Chapter-9

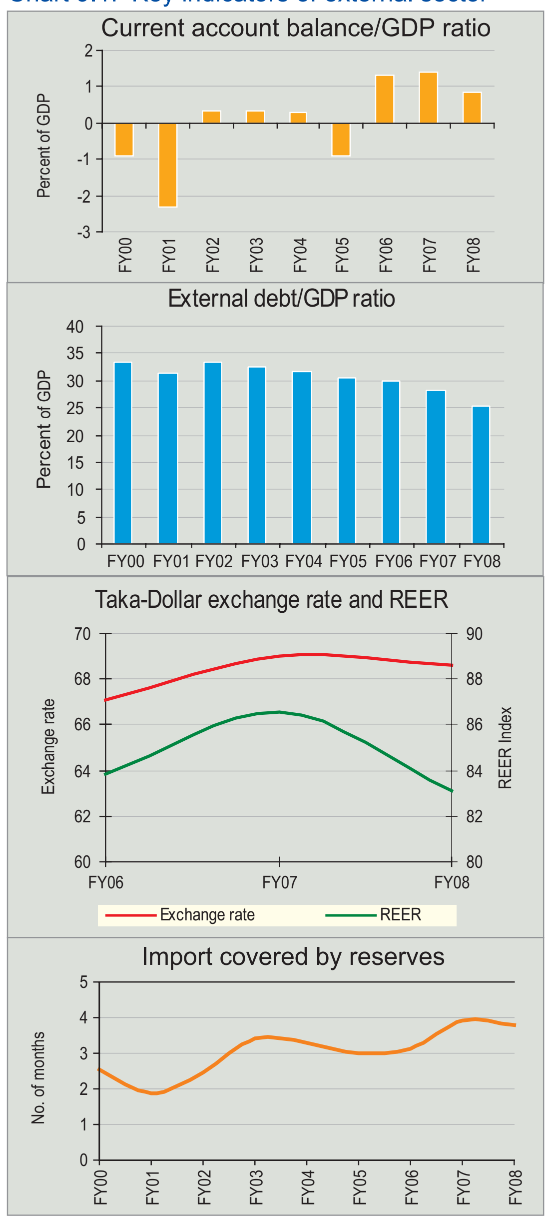
# External Sector

9.1 The external sector witnessed a strong performance in FY08 with both exports and imports registering a robust growth in spite of two consecutive floods and devastating cyclone Sidr in the first half of FY08. Massive losses of agricultural production forced Bangladesh to import more food items. Enhanced imports of food items and agriculture inputs coupled with their rapidly rising prices in the global market, alongside higher import prices of fuel oil caused excessive demand for foreign exchange during FY08. Fortunately, the robust growth of remittances and export receipts overweighed the demand stresses resulting in stability of exchange rate during FY08 and foreign exchange reserve increased by 21.1 percent to 6.15 billion at the end of FY08. There was no unusual volatility in the foreign exchange market.

Taka-Dollar exchange rate remained almost stable in FY08 due to BBs intervention in the foreign exchange market. Taka appreciated against US Dollar by 0.63 percent during FY08.

Trends of some major external sector indicators may be seen in Chart 9.1.

Chart 9.1: Key indicators of external sector




**External Trade and the Balance of Payments - the Overall Situation**

9.2 Merchandise exports (fob) increased by USD 1892.0 million (or 15.7 percent) to USD 13945.0 million in FY08. Except jute goods and fertilizer (which recorded a negative growth of about 0.8 percent and 27.0 percent respectively), earning form all other major exportable items increased significantly. A substantial growth of knitwear products (21.5 percent) and woven garments (10.9 percent) continued to increase the growth of merchandise exports in FY08 over FY07. The export of miscellaneous products, subsumed under the "others" category showed a high growth of 43.6 percent in value terms during FY08. As a percentage of GDP, exports increased from 17.6 percent in FY07 to 17.7 percent in FY08.

9.3 Merchandise imports (fob) increased by USD 3975.0 million (25.6 percent) in FY08 to USD 19486.0 million. Increased demand and higher international prices resulted in rising import payments for rice, spices, sugar, wheat, staple fibre, edible oil, plastic and rubber & articles thereof, POL, pulses, oil seeds, yarn, raw cotton, clinker, crude petroleum and pharmaceutical products. On the other hand, import of capital machinery declined markedly. Imports (c&f) as a percentage of GDP increased from 22.7 percent in FY07 to 24.7 percent in FY08.

9.4 A higher absolute increase of imports than exports widened the trade deficit from USD 3458.0 million in FY07 to USD 5541.0 million in FY08. The deficit on the services account, however, widened to USD 1525.0 million in FY08 from USD 1255.0 million in the previous year. The deficit on the income account also rose to USD 1005.0 million in FY08 from USD 905.0 million in FY07. Current transfers increased substantially from USD 6554.0 million in FY07 to USD 8743.0 million in FY08, thanks to a hefty 32.4 percent rise in workers' remittances. The net outcome of all these developments narrowed down the current account balance surplus from USD 936.0 million in FY07 to USD 672.0 million in FY08. Current account balance as a percentage of GDP stood at 0.85 in FY08 against 1.37 in FY07.

Chart 9.2

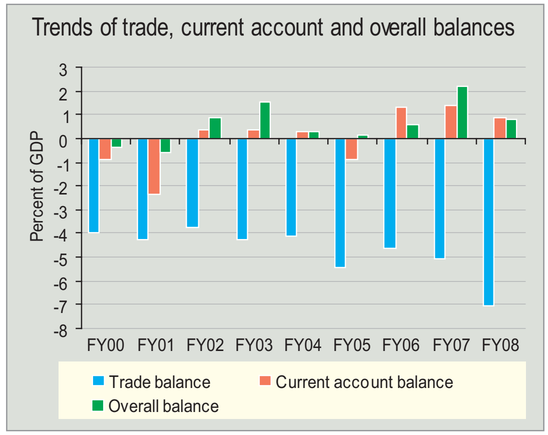


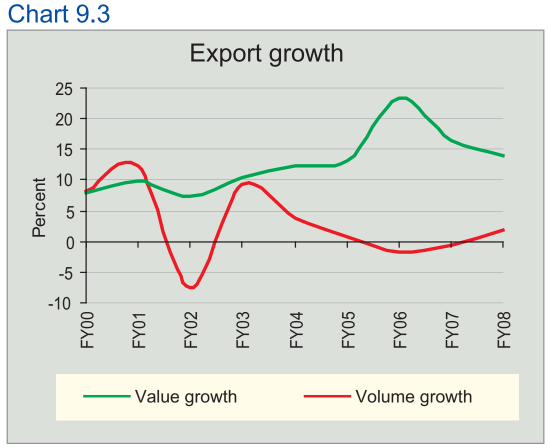

Table 9.1 Composition of merchandise exports

(million US Dollar)

