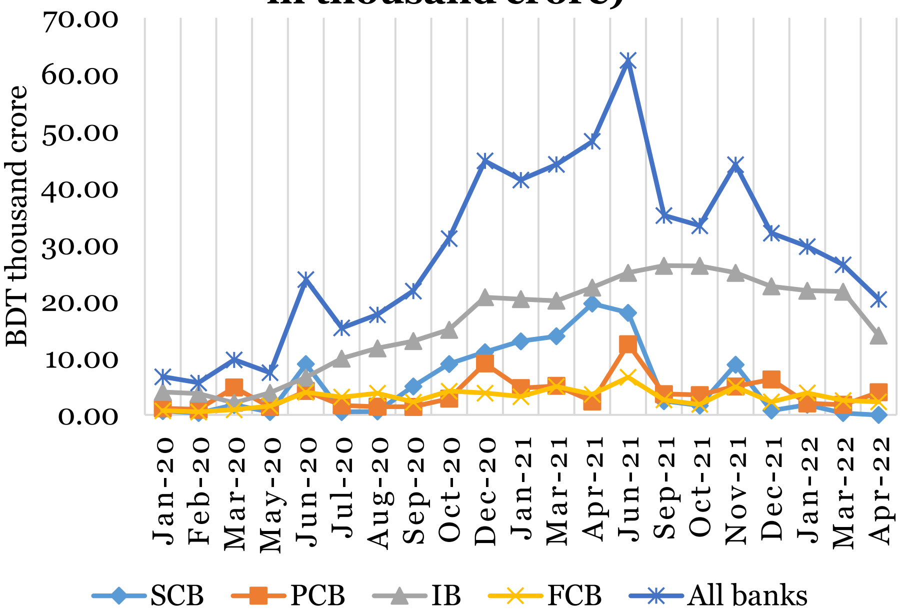
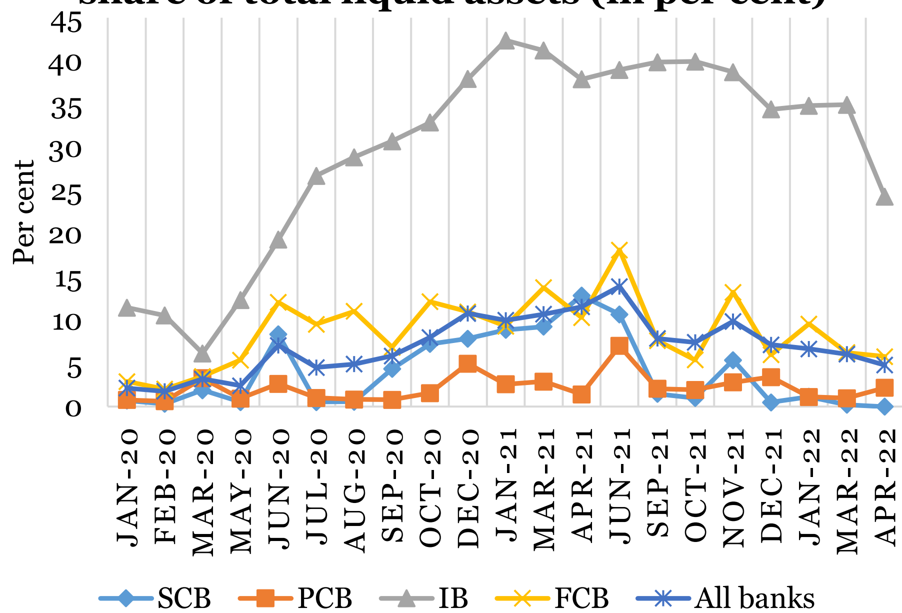


Figure: Excess reserve (un-invested cash) as a share of total liquid assets (in per cent)



Poorly Performing Banks

- **In 2021, five commercial banks failed to publish their mandatory disclosures under BASEL III.** These banks are: Bangladesh Krishi Bank, Rajshahi Krishi Unnayan Bank, Al-Arafah Islami Bank Limited, Bangladesh Commerce Bank Limited, ICB Islamic Bank Limited, and Prime Bank Limited.
- Additionally, **11 banks were unable to meet minimum BASEL III requirements**, as per their latest disclosures.

