State of the Bangladesh Economy in FY2007-08 And Some Early Signals Regarding FY2008-09
(First Reading)

Paper 70

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The present paper titled **State of the Bangladesh Economy in FY2007-08 and Some Early Signals Regarding FY2008-09: First Reading** has been prepared under the CPD IRBD programme. This programme aims at strengthening institutional capacity in Bangladesh in the area of trade policy analysis, negotiations and implementation. The programme, *inter alia*, seeks to project the civil society’s perspectives on the emerging issues emanating from the process of globalisation and liberalisation. The outputs of the programme have been made available to all stakeholder groups including the government and policymakers, entrepreneurs and business leaders, and trade and development partners.

The paper has been prepared by the CPD IRBD Team 2008.

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The CPD-IRBD team alone remains responsible for the analyses and interpretations presented in this report.

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ACRONYMS

ADP	Annual Development Programme
AfT	Aid for Trade
BB	Bangladesh Bank
BCIC	Bangladesh Chemical Industries Corporation
BEPZA	Bangladesh Export Processing Zones Authority
BGTB	Bangladesh Government Treasury Bond
BMET	Bureau of Manpower, Employment and Training
BPC	Bangladesh Petroleum Corporation
BPDB	Bangladesh Power Development Board
BRAC	Bangladesh Rural Advancement Committee
CPI	Consumer Price Index
CSE	Chittagong Stock Exchange
CTG	Caretaker Government
DAE	Department of Agricultural Extension
DAP	Di-Ammonium Phosphate
DF-QF	Duty Free-Quota Free
DSE	Dhaka Stock Exchange
EP	Essential Priority
EPZs	Export Processing Zones
EU	European Union
FAO	Food and Agriculture Organization
FDI	Foreign Direct Investment
FFE	Food for Education
FFW	Food for Works
FPC	Fair Price Card
FY	Fiscal Year
GDP	Gross Domestic Product
IDB	Islamic Development Bank
IFIs	International Financial Institutes
IMF	International Monetary Fund
IMO	International Maritime Organisation
IPOs	Initial Public Offerings
KAFCO	Karnaphuli Fertiliser Co.
LCs	Letter of Credits
LDC	Least Developed Countries
LEI	Large Employee Industries
MoA	Ministry of Agriculture
MoP	Muriate of Potash
MPS	Monetary Policy Statement
NCBs	Nationalised Commercial Banks
NPDA	New Partnership for Development Act
NSD	National Savings Directorate
OMS	Open Market Sale
OP	Other Priority
PDB	Power Development Board
PFDS	Public Foodgrain Distribution System
PKSF	Palli Karma-Sahayak Foundation
RMG	Readymade Garments
RRI	Real Rate of Interest
TSP	Triple Super Phosphate
US$	United States Dollar
VGD	Vulnerable Group Development
VGF	Vulnerable Group Feeding
WTO	World Trade Organisation

STATE OF THE BANGLADESH ECONOMY IN FY2007-08 AND SOME EARLY SIGNALS REGARDING FY2008-09

1. INTRODUCTION

As Bangladesh enters into the second quarter of FY2008-09, a number of challenges confront the economy. The confidence generated through the strong resilience, demonstrated by overcoming the formidable difficulties faced in FY2007-08, has given way to uncertainties originating from global financial crisis and the political transition. FY08 will be remembered for the consecutive floods, cyclone S*idr*, uncertainties with regard to savings and investment as a consequence of some of the steps taken by the Caretaker Government (CTG) and the rise in food prices driving up the inflation. FY08 also saw important institutional reforms which hopefully will leave positive impact on subsequent economic governance. It is encouraging to also note that after considerable uncertainties there are positive developments with regard to transition to democratic governance through free and fair national elections.

Relatively high growth rates with modest levels of inflation have given Bangladesh economy some measures of success in the recent past. High inflationary pressure, with consequent erosion of purchasing power and reversal of poverty alleviation trends, have somewhat weakened those achievements in FY08. Nevertheless, it must be recognised that the Bangladesh economy proved to be quite resilient, posting a 6.2 per cent GDP growth rate inspite of the formidable difficulties. Thanks to higher apparels earnings the industrial sector and exports picked up in the second part of the fiscal year, and agriculture bounced back with a higher *boro* crop thanks to the country's farmers and CTG's timely intervention in the input market. The larger than trend trade deficit was bridged mainly thanks to the high inflow of remittances, which was able to generate even some surplus in the current account. Fiscal surplus was underwritten by higher than trend growth of revenue generation, particularly from the income tax component. Safety net programmes and government's direct interventions in the foodgrains market worked reasonably well at a time of considerably distressed situation facing particularly the low income people, fixed income earners and the middle class. FY09 thus got off with some success in the form of rebounce of the economy, continuing financial inflationary pressure and uncertainties about how the global crisis will evolve.

It is also hoped that the macroeconomic governance in FY09 will be benefited from the large number of institutional reforms carried out by the CTG in 2007 and 2008. Reforms amid at improving transparency and accountability in public administration are expected to improve the quality of public expenditure and efficacy of public service delivery. It is hoped that the newly elected government will further strengthen these reforms and initiate new ones to raise quality of governance in various sectors of the economy.

This paper examines the performance of major macroeconomic variables relating to performance of both the financial and the real economy sectors in FY08. The paper also makes an attempt to capture the signals emanating from the macroeconomic situation emerging from the first few months of FY09.

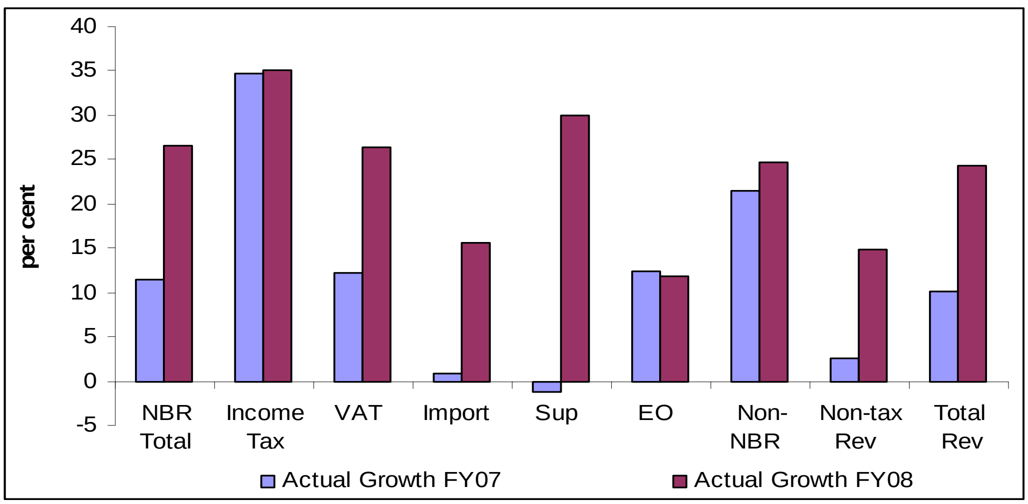
2. PUBLIC FINANCE

2.1. Revenue Receipts

In the context of the 10.1 per cent revenue growth achieved in FY07, growth target for FY08 was set at 22.3 per cent in the original budget. However, this target was later revised upward at 29.2 per cent. According to the revenue data published by the Finance Division, at the end of FY08 total revenue receipt amounted to Tk. 58,170 crore, posting a growth of 24.3 per cent over the Tk. 46,807 crore revenue mobilised during FY07. Albeit lower than the revised growth target, this indicates higher revenue mobilisation than the original target, a first time occurrence in Bangladesh. Revenue-GDP ratio stood at 10.7 per cent in FY08, which was 9.9 per cent in FY07.

Both NBR tax component and non-NBR tax component observed significant growth in FY08. Out of the total revenue mentioned above, NBR component amounted to Tk. 45,777 crore in FY08, which is 26.6 per cent higher than the collection of FY07. The NBR growth was mostly driven by higher income tax collection that increased substantially by 35.2 per cent. Non-NBR tax collection also posted a respectable growth of 24.7 per cent, amounting to Tk. 2,313 crore.

FIGURE 2.1: GROWTH STRUCTURE OF REVENUE EARNINGS IN FY08



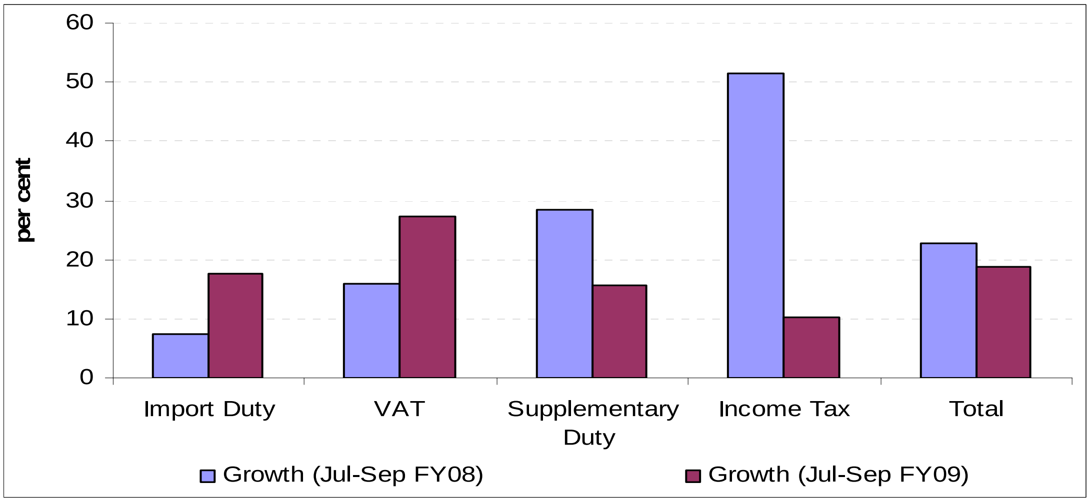
Source: CPD IRBD Database.

Considering the revenue data published by the NBR, the budget for FY09 has set a target for 15.25 per cent growth in NBR revenue collection. However, the growth target comes at 19.06 per cent if we consider revenue data provided by the Finance Division, since Finance Division reported the actual revenue collection by the NBR in FY08 to be Tk 1,512 crore, less than what the NBR had claimed.

According to the latest available figures from the NBR, during the first quarter of FY09 (July-September) NBR achieved 18.76 per cent growth over the corresponding period of FY08. This growth performance is lower compared to the same period of FY08 (22.84

per cent), mostly owing to the slower rise in income tax collection achieved in the first quarter of FY09.

FIGURE 2.2: GROWTH IN NBR REVENUE COMPONENTS IN FY09



Source: CPD IRBD Database.

In comparison to FY08, pace of income tax collection was relatively slow during July-September period of FY09. Only 16.47 per cent of the total target for income tax collection was realised during this period, posting a growth of 10.35 per cent over the corresponding period of FY08. However, income tax collection is likely to be accelerated by the end of October, 2008 bearing in mind the extended deadline for tax return submission till 31 October, 2008 and phase-out of the provision of legalising undisclosed money with 7 per cent penalty on the same date.

Import duty and VAT registered 17.72 per cent and 27.27 per cent growth respectively during the period under consideration. Supplementary duty collection by the NBR during this period also increased by 15.75 per cent.

It is pertinent to mention here that Bangladesh's revenue structure continues to be weak owing to the predominance of indirect tax compared to direct tax, and prominence of revenue earnings from import-related duties within the indirect tax component. There is a need for renewed effort to increase the share of direct taxes, since it is more equity friendly and more attuned to distributive justice.

2.2. Public Expenditure

The double jeopardy of higher international prices and natural calamities throughout the year resulted in increased revenue expenditure of the government during FY08. Even in the context of the actual ADP expenditure for the year being Tk 7,508 crore, lower than the original budget, total public expenditure of the government (Tk 8,4821.1 crore) increased significantly by 41.5 per cent over the actual expenditure of FY07 (Tk 59,932.0 crore).

Although policymakers have expressed concern about increasing regional inequality, and taken some steps to address the issue, public expenditure does not fully reflect this. Recently released district-wise development and non-development expenditure of the government in FY08 shows that the top three hardcore poverty prone divisions (Barisal, Rajshahi and Khulna, according to HIES 2005) had actually received the lowest (Tk 5.8 thousand, Tk 5.6 thousand and Tk 5.0 thousand respectively) per capita government expenditure (combined development and non-development expenditure).

TABLE 2.1: DIVISION-WISE PER CAPITA PUBLIC EXPENDITURE OF THE GOVERNMENT DURING IN FY06-FY08

Division	Lower poverty rate (%)	Per capita public expenditure (thousand Tk)		
	2005	2005-06	2006-07	2007-08
Barisal	***35.6***	***4.5***	***4.5***	***5.8***
Rajshahi	***34.5***	***4.3***	***4.3***	***5.6***
Khulna	***31.6***	***4.1***	***4.2***	***5.0***
Sylhet	20.8	4.5	4.9	6.1
Dhaka	19.9	4.7	5.1	6.2
Chittagong	16.1	5.0	5.1	8.0

Source: Ministry of Finance 2008 and HIES 2005

BBS in a recent survey (2008) showed that according to DCI method Patuakhali and Barguna are the two most poverty prone districts of the country, with 69.2 per cent of the district population having been identified as poor. Based on the district-wise expenditure information of the government, these two districts belong in the list of three districts (including Bhola) of Barisal division (the most hardcore poverty prone division) that received the lowest per capita revenue expenditure in FY08.

Revenue Expenditure

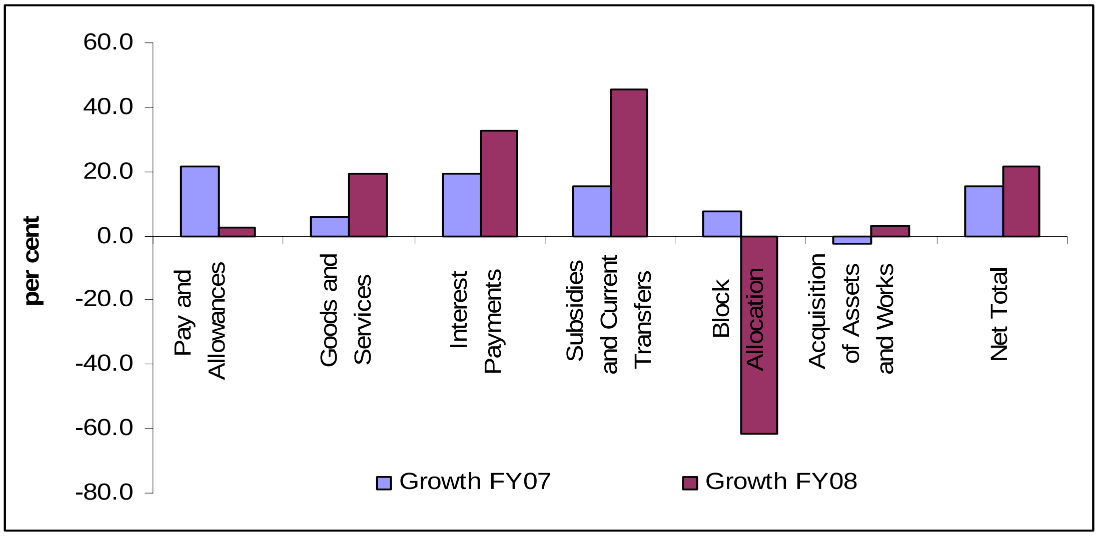
According to the expenditure figures published by the Finance Division, revenue expenditure increased by 21.7 per cent during FY08 over the corresponding figure of the previous year, amounting to Tk. 51,435.6 crore. The original growth target for the fiscal year was of 19.0 per cent and the revised growth target was set at 22.8 per cent. Expenditure was, thus, somewhat lower than the revised target, but higher than the original. The structure of revenue expenditure by the government in FY08 was characterised by high growth in subsidies and interest payments.

Among the major three heads that accounted for 82.9 per cent in the total actual revenue expenditure, “subsidies and transfers” and “interest payments” registered high growths during FY08, with 45.2 per cent and 32.5 per cent rise respectively. “Salary and allowances” on the other hand posted a rise of only 2.7 per cent.

Revenue expenditure data for FY08 shows significant rise in subsidies, by 97.8 per cent. It was because of the substantial rise in price of petroleum products, fertiliser and food in the international market. Expenditure on interest payments increased by 32.5 per cent in

FY08 over the expenditure of FY07. The high growth in interest payment creates concern over the growing deficit budget that was experienced over the past few years.

FIGURE 2.3: GROWTH OF REVENUE EXPENDITURE BY ECONOMIC CLASSIFICATION FY07 & FY08 (JUL-JUN)



Source: CPD IRBD Database.

The budget for FY09 allocated Tk 13,641 crore as subsidy. Major sources of this significant allocation for subsidy were for food, fertiliser and fuel. However, since the time when the national budget was prepared, fuel price in the international market has decresed to a significant extent. Having reached the highest level of USD147/barrel in July 11, 2008, crude oil price has fallen below USD70, in October, 2008. Even though the OPEC is considering a production cut to stabilise price (a reduction of 1.5 million barrels/day), crude oil price is expected to hover around USD70-80 in the near future. Along with the lower fuel prices, in view of the financial crisis, commodity prices in the international market including food and fertiliser could decline further. Therefore, the government may experience a lower than projected revenue expenditure by the end of the fiscal year, particularly on subsidy payment.

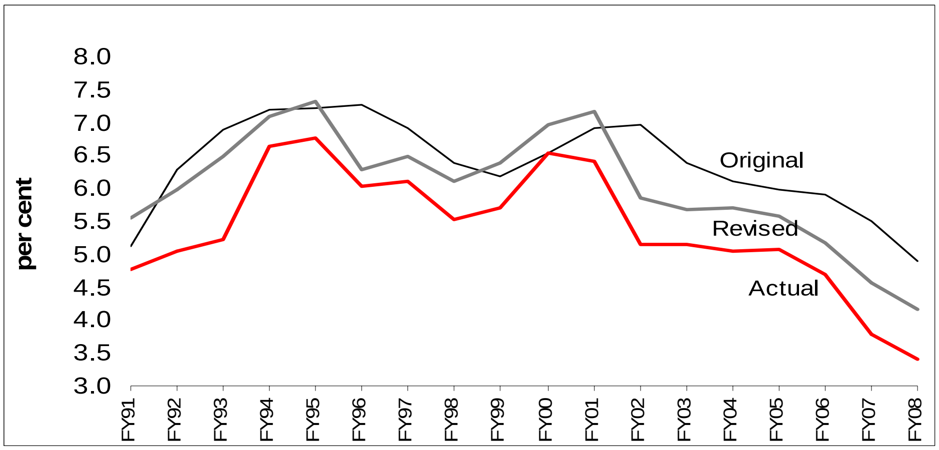
With about 50 per cent fall in fuel prices in the international market, since the last upward fuel price adjustment, the government is considering lowering fuel prices in the domestic market. In doing so, the need for subsidised diesel in securing higher agricultural output in order to ensure food security and taming the inflation, needs to be kept in mind. However, policymakers will need to subsidise diesel and kerosene; thus, the fall in price of petrol/octane will not be passed to the retail/customer level in its entirety.

Annual Development Programme (ADP)

ADP implementation performance remained more or less same in FY08 as compared to the previous years. While the size of the ADP was revised downward by 15.1 per cent, from Tk. 26,500 crore to Tk. 22,500 crore, actual implementation stood at Tk. 18,492 crore, which was 82 per cent of the revised ADP. This was 83 per cent in FY07 and 91 per cent in FY06. Apart from the higher revenue expenditure requirements and rising cost of inputs that made the contractors demand a review of cost estimations, risk aversion and fear psychosis have played its role in the lower ADP achievement of FY08.

Actual ADP as a percentage of GDP stood historically low at 3.4 per cent in FY08, which was 3.8 per cent in FY07. Under-implementation of ADP, with subsequent negative implications for growth, employment and social welfare continues to remain a nagging problem in Bangladesh.

FIGURE 2.4: ADP AS A PERCENTAGE OF GDP DURING FY91-FY08



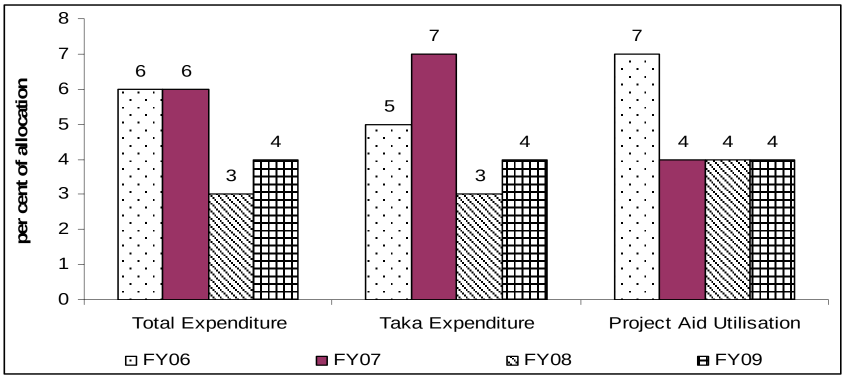
Source: CPD IRBD Database.

New ADP target for FY09 has been set at Tk. 25,600 crore. This is 13.8 per cent higher than the revised ADP and 38.4 per cent higher than the actual ADP of FY08. However, the new ADP is also 3.4 per cent lower than the original ADP of FY08; a unique feature. Perhaps the idea was to give more emphasis on quality. However, in such an investment starved situation as in Bangladesh, both quantity and quality aspects need to be perceived as equally important.

Recently released figures by the IMED (Implementation, Monitoring and Evaluation Division) for July-August period of FY09 shows the similar slow start in ADP implementation, as has been the case in the previous years, with only 4 per cent of the of the total allocation spent during these two months.

Taka release as a percentage of Taka allocation stood lower at 16 per cent during the initial two months of FY09, compared to 22 per cent of FY08. Actual spending of the Taka component stood at 4 per cent of the released amount, which was somewhat higher compared to FY08 (3 per cent).

FIGURE 2.5: ADP IMPLEMENTATION DURING JULY-AUGUST PERIOD IN FY06-FY09



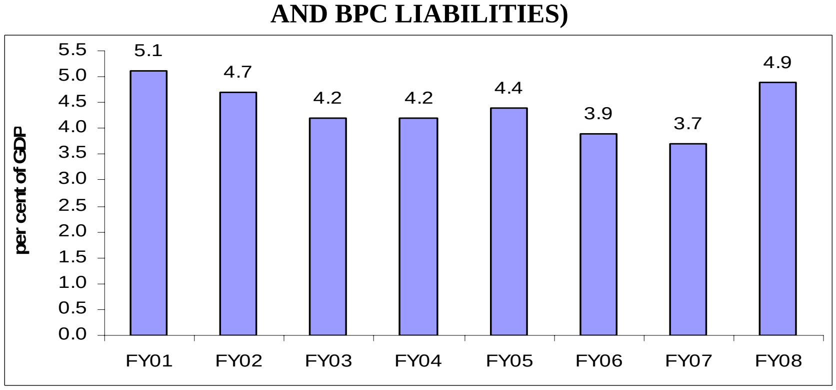
Source: CPD IRBD Database

The slow start of ADP implementation in FY09 will be of particular concern since the upcoming election and settling down of the new government is also likely to result in further slowdown of ADP implementation in the second and perhaps third quarter of the current fiscal year. It will be a major challenge for the upcoming government to maintain a satisfactory level of ADP implementation in FY09, both in its quantitative and qualitative terms.

2.3. Budget Deficit and Financing

Excluding grants and BPC liabilities, national budget for FY08 projected a Tk. 22,313 crore deficit in FY08 (4.2 per cent of the GDP). However, actual deficit at the end of FY08 stood at Tk. 26,650.9 crore against a deficit of Tk. 13,125.4 crore experienced during FY07. This indicates a substantial growth in deficit by 103.0 per cent in FY08. Deficit as percentage of GDP stood at 4.9 per cent against the original target of 4.2 per cent.

FIGURE 2.6: BUDGET DEFICIT AS PER CENT OF GDP (EXCLUDING GRANTS AND BPC LIABILITIES)



Source: CPD IRBD Database.

In financing the deficit, the government had to mostly rely on the banking sector (173.3 per cent growth) since the availability of credit from non-bank financing was low, probably owing to the anti-corruption drive that resulted in a fall in the sale of NSD certificates and also shifted towards the equity market.

