

# **EXTERNAL SECTOR: RECENT TRENDS AND CHALLENGES**

**Bangladesh Economic Update**

**October 2015**



### **Acknowledgement**

Bangladesh Economic Update is a monthly publication of the Economic Policy Unit of Unnayan Onneshan, a multidisciplinary research organisation based in Dhaka, Bangladesh. The report has been prepared by **Ebney Ayaj Rana**. The Update has been copy edited by **Abid Feroz Khan**.



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## 1. INTRODUCTION

The current issue of Bangladesh Economic Update attempts to understand the current status of external sector against the backdrop of trade imbalance, negative balance in the account of service for a long time, declining rate of growth in remittance inflow, unsatisfactory inflow of Foreign Direct Investment (FDI), and large gap between the commitment and disbursement of foreign aid in the country.

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The Update reveals that imbalance in the current account of FY 2014-15 compared to that of FY 2013-14 is likely to exert pressure on country's balance of payments and thus on the trend in external sector. Overall external balance is showing positive balance because of inflow of one or two items in a huge amount, but decrease in remittance and export of manpower, increasing deficit in service and trade balance are likely to impede the growth rate of the economy.

Inflows of remittance become negative in the last Fiscal Year (FY) for the first time within ten years mainly because of the decline in labour migration in major markets like Saudi Arabia and UAE. This declining inflow of remittance is likely to exert adverse impact on rural economy since consumption and expenditure of people living in rural areas are largely contingent upon remittance sent by their household members living abroad.

Increase in Import payments and export earnings show a decrease in trade deficit, because earnings from export grow more than that of import payment. However, decrease in the disbursement of industrial term loan and the recent political contestations in the country may create an uncertain business environment as regards setting up new industries resulting in decreased investment demand-induced import of capital machinery which will further affect the trade balance.

Large gap between commitment and disbursement of foreign aid and insufficient foreign direct investment over the years have been noticed which can be ascribed mainly to lack of infrastructural facilities and political tumult as well as a good deal of foreign aid trapped in the pipeline. In these circumstances, the Update concentrates on the composition, sources, directions and performance of export and import over the years.

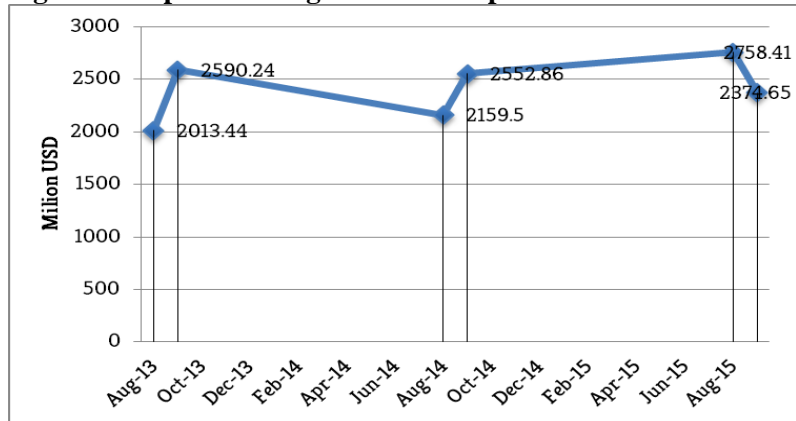
## 2. EXPORT EARNING

Export earnings declined by 13.91 percent in September 2015 compared to the month of August 2015 and stood at USD 2.37 billion. In addition, export earnings fell by 6.98 percent in September 2015 compared to that in September 2014. However, export increased slightly by 0.83 percent in July-September 2015 compared to the corresponding period of the previous year. However, export earnings showed a negative rate of growth in the first month of FY 2014-15 which was positive in same period in previous year 2013-14 for especially decreasing export in the non-traditional markets. In July'2014 Export earnings decreases to USD 2982.74 million from USD 3024.29 in FY2013-14 million represent a decrease in growth rate to -1.37 percent from 23.99 percent that is 25.36 percentage point decrease. Moreover, export earning is increasing from FY 2010-11 to FY 2013-14. In FY 2009-10, export earnings were USD 16204.7 million. In FY 2012-13, export earnings were USD 27027 million which stand to USD 30186.6 million in FY 2013-14. The consequences of global economic recession, political crisis in North Africa and the Middle East exacerbated the situation of the import expenditure and the export earnings in Bangladesh in FY 2011-12.