Figure: Commercial banks which have failed to meet minimum BASEL III requirements

Name	CET1 (in %)		LCR (in %)	NSFR (in %)	LR (in %)		Year
	Solo	Cons.			Solo	Cons.	
Agrani Bank Limited	4.63	4.59	222.91	107.13	2.37	2.38	2021
BASIC Bank Limited	-1.56	-	368.98	107.35	-0.82	-	2021
Janata Bank Limited	5.16	5.11	357.78	111.86	2.94	2.93	2021
Rupali Bank Limited	5.37	3.65	509.44	98.75	2.19	2.24	2021
Sonali Bank Limited	7.81	8.47	422.54	100.73	2.83	3.05	2021
Bangladesh Krishi Bank	-42.68	-	99.57	75.03	-30.88	-	2020
Rajshahi Krishi Unnayan Bank	-16.55	-	461.00	114.00	-12.16	-	2020
Bangladesh Commerce Bank Limited	-14.80	-14.34	100.93	119.31	-16.16	-16.24	2020
ICB Islamic Bank Limited	133.33	-	58.06	148.56	-161.55	-	2020
Padma Bank Limited	6.42	6.25	95.27	170.75	5.02	4.89	2021
National Bank of Pakistan	30.46	-	91.74	28.5	17.5	-	2021

Note: BASEL III requirements stipulate that banks should maintain Common Equity Tier 1 (CET1) to Risk Weighted Assets (RWAs) ratio greater than 4.5%, Liquidity Coverage Ratio (LCR) greater than 100%, Net Stable Funding Ratio (NSFR) greater than 100%, and Leverage Ratio greater than 3%.

Rescuing Banks Through Recapitalisation Has Been Futile

- Recurrent recapitalization of the SCBs by the government has emerged as an issue of grave concern, as the performance of the banks is not improving.
- It has been estimated that the government has spent **BDT 15,705 crore** in recapitalising the banks during the period FY2009-FY2017.
- This amount would be sufficient for building **4 deep sea ports like Payra**.
- This has set bad examples and will encourage banks involved in irregularities.

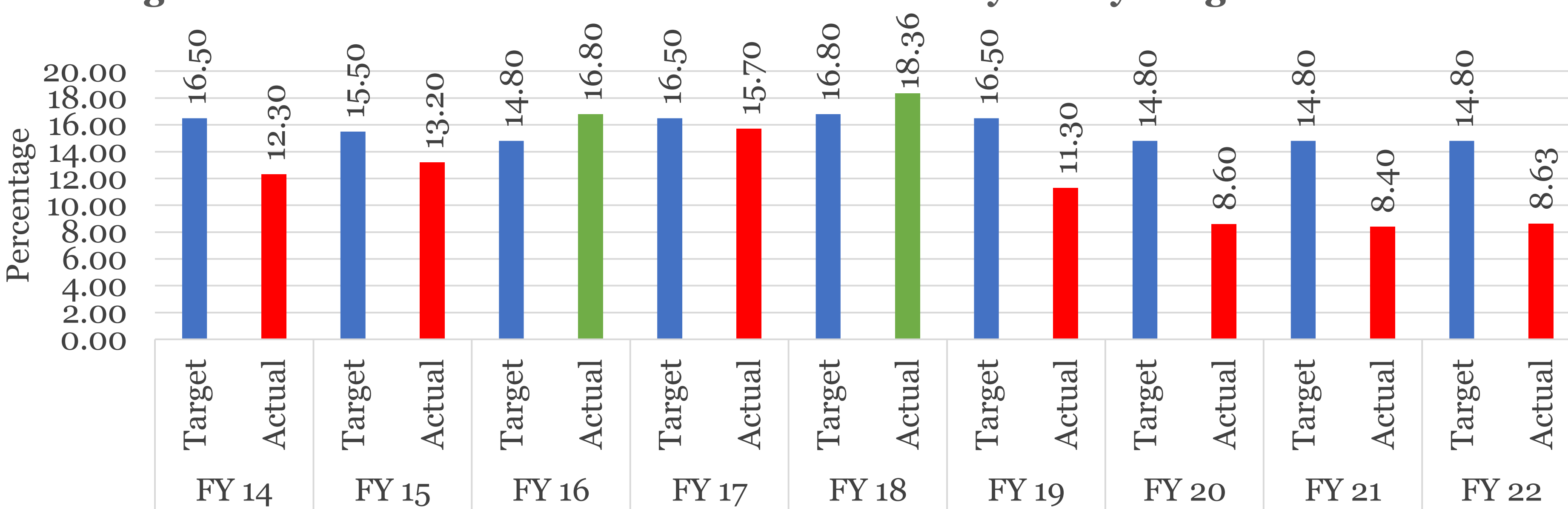
Monetary Policy for a Pandemic-affected Economy

- Monetary policy in the upcoming fiscal year will have to tackle the challenges posed by the uncertainties caused by COVID-19, while at the same time reigning in the rising cost of living which is harming the middle class and the poor.
  - Such formidable feats must be performed in the backdrop of excess liquidity in the banking sector, which will make this effort even more arduous.
- **Excess liquidity in the banking system may induce commercial banks to behave in ways which may jeopardise the stability of the financial system and make it difficult for the central bank to achieve its monetary policy goals.**
  - For example, banks may attempt to offset their losses from holding excess liquidity by giving out risky loans which may lead to higher volume of NPLs, higher inflation, and the creation of asset bubbles.
- Excess liquidity in the banking system also weakens the interest-rate transmission mechanism of monetary policy, making monetary policy less effective in fine-tuning aggregate demand.
- Moreover, when there is excess liquidity in the banking system, commercial banks may perceive the opportunity cost of holding excess balances at the central bank to be low, and hence be slow to act to reduce excess liquidity.
  - As a result the central bank would find it more challenging to determine the ideal level of desired and excess reserves.