| Items | FY07 | FY08 | % change |
|---|---|---|---|
| 1) Raw jute | 147.2 | 165.1 | 12.2 |
| 2) Jute goods | 320.8 | 318.3 | -0.8 |
| 3) Tea | 6.9 | 14.9 | 114.6 |
| 4) Leather | 266.1 | 284.4 | 6.9 |
| 5) Frozen shrimps and fish | 515.3 | 534.1 | 3.6 |
| 6) Woven garments | 4657.6 | 5167.3 | 10.9 |
| 7) Knitwear products | 4553.6 | 5532.5 | 21.5 |
| 8) Fertilizer | 125.1 | 91.3 | -27.0 |
| 9) Terry towel | 106.0 | 112.9 | 6.5 |
| 10) Others | 1479.3 | 1890.0 | 27.8 |
| **Total:** | **12177.9** | **14110.8** | **15.9** |

Source : Export Promotion Bureau.

Chart 9.3



9.5 Receipts under the capital and financial account decreased by USD 1107.0 million due mainly to bulk payments made by BPC. Thus, the surplus in overall balance came down to USD 604.0 million in FY08 compared to USD 1493.0 million in FY07. Table XVI at Appendix-2 of this Report shows the balance of payments statement for FY08 and FY07. Chart 9.2 portrays the trends of trade, current account and overall balances as a percentage of GDP in recent years.

9.6 As a potential source of foreign exchange reserves, foreign direct investment (FDI) has been emphasized by the Government. However, as per provisional estimate, it is seen that FDI flows decreased by 18.0 percent to USD 650.0 million in FY08 from USD 793.0 million in FY07.

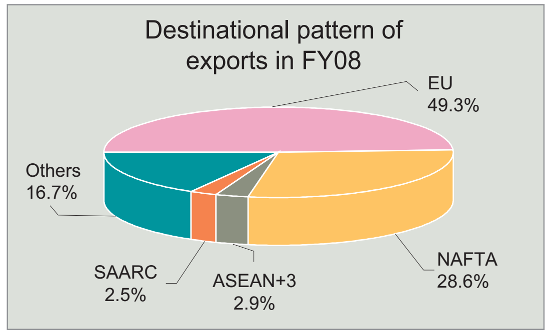
### Exports

9.7 Table 9.1 and Chart 9.3 show that total exports in FY08 had a significant growth over FY07. Aggregate exports increased by 15.9 percent to USD 14110.8 million in FY08, from USD 12177.9 million of FY07. Apparels (woven garments and knitwear products) continued to occupy an overwhelming (three fourth) share of the export basket in FY08.

### Destination

9.8 The destinational pattern of exports in FY08 showed continued heavy dependence on the markets in Europe and North America. 49.3 percent of exports were destined for the EU bloc while another 28.6 percent entered into the NAFTA bloc. Export to the ASEAN+3 (i.e. the ASEAN bloc, China, Japan and South Korea) countries, SAARC and other regions constituted 2.9, 2.5 and 16.7 percent respectively of total exports in FY08 (Chart 9.4).

Chart 9.4




### Composition

9.9 **Readymade garments (woven and knitwear) :** Woven products, which fetched about 48.29 percent of total export earnings of the apparels sector, registered a high increase in receipts, from USD 4657.6 million of FY07 to USD 5167.3 million in FY08, contributed mainly by increased shipment (10.8 percent), while unit price increased only marginally (0.14 percent). Knitwear products showed a significant growth (21.5 percent), fetching USD 5532.5 million in FY08 compared with USD 4553.6 million earned in FY07 due mainly to increase of shipment (21.1 percent) as well as unit price (0.4 percent).

9.10 **Frozen food:** The frozen food sector, comprising principally of shrimps, marked an increase in earnings during FY08. Receipts from export of shrimps and fish increased by 3.6 percent from USD 515.3 million of FY07 to USD 534.1 million in FY08. Despite the export volume of shrimps decreased by 22.2 percent, export receipts increased as average unit price increased substantially by 25.2 percent in FY08.

9.11 **Raw jute:** In FY08, 3.8 million bales of raw jute valued at USD 165.1 million were exported against 3.4 million bales valued at USD 147.2 million in FY07. Both the volume of export of raw jute and unit price increased by 11.9 percent and by 0.2 percent respectively in FY08.

9.12 **Jute goods:** In FY08, 0.53 million metric tons of jute products valued at USD 318.3 million were exported, against 0.54 million metric tons valued at USD 320.8 million exported in FY07. Despite increase of average unit price by 0.5 percent, export of jute goods decreased by 0.8 percent in FY08 due to 1.8 percent decrease in volume.

9.13 **Leather:** Export earnings from leather registered an increase of 6.9 percent in FY08. In FY08, 56.9 million sft. of leather valued at USD 284.4 million were exported against the export of 53.8 million sft. valued at USD 266.1 million in FY07. Despite the average unit price was almost the same, export of leather increased due to 5.8 percent increase in volume in FY08.

9.14 **Tea:** In FY08, 10.3 million kilograms of tea valued at USD 14.9 million were exported against 4.8 million kilograms valued at USD 6.9 million in FY07. The volume of exports of tea increased markedly by 113.6 percent while average unit price was almost the same. As a result, export of tea increased by 114.6 percent in FY08.

