MINISTÈRE DE L'ÉCONOMIE, DES FINANCES ET DE L'INDUSTRIE
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ECONOMIC LETTER OF BANGLADESH

A LETTER FROM THE ECONOMIC DEPARTMENT OF THE EMBASSY OF FRANCE IN DHAKA

N°11 – October-November 2024

A. FRANCE-BANGLADESH NEWS

Discussion with student leaders at the French Residence

The French Ambassador hosted several student leaders at the French Residence to engage in a dynamic exchange of ideas and perspectives. The discussion centred on the students' aspirations, their vision for the Bangladesh's future, and the role of young leaders in driving positive change. The Ambassador emphasized the importance of fostering dialogue with the youth and reiterated France's steadfast support for the interim government in this transition period.

Following this meeting, our Economic Counsellor visited BRAC University to engage with students on France-Bangladesh collaboration in tackling climate issues and promoting skills development.

Meeting with the BIDA Executive Chairman

The Economic Department of the French Embassy and representatives of the France-Bangladesh Business Council met with Ashik Chowdhury, the new Executive Chairman of the Bangladesh Investment Development Authority (BIDA). It was an excellent opportunity to discuss concrete actions to enhance bilateral business relationship, in particular French investments in Bangladesh. Our Economic Counsellor expressed Embassy's full support to BIDA'S efforts to improve ease of doing business in the country.

Online meeting with MEDEF International

The French Ambassador and the Economic Counsellor discussed with a panel of French companies gathered by MEDEF International, a French Business Confederation. This meeting served as a platform to provide an overview of the political and economic landscape in Bangladesh. Some French companies expressed their interest in strengthening their activities in Bangladesh

Annual Consultation meeting between AFD and the Government of Bangladesh

Annual Consultation meeting between AFD and the Economic Relations Division (ERD) took place to discuss the implementation of ongoing development projects. Both parties reaffirmed their will to deepen cooperation, and AFD confirmed its commitment to supporting sustainable projects in the fields of adaptation, energy, access to clean water, and urban development.

B. FRESH NEWS FROM BANGLADESH

This section provides a brief overview of economic and business-related news from Bangladesh

---------------------------- MACRO --------------------------

Moody's downgrades Bangladesh's sovereign credit rating from B1 to B2 with negative outlook

The credit rating agency Moody's has downgraded Bangladesh's sovereign credit rating by one notch from B1 to B2. This marks the second downgrade by Moody's in just over a year, following the change from Ba3 to B1 in May 2023. The rating comes with a negative outlook, indicating the possibility of further downgrades during the next review in 2025.
This downgrade reflects heightened political uncertainty and slower-than-expected economic growth for 2024-2025, with GDP growth forecasts revised downward from 6.3% to 4.5%, according to the agency. The situation may exacerbate the country's liquidity crisis, banking sector vulnerabilities, and already weakened external position. Moody's also questions the interim government's ability to implement promised reforms amid high unemployment, elevated inflation, and the lack of a clear roadmap for upcoming elections.
Additionally, Moody's has downgraded the credit ratings of six local banks by one notch: from B1 to B2 for BRAC, City, Dutch-Bangla, and Eastern Banks, and from B2 to B3 for Mercantile and Premier Banks.

Growth slows to 3.9% in the last quarter of 2023-24

GDP grew by just 3.9% during the April-June 2024 period, marking the lowest quarterly growth for the 2023-24 fiscal year (following 6.0%, 4.9%, and 5.4% in the previous three quarters). According to provisional data from the Bangladesh Bureau of Statistics, annual growth is expected to reach 5.8% (compared to the IMF's estimate of 5.4%).
Quarterly growth was particularly impacted by weaker performance in the industrial sector (representing nearly 40% of GDP), which grew by 4.0% in the last quarter of 2023-24 compared to 6.3% in the previous quarter. This sector has been hampered by import restrictions and rising interest rates since 2022.