TABLE 2.2: GROWTH IN DEFICIT AND SOURCES OF FINANCING DURING JULY-JUNE OF FY2007 AND FY2008

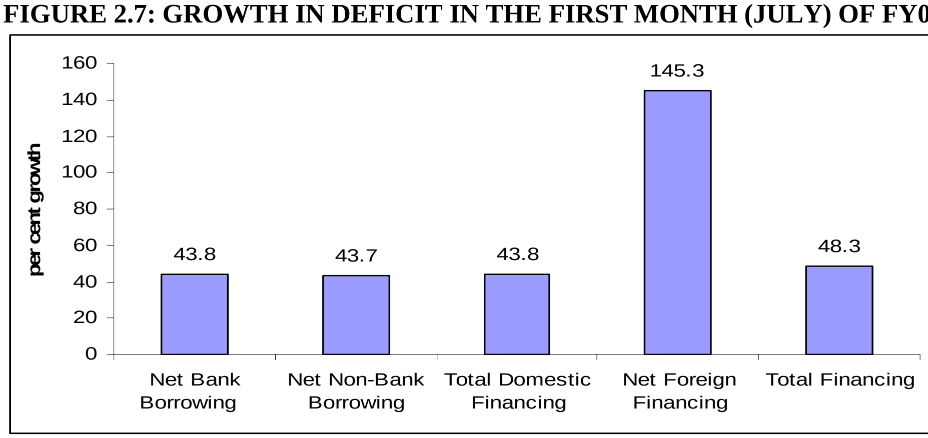
(Crore Taka)

	FY07			FY08			
	Budget	Revised Budget	Actual	Budget	Revised Budget	Actual	Growth in Actual
Net Foreign Financing	**8364.4**	**7332.5**	**2790.0**	**10560.2**	**13144.2**	**7775.5**	178.7
Grant	2508.0	2150.0	1037.4	4255.0	4388.2	2007.4	93.5
Loan	9618.0	9047.5	5743.7	10403.0	13024.4	10137.7	76.5
Amortisation	3761.6	3865.0	3991.1	4097.8	4268.4	4369.5	9.5
Domestic Financing	**8896.8**	**10088.3**	**10335.4**	**11808.8**	**12452.1**	**18875.4**	82.6
Non-Bank Borrowing	3400.0	3500.0	4282.6	4500.0	2002.0	2501.4	-41.6
Bank Borrowing	5434.0	6531.0	5982.3	7253.0	10398.0	16349.3	173.3
Sale of Assets	62.8	57.3	70.6	55.8	52.1	24.7	-65.0
Total Financing	**17261.2**	**17420.8**	**13125.4**	**22369.0**	**25596.2**	**26650.9**	103.0
Total Financing as % GDP	**3.7**	**3.7**	**2.8**	**4.1**	**4.7**	**4.9**	

Source: CPD IRBD Database

According to the latest available information, deficit experienced 43.8 per cent growth in the first month (July) of FY09. Both bank borrowing and non-bank borrowing shows high growth during this month (43.8 per cent and 43.7 per cent respectively). However, in financing the deficit, commendable success has been achieved in mobilising foreign resources with net foreign financing growth of 145.3 per cent, taking its share to 7.4 per cent in the total financing of the first month, up from 4.5 per cent in July, FY08. With the commitment of the World Bank for the highest ever financial support to Bangladesh, for the current fiscal year, in the amount of USD1.34 billion and with the already signed deal of USD165 million from the Asian Development Bank (ADB), so far the availability of foreign resources to finance the projected Tk 30,580 crore deficit for the fiscal year looks promising, despite the worries regarding the global financial meltdown and resultant bailout plans, which was likely to have negative impact on global aid flow in FY09.

FIGURE 2.7: GROWTH IN DEFICIT IN THE FIRST MONTH (JULY) OF FY09



Source: CPD IRBD Database

Expected lower than projected subsidy demand in FY09, resulting from both lower oil price and international prices of food and fertiliser may provide the upcoming government a breathing space in terms of deficit financing. An effort is needed to bring back confidence among the investors in government savings certificates in order to increase the share of non-bank sources in financing the deficit, considering the comparatively higher inflationary effect of borrowing from the banking sector.

3. MONETARY SECTOR

In view of the global financial crisis, in addition to the already high inflation rate, Bangladesh will need to face the challenge of following a monetary policy which can ensure adequate liquidity in the banks and generate economic activities in order to alleviate poverty and accelerate economic development. A prudent monetary policy is critical at the moment to deal with any possible adverse impact of the ongoing global financial crisis. Such a policy is needed in order to ensure appropriate and timely resource allocation through the banking and financial institutions of the country.

The Bangladesh Bank (BB) has embarked upon pursuing a transparent monetary policy through its Monetary Policy Statement (MPS), which has been in place since January 2006. The MPS of the BB for the period July-December 2008 “aims at using the monetary policy for ensuring reasonable price stability essential to sustaining high economic growth, shielding the economy from global price and financial turbulences and downside risks, and tapping new upside opportunities” (Monetary Policy Statement, Bangladesh Bank, July 2008).

As a response to the current financial crisis the BB will need to fashion its monetary policy in a manner that keeps the economic activities vibrant. As a matter of fact, the BB has been pursuing an accommodative policy in view of domestic and global economic developments, and has resisted the repetitive suggestion of the International Monetary Fund (IMF) to raise interest rate and follow a contractionary monetary policy. It is expected that the BB will follow an independent monetary policy to control inflation and stimulate investment as always, keeping in view the domestic and global realities. However, in very recent times, the BB has raised the repo rate to somewhat discourage credit expansion (from 8.50 per cent in August, 2008 to 8.60 per cent in September 2008. Reverse repo rate remained same over this period at 6.50 per cent).

A brief overview of the trends of some of the major variables in the monetary sector during the FY08 is presented below to understand the recent dynamics in the sector.

3.1 Demand and Time Deposits

Striking a balance between high inflation and interest rate has always been a challenge for the BB while devising a monetary policy. The long term interest rates have either declined or remained the same over the years. For example, interest rates on 5-year and 10-year Bangladesh Government Treasury Bond (BGTB) have declined, while the interest rate on National Savings Directorate (NSD) certificates remained same in June 2008, compared to December 2007 (Table 3.1). This implies that the real rate of interest (RRI) has declined in the face of high inflation. This has been a disincentive to the depositors who are currently shifting towards the capital market instead of saving in NSD certificates. As a matter of fact, net sale of NSD certificates during July-June FY08 was 39.68 per cent lower compared to July-June FY07, while total sale was 6.73 per cent less during the same period (Table 3.2).

Deposits increased by 16.90 per cent during FY2008 compared to FY07. Of this, Demand Deposits (DD) increased by 15.46 per cent and Time Deposits (TD) by 17.11 per cent during this period. A comparison between July 2008 and July 2007 shows that DD increased by 11.18 per cent and TD by 18.21 per cent. The increase in TD implies that even with high inflation rate, the opportunity cost of holding money in these instruments is still attractive.

The RRI has been declining on all deposits. For example, the RRI in June 2008 was only 0.66 per cent on 5-year BGTB, 1.78 per cent on 10-year BGTB, 1.56 per cent on 3-year NSD certificate and 2.06 per cent on 5-year NSD certificate. Such low interest rate has made savings instruments such as NSD less attractive and led private savers to move towards other forms of investment, such as the capital market. The heated capital market during FY08 is the reflection of such moves. Table 3.1 shows the weighted average interest rates and real interest rates of various savings instruments.

TABLE 3.1: WEIGHTED AVERAGE INTEREST RATE OF GOVERNMENT LONG TERM T-BILL/BONDS AND INFLATION

	BGTB		NSD		Inflation Rate (12 month average)	Real Rate of Interest on			
Period	**5-Year**	**10-Year**	**3 Year**	**5-Year**		**5-Year BGTB**	**10-Year BGTB**	**3-Year NSD**	**5-Year NSD**
June 2004	8.00	10.00	10.50	11.00	5.83	2.17	4.17	4.67	5.17
June 2005	8.75	9.93	10.00	10.50	6.49	2.26	3.44	3.51	4.01
June 2006	10.60	12.09	10.00	12.00	7.16	3.44	4.93	2.84	4.84
June 2007		12.14	11.50	12.00	7.20		4.94	4.30	4.80
December 2007	10.65	11.73	11.50	12.00	9.11	1.54	2.62	2.39	2.89
March 2008	10.60	11.72	11.50	12.00	10.00	0.60	1.72	1.50	2.00
June 2008	10.60	11.72	11.50	12.00	9.94	0.66	1.78	1.56	2.06

Source: Monetary Policy Department, Bangladesh Bank.

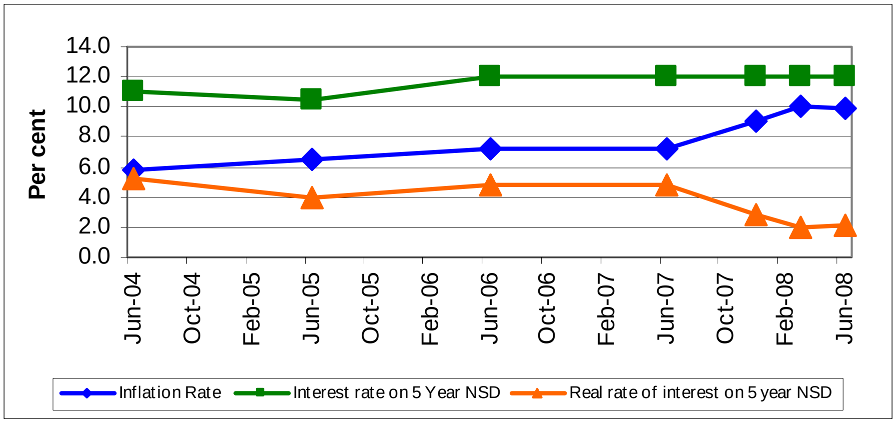
TABLE 3.2: SALE AND REPAYMENT OF NSDS

(In Crore Tk)

Period	Sale	Repayment	Net Sale	Outstanding at the end period
Jul - Jun’ 2006-07	15123.53	10948.61	4174.92	43639.18
Jul - Jun’ 2007-08	14105.79	11587.50	2518.29	46157.47

Source: Bangladesh Bank.

FIGURE 3.1: REAL RATE OF INTEREST



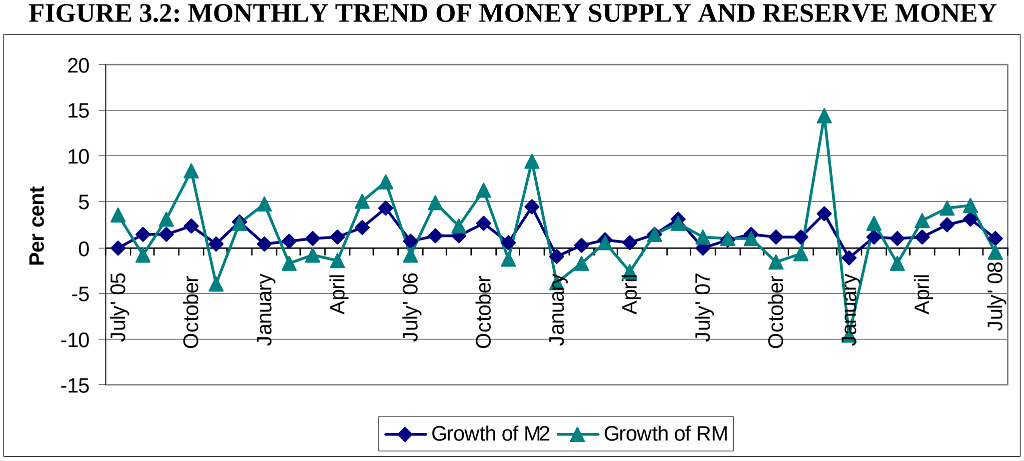
Source: Bangladesh Bank.

3.2. Money supply, reserve money and liquidity

There has been an upward trend in case of *Broad Money Supply (M2)* during the FY08. M2 has posted a rise of 18.64 per cent as of end July 2008 compared to July 2006 (Figure 3.2). This growth has been due to growth in the domestic credit by 21.61 per cent during July 2007 and July 2008. Due to increased remittance flow, Net Foreign Assets (NFA) has continued to increase in recent times. During July 2007 and July 2008, NFA increased by 13.98 per cent. Net Domestic Assets (NDA) has also experienced an increase of 19.51 per cent during July 2007 and July 2008.

Reserve Money (RM) recorded a decrease of 0.57 per cent (Tk. 300.70 crore) in July 2008 compared to the increase of 1.18 per cent (Tk. 520.90 crore) in July 2007. However, RM registered a rise of 16.45 per cent as of end July 2007 compared to July 2006. The money multiplier (M2/RM) increased to 4.79 at the end of July 2008 compared to 4.70 in July 2007.

FIGURE 3.2: MONTHLY TREND OF MONEY SUPPLY AND RESERVE MONEY



Source: Bangladesh Bank.

The scheduled banks had an excess liquidity of Tk. 11,221.43 crore as of end July 2008 which is lower compared to Tk. 14,279.42 crore as of end June 2007. This is reflected in attempts at undertaking deposit collection drive on the part of some commercial banks through offering of competitive interest rates on long term deposits. Banks are borrowing from the call money market at a high interest rate for their day-to-day operations.

In order to ease the liquidity crisis, the government has also started to inject money in the economy. The government had earlier withdrawn an amount of Tk. 5,000 crore in FY08 from the banking sector, through primary dealers (by way of sale of treasury bills to nationalised banks and a few commercial banks) for government's use, and to control inflation by reducing the money supply in the market. However, this has raised the call money rate, which sometimes reaches as high a level as 15 to 20 per cent. The government is now trying to keep the call money rate around 8 to 8.5 per cent and has recently injected Tk. 1,000 crore to this end. The weighted average call money rate in the inter-bank money market was 9.92 per cent in September 2008.

The reasons behind a decline in excess liquidity could be the following. *First,* private sector credit has increased to some extent (Section 3.3). *Second,* due to anti-corruption drive since January, 2007 black money is out of the banking system. *Third,* due to high inflation rate and high commodity prices, the middle income group is using their savings to cope with high cost of living. *Fourth,* because of anti-corruption drive and low interest rate on deposits, both large and small depositors have invested in the capital market which is reflected through 71.45 per cent increase of market capitalisation during August, 2007 and 2008. The increase was 122.87 per cent during August, 2006 and 2007.

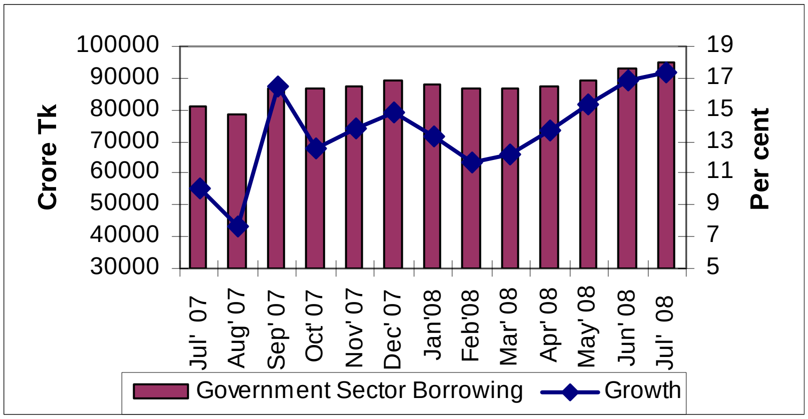
3.3. Domestic credit

Total domestic credit increased by 21.61 per cent (Tk. 44,784.40 crore) during July 2007-July 2008 against the increase of 14.41 per cent (Tk. 26,099.9 crore) during July 2006-July 2007. The rise in domestic credit is due to the rise of private sector credit and public sector credit. Private sector credit experienced an increase of 24.38 per cent (Tk. 41,545.6 crore) during FY08. Domestic credit to the public sector experienced an increase of 7.86 per cent (Tk. 4,274.3) in the same period. On the other hand, credit to other public sectors declined by 32.51 per cent (Tk 4,395.4) during FY08.

Government sector borrowing

There has been an increase in government sector borrowing which comprises of bank borrowing plus non-bank borrowing. The increase was 17.34 per cent during July, 2007 and July, 2008. In July, 2008 government sector borrowing was Tk. 95,063.31 crore, of which, banking sector contributed 51 per cent and the remaining from non-banking sector. Outstanding borrowing of the government through NSD certificates as of end July, 2008 stood at Tk. 46,578.71 crore, recording an increase of Tk. 2,687.43 crore or 6.12 per cent, against Tk. 43,891.28 crore as of end July, 2007. The volume and growth of the government sector borrowing are shown in Figure 3.3.

FIGURE 3.3: GOVERNMENT SECTOR BORROWING

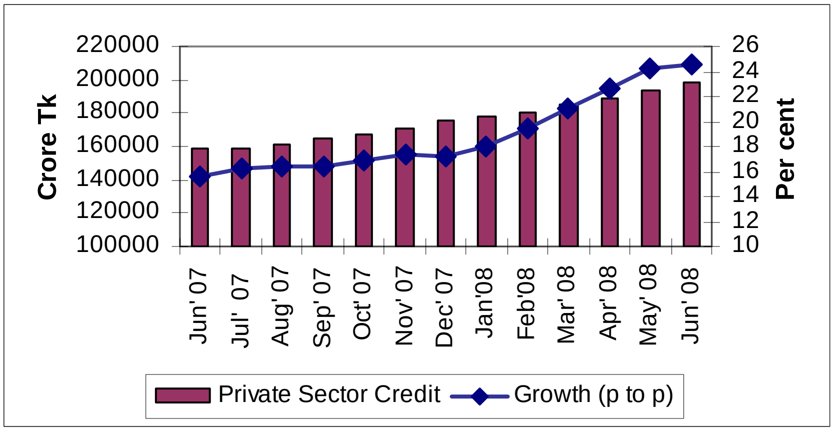


Source: Bangladesh Bank Economic Trends.

Private sector borrowing

The private sector demand experienced a decline in the beginning of the FY08, partly due to uncertainty and fear created in view of the changed governance framework and anti-corruption drive pursued by the interim government. The situation started to improve gradually with renewed activities in the economy, which was reflected in strong growth of the private sector credit during FY08. In FY08 total outstanding domestic credit to the private sector posted an increase of 24.52 per cent over FY07. Within total credit to the private sector, 92.45 per cent came from the banking sector while the rest came from the Non-Bank Depository Corporations (NBDCs).

FIGURE 3.4: PRIVATE SECTOR BORROWING



Source: Bangladesh Bank Economic Trends.

3.4. Industrial loan

Compared to the corresponding period of FY07, disbursement of industrial term loan during April - June 2008 recorded a significant 54.11 per cent growth. Overall recovery of the term loan also posted a significant growth of 48.59 per cent during the reported period (Table 3.3). Disbursement of industrial term loans during FY08 was 62.58 per cent higher than that of FY07. The high disbursement can be related to higher investment which can also be observed through growth in industrial credit, and working capital financing through the private sector. On the other hand, recovery of industrial term loans during FY08 was 49.47 per cent higher than that of FY07, implying that overdue loan as percentage of the total outstanding has increased. The amount of overdue industrial term loans at the end of June 2007 stood at Tk. 4,970.42 crore and overdue as percentage of outstanding industrial term loans was 12.40 per cent at the end of June 2008.

TABLE 3.3: INDUSTRIAL CREDIT

(In Crore Tk)

Period	2007-08		2006-07	
	Disbursement	Recovery	Disbursement	Recovery
July-September	3784.76	2625.19	2660.34	1740.93
October-December	5878.47	3311.45	3204.46	2393.95
January-March	4911.08	3700.03	2911.39	2297.10
April- June	5576.51	3917.53	3618.59	2636.47

Source: Agricultural Credit & Special Programme Department, Bangladesh Bank.

3. 5. Loan default scenario

Total classified loan as on March, 2008 was Tk. 23,838.28 crore. Total classified loan increased by 12.32 per cent as on March, 2008 compared to the corresponding period of the previous year. Except for the Development Finance Institutions (DFIs), no banks were able to make any progress in reducing classified loans. The increase in classified loan was 17.12 per cent for the State owned Commercial Banks (SCBs), 96.03 per cent for Foreign Banks (FBs) and 19.05 per cent for Private Commercial Bank (PCBs). However, the DFIs made an impressive progress in reducing the total classified loan recording negative growth rate of (-) 11.90 per cent as of March, 2008 from the corresponding time of the previous year (Table 3.4).

The negative performance in loan recovery is partly due to the anti-corruption drive which put several businessmen behind the bar and led many to flee from the country. Since the corporate governance of most of the companies in Bangladesh is weak with heavy dependency on particular individuals, business has been experiencing a downturn trend due to the cleansing operation. Many of these companies are not being able to service their respective loans. Also due to the fear factor among the businessmen there was very limited investment during the beginning of the FY08 leading to weak performance of their business which in turn could have had an impact on the loan default scenario.

TABLE 3.4: CLASSIFIED LOAN

(In Crore Tk)

Bank Type	*As on March' 07*	*As on March' 08*	*Growth in 08 compared to FY07*
SCBs	12134.81	14212.56	17.12
PCBs	4826.86	5746.16	19.05
FBs	115.80	227.00	96.03
DFIs	4145.80	3652.56	-11.90
Total	**21223.27**	**23838.28**	**12.32**

Source: Banking Regulation and Policy Department, Bangladesh Bank.

3.6. Agricultural credit

The BB has directed all nationalised and private commercial banks to increase disbursement, of agricultural credit in order to increase agricultural production in view of global food crisis, and the loss of domestic production due to flood and cyclone in 2008. The emphasis of the BB was reflected in increased disbursement of agricultural credit by the Nationalised Commercial Banks (NCBs), Specialised Banks, Bangladesh Rural Development Board (BRDB) and Bangladesh Samabya Bank Limited (BSBL). This increased disbursement is also due to the directive of the BB to the private commercial banks to increase the disbursement of agricultural credit. Table 3.5 shows the monthly disbursement and recovery of agricultural credit.

TABLE 3.5: AGRICULTURAL CREDIT POSITION

(In crore taka)

Month	Disbursement	Recovery
August ’07	264.32	211.07
September	655.79	853.65
October	636.09	493.93
November	834.91	490.73
December	1271.06	845.77
January ’08	624.56	576.03
February	992.88	411.1
March	770.66	353.66
April	416.57	532.81
May	803.47	410.71
June	1045.84	619.8
July	405.73	660.08
August	566.56	308.74

Source: Agricultural Credit & Special Programme Department, Bangladesh Bank.

Disbursement and recovery of agricultural credit in August, 2008 was Tk. 566.56 crore and Tk 308.74 respectively, compared to Tk. 264.32 crore and Tk 211.07 in August, 2007. The month-wise disbursement and recovery scenario is somewhat different, however. Since June, 2008 both disbursement and recovery of agricultural credit have been declining (Table 3.5). This is a bit worrisome in view of the fact that increased food production is essential for food security. The position of overdue agricultural credit as percentage of total outstanding loans has improved. It has decreased from 43.71 as recorded at the end of August, 2007, to 35.75 at the end of August, 2008 (Table 3.6).

TABLE 3.6: AGRICULTURAL CREDIT POSITION FOR OVERDUE AND OUTSTANDING LOANS

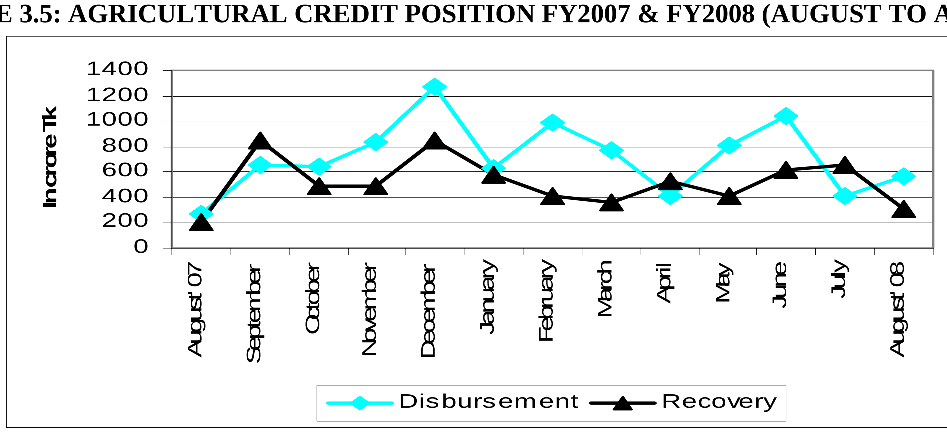
(*In crore Taka*)

Year	2008- 2009 *P*			2007-2008 *R*		
End-Month	Overdue	Outstanding	Overdue as % of outstanding	Overdue	Outstanding	Overdue as % of outstanding
August	6299.01 (-5.60)	17620.00 (+15.42)	35.75	6672.75 (+0.98)	15265.36 (+1.72)	43.71

Source: Agricultural Credit & Special Programme Department.
Note: *P* = Provisional; *R* = Revised

Though private banks have also initiated programmes for disbursing agricultural credit, the effort is still very limited. Private banks are lending to the agriculture sector in two ways. *First,* following the model of the Indian ICICI Bank's *Para Banking* (which has in fact been developed on the basis of the Grameen Bank model blended with the Indian reality), a number of private banks have come to an agreement with some large non-government organizations (NGOs) such as BRAC, ASA and TMSS to disburse agri-loan through them. They are now finding out that agriculture credit can also be profitable. Such arrangements have been made in view of the fact that these NGOs have infrastructural and institutional set up in the rural areas, and it is not always financially viable for the banks to establish a new set up in the remote areas. *Second*, under a tripartite arrangement among the government, private banks' and NGOs' credits are being disbursed in the agriculture sector. Currently, a pilot project is being implemented through two private banks – Eastern Bank Ltd and BASIC Bank. The Asian Development Bank (ADB) has provided a fund of USD42 million to the Ministry of Finance (MoF) for this. The government has disbursed USD36 million to these two private banks at 3.5 per cent interest rate. The private banks are lending these funds to the aforesaid three NGOs at 7 per cent interest rate.