9.15 **Fertilizer:** Export earnings from fertilizer decreased substantially by 27.0 percent in FY08. In FY08, 0.26 million tons of fertilizer valued at USD 91.3 million were exported against 0.44 million tons valued at USD 125.1 million in FY07. Export earnings from fertilizer decreased due mainly to the decrease of volume by 40.9 percent while average unit price increased by 22.7 percent.

**Export Promotion and Diversification**

9.16 The main source of hard earned foreign exchange of Bangladesh is the export sector. Though the international business has been opened and easier due to the globalization, the participating countries are being faced gradual mutual competition for existence in the international market. In this respect, each country is engaged in continuous endeavour to exist in the competition using its comparative advantages in commodity production. Bangladesh is also not exceptional. The Government has taken all necessary initiatives for all out development of this sector. The Government has taken the initiative to diversify the export sector by freeing this sector from the dependence on the limited export commodities and ensuring the commodity supply at competitive price in the world market. Use of modern technology in the business, simplification of import-export policies, market expansion, capacity building activities such as growth of productivity, production of quality commodities, reducing the trading cost and improvement of governance condition etc. are the prime areas that got utmost attention. At the same time, the Government has taken the initiative to enhance the export earnings through offering all probable scopes for the development of the service sector such as information and communication technologies, consultancy services, construction etc.

9.17 In order to facilitate export of the country, Export Development Fund (EDF) consisting USD 150.0 million as revolving fund is used to provide rediscounting facilities to the scheduled commercial banks in financing the exporters for imports of raw materials, accessories, spare parts and packing materials under export L/Cs with a single borrower exposure up to a maximum limit of USD 1.5 million.

Total disbursement from EDF in FY08 stood at USD 215.97 million against USD 175.22 million in FY07. The outstanding balance as of end June 2008 stood at USD 75.85 million, which was USD 54.99 million in FY07. The interest rate on USD under EDF remained unchanged at LIBOR+1%.

Box 9.1

## Export Processing Zones in Bangladesh

With a view to achieving rapid economic growth through industrialization Bangladesh Government has adopted an open door policy to attract foreign direct investment (FDI) in Bangladesh. With this aim in view, Bangladesh Export Processing Zones Authority Act XXXVI was passed by the Parliament in 1980.

Bangladesh Export Processing Zones Authority (BEPZA) is an official organ of the Government to promote, attract and facilitate foreign direct investment as well as local investment. The first EPZ started operation in Chittagong in 1983. Having the one decade experience second EPZ was established at Savar, Dhaka in 1993.

Presently, a total of 8 EPZs are functioning/ operating in different locations of the country. The main objectives of EPZs are: (i) Promotion of foreign direct investment and local investment, (ii) Transfer of technology, (iii) Employment generation & poverty alleviation, (iv) Development of backward & forward linkages, and (v) Promotion of export.

Incentives and facilities provided by the Government in EPZs are: (i) 100% foreign ownership permissible (ii) Enterprises enjoy MFN (Most Favoured Nation) status (iii) No ceiling on foreign investment (iv) Full repatriation of capital & dividend (v) BEPZA accords recommendation for residentship/ citizenship (vi) Tax holiday for 10 years followed by reduced rate for next 5 years (vii) Duty free export & import (viii) GSP facility available (ix) Duty & quota free access to EU (EBA), Canada, Norway, Australia & USA under process.

In addition, EPZs provide infrastructure and support services as follows: (i) Fully serviced plots (average size 2000 SQM) (ii) Factory building available on rental basis (iii) Business support services (iv) Courier, banks, C & F agent, shipping agent, MTO, etc. (v) Administrative support services (vi) Commissariat, health club, investors club, medical center, sports complex, etc. (vii) Work permits issued by BEPZA (viii) IP & EP issued within the same day (ix) No UD (Utilization Declaration), IRC (Import Registration Certificate), ERC (Export Registration Certificate) & Renewal of Bond license required (x) Import from & 10% sale to DTA (Local market) allowed (xi) Customs clearance at factory site (xii) Intra/Inter Zone sub-contracting & transfer of goods allowed (xiii) Available workforce.

It is to be noted that as on 30 June 2008 a total of 33 countries including South Korea, Bangladesh, Japan, China, Malaysia, Taiwan, U.S, U.K, Italy, Canada, Netherlands, Germany, British Virgin Island, India, Sweden, Singapore, Pakistan, Panama, Switzerland, Belgium, Denmark, France, Thailand, Sri Lanka, Indonesia, Australia, Nepal, Mauritius, Ireland, U.A.E., Turkey, Ukraine, Marshal Island have already invested in the eight EPZs. Further to be mentioned that in order to cater the need of the investors two more EPZs, one at Feni and another at Munshigonj are in the process.

There are three categories of investment.

- A - 100% Foreign Ownership
- B - Joint Venture
- C - 100% Local Venture

The category-wise enterprises in the EPZs* of Bangladesh is mentioned below:

| Name of EPZ | A | B | C | Total |
|---|---|---|---|---|
| Chittagong EPZ | 95 | 24 | 52 | 171 |
| Dhaka EPZ | 73 | 18 | 30 | 121 |
| Mongla EPZ | 13 | 2 | 1 | 16 |
| Ishwardi EPZ | 9 | 5 | 7 | 21 |
| Comilla EPZ | 12 | 11 | 12 | 35 |
| Uttara EPZ | 2 | 1 | 5 | 8 |
| Adamjee EPZ | 17 | 10 | 10 | 37 |
| Karnaphuli EPZ | 25 | 7 | 13 | 45 |
| **Total :** | 246 | 78 | 130 | 454 |
| As % of total | 54.19 | 17.18 | 28.63 | 100.00 |

* As of June 2008.

A total investment of around US$ 1435.45 million was made in the EPZs of Bangladesh since their inception. Out of this, Chittagong EPZ accounted for 46.56% of investment followed by Dhaka EPZ at 43.14% and Comilla

## Export Processing Zones in Bangladesh

*(Contd.)*

EPZ at 5%. Most of the investment in EPZs are in RMG sector (Woven, knitwear and accessories) followed by textile, electronic, footwear & leather goods, metal products.