Private Sector Credit Growth

- Despite stellar economic growth in the pre-pandemic years, private sector credit growth targets were not met in FY14, Fy15, FY17, FY19, FY20, FY21, and FY22.
- In response to low private sector credit growth, the central bank had to reduce its monetary policy targets in several years.
- **Weak private sector credit growth in an economy is indicative of low private sector investment**

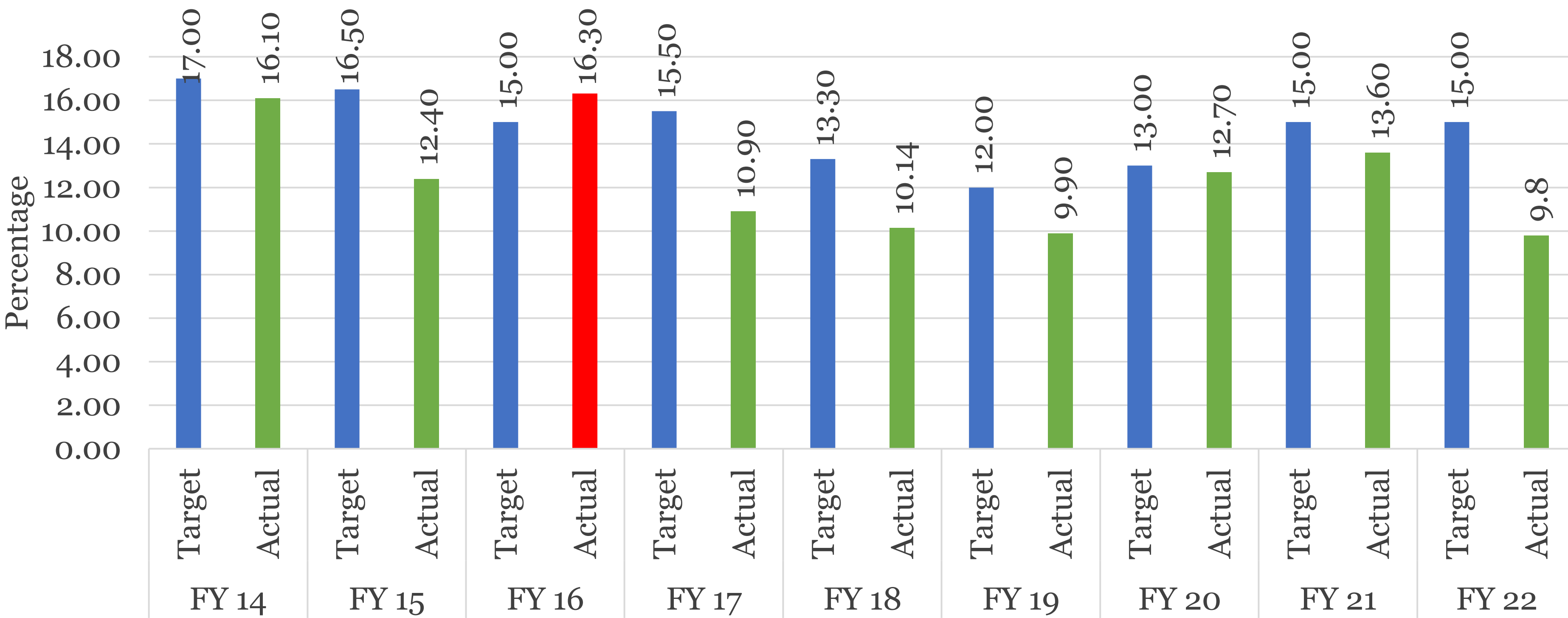
Figure: Private Sector Credit Growth - Monetary Policy Targets vs. Actual



Broad Money Growth

- Broad money growth was within the targets set by the monetary policy in FY20, FY21, and FY22.
- During FY14 to FY22, broad money growth was always below the target set by the monetary policy, except in FY16.