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In FY 2011-12, the growth rate of export earning was 5.99 percent which was 41.49 percent in FY 2010-11 which implies 35.5 percentage point decrease in the growth rate in export. The decreasing rate of raw jute (25.4 percent), jute goods (7.5 percent) and ceramic products (10.2 percent) decreased the export earnings in FY 2011-12. The growth rate in export then increases to 11.22 percent in FY 2012-13 and 11.69 percent 2013-14 which shows a positive trend. Taking account the export earnings and its growth rate for five years it can be projected that in FY 2014-15 and FY2015-16 export earnings will be USD 32575 million and USD 34964.72 million.

**Figure 1: Export earnings over recent periods**



Source: Bangladesh Bank, 2015a

### 2.1. Sector-wise Export Earnings

Category-wise breakdown of exports shows that during July, 2014 exports of knitwear, frozen food and chemical products experienced positive growth compared to the same period of the previous year. On the other hand, exports of woven garments, jute goods (excluding carpet), agricultural products, engine and electric goods, leather and raw jute experienced a negative growth in July compared to the same period of the previous year.

**Table 1: Commodity-wise breakdown of export earnings**

Particulars	July-September 2015	July-September 2014	Changes during July-September 2015 over July-September 2014	
			In absolute amount	In percentage
Raw Jute	52.54	23.19	29.35	126.56
Jute Goods	154.02	174.23	-20.21	-11.60
Tea	0.46	0.78	-0.32	-41.03
Frozen Food	120.07	190.8	-70.73	-37.07
Leather	70.73	109.29	-38.56	-35.28
Woven Garments	3189.12	2962.71	226.41	7.64
Knitwear	3250.11	3270.46	-20.35	-0.62
Chemical Products	25.73	25.54	0.19	0.74
Agricultural Products	43.67	82.51	-38.84	-47.07
Engine and Electric Goods	130.98	83.48	47.5	56.90
Others	721.56	772.11	-50.55	-6.55
<b>Total</b>	<b>7758.99</b>	<b>7695.1</b>	<b>63.89</b>	<b>0.83</b>

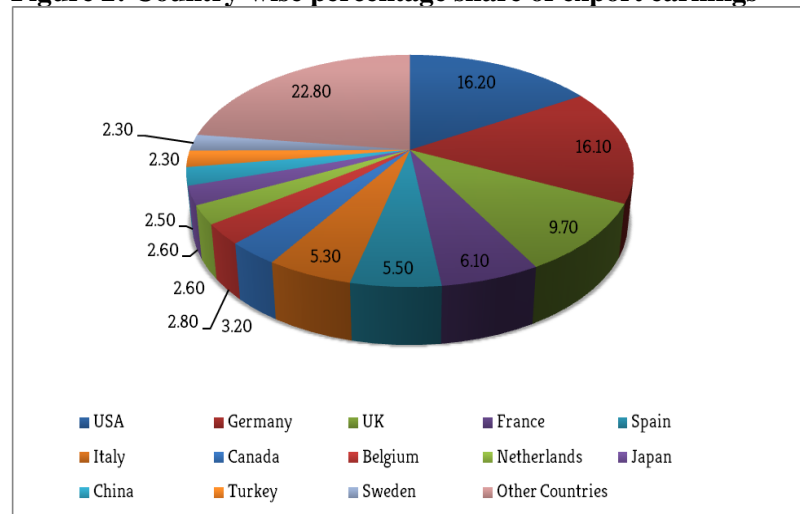
Source: Bangladesh Bank, 2015b

*Export earnings are mounting at an increasing rate over the years because of the increasing exports to the traditional market like USA, European countries like Germany, France, United Kingdom, Italy and Spain.*