One of the most important objectives of establishing EPZs is the creation of employment opportunities. As such, the number of people working in the EPZs stood at 218,299 in June 2008. Out of this, about 56.71% are in Chittagong EPZ followed by 34.55% in Dhaka EPZ and 3.56% in Comilla EPZ. Pragmatic employment policy is followed in issuing EPZ's work permit by BEPZA within minimum period of time for foreign technicians/ expatriates. They enjoy equal rights similar to those of Bangladesh nationals. BEPZA is vested with the responsibility to administer labour matters for all enterprises located in EPZs. Minimum monthly wages in EPZs as per EPZ rule have been set as follows: Unskilled labour US$ 30-38, Semi-skilled labour US$ 45 and Skilled labour US$ 59-60. It is to be mentioned that among the Asian countries, the lowest minimum wages are being provided to the workers in Bangladesh's EPZs.

Bangladesh achieved a significant growth in export through the EPZs. Initially, the share of export earnings from EPZs in total exports was low. But it increased gradually. This share was 15.49 percent in FY00 and increased to 17.22 percent in FY08. Export earnings from the EPZs registered a growth of 17.73 percent in FY08 which kept pace with the national export growth. Recently export from the EPZs has markedly increased mainly due to increases in investment as well as productivity.

Export, import and value addition by EPZs

(million USD)

| Year | Total export* | Exports from EPZs** | Share of EPZs export in total export (%) | Imports by EPZs** | | | Gross value addition (%) |
|---|---|---|---|---|---|---|---|
| | | | | Total import | Of which, Capital machinery | Building & others materials | |
| FY00 | 5752.20 | 890.81 | 15.49 | 766.52 | 22.16 | 4.973 | 19.75 |
| FY01 | 6467.28 | 1067.87 | 16.51 | 802.28 | 24.92 | 10.98 | 37.58 |
| FY02 | 5986.10 | 1077.02 | 17.99 | 755.58 | 28.43 | 14.73 | 48.25 |
| FY03 | 6548.40 | 1200.00 | 18.33 | 876.82 | 29.10 | 5.44 | 40.82 |
| FY04 | 7603.00 | 1354.00 | 17.81 | 1098.38 | 49.34 | 9.21 | 28.60 |
| FY05 | 8654.50 | 1548.68 | 17.89 | 1180.13 | 47.92 | 14.91 | 36.48 |
| FY06 | 10526.20 | 1836.18 | 17.44 | 1340.32 | 69.49 | 15.33 | 43.32 |
| FY07 | 12177.90 | 2063.67 | 16.95 | 1436.69 | 67.84 | 17.39 | 49.57 |
| FY08 | 14110.80 | 2429.58 | 17.22 | 1723.18 | 107.28 | 39.81 | 49.53 |

Source : * Export Promotion Bureau.
** Bangladesh Export Processing Zones Authority.

Note : In this table, exports of EPZ include foreign, intra-zone, inter-zone and export oriented industry (EOI) and imports of EPZ include foreign, intra-zone, inter-zone and domestic tariff area (DTA).

It is seen from the above table that the gross value addition by EPZs has been increasing in recent years. This was 19.75 percent in FY00 which increased to 36.48 percent in FY05 and further to 49.53 percent in FY08. At present, the principal export item of Bangladesh is RMG. But firms in EPZs have been exporting different kinds of products like textile, terry towels, hats, lens, electrical equipments and electronics products, footwear and leather products, plastic products, optical goods, packaging materials, ropes and agro products etc. Besides, there are many kinds of brand products like Nike, Reebok, H&M, J.C Penny, Wal-Mart, Adidas etc. (RMG products), camera lens of Konica, Minolta, Nikon, Fuji, Olympus, mobile parts of Sony, automobile parts of Nissan, Mitsubishi, and Hino are being produced in EPZs and exported from Bangladesh. These sorts of exports carry the sign of diversification in Bangladesh's export sector, with EPZs playing an important role in this regard.

## Imports

9.18 Import payments (fob) during FY08 stood at USD 19486.0 million registering a growth of 25.6 percent compared to USD 15511.0 million in FY07. Except capital machinery, payments for all import items increased substantially during FY08. Capital machinery import decreased by 13.7 percent and textile & articles thereof remained almost same during FY08. Food grains & other food items, consumer & intermediate goods and capital goods & others contributed in varying degrees to the rise in aggregate imports during FY08 over FY07 (Table 9.2). Increasing consumer and industrial needs raised the import of petroleum & petroleum products, industrial raw materials (clinker, chemicals, raw cotton, yarn etc.). In particular, food grains import increased substantially by 142.9 percent to USD 1411.0 million in FY08 from USD 581.0 million in FY07 (rice 385.6 percent & wheat 33.9 percent) due mainly to the two consecutive devastating floods and cyclone 'Sidr'. Other food items increased by 55.7 percent to USD 2082.0 million in FY08 from USD 1337.0 million in FY07 (edible oil 72.6 percent, pulses 67.7 percent, milk & cream 65.1 percent, sugar 34.7 percent, oil seeds 28.3 percent and spices 5.3 percent). Consumer and intermediate goods import increased by 23.6 percent to USD 9616.0 million in FY08 from USD 7781.0 million in FY07 (fertiliser 77.0 percent, clinker 44.6 percent, raw cotton 41.2 percent, tanning & dyeing extracts 35.4 percent, chemicals 33.2 percent, crude petroleum 32.6 percent, pharmaceutical products 26.5 percent, plastics and rubber & articles thereof 25.7 percent, petroleum products 20.4 percent, yarn 18.7 percent and staple fibre 13.4 percent). Capital goods and other imports also increased by 14.4 percent to USD 7226.0 million in FY08 from USD 6314.0 million in FY07 (others 28.9 percent and iron, steel and other base metal 19.8 percent). Imports by EPZs increased by 13.1 percent to USD 1294.0 million in FY08 from USD 1144.0 million in FY07.

