MINISTÈRE DE L'ÉCONOMIE, DES FINANCES ET DE LA SOUVERAINETÉ INDUSTRIELLE ET NUMÉRIQUE
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ECONOMIC LETTER OF BANGLADESH

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

N°9 – May/June 2024

A. FRANCE-BANGLADESH NEWS

Meeting in France between Franck Riester, Foreign Trade Minister, and Zunaid Palak, State Minister for Posts, Telecommunications and Information Technology

During his visit in France from 21st-25th of May, Zunaid Palak, State Minister for Posts, Telecommunications and Information Technology, met with Franck Riester, Foreign Trade Minister, to exchange on digital and space cooperation. Mr. Palak also participated in VivaTech, an international tech and start-ups fair, which hosted for the first time a Bangladeshi pavilion. In addition, he visited Airbus Defence and Space's satellite assembly site in Toulouse, in the context of the ongoing discussions about the Bangabandhu-2 project's observation satellite system.

On May 24th, H.E. Marie Masdupuy held a follow-up discussion with State Minister Palak after his successful visit to France. It was an opportunity to discuss further a wide range of areas including space, artificial intelligence and cybersecurity.

The French Development Agency (AFD) signs a 300 M EUR budget support agreement with Bangladesh to help combat climate change

On May 20th, the AFD and the Bangladeshi government signed an agreement providing a 300 M EUR budgetary support to Bangladesh in the fight against climate change. This three-year program from 2023 to 2026 aims to: (i) strengthen the planning, budgeting and monitoring of Bangladesh's climate policy at the national and local level, and (ii) foster the country's climate and environmental resilience and prosperity in key sectors, such as water and energy. This concessional loan also includes 5 M EUR of grants to finance environmental initiatives and technical cooperation. A first disbursement of 43 M EUR has already been made in June 2024.

Kick-off meeting of the Business Club

On June 23rd, the French Embassy hosted the first session of the Business Club, gathering French companies operating in Bangladesh. The Business Club, a dynamic informal platform, is dedicated to amplifying the presence of French businesses in Bangladesh and strengthening trade ties between the two countries. The Club aims at fostering a rich exchange of knowledge and experience to strengthen Franco-Bangladeshi economic relations.

B. FRESH NEWS FROM BANGLADESH

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

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

The budget proposed to Parliament shows a slight decrease as a percentage of GDP

On June 6th, the Bangladeshi government presented to the Parliament its budget for the FY2024-2025. The total budget reached 7 970 Bn BDT (around 68 Bn USD), or 14.2% of GDP, down from 15.2% of GDP the previous fiscal year.

It is based on a growth forecast of 6.75% in 2024-2025, compared with 5.82% expected for 2023-2024 and 5.78% achieved in 2022-2023, and on the assumption that inflation will fall sharply to 6.5%. These assumptions are considerably more optimistic than those of international institutions. For instance, the IMF anticipates a 5.7% growth for FY 2024. It also seems difficult to reduce inflation to 6.5%, as it reached 9.89% in May.

Fiscal revenue should reach 9.7% of GDP, or 5 450 Bn BTD (around 46.5 Bn USD). This estimation should be welcomed, as the IMF, on a mission to Dhaka in May 2024, has called on the government to pursue its efforts to increase tax revenues. However, it will require an important effort, given that in 2023, fiscal revenues amounted to 7.6% of GDP, one of the lowest tax-to-GDP ratios in the world.

The deficit is forecasted at 2 510 Bn BDT, or 4.6% of GDP, compared to 5.2% last year. It would be financed 36% by external resources (around 7.7 Bn USD versus 9 Bn USD y.o.y.), and 64% by internal financing (mainly by the banking sector and the central bank).

The Annual Development Program (ADP) for FY2024-2025 would amount to 2 650 Bn BDT (22.5 Bn EUR), a slight y.o.y. increase (2 630 Bn BDT in FY24). As last year, the transport and communication sectors will represent the main expenditure for the ADP (27%) while the energy sector will be the second largest item totalling around 15% of the spending. While allocations to the first two sectors are down y.o.y. (-7% and -8% respectively), spending on education and health is up by respectively 5.5% and 27%. Nonetheless, they remain relatively low, at 12% and 8% of total expenditure respectively.

Fitch downgrades again Bangladesh's credit rating

On May 27th, the rating agency Fitch downgraded Bangladesh's ability to meet its foreign currency debt obligations from "BB-" to "B+". This revision is explained by a sustained weakening of the country's foreign exchange reserves, as the rating agency estimates that the recent reforms announced by the Central Bank won't be sufficient to reverse this downward trend. Since the beginning of the year, the foreign exchange reserves fell by 15% to reach a historic low of 13.76 Bn USD in May 2024.