Figure: Broad Money - Monetary Policy Targets vs. Actual



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Banking Sector as the Factor Inhibiting Development

- The **severity of high NPLs is currently invisible** due to the measures taken to ease loan classification.
  - However, the volume of NPL may rise significantly in the coming days as impact of lifting the moratorium on loan classification becomes visible
- At present, problems of the banking sector are being tackled by government's support. This is possible since banking assets are only about 56% of GDP. When banking assets will increase, the government may not be able to do so.
- As Bangladesh prepares for graduation from a Least Developed Country (LDC) to a developing country and from a lower middle-income country to an upper middle-income country, it is crucial to develop a sound financial system which will ensure **finance for development, not finance for crony capitalism**.
- Regrettably, reform in the banking sector is still an unfinished agenda

Independent Review of IRBD Bangladesh's Development

Policy Recommendations

- This presentation has discussed some of the pressing issues of the banking sector based on the limited data which was available at the time of writing.
- Based on the performance of the banking sector, a number of recommendations have been made for enabling the banking sector to play a more constructive role in the economic recovery from the pandemic.
- In the short term, loans should be provided to the CSSMEs.
- Disbursement of the government's COVID-19 **liquidity support for small businesses, farmers and low-income professionals** should be expedited immediately.
- In the medium term, reforms should be the priority of the policymakers, in view of the increased responsibility of the sector for a growing economy
- **Transparency and accountability** mechanisms should be built into all COVID-19 related liquidity support packages, and more disaggregated data on the implementation status of all liquidity support packages should be published on a monthly basis.
- Banks with excess liquidity should be discouraged by the central bank from taking unnecessary risks.

6. External Sector: A Time of Unforeseen Volatility and Unprecedented Pressure

External Sector: A Time of Unforeseen Volatility and Unprecedented Pressure

- Bangladesh's external sector has never been under so much pressure, and has experienced so much volatility as in the recent past.
- Trade deficit is anticipated to cross USD 30.0 billion mark, current account deficit the USD 18.0 billion mark and the negative overall balance crossing the USD 5.0 billion mark by the end of FY22.
- The resultant drawdown on reserves, volume-driven export not catching up with price-driven imports, and the negative growth in remittances had led to significant uncertainties and speculative behavior in the exchange rate market.
- This has lead to, in the end, the significantly important policy shift after about a decade, to *free float* from the *managed float*.
- Bringing back stability in the exchange rate market and addressing the adverse consequences of imported inflation will call for prudent monetary management, and strategic fiscal management and the coordination between the two.

The Deteriorating BoP Position

Table: Disquieting Development in BoP during July-April period (FY21 versus FY22)

(in million USD)

Items	2020-21[R] July-Apr	2021-22[P] July-Apr	% Changes
Trade balance	-18013	-27569	-53.1
Current Account Balance	-1653	-15317	-826.6
Financial account	9598	12029	25.3
Overall Balance	7499	-3710	-149.5

Source: Based on Bangladesh Bank (2022)

- The negative trade balance is anticipated to exceed (-) USD 30.0 billion in FY22 driven by rising imports and relatively lower rise in exports.
- In the backdrop of the negative growth of remittances, the negative current account balance rose sharply in the FY 2021-22 (July-April): rising from (-) USD 1.6 billion to (-) USD 15.3 billion, unprecedented in recent history.
- The increase of (+) USD 2.5 billion in the Financial Account could not dent on the overall balance position which went from the positive (+) USD 7.49 billion to the negative terrain of (-) USD 3.7 billion.

Volume-driven Export Earnings

Table: Stylised Data on Bangladesh's Export FY22 & FY21 (July-May)

(in billion USD)

Major export items	FY22 (July-May)	FY21 (July-May)	Export growth (in %)	Net export (July-May FY22)	Net export (July-May FY21)	Net export growth (in %)
RMG	**38.52**	**28.56**	**34.9**	**18.56**	**13.73**	**35.2**
Knitwear	20.99	15.36	36.6	11.54	8.45	36.6
Woven garments	17.54	13.20	32.8	7.01	5.28	32.8
Non-RMG	**8.65**	**6.62**	**30.7**	**7.35**	**5.65**	**30.2**
Total	**47.17**	**35.18**	**34.1**	**25.90**	**19.37**	**33.7**

Source: Estimated from EPB (n.d.)
Note: For calculating net export, below-mentioned weights were considered for the export items:
Knitwear: 0.55, Woven garments: 0.4, Home Textiles: 0.6, Other Non-RMG products except Home textiles: 0.9

- While export growth has been robust at 34.1 percent over the first 11 months of FY2021-22, from foreign exchange retention perspective, estimation of net export as against gross export is important. The two figures for FY2021-22 (July-May) are estimated to be USD 25.90 billion and USD 47.17 billion respectively (net export being about 55.0% of gross export).
- The slowdown in export growth in May, 2022 in the face of lower growth and even signs of recession in some of the key markets, do not augur well for export sector performance in the coming months.