### Terms of Trade

9.19 In FY08, both the export price index and import price index have increased by 3.5 and

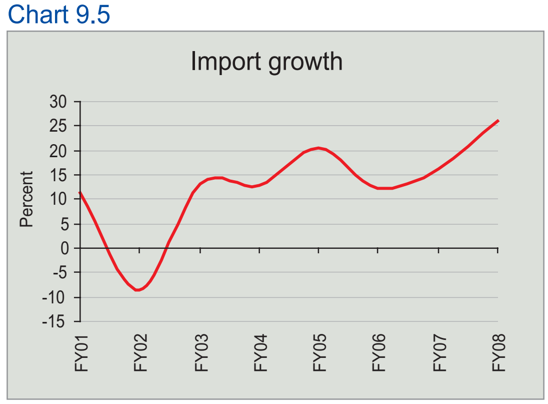
Table 9.2 Composition of merchandise imports

(million US Dollar)

| Items | FY07 | FY08[P] | % changes |
|---|---|---|---|
| **A. Food grains** | **581** | **1411** | **142.9** |
| 1. Rice | 180 | 874 | 385.6 |
| 2. Wheat | 401 | 537 | 33.9 |
| **B. Other food items** | **1337** | **2082** | **55.7** |
| 1. Milk & cream | 83 | 137 | 65.1 |
| 2. Spices | 76 | 80 | 5.3 |
| 3.Oil seeds | 106 | 136 | 28.3 |
| 4. Edible oil | 583 | 1006 | 72.6 |
| 5. Pulses (all sorts) | 195 | 327 | 67.7 |
| 6. Sugar | 294 | 396 | 34.7 |
| **C. Consumer and intermediate goods** | **7781** | **9616** | **23.6** |
| 1. Clinker | 240 | 347 | 44.6 |
| 2. Crude petroleum | 524 | 695 | 32.6 |
| 3. Petroleum products | 1709 | 2058 | 20.4 |
| 4. Chemicals | 668 | 890 | 33.2 |
| 5. Pharmaceutical products | 49 | 62 | 26.5 |
| 6. Fertilizer | 357 | 632 | 77.0 |
| 7. Tanning & dyeing extracts | 161 | 218 | 35.4 |
| 8 Plastics and rubber & articles thereof | 643 | 808 | 25.7 |
| 9. Raw cotton | 859 | 1213 | 41.2 |
| 10. Yarn | 582 | 691 | 18.7 |
| 11.Textile & articles thereof | 1892 | 1892 | 0.0 |
| 12. Staple fibre | 97 | 110 | 13.4 |
| **D. Capital goods and others** | **6314** | **7226** | **14.4** |
| 1. Iron, steel & other base metal | 985 | 1180 | 19.8 |
| 2. Capital machinery | 1929 | 1664 | -13.7 |
| 3. Others | 3400 | 4382 | 28.9 |
| **E. Imports by EPZ** | **1144** | **1294** | **13.1** |
| **Total import (cif) (A+B+C+D+E)** | **17157** | **21629** | **26.1** |
| Less (-) freight & insurance charges | 1646 | 2143 | |
| **Total Import (fob)** | **15511** | **19486** | **25.6** |

Source: Statistics Department, Bangladesh Bank.
P= Provisional.

Chart 9.5



3.4 percent respectively. As a result, the terms of trade improved slightly by 0.1 percent in FY08 over FY07.

**Workers' Remittances**

9.20 Inward remittances from Bangladeshi nationals working abroad continued to play an important supporting role in strengthening the current account balance. Receipts on this sector increased by 32.4 percent to USD 7914.8 million in FY08 from USD 5978.5 million in FY07. The underlying reason was that Bangladesh Bank made vigorous efforts such as expansion of activities of drawing arrangements, review of statements received from foreign banks/exchange houses, close monitoring and supervision of banks etc. Besides, the concerned scheduled banks had ensured quick delivery of remittances by reducing lead-time to the beneficiaries in Bangladesh, which brought substantial development in the delivery system. It is to be mentioned that, drawing arrangements have been made between 39 Bangladeshi banks and 270 foreign banks/exchange houses situated throughout the globe. Furthermore, annual remittance threshold has been refixed up amounting to USD 3.00 million for each USA-based exchange houses, GBP 2.00 million for UK-based exchange houses, EURO 2.00 million for Italy-based exchange houses, USD 2.5 million for Canadian exchange houses, USD 3.00 million each for KSA, UAE, Kuwait, Qatar, Oman and Bahrain based exchange houses and USD 1.5 million for each all other country exchange houses. For these measures, remittances recorded a substantial increase by 32.4 percent to USD 7914.8 million during the year under report. Remittances as percentage of GDP increased by 1.3 percentage point to 10.02 in FY08 from 8.72 in FY07. The shares of major source countries in the remittance receipts of FY07 and FY08 are given at Chart 9.7.

**Foreign Aid**

9.21 Total official foreign aid disbursement increased by 25.0 percent to USD 2039.0

Table 9.3 Terms of trade of Bangladesh
(base : FY96=100)

| Year | Export price index | Import price index | Commodity terms of trade |
|---|---|---|---|
| FY00 | 117.49 | 126.64 | 92.77 |
| FY01 | 120.31 | 136.17 | 88.35 |
| FY02 | 123.15 | 146.41 | 84.11 |
| FY03 | 126.23 | 157.76 | 80.01 |
| FY04 | 135.19 | 164.15 | 82.36 |
| FY05 | 139.60 | 169.96 | 82.14 |
| FY06 | 142.38 | 176.66 | 80.60 |
| FY07 | 149.28 | 183.09 | 81.53 |
| FY08* | 154.54 | 189.39 | 81.60 |

Source: Bangladesh Bureau of Statistics.
* estimated.

