Macroeconomic Performance and Prospects

Global Economic Outlook

1.1 The global economic growth for 2015 is projected to be 3.1 percent, slightly lower than the actual 3.4 percent growth in 2014 (latest World Economic Outlook, October 2015). However, global economic growth in 2016 is expected to increase to 3.6 percent in light of the modest recovery in advanced economies and higher growth prospects for emerging markets and developing economies. In the advanced economies, growth is expected to be 2.0 percent in 2015 and increase to 2.2 percent in 2016. However, growth in emerging markets and developing economies is projected for 2015 at 4.0 percent, 0.6 percentage point lower than in 2014, but expected to increase to 4.5 percent in 2016.

1.2. The forecast of modest economic growth in advanced economies reflects the gradual acceleration of economic activity in the US as well as the euro area supported by lower fuel prices, higher employment, monetary easing, higher investment, etc. and the restoration of the Japanese economy towards a positive growth path. Growth rate of the United States is expected to increase to 2.6 percent in 2015 and 2.8 percent in 2016 from 2.4 percent in 2014. The prospect of economic recovery in the euro area seems reasonable with the increase in domestic demand and growth is projected to be 1.5 percent in 2015 and 1.6 percent in 2016. The economic growth in Japan is projected to be 0.6 percent in 2015, and 1.0 percent in 2016 from negative 0.1 percent growth in 2014.

Table 1.1 Overview of the World Economic Outlook projections

(annual percentage change)

	2013	2014	Projections 2015	Projections 2016
World output	**3.3**	**3.4**	**3.1**	**3.6**
Advanced economies	1.1	1.8	2.0	2.2
United States	1.5	2.4	2.6	2.8
Euro area	-0.3	0.9	1.5	1.6
Germany	0.4	1.6	1.5	1.6
France	0.7	0.2	1.2	1.5
Italy	-1.7	-0.4	0.8	1.3
Spain	-1.2	1.4	3.1	2.5
United Kingdom	1.7	3.0	2.5	2.2
Japan	1.6	-0.1	0.6	1.0
Canada	2.0	2.4	1.0	1.7
Other advanced economies	2.2	2.8	2.3	2.7
Emerging market and developing economies	5.0	4.6	4.0	4.5
Emerging and developing Asia	7.0	6.8	6.5	6.4
China	7.7	7.3	6.8	6.3
ASEAN-5	5.1	4.6	4.6	4.9
South Asia				
Bangladesh	6.0	6.3	6.5	6.8
India	6.9	7.3	7.3	7.5
Pakistan	3.7	4.0	4.2	4.5
Sri Lanka	7.3	7.4	6.5	6.5
World trade volume (goods and services)	**3.3**	**3.3**	**3.2**	**4.1**
Imports				
Advanced economies	2.0	3.4	4.0	4.2
Emerging and developing economies	5.2	3.6	1.3	4.4
Exports				
Advanced economies	2.9	3.4	3.1	3.4
Emerging and developing economies	4.4	2.9	3.9	4.8
Commodity prices (U.S. dollars)				
Oil	-0.9	-7.5	-46.4	-2.4
Nonfuel	-1.2	-4.0	-16.9	-5.1
Consumer prices				
Advanced economies	1.4	1.4	0.3	1.2
Emerging market and developing economies	5.8	5.1	5.6	5.1
South Asia				
Bangladesh	7.5	7.0	6.4	6.6
India	10.0	5.9	5.4	5.5
Pakistan	7.4	8.6	4.5	4.7
Sri Lanka	6.9	3.3	1.7	3.4

Source: World Economic Outlook, October 2015, IMF.

1.3 The growth in emerging market and developing economies in 2015 is expected to decline as a result of lower commodity prices, slower capital inflows, embargoes and conflicts in a number of countries and the gradual fall in growth in China. However, the growth is projected to rebound in some countries in 2016. Growth rate of China is forecast to decrease to 6.8 percent in 2015 and 6.3 percent in 2016 from 7.3 percent in 2014. India's economic growth is expected to remain unchanged in 2015 and projected to be 7.5 percent in 2016 taking advantage of the recent policy reforms and gradual increase in investment.