Volume-driven Export Earnings

Table: Bangladesh exports to US: Value, Price & Volume effects

HTS Code	FY21 (Jul-Mar)			FY 22 (Jul-Mar)			Percentage increase		
	Volume (in millions)	Value (in million dollars)	Per Unit price (in USD)	Volume (in millions)	Value (in million dollars)	Per Unit price (in USD)	Value	Volume	Per unit price
61 (Knit)	814.6	1456.4	1.8	1,141.7	2,377.3	2.1	63.2%	40.2%	16.7%
62 (Woven)	569.3	2802.4	4.9	747.0	3900.1	5.2	39.2%	31.2%	6.1%
Overall	1383.9	4258.8	3.1	1,888.7	6,277.4	3.3	47.4%	36.5%	6.5%

Source: Estimations based on USITC, n.d.

- Also to note, Bangladesh export growth has been mostly volume-driven. Buyers and brands have been able to pass on the rise in the price of the key inputs going into apparels export (cotton, yarn and fabrics, with price of cotton rising by more than 50.0% in April 2022 compared to corresponding period of 2021.
- This is true both for the US and the EU markets (more for woven-RMG).

Volume-driven Export Earnings

Table: Bangladesh exports to EU: Value, Price & Volume effects

HTS Code	FY21 (Jul-Mar)			FY 22 (Jul-Mar)			Percentage Change		
	Volume (in million Kg)	Value (in million euros)	Per Kg price (in euros)	Volume (in million Kg)	Value (in million euros)	Per Kg price (in euros)	Value	Volume	Per Kg price
61 (Knit)	502.6	5935.1	11.8	613.3	8193.7	13.4	38.1%	22.0%	13.2%
62 (Woven)	244.3	3512.7	14.4	285.2	4390.4	15.4	25.0%	16.7%	7.1%
Overall	746.9	9447.8	12.6	898.5	12584.1	14.0	33.2%	20.3%	10.7%

Source: Estimations based on EuroStat, n.d.

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Remittance Flows Have Been Declining, But Expected to Catch Up

Table: Remittance inflow July-May (FY20-FY22)
(in billion USD)

FY20 (July-May)	FY21 (July-May)	FY22 (July-May)	FY20-FY21 (July-May) remittance earnings growth (in %)	FY21-FY22 (July-May) remittance earnings growth (in %)	FY20-FY22 (July-May) remittance earnings growth (in %)
16.37	22.84	19.19	39.5	-15.9	17.2

Source: Based on Bangladesh Bank (n.d.)