Bangladesh to apply for membership in the Regional Comprehensive Economic Partnership (RCEP)

The interim government has announced that Bangladesh will soon apply to join the Regional Comprehensive Economic Partnership (RCEP) free trade agreement. The RCEP includes fifteen member countries: the ten ASEAN nations, China, Japan, Australia, South Korea, and New Zealand.
Trade in goods with RCEP countries is heavily skewed against Bangladesh, with a trade deficit of nearly 34 billion USD in 2021. While RCEP accounted for 44% of Bangladesh's imports in 2021, it represented only 9% of the country's exports. A 2023 government study suggested that RCEP membership could boost Bangladesh's exports by more than 17%.
In the short term, RCEP membership could negatively impact customs revenue, which accounts for a quarter of tax revenue. In 2021, imports from RCEP represented 58% of customs revenue.
Bangladesh is pursuing free trade agreements as it prepares to graduate from the Least Developed Countries (LDC) status in 2026, a transition that could result in the loss of many market access benefits. Currently, Bangladesh already enjoys preferential access to China and Australia, which together account for 40% of its exports to RCEP countries.

FDI inflows drop by 9% in 2023-24 and data revised sharply downwards

Net foreign direct investment (FDI) inflows decreased by 8.8% during the 2023-24 fiscal year, a decline attributed to factors such as uncertainty over the January 2024 legislative elections, significant depreciation of the taka against the dollar, and the deteriorating economic situation. Net FDI inflows stood at 1.5 billion USD, down from 1.6 billion USD in 2022-23.
The Central Bank has also revised its methodology by adopting the BPM6 international standard,

resulting in significant changes to historical data. For instance, net FDI inflows for 2022-23 have been adjusted from the previously reported 3.2 billion USD to 1.6 billion USD, a 50% decrease. Notably, the balance of payments data had already been based on BPM6 figures.

Foreign exchange reserves continue to be under pressure

In October, Bangladesh's foreign exchange reserves stood at 19.93 billion USD (as per BPM6 standards), compared to 19.46 billion USD the previous month. According to the Central Bank, remittance inflows in the first quarter of the current fiscal year rose by over 33% year-on-year to 6.54 billion USD.

This increase reflects a growing tendency among expatriates to use formal banking channels, especially since the Central Bank eased its "crawling peg" exchange rate system in August to accelerate the liberalization of the USD/BDT exchange rate.

Commercial banks' purchases of US dollars, amounting to approximately 50 million USD in October, also contributed to the rise in foreign exchange reserves. Meanwhile, Central Bank dollar sales have nearly ceased, totalling only about 10 million USD this month.

Moreover, Bangladesh continues to maintain import restrictions. The opening of letters of credit fell by 8.4% year-on-year in the first quarter of the 2024-2025 fiscal year, amounting to 15.6 billion USD.

However, reserves dropped sharply to 18.5 bn USD mid-November following a quarterly payment to the Asian Clearing Union.

--------------------------- BANKING -------------------------

Central bank Governor claims 17 billion USD illegally transferred abroad over 15 Years

In an interview with the Financial Times, the Governor of the Bangladesh Bank revealed that $16.7 billion had been siphoned abroad over the past 15 years during Sheikh Hasina's administration. These funds were reportedly transferred primarily through unpaid bank loans and falsified import invoices.

The Governor specifically mentioned the S. Alam Group, accusing it of transferring abroad nearly 10 billion USD alone—a claim the group denies. The interim government has engaged with multiple countries to attempt to recover the stolen funds. A task force has been established, comprising members from the Central Bank, the Bangladesh Financial Intelligence Unit, and the Attorney General's Office.

Historic surge in non-performing loans reaches 17% of outstanding credit

Non-performing loans (NPLs) in Bangladesh have skyrocketed by nearly 20% in just three months, reaching an unprecedented level of 2,850 billion BDT (approximately 24 billion USD) in September 2024. This figure represents slightly over 16.9% of total outstanding loans. On an annual basis, the increase is particularly sharp at +84%.