1.4 Consumer prices in advanced economies are expected to decline to 0.3 percent in 2015 from 1.4 percent in 2014 and then increase to 1.2 percent in 2016. In contrast, consumer prices in emerging markets and developing economies are expected to increase to 5.6 percent in 2015 from 5.1 percent in 2014. However, it is expected that the declining oil and other commodities prices will reduce the overall consumer prices by 0.5 percentage points restoring it to 5.1 percent again in 2016. The headline inflation in advanced economies decreased in 2014 as a result of low oil and other commodity prices.

1.5 World trade volume growth is projected to decrease from 3.3 percent in 2014 to 3.2 percent in 2015 and then increase to 4.1 percent in 2016. The balance of trade in advanced economies is expected to deteriorate in 2015 and 2016, since export growth is projected to be weaker than import growth. The growth rate of imports for advanced economies is expected to increase from 3.4 percent in 2014 to 4.0 percent in 2015 and further to 4.2 percent in 2016. However, the balance of trade in emerging markets and developing economies is expected to improve in 2015 and 2016, since export growth is projected to be stronger than import growth. In emerging markets and developing economies, growth rate of imports is projected to decline from 3.6 percent in 2014 to 1.3 percent in 2015, and then rise to 4.4 percent in 2016. Exports of advanced economies are expected to grow by 3.1 percent and 3.4 percent in 2015 and 2016 respectively while the same in emerging markets and developing economies are expected to grow by 3.9 percent and 4.8 percent during the same years.

1.6 According to Global Financial Stability Report (GFSR) of October 2015, the financial stability has improved in advanced economies reflecting a strong macro-financial environment in those which coincided with broadening of economic recovery, augmented confidence in monetary policies, and abated deflation risks. Although resilience to external shocks has increased in many emerging market economies, several key economies face substantial domestic imbalances and lower growth. Some of the emerging market economies relied on rapid credit creation to side step the worst impacts of the global crisis. As a result, banks in emerging market economies have thinner capital cushions, while nonperforming loans are set to rise as corporate earnings and asset quality deteriorated. These developments in emerging market banking systems stand in contrast to those in advanced economies, where banks have spent the past few years deleveraging and repairing balance sheets, raising capital, and strengthening funding arrangements. Against a challenging backdrop of falling commodity prices and weaker growth, several emerging market sovereigns are at greater risk of losing investment-grade ratings in the medium term.

1.7 According to World Economic Outlook (WEO) of October 2015, the balance of risks is still tilted to the downside. Vulnerabilities and financial stability risks in emerging market economies have likely increased amid lower growth, recent commodity price declines, and increased leverage after years of rapid credit growth. Increased financial market volatility can pose financial stability challenges in advanced economies, with substantial spillovers onto emerging markets, including through tighter financial conditions and a reversal of capital flows. The main medium-term risk for advanced economies is a further decline of already-low growth into near stagnation, particularly if global demand falters further as prospects weaken for emerging market and developing economies. In emerging markets, medium-term risks come from spillovers from much slower potential growth in China, or lower potential growth more generally.

Developments in the Bangladesh Economy

1.8 Over the last decade, the Bangladesh economy secured an average of 6.2 percent growth rate well above the global economic growth. Despite political doldrums, structural constraints and global volatility, the Bangladesh economy maintained its macroeconomic stability and high growth trajectory. In FY15, Bangladesh graduated to the status of a lower middle income country from the low income country, and to OECD Export Credit Eligibility group 5, which is just below India but ahead of all other South Asian neighbours. The recurrence of political problems in January 2015 took toll on economic activity, particularly in services sector, agriculture, exports, and non-formal sector businesses. Domestic supply chain was disrupted due to disruptions of inter-district transportation. Yet, Bangladesh economy remained resilient and recorded a 6.5 percent growth of GDP in FY15. Higher growth of industry sector along with satisfactory growth of services sector helped to achieve this satisfactory growth of the overall economy. The growth of agriculture sector was lower in FY15 compared to the preceding fiscal year due to the lower growth in crops and horticulture sub-sector. During FY15, the average inflation showed a downward trend due to favorable international commodity price movements and sound macroeconomic management.