However, Fitch Ratings believes that the financial perspectives remain stable. Certain factors are likely to mitigate external refinancing risk, such as the implementation of the IMF program, the moderate level of public debt, the favourable medium-term growth outlook, and the favourable composition of external creditors (mainly international lenders such as the World Bank and the ADB).

Bangladesh and India launch negotiations for a Comprehensive Economic Partnership Agreement (CEPA)

On June 22nd, Prime Minister Sheikh Hasina's visit to India has been the occasion for Modi to announce the launch of negotiations around the CEPA (Comprehensive Economic Partnership Agreement). This agreement aims to (i) strengthen economic interactions between the two countries, (ii) simplify trade procedures and (iii) promote investment between the two countries. The CEPA is expected to generate significant economic benefits fostering closer economic integration and cooperation. The two parties also agreed to work on enhanced environmental, maritime and security cooperation (notably within the Indo-Pacific Oceans Initiative).

Bangladesh currently benefits from customs preferences in India under the South Asia Free Trade Agreement (SAFTA). These preferences allow products from Bangladesh, as a Least Developed Country (LDC), to have free access to the Indian market without tariffs or quotas, except 26 tobacco and alcohol products. However, Bangladesh will lose its preferential access to the Indian market post 2026, when it will graduate from the LDC list. It is therefore crucial for Bangladesh to seek to maintain these trade advantages in the CEPA discussions with India.

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

Public bank's non-performing loans (NPL) increased by 73.2% between 2022 and 2024

On May 7th, the Bangladesh Bank (BB) published a report revealing that NPL increased by 73.2% between 2022-2024. For example, Janata Bank recorded a 131% increase of unpaid loans, while Agrani Bank saw a 121% increase over the same period. In line with the IMF conditions, the BB published a roadmap to reduce NPL by 10% in two years and a half. In this context, the six main public banks are failing to meet their loan recovery targets. Their recovery rate is only 4.67% of target. The inefficient loan management of public commercial loans undermines financial stability and slows down economic activity, hampering new lending and job creation.

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

The IMF approved the third tranche of the 4.7 Bn USD loan

On June 23rd, the IMF board approved the third tranche (out of seven) of the 4.7 Bn USD loan, as Bangladesh met most of its reform objectives. However, the country did not achieve its target for increasing foreign exchange reserves. To release the third tranche, the IMF lowered the target for Bangladesh to maintain its net foreign exchange reserves at 14.7 Bn USD by June 30th 2024, against a previous target of 20.1 B USD.

To support Bangladesh in its reforms and address its liquidity crisis, the IMF decided to disburse 1.15 Bn USD for this third tranche which represents 70% more than the initially planned allocation of 681 M USD.

The World Bank approved a 900 M USD loan for the improvement of urban, financial and fiscal resilience in Bangladesh

On June 21st, the World Bank approved a 900 M USD loan for an urban infrastructure improvement project and a second project to strengthen Bangladesh's fiscal and financial sectors.

Bangladesh benefits now from a 400 M USD program aiming to reinforce urban resilience in the face of climate change. It covers seven city clusters along an economic corridor stretching from Cox's Bazar to Panchagarh. The development of these cities will help absorb climate migrants, create jobs, improve the links between rural and urban areas, and finally strengthen food supply chains. According to estimates, the income of the selected cities should increase by 20%.

The remaining 500 M USD aims to reform the fiscal and financial sectors in order to accelerate sustainable growth and strengthen banks' resilience to future shocks. In particular, it supports the transition from trade taxes to consumption and income taxes. The reforms will increase public and private investment in climate change adaptation and mitigation.

Two World Bank projects to support the Rohingya have been approved for 700 M USD

On May 28th, the World Bank board approved two projects to improve the living conditions and the access to services for host communities and Rohingya populations. In total, the loan component of the two projects amounts to 407.5 M USD, while the grant component represents 295.5 M USD.

The first project focuses mainly on the construction of basic water, sanitation and hygiene infrastructures, as well as infrastructure resilient to the effects of climate change. The second project aims to foster economic opportunities in the Chattogram district, encompassing refugee camps, implementing employment programs while reinforcing the access to education for children and healthcare for vulnerable populations.

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

New export policy strategy aims to double Bangladeshi exports to 110 B USD by 2027

On May 15th, the Cabinet Committee on Economic Affairs (CCEA) approved its 2024-2027 export policy. The project aims at exporting 110 Bn USD by 2027, double the volume recorded last year (55 Bn USD for FY2023). This target export takes into account Bangladesh's graduation from the list of LDCs in 2026 and the economic slowdown caused by the Covid-19 pandemic and the war in Ukraine.

In parallel, Bangladesh solicited the UN's support in drawing up its strategy for graduating from the LDC category. This document, which will be finalized this summer, will most likely focus on trade agreements and economic diversification.