FIGURE 3.5: AGRICULTURAL CREDIT POSITION FY2007 & FY2008 (AUGUST TO AUGUST)

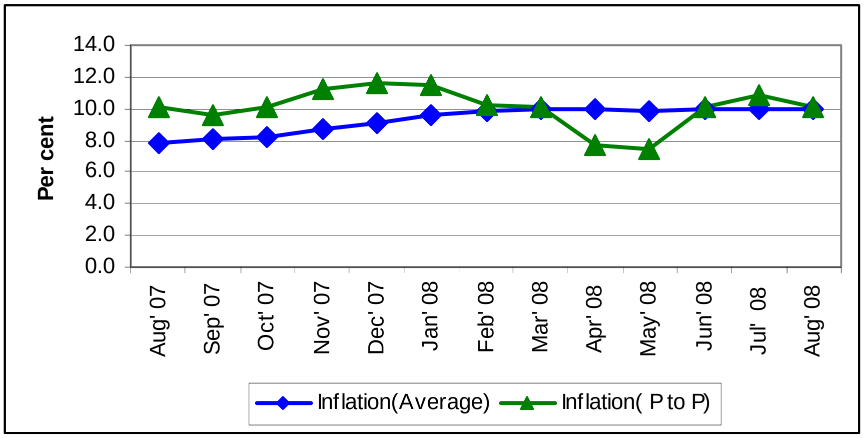


Source: Bangladesh Bank Agricultural Credit & Special Programme Department.

3.7. Consumer price inflation

National CPI: The annual average rate of inflation (12-month annual average CPI, 1995-96 = 100) increased to 10.00 per cent in August, 2008 from 7.78 per cent in August, 2007. The increasing trend continued till March, 2008 when it reached 10.0 per cent. It had declined slightly during April-June 2008. Higher inflation is due to higher domestic price of food and higher global commodity prices. However, as food comprises about 59 per cent of total CPI in Bangladesh, higher domestic food prices is the dominant factor for high inflation (Figure 3.6).

FIGURE 3.6: CPI INFLATION

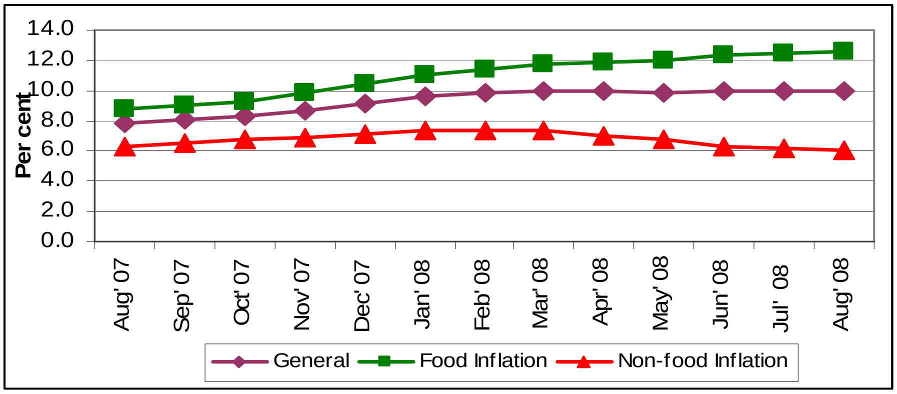


Source: Bangladesh Bureau of Statistics.

Urban and rural Inflation: Both rural and urban consumers have been feeling the heat of high prices. The point-to-point (P to P)inflation rate in rural areas in August, 2008 was 10.51 per cent, an increase from 10.07 in August 2007. The food price inflation rate was 12.34 per cent while non-food price inflation rate was 7.05 per cent in August 2008. The point-to-point inflation rate in urban areas in August, 2008 was 9.11 per cent, compared to 10.24 in August, 2007. The urban food and non-food price inflation rates were 12.40 per cent and 5.20 per cent respectively in August, 2008.

Food and non-food Inflation: At the end of August, 2008, food and non-food inflation rates on a point-to-point basis were 12.36 per cent and 6.55 per cent respectively, compared to 11.62 and 7.99 respectively in August, 2007. On the other hand, food inflation rate on the basis of 12-month average increased from 8.80 per cent in August, 2007 to 12.56 per cent in August, 2008. Non-food inflation rate decreased from 6.29 per cent to 6.01 per cent during the same period (Figure 3.7).

FIGURE 3.7: GENERAL, FOOD AND NON-FOOD INFLATION (12 MONTH AVERAGE)



Source: Bangladesh Bank Quarterly (January to March).

Global price scenario: As opposed to an unprecedented increase of commodity price during the FY08, the prices have recently taken a downward in the face of global financial crisis. Except for soyabean oil, prices of all other major commodities including rice, wheat and crude oil suffered a falling price since September 2008.

Prices of rice (from Thailand 5 per cent parboiled) declined to USD686.3 per metric tonne in September, 2008 from USD855 per metric tonne in April, 2008. Crude oil price touched a record low of USD64.15 per barrel on 26 October, 2008 from USD131 per barrel on 29 May 2008. Similar trend was observed in case of wheat. However, prices of soyabean oil jumped to USD1,227 per metric tonne in September, 2008 from USD425.0 per metric tonne in February, 2008 (Table 3.7).

TABLE 3.7: GLOBAL PRICE OF SOME IMPORTANT COMMODITIES

Period	Rice USD/mt
	Thailand 5 % parboiled
April 2007	324
April 2008	855
September 2008	686.3
	Crude oil USD/barrel
18 May 2007	63.92
29 May 2008	131
26 October 2008	64.15
	Soyabean oil USD/mt
March 2007	199.1
February 2008	425.0
September 2008	1227
	Wheat USD/mt
Jul-Sep 2007	309.0
Jan-Mar 2008	621.7
Jul-Sep 2008	390.2
July 2008	400.7
August 2008	400.8
September 2008	369.1

Source: World Bank - The Pink Sheet, www.bloomberg.com/energy, www.eia.doe.gov, www.ers.usda.gov.

Regional inflation: High inflationary trend was also observed in South Asian countries. The point-to-point inflation was 12.1 per cent in India and 24.9 per cent in Sri Lanka in August, 2008, compared to 7.9 per cent and 28.1 per cent in India and Sri Lanka respectively in March, 2008. In Pakistan, inflation rate was 25.3 per cent in August, 2008. Table 3.8 shows a comparison of inflation rates at various points of time.

TABLE 3.8: REGIONAL COMPARISON OF INFLATION (POINT TO POINT)

Period	Bangladesh	India	Pakistan	Sri Lanka
December' 06	6.1	6.6	8.9	19.3
December' 07	11.59	5.9	8.8	16.4
March' 08	10.06	7.9	14.1	28.1
July' 08	10.82	12.0	24.3	26.6
August' 08	10.11	12.1	25.3	24.9

Source: Bangladesh Bank, http://www.sbp.org.pk, http://www.statistics.gov.lk/.

Impact of inflation on real income: **I**nflationary pressure during the last several months has had an adverse impact on the consumers through reduction of their purchasing power due to and income erosion. High inflation, particularly high food inflation, has particularly affected the poor and people in the fixed income group. *A CPD estimate shows that those below the poverty level of income experienced an income erosion of 36.7 per cent during January, 2007 to March, 2008.* This section of the population spends 45.6 per cent of their income on rice alone. Given the increase of rice price by 66.9 per cent during January, 2007 and March, 2008 income erosion, due only to price hike of rice, was about 30.5 per cent. For the remaining 54.4 per cent expenditure, income erosion would be to the tune of 6.2 per cent, if only the overall inflation rate is considered. Indeed, most of the workers in the manufacturing and other sectors whose income level is very low, are experiencing considerable income erosion. If wages of the lower income groups are adjusted against this inflationary trend, real wage would be much lower. For example, monthly wages of the workers in grades 5, 6 and 7 in the ready made garments (RMG) sector have been fixed at Tk 2,046, Tk 1,851 and Tk 1,662.5 respectively at the time of the last minimum wage review. Taking into account an average income erosion of 36.7 per cent, the real wages come down to Tk 1,295, Tk 1,172 and Tk 1,052 for workers belonging to the respective grades per month.

The CPD estimates also show that even when the increase in cumulative Gross National Income (GNI) is considered (between 2005 and 2008), given the price hike (particularly taking into consideration of the weighted inflationary impact of price of rice), an additional 8.5 per cent people have fallen below the poverty line in recent times because of high inflation (taking Household Income and Expenditure Survey data for 2005 as reference point). *This would mean that as high as an additional 2.5 million households could have fallen below the poverty line in terms of real income.* The Public Food Distribution System (PFDS) and other safety net programmes of the government, covering about 10 million people have helped to mitigate the food deprivation of people below the hardcore poverty line.

3.8. Interest rate

In view of high spread between lending and borrowing rates, interest rate has been an contentious issue as far as business and banking community were concerned. This conflict of interest has persisted for quite some time now. The BB has already directed the major commercial banks to reduce the interest rate spread and reduce their lending rates. There has been an agreement recently to fix the highest lending rate at 14.0 per cent.

Private commercial banks feel that given the high cost of funds and high risks of lending in Bangladesh, any further reduction in the lending rate is not feasible. Moreover, a lower lending rate calls for a lower deposit rate which will discourage savers to keep money in the bank and thus, create liquidity crisis. This, in turn, will have an impact on the overall economy. However, the business community is still pursuing for a higher cut in the lending rate. This demand is being voiced afresh by the business community in view of the global meltdown of financial markets.

Ensuring better returns on deposits would be one way to improve the liquidity situation. The lending rate (calculated on a quarterly basis) of scheduled banks was 12.29 per cent in June, 2008 as compared to 12.75 per cent in December, 2007. Their deposit rate (also calculated on a quarterly basis) stood higher at 6.95 per cent in June, 2008 as compared to 6.77 per cent in December 2007 (Table 3.9 and Figure 3.8).

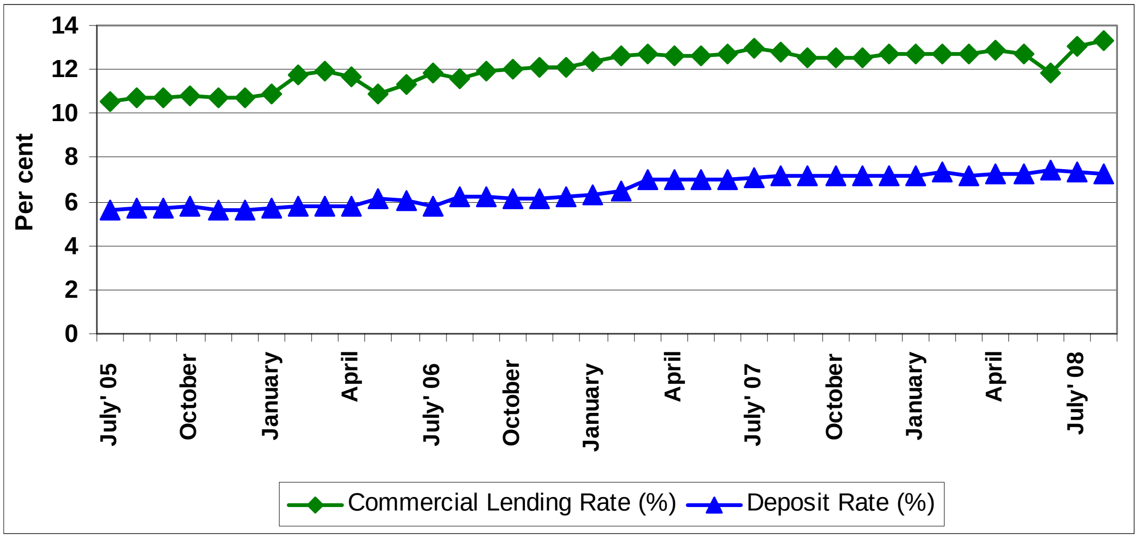
The BB has to strike a balance here as the demand for liquidity in the banks has to be ensured to tackle the financial crisis. The problem of spread between banks' lending and deposit rates in Bangladesh owes also to some other factors. A study by the BB pointed out that the spread is relatively high in Bangladesh because of inefficiencies, market segmentation and lack of competition (Bangladesh Bank, Policy Analysis Unit, May 2008).

TABLE 3.9: WEIGHTED AVERAGE OF INTEREST RATES

Period	Lending rate	Deposit rate	Call money rate
December 2004	10.83	5.56	7.62
December 2005	11.25	5.90	8.40
December 2006	12.60	6.99	7.16
December 2007	12.75	6.77	9.37
June 2008	12.29	6.95	9.90
September 2008			9.92

Source: Bangladesh Bank.

FIGURE 3.8: MONTHLY TREND OF LENDING AND DEPOSIT RATES



Source: Bangladesh Bank.

3.9. Exchange rate

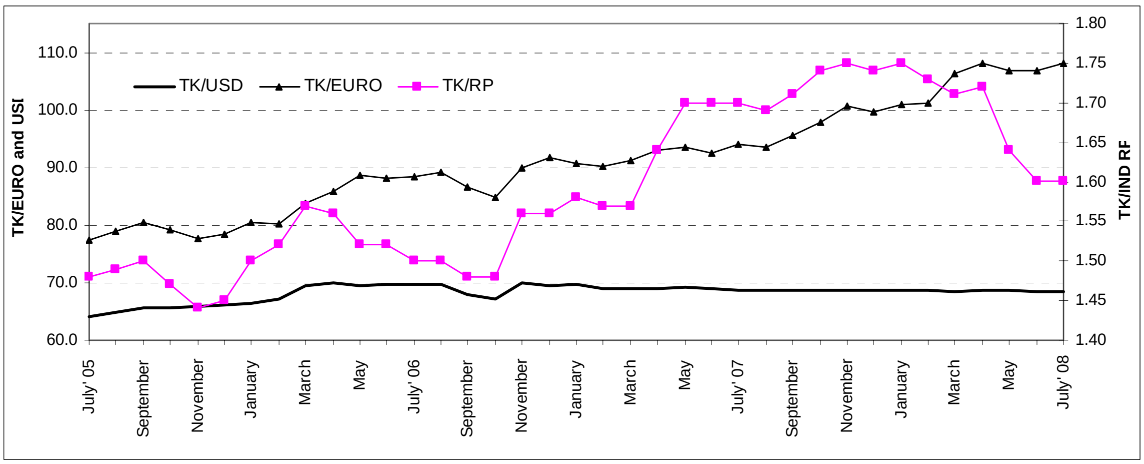
The exchange rate between Bangladesh Taka (BDT) and US Dollar (USD) has remained stable for the last one year or so. This is because of the introduction of floating exchange rate in 2003 to contain fluctuations of Taka against foreign currencies, particularly the US Dollar. During August, 2007 and August, 2008, Taka appreciated slightly by 0.26 per cent. At the end of August, 2008 Taka per USD decreased to Tk.68.52 from Tk.68.70 at the end of August, 2007. Taka depreciated against Euro by 7.38 per cent in August, 2008 compared to August, 2007. However, very recently taka is appreciating against the EURO owing to the global financial crisis.

High levels of foreign exchange reserves underpinned by unprecedented growth in remittance flows have helped BDT to remain strong against USD, notwithstanding high inflation rate. At the end of August, 2008 BDT per USD declined to Tk.68.52 from Tk. 68.70 at the end of August 2007. In FY08 the BB injected about USD500 million in the foreign exchange market to keep BDT from depreciating further. A stable exchange rate against the USD has been helpful in not allowing import prices to rise further. In Bangladesh, there is no EURO/BDT market and EURO/BDT rate is calculated from the traded rates of USD/BDT. Recently, BDT appreciated against EURO as EURO had been depreciating against USD; USD continued to remain stable against BDT.

Given the increase in volume of trade between Bangladesh and India, the exchange rate of BDT with Indian Rupee (INR) is assuming importance. Depreciation of BDT against INR in recent years has helped Bangladeshi exporters. However, BDT has started to appreciate against INR as INR depreciated significantly against USD. Indeed, whilst BDT remained stable against dollar over the last one year, INR depreciated by about 5.12 per cent during August, 2007 and August, 2008. Figures 3.9, 3.10 and 3.11 present monthly movements of BDT against USD, EURO and INR between July 2005 and March 2008.

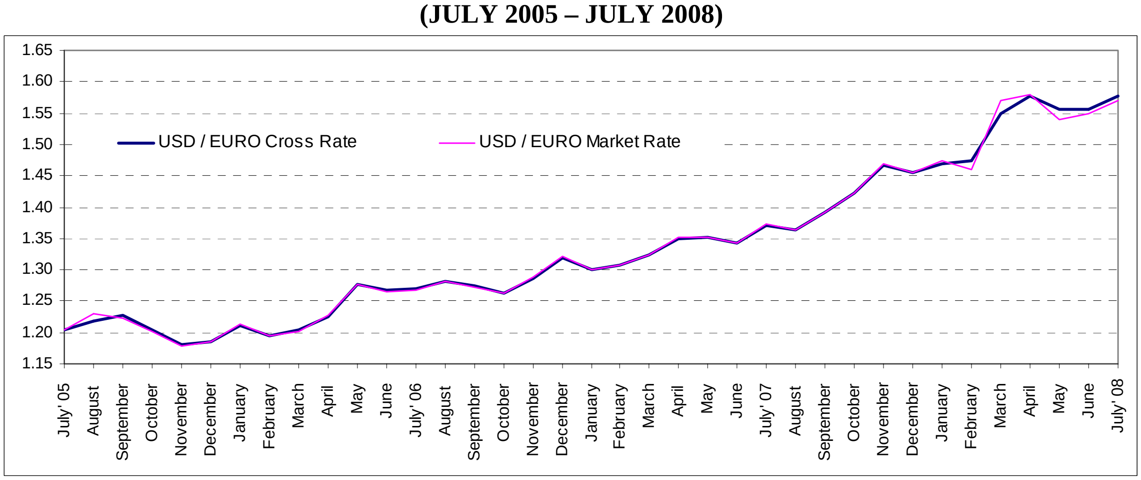
Some exporters have demanded that BDT should be depreciated to cover the probable loss of export income as a result of global recession. The importers oppose the idea as some of them have suffered significant loss due to fall of commodity price. In this context, the BB has to devise a balanced policy to take care of the interests of both exporters and importers. The proposal of dual exchange rate, however, is not applicable under the present situation. The BB has to carefully examine the request of the exporters to devise special packages for making up for the likely losses of export income at this juncture of global economic crisis.

FIGURE 3.9: MOVEMENTS TO TK. AGAINST USD, EURO AND INDIAN RUPEE (JULY 2005 – JULY 2008)



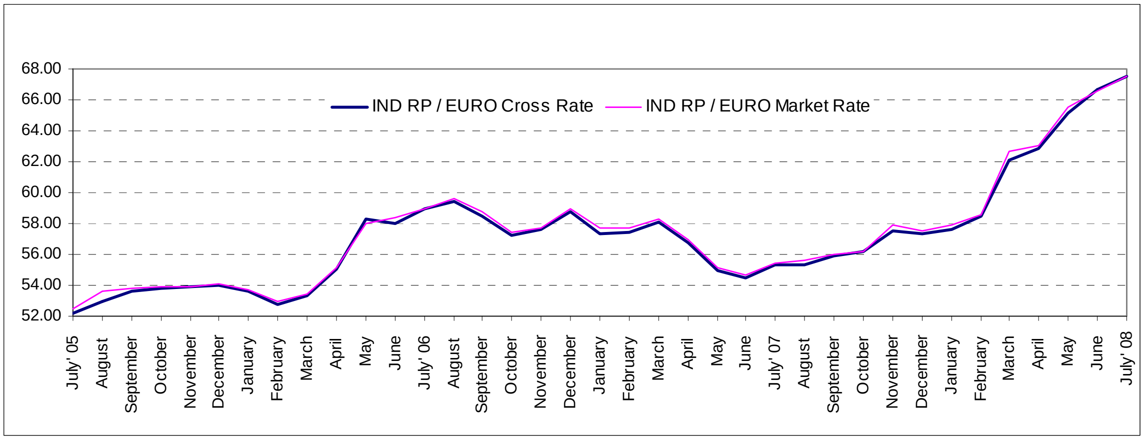
Source: Bangladesh Bank.

FIGURE 3.10: USD/EURO CROSS RATE AND MARKET RATE (JULY 2005 – JULY 2008)



Source: Bangladesh Bank, http://www.exchange-rates.org/history/USD/EUR/G/M.

FIGURE 3.11: INDIAN RUPEE/EURO CROSS RATE AND MARKET RATE (JULY 2005 – JULY 2008)



Source: Source: Bangladesh Bank, Indian Ministry of Finance.

4. REAL SECTOR

4.1 Agriculture

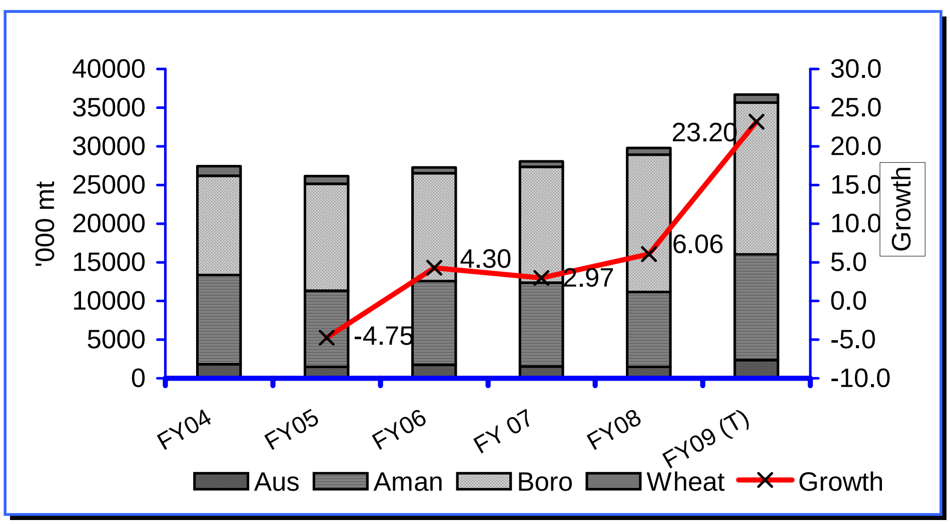
Production of Foodgrains

According to the final estimates of the BBS, total foodgrains (rice and wheat) production in FY08 was 29.78 million metric tonnes (mmt) (Aus: 1.51 mmt, Aman: 9.66 mmt, Boro: 17.76 mmt and wheat: 0.84 mmt) which was 6.13 per cent higher than the previous fiscal year. Total production of foodgrains in FY08 increased due to increase in Boro rice production. It should be noted here that wheat production was 14.5 per cent higher than the comparable period, a welcome change in the declining trend since 1999.

The Department of Agricultural Extension (DAE) has set the operational target for foodgrains production in FY09 at 36.68 million mt (Aus: 2.37 mmt, Aman: 13.66 mmt, Boro: 19.61 mmt and wheat 1.04 mmt) which is ambitiously 23.20 per cent higher than actual production in FY08. Farmers have already harvested Aus rice, but BBS is yet to release any estimate of production.

The ongoing Aman crop has been affected by flood in some areas. According to the *Situation Report* (17 September 2008) of the Disaster Management Bureau (DMB), 88 upazilas of 22 districts (Bogra, Chandpur, Chapainawabganj, Dhaka, Faridpur, Gaibandha, Jamalpur, Kurigram, Kushtia, Lalmonirhat, Madaripur, Manikganj, Munshiganj, Nilphamari, Rajbari, Rangpur, Satkhira, Shariatpur, Sherpur, Sirajganj, Sylhet, Tangail) have been affected by this year's flood, which has fully damaged 9.31 thousand hectares and partially damaged 132.74 thousand hectares of the planted Aman crops in the affected upazillas.