1.9. A cautious yet growth and investment friendly monetary policy stance was implemented during FY15. Bangladesh Bank maintained policy continuity by keeping the policy rates unchanged to dispel the inflationary pressure and support economic growth. Broad money (M2) registered a 12.4 percent growth in FY15 against the target set at 16.5 percent and the actual growth of 16.1 percent in FY14. Total domestic credit decreased from 11.6 percent in FY14 to 10.1 percent in FY15. Private sector credit growth was 13.2 percent in FY15 which was slightly higher compared to the preceding fiscal year but remained lower against the targeted growth rate of 15.5 percent. On the other hand, the growth of credit to the public sector registered a negative growth rate at 2.5 percent in FY15 against the target set at a 25.3 percent increase. But a good amount of resources through selling National Savings Certificates and a higher amount of NBR tax revenue was collected.

1.10 Due to a steady appreciation of the Real Effective Exchange Rate (REER), export has suffered to some extent. The growth of export fell from 12.1 percent in FY14 to 3.3 percent in FY15 but the growth of imports increased from 8.9 to 11.3 percent during the same period. The higher growth of imports compared to exports led to an increase in trade deficit to the tune of USD 9917 million in FY15 from USD 6794 million in FY14. Workers' remittances growth stood at 7.5 percent in FY15 compared to 1.5 percent negative growth in FY14. A surplus in the overall balance of payments was maintained despite a deficit in current account balance. The foreign exchange reserves reached USD 205021 million at the end of FY15, at a comfortable level to meet over seven months of imports of goods and services. Bangladesh Bank continued its interventions in the domestic foreign exchange market by purchasing foreign currencies as and when deemed appropriate. As a result, nominal Taka-USD exchange rate remained stable during FY15.

Growth Performance

1.11 The growth of agriculture sector decreased to 3.0 percent in FY15 from 4.4 percent in FY14 due to the lower growth in crops and horticulture sub-sector. The growth rates of different sectors of GDP are presented in Table 1.2.

1.12 Industry sector growth increased to 9.6 percent in FY15 from 8.2 percent in FY14. In fact, the rate of growth of all sub-sectors of industry sector increased in FY15 compared to FY14. The most notable increase was in the case of small scale manufacturing sub-sector.

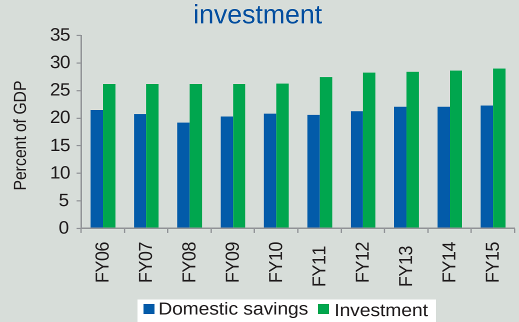
Table 1.2 Sectoral GDP growth rates

(at FY06 constant prices)

	FY06-FY13 (Average)	FY14^{R}	FY15^{P}
1. Agriculture	**4.4**	**4.4**	**3.0**
a) Agriculture and forestry	3.9	3.8	2.1
i) Crops and horticulture	3.9	3.8	1.3
ii) Animal farming	2.5	2.8	3.1
iii) Forest and related services	5.4	5.0	5.1
b) Fishing	6.3	6.4	6.4
2. Industry	8.6	8.2	9.6
a) Mining and quarrying	7.0	4.7	7.5
b) Manufacturing	9.1	8.8	10.3
i) Large and medium scale	9.4	9.3	10.2
ii) Small scale	7.9	6.3	10.7
c) Power, gas and water supply	8.2	4.5	7.0
d) Construction	7.5	8.1	8.6
3. Services	**5.9**	**5.6**	**5.8**
a) Wholesale and retail trade, repair of motor vehicles, motorcycles, and personal and household goods	6.7	6.7	6.6
b) Hotel and restaurants	6.1	6.7	6.9
c) Transport, storage and communication	7.8	6.1	6.0
d) Financial intermediations	9.5	7.3	8.8
e) Real estate, renting and other business activities	4.0	4.3	4.7
f) Public administration and defence	7.9	6.9	7.5
g) Education	7.1	7.3	7.6
h) Health and social works	5.1	5.1	5.7
i) Community, social and personal services	3.1	3.3	3.4
GDP (at FY06 constant market prices)	**6.2**	**6.1**	**6.5**

R = Revised, P = Provisional.
Source: Bangladesh Bureau of Statistics.