Export revenues fell sharply in May

In May, exports fell by 16% y.o.y., almost reaching 4.07 Bn USD. Although overall exports for the July-May period of the current fiscal year grew by 2% to reach 51.54 B USD, revenues remain 8.47% below the objective set for this period.

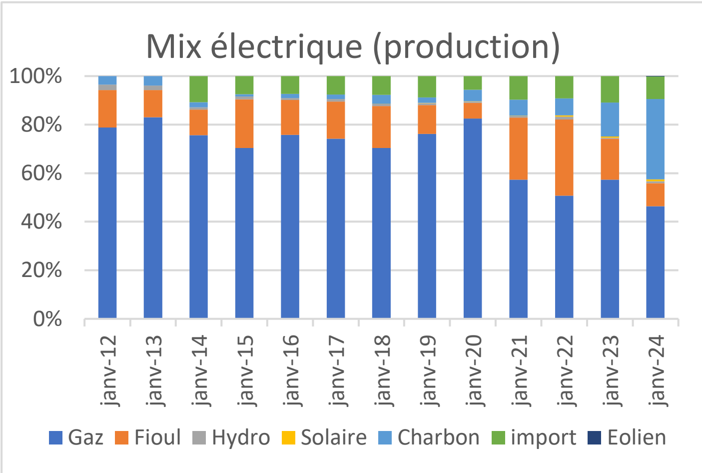
In detail, over the month of May, the revenues of the RMG sector recorded a 17% drop compared to May 2023, amounting to 3.35 Bn USD. This drop in revenues is attributed to a diminution of the selling price of locally manufactured garments, while production costs rose due to higher wages, higher interest rates and higher transport costs, impacting the competitiveness of Bangladeshi companies. In addition, lower import demand on the European market, the main destination for RMG exports, contributed to the decline in revenues.

C. Overview of the energy sector in Bangladesh

1. A power mix based on natural gas, fuel, and more recently, carbon

Strong historical dependence on natural gas, linked to the presence of onshore deposits. Bangladesh has historically relied on natural gas for its electricity production, with this resource representing nearly 80% of production until the late 2010s. The rest of the electricity was mainly generated by oil-fired powerplants and imports from India.

This over-representation of natural gas is primarily due to the presence of onshore deposits, mainly exploited by the American Chevron. However, those reserves are diminishing and production peaked in 2018-19 (see graph). Since that year, Bangladesh imports Liquefied Natural Gas (LNG) under long-term agreements and on the spot market, but at a rate that cannot compensate for declining local production and growing demand. As a result, since 2020, gas-fired power generation has fallen to around 50%.



High-priced use of fuel oil in the early 2020s, to compensate for peak gas production. To offset the low availability of gas, the country had to increase the use of its oil-fired power plants in 2021 and 2022, fuelled by imported oil refined at high prices due to the lack of refinery capacity, at a time when the war in Ukraine was pushing up the cost of oil on world markets. Refined oil imports thus reached nearly 6.4 B USD in 2021-2022 (+142% in one year). These accounted for up to 10% of Bangladesh' total imports, against only 5% the previous year.

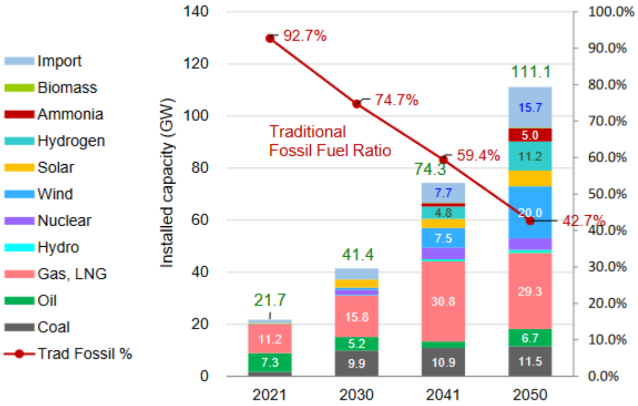
Since 2023, a sharp rise of coal in the mix. Since 2023, the commissioning of large coal-fired power plants, which are less costly to operate, have largely taken over oil, rising from 9% of production in 2022 to 19% in 2023 (fuel thus falls from 30% to 17%). The coal industry is set to continue growing over the next few years. The 2010 roadmap proposed increasing the share of coal to 51% by 2030, compared with less than 2% at the time.

Significant overcapacity, costing the public authorities dearly. Bangladesh is regularly singled out for its installed capacity (24,911 MW) for a much lower peak demand (15,648 MW) in 2022-23, i.e., 63% utilization. To achieve this, it has relied on substantial private investment, reassured by the assurance of being paid whether or not the plant is operating (through the payment of a capacity charge). Bangladesh is paying the high price for this strategy: in 2020-21, the public agency BPDB paid the equivalent of 1.5 Bn USD in capacity charges to private companies (+21% y.o.y.), an amount close to the public subsidies paid by the government to BPDB that fiscal year (1.4 Bn USD).