The surge is largely attributed to local private banks, especially islamic banks, which saw their NPL amounts jump from 999 billion BDT to 1,490 billion BDT within three months (12% of outstanding loans). Meanwhile, public sector banks report an alarming NPL ratio of 40% of outstanding loans.

Since the appointment of a new governor at Bangladesh Bank, a series of disclosures have exposed governance issues within the banking sector. Moreover, several large corporations have faced severe financial difficulties further limiting their repayment capacities. By the end of 2023, the total amount of NPLs, including restructured and rescheduled loans, was estimated at 32% of outstanding loans.

Central bank raises policy rate to 10%

On October 22, Bangladesh Bank announced an increase in its policy rate from 9.5% to 10%. This marks the third hike since the appointment of the new Bangladesh Bank Governor in August. Prior to his tenure, the policy rate was set at 8.5%.

Despite frequent rate increases, inflation remains high, recorded at 9.92% in September, showing only a slight month-on-month decline. Consumer prices in Bangladesh are now primarily driven by domestic factors, including market manipulation in retail sales and extortion practices within supply chains.

---------------------------- ENERGY ---------------------------

Fuel shortages impact electricity production

Electricity production in Bangladesh has significantly declined due to supply shortages of key raw materials in the energy sector. Early November, 50 power plants were non-operational due to fuel shortages, primarily natural gas but also oil and coal, out of 144 total production sites. Milder temperatures, however, have sharply reduced demand, allowing load shedding to remain manageable and primarily affecting areas outside the capital.

This drop in production coincides with a decision by Adani Power, which has an export contract with Bangladeshi authorities for a 1,496 MW coal-based capacity, to halve its power supply to Bangladesh on October 31. This reduction stems from outstanding bills totalling approximately 800 million USD.

Bangladesh is particularly vulnerable to coal supply issues after significant investments in coal power plants in recent years. For instance, the 1,200 MW Matarbari coal plant, financed by JICA, was shut down at the end of October. Similarly, the Rampal power plant, funded by Indian investments, is operating at half capacity due to coal shortages.

--------- INTERNATIONAL DEVELOPMENT ---------

IMF mission to visit Dhaka starting on December 3

An IMF delegation is set to visit Dhaka during the first week of December as part of the third review of the ongoing 4.7 billion USD program. The mission will focus on key areas such as the ongoing political transition, inflation, the financial sector, taxation, and foreign exchange reserve management

Following the previous review mission in May 2024, the IMF approved the disbursement of the third tranche, amounting to 1.15 billion USD—up from the originally planned 668 million USD. Bangladesh had successfully met all IMF targets except for revenue collection. The IMF had previously disbursed 476 million USD in February 2023 and 681 million USD in December 2023.

During this mission, the IMF is also expected to recommend reforms necessary for granting an additional loan requested by the interim government to bolster the country's foreign exchange reserves. The loan amount will depend on the government's financing needs and the budgetary support provided by development partners. The IMF is likely to focus on addressing this financing gap.

Interim Government approves the cost escalation for the JICA-Funded Deep-Sea Port Project

During a meeting of the interim government's ECNEC (Executive Committee of the National Economic Council), chaired by Prof. Yunus, Bangladesh approved a substantial 38% budget increase for the construction of the country's first deep-sea port at Matarbari, located between Chittagong and Cox's Bazar.

The project was initially approved in 2020 by the previous administration for a budget of 177 billion BDT (1.8 billion EUR at the time) with a target completion date of 2026. The revised timeline now sets completion for 2029, with the budget increased to 244 billion BDT. However, the cost in euros remains stable (1.9 billion EUR) due to the significant devaluation of the taka.

This fourth port is considered vital by local authorities as it will accommodate large vessels, easing the burden on the overcrowded Chittagong port. Ultimately, the Matarbari port is expected to handle up to 4.8 million containers annually.