Chart 1.1 Domestic savings and investment



1.13 Services sector growth increased slightly to 5.8 percent in FY15 from 5.6 percent in FY14. This was driven by the higher growth of financial intermediations; public administration and defence; health and social works; real estate, renting and other business activities; education; hotel and restaurants; and community, social and personal services sub-sectors. However, growth of wholesale and retail trade, repair of motor vehicles, motorcycles, and personal and household goods and transport, storage and communication sub-sectors was lower than the preceding fiscal year. Financial intermediations sub-sector performed well registering a growth of 8.8 percent in FY15 compared with 7.3 percent in FY14 (Table 1.2).

Savings and Investment

1.14 Gross fixed investment as a percentage of GDP increased marginally to 29.0 percent in FY15 from 28.6 percent in FY14 (Chart 1.1). Within gross fixed investment, public investment grew faster than the private investment. As a result, the share of public investment in GDP increased from 6.6 percent in FY14 to 6.9 percent in FY15, the share of private investment increased slightly from 22.0 to 22.1 percent of GDP over the same period. The national savings as a percentage of GDP decreased slightly from 29.2 percent in FY14 to 29.1 percent in FY15. Domestic savings as a percentage of GDP increased from 22.1 percent in FY14 to 22.3 percent in FY15. The domestic savings-investment gap as a percentage of GDP increased to 6.7 percent in FY15 from 6.5 percent in FY14.

Price Developments

1.15 The average inflation rate (base: FY06=100) decreased to 6.4 percent at the end of FY15 from 7.4 percent at the end of FY14. This was driven by decrease in food inflation from 8.6 percent at the end of FY14 to 6.7 percent at the end of FY15. On the other hand, non-food inflation showed a gradual increase and stood at 6.0 percent in June 2015 compared with 5.5 percent in June 2014. Point-to-point inflation also decreased to 6.3 percent in FY15 from 7.0 percent in FY14.

Chart 1.2 National CPI inflation (12 month average : base FY06=100)

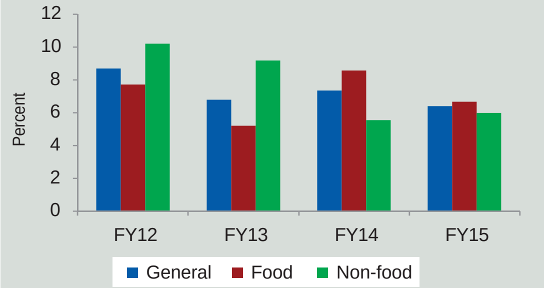


Chart 1.3 Monetary aggregates

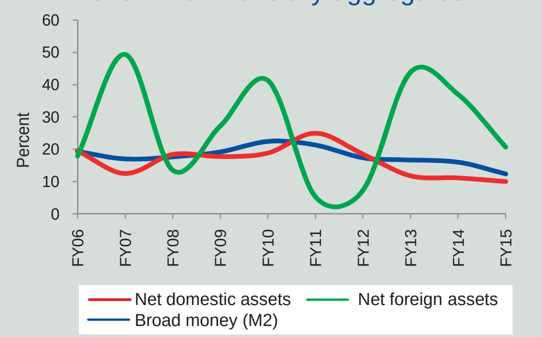
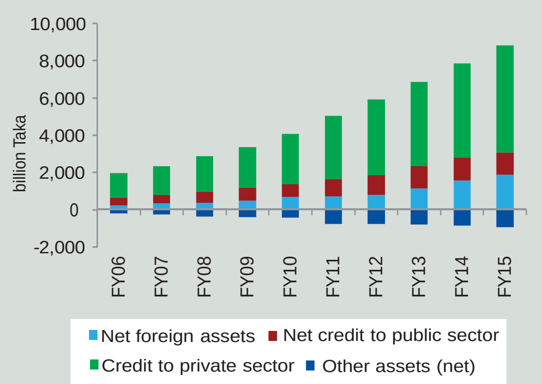


Chart 1.4 Sources of broad money (M2)



Money and Credit Developments

1.16 In FY15, Bangladesh Bank pursued a cautious but growth supportive monetary policy. The policy stance for FY15 was designed in line with the target of 7.3 percent real GDP growth in a scenario of 6.5 percent annual average CPI inflation. To keep the inflation at target level, BB continued to pursue a restrained policy stance in both H1 and H2 of FY15 and policy rates namely repo and reverse repo rates were kept unchanged at 7.25 and 5.25 percent respectively.