FIGURE 4.1: FOODGRAIN PRODUCTION IN BANGLADESH



Source: Bangladesh Bureau of Statistic (BBS) and Department of Agricultural Extension (DAE)

Input supply and subsidy for the crop sector

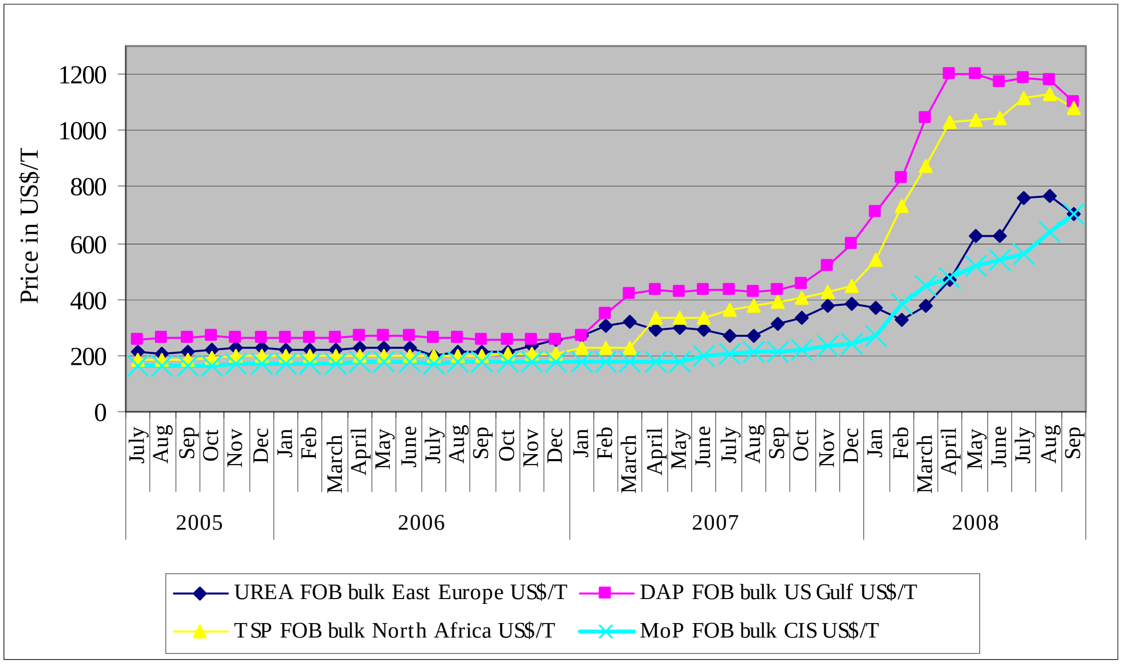
Input supply situation was relatively better in the Boro season of FY08, compared to that of FY07. Total consumption of electricity by irrigation pumps during July-March of FY08 was 75.84 mkwh which was 17.9 per cent higher than that of FY07 (comparable months). Electricity consumption by irrigation pumps during the Boro season (November-March) of FY08 was 72.99 mkwh which was 24.6 per cent higher than that of FY07 (comparable months). As is known, subsidy on account of electricity for irrigation was about Tk75 crore in FY08. On the other hand, Ministry of Agriculture distributed Tk250 crore on account of subsidy for diesel. Boro cultivating small and marginal farmers had received this subsidy at the rate of Tk545 per acre. A total of 67 lakh farmers have received benefit under this scheme.

Total supply of fertiliser in FY08 was less than the requirement. There was a gap between the actual requirement to attain high yield goal and the amount of total fertiliser distributed on the ground. However, concerned agencies were able to distribute the available fertiliser in an effective manner. National Budget FY08 allocated Tk1,500 crore for fertiliser and Tk750 crore as subsidy for diesel. Available information suggests that total subsidy for fertiliser used in FY08 was about Tk.3,408.5 crore. Though the amount of subsidy on account of fertiliser was increased, farmers could not reap the full potential benefit due to substantial (2-3 times) increase in prices of all types of fertiliser in the international market.

Bangladesh is a net importer of urea fertiliser. Between June, 2007 (Budget announcement) and June, 2008, prices of all types of fertiliser have consistently increased in the international market. Price of urea increased from USD289.00 per metric ton in June'07 to USD628.4 in June'08. During this period, per metric ton price of TSP has increased from USD331.00 to USD1,043.00, and that of DAP increased from USD434.50 to USD1,175.00; price of MOP has increased from USD196.90 to USD537.50. Increase in amount of fertiliser subsidy was unable to deliver the expected amount of total fertiliser to cater the demand for fertiliser. It is pertinent to note here that international prices of fertilisers has declined, albeit not significantly, in August and September'08.

Total supply of fertiliser in FY08 was less than what was required. A recent report (Karim, 2008), prepared on the basis of field visits to a large number of areas, observed that supply of fertiliser was able to cater to the need of medium-yield goals. The report added that for achieving high-yield goals, fertiliser requirement needed an upward revision. According to the report, fertiliser requirement in 2007/08 was 35.2 lac metric tons of Urea, 5.9 lac metric tons of TSP, 5.0 lac metric tons of MOP and 3.2 lac metric tons of DAP. On the other hand, fertiliser demand as estimated by the government was 28.14 lac metric tons of Urea, 4.75 lac metric tons of TSP, 4.0 lac metric tons of MoP and 2.5 lac metric tons of DAP. Thus, there was a gap between actual requirement to attain high-yield goals and amount of total fertiliser that was actually distributed; however, concerned agencies were able to distribute the available fertiliser in an effective manner.

FIGURE 4.2: INTERNATIONAL PRICE OF FERTILISER (UREA, DAP, TSP & MOP): JULY 2005 TO SEPTEMBER 2008



Source: Commodity market review, World Bank.

It is possible that gaps remain between actual fertiliser requirement by farmers and fertiliser demand estimated by the Ministry of Agriculture. Demand-supply gap in urea fertiliser is becoming increasingly evident.

Availability of urea fertiliser has been reported as a problem in several areas including Madhukhali (Faridpur), Rajbari Sadar, Narail Sadar, Bagharpara (Jessore). In these areas, farmers blocked highways to stress their demand for making urea fertiliser available to them. Urea production in Jamuna Fertiliser Factory in Jamalpur has also been affected negatively on account of lack of gas supply, which is an essential input for urea production.

Increase in fertiliser price is another major concern to farmers. During last five months prices of all types of fertiliser has increased. In July and August 2008, prices of all types of fertiliser were highest than those of May, 2008. Administered price of Urea fertiliser was increased to Tk.11.86 per kg from Tk.6 a kg. On the other hand, market price of triple super phosphate (TSP) has increased to Tk.68 to from Tk.34 and price of murate of potash (MOP) has increased to Tk.46 per kg from Tk.30. High price of TSP and MOP has created problems for farmers and farmers in many areas have used lower quantity of TSP and MOP in the current Aman season.

Food Aid and Commercial Import

Imports of foodgrain to Bangladesh are sustained from two sources: food aid and commercial imports. The latter comes through both government and private channels. In FY08, total foodgrain import (rice: 2,059 thousand mt and wheat: 1,412 thousand mt) was 3,471 thousand mt, out of which 259 thousand mt was food aid, 296 thousand mt came as commercial import by public sector, and 2,916 thousand mt was imported by the private sector (Table 4.1). Total import of foodgrains and rice in FY08 were 43.4 and 185.8 per cent higher than that of the pervious fiscal year. Though the total import in FY08 was high additional import was not adequate to meet the loss caused by floods and Sidr in FY08 (to the tune of 2.0 mmt).

TABLE 4.1: FOOD IMPORT TO BANGLADESH IN FY08

In ’000 mt

Category of imports	FY2006-07			FY2007-08		
	Rice	Wheat	Total Foodgrains	Rice	Wheat	Total Foodgrains
Food Aid	25	65	90	82	177	259
Public Commercial Import	-	121	121	296	-	296
Private Import	695	1514	2209	1681	1235	2916
Total	720	1700	2420	2059	1412	3471

Source: Food Planning and Monitoring Unit (FPMU), Ministry of Food and Disaster Management

During the first three months (July-September ’09) of FY09, total import of foodgrains was 515.3 thousand metric tons (314.2 thousand mt rice and 201.2 thousand mt wheat) against 861.8 thousand metric tons (400.7 thousand mt rice and 461.1 thousand mt wheat) during the same period in the previous year (Table 4.2). During the first three months of FY09, rice was imported mainly by the public sector through commercial import from India.

TABLE 4.2: FOOD IMPORT TO BANGLADESH IN FY09 (JULY-SEPTEMBER)

Category of imports	FY2007-08 (July-September)			FY2008-09 (July-September)		
	Rice	Wheat	Total Foodgrains	Rice	Wheat	Total Foodgrains
Food Aid	4.4	87.2	91.6	9.8	26.7	36.5
Public Commercial Import	45.5	0.0	45.5	297.3	35.7	332.9
Private Import	350.8	373.9	724.7	7.1	138.8	145.9
Total	400.7	461.1	861.8	314.2	201.2	515.3

Source: Food Planning and Monitoring Unit (FPMU), Ministry of Food and Disaster Management

Rice Price

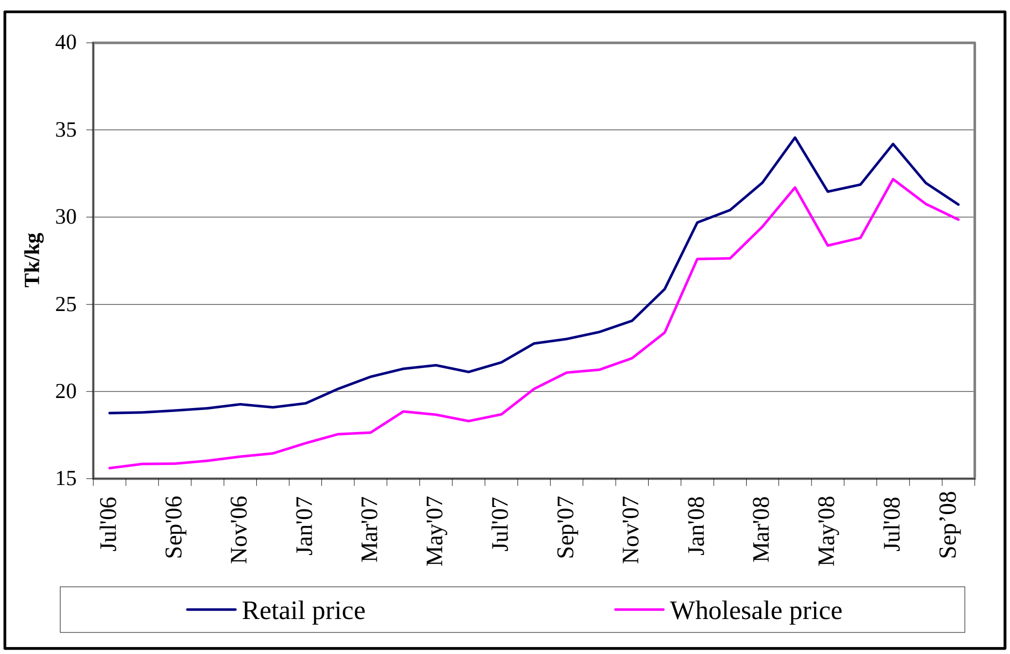
An analysis of trends in monthly wholesale and retail price of coarse rice during the last two years is shown in Figure 4.9. Both wholesale and retail price of rice increased at a high rate in FY07. On the other hand, rice price increased exponentially in FY08. Until January, 2007, retail price of coarse rice was lower than Tk.20 per kg. Since February

2007, rice prices started to increase at a rapid and very high rate (exponentially) and retail price of coarse rice reached the record high level (Tk.34.57 per kg) in April, 2008. After starting the harvest of Boro rice, price started to decline from the third week of April, 2008 but started to rise again in June, 2008. After July, 2008 both wholesale and retail price of rice has started to decline once again. In September, the retail price of coarse rice stood at Tk.30.73 per kg.

Comparison of wholesale and retail price of coarse rice revealed that there was a general correspondence between the two variables. Both the retail and wholesale price generally tended to move in the same direction (upward or downward). However, the difference between wholesale and retail price varied. During July, 2006 to January, 2007, on an average, retail price was 15.1 per cent higher than the wholesale price. During February, 2007-September, 2008, on an average, retail price was 9.6 per cent higher than wholesale price.

When price was risingly sharply, difference between the wholesale and the retail price was relatively low. On the other hand, difference was relatively high during the time of decline in rice price. This indicates the fact that consumers have to pay higher price immediately when there is any increase in rice price in the wholesale market, but they do not get the benefit, to the same extent, when there is a decline in rice price in the wholesale market. Accordingly, there is much room for improving the market mechanism for better transmission of pricing signals from the wholesale to the retail levels. Both the GoB and FBCCI have been talking about this; however, till now not much change has been visible.

FIGURE 4.3: MONTHLY WHOLESALE AND RETAIL PRICE OF RICE (COARSE): JULY 2006 TO SEPTEMBER 2008

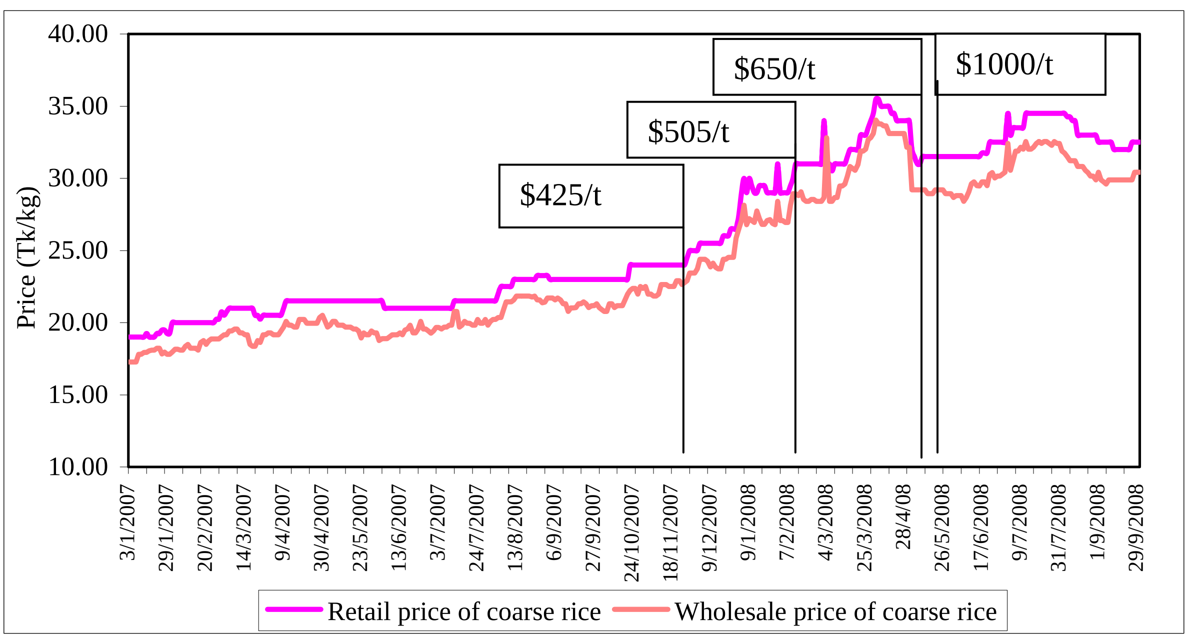


Source: Monthly Statistical Bulletin, FPMU and Directorate of Agricultural Marketing (DAM).

In FY08, Bangladesh faced two consecutive floods and the devastating cyclone Sidr which had damaged production of Aman rice and other crops. For obvious reasons, food deficit in that year was more than that of the normal years. It was expected that import of rice from India would bridge the gap in Bangladesh (like it did after the floods in 1998 and 2004). In late 2007 and early 2008, India took restrictive measures on export of both rice and wheat. India banned export of wheat and imposed minimum export prices (MEP) for non-Basmati and Basmati rice. India initially fixed MEP of non-Basmati rice at USD425 per metric ton on 25 October, 2007. Subsequently, India increased MEP to USD505 per metric ton on 27 December 2007 and USD650 per metric ton on 19 March 2008. India announced MEP as USD1,000 per metric ton for non-Basmati rice and USD1,200 per metric ton a few days later, on 28 March 2008. Finally, India banned rice export on 1 April 2008.

Policies pursued and implemented by India as well as other major producers and exporters of rice, had important implications for the international price of rice. It also led to rise in price of rice in Bangladesh. It becomes evident from price analysis that domestic price of rice has increased sharply following the announcement of MEP by India. Policies pursued by India had, to some extent, influenced rice price in Thailand, as it did also, in various degrees, influenced those of other countries such as Vietnam, Cambodia and Egypt, who were persuaded to rethink their export strategy. These countries also imposed temporary bans on rice export at various points in time.

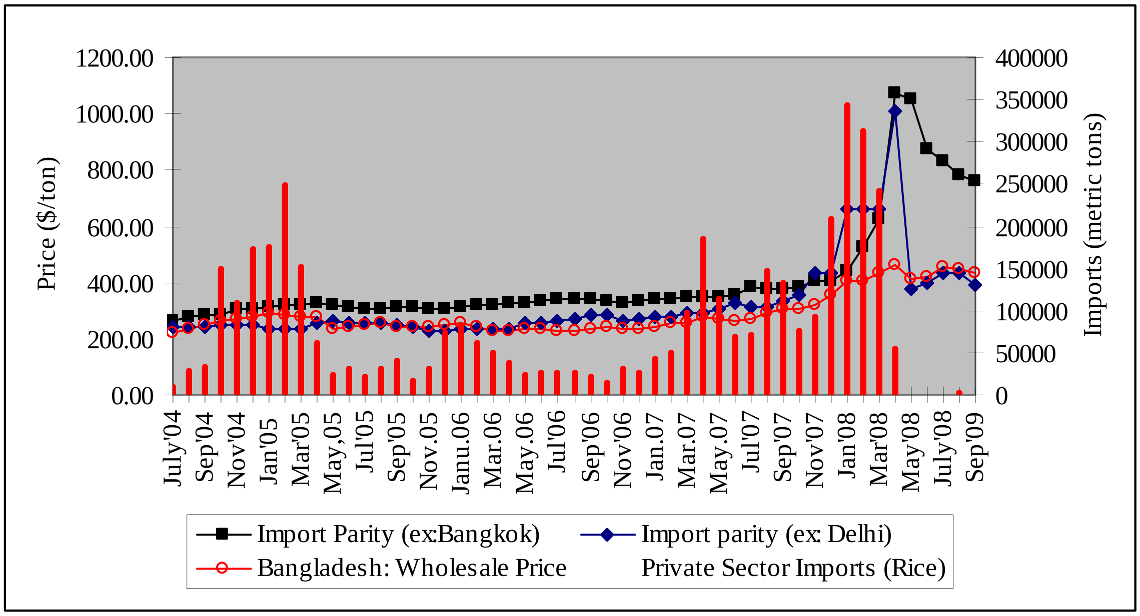
FIGURE 4.4: RETAIL AND WHOLESALE PRICE OF COARSE RICE (BR 8, BR 11, SWARNA): JAN 2007 - SEPTEMBER 2008



Source: Directorate of Agricultural Marketing (DAM).

As mentioned earlier, following the floods in 1998 and in 2004, Bangladesh was able to import huge quantities of rice and wheat from international market to offset the production loss. Due to restrictions imposed on rice exports by major exporters, import of rice was a problem in FY08. However, private sector of Bangladesh has responded well to the domestic and international prices and the policies aimed at bridging the gap between demand and supply of rice in Bangladesh. Private sector imported 16.81 lakh metric tons of rice in FY08, which was 81.8 per cent of total rice imported by Bangladesh in FY08. During the first three months (July-September) of FY09, rice was imported mainly by the public sector through commercial import from India.

FIGURE 4.5: RICE PRICES AND QUANTITY OF PRIVATE RICE IMPORTS IN BANGLADESH: JULY 2004- SEPTEMBER 2008



4.2 Industrial Sector

The performance of the industrial sector needs to be examined in the context of global financial crisis and economic downturn in the developed world in recent months, which could be a more prolonged one. Bangladesh economy is increasingly integrated with the global economy, and its share has increased over time – from 21 per cent in 1981 and 25 per cent in 1991, to about 56 per cent in 2007. Real sector of the economy is at present more integrated compared to the financial sector, which could provide some shield from the current financial turmoil. However, lack of adequate real time data on various indicators related to the industrial sector constraints analysis of the possible impact of global economic crisis on the domestic economy, especially on the industrial sector, capital market, domestic and foreign investment (FDI) particularly on export-oriented industries. A large part of the analysis presented in this section is based on the data which is often back-dated for two-three months. However, an attempt has been made to give an indication on the impact of the crisis on the domestic manufacturing sector, capital market and private investment in relevant sub-sections. A more thorough and indepth investigation will be required on the nature and extent of global financial crisis and economic downturn on Bangladesh's industrial sector.

Production of Manufacturing Sector: Manufacturing sector has registered a relatively low level of growth in FY08 compared to that of immediate past years. However, no data is available for the first quarter of FY09, which could have reflected some consequences of the current crisis (if any). QIP of medium and large scale manufacturing industries during FY08 was 6.8 per cent higher, compared to the same period of the previous year (Table 4.3). A number of sub-sectors have attained a two-digit level growth during this period; these included jute, cotton, wearing apparels, leather and wood product, mainly because of their high demand in the global market in that period. Several other sectors, on the other hand, attained a rate of growth of lesses than 5 per cent, such as non-metallic products, chemical, petroleum and rubber, food, beverages and tobacco etc., possibly because of sluggish growth of demand in domestic market owing to high inflation and economic loss caused by the natural disasters. Small scale manufacturing industries, on the other hand, posted a rise at a relatively slow pace (4 per cent) during the last quarter of FY08. In previous years, growth of these industries tended to be at lower levels compared to that of large and medium scale industries. Overall, growth of the manufacturing sector during FY08 was not at the expected level owing to various internal and external factors, though performance of major manufacturing industries was not off the recent trends. Although data on production of the manufacturing sector during the first quarter of FY09 is not available, a considerably high level of export by major export-oriented industries during July, 2008 (overall export growth was 71 per cent) provides indication of an early healthy start for the manufacturing sector in FY09.

TABLE 4.3: QUANTUM INDEX OF MEDIUM AND LARGE SCALE MANUFACTURING INDUSTRIES

(Base: 1988-89=100)

	FY2006-07 (July-June)	FY2007-08 (July-June)	% change in FY2008 over 2007
1. General Index	360.33	384.82	6.8
2. Sub-indices			
a. Food beverages & tobacco	281.8	285.82	1.43
b. Jute, cotton, w. apparels & leather	460.21	509.47	10.70
c. Wood product including furniture	257.78	287.8	11.66
d. Paper & paper product	437.67	475.01	8.53
e. Chemical, petroleum & rubber	305.98	313.41	2.43
f. Non-metallic product	439.38	459.15	4.5
g. Basic metal product	282.39	304.24	7.74
h. Fabricated metal product	158.53	168.55	6.3

Source: Bangladesh Bureau of Statistics (BBS).

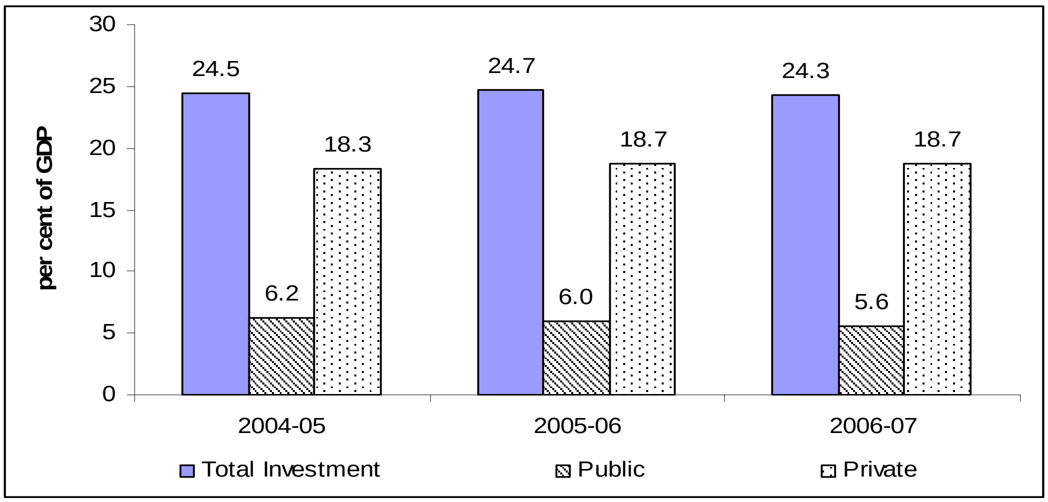
Investment: Bangladesh's overall investment has not improved perceptively since FY04, hovering around 24 per cent of the GDP (Table 4.4); national investment gradually picked up to 24.7 per cent of GDP in FY06 from its previous year, while it registered a decline in the following fiscal (0.4 per cent). The contribution of public sector in total investment has been gradually decreasing since FY02, while private sector investment is on rise but at a relatively slow pace. The share of public investment is merely one-fourth of the total investment, which was inadequate in view of the large scale investment required for infrastructural sectors (such as power, gas, road and railway sectors), and social sectors (education, health and employment guarantee schemes etc.) and also in view of the need for providing better support to the private sector. Private investment, on the other hand, is largely constituted by domestic private investment, where contribution of foreign investment is rather low.