## 2.2. Destination of Exports

Export earnings are mounting at an increasing rate over the years because of the increasing exports to the traditional market like USA, European countries like Germany, France, United Kingdom, Italy and Spain. During the period of January-March of FY 2014-15, major exports go to USA worth as USD 1024 million which is 16.2 percent of the total export as compared to 15 and 18.5 percent during the period of October-December of 2014 and January-March of 2014 respectively. Out of the various commodities such as fish and shrimp, jute goods, leather, raw jute, readymade garment was the highest contributor to increase export in Bangladesh. The second largest buyer is Germany which was 16.1 percent during the period of January-March of 2015 as compared to 16.3 percent during the corresponding period of the previous fiscal year. In addition, export to UK, France, Spain, Canada, Italy, Netherland, India and Turkey as percent of total export increased by a decreasing rate. However, in FY 2012-13, the export from Bangladesh was highly concentrated in few markets. For example, in FY 2013-14, 65.66 percent of total export earnings has come from nine countries- USA, Germany, UK, France, Belgium, Italy, Netherlands, Canada and Japan.

**Figure 2: Country-wise percentage share of export earnings**



Source: Bangladesh Bank, 2015a

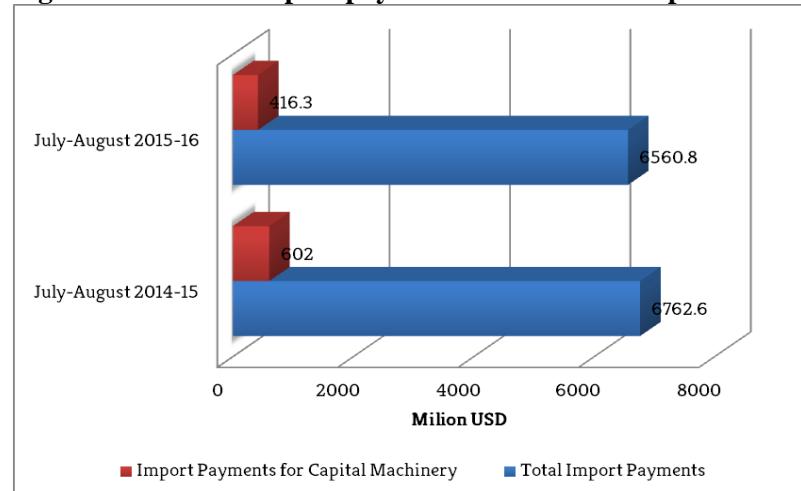
## 3. IMPORT PAYMENT

The total import payments during the period of July-August 2015 decreased by 2.98 percent and stood at USD 6.56 billion compared to USD 6.76 billion during the corresponding period of 2014. The import of capital machineries declined by

*Due to the continuous contractionary monetary policy, liquidity crisis and shortage of US dollars, imports of capital machinery and industrial raw materials massively decreased in the last two fiscal years before 2013-14.*

30.85 percent during the period of July-August 2015 and stood at USD 416.3 million compared to USD 602 million in July-August 2014. However, import payment decreased from FY 2010-11 because of lower import of food grains, capital machinery and industrial raw materials and the continuous bumper harvest of food grain. Due to the continuous contractionary monetary policy, liquidity crisis and shortage of US dollars, imports of capital machinery and industrial raw materials massively decreased in the last two fiscal years before 2013-14. In FY 2012-13, import payments were USD 34084 million which was decreased by 4.03 percent as compared to USD 35516 million with a growth rate of 5.52 percent in the corresponding previous fiscal year but in 2013-14 import payment increases to USD 40692.92 million; a increase of 19.39 percent.

