2014

Country Report – Bangladesh

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In manufacturing, export growth in the first quarter of this fiscal year has been almost non-existent and has seen a gradual decline. This is mainly due to garment exports. The garment sector is going through a structural reform on account of twin disasters. The international market recovery was not as it was expected, particularly in the European market. However, there are some positive indicators notably in the agricultural sector, which has seen a hike in crop production. Public investment also performed well and rose from 6.6 percent of GDP in FY 2013 to 7.3 percent in FY2014. The rate of growth of tax revenue raised by NBR during July-November 2014 was lower than the rate during the corresponding period last year.

Highlights of the economy

GDP size	: USD 194 Bn
Budget Outlay (2015-2016)	: USD 37.83 Bn (BDT 2.95 Tn)
Development Outlay	: USD 13.15 Bn (BDT 1.02 Tn)
Public Debt to GDP	: 28.6% (FY 2014)
External Debt to GDP	: 13.6% (FY 2014)
Total Exports	: USD 30.4 Bn (FY 14)
Total Imports	: USD 41.4 Bn (FY 14)
Inward Remittance	: USD 14.94 Bn (FY 14)
Balance of Payment	: USD (–ve) 1.06 Bn (FY 14)

Reserves

Another oft-repeated success of the economy is the rapid increase in the international reserves to over USD 24 billion, sufficient for 5 months import. Monetary management was challenged by fast reserve accumulation as the remittance was reduced by 1.6 percent. However, Bangladesh Bank (BB) managed to keep reserve and broad money growth within target by stepping up sterilization operations. The surplus in balance of payment increased from USD 5.1 billion in FY13 to USD 5.5 billion, creating an excess supply of foreign exchange. BB's interventions in the foreign exchange market, limited appreciation of taka. The real exchange rate appreciated by 8.5% in FY14 relative to FY13 due to small (2.7 percent) nominal appreciation and higher domestic inflation relative to international inflation.

National Budget

On June 4, 2015 the national budget was placed in the Parliament with an aim to achieve 7% growth. The total outlay was USD 37.83 Bn and the development outlay was USD 13.15 Bn. A Revenue target of BDT 2.08 trillion (USD 26.88 Bn) is set leaving BDT 862.48 billion (USD 11.14 Bn) deficit. Inflation is targeted at 6.2%, down from 6.6% of the previous year.

With an aim to spur growth in an otherwise stagnant Corporate Sector and Capital Market, several incentives have been proposed in Budget 2015-16. Other than Banks, Insurance and NBFIs, Tax rate is proposed to be

reduced from 27.5% to 25.0% for publicly traded companies. In case of Banks, Insurance and NBFIs proposal has been placed to reduce tax from 42.5% to 40.0%. Tax exemption for dividend income has been raised to BDT 25,000 from BDT 20,000. A proposal has also been placed to withdraw provision of 10.0% deduction at source on income from share market by any company or partnership firm.

Public Private Partnership Programs

As a growing economy, infrastructure development has become a priority. With this end in view, a Private Public Partnership (PPP) Office has been set up at the Prime Minister's Office. The PPP program has met with a fair degree of success and has been entrusted with a few mega projects. The PPP has been working as an independent entity and has attracted the attention of foreign and local partners. Some of the notable projects undertaken by PPP is Dhaka bypass projects, Dhaka elevated expressway, Moghbazar Mawa elevated expressway. A mega tourist attraction is underway at Cox's Bazar on a 100 acre land and the Airport is scheduled to be modernized to enable tourists to land directly bypassing Dhaka or Chittagong. In the current budget, Government is set to allocate BDT 20 Bn (USD 258.43 Mn) for PPP projects.

Fiscal

Fiscal policy is affected by revenue collection and development budget implementation shortfalls. The overall fiscal deficit in FY14 was a modest 3.1 percent of GDP. Public debt as a share of GDP is declining. The financial system remains under stress and capital market activities have been weak. Several financial scams and resultant loan defaults in the state-owned commercial banks (SCBs) moved them into a position of insolvency.

Inflation

Inflation is still high but stable. Overall consumer inflation increased to 7.4 percent in FY14 relative to 6.8 percent in FY13, driven by an increase in food inflation. Part of the rise was due to supply disruptions caused by the political unrest of 2013. The gap between rural and urban food inflation narrowed. Stable international oil prices and prudent monetary management helped reduce non-food inflation from 9.2 percent in FY13 to 5.5 percent in FY14.