The project aligns with Japan's Bay of Bengal Industrial Growth Belt (BIG-B) initiative launched in 2014, which aims to develop the Matarbari-Dhaka corridor into a major logistics and industrial hub linking South Asia and Southeast Asia.

---------------------------- EXPORTS ---------------------------

Factory protests estimated to cost 400 million USD to textile sector

The Bangladesh Garment Manufacturers and Exporters Association (BGMEA) reports that worker protests in the textile sector resulted in production losses estimated at 400 million USD during September and October. Social unrest led to some

orders being diverted to competing countries, primarily India, Pakistan, Sri Lanka, and Vietnam. These redirected orders would represent approximately 5-6% of the country's exports, equating to around 2 billion USD.
However, the situation has reportedly stabilized, with orders beginning to return to normal levels, driven in part by increased demand from the United States, the United Kingdom, and Germany.

Export revenues up by 5% in the first quarter of current fiscal year

Bangladesh's export revenues rose by 6.8% year-on-year in September. Ready-made garments (RMG) remain the largest export category, accounting for 80% of total exports at 2.8 billion USD (+6% year-on-year). Agricultural products followed, comprising 2.7% of total exports at 97 million USD (+17% year-on-year). For the first quarter of the current fiscal year, exports increased by 5% year-on-year, reaching 11.4 billion USD despite ongoing political tensions.
While the export revenue figures are encouraging, they may partly reflect current inflation levels and rising operational costs, such as gas, electricity, and wages. Additionally, widespread protests in the garment sector disrupted activities and contributed to the redirection of orders to competitor nations.

C. A Banking Sector in Severe Distress

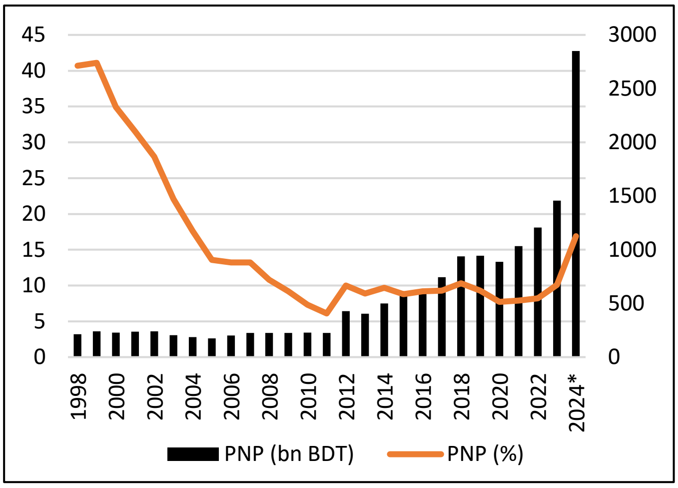
The banking sector in Bangladesh appears to be undergoing significant restructuring after years of mismanagement. The situation is particularly alarming, with non-performing loans reaching 32% of total assets in 2023, and many banks remaining heavily under-provisioned. Some institutions are also grappling with severe liquidity issues, forcing the Central Bank to provide substantial refinancing support in an environment of high inflation. To date, the true state of the sector remains largely opaque due to its lack of transparency, while new revelations continue to emerge. In October 2024, the central bank Governor, appointed by the interim government, disclosed that approximately 17 billion USD had been siphoned out of Bangladesh through fraudulent loans tacitly approved by the previous administration.
Despite these challenges, the interim government has prioritized restoring confidence in the banking sector. The Bangladesh Bank has established a task force to provide recommendations in the coming months, and a White paper on the state of the economy is expected to be published soon, offering more reliable and transparent data. Meanwhile, the central bank has already initiated several reforms aimed at improving governance within the banking system.

1. Overview of one of the major weaknesses in the economy

The banking sector in Bangladesh has seen significant growth in the early 2000s, but it remains underdeveloped compared to other countries in the region. Bank deposits represent nearly 40% of GDP, compared to 72% in India and 32% in Pakistan.