Chart 9.6

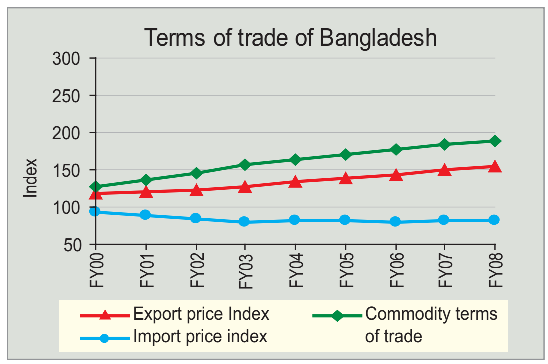
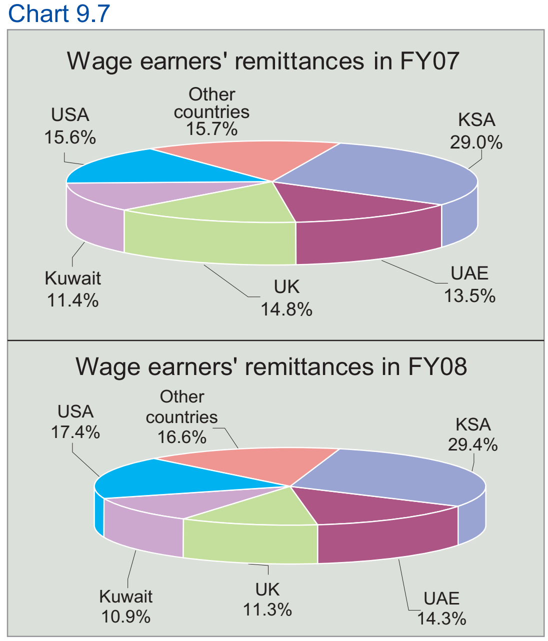



Chart 9.7



million in FY08 from USD 1631.0 million received in FY07 (Table 9.4). Food aid disbursement increased by 38.3 percent to USD 83.0 million in FY08 from USD 60.0 million in FY07. The disbursement of project assistance stood at USD 1956.0 million in FY08 which was USD 1571.0 million in FY07. It is mentionable that, no commodity aid was received in FY08 as in the preceding year.

Total outstanding official external debt as of 30 June 2008 stood at USD 20110.0 million (25.5 percent of FY08 GDP) against USD 19355.0 million as of 30 June 2007 (28.3 percent of FY07 GDP). Repayment of official external debt stood at USD 767.0 million (excluding repurchases of loans from the IMF) in FY08. This was USD 63.0 million or 8.9 percent higher than the repayment in FY07. Out of the total repayments, principal payments amounted to USD 580.0 million while interest payments stood at USD 187.0 million in FY08, against USD 525.0 million and USD 179.0 million respectively paid during FY07. The debt-service ratio as percentage of exports was 5.5 percent in FY08.

**Foreign Exchange Market Operations**

9.22 Under floating exchange rate regime, banks are free to set their own rates for inter-bank and customer transactions. The exchange rate is being determined on the basis of market demand and supply forces of the respective currencies. For avoiding unusual volatility in the exchange rate, Bangladesh Bank may purchase and sell US dollar as and when it deems necessary to maintain stability in the foreign exchange market.

During June-August 2007, Taka fairly appreciated by 0.47 percent moving from Taka 68.93 to Taka 68.61 against US Dollar while it depreciated slightly by 0.14 percent turning around to Taka 68.70 during August-October 2007. After that the local currency gained against Dollar due mainly to sufficient inflow of foreign exchange as remittances & export receipts in the market and the trend continued till the end of FY08 standing at Taka 68.53

Table 9.4 Foreign aid receipts and debt repayments*

(million US Dollar)

| Particulars | FY06 | $FY07^R$ | $FY08^P$ |
|---|---|---|---|
| 1. Receipts | 1568 | 1631 | 2039 |
| i) Food aid | 97 | 60 | 83 |
| ii) Commodity aid | - | - | - |
| iii) Project aid | 1471 | 1571 | 1956 |
| 2. Repayments (MLT) | 666 | 704 | 767 |
| i) Principal | 488 | 525 | 580 |
| ii) Interest | 178 | 179 | 187 |
| 3. Outstanding external debt as of end June | 18603 | 19355 | 20110 |
| 4. Outstanding debt as percentage of GDP | 30.0 | 28.3 | 25.5 |
| 5. External debt services (MLT) as percentage of exports | 6.4 | 5.8 | 5.5 |

R=revised. P=Provisional.
* Excluding transactions with the IMF.

Table 9.5 Gross foreign exchange reserves of the Bangladesh Bank

(million US Dollar)

| Date | balance |
|---|---|
| June 1996 | 2,039 |
| June 1997 | 1,719 |
| June 1998 | 1,739 |
| June 1999 | 1,523 |
| June 2000 | 1,602 |
| June 2001 | 1,307 |
| June 2002 | 1,583 |
| June 2003 | 2,470 |
| June 2004 | 2,705 |
| June 2005 | 2,930 |
| June 2006 | 3,484 |
| June 2007 | 5,077 |
| July 2007 | 5,042 |
| August 2007 | 5,225 |
| September 2007 | 5,158 |
| October 2007 | 5,410 |
| November 2007 | 5,095 |
| December 2007 | 5,515 |
| January 2008 | 5,387 |
| February 2008 | 5,978 |
| March 2008 | 5,302 |
| April 2008 | 5,773 |
| May 2008 | 5,335 |
| June 2008 | 6,149 |

Source : Accounts and Budgeting Department, BB.

against Dollar. During October 2007 to June 2008, Taka appreciated by 0.25 percent. The weighted average exchange rate came down from Taka 68.8000 at the end of June 2007 to Taka 68.5297 at the end of June 2008.

During FY08, Bangladesh Bank sold USD 533.0 million (net) to increase liquidity in the foreign exchange market.

The volume of inter-bank foreign exchange transactions in FY08 stood at USD 3.57 billion including spot, forward and swap transactions, which was 17.4 percent lower than the USD 4.32 billion in FY07.

### Foreign Exchange Reserves

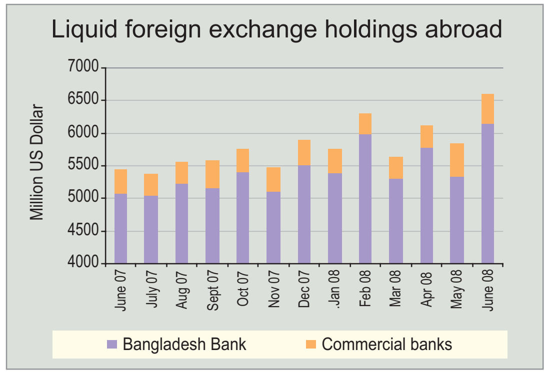
9.23 The gross foreign exchange reserves of the Bangladesh Bank continued to grow in the backdrop of steadily increasing export earnings and workers' remittances, and stood at USD 6149 million as at the end of June 2008 (Table 9.5). This represented a growth of 21.1 percent over USD 5077 million of end June 2007.