Banking Sector

Prolonged political unrest in the year 2013 followed by another bout of uncertain political situation in 2014 raised the specter of default risk in the banking sector. The growing nonperforming loans of private commercial banks were also a matter of concern. Asset quality in the state-owned commercial banks (SCB) deteriorated in FY14. While their aggregate stock of assets and share in the total assets of the banking system declined, deposits continued to grow at a healthy rate, thus ensuring adequate liquidity.

Structural Reforms

Some structural reforms have moved forward. NBR is implementing a comprehensive reform program to enhance policies and modernize tax administration. Reforms seek to encourage voluntary compliance by simplifying and automating the tax payment system and by reducing the discretionary power of tax officials. To enhance the efficiency of customs administration, the Automated System for Customs Data (world clearance system) has been introduced at all major customs houses, aiming to have a national paperless customs management system operating in the near future.

Foreign Trade

Total exports in FY 2013-2014 increased 9% from the previous year. Imports rose by 10% in FY13-14. Inward remittances dropped by 1.6% in FY 13-14 compared to 12.6% growth in FY 12-13. Balance of Payment came down to USD (-ve) 1.06 Bn, a marked decline from the previous year's position of USD 5.1 Bn.

Gross international reserves reached to record USD 24 billion at the end of December 2014. Bangladesh Bank intervened frequently to prevent a large appreciation, leading to historic highs in building up official foreign exchange reserves.

Cautionary Monetary Policy

Monetary Policy in the year 2014 remained largely the same as the year 2013. Cautionary monetary stance with a twofold objective of reining in inflation and availability of liquidity for the private sector led growth remained in place. Prudent monetary policy helped to reduce nonfood price increases. At the same time Central Bank intervention kept the exchange rate favorable to help the exporters in fulfilling the targets.

Money supply growth was below the central bank's program target, even as banks' net foreign assets rose sharply. The reason was growth in credit to the private sector was languishing far below target as political uncertainty deterred investment. The financial system remains under stress and capital market activities have been weak.

Financial Inclusion Programme

A positive development is the **financial inclusion programme** spearheaded by Bangladesh Bank. Millions have been brought into the banking network either through opening of bank accounts or with increased access to mobile banking. The measures adopted to bring the masses into the fold of banking network are likely to have far reaching positive impact for the country. Bangladesh has emerged as the fastest growing mobile banking country in the world.

Capital Market Scenario

Capital Market, overall in 2014 has been a year of some recovery and relative stability. The stock index gained grounds in the second half of FY14 after remaining sluggish in the first half. The benchmark index of Dhaka Stock Exchange, DSEX, gained 5 percent between January and June. The uptrend started at the beginning of the calendar year, following national parliamentary election on January 5, 2014. DSEX reached its peak at 4,845 on February 6, 2014.

From July onward it moved within a band of 4,400 to 4,600. Stocks with good fundamentals marked higher return compared to the overall return on the market portfolio. DS30, the blue chip index, marked a sustained 12.7 percent yield, which is more than double the return on the benchmark index.

The trade volume improved between January and June, 2014. Average daily turnover exceeded the BDT 6 plus billion (USD 0.08 Bn) in January 2014 for the first time after 2011, when the average daily turnover was BDT 6.6 billion (USD 0.09 Bn) following the 2010 market crash. Improvement in the average daily turnover was also a result of the excess liquidity that accumulated on account of slowdown in investment. After declining to around BDT 3 billion in May, daily turnover started picking up again from early August and crossed BDT 6 billion (USD 0.08 Bn) mark once again on September 4, 2014.

In terms of corporate profitability, listed companies achieved 28.9% earnings growth as of Sep 14. This growth was mainly due to robust growth in net profit of banking sector of 91.5% during the same period. Average daily turnover slightly enhanced to BDT 4993.79 million (USD 64.53 Mn) in 2014 to BDT 4003.12 million (USD 51.73 Mn) in 2013 where year-end market PE was 15.69 and 15.07 respectively for 2014 and 2013.