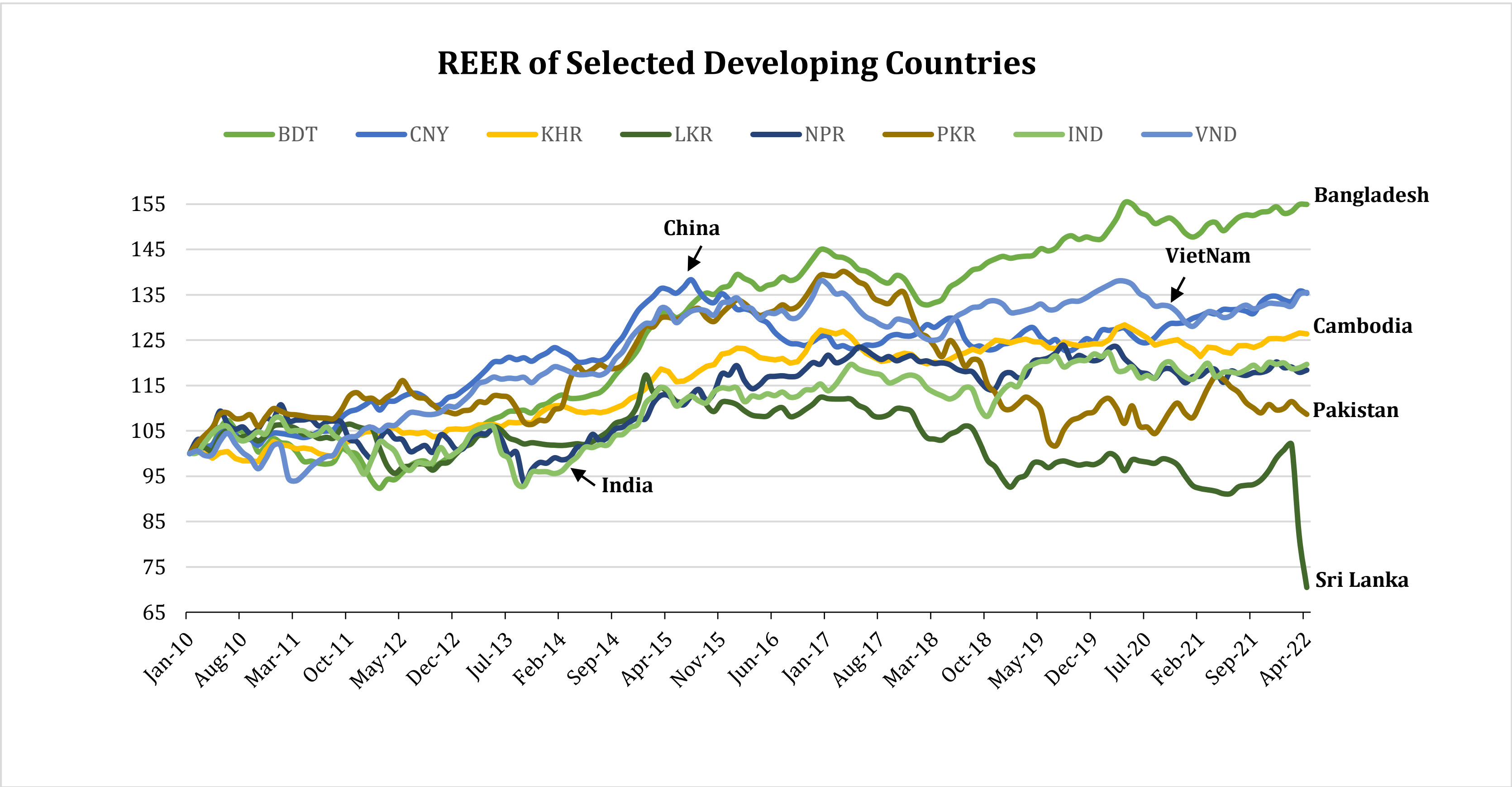
- While remittance growth was a negative (-15.9%) in the first eleven months of FY2021-22 (July-May), compared to the corresponding period of pre-pandemic FY2019-20 this was 17.2% cent higher.
- The floating of currency should reduce the significant difference between the official exchange rate and the curb market and in the informal hundi/howla transactions.
- However, the incentive for remittance (at 2.5% of remitted amount) should continue for now till the market stabilises when decision can be taken as regards reduction or elimination of the incentives.

Remittance Flows Have Been Declining, But Expected to Catch Up

- The high number of people joining overseas job markets should be reflected in the remittance flow in FY2022-23. In the July-April of FY21-22 about 7.99 lac people have gone to various countries in middle east. Comparable figures for FY2019-20 and FY2020-21 were 5.31 lac and 2.17 lac.
- Special attention should be given to new employment opportunities in post-pandemic Malaysia and Singapore job markets.
- In view of the steps taken by the Bangladesh Bank (floating exchange rate) and the incentive, and the rising number of migrant workers joining overseas job market, remittance flows should approximate the spike of FY2020-21 in FY2022-23.

Prudent Exchange Rate Management: Call of the Day

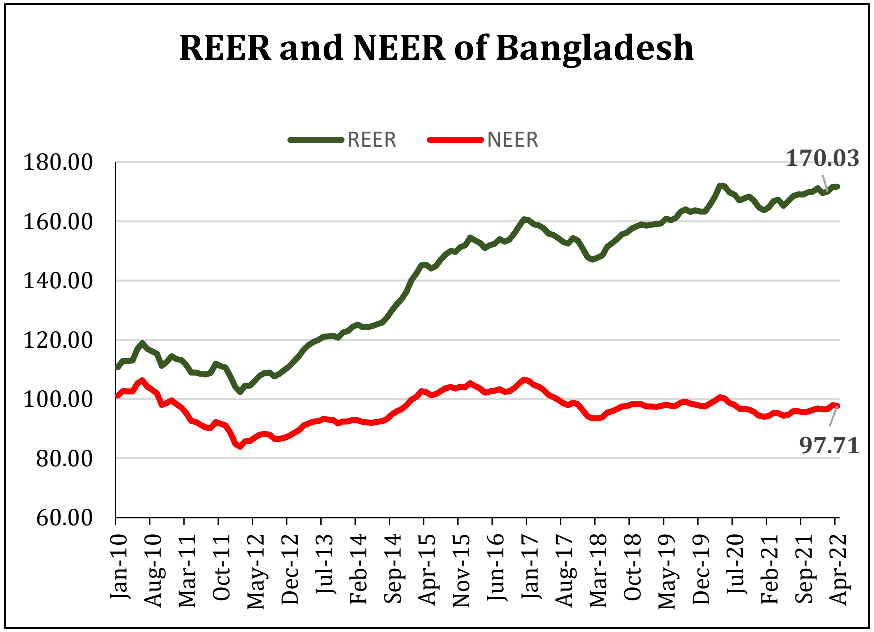
- REER of BDT was consistently higher vis a vis Bangladesh's competitors (with 2010 as base year)