Foreign exchange balances held abroad by the commercial banks, on the other hand, increased by USD 89.36 million to USD 457.5 million over the same period. Total liquid foreign exchange holdings of the banking system (i.e., including the holdings of commercial banks) increased to USD 6606.5 million (Chart 9.8). The foreign exchange reserves represent approximately 57.0 percent of the BB's balance sheet and the income from these reserves is one of the most significant revenues of the BB.

### Reserve Management Strategy

9.24 The BB's reserve management strategy and operational procedure are strongly influenced by developments in the financial markets and by various aspects of the policy environment in which a central bank operates. The most relevant elements of policy environment in which reserve management operates are monetary policy framework, the exchange rate policy & regime and external debt position. After switching over from a pegged exchange rate regime to a floating exchange rate regime in May 2003, BB brought about significant changes in the monetary management in relation to its reserve management and investment.

Chart 9.8




Main objectives of the BB for holding foreign exchange reserves include maintenance and safety of adequate level of reserve to meet foreign obligations, liquidity of reserves for the purpose of monetary and exchange rate management and finally, optimal return from the reserves assuming controlled risks in a prudent manner that will preserve the nominal value of the reserve.

To contain counterparty risk, BB diversifies its investments out of its reserves among a number of internationally reputed central and commercial banks having good credit ratings assigned by the international rating agencies. With a view to minimizing exchange rate risk currency composition has been diversified among the major currencies. Duration benchmark is followed to minimize interest rate risks, while reserve management and investment functions have been segregated under three different reporting authorities.

However, keeping in view the stipulated liquidity restrictions and market & credit risk limits, BB diversified its portfolio investment into T-bills, repos, short term deposits including other money market instruments and corporate bonds etc. During FY08, BB had to keep a vigilant eye on placement/investment of funds with banks affected by U.S. sub-prime crisis.

### Transactions under Asian Clearing Union (ACU)

9.25 Total transactions of Bangladesh under the Asian Clearing Union (ACU) increased during FY08 compared to the preceding year. As in the preceding years, Bangladesh remained a net debtor in all the six bi-monthly settlements during FY08. Import payments increased substantially than export receipts with the ACU member countries during the year under report. Export of Bangladesh to ACU member countries recorded increase of USD 21.51 million or 16.4 percent from USD 131.5 million (Taka 902.3 crore) in FY07 to USD 153.01 million (Taka 1048.6 crore) in FY08. Import from the ACU member countries increased substantially by USD 1436.3 million or 62.4 percent from USD 2301.1 million (Taka 15808.7 crore) in FY07 to USD 3737.3 million (Taka 25611.8 crore) in FY08. As a result, the net debtor position of Bangladesh increased by USD 1414.8 million or 65.2 percent to USD 3584.3 million (Taka 24563.2 crore) in FY08 compared to USD 2169.6 million (Taka 14906.4 crore) in the preceding year. Receipts and payments of Bangladesh under ACU arrangement during the last three years are shown in Table 9.6.

### Transactions with the IMF

9.26 In April 2008, Bangladesh received SDR 133.32 million for assistance/recovery of millions of people affected by Sidr and two preceding floods under 'Emergency Natural Disaster Assistance Programme' of the IMF. Repayment of this fund will begin three years after the date of receipt of the fund.

Bangladesh was granted a loan of SDR 347.0 million from the IMF in June 2003 under its 3-year arrangement of Poverty Reduction and Growth Facility (PRGF). As per the request of Bangladesh, the PRGF was augmented and Bangladesh was granted a loan of SDR 53.33 million under the Trade Integration Mechanism (TIM) in July 2004. However, total purchase under PRGF stood at SDR 316.73 million at the end of June 2007 against the total loan facilities of SDR 400.33 million. No purchase/repayment was made to the IMF in FY08. Service charges paid to the IMF during the year amounted to SDR 5.11 million. Outstanding liabilities to the Fund at the end of June 2008 stood at SDR 450.06 million (Table 9.7).

Table 9.6 Receipts and payments of Bangladesh under the ACU

(million US Dollar)

| Head of transaction | FY06 | FY07 | FY08 |
|---|---|---|---|
| 1. Receipts (Export) | 144.7 | 131.5 | 153.0 |
| | (975.7) | (902.3) | (1048.6) |
| 2. Payments(Import) | 1932.8 | 2301.1 | 3737.3 |
| | (13009.7) | (15808.7) | 25611.8 |
| Net: Surplus (+)/ Deficit (-) | -1788.1 | -2169.6 | -3584.3 |
| | (-12034.0) | (-14906.4) | (-24563.2) |

Note: Figures in parentheses indicate Taka in crore.
1 ACUD = 1 USD; 1 USD = Taka 68.5297.

Table 9.7 Outstanding principal liabilities against the facilities received from the IMF

(million SDR)

| Facility | Cumulative drawing/ purchase | Outstanding liability as of end June 2007 | Purchase/ drawing in FY08 | Outstanding liability as of end June 2008 |
|---|---|---|---|---|
| PRGF June 2003 | 316.73 | 316.73 | - | 316.73 |
| Emergency Assistance April 2008 | 133.33 | - | 133.33 | 133.33 |
| **Total** | | **316.73** | **133.33** | **450.06** |

Source : Forex Reserve & Treasury Management Department, BB.

### Exchange Rate

9.27 During the 1st quarter of FY08, Taka-Dollar exchange rate started with Taka 68.85 per US Dollar. Initially there was a modest pressure on exchange rate due to higher demand in the foreign exchange market. With the beginning of 2nd quarter, Taka started to appreciate and in the mid December 2007 it stood at Taka 68.48 per US Dollar. During the 3rd quarter of FY08, exchange rate was relatively stable ranging within Taka 68.56-68.60. However, at the end of FY08, Taka gained slightly and stood at Taka 68.53.