Unprecedented and concerning volumes of non-performing loans (NPLs). In connection with a lenient regulatory environment, undue facilities granted to large borrowers, and a lack of sanctions against bad payers, the volume of non-performing loans (NPLs) surged from 200 billion BDT in 2011, after a decade of stability, to 2850 billion BDT (22 billion USD) in 2024, representing 17% of total loans. Including restructured and rescheduled loans, the total amount of doubtful debts reached 4750 billion BDT by the end of 2023 (32% of total loans or nearly 11% of GDP). This is an unprecedented level for the country, and few other nations have experienced such a situation in the past (Greece at 49% in 2017, Algeria at over 20% today). These amounts are likely to be revised upwards under the interim government, as many cases are coming to light. The Chief Adviser has appealed to several governments (the United States, Canada, the United Kingdom, Switzerland, etc.) for assistance in recovering these sums, a significant portion of which is believed to have been siphoned abroad.

The situation is particularly concerning for a small number of banks: public banks and Islamic banks, which represent 26% of total deposits. These banks are particularly affected by provisioning that is lower than required by regulations, with an overall underprovisioning of 20% (1.9 billion BDT). The risk of contagion to other banking players remains difficult to assess.



Liquidity shortage. Some of the most fragile banks are experiencing severe liquidity problems, forcing the central bank to intervene massively in the interbank market to refinance certain banks. Nine of them had a liquidity deficit of more than 180 billion BDT (1.5 billion USD). Multiple factors explain this pressure, particularly the use of commercial banks to finance the public deficit, the collapse of confidence in Islamic finance, the depreciation of the taka, and the rise in NPLs. For example, net public borrowing from the banking sector amounted to 533 billion BDT (5 billion USD) in 2023-24.

Public banks particularly affected. The six public banks, which represent 25% of total banking assets, are undercapitalized and suffer from a very high level of NPLs, amounting to 40% of their balance sheets, representing 44% of the country's doubtful debts. While the cost of managing an extensive network and their public service missions weighs on their results, several institutions have accumulated management failures. Their recovery rate for NPLs is only 5% compared to their annual targets. This affects their profitability, with a negative return on equity (ROE) of 19% in March 2024, compared to a positive ROE of 6% for private banks and 20% for foreign banks. Their expenditure-to-income ratio is 82% for public banks, compared to 76% for private local banks and 35% for foreign banks, reflecting, among other things, overstaffing. Recurring failures to meet obligations (Capital Adequacy Ratio, Liquidity Adequacy Ratio) have frequently forced the government to recapitalize public banks, to the tune of 306 billion BDT (3 billion USD) over the past ten years.

No massive decline in deposits, but a shift. According to the latest data from the central bank, available up to September 2024, there has not yet been a massive withdrawal (bank run) of deposits. However, several experts report that while the total deposit volume remains stable, this hides significant transfers of deposits from unhealthy banks (mainly Islamic banks) to more stable ones, further exacerbating the liquidity imbalance.

2. Poor governance of the sector: a critical issue

A legal framework in need of strengthening. The banking sector has suffered from an inadequate legal framework to prevent fraud, detect it, and investigate potential shortcomings. This includes issues such as the ability to elect board members closely connected to the owners, the weakness of audit committees, the lack of regulations governing the issuance of new loans, the inefficiency of the judicial system, and the sector's general lack of transparency.

Corruption has become systemic. In 2023, Bangladesh ranked 12th in South Asia on the Corruption Perception Index (CPI), just ahead of Afghanistan. This poor score is attributed to factors such as the lack of follow-up on the government's zero-tolerance policies regarding corruption, money laundering, and the prevalence of bad debtors. Globally, the country dropped two places, ranking 149th out of 180.