Renewable energies account for barely 2% of production by 2023. Renewable energies still remain marginal, despite stated ambitions, at 2.8% of installed capacity, including 1.7% solar, 0.9% hydro and 0.2% wind. Bangladesh has set itself a target of 10% renewable energy by 2020. To date, the country has installed 460 MW of solar power, including a 200 MW array owned by Beximco. The country very recently inaugurated its first wind farm near the Burmese border, 60 MW built with Chinese financing.

2. Development still based on gas, with a target of 40% clean energy by 2041

The latest roadmap, IEPMP 2023, should enable Bangladesh to achieve 40% "clean" energy by 2041, with mainly 7.5 GW of wind power (mainly offshore), 4.8 GW from hydrogen and as much from nuclear power, and around 4 GW of solar power.



Underdeveloped wind energy sector with some offshore opportunities. Government and experts agree on the low potential of onshore wind power due to low winds speeds and land scarcity. As for offshore wind power, the Ministry of Energy is currently conducting a study of the potential. In July 2023, the Danish investment fund Copenhagen Infrastructure Partners (CIP) and the Danish company Copenhagen Offshore Partners (COP) have submitted to the Bangladeshi government a proposal to build an offshore wind farm off the Bay of Bengal. The project, with a 50 MW capacity, would represent a 1.3 Bn USD investment.

Numerous solar projects but slow to get off the ground. Investment in solar power is certainly on the increase but, as underlined by the recent acceleration of project deliveries and good prospects: the Ministry of Energy reports that there are currently 108 projects in the pipelines, 8 of which are under construction (435 MW). Administrative hurdles, land scarcity and fragmentation, and high tariffs on solar panels are the main obstacles to the development of large-scale infrastructure. However, other markets with potential include floating solar and rooftop solar panels.

An EU Global Gateway project to support the development of renewable energies. The first Global Gateway flagship project in Bangladesh focuses on supporting renewable energy production capacity. In October 2023, during the Global Gateway Forum, the European Investment Bank signed a 350 M EUR loan, accompanied by a 45 M EUR grant package for technical assistance and investment subsidies. With co-financing of a further 350 M EUR from other donors, this program will invest in solar power plants and, probably to a lesser extent, wind farms.

The country is betting heavily on gas exploration in the Bay of Bengal. In fact, since the roadmap validated in 2023 still envisages a share of over 40% for natural gas in the electricity mix, Bangladesh is looking to explore new gas deposits on its territory. As discoveries are scarce on land, the authorities are naturally turning to the Bay of Bengal, which neighbouring Burma has been using for several years. At the end of 2023, the Ministry of Energy reformed a legal framework deemed unattractive by the *majors*, and relaunched auctions at the beginning of March 2024 for oil and gas exploration in the Bay of Bengal. The bidders will have until September 2024 to present their bids for the 24 offshores zones.

In practice, regional connectivity seems to be the main lever for the energy transition. Average sunshine levels, land scarcity and frequent cyclones mean that the potential for renewable energies in the short term is fairly limited. The region's main energy reservoir lies in the hydropower potential of the Himalayas, in Nepal and Bhutan.

In March, the Nepal Electricity Authority (NEA) and the Bangladesh Power Development Board (BPDB) reached an agreement on the price of electricity to be exported from Nepal. In July 2024, Nepal announced that it is set to export around 40 MW of electricity to Bangladesh in the upcoming months after India validated this initiative. The NEA is therefore planning to sell 40 MW of electricity to Bangladesh for the 6 months of the rainy season, i.e., from June 15 to November 15, every year for five years. According to studies, the potential capacity for Nepal alone is between 72 and 83 GW.

The Bangladeshi government recently announced that it is ready to invest 1 Bn USD in a hydropower project in Bhutan (Dorjilung Hydropower Project) with a total capacity of 1,125 MW. This project would involve trilateral cooperation with India, which would notably ensure the transit of electricity from Bhutan to Bangladesh. The three countries are currently working on an MoU.

Use of nuclear power to remain limited. Two Russian-designed VVER-1200 reactors (1,200 MW each) are currently under construction at the Rooppur site, 140 km west of Dhaka. A 11.38 Bn USD Russian loan was signed with Bangladesh in 2016. Since the start of the war in Ukraine, the construction site has nevertheless encountered financial and technical complications, but the authorities are keeping to the original schedule: first unit to be delivered by the end of 2024, and the second by 2025. In early April 2024, Prime Minister Sheikh Hasina reportedly asked Rosatom's CEO to consider building a second nuclear power plant in Rooppur during a meeting in Dhaka.

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