In 2014, 17 companies raised BDT 9,893.7 million (USD 127.84 Mn) through the primary market which was a bit lower than 2013. 43% of total fund withdrawn was utilized to repay debt. After inclusion of new securities, total number of listed Companies in 2014 stand at 317 and 289 in DSE and CSE respectively. On the other hand 9 listed companies raised BDT 20,630.45 million (USD 266.58 Mn) from the secondary equity market through

issuing rights shares which is 1044.2% higher than the FY 2013. In 2014, Bangladesh Securities and Exchange Commission (BSEC) introduced pilot project where investors could deposit IPO subscription fee to some brokerage houses and merchant banks in addition to Banks. BSEC is expected to establish this project in 2015.
Both the bourses started 2014 with demutualized status and continue reformation through launching of Shariah based index, surveillance software, commencement of CRO's operation, implementation of NASDAQ OMX designed trading software and initiation of single share market lot etc.

Demutualization Act, 2013 with the objective of separating the bourses management from the ownership is yet to make a meaningful impact in the Capital Market. BSEC's endeavor to bring in the qualitative changes helped it achieve a higher regulatory status from the International Organization of Securities Commissions (IOSCO), the association of national securities regulatory agencies. It has been upgraded to an A-category regulatory agency which ensures the regulator's access to international cooperation on securities markets worldwide.

Industry Analysis

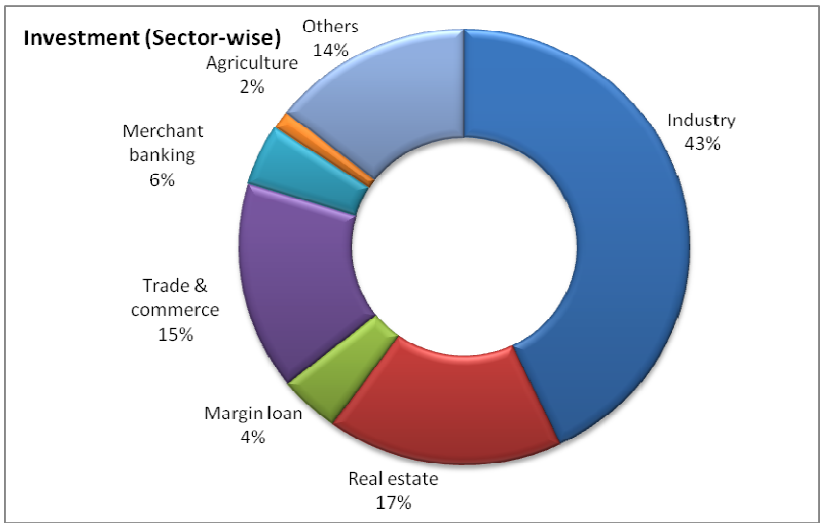
NBFIs have turned out to be engines of growth and are integral part of the Bangladesh financial system; enhancing competition and diversification in the financial sector have been increasingly recognized as complementary of banking system at competitive prices. Simplified sanction procedures, flexibility and timeliness in meeting the credit needs and low cost operations resulted in the NBFIs getting an edge over banks in providing long term funding. The total number of NBFIs now stands at 32 with the induction of one more in 2015. 3 are Government dealing either in micro finance program or infrastructure development funded by external financiers.

Recently NBFIs have become more integrated with the general masses through creative products in the Assets and Liabilities side and have displayed a certain degree of resilience despite the tension in the economic and political developments.

With the growing importance assigned to financial inclusion, NBFIs have come to be regarded as important financial intermediaries particularly for the small-scale and retail sectors. In line with the central bank's policy directives, loans to agriculture and SMEs are being prioritized considering their role in contributing to inclusive economic growth and job creation.