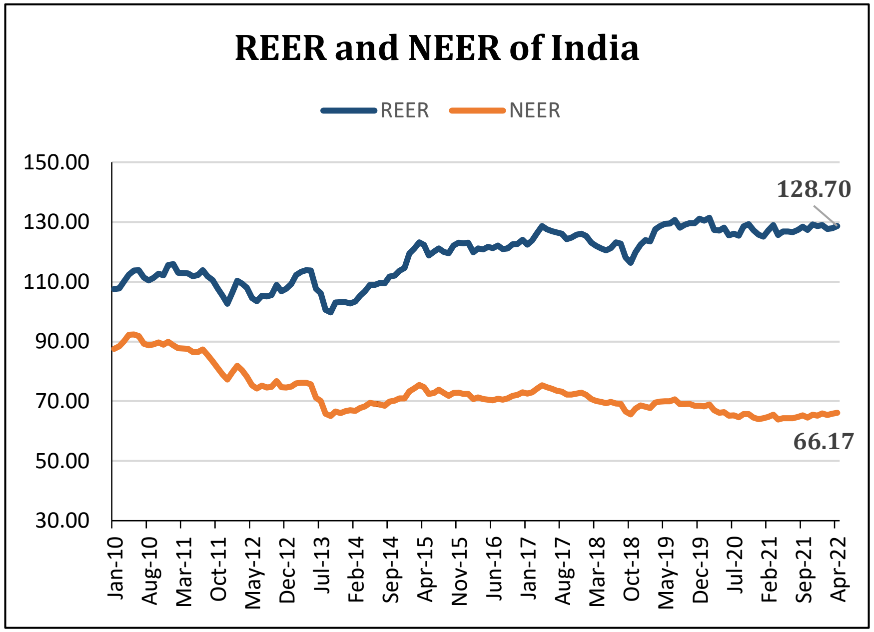


Source: Bruegel (2022)

Prudent Exchange Rate Management: Call of the Day

- The gap between REER and NEER of Bangladesh was widening over the years which called for adjustment through depreciation of BDT.





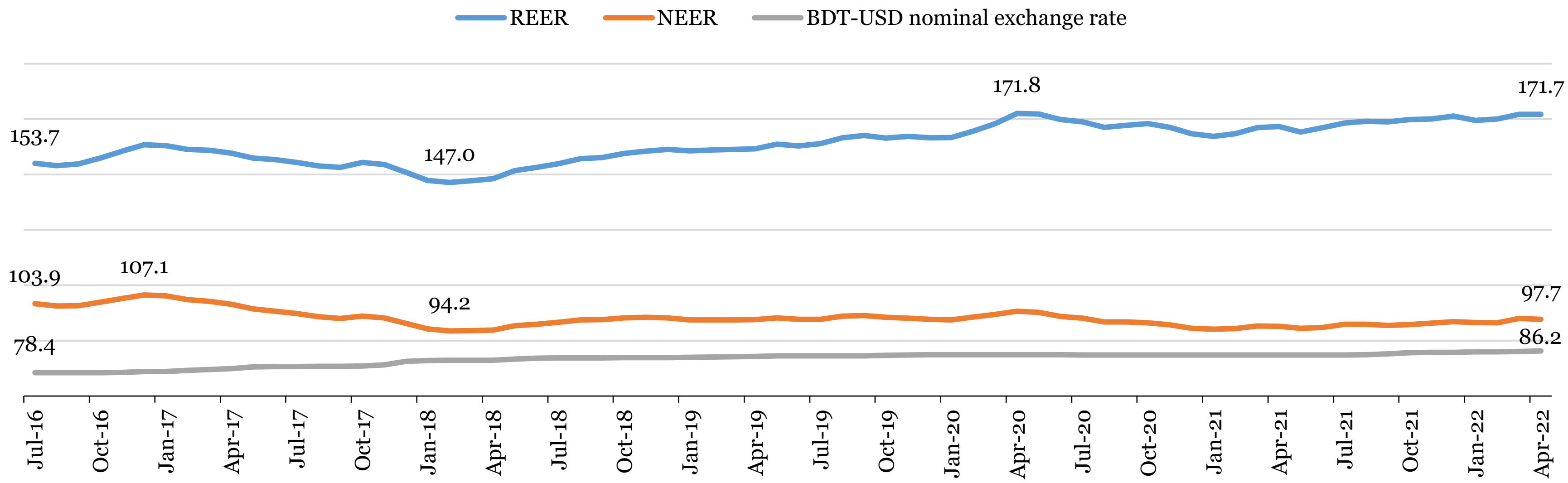
Source: Bruegel (2022).