TABLE 4.4: INVESTMENT AS PERCENTAGE OF GDP: PUBLIC AND PRIVATE

	2004-05	**2005-06**	**2006-07**
Total Investment (% of GDP)	24.5	24.7	24.3
Public	6.2	6	5.6
Private	18.3	18.7	18.7

Source: Bangladesh Economic Survey, 2008

FIGURE 4.6: INVESTMENT (AS A PER CENT OF GDP)



Source: Bangladesh Economic Review 2008

Analysis of investment in FY08 has been carried out by using various proxy indicators, such as disbursement of credit, opening and settlement of L/Cs, etc. A rise in investment in the industrial sector, especially in terms of disbursement of industrial term loans, opening and settlement of L/Cs for import of capital machineries, raw materials and intermediate products needs some explanation. Disbursement of industrial term loan in FY08 was Tk.20,151 crore, which was 62.6 per cent higher compared to the previous fiscal year (Table 4.5). This may be attributed to the rise of the number of projects considered for bank financing as well as higher level in cost involved in each of those projects owing to high inflation, high cost of raw materials including building construction materials, cost of land and high price of oil to be used in industries, etc.

Growth of recovery of industrial term loan during this period was also encouraging, which was more than 50 per cent higher in FY08 compared to that of the previous fiscal year (comparable figure for FY07 was 34 per cent, see Table 4.5). These positive changes in the recovery of loan could somehow be related to the strict banking practices followed under the current caretaker government. On the other hand, overdue loan as percentage of outstanding loans reduced at the end of June, 2008 (12.4 per cent), which was about 16 per cent in January-March quarter of FY08. Reduction of overdue loans is mainly because of the write-off of a large amount of bad debts by shifting necessary capital from the statutory reserve requirement (SRR), since some banks did not make appropriate provisions against bad debts (as reported in the national dailies). This, in other ways, has reduced commercial bank's level of SRR maintained with the Central Bank. Net disbursement of industrial term loan has doubled (96 per cent) in the last fiscal year compared to that of the previous fiscal. In the backdrop of relatively slow pace of growth of major manufacturing sectors, such a high rate of growth of industrial term loan indicates some changes in commercial bank's focus in the disbursement pattern of loan, possibly targeting SMEs. Commercial banks' recent focus on SMEs is mainly because of availability of low cost fund from Bangladesh Bank for lending purposes as also the requirement of lower levels of provisioning required against SME loan (5 per cent), as against loans to large scale firms (20 per cent).

TABLE 4.5: INDUSTRIAL TERM LOANS (IN CRORE TAKA)

Year	**Disbursement (a)**	**Recovery (b)**	**Net (a-b)**
2005-06	9650.02 (10.86%)	6759.52 (-20.91%)	2890.5
2006-07	12394.78 (28.44%)	9068.45 (34.15%)	3326.33
2007-08	20150.91 (62.58%)	13624.23 (50.24%)	6526.68

Source: Bangladesh Bank

Financing SMEs: Disbursement of credit to the SMEs has registered considerable growth in all quarters of the previous fiscal year (Table 4.6). Outstanding loan in the SME sectors in the last three quarters of FY08 have registered growths of 7 per cent, 3 per cent and 11 per cent respectively. Share of outstanding SME loans had increased to one-fifth of the total outstanding loans in April-June 2008. This rise in credit growth is mainly attributed to the increasing share of funds transferred by state-owned banks, commercial banks and specialised banks; growth of outstanding advance of private commercial banks was moderately high (17 per cent) in the last quarter of FY08. Private commercial banks special interest in SME financing is possibly coming from pressure on their deposits which have been partially leveraged with the supply of soft-loan from Bangladesh Bank for SME financing, as well as the very low provisioning requirement in case of SME financing as mentioned earlier. However, most of these credit disbursed by commercial banks were targeted at SMEs located in urban areas (perhaps 'big' in size) or in peri-urban areas, and less in rural areas. Thus, more focus on rural based SMEs was needed.

TABLE 4.6: OUTSTANDING POSITION OF SME LOANS (TK IN CRORE)

Types of financial institution/Banks	State owned banks	Private Banks	Foreign Banks	Specialised banks	Non-financial institutions	Total
July-September, 2007	9670.3 (+22.29)	14336.64 (+16.29)	486.98 (+6.15)	2789.51 (+21.85)	1185.07 (+17.71)	28468.5 (+17.93)
October-December, 2007	9577.6 (+22.66)	16248.61 (+18.21)	427 (+5.10)	3054.38 (+23.25)	1279.37 (+18.70)	30586.96 (+19.14)
January-March, 2008	9603.8 (+22.26)	16930.24 (+17.90)	506.66 (+5.42)	3200.08 (+23.99)	1286.87 (+18.03)	31527.65 (+18.81)
April-June, 2008	9918.87 (+33.29)	19889.76 (+19.67)	611.67 (+6.51)	3249.09 (+22.87)	1367.69 (+19.65)	35037.07 (+21.70)
% change of SME loans during October-December, 2007 over July-September, 2007	-0.96	13.34	-12.32	9.50	7.96	7.44
% change of SME loans during January-March, 2008 over October-December, 2007	0.27	4.20	18.66	4.77	0.59	3.08
% change of SME loans during April-June, 2008 over January- March, 2008	3.28	17.48	20.73	1.53	6.28	11.13

Source: Agricultural credit & special programmes department, Bangladesh Bank.
Note: Figures in brackets indicate SME loans as percentage of total loans.

TABLE 4.7: OUTSTANDING POSITION OF SME LOANS (AS PERCENTAGE OF TOTAL SME LOANS)

Types of financial institution/Banks	State owned banks	Private Banks	Foreign Banks	Specialised banks	Non-financial institutions	Total
July-September, 2007	33.97	50.36	1.71	9.80	4.16	100 (28468.50)
October-December, 2007	31.31	53.12	1.40	9.99	4.18	100 (30586.96)
January-March, 2008	30.46	53.70	1.61	10.15	4.08	100 (31527.65)
April-June, 2008p	28.31	56.77	1.75	9.27	3.90	100 (35037.07)

Source: Agricultural credit & special programmes department, Bangladesh Bank.
Note: Figures in brackets indicate total SME loans.

TABLE 4.8: CHANGES IN THE FRESH OPENING AND SETTLEMENT OF L/Cs BETWEEN FY2007 AND FY2008

Sectors / Commodities	Fresh L/Cs opening	Settlement of L/Cs	Outstanding L/Cs
Consumer goods	98.87%	84.84%	59.57%
Intermediate Goods	33.90%	29.28%	63.18%
Industrial Raw Materials	40.02%	29.26%	46.37%
Capital machinery	15.96%	-8.38%	30.88%
Machinery for misc. industry	34.33%	24.76%	33.83%
Petroleum & petro Products	8.95%	12.62%	36.42%
Others	48.79%	25.71%	47.42%

Import of Raw Materials, Intermediate Products and Capital Machineries: Data for fresh opening and settlement of L/Cs, which is usually considered as proxy indicators for investment in the industrial sector, indicates some positive changes. Growth of opening and settlement of L/Cs in case of import of intermediate goods and industrial raw materials were found to be about 30-40 per cent in FY08, which indicates higher levels of investment for expansion of existing industries. In case of import of capital machineries, while growth in fresh opening of L/Cs was found to be positive (16 per cent), growth in settlement of L/Cs was negative (-8.4 per cent). This indicates a slow pace of growth with regard to new investments for expansion and establishments of new industrial units in the industrial sector. The slow pace of growth of import of capital machineries needs to be closely examined by matching with the high level of disbursement of term loan for industries, as to which sectors had received these loans (but do not require higher levels of import of capital machineries). One possible explanation could be disbursement of credit to SMEs, which procured large part of their raw materials and capital machineries from domestic sources.

TABLE 4.9: CHANGES IN FRESH OPENING AND SETTLEMENT OF L/CS IN CASE OF IMPORT OF CAPITAL MACHINERIES BETWEEN FY2007 and FY2008

	Fresh L/Cs opening	Settlement of L/Cs	Outstanding L/Cs
Capital Machinery	15.96%	-8.38%	30.88%
Textile Machinery	27.17%	-17.10%	39.40%
Leather/tannery	-0.11%	40.49%	26.21%
Jute industry	16.63%	-26.48%	117.59%
Garment industry	16.87%	1.78%	25.35%
Pharmaceutical Industry	19.51%	-19.31%	35.87%
Packaging Industry	-23.93%	23.02%	19.18%
Other industry	9.09%	-7.23%	27.44%

Source: Bangladesh Bank

Analysis of the figures relating to opening and settlement of new L/Cs during July, 2008 suggests an increase by 14 per cent and 21 per cent respectively compared to the corresponding figures for July 2007 (Table 4.10). It is to be noted that this sign of import dynamism was largely underwritten by significant growth of intermediate goods (58 per cent) and industrial raw materials (55 per cent). In more disaggregated terms, within industrial raw materials, opening and settlement of chemicals and chemical products rose by 65.4 per cent and 62.5 per cent respectively. Some growth was also observed in cases of machinery for miscellaneous industries (40 per cent). Over the period of July 2008, textile, leather and pharmaceuticals had registered high negative growth in terms of opening of new L/Cs. However, it is heartening to observe that the packaging industry has recorded a comeback, registering 163 per cent growth in opening of fresh L/Cs compared to the same period of the previous year. A negative growth in settlement of L/Cs for importing of capital machineries, mainly in major manufacturing industries, needs to be closely monitored in the coming months, taking into cognisance entrepreneurs' projections with regard to the possible impact of global economic crisis on Bangladesh economy.

TABLE 4.10: PERCENTAGE CHANGES DURING JULY 2008 OVER JULY 2007 (LCs)

	Fresh L/Cs opening	Settlement of L/Cs	Outstanding L/Cs
Capital Machinery	14.16%	21.44%	30.00%
Textile Machinery	-23.30%	61.20%	33.60%
Leather/tannery	-100.00%	100.00%	-18.50%
Jute industry	-51.90%	N.A	88.20%
Garment industry	71.34%	-7.33%	36.40%
Pharmaceutical Industry	-27.11%	245.61%	25.20%
Packaging Industry	162.96%	-35.14%	25.20%
Other industry	15.76%	8.80%	24.32%

All major industries such as textile, jute, pharmaceuticals etc. were found to register negative growth in terms of settlement of L/Cs during FY08, compared to the previous fiscal year. The highest change in settlement of L/Cs took place in the leather/tannery industry registering a 41 per cent growth. Based on the figures, it can be deduced that the garment sector experienced a marginal rate of growth (1.8 per cent) in settlement of L/Cs. This is corroborated by the fact of slower pace of growth of large industries. It is important to examine the growth of L/Cs closely, both in terms of opening and settlement, in the coming years in order to assess the investment trends.

Foreign Direct Investment (FDI)

Foreign direct investment (FDI) flow in the country has not been encouraging for the last several years. According to UNCTAD's World Investment Report 2008, Bangladesh's rank in terms of FDI performance index in 2007 has slipped down by 1 position, from 120 to 121. During FY08, flow of FDI in Bangladesh registered a decline by 22.4 per cent compared to that of the previous fiscal year. Both direct investment and portfolio investment had declined by 18 per cent and 54.7 per cent respectively (Table 4.11). There has not been any improvement in the situation in FY08 compared to that of the previous fiscal year. In view of the global financial crisis and economic slow down, multinational companies could be averse to taking risks and to invest overseas in countries such as Bangladesh (where size of the domestic market is not so big and the economy is less diversified; however, this would not be the case for export-oriented industries).

While equity capital and reinvested earnings have declined by about 20 per cent in 2007 (January-December, 2007) compared to that of the previous year, intra company loans, a small component in total FDI share, has increased by more than 100 per cent (Table 4.12). It is to be noted that reinvestment of earnings of foreign companies was lower than the amount that was repatriated every year.

TABLE 4.11: FOREIGN DIRECT INVESTMENT IN BANGLADESH, 2006-2008

(million USD)

Type of investment	FY05-06	FY06-07[R]	FY07-08[P]	Percentage change between FY07 and FY08	July, 2007 (FY08)	July, 2008 (P) (FY09)	Percentage change between July, 2007 and July, 2008
Foreign direct investment	743	793	650	-18.03	48	63	31.3
Portfolio investment	32	106	48	-54.72	33	-1	-103.0
Total	775	899	698	-22.36	81	62	-23.5

Source: Bangladesh Bank.

TABLE 4.12: DIFFERENT TYPES OF FDI

(million USD)

FDI inflow	2005	2006	2007	Percentage in 2007 over 2006
Equity capital	425.6	503.6	401.6	-20.3
Reinvested earnings	247.5	264.7	213.2	-19.5
Intra-company loans	172.2	24.1	51.6	114.1
Total FDI inflow	845.3	792.4	666.4	-15.9

Source: Bangladesh Bank.

Capital Market

Market Capitalisation: In the context of the ongoing global financial crisis, impact on the local capital market needs to be closely monitored and on a regular basis. Considering the low level of integration of the local financial market with the global market (2.48 per cent of market capitalisation), the impact on the financial market is likely to be insignificant. Portfolio investment in FY08 has declined compared to that in the previous fiscal year; this has continued in the following period (July, 2008) even at faster pace (a reduction of 103 per cent).

Market capitalisation, both in Dhaka and Chittagong Stock Exchanges, has been robust, underwritten by buoyant performance over the market since the second half of FY07 (Figures 4.7 and 4.8). During July-October (up to 19 October, 2008) market has further strengthened as capitalisation increased by more than 30 per cent, compared to the same period of the previous year (Table 4.13). In the backdrop of the poor state of investment situation in major industrial sectors, such high level of performance of the capital market remains somewhat enigmatic and does not appear to be a true-reflection of the realities on the ground. Both the DSE and CSE are found to witness frequent fluctuations in the share price indices, with resultant losses for small investors. Security Exchange Commission (SEC) has attempted to control this volatility with various regulatory tools, including those that related to issuance of right shares against mutual fund. However, such short term measures were not found to be very effective. Overall, the country's capital market needs structural reforms and overhaul in terms of management, operation, transparency and accountability. Some reform measures have been put into effect in recent times (i.e. introduction of book building system for IPO). However, SEC will need to be ever vigilant, particularly in view of the emerging situation.

FIGURE 4.7: MARKET CAPITALISATION OF DSE

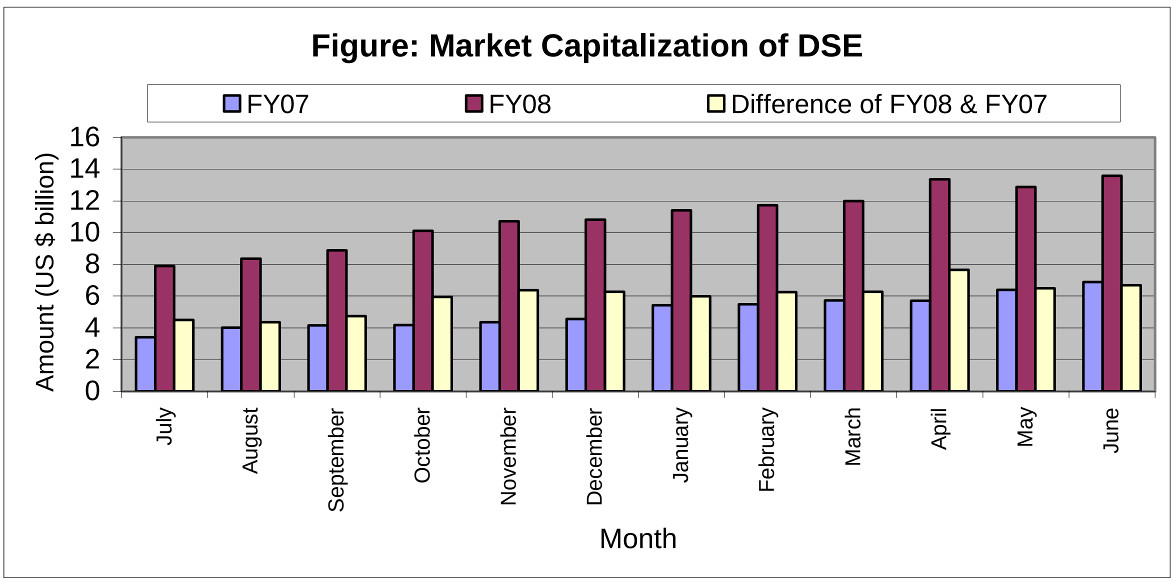
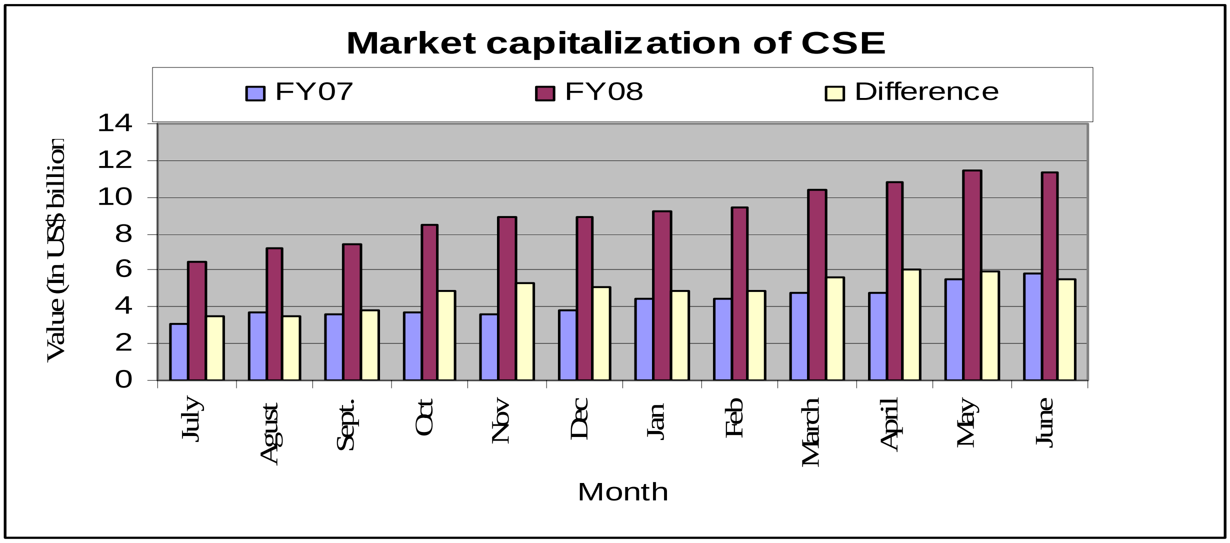


TABLE 4.13: MARKET CAPITALISATION OF DSE (JULY-OCTOBER, 2007 AND 2008)

Market Capitalisation (USD billion)	July	August	September	October
FY08	7.9	8.37	8.89	10.12
FY09	13.95	14.15	15.18	14.64
% change between FY09 & FY08	43.37	40.85	41.42	30.87

Source: DSE website
Note: Data for October FY09 is up to 21 October, 2008.

FIGURE 4.8: MARKET CAPITALISATION OF CSE



Initial Public Offering (IPO): With respect to IPOs, the number of companies that floated their shares in FY08 were 12, which was 2 more compared to the previous fiscal year. However, total issued shares, sponsors' part, and public offer etc. in FY08 were not found to be very promising for potential investors. Oversubscription in the context of IPOs had made the share of public offer to decreased by about 49 per cent. In case of 9 upcoming IPOs (four from insurance and one each from leasing, housing finance, textile, iron steel and ICD) public offering as percentage of total shares was found to be low (22 per cent of total shares vis-a-vis 37 per cent in FY08) which is a matter of concern for small scale investors (Table 4.14).

Grameen Phone, the largest telecom company in Bangladesh, has submitted its prospectus for the purpose of issuance of IPO to the tune of about USD300 million. If this is successful, it will substantially increase market capitalisation in Bangladesh. This initiative by a multinational company should encourage other big companies to float their shares in the capital market. For example, AKTEL, another telecom company, has also announced that they would offload a part of their shares in the capital market. SEC needs to take into account the possible impact of floating of such a large volume of shares by a single company (Grameen Phone) and take necessary precautionary measures to reduce the possibility of any kind of volatility in the market.

Enlistment of Public Sector Companies: In line with government's decision to convert public sector corporations into public limited companies through offloading of their shares in the capital market, a number of enterprises have already registered as limited companies. In recent times, the government has taken a decision to enlist Bangladesh Shipping Corporation and Bangladesh Telephone Company Limited in the stock market. SEC's initiative to relax the rule for listing IPOs, i.e., deposit of 25 per cent of the subscription value as first installment and rest 75 per cent as final installment within 15 days of IPO allotment, should contribute towards increasing money-flow in the capital market.

TABLE 4.14: IPO'S PERFORMANCE OF DSE

Year	FY07	FY08	% change of FY08 and FY07	FY09 (Upto, 23 Sep,2008)
No. of IPO's	10	12	20	1
Total Issued Shares	143310876	76127314	-46.88	23000000
Sponsors Portion (Share)	90153081	45245264	-49.81	11500000
Public Offer (Share)	53157795	30882050	-41.90	11500000
Public offer as percentage of total Issued Shares	37.09	40.57	9.36	50
Total Paid up Capital (after IPO) (in croe Tk)	651.54	749.68	15.06	230
Over-subscription as % of total public offer	734.3	378.44	-48.46	

Source: Calculated based on information collected from the DSE website
Note: For FY2008 over-subscription includes eight IPO's

TABLE 4.15: FORTHCOMING IPOd OF DSE APPROVED BY SEC (UPTO 21 OCTOBER, 2008)

No. of IPO's	9
Total Issued Shares	70740000
Sponsors Portion (Share)	54620000
Public Offer (Share)	16120000
Public offer as percentage of total Issued Shares	22.79
Total Paid up Capital (after IPO) (in croe Tk)	365.4

Source: Calculated based on information of DSE website.

Power and Energy

Power Generation: Inadequate power supply has been a major bottleneck that has severely constrained investment and business activities in Bangladesh. New industries and economic activities are slow to emerge because of shortage in power supply; the existing ones suffer from frequent outages, leading to damage to equipments, production disruption and cost escalation. When more costly alternative sources are used, production costs escalate. A large gap exists between demand for power generation and distribution, though generation has somewhat increased in recent months.

In FY08, maximum power was generated in March, 2008 (3,783.3 MW), which was 21.5 per cent higher than the corresponding period of the previous year. On an average, 3,548.2 MW power was generated in FY08 which was 12.1 per cent more than that of the comparable period (Table 4.16). No considerable improvement in power generation was observed in the first quarter of FY09 (Table 4.17). Since January, 2008 production has increased by more than 10 per cent, but this still lags behind the demand for electricity. Average demand-supply gap has been reduced by 27.7 per cent in FY08 compared to the same period of the previous fiscal year (Figure 4.9). Load shedding was frequent over the recent past years - increasing from 720 MW in February, 2008 to 777.7 MW in August, 2008; however, it has declined in subsequent months, from 456.3 MW in September, 2008 to 278.1 MW in October, 2008.

Because of frequent power outages, industries and businesses are becoming increasingly dependent on captive power in order to ensure uninterrupted power supply to factories and business premises. As a result, in recent years various types of power generator, mainly gas based, are being imported at an increasing rate. This is corroborated by the fact that consumption of gas for captive power generation has substantially increased-in FY03 the share of use of gas for captive power generation was 6.5 per cent of the total (741.4 mmcm) which increased to 11.4 per cent in FY07 (1770.2 mmcm) and 13.5 per cent till February, FY08 (1433.1 mmcm). Government is also encouraging large manufacturing and business units to set up captive power plants; recently, twelve companies have received permission to set up power plants. In view of this, the government has provided fiscal support in the form of low import duties on generators.

According to BPDB, major reasons for the shortfall in power generation are repair and maintenance works of plants and forced stoppage, and due to shortages of gas. Power generation has been hampered in recent months due to shortages of gas to the tune of 939 MW in February, 2008, 728 MW in March, 2008 and 720 MW in April, 2008.