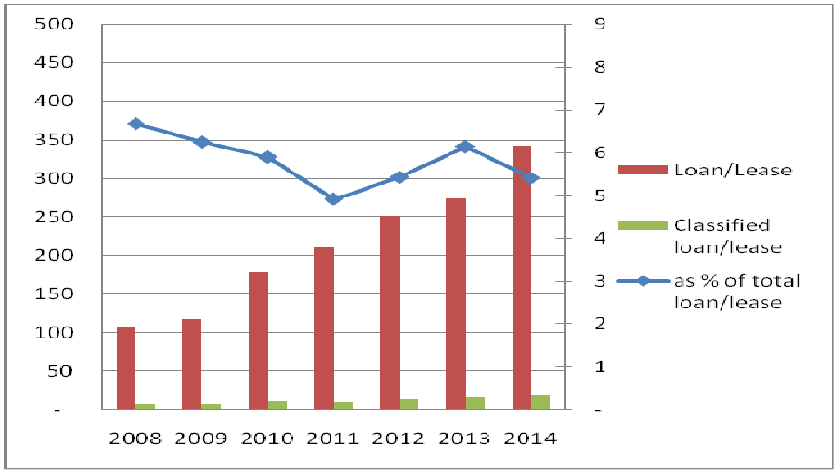
With total assets equivalent to less than 4 percent of GDP in 2014, the role of Nonbanking Financial Institutions (NBFIs) has been growing. In 2014, NBFIs recorded notable growth in total assets, borrowings, deposits, and capital. The asset of NBFIs have increased substantially in FY14, by 30.7 percent to BDT 436.3 billion (USD 5.64 Bn) in 2013 from BDT 333.9 billion (USD 4.31 Bn) in 2012. At the end of June 2014, total assets stood at BDT 500.6 billion (USD 6.47 Bn). As of June 2014 investment of NBFI sector was majorly driven to industry clocking 43 percent, real estate 16.9 percent, trade and commerce 15.4 percent, power, gas, water and sanitary service 12 percent, garment and textile 9 percent and so on. Despite the overall Investment scenario in 2014 was almost same to 2013, an enhancement of 4.1 percent in trade & commerce has been observed. As of September 2014, total BDT 2,441.70 million (USD 31.55 Mn) disbursed in SME sector.

Investment



Asset quality of NBFI sector remained stable compare to banking sector. As of June 2014, the number of default loans of NBFIs increased at a lower rate i.e. increased by 4.69 percent as compared to the Banks 26 percent. As of June 2014 nonperforming loan ratio was 5.4 percent for the NBFI sector. In the total asset composition of all NBFIs, the concentration of loans, lease and advances is 72.2 percent. At the end of June 2014, the industry as a whole was able to maintain adequate provision. As of June, 2014 the total outstanding of loan/lease was BDT 341.7 billion (USD 4.42 Bn) against which NPL was BDT 18.5 billion (USD 0.24 Bn) i.e. 5.4 percent which was 5.6 percent in December 2013. At the end of September 2014, most NBFIs listed on stock exchange posted better profit than September 2013. Efficient management system has driven the industry to a better position despite substantial competition and negative growth in private sector investment. According to CAMELS rating, majority of the NBFIs have been performed satisfactorily.

Non Performing Loan



<u>Strategic shift</u>

Few years back NBFIs were dependent on Banks as their major source of funding which made them vulnerable to systemic risks in the financial system. But now, NBFIs are generating fund directly from the market as short or long term deposits like Banks. Total deposits of the NBFIs are gradually increasing; in 2013 it was BDT 198.3

billion (USD 2.56 Bn) whereas in 2012 it was BDT 145.4 billion (USD 1.88 Bn) and as of June 2014 it increased to BDT 233.2 billion (USD 3.01 Bn) represented almost 58 percent of total liabilities. Despite narrow business line comparison to Banks NBFIs are offering some products to a greater extent than Banks.

Central Bank Monitoring

Bangladesh bank's (BB) monitoring on NBFIs remains prudent and during a year hundreds of various reports are required to be submitted to BB by each NBFI. As a part of better transparency, complete schedule of charges and base rate are displayed by every NBFI. No charge, fees or commission in any kind other than stipulated range prescribed by Bangladesh Bank can be charged. In 2014 BB emphasized on green financing to ensure sustainable development of the country and to finance in renewable energy and eco-friendly projects. In 2014 BB launched an automated system to detect the financial problems of any NBFIs and to protect them from devastating loss in sudden business crisis.

Industry outlook

Despite inclusive growth focused monetary policy, the overall economic progress will be slowed further unless political tension eases and share of private sector investment in gross domestic product increases significantly. The biggest challenge for the private sector growth will be restoring business confidence besides prompt addressing to the infrastructure and power.

Cost of fund is reducing gradually and it is expected that the money market will continue to remain easy. Excess liquidity of the banks due to poor demand from borrowers will push the banks not to take deposits at higher rates which may have impact on reducing lending rates. Competition will intensify as the environment may not be conducive for business growth. However, incremental output from the agriculture, refinancing and SME financing could be the options to maintain minimum spread in the adverse economic condition.

USD 1= BDT 77.39