Major cases of corruption in the banking sector. The banking sector has been plagued by major corruption scandals. Since the fall of the Awami League government, numerous revelations have emerged. In October 2024, the Governor of the central bank revealed that several leaders of Islamic banks were abducted by Bangladesh's military intelligence (DGFI), primarily in 2017, and forced to sell their shares under the Prime Minister's orders. The central bank estimates that about 17 billion USD was transferred out of Bangladesh following these fraudulent acquisitions, largely through loans granted to new shareholders.

3. A significant task for the interim government

The interim government and the new Governor of the central bank, Dr. Mansur, have made restoring trust in the banking sector one of their many priorities.

White paper on the economy and the banking sector. The government has commissioned a White paper to be drafted by a committee of ten experts tasked with providing an overview of the economy, with a focus on corruption. This committee is expected to submit its report in early December and should contribute to the publication of more reliable and transparent data (GDP, inflation, NPLs). Additionally, the central bank set up a task force in early September to reform the banking sector. This task force is responsible for proposing regulatory changes to improve governance and risk management, as well as to limit the influence of politics and businesses on decision-making. For weak institutions, the task force will recommend reforms to regulate mergers and acquisitions and develop a legal framework for the recovery of troubled banks.

Initial measures by Bangladesh Bank. Several banks are currently under strict supervision by the central bank. Around ten banks are required to report 20 key indicators daily. Some banks now need the regulator's approval for any loan above 400,000 EUR. The Governor of Bangladesh Bank has also ruled out using the printing press to finance banks in trouble, opting instead for interbank borrowing.

Leadership changes at many banks. August and September saw significant changes in the boards of directors and CEOs of both public and private banks. About ten banks had their boards dissolved by the central bank and replaced with independent directors. Additionally, most CEOs of public banks have been forced to resign.

Uncertain future of mergers and acquisitions. The previous administration had initiated a banking consolidation movement in early 2024, aiming for voluntary mergers between "weak" and "strong" banks by the end of the year. Following the adoption of the Bank Companies Act 2023, the central bank can also mandate mergers and acquisitions. However, only one merger has been formalized, between EXIM Bank and Padma Bank. While Padma Bank has ceased issuing new loans and accepting deposits for several months, the future of this merger is now uncertain under the interim government, which assured in mid-November that no banks would be closed.

Asset Quality Review. Under the IMF's guidance, an Asset Quality Review (AQR) will be launched in December 2024 to clarify future actions by Bangladesh Bank to strengthen the sector. A first batch of 12 banks identified as weak by the central bank will be analyzed over the next 4-6 months. In parallel, the IMF is supporting Bangladesh Bank in drafting a Bank Resolution Act, which will empower the central bank to implement the AQR results.

Expected support from donors. The new interim government has entered into negotiations with the IMF for an additional loan of 3 billion USD. In this context, stronger reform expectations, especially in the banking sector, are anticipated from the IMF. Meanwhile, the World Bank has announced support for the Anti-Corruption Commission (ACC) through the Stolen Asset Recovery (StAR) initiative, which could help strengthen efforts to recover some of the doubtful debts siphoned abroad, although the recoverable amounts are likely to be minimal.

Key Takeaways

Three ideas

1. The banking sector has suffered for many years from governance issues exploited by the political and economic elite for personal gain;
2. The true state of the sector remains poorly understood due to low transparency, and the publication of an honest assessment could create a trust shock regarding a handful of weak banks. In this regard, an asset quality review of each bank will begin in December with the support of the IMF;
3. The Bangladesh Bank has set up a task force to make recommendations within a few months.

Three figures

1. The share of non-performing loans, including restructured loans, reached **32%** of total loans in 2023.
2. The Bangladesh Bank estimates that approximately **17 billion USD** were transferred out of the country following fraudulent bank acquisitions, mainly through loans.
3. A highly uneven non-performing loan rate across banks, exceeding **40%** for public banks.

The French Treasury is present in more than 100 countries through its Economic Departments. To learn more about its missions and network: https://www.tresor.economie.gouv.fr/Institutionnel/our-international-network

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