TABLE 4.16: POWER GENERATION BETWEEN FY2007 AND FY2008

Average Power generation (MW)			% change in FY08 over FY07
Month	FY07	FY08	
July	3447.1	3511.0	1.9
August	3326.2	3612.0	8.6
September	3265.1	3697.3	13.2
October	3052.2	3507.5	14.9
November	2964.9	3321.4	12.0
December	2897.6	3315.7	14.4
January	2729	3399.9	24.6
February	2694	3529.0	31.0
March	3113	3783.3	21.5
April	3378	3639.0	7.7
May	3348	3423.9	2.3
June	3333	3365.5	1.0
Average	3129.0	3508.8	12.1

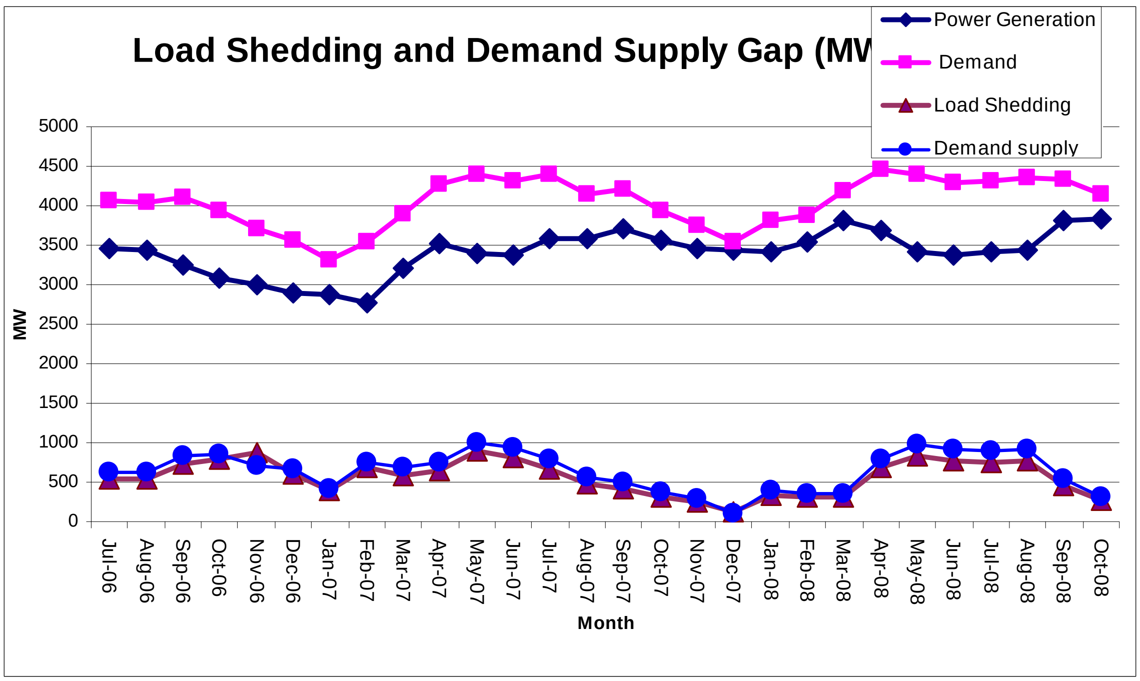
Source: BPDB, Daily report

TABLE 4.17: POWER GENERATION BETWEEN JULY-OCTOBER, FY2007 AND FY2008

Power generation (MW)			% change in FY08 over FY07
Month	FY08	FY09	
July	3511.0	3400.9	-3.1
August	3612.0	3435.9	-4.9
September	3697.3	3804.9	2.9
October	3502.5	3820.9	9.1
Average	3580.7	3615.7	1.0

Source: BPDB, Daily report
Note: Data on October, FY2008 is upto 20 October, 2008

FIGURE 4.9: LOAD SHEDDING AND DEMAND-SUPPLY GAP



To generate the required amount of electricity in the country, the government should take immediate steps to establish several large and small scale power plants in the country. According to BPDB, a total of 30 power plants are planned to be set up in the country by 2012, of which 17 power plants are now under construction phase. These are expected to be commissioned by 2009 and another 13 power plants are under processing, which are planned to be commissioned by 2010 or 2012. If all these power plants are constructed on time, a maximum of 4,445 MW additional power supply could be added to the national power grid. A total of 12 power plants with a production capacity of 694 MW is planned to be built during 2008. However, only one has been established as of date and others are still under construction. Out of this, 11 power plants will be constructed on rental terms for 3 to 15 years. World Bank's recent disbursement of credit for establishing 450 MW Shiddirgonj power plant and ADB's USD165 million worth of credit for infrastructure development, including small scale power plants and renewable energy etc., will hopefully improve the power generation situation in the country.

It will be a challenge for Petrobangla to supply the required quantity of gas to the power plants from its limited reserves for a prolonged period of time, unless it explores new sources of gas in the country. Government should take necessary measures to set up coal-based power plants by using the coal reserve of the country. The first step towards this would be to take a decision with regard to the *National Coal Policy*, which is now in the process of review by the CTG.

Gas Generation: Gas generation has not substantially improved in FY08 compared to that in the previous fiscal year; a total of 17,015 mmcf gas has been generated in FY08 which was 6.9 per cent higher (Table 4.18) then the previous fiscal year. Whilst plants operated under the Petrobangla (which supplied 55 per cent of the total share) generated 8 per cent less gas compared to the previous year, plants under the private companies generated 25 per cent more during the same period. It is important to investigate why the performance of Petrobangla has gradually declined, while that of private companies has been improving. More importantly, share of private companies in overall gas distribution has been increasing over time – within 5 years its share has more than doubled from 21 per cent in FY03 to 45 per cent in FY08 (Table 4.19). This sudden rise of exploration of gas by private companies (especially in FY08 by 25 per cent) by using the same set of wells in order to meet the domestic requirement has often caused damages of the wells, which has long term negative impact on the expected level of exploration, as it perhaps happened in case of Sangu and Bakhrabad gas fields. The operation of BAPEX is often constrained by shortage of adequate capital for exploring wells; over time, the capacity of the BAPEX has also been significantly reduced. In this context, the allocation of Tk. 3,000 crore to the BAPEX in the budget FY09 for next three years is a welcome initiative. In view of the increasing share of private companies in country's gas generation, which could further increase once the off-shore gas exploration starts, strengthening of BAPEX is critically important from Bangladesh's long term strategic perspective.

TABLE 4.18: TOTAL GAS PRODUCTION IN DIFFERENT YEARS (MMCF)

Year	Petrobangla	IOC	Total	Growth rate
2002-03	9449.125	2476.721	11925.85	
2003-04	9715.113	3106.01	12821.12	7.51
2004-05	10086.484	3696.907	13783.39	7.51
2005-06	10116.56	4804.284	14920.85	8.25
2006-07	10148.452	5771.65	15920.1	6.70
2007-08	9282.038	7732.488	17014.53	6.87

Source: MIS Report, Petrobangla (June, 08)

TABLE 4.19: TOTAL GAS PRODUCED BY DIFFERENT COMPANIES

Year	BGFC	SGCF	BAPEX	IOC	Total
2002-03	59%	18%	2%	21%	100%
2003-04	59%	16%	1%	24%	100%
2004-05	57%	13%	3%	27%	100%
2005-06	52%	12%	4%	32%	100%
2006-07	49%	12%	3%	36%	100%
2007-08	43%	10%	2%	45%	100%

Source: MIS Report, Petrobangla (June, 08)

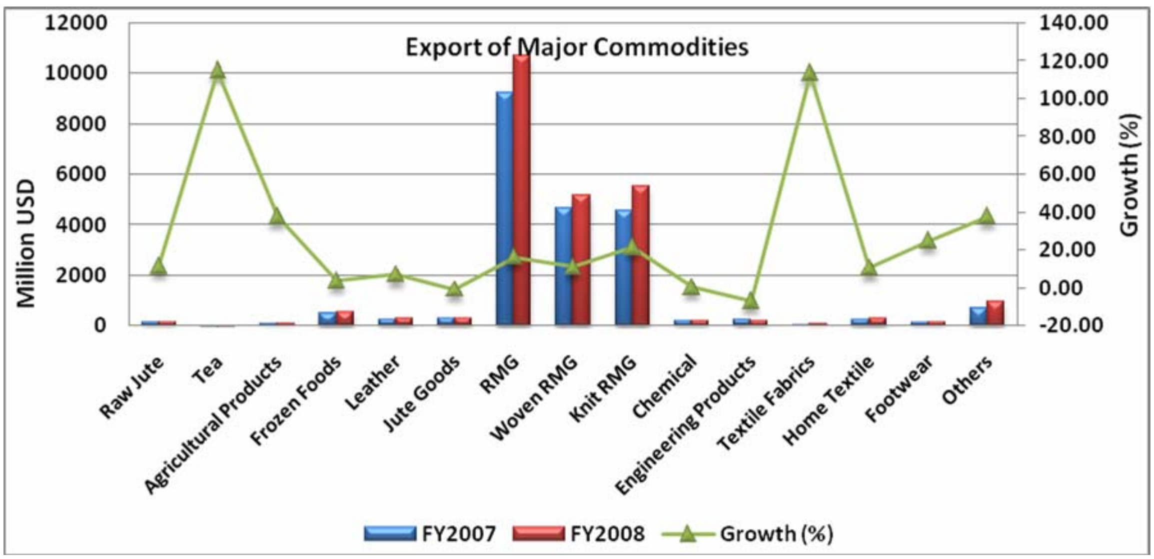
According to energy experts, current gas reserves, estimated to be 8.0 trillion cubic feet (tcf), will not be able to meet the demand of the country after 2015; about 24 tcf gas will be required to meet the energy demand up to 2025. An estimated investment of USD8 billion will be required in the energy sector for this. It is also important to consider developing long term debt market in the country in order to generate investible resources for large scale long term projects including in such areas as energy, power sector and other types of infrastructure. Big commercial banks, including foreign banks, should take a lead role to finance such large-scale infrastructure projects. Currently, Infrastructure Development Company Limited (IDCOL), a non-blank financial institution, is financing two power plants namely Meghnaghat 450 MW Power Plant Project and Summit Power Ltd. 33.75 MW Power project with a credit support of USD90 million and Tk.90 crore. Possibility of raising resources through securitisation coupled with a greater role of the private sector should also be explored on an urgent basis.

5. BANGLADESH'S EXTERNAL SECTOR IN FY2007-08

5.1. Export Sector's Performance

Bangladesh's total export earnings during FY08 stood at USD14,088.27 million, registering a double-digit growth of 15.92 per cent over FY07. The sector was able to recover from the debacle suffered in the first quarter of FY08 when export earnings registered a negative growth of (-) 5.39 per cent. The growth rate posted during this period is also impressive because it comes in the backdrop of high growth rates of 24.65 per cent and 15.60 per cent attained over the previous two fiscal years. This was quite an impressive performance given the challenges Bangladesh faced in FY08. Exports fell just short of the target of USD14.5 billion set in the beginning of the fiscal (Figure 5.1).

FIGURE 5.1: EXPORT OF MAJOR COMMODITIES (FY2007 & FY2008)



Source: CPD Trade Database, 2008.

Bangladesh's export performance in the first month of FY09 (July 2008) has been phenomenal. She was able to expand her export growth by 71.01 per cent in July FY09 compared to the same period of FY08 – exporting more than USD1.54 billion in a single month. This high growth rate, however, was achieved in the backdrop of a negative growth of (-) 22.6 per cent observed in July FY08.

TABLE 5.1: BANGLADESH'S EXPORT OF MAJOR COMMODITIES (FY2008 AND FY2009, JULY)

(Million USD)

	FY2008	FY2009	Growth (%)
Raw Jute	6.49	11.57	78.27
Tea	0.73	0.52	-28.77
Agricultural Products	15.10	15.65	3.64
Frozen Foods	45.93	64.06	39.47
Leather	20.54	19.13	-6.86
Jute Goods	22.66	30.07	32.70
RMG	691.94	1187.80	71.66
Woven RMG	*345.20*	*547.30*	*58.55*
Knit RMG	*346.74*	*640.50*	*84.72*
Chemical	11.38	39.96	251.14
Engineering Products	12.33	19.74	60.10
Textile Fabrics	0.96	7.66	697.92
Home Textile	18.68	28.99	55.19
Footwear	10.58	18.58	75.61
Others	45.01	99.36	120.75
Total Export	***902.33***	***1543.09***	***71.01***

Source: CPD Trade Database, 2008.

Bangladesh's foremost export item, readymade garments, posted a high growth of 71.66 per cent during the first month of FY09. It was about 16.17 per cent in FY08 compared to FY07. RMG's contribution stood at 76.98 per cent of Bangladesh's total export earnings in this period (July FY09). Bangladesh earned USD1.19 billion from export of apparels in July FY09, compared to USD691.94 million earned over the corresponding period of FY08. During FY08 this was 75.95 per cent (USD10.70 billion) of total export earnings.

It is of interest to note that, Bangladesh's export earnings from the RMG sector crossed the USD10 billion threshold for the first time ever in FY08. During the period under review (FY08), an additional amount of USD1.49 billion was earned by the sector compared to FY07, major share in this originating from the increasing export of knit-RMG (amounting to USD978.20 million or 65.69 per cent). A decomposition of the RMG export indicates robust growth for both woven-RMG (10.97 per cent) and knit-RMG (21.48 per cent). Thanks to the consistently high growth rates of knitwear in recent years, share of this sub-sector in the total RMG export now exceeds that of the woven-wear. Since domestic value retention of knitwear (55-60 per cent) was substantially higher than woven wear (25-30 per cent when fabric is imported, and about 60 per cent when fabric is locally sourced), this structural shift within the RMG must be viewed as a commendable achievement. Indeed estimates of net export carried out by the CPD illustrates that during FY08, value retention in knit-RMG was about USD3042.99 million compared to USD1744.05 million for the woven-RMG (or about 1.74 times more). RMG's performance must be seen as an indication of the sector's inherent strength in the context of the quota-derestricted regime of the increasingly competitive post-MFA global market. The quota imposed on the Chinese export of apparels by both the USA (2003) and the EU (2005) has worked in favour of Bangladesh.

Of the other major items of export, home textile (10.26 per cent), textile fabrics (113.45 per cent), footwear (24.72 per cent), frozen food (3.59 per cent) and leather (6.91 per cent) demonstrated high growth rates. On the other hand, earnings from Bangladesh's traditional export items such as jute goods, continued to slide and experience negative growth (-0.76 per cent) during FY08. Of all these major export items, only export of leather experienced a decline during the first month of FY09 compared to the same period of FY08. Export of leather in July FY09 shrank by (-) 6.86 per cent. Tea export has also been on the downside – growth declining by (-) 28.77 per cent or by USD0.21 million.

In terms of markets for Bangladesh's export, there was no marked deviation from the traditional destinations. The EU(27) continued to be the major destination, accounting for USD5.44 billion (first nine months of FY08) – exports to the EU rose by nearly 15.35 per cent over this period (which meant an additional earning of USD723.66 million). Performance in the US market was rather discouraging, with exports increasing by a mere 0.29 per cent (to USD2611.38 million), perhaps because of depressed demand following the recent economic downturn. A steady taka-dollar exchange rate could also have contributed to this. In the first 9 months of FY08, Bangladesh was able to register an increase in export of only USD7.57 million to the USA. While export earnings from RMG rose by 1.16 per cent (or increase of USD26.81 million), as noted earlier total export growth was only 0.29 per cent, which indicated declining export earnings from other sectors (barring RMG). With sanctions on China to be withdrawn in January 2009, this should be a cause of concern for Bangladesh. Phase-out of quota on 21 categories of apparels from China (which accounted for about 70 per cent of Bangladesh's export to USA in 2006) is likely to put Bangladesh's export of apparels to US under more competitive pressure in 2009.

It is a matter of interest to note that export to India has been on the rise in recent years. In FY03 export to India was USD84.08 million which increased to USD241.96 million in FY06 and USD289.42 million in FY07. Exports during the first nine months of FY08, matched those of the same period of FY07 registering a growth of 20.43 per cent (taking the tally to USD237.01 million from USD196.08 million). It is important to identify the new products of export to India (ceramic, cement, melamine) and build on this. It is a good sign that the zero-duty offer by India for 8 million prices of garments export from Bangladesh (worth about USD30-35 millions export) has now been put into effect. Bangladeshi exporters should make every effort to realise this offer on the ground. A comprehensive strategy is required to take advantage of the bringing forward the time line for duty-free access by India under the SAFTA and also in view of the decision to reduce the negative list. Although intra-developing country trade is on the rise globally, Bangladesh is yet to take advantage of the expanding markets in developing and emerging economies.

Product and market diversification along with the increase of local value addition, continue to remain major obstacles facing Bangladesh's export sector. Export growth, whilst impressive, has continued to be driven, to a large measure, in terms of volume growth rather than rise in prices. A decomposition evaluation of growth dynamics reveals that the rise in export (15.10 per cent) was accounted for mostly by rise in volume (14.05 per cent) and less by rise in average prices (1.82 per cent). This also needs to be considered in relation to the considerable deterioration of Bangladesh's terms of trade (ToT) experienced in recent years. As is evident from Table 5.2, if prices of FY00 are taken as the base year, TOT declines significantly to 85.6 by FY07. A CPD analysis of export prices and import prices of selected major essential items vividly illustrates the deteriorating ToT (Table 5.3). While in 2006, to import a barrel of crude petroleum Bangladesh had to export 2.34 dozens of RMG, in 2008 it increased to 4.72 dozen. Similarly, to import one ton of rice in 2006 Bangladesh had to export 0.52 tons of jute goods; now in 2008, to import the same amount of rice Bangladesh has to export 1.70 tons of jute goods.

TABLE 5.2: DETERIORATING TERMS OF TRADE

(Base: FY2000 = 100)

	Export Price Index	Import Price Index	Terms of Trade
FY2000	100.00	100.00	100.00
FY2001	102.40	107.53	95.23
FY2002	104.82	115.61	90.66
FY2003	107.44	124.57	86.25
FY2004	115.07	129.62	88.77
FY2005	118.82	134.21	88.53
FY2006	121.18	139.50	86.87
FY2007	124.21	145.14	85.58

Source: CPD Trade Database, 2008.

TABLE 5.3: FALLING PURCHASING POWER OF EXPORTS

	dozens of RMG		Rise (in times)	Tons of Jute Goods		Rise (in times)
	2006	**2008**		**2006**	**2008**	
1 barrel of Oil (Fuel)	2.34	4.72	2.0	0.11	0.23	2.1
1 ton of rice	10.97	34.59	3.2	0.52	1.70	3.3
1 ton of wheat	6.23	17.25	2.8	0.30	0.85	2.9
1 Metric Ton Soya bean Oil	21.19	48.46	2.3	1.00	2.38	2.4
1 Metric Ton Whole Milk Powder	77.87	154.68	2.0	3.69	7.61	2.1

Source: CPD Trade Database, 2008.

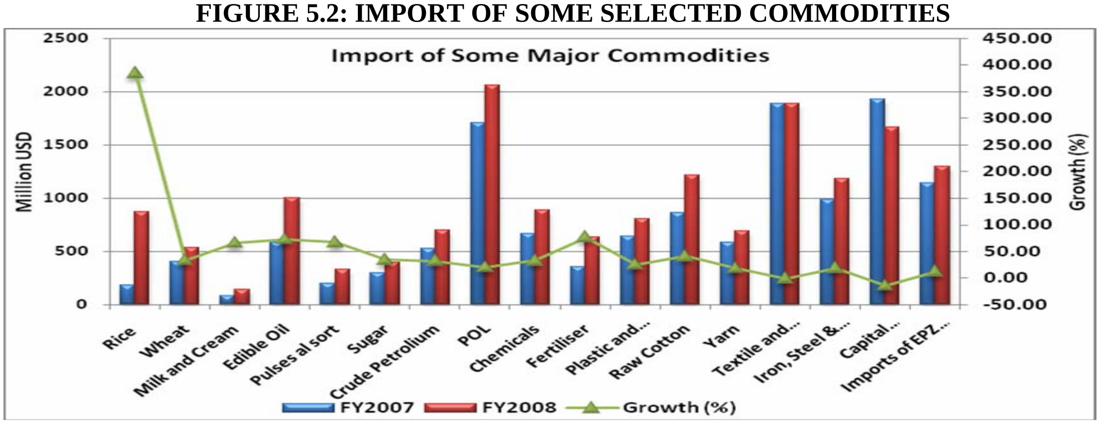
Bangladesh's narrow export base is one of the reasons for the sector's vulnerability in the global market. There is thus a need for both intra-RMG and extra-RMG diversification. Special attention ought to be given to stimulate the production and export of the new non-traditional products such as home textile, light engineering and ship-building. The prospects of ship building industry calls for special mention. Bangladesh has started to gain a foothold in this lucrative market with the first export having been made in May, 2008. A number of Bangladeshi companies have received orders for small-scale ships (of less than 10 thousand dwt). Bangladesh has the maritime tradition and skilled manpower and entrepreneurial expertise to emerge as a major player in the global market for smaller vessels. The sector will need support in such areas as (a) bonded warehouse facilities, (b) availability of bank guarantee, (c) duty rebate for import of capital machineries, and (d) special zoning policy to facilitate setting up of shipyards. The global market for relatively low tonnage ships was worth USD80 billion and if Bangladesh is able to capture a 10 per cent market share, this will be worth USD8 billion!

The ongoing global financial meltdown could have an adverse impact on Bangladesh's export earnings. Countries like Bangladesh with high share of manufactures in its export basket could be harmed because of falling demand. Strengthening market exploration efforts, particularly in emerging economies where economic slowdown could be less severe, should be given high priority.

5.2. Key Features of the Import Sector

Total merchandise imports to Bangladesh during FY08 amounted to USD21.63 billion, registering a growth of 26.07 per cent compared to the corresponding period of FY07. Imports to the EPZs also registered a positive growth of 13.11 per cent. Import share of POL recorded the highest share, around 9.52 per cent of total import. The second highest import share (in value terms) was of textile and articles thereof, accounting for about 8.75 per cent of total import. Imports of foodgrains posted a staggering growth of 142.64 per cent (6.52 per cent of total import), with rice registering a phenomenal increase of 4.9 times and wheat 1.3 times. The huge rise in imports of foodgrains, particularly rice and wheat, was necessary to address the shortage caused by the two consecutive floods and cyclone *Sidr*. (Figure 5.2)

FIGURE 5.2: IMPORT OF SOME SELECTED COMMODITIES

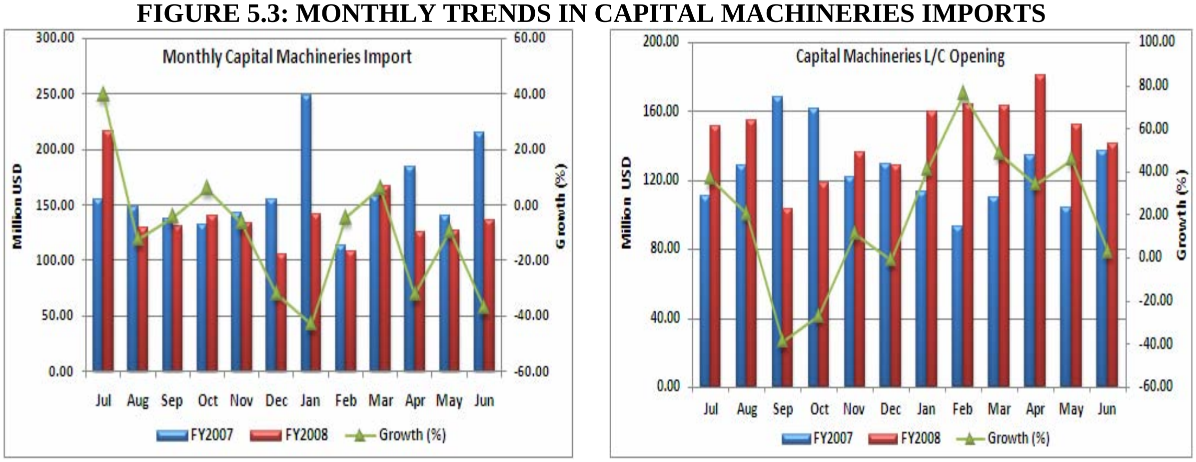


Source: CPD Trade Database, 2008.

Import growth was high to moderate for all major non-food items excluding capital machineries, which posted negative growth rate of (-) 13.74 per cent. Import growth of crude petroleum was high at 32.71 per cent, fuelled by the rise in global oil prices. By the third week of May 2008, crude oil price/barrel has already hit USD132. But in more recent times (22 October 2008), oil price has come down to USD70.60/barrel. Import of POL also posted a huge growth of 20.43 per cent. The bill for this was to the tune of USD2058.00 million. High import growth of intermediate inputs such as raw cotton (41.10 per cent) would indicate further strengthening of backward linkage in textiles; yarn (18.65 per cent) and iron, steel and other base metals (19.73 per cent), also posted significant increase (Figure 5.2).