**Figure 3: Trend in import payments over the recent periods**



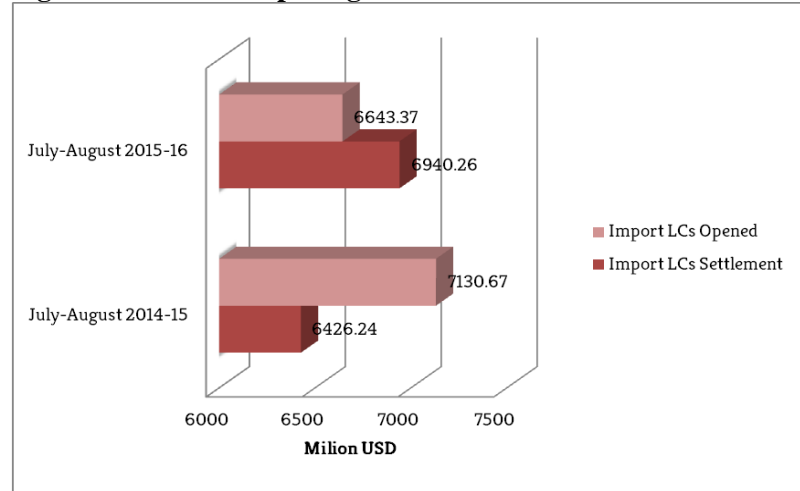
Source: Bangladesh Bank, 2015a

### 3.1. Opening and Settlement of Letter of Credit

Settlement of import letters of credit (LCs) during July-September, 2015 increased by 8.00 percent and stood at USD 6.94 billion against USD 6.43 billion in July-August, 2014. Fresh opening of import LCs during July-August, 2015 decreased by 6.83 percent and stood at USD 6.64 billion compared with USD 7.13 billion in July-August, 2014. Import payment shows an upward trend in FY 2013-14 compared to FY 2012-13 in terms of opening and settlement of LCs. However, import payment in July-June of FY 2013-14 was USD 37188.84 million which was USD 32358.52 million in July-June of FY 2012-13. Industrial raw materials, machineries for miscellaneous industries, petroleum and petroleum products, consumer goods, and intermediate goods rise both in terms of

opening of fresh LCs and settlements. During July-June period of FY 2012-13 opening of fresh LCs was USD 35961.05 million but rises to 41818.56 in FY 2013-14 which implies a 16.29 percent increase.

**Figure 4: Trends in opening and settlement of LCs**



Source: Bangladesh Bank, 2015b

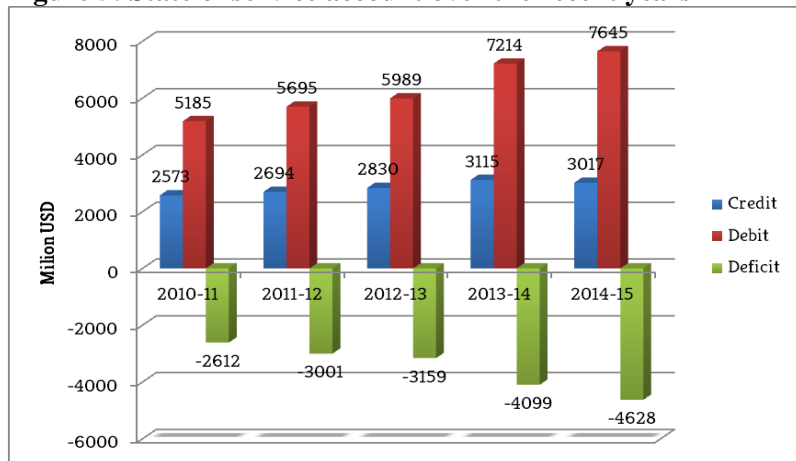
*A gap of USD 4099 million in FY 2013-14 and USD 4628 million in FY 2014-15 is found in service in balance of trade. In FY 2013-14 and FY 2014-15, the amount in credit in service was USD 3115 million and USD 3017 million respectively, whereas the amount in debit was USD 7214 million and 7645 million respectively.*