Prudent Exchange Rate Management: Call of the Day

- Bangladesh's managed float pursuit till now could not be made to work for several reasons:
  - While the BB had depreciated the taka eight times this year, it proved to be too little too late. The declining reserves situation did not allow the BB to go for unlimited dollar injection (it had already done so to the extent of USD 6.2 billion in FY 2021-22).
- CPD had also argued in successive IRBD's that Bangladesh's exports were becoming less competitive vis-à-vis competitors and remittance flows were also being disincentivised because of this.
- CPD has been pointing out the need for depreciation of BDT in view of the growing gap between REER and NEER.

Prudent Exchange Rate Management: Call of the Day

Figure: REER, NEER and USD-BDT exchange rate trends



Source: Based on bruegel (2022) and Bangladesh Bank (2022)

- While the gap between REER and NEER had been rising, the USD - BDT 'Managed Float' exchange rate did not go for necessary correction. Taka became appreciated as a consequences. A market correction, induced by the current BoP position and free float thus did not come as a surprise.

Prudent Exchange Rate Management: Call of the Day

- To recall, CPD's Policy Suggestions three years back included the followings

CPD's Policy Suggestions: IRBD 2019 (June 11, 2019)

- A gradual depreciation of the BDT should be pursued with the help of the central bank's sterilisation interventions
- A sharp depreciation may have adverse implications for import payments, consumer prices and foreign debt servicing
- Depreciation of BDT will also help incentivising export and remittances – hence, cash incentives will not be required!
- In the short term, the expected deficit in the current account may be brought down by containing imports
- The government may also consider raising import duties on selected luxury items and consumer goods
- Bangladesh Bank can selectively impose higher LC margin to discourage imports

Prudent Exchange Rate Management: Call of the Day

However, while Bangladesh did start to actively pursue a policy of depreciation, after exhausting its tool of dollar injection, it proved to be too late requiring the surgical operation of moving from managed float to free float.

- This, under the circumstances, is a step in the right direction. There will be market correction in the USD-BDT exchange rate. However, as in 2012 there is a possibility of (reverse) correction once the foreign exchange market settles down.
- In the short run, free float was likely to lead to deepening of imported inflation.
- However, it is to be noted that Bangladesh was not being able to enforce its 'managed float' anyway in case of L/C openings and settlements and inter-Bank dollar market (as also for export settlements and remittance flows). So the apprehension about 'imported inflation' could not be addressed in any way through the 'managed float'.

Prudent Exchange Rate Management: Call of the Day

- In view of the adverse implications of imported inflation on consumer prices and purchasing power of fixed income earners, and to contain import demand, the GoB and BB have taken a number of steps: discouraging import of luxury items through higher L/C margin and imposition of duties on selected items, on the one hand, and tariff rate adjustments (reduction of VAT and duties on essential commodities) on the other.
- There is a need to coordinate Monetary Policy and Fiscal Policy, particularly in view of the upcoming FY 2022-23 budget.
- To address the adverse impacts of imported inflation, in view of Budget FY 2022-23 the Government should go for (a) import duty adjustment, (b) improvement of market management (from import stage to retail, consumer and producer level, (c) use of strategic food stocks and OMS and (d) strengthening of SSNPs, particularly programmes for food distribution and cash transfer.

7. Concluding Remarks

Concluding Remarks

- The economy is under pressure in view of the emergent challenges caused due to both external and domestic factors. These challenges are apprehended to be continued for some time as predicted by various international organisations in view of slower growth globally, including in some major economies.
- This is worrisome for the overall macroeconomic situation in Bangladesh. It requires proactive measures by the policymakers both in the immediate and medium terms.
- The quality, reliability and consistency of data of economic indicators will be the first step since the effectiveness of policymaking depends on credible real time data.
- Policymakers will have to come out of growth obsession and focus on the quality of growth in terms of distribution of the benefits of growth more equally.

Concluding Remarks

- Since the poor and disadvantaged people are yet to overcome the impact of the pandemic and have been affected further due to high prices of essential commodities, the policy should protect the purchasing power of the poor and low-income groups.
- CPD has been proposing various measures to ease the burden of rising prices and shrinking purchasing power of low- and fixed-income earning people including selectively reduce taxes at import and domestic stages and expanding social protection.
- Besides, strategic sectors such as energy and agriculture will have to be supported through subsidies for economic growth and food security.
- The above measures should be combined with higher efforts for domestic resource mobilisation and reduced unnecessary and less important expenditures.
- In the FY23 budget, fiscal measures pertaining to the external sector should focus on addressing the adverse impacts of imported inflation.

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Thank You

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