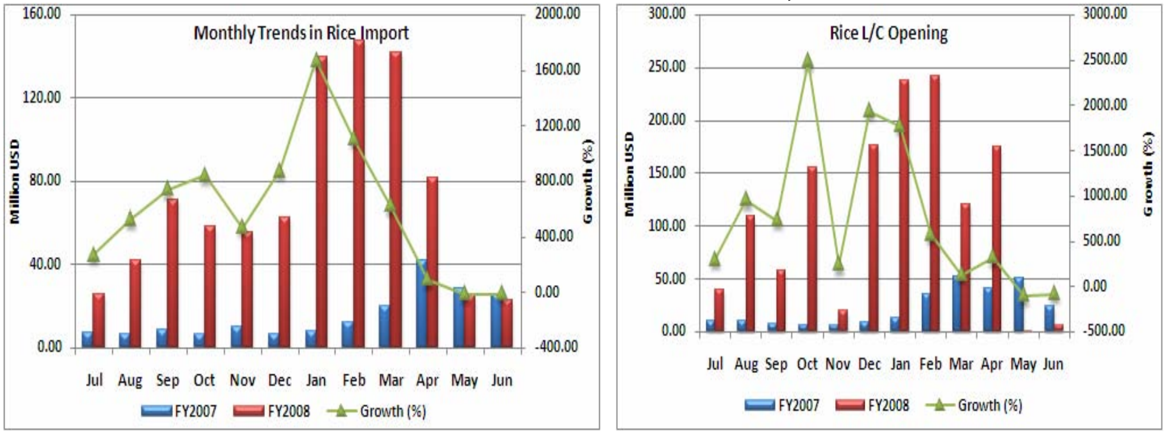
As mentioned earlier, import of capital machineries fell by (-) 13.74 per cent during FY08 compared to FY07. Except for the months of July and March (growth of 6.07 per cent and 6.23 per cent respectively), in all the other months (compared on a month to month basis with the previous fiscal), import of capital machineries maintained a declining trend. Interestingly, opening of L/C in case of capital machineries during FY08 showed a positive trend of 15.96 per cent (Figure 5.3), whereas settlement of L/C for capital machineries revealed a negative growth of (-) 8.38 per cent when compared against the same period of FY07. The fact of declining import of capital machineries is disturbing since this was likely to have negative implications for investment. However, double-digit growth of L/C openings for capital machineries transmits positive signals as to future demand with subsequent positive impact on investment.

FIGURE 5.3: MONTHLY TRENDS IN CAPITAL MACHINERIES IMPORTS



Source: CPD Trade Database, 2008.

FIGURE 5.4: MONTHLY TRENDS IN RICE IMPORTS, IN VALUE TERMS



Source: CPD Trade Database, 2008.

In view of the crop losses caused by two successive floods and cyclone *Sidr*, high import of rice was expected to be a salient feature of FY08. Import of rice rose by about 4.9 times in FY08 (USD873.60) million compared to FY07 (USD180 million). Monthly import trends of rice presented in Figures 5.4 indicate this high growth. Import of rice in FY08 picked up from the very beginning of the fiscal year (July 2007) and continued to be on the rise till March 2008 – not only in value terms, but also in volume terms. Relatively higher growth rate in value terms indicate the effect of rising prices of rice in the international market. Whereas, on average, import parity price (Bangkok) of rice was USD340.25/ton during FY07, it stood at USD584.67/ton in FY08 (an increase of 71.84 per cent in unit price). The price rise of rice was due to the unprecedented increase in global rice price over the preceding one year, combined with the export ban on rice by major rice producing countries.

Increasing global population, higher demand in India and China, soaring demand for bio-fuels and animal feed, and unfavourable weather conditions are major reasons which contributed to the sudden hike in rice prices. Use of corn for ethanol and biofuels started to become economically viable once fuel prices went beyond USD80-90 per barrel. The tension between fuel and food, factory and farm is likely to be a feature in the global scenario with major implications for net food importing countries such as Bangladesh.

5.3. L/C Opening and Settlement

L/Cs opened during FY08 were worth USD24.44 billion, which was 40.02 per cent higher compared to L/Cs opened during FY07. To compare, L/Cs settled in FY08 amounted to USD20.37 billion which was 27.56 per cent higher than FY07. Indeed, as Figure 5.5 indicates, for FY08, L/Cs opened for all commodities registered high positive growth rates ranging from 8 – 40 per cent. For some items including capital machinery, there was a decline in terms of L/C settlement (- 8.38 per cent). Also opening of B/B L/C has registered a positive growth of around 19.51 per cent over the corresponding period.

The high growth trend in case of opening and settlement of L/Cs continued in FY09 as well. L/Cs opened during FY09 (Jul-Aug) were worth USD4.28 billion, which was 19.09 per cent higher than the corresponding period of FY08. Similarly, L/C settled during this period was 31.83 per cent higher than that of the comparing period of FY08. (Table 5.4)

TABLE 5.4: OPENING AND SETTLEMENT OF L/C (FY2008 VS. FY2009, JULY – AUGUST)

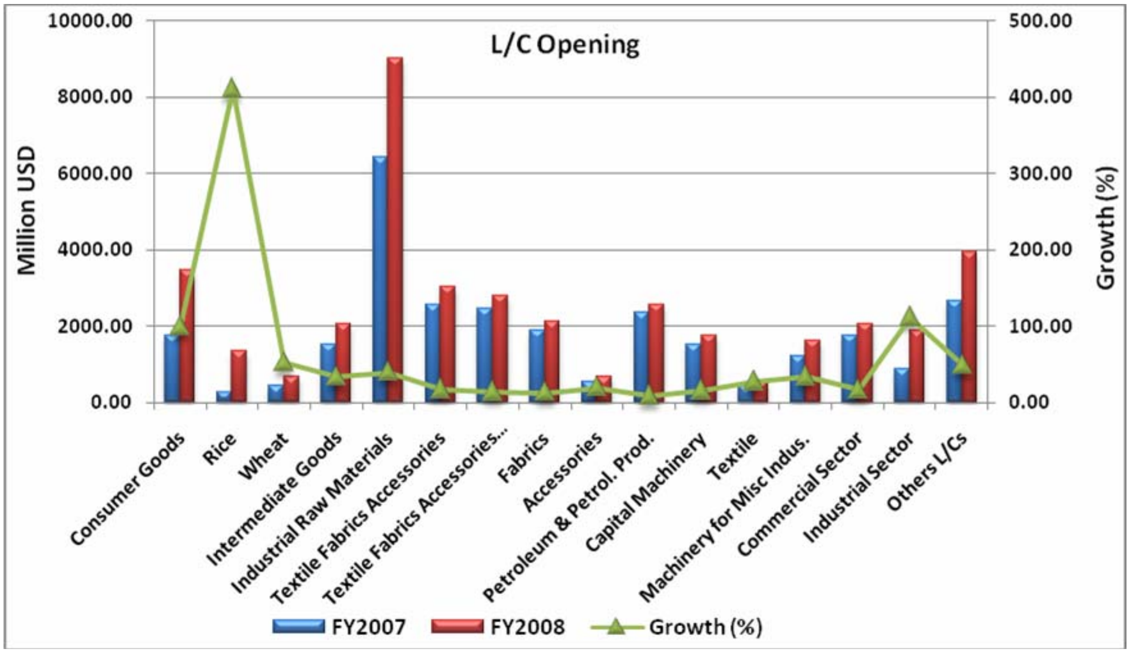
(Million USD)

	FY2008		**FY2009**		**Growth (%)**	
	LC Opening	**LC Settlement**	**LC Opening**	**LC Settlement**	**LC Opening**	**LC Settlement**
Consumer Goods	**526.04**	**334.56**	**269.59**	**277.29**	**-48.75**	**-17.12**
Rice	*149.42*	*69.71*	*0.67*	*81.15*	*-99.55*	*16.41*
Wheat	*168.24*	*69.06*	*98.10*	*16.79*	*-41.69*	*-75.69*
Intermediate Goods	**267.70**	**227.66**	**393.61**	**251.65**	**47.03**	**10.54**
Industrial Raw Materials	**1330.02**	**1114.18**	**1784.82**	**1619.39**	**34.19**	**45.34**
Textile Fabrics Accessories	*468.31*	*463.49*	*554.69*	*545.63*	*18.44*	*17.72*
Textile Fabrics Accessories BBLCs	*432.45*	*426.23*	*513.40*	*512.31*	*18.72*	*20.20*
Fabrics	*338.66*	*327.29*	*394.22*	*393.58*	*16.41*	*20.25*
Petroleum and Petroleum Products	**276.87**	**371.82**	**489.55**	**435.32**	**76.82**	**17.08**
Capital Machinery	**306.80**	**250.81**	**267.30**	**293.63**	**-12.88**	**17.07**
Machinery for Misc Industries	**262.66**	**207.43**	**353.14**	**281.76**	**34.45**	**35.83**
Commercial Sector	*368.05*	*250.29*	*427.81*	*357.24*	*16.24*	*42.73*
Industrial Sector	*252.00*	*161.59*	*289.63*	*331.10*	*14.93*	*104.90*
Other L/Cs	**620.05**	**411.88**	**717.44**	**688.34**	**15.71**	**67.12**
Total	***3590.14***	***2918.34***	***4275.45***	***3847.38***	***19.09***	***31.83***

Source: CPD Trade Database, 2008.

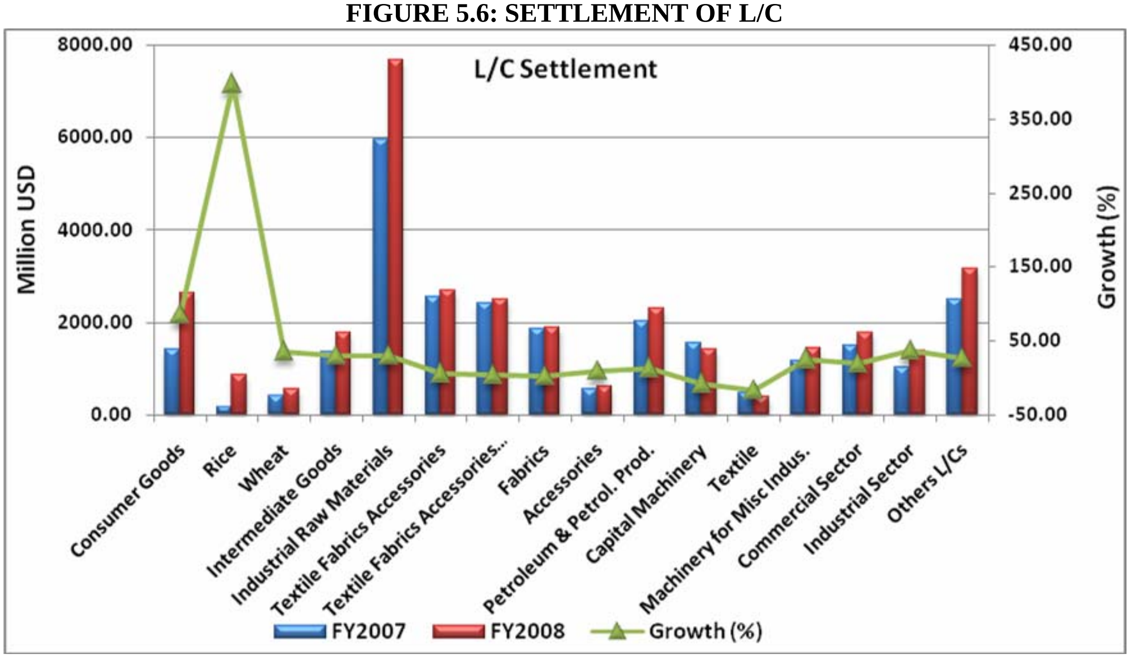
During FY08, L/C opening for consumer goods has been exceptionally high (99.17 per cent), driven by import of cereals, particularly rice, and also wheat, soyabean, vegetable oil etc. As Figures 5.5 and 5.6 bear out, following comparatively lower levels of L/Cs opened for rice in the months of November, May and June the number of import L/Cs opened in other months demonstrated quite high growth (with overall FY08 growth standing at 411.26 per cent). On the contrary, L/C opening for rice during the first two months of FY09 was to the tune of only USD0.67 million – a deceleration of (-) 99.55 per cent in comparison to the same period of the earlier fiscal.

FIGURE 5.5: OPENING OF L/C



Source: CPD Trade Database, 2008.

FIGURE 5.6: SETTLEMENT OF L/C



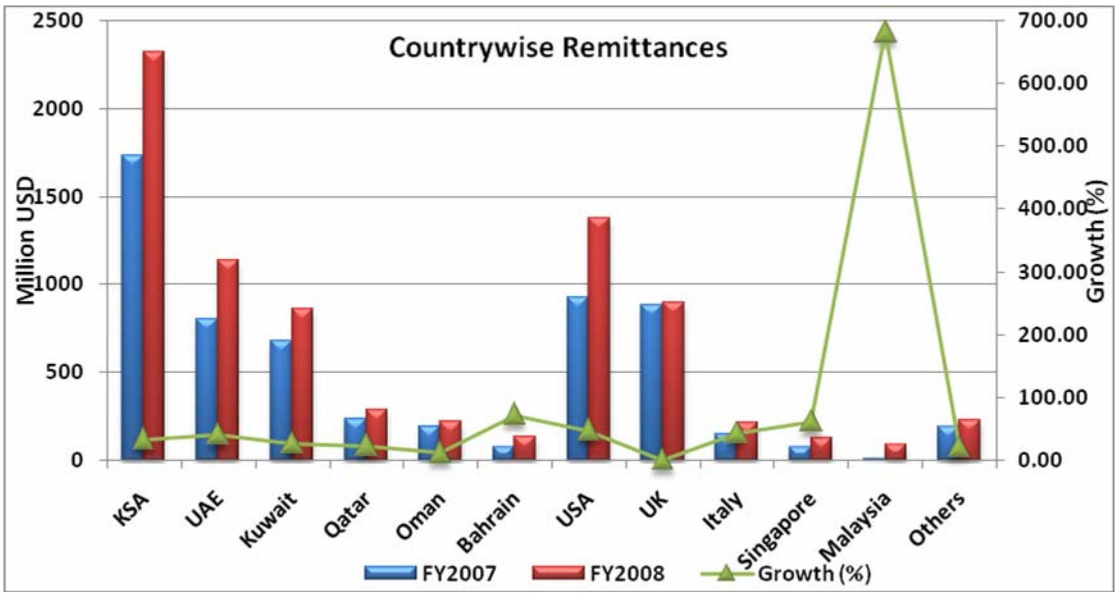
Source: CPD Trade Database, 2008.

In case of wheat, the trend in L/C opening was somewhat inconsistent during FY08, with higher amounts of L/Cs between July – September 2007, lower in October – March period, and again picking up during April and declining during the next 2 months. Overall, import L/Cs for wheat during FY08 increased by 51.68 per cent. During the first two months of FY09 wheat, L/C opening also suffered a serious setback; total L/C opening shrunk by (-) 41.69 per cent.

5.4. Remittance Flow

In recent years, remittance flow has demonstrated phenomenal growth. From under two billion dollars in 2000 (USD1.95 billion), remittance rose to USD7.91 billion in 2008. During the first two months of FY09, earnings from remittance was USD1.54 billion which was about USD504.57 million more than the corresponding period of FY08 (48.61 per cent growth). CPD estimates for FY08 indicate that remittance earnings was equivalent to more than half of Bangladesh's gross export (56.18 per cent), and approximated that of net export (101.00 per cent).

FIGURE 5.7: COUNTRYWISE FLOW OF REMITTANCES



Source: CPD Trade Database, 2008.

It is seen from Figure 5.7 that, Saudi Arabia continued to rank as the major source, accounting for 29.37 per cent of all remittance (FY08), recording a growth of 33.98 per cent compared to FY07. This trend continued also in FY09. During the first two months remittance earnings from Saudi Arabia accounted for 29.85 per cent of our total remittance earnings. Of the other major sources, growth rates of remittance (in FY09) from UAE (67.28 per cent), Kuwait (41.25 per cent) and USA (56.17 per cent) have been very high. Significant growth of remittance earnings has been observed from countries such as Malaysia. During the July – August period of FY08 remittance earnings from Malaysia was only USD2.03 million, which increased to USD27.19 million in FY09, posting an impressive growth of 1239.41 per cent. Though in terms of aggregate remittance earnings this value does not hold much significance considering the earnings from KSA, UAE, USA and Kuwait, it has important policy implications. Contracts signed in FY07 with the UAE, Malaysia and South Korea have contributed importantly to the growth in remittances. Recent market opening in Oman also created a favourable environment for Bangladesh in terms of boosting her manpower export.

However, more than half of Bangladesh's migrant workers belonged to the unskilled group. Average wage of Bangladeshi migrant workers was about 20-30 per cent of those from the Philippines which earned about two and half times more with about half the number of Bangladeshi workers. In view of the need for energetic steps for skill upgradation of migrating workers, initiatives such as private-public partnerships in vocational training, targetted at aspiring workers, ought to be given high priority if Bangladesh is to take advantage of this expanding market. Recent private-sector led initiatives for manpower training for the ship building sector is a welcome initiative. In view of the positive income and equity effect of remittances, there is also a growing need for providing support to facilitate aspiring migrant workers from low income households and backward regions in the form of credit and other facilities. Recently, PKSF has teamed up with BMET, to provide support through easy term loans for aspiring migrant workers from hard core poor families which is a welcome initiative. Organisations such as, Grameen Bank could also think of initiating this type of programme for the poor.

The ongoing global financial crisis could impact on Bangladesh's earnings from remittance. Middle East economies are unlikely to be affected by this, at least in the short term. As a consequence, out-migration and remittances could follow historical trends in 2008-09. However, if the slowdown degenerates into recession it will have adverse impact on both migration and remittance. Countries such as the Philippines, anticipating fall in remittance earnings as a result of global financial crisis, have prepared a "worst-case scenario" incorporating mechanisms to assist their workers. Support to the returnee workers and creating investment opportunities for them should be seen as priority tasks by the policymakers. Consolidation of labour markets in the non-OECD countries, particularly in the Middle East and increasingly in South-East Asia, will be a major task ahead.

5.5. Balance of Payments

Bangladesh's external sector was in tight situation in FY08, with export earnings of USD13.94 billion and import payments exceeding USD19.48 billion in the FY08 (figures cited earlier could vary depending on data in f.o.b. or c.i.f. basis). However, July FY09 experienced an improvement in trade balance in comparison to July of the last fiscal (In July FY08, trade balance was USD507 million whereas in FY09 it came down to USD342 million). Trade balance recorded a larger deficit of USD5541 million in FY08 compared to the deficit of USD3458 million in FY07. However, balance on the current account recorded a surplus of USD672 million in FY08 against the surplus of USD936 million during FY07, mainly thanks to a larger current transfer of USD8743 million. There was surplus in current account in July FY09 (USD269 million) in the backdrop of negative balance in the corresponding month of the last fiscal year (USD130 million). This surplus mainly originated from private transfers in the form of worker's remittances which was USD7915 million in FY08 with a robust growth of 32.38 per cent against USD5979 million in FY07. The growth of workers' remittances also continued in July FY09 (USD821 million) compared to the corresponding period of July FY08 (USD567 million). The overall balance also showed a surplus of USD604 million during FY08 against the surplus of USD1493 million during FY07 due to surplus in current account and capital account of USD672 million and USD576 million respectively (Table 5.5). Overall surplus balance was registered in the first month (July) of FY09 (USD178 million) against the surplus of USD161 million in July of FY08.

TABLE 5.5: BALANCE OF PAYMENT

(In million USD)

	FY2007	FY2008	July FY2008	July FY2009
Trade balance	-3458	-5541	-502	-342
Services	-1255	-1525	-125	-175
Income	-905	-1005	-115	-93
Current transfers	6554	8743	612	879
Official transfers	97	127	0	0
Private transfers	6457	8616	612	879
of which : Workers' remittances	5979	7915	567	821
Current account balance	936	672	-130	269
Capital account	490	576	1	1
Financial account	762	-431	230	-243
Errors and omissions	-695	-213	60	151
Overall balance	1493	604	161	178
Reserve assets	-1493	-604	-161	-178

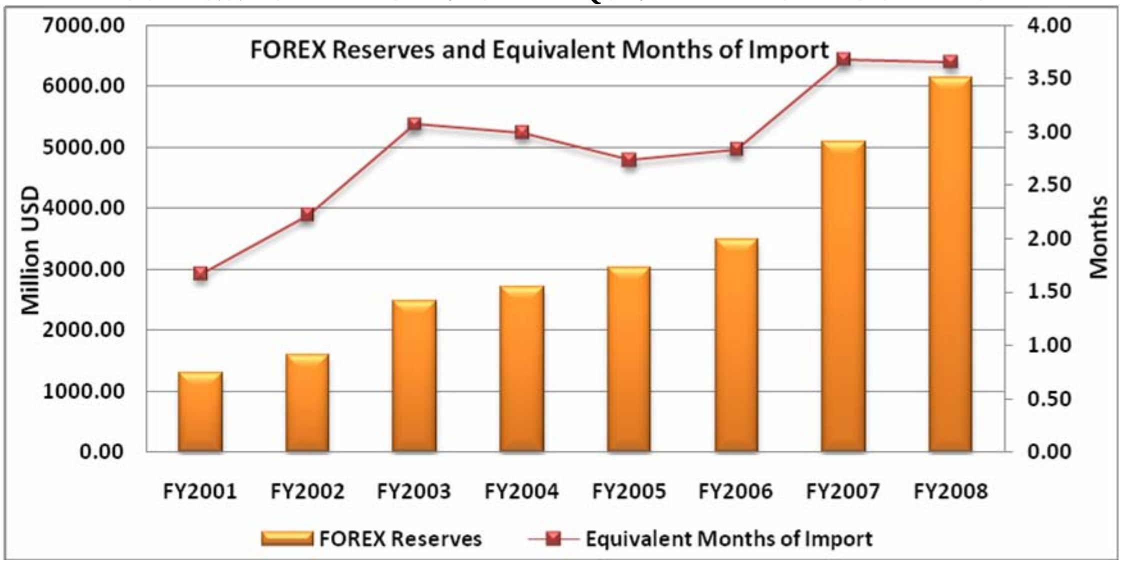
Source: CPD Trade Database, 2008

As observed earlier, balance of current transfer responded positively to robust remittance flow, which increased by 32 per cent (from USD5979 million in the FY07 to USD7915 million in FY08), somewhat compensating for the negative trends in balances on account of trade and services. Performance of related correlates will hinge on the impact of the ongoing financial crisis on export and remittances; however, the fall in commodity prices could play a positive role in this respect.

5.6 Foreign Exchange Reserves

In the backdrop of high export and remittance earnings, the foreign exchange (FX) reserves stood at USD6148.82 million at the end of FY08. This was 21.11 per cent higher than the comparable figure of FY07. The current forex reserve is equivalent to about 3.6 months of import payment (Figure 5.8). Interestingly, the July 2008 data shows that foreign exchange reserves had came down to USD5820.11 million (mainly due to ACU payment of USD591.51 million on 7th July 2008). Gross foreign exchange reserves stood higher at USD5965.77 million in end-August, 2008. This was 14.1 per cent higher than the USD5224.94 million reserves as of end-August, 2007.

FIGURE 5.8: FOREX RESERVES AND EQUIVALENT MONTHS OF IMPORT



Source: CPD Trade Database, 2008

Given the depreciation of the dollar against all foreign currencies, particularly Euro, and given that a large part of Bangladesh's import is from Euro-denominated area, it appears that keeping a higher share of reserves in Euro would be advisable. However, given the volatility in the exchange market, even those businessmen who deal with euro zone countries prefer to deal in dollar terms. As of October 6, 2008, in the total forex reserve 47 per cent was in US dollar, 27 per cent in Euro and 19.5 per cent in Pound sterling. Composition of reserves at present more or less reflects the structure of the business carried out in major currencies. However, there will be a need to carefully monitor exchange rates movements of various currencies so that the most desirable basket of currencies is kept at any particular time.

There is an apprehension regarding the impact of financial crisis on Bangladesh over the near and medium term. Bangladesh Bank (BB) has prudently shifted about USD2,000 million worth of fund, invested in different foreign banks. BB has already shifted some of its reserves from various foreign banks as well which it perceives to be at risk. Commercial banks had about USD500 million worth of foreign exchange assets with various commercial institutions (and savings instruments) abroad (Nostro Account). BB is keeping an eye on activities of commercial banks in this regard and advising them on a day to day basis. Adequate oversight of nostro accounts (which have to be maintained also for L/C and trading purposes) and keeping an eye on the credit rating agencies will be needed. Active exchange rate management will be required in view of competitive devaluation by computing countries and also taking cognisance of the movements of major currencies. Interest of both export and import sector, often conflicting, will need to be considered in this context.