### 3.2. Service Account

A gap of USD 4099 million in FY 2013-14 and USD 4628 million in FY 2014-15 is found in service in balance of trade. In FY 2013-14 and FY 2014-15, the amount in credit in service was USD 3115 million and USD 3017 million respectively, whereas the amount in debit was USD 7214 million and 7645 million respectively. A large imbalance in service sector is prevailing for a long time which remains unnoticeable. The components of service sector are intangible which are travel, transportation, commercial services and government services. In 2013-14 the gap between the credit and debit was USD 4189 million which was USD 3162 million in 2012-13; 32.42 percent increase in gap. The increasing deficit in service explicates that our economy not only lagging behind in terms of trade but also in terms of service which is worsening the balance of payment.



**Figure 5: State of service account over the recent years**

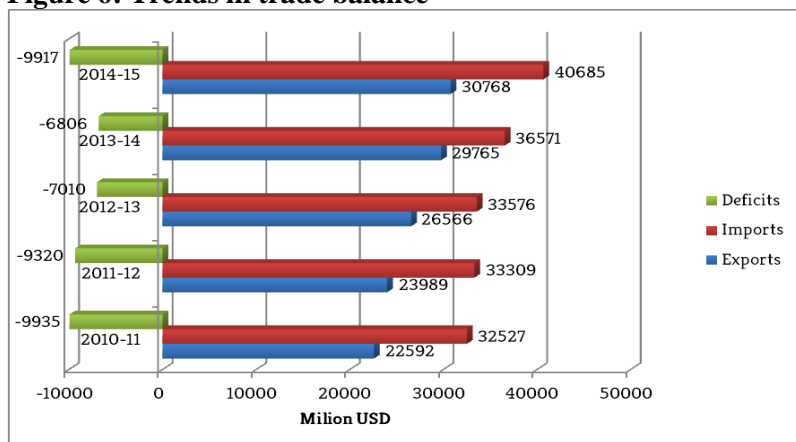


Source: Bangladesh Bank, 2015b

#### 4. TRADE BALANCE

The country has been experiencing a negative balance of trade, importing more goods than export. The deficit in trade balance increased significantly and stood at USD 9917 million in FY 2014-15, whereas the deficit was USD 6794 million in FY 2013-14. Trade balance slightly decreased to USD 6806 million in FY 2013-14 from USD 7010 million in FY 2012-13 and from USD 9310 million in FY 2011-12. The reason behind the decline in negative trade balance is that the increase in export. If the trend remains as usual, trade deficit might decline to USD 2494.33 million in 2013-14 and to USD 2667.71 million in 2015-16.

**Figure 6: Trends in trade balance**



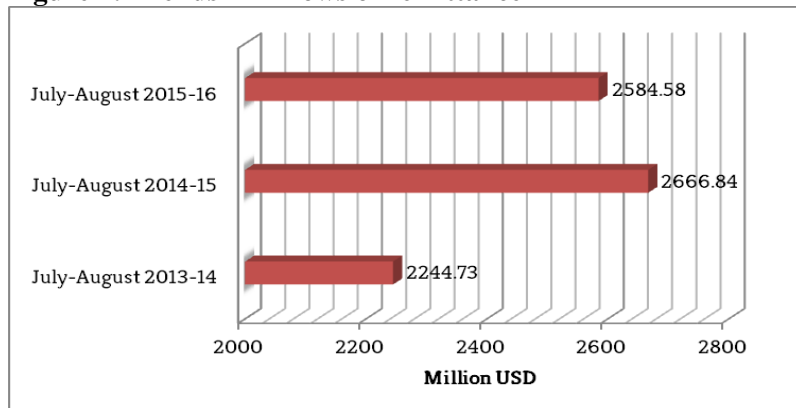
Source: Bangladesh Bank, 2015b

## 5. REMITTANCE

*The inflow of remittance declined by 3.08 percent and amounted to USD 2584.58 million during the period of July-August of FY 2015-16 compared to USD 2666.84 million during the corresponding period of FY 2014-15.*