### Changes in Foreign Exchange Regulations

9.28 The major changes in foreign exchange regulations in FY08 were as under:

a) Cash incentives for export of selected items during FY08 were as follows: 5

percent for export oriented local textile sector, 10 percent for frozen shrimp and fishes, 15 percent for leather products, 15 percent and 20 percent (depend on using local material) for products made by hoogla, straw, coir of sugar cane, 20 percent for agro (fruit and vegetables) and agro processing products, 10 percent for tobacco, 10 percent for potato, 15 percent for bicycle and crust bone, 7.5 percent for jute products, 15 percent for hatching eggs and day-old chicken of poultry industries, 10 percent for light engineering products, 20 percent for liquid glucose from Ishwardi EPZ and 20 percent for halal meat.

b) The credit facility under EDF increased from USD 100 million to USD 150 million to expand and facilitate the export oriented industries and a single borrower's exposure limit was also increased up to USD 1.5 million from USD 1 million.

c) For implementation of the Uniform Customs and Practice for Documentary Credits (UCP-600), the Authorized Dealers (ADs) were advised to explicitly mention that UCP-600 shall apply for all Letters of Credit (LCs) to be opened from 1 July 2007. Similarly, in case of exports from Bangladesh against LCs, the ADs must ensure that the terms of the LCs are in conformity with the rules of UCP 600. If otherwise, ADs shall get the LCs amended accordingly.

d) The compulsory registration of Letter of Credit Authorisation Form (LCAF) with the BB for import without LCs has been relaxed according to Import Policy Order 2006-09. Under the changed situation for import without LC, the LCAF is to be registered with authorised dealer rather than the BB.

e) Release of foreign exchange in the form of cash favouring passengers proceeding abroad has been increased up to USD 2000 or equivalent from USD 1500 or equivalent.

f) It has been decided that authorised dealers can release foreign exchange favouring persons proceeding abroad for a valid job or migration abroad against one-way ticket. However, amount of such release of foreign exchange will not exceed the half of the un-utilised annual travel quota entitlement of the person concerned in the related calendar year.

g) To facilitate export from Bangladesh, BB has allowed use of seven more incoterms in addition to existing two incoterms. Under the new arrangement, exports may be made on EXW, FCA, FAS, CIF, CPT, CIP and DAF provided those are stipulated in the relevant LCs or sales contracts in addition to FOB and CFR. ADs are strongly advised to inform the exporters about the risk and responsibility involved in such cases. While verifying the EXP Forms, the ADs must show the FOB or its equivalent value and cost of freight, insurance and other charges separately on the reverse of the related EXP Form.

Appropriate incoterms should be incorporated in the purchase contract/LC in case of import into Bangladesh in compliance with the Import Policy Order in force.

h) To facilitate outgoing foreign tourist/non-resident Bangladesh national, general permission has been accorded to reconvert their unspent Bangladesh Taka equivalent to maximum USD 100 at the bank booth situated at the departure lounge of international airport.

i) BB has allowed the ADs in foreign exchange for hedging of the price risk of commodities of their customers through standard exchange traded future/options and over-the-counter (OTC) derivatives on commodities subject to prior approval of BB. Only genuine underlying commodity price risk exposure(s) of the customers will be permitted to be hedged by commodity derivatives. Any kind of speculation through the use of commodity derivative instruments will not be permissible.

j) Policy guidelines for establishing drawing arrangements by banks in Bangladesh with exchange houses abroad have been in place from 9 October 2007 in order to make monitoring system more intensive and effective on drawing arrangement. While applying to BB for approval of establishing drawing arrangements with exchange houses abroad, banks are now required to comply with the instructions as mentioned in the said policy guidelines.

k) The satellite channel distributors have been instructed to obtain permission from BB under Section 18A of FER Act, 1947 to act as agent of foreign principals. For effecting remittance abroad by the satellite channel distributors, the AD banks shall forward application along with relevant/necessary documents to BB seeking approval.

**Anti-money Laundering Surveillance**

9.29 Bangladesh continued its effort during FY08 to combat money laundering under the Money Laundering Prevention Act, 2002 and Money Laundering Prevention Ordinance, 2008 that empowered BB to perform the anchor role in combating money laundering by building awareness in the financial community and monitoring suspicious transactions. The Anti-Terrorist Ordinance, 2008 also empowered BB with specific power for detection and prevention of terrorist financing and to take necessary measures so that banking channel cannot be misused for financing in terrorism.

9.30 The Financial Intelligence Unit (FIU) of Anti-Money Laundering Department (AMLD) has taken initiative to maintain a strong database for financial crime, suspicious transaction report (STR) and cash transaction report (CTR). All necessary steps have been taken to ensure the security and confidentiality of the FIU. FIU is working actively to establish relationship with other FIUs around the globe to get benefit from experiences and information, and trying to become member of Egmont Group.

9.31 During FY08, BB received 466 suspicious transaction reports (STR)/complaints from the banks. 25 commercial banks have been penalized under the provision of MLPA, 2002 for non-compliance of the Act.

9.32 BB has revised and changed the threshold of CTR from Bangladesh Taka 0.50 million and above to 0.70 million and above that came into effect from September 2007. Uniform account opening and KYC profile form for all banks have also been introduced in June 2008.

9.33 AMLD has continued its effort to create awareness among the bank officials during FY08. It assisted the banks to conduct massive training for the bank officials for this issue throughout the country. AMLD also arranged workshop for other law enforcing agencies

9.34 During FY08, AMLD represented Bangladesh in different international conferences/meetings/workshops related to money laundering, terrorist financing and strengthening co-operation with other countries in its drive against money laundering and terrorist financing. FIU continued its effort to become a member of Egmont Group (the association of FIUs) during FY08. Bilateral and multilateral development partners are providing good support in fighting money laundering and terrorist financing as also bringing dirty money back home.

An Inter-Agency Task Force has also been constituted by the Government for recovering the stolen asset. Governor of BB is acting as a convener while FIU head is acting as the member secretary of the Task Force.