5.7 Foreign Aid

Total aid disbursement in FY08 was higher at USD1956.70 million, compared to USD1624.62 million in FY07. Net receipts of foreign aid during FY08 also stood markedly higher at USD1376.54 million, against USD1099.52 million during FY07. Aid disbursements in July 2008 totalled USD80.01 million, compared to USD38.33 million in July 2007. Net receipts of foreign aid in the same month also stood significantly high at USD23.71 million, compared to USD9.65 million that was received during the same month in the previous year. Recent financial crisis could have an adverse impact on the commitment and disbursement of future foreign aid and Bangladesh will have to remain vigilant in this regards. It is worth mentioning here that following each of the financial crises of the recent past (Japan after its real estate and stock bubble burst in 1990; Finland, Norway and Sweden after their shared crisis in 1991), the donors tended to curb their aid in terms of both their commitment and disbursement. Shortfall of ODA (if there is any) may also have adverse affect on the prospects of attaining the MDGs and financing of the budget shortfall in the short run. The World Bank (WB) has recently promised USD1.34 billion worth of aid to Bangladesh of which USD953 million will be made available to finance seven major projects and the remaining USD38.1 million will be released gradually during the December-June period of FY09, which is expected to ease the pressure on financing budget. On-time disbursement and subsequent effective implementation of aid would be a major challenge for both the CTG and the newly elected government in December. During October, the Asian Development Bank (ADB) also committed to provide a loan of USD165 million of which USD82 million is to help finance large infrastructure projects; USD50 million to assist small and medium-sized energy projects; and, USD33 million to promote renewable energy. The three most critical challenges facing the country are – (a) availability of future aid; (b) disbursement of committed aid; and, (c) effective implementation.

6. SOCIAL SAFETY NET

Social Safety Net Programmes are designed for social protection and social empowerment purposes. Total allocation in the budget for targetted social empowerment, social safety net, poverty reduction, and employment generation (including micro credit support scheme) programmes, for FY08 was Tk. 3893 crores. The target was for 20 lakh people to be directly benefited through these programmes. These programmes are administered by different ministries, departments and organisations. A large number of Non Government Organisations (NGOs) are also involved in the implementation of some of these schemes. Programmes under the social safety net include old-age allowance; allowances programme for the widowed, deserted and destitute women; capitation grant for public and private orphanage; honorarium programme for insolvent freedom fighters; programme for the assistance to the fully retarded; fund for mitigating risk due to natural disaster; fund for rehabilitation of the acid burnt women and the physically handicapped; seasonal unemployment reduction fund; development fund for the readymade garments workers; maternity allowance for the poor lactating mother; VGD, VGF, Test Relief (TR) and Gratuitous Relief (GR).

In FY08, a monthly allowance of Tk. 220 per person was provided to the beneficiaries of the old-age allowance; Tk. 300 per month was provided to the beneficiaries of the ‘Maternity allowance for the poor lactating mother’ programme. Tk. 600 per month was provided to the public and private orphanages for each orphan. The programme for assistance to fully retarded people provided a monthly allowance of Tk. 200 for diasabled studying in the primary level, Tk. 300 for secondary level, Tk. 400 for higher secondary level and Tk. 600 for university level. Tk. 600 was provided as honorarium for insolvent freedom fighters, on a monthly basis. Under the Vulnerable Group Development (VGD) programme women received 30 kg of rice or wheat or 25 kg atta for one year.

During FY08 (July-April), 100 per cent of the target for the full fiscal year was achieved in case of allowances programme to the widowed, deserted and destitute women, and Maternity allowance for the poor lactating mother and Capitation Grant for public orphanage (Table 6.1). More than 99 per cent of the target was achieved in case of Capitation Grant for private orphanage. In case of honorarium programme for insolvent freedom fighters, about 93 per cent of the target beneficiaries were covered, but only 40 per cent of the total budget allocation was spent during July-April of FY08. About 88 per cent of the target beneficiaries received benefit from the programme for the Assistance to the Fully Retarded but total spending was about 66 per cent of the budget allocation. Under the fund for rehabilitation of the acid burnt women and the physically handicapped, 83 per cent of the targetted beneficiaries received support but total spending was only 48 per cent of the budget allocation. Under the VGD programme, 2.60 lakh metric tons of rice has already been distributed among 7.5 lakh women.

TABLE 6.1: UTILISATION OF FUNDS ALLOCATED FOR SOCIAL SAFETY NET PROGRAMMES

(CroreTaka)

Programmes	FY2008 (B)	Target number of beneficiaries (thousand)	Achievement in FY2008 (July-Apr)			Achievement in FY2008 (July-Apr) as % of target	
			Disbursed	Distributed	Number of Beneficiaries (Thousand)	Distribution with respect to FY2008 (B)	Beneficiary
Old-age allowance	448.80	1700	336.60	331.17	1672	73.79	98.39
Allowances programme to the widowed, deserted and destitute women	198.00	750	198.00	198.00	750	100.00	100.00
Capitation Grant for Public orphanage	14.94	10	14.94	14.94	10	100.00	100.00
Capitation Grant for Private orphanage	30.74	42.7	30.78	30.58	42.5	99.48	99.48
Honorarium programme for insolvent freedom fighters	99.50	100	36.00	33.40	93	39.57	92.78
Programme for the Assistance to the Fully retarded	52.80	200	39.60	34.65	175	65.63	87.50
Fund for Mitigating risk due to natural disaster	35.00	n.a.	20.00.	n.a.	n.a.	57.14	n.a.
Fund for rehabilitation of the acid burnt women and the physically handicapped	10.00	6	4.84	4.84	5	48.40	83.24
Seasonal unemployment Reduction Fund	50.00	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Development fund for the readymade garments workers	20.00	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Maternity allowance for the poor lactating mother	17.00	450	17.00	17.00	450	100.00	100.00

Source: Budget Documents.

Four types of programme will be implemented in FY09. These are: (1) Cash Transfer programmes, (2) Food Security Programmes, (3) Micro-Credit Programmes and Special Funds, and (4) Development Sector Programmes. Total outlay for social safety net in FY09 is Tk 16,932 crore which is 2.8 per cent of the Gross Domestic Product (GDP) against Tk 11,467 crore (or 2.1 per cent of GDP) in the revised budget of FY09. Number of beneficiaries from Social Safety Net Programmes is projected to be increased from 366.90 lakh in FY08 to 534.89 lakh in FY09. Thus, allocation for social safety net is planned to be increased by 48 per cent and number of beneficiaries from such programmes will be increased by 45.8 per cent. It is planned that through these programmes employment creation would be to the tune of 257.14 lakh man-month in FY09, compared to 235.75 lakh man-month in FY08 (that is, 9.0 per cent increase in employment generation).

In FY09, monthly allowance for old age, allowance for the widowed, deserted and destitute women and allowance for the financially insolvent disabled have been increased from Tk 220 to Tk 250 per person. Honorarium for Insolvent Freedom Fighters Rate has been raised from Tk.600 to Tk.720 per person per month. Grants for Residents in Government Orphanages and other institutions have been increased from Tk.1,200 to Tk.1,500 on a monthly basis. Capitation Grants for Orphan Students in non-government orphanages has been increased from Tk.600 to Tk.700 per month. Monthly stipend for disabled students has been increased from Tk. 200 to Tk 300 for those studying at the primary level, from Tk. 300 to Tk 450 for secondary level, from Tk. 400 to Tk 600 for higher secondary level and from Tk. 600 to Tk 1000 for university level. Tk. 300 per month is provided to the beneficiaries of the 'Maternity allowance for the poor lactating mother' programme. A new protection scheme for the poor lactating mothers in urban areas will be started in FY09 with an allocation of Tk 20 crore targeting 40 lakh urban low-income lactating mothers.

Programmes under the Ministry of Food and Disaster Management

The government mainly distributes rice and wheat under the *Public Foodgrain Distribution System* (PFDS) through monetised and non-monetised (targeted) channels. Monetised distribution is the sale of rice and wheat through Essential Priority (EP), Other Priority (OP), Large Employee Industries (LEI), Flour Mill (FM), Open Market Sale (OMS), and Fair Price Card (FPC). Non-monetised (targetted) channels include targetted safety net programmes such as Food for Works (FFW), Test Relief (TR), Gratuitous Relief (GR), Vulnerable Group Development (VGD), Vulnerable Group Feeding (VGF), Food for Education (FFE) and other relief channels.

It is to be noted that total distribution of foodgrains under PFDS (including distribution of 231 thousand mt rice distributed as VGF relief obtained from Saudi grant) in FY08 was only 6.7 per cent higher than that of previous year (Table 6.2). Another important point that was noted by the CPD (2008) is that actual distribution of total foodgrains through PFDS during the first six months of FY08 (July-December) was 15 per cent less than the comparable months of FY07, while it was 9 per cent lower for non-priced distribution (Food for Works, VGF, VGD, GR, TR, Others) of foodgrains.

TABLE 6.2: CHANNEL WISE DISTRIBUTION OF FOODGRAINS UNDER PFDS IN BANGLADESH: 2006/07 AND 2007/08.

(In thousand mt)

Channel	FY2006/07			FY2007/08		
	Rice	Wheat	Total	Rice	Wheat	Total
Priced						
Essential Priorities (EP)	153.4	106.9	260.3	128.2	81.3	209.5
Other Priorities (OP)	11.3	9.7	21.0	14.6	5.9	20.6
Large Employers (LE)	5.9	8.9	14.8	7.9	4.4	12.3
Open Market Sale (OMS)	407.9	-	407.9	268.0	-	268.0
Flour Mill (FM)	-	2.0	2.0	-	-	-
Fair Price Campaign (PC)	-	-	-	-	-	-
Other	-	-	-	-	-	-
Sub Total	***578.5***	***127.5***	***706.0***	***418.7***	***91.6***	***510.4***
Non-Priced						
Food for Work (FFW)*	121.3	0.2	121.7	98.5	55.9	154.3
Test Relief (TR)	148.2	-	148.2	65.6	10.4	75.9
Vulnerable Group Development (VGD)	103.0	44.3	147.3	198.5	69.2	267.7
Vulnerable Group Feeding (VGF)	230.2	-	230.2	187.6	-	187.6
Gratuity Relief (GR)	33.3	0.2	33.5	38.2	-	38.2
VGF (Relief)						231.0*
Others	57.9	15.8	73.7	73.7	21.5	95.1
Sub Total	***693.9***	***62.3***	***756.2***	***661.9***	***156.9***	***818.8***
Total	**1272.4**	**189.8**	**1462.2**	**1080.7**	**248.5**	**1560.2**

Note: * includes direct distribution of wheat by World Vision International;
** In FY08, 231 thousand mt foodgrain have been distributed as VGF relief (Saudi grant) through non-priced channel.

Source: Food Planning and Monitoring Unit (FPMU), Ministry of Food and Disaster Management.

In FY09, the government has planned to distribute 29 lakh 74 thousand metric tons of foodgrains though the monetised and non-monetised channels under the PFDS. During the July-September period of FY09, a total of 366.47 thousand metric tons of foodgrains were distributed under the PFDS which was 54.7 per cent higher than that the comparable months of FY08 (Table 6.3).

TABLE 6.3: CHANNEL-WISE DISTRIBUTION OF FOODGRAINS UNDER THE PFDS IN BANGLADESH: 2008/09 (JULY-SEPTEMBER) AND 2007/08 (JULY-SEPTEMBER)

(In thousand mt)

Channel	July – September FY08			July-September FY09		
	Rice	Wheat	Total	Rice	Wheat	Total
Priced						
Essential Priorities (EP)	15.81	12.97	28.78	32.95	21.15	54.10
Other Priorities (OP)	3.30	1.67	4.97	4.83	0.91	5.75
Large Employers (LE)	0	4.41	4.41	2.90	0.00	2.90
Open Market Sale (OMS)	48.08	0	48.08	119.72	0.00	119.72
Flour Mill (FM)	0.00	0	0	-	-	-
Fair Price Campaign (PC)	0	0	0	-	-	-
Credit Sale	17.28	9.05	26.33	-	-	-
Other	0	0	0	0.00	0.00	0.00
Sub Total	***84.49***	***28.11***	***112.6***	***160.40***	***22.06***	***182.46***
Non-Priced						
Food for Work (FFW)*	0	0	0	0.35	0.17	0.53
Test Relief (TR)	0	0	0	0.68	1.60	2.28
Vulnerable Group Development (VGD)	48.09	14.62	62.71	43.61	23.91	67.52
Vulnerable Group Feeding (VGF)	43.99	0	43.99	69.62	0.00	69.62
Gratuity Relief (GR)	11.59	0	11.59	1.61	0.00	1.61
VGF (Relief)	-	-	-	34.13	0.00	34.13
Others	1.00	5.035	6.03	8.32	0.00	8.32
Sub Total	104.68	***19.66***	***124.33***	***158.32***	***25.68***	***184.01***
Total	**189.17**	**47.78**	**236.93**	**318.72**	**47.74**	**366.47**

Source: Food Planning and Monitoring Unit (FPMU), Ministry of Food and Disaster Management.

7. CONCLUDING REMARKS

As was noted at the very outset of this paper, Bangladesh economy will be passing through challenging times in FY2008-09. Data is scant with regard to most of the critically important macroeconomic indicators for FY09. Early signals, however, indicate some improvements in trade and current account balance in July, FY09, underwritten by robust export performance and some slowdown in import growth. High growth of fresh L/C opening for intermediates and raw materials during the first quarter of FY09 should transmit positive signals for the performance of the productive sectors in FY09. Import of capital machineries has picked up in FY09 and openings under back-to-back L/Cs, mostly for apparels, have also posted very high growth. Opening of import L/Cs for consumer goods, as expected, has declined in view of the falling commodity prices in the global markets. Remittance receipts have kept up with the high trends seen in the recent past, helping to keep forex reserves at USD5965.8 million in end-August, 2008. Foreign aid flow is also expected to be high in view of the commitments by the World Bank and the ADB. The aid flow should match the high flows of FY08 when it reached USD1.96 billion.

Capital market is seeing some volatility; oversubscription for new IPOs is somewhat dampened. Expected offloading of Grameen Phone shares should help in bringing back some of the lost buoyancy in the country's stock market.

Thus Bangladesh economy stands challengingly poised as it moves towards the half-way mark of FY09 in December 2008. Several new concerns having important implications for macroeconomic performance in FY09 have to be addressed in the course of the coming fiscal year.

The Ongoing Global Financial Crisis

The consequences of the ongoing global financial crisis for the Bangladesh economy are too early to predict with a measure of reliability; much will depend on how the crisis evolves and unravels in the near term. Three possible scenarios could unfold, though, with the implication for economies such as that of Bangladesh depending on the width and depth of the crisis. In the *first scenario*, the crisis leads to a slowdown in global economy but is followed by a quick upturn. The financial rescue packages start to work and the developed country economies get back to their recent growth trends. The *second scenario* could be a recession lasting for 1-2 years with negative to zero growth rates. This would result in sluggish demand and higher rates of unemployment in developed economies. The *third scenario* could be one where recession develops into depression, lasting for 3-4 years, with negative growth rates, high unemployment in developed countries, and a drastic fall in effective demand. This is likely to have dire global repercussions. Impact on and implications for Bangladesh economy will critically hinge on which particular scenario actually emerges from the current crisis. Anything bordering the third scenario will have adverse consequences for economies such as Bangladesh, while even the second scenario is likely to be detrimental to the interests of Bangladesh economy in FY09.

There are several transmission mechanisms through which global financial crisis could impact on the Bangladesh economy. Exports, although earnings posted a very high growth in July, 2008, could slow down in the face of sluggish demand in the developed country markets which account for four-fifths of Bangladesh's global exports. Anecdotal information from apparels exporters indicate some slowdown in order placement, although it is still not clear whether it is cyclical, seasonal or is originating from the expected sluggish consumer demand in developed countries. In general, low-priced, mass-produced items, where Bangladesh is most strong, are not affected by economic slowdown in developed market since income elasticity of such items tends to be very low. Economic slowdown could even induce some shift in demand from the middle-segment of the market to the lower-end (the so-called Wal-Mart effect). Indeed, Wal-Mart sales went up by about 3 per cent in August 2008. However, a tightening of apparels price is to be expected, with major buyers putting pressure on exporters to reduce their price offers. Additionally, WTO negotiations could be adversely affected because of the global crisis and initiatives such as the DF-QF market access for LDCs may not witness much progress. Developed countries could become more protective. Initiatives such as the New Partnership for Development Act (NPDA 2007) could become victims of the crisis.

Remittance flow, three-fourth of which comes from the Middle-Eastern countries, could be affected if there is a recession in developed economy with knock-on effect on investment flow to the region.

Commodity prices are coming down already; any economic slowdown could lead to further fall in prices. This should benefit commodity dependent Bangladesh and have positive impact on the inflationary situation in the economy. The challenge will be to identify an optimal strategy to pass on the benefits to the long suffering consumers. Evidently, in case of commodities such as fuel cross-subsidisation considerations (between octane, petrol, diesel and kerosene) will be required.

The aid scenario is promising in FY09 with the CTG having negotiated commitments with the World Bank and the ADB. However, as has been seen in earlier recessions, aid to developing countries tends to be an early and soft target. Aid fatigue, thus, could set in. This will be particularly relevant for commitments by developed countries in the context of Aid for Trade in the WTO, support for Millennium Challenge Fund in the USA and in case of bilateral trade.

Of crucial importance in view of the above discussion will be how Bangladesh manages exchange rate of BDT with major currencies. Here, the interest of exporters, particularly taking into consideration competitive devaluation by neighbouring countries, on the one hand, and interest of domestic consumers who are interested to benefit from declining commodity prices in the global market, on the other, will need to be cleverly balanced.

Bangladesh's share market is not exposed to global capital flows to any large extent (only about 2.5 per cent in the context of market capitalisation of about USD14.0 billion). However, the continuing need for strengthening of the oversight function of SEC should not be undermined. Whilst the ongoing crisis sends a cautionary note with regard to risky and foreign currency denominated derivatives, opportunities to attract portfolio investment to Bangladesh's share market should not be left unattended, and will need to be explored and exploited.

A CPD dialogue held on October 25, 2008 suggested that a "Task Force" be set up to monitor the impact of the global crisis on the economy and to recommend appropriate measures to the government with a view to addressing the attendant risks and problems, and also to realise the potential opportunities.

Issues That Will Need Urgent Attention

As was pointed out earlier, one of the major challenges facing Bangladesh in the coming months lies in ensuring a credible and smooth transition to democratic governance. Whilst the CTG will have been responsible for macroeconomic management during the first half of FY09, the burden of managing the economy during the second half will hopefully fall on the shoulders of the newly elected government. Implementation of the PRS-II (2009-11) will also be the responsibility of the new government. A number of institutional measures and initiatives undertaken by the CTG, aimed at raising efficacy of public institutions and quality of governance, improving efficiency of regulatory institutions, raising social empowerment, and enhancing overall efficiency and efficacy of macroeconomic management, should help the elected government in addressing the challenges it may face in this regard.

In view of the enormity of the tasks awaiting the new government, it will need to prioritise its actions for the second half of FY09.In case of many challenges comprehensive policy recommendations already exist. The task will be to ensure their high quality implementation. Some of the tasks that require urgent attention appear to be the followings:

- *Energy Security:* Lack of gas and power has emerged as a major limiting factor in the context of realising Bangladesh's potentials for development. The newly elected government will need to come up with a comprehensive strategy to ensure energy security of the country. This strategy will need to have short, medium and long term goals, and a road map to realise the targets. Of critical importance here will be decisions in such areas as finalising the coal policy, completing the off-shore bidding process, appropriate pricing of power and energy, building of necessary infrastructure, strengthening of Bangladesh's own capacity to explore, institutional strengthening of BPC and setting conditions to attract FDI to the power sector.

- *Bringing Down the Inflationary Pressure:* FY08 will go down as the year of high inflation in Bangladesh's recent economic history. Whilst inflationary pressure is expected to come down in response to the general trend of falling prices in the global market, and devaluation in major import sources (e.g. India), consumers will gain only if and when transmission mechanisms from import to retail and consumer levels work efficiently and effectively. More focus on meeting domestic market demands from domestic produces will be required. All out effort to raise productivity will have to be given. Raising purchasing power of people through employment creation in sectors with high productivity will have to be given high priority. Of critical importance here will be a prudent exchange rate management and implementation of a pragmatic interest rate policy. Monetary policy should be geared towards creation of effective demand and raising the level of production and productivity and encouraging investment.

- *Reducing Income Inequality and Regional Disparity:* An emerging issue of heightened policy concern is the increasing income inequality and the growing regional disparity in Bangladesh. Although Bangladesh has been able to achieve appreciable results in terms of poverty alleviation in the recent past, because of high inflation a reversal of these trends over the last couple of years is discernible. Whilst estimates vary, the fact of severe income erosion of the poor is accepted by all. A major task of the newly elected government will be to undertake targeted programmes that reduce income inequality and regional disparity. Targetted investment programmes, connecting the backward regions with opportunities of domestic, regional and global markets (goods, and also services market that create opportunities for remittance earnings) will be required. A renewed effort to create employment opportunities in rural non-farm areas through credit and skill development programme is needed. Developing a healthy and educated workforce should receive the highest priority. Targetted efforts will be required to reduce the rural-urban gap in terms of both access to and quality of education and health services. In view of the increasing gap between what is available and what is required in health and education sectors, a renewed effort is needed to improve the quality of health and education services. Effective public-private partnership for services delivery will have to be worked out. Incentives to connect commercial banks with rural farm and non-farm investment activities should be given attention. The budget for FY08 and also FY09 have made provisions for targeted investments for development of backward regions. The newly proposed Employment Guarantee Scheme should reflect this priority. Social Safety Net funds should be appropriately allocated and efficiently utilised. There is a need for raising the efficiency of public food distribution and other safety net programmes through better targeting, timely delivery of services and prevention of leakages.

- *Ensuring Food Security:* The volatility seen in the global foodgrains market in FY08 should have a sobering effect for future stewards of country's macroeconomic governance. Whilst avenues for effective interface with the global market (through import by both public and private sector, mechanism for speedy delivery, ability for market intervention through import, maintaining food stocks by way of import) should receive due attention, priority should be given to domestic self-sufficiency in foodgrains production. Introduction and adoption of modern agricultural practices must be seen as a necessary precondition for raising both productivity and production in the agriculture sector. R&D in agriculture, development of local HYVs, crop insurance, agricultural credit and marketing should receive highest attention of policymakers in this regard. Bangladesh should also not lose sight of emerging global market opportunities in agricultural trade, particularly in view of the more liberal trading regime that could emerge as a result of the ongoing WTO negotiations in agriculture. Here, maintaining quality and ensuring compliance with SPS-TBT standards will play a critically important role.

- *Export Diversification and Realising Global Market Opportunities:* Both intra-RMG and extra-RMG diversification ought to receive high priority. For this, both domestic investment and higher FDI flow will be required. Till now strategies to develop thrust export sectors have not been very successful. Sectors such as home textiles, ship-building and pharmaceuticals need to be supported with appropriate incentives, infrastructure, skill development programmes and R&D. Of critical importance here will be to connect Bangladesh's agriculture with global export opportunities. Graduating to upmarket segment of the apparels market should be seen as a strategic move to ensure higher value addition and intra-RMG diversification. In view of this, strengthening fashion and design capabilities, handing over management of selected vocational training institutions to trade associations, developing clusters and providing common facilities such as effluent treatment facilities should be given priority.

- *Implementing the PRS-II:* As is known, PRS-II was finalised recently. There is an apprehension that PRS-II, prepared under the CTG, may not be 'owned' by the newly elected government. Whilst the elected parties will be guided by their election manifestos in economic management, the PRS could provide an important guideline for initiating various programmes. The task of preparing a strategic document, be it a revised version of PRS-II or the PRS-II itself or a new plan document, should receive highest priority. This will be the prerogative of the new government. The Medium Term Macroeconomic Framework (MTMF) targets in the PRS-II could also be revisited in view of the emerging economic situation, global scenario and the priorities of the new government. However, whatever be the decision, it should be made on an urgent basis. The mandate of the Parliamentary Standing Committees should be strengthened so that these could function independently and efficiently and ensure a continuing monitoring and oversight of macroeconomic governance.

- *Elections and Economic Governance:* The nation is waiting for the parliamentary elections to be held in December 18, 2008. Whilst it is understandable that formation of the government and political issues will receive priority in the first few weeks, the urgency of getting on with the task of economic governance should be given highest priority. Concrete economic policy plans and action programmes, prepared as part of the party manifestos, will help political parties in initiating various activities related to macroeconomic management in a speedy manner. The government could think about constituting task forces for policy leadership in key areas. Some of these could be to address Food Security, Energy

Security, Global Financial Crisis, Productivity Enhancement, Skill Development, SME Development and Export Diversification.

- *Global Crisis and the Need for Vigilance:* Some of the possible negative consequences of the ongoing financial crisis have already been mentioned in this section. It is to be noted and appreciated that the Bangladesh Bank was able to take prompt and pre-emptive measures in anticipation and in view of the ongoing financial crisis. The reserves were put in more secured assets, exchange rate basket was reviewed to reflect relative strength of currencies, foreign assets of commercial banks including the component kept in 'nostro accounts' were brought back to reduce risk and exposure. There will be a need to continue this vigilance in future, particularly by keeping a cautious eye on exchange rate movements, exposure of commercial banks and capital movements. Further strengthening of BB's supervisory role and oversight functions of the SEC should be given highest priority.