The inflow of remittance declined by 3.08 percent and amounted to USD 2584.58 million during the period of July-August of FY 2015-16 compared to USD 2666.84 million during the corresponding period of FY 2014-15. Noting the decline of inflow of remittance to -1.61 percent during the period of July-June of FY 2013-14 from the corresponding period of FY 2012-13, the finding is that total inflow of remittance during July-February of FY 2013-14 came down to USD 14227.84 million from USD 14461.15 million during the corresponding period of FY 2012-13. Remittance is increasing at a decreasing rate after FY 2007-08 because of the decrease in the labour migrations to the different destinations due to the global economic recessions and decline in the labour demand by the Middle East countries due to collapsing construction sector. In FY 2012-13, flow of remittance was USD 14461.15 million with a growth rate of 12.60 which was USD 12843.43 million with 10.24 percent growth rate in FY 2011-12.

**Figure 7: Trends in inflows of remittance**



Source: Bangladesh Bank, 2015a

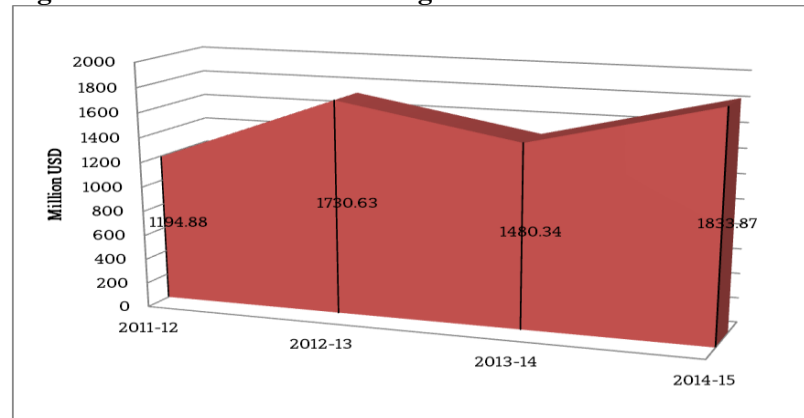
## 6. FOREIGN DIRECT INVESTMENT

Both the investor and the recipient can take advantage from foreign direct investment (FDI). It allows money to go freely to whatever business has the best prospects for growth. The FDI in the country has usually observed much fluctuation. For example, inflow of FDI decreased to USD 1480.34 million in FY 2013-14 from USD 1730.63 million in FY 2012-13, although FDI inflow reached USD 1833.87 million in FY 2014-15. In addition, FDI decreased after FY 2005-06 from 845million to 792million in FY 2006-07, and then to 692 million in FY 2007-08. FDI increased to 1086 million in FY

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2008-09. After showing a negative growth rate in 2009 of -35.54 percent, flow of FDI follows a positive growth rate of 30.42 and 24.42 percent in FY 2010 and FY 2011. Most importantly, rate of growth in FDI (net) has been seen a negative trend in FY 2013 (January-June) of -28 percent. In developing country like Bangladesh the current amount of FDI is insufficient for inclusive growth; more incentive should be given to foreign partners to increase the inflow of capital through FDI.