1.17 Broad money (M2) recorded lower growth of 12.4 percent in FY15 against the target growth of 16.5 percent and 16.1 percent actual growth in FY14. The lower growth in broad money was attributed mainly to the lower growth in domestic credit. The growth of domestic credit from the banking system declined to 10.1 percent against the target growth of 17.4 percent for FY15 and the actual 11.6 percent growth in FY14. The lower growth in domestic credit resulted from the lower investment demand for several reasons. The credit to public sector recorded a negative growth of 2.5 percent in FY15, which was much low compared with the target growth of 25.3 percent for FY15 and 8.8 percent actual growth in FY14. The growth rate of the credit to private sector increased moderately from 12.3 percent in FY14 to 13.2 percent in FY15 against the target growth of 15.5 percent. Accordingly, the growth rate of net domestic assets (NDA) declined to 10.0 percent in FY15 against the target growth of 20.2 percent and actual growth of 11.0 percent in FY14. The net foreign assets (NFA) of the banking system grew by 20.7 percent in FY15 which remained high against the target growth of 3.6 percent but low compared with 38.6 percent actual growth in the preceding fiscal year. The lower growth of NFA in FY15 compared to FY14 was due to weak export growth compared to high import growth. Reserve Money (RM) grew at a rate of 14.3 percent in FY15 which was lower than the projected growth rate of 15.8 percent and actual growth of 15.4 percent in FY14.

Chart 1.5 Revenue receipt, revenue expenditure, revenue surplus and budget deficit

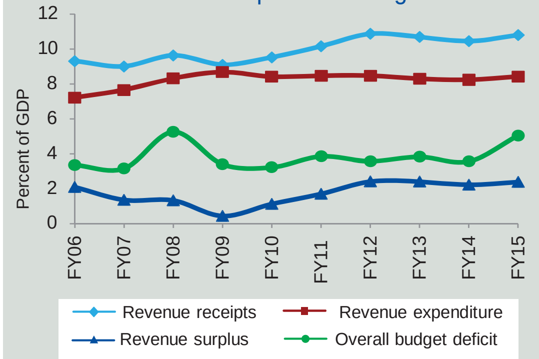
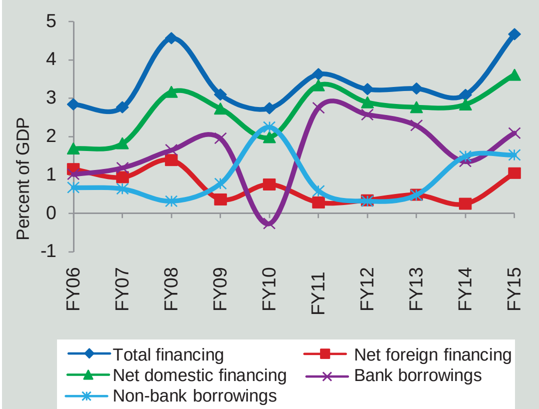


Chart 1.6 Budget deficit financing



1.18 The income velocity of money decreased slightly to 1.92 in FY15 from 1.93 in FY14, indicating increased financial deepening in the economy.

1.19 The weighted average interest rate on bank advances and deposits declined to 11.7 percent and 6.8 percent respectively at the end of FY15 from 13.1 percent and 7.8 percent respectively at the end of FY14. The spread between them also narrowed slightly to 4.9 percent from 5.3 percent over the same period as lending rates declined more than deposit rates. Lending rates declined due to sluggish domestic credit demand and part of which was met by overseas loans.

Public Finance

1.20 The Government has undertaken a range of regulatory and structural fiscal measures to strengthen revenue collection and widen fiscal space through public expenditure control.

1.21 The overall budget deficit (excluding grants) to GDP ratio increased from 3.6 percent in FY14 to 5.0 percent in FY15. However, domestic financing of the budget deficit increased to 3.6 percent of GDP in FY15 from 2.8 percent of GDP in FY14.

1.22 The growth of total revenue increased from 9.6 percent in FY14 to 16.4 percent in FY15. Consequently, revenue-GDP ratio increased from 10.5 percent to 10.8 percent over the same period.

1.23 Public expenditure as a percentage of GDP increased from 14.0 percent in FY14 to 15.8 percent in FY15. It grew by 27.3 percent in FY15 compared to 