**Figure 8: Trends in inflows foreign direct investment**



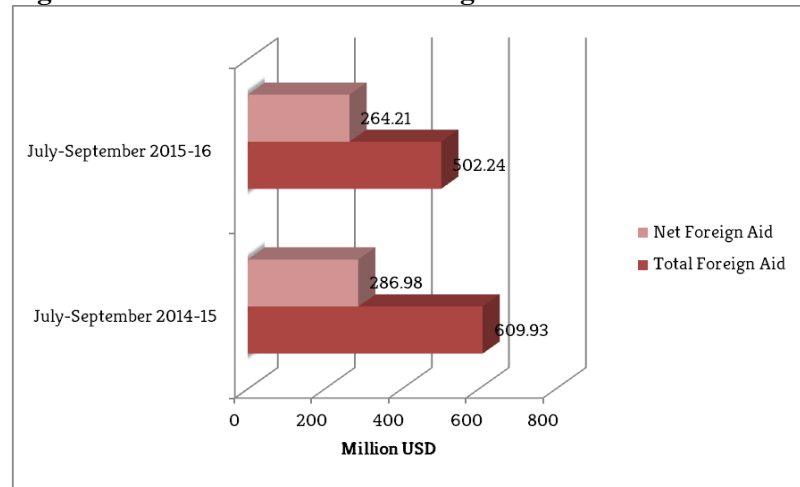
Source: Bangladesh Bank, 2015b

## 7. FOREIGN AID

The country has received a sizable amount of foreign aid over the years which help to recover from a bottomless situation to a more favourable economic situation. The total foreign aid disbursements during the period of July- September of 2015-16 decreased by USD 0.11 billion or 17.66 percent and stood at USD 0.50 billion compared to USD 0.61 billion during July-September of FY 2014-15. Net receipts of foreign aid were also lower and stood at USD 0.26 billion in July-September of FY 2015-16 compared to USD 0.29 billion in the corresponding period of FY 2014-15. In FY 2013-14 net foreign aid stood at USD 1878.82 million with a negative growth rate of .41 percent where in FY 2012-13 (July-June), net foreign aid was USD 1886.61 million with a positive rate of growth of 51.19 percent as compared to USD 1247.82 million with 18.88 rate of growth in the previous fiscal year 2011-12. However, net foreign aid decreased by 28.93 and 25.69 percent respectively in FY 2010-11 and FY 2008-09. In FY 2013-14, the payment (principal) increased by 24.66 percent than that of the previous fiscal year where growth rate of food aid increased by 53.15 percent and project aid increased by 7.35 percent. Therefore, government had to

finance a significantly larger proportion of the deficit through domestic borrowing, specifically through domestic banks. Due to 55 and 13.18 percent declining rate of food aid and project aid respectively led the net foreign aid shrink for the global economic recession and crisis in the Middle East countries declines.

**Figure 9: State of total and net foreign aid**

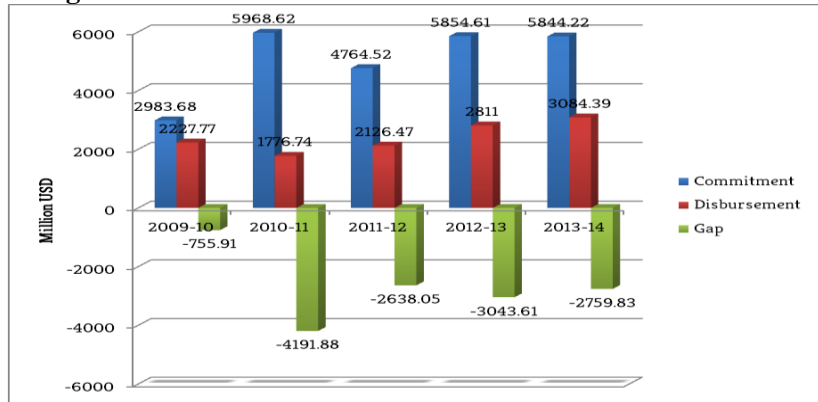


Source: Bangladesh Bank, 2015b

*The historical data of the foreign aid showed that the gap between the commitment and disbursement is increasing over the years. The gap between commitment and disbursement in FY 2013-14 was USD 2759.83 million.*

The historical data of the foreign aid showed that the gap between the commitment and disbursement is increasing over the years. The gap between commitment and disbursement in FY 2013-14 was USD 2759.83 million. Although the gap between commitment and disbursement of aid increased to USD 3139.92 million in the last FY 2012-13 but the disbursement of foreign aid increased by 31 percent than that of the previous fiscal year which stand to 1017.41 million (February'14). The commitment was higher in FY 2012-13 as USD 5926.05 million which was USD 4764.52 million in FY 2011-12. Huge Gap between commitment and disbursement over the years results in huge pipeline of foreign aids. Therefore, government should take necessary steps to approval of projects and meeting conditions in speedy way so as to increase the disbursement, investment and GDP growth.

**Figure 10: Gap between commitment and disbursement of foreign aid**

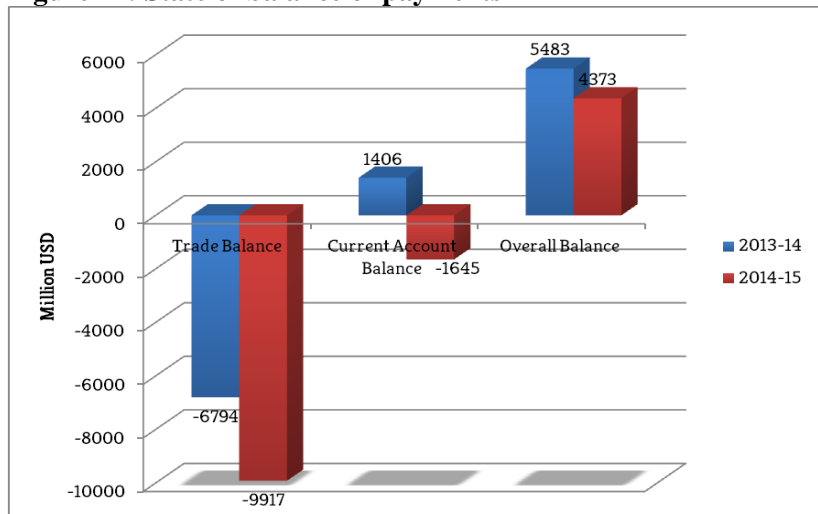


Source: Ministry of Finance, 2015a

## 8. OVERALL BALANCE

The current account balance stood at USD 1406 million in FY 2013-14, whereas the balance became negative and stood at USD – 1645 million in FY 2014-15. However, current account surplus soared by 35.21 percent during July-June of FY 2013-14 than that of the same period of FY 2012-13 because of the increasing rate of import payments and slower rate of remittance. Import showed a decreasing rate over the months of calendar year 2011 and 2012 which slowed the business activities although increases in FY 2013-14. However, recent monetary policy statement (MPS) estimated that this surplus might decrease in the next six months. According to MPS, surplus in overall balance of payment might reduce by the slower rate of RMG sectors and escalating in imports for growing the confidence of investors. At the mean time, imports to crude petroleum and petroleum products decreased by 22 percent due to the hamper in transportation for continuous shutdowns and blockades in the last few months. Bangladesh will have to fulfil a number of conditions to continue enjoying the trade privilege generalised system of preferences (GSP) of the European Union. Even, European GSP might be cancelled if Bangladesh government does not fulfil many of the conditions of GSP. To reduce the imbalances in balance of payment, government has set up various steps to manpower exports, upgrading skills of migrants and enhanced incentives to use formal channels to remit and invest funds (Byron, 2014). The financial account increased to USD 5150 million in FY 2014-15 from USD 2813 million in FY 2013-14 because of the increase in FDI and other investment.

**Figure 11: State of balance of payments**



Source: Bangladesh Bank, 2015a

## 9. CONCLUSIONS

Although the economy observed a comfortable current account balance, the decreasing rate of remittance and manpower exports might cause a serious hamper to the economy by reducing employment opportunities and output levels. In addition, declining industrial term loan will decrease the investment demand-induced import of capital machinery and industrial raw goods which may further aggravate the current declining growth in the manufacturing sector. After exploring the implications of unsatisfactory performances of the external sector, the Update concludes that the declining growth in GDP may persist if the indicators of external sector continue assuming current trends although the overall balance demonstrates surplus.

However, in order to address the current structural bottlenecks that impede developments in the external sector of economy, a thorough re-examination of the current trade and industrial policies is pressing. Adoption of a new policy regime aiming at expansion of productive capacities of the country that enhances utilisation of productive resources through enhanced entrepreneurial capabilities and increased production linkages may be fruitful in achieving developments in this sector, thereby fostering growth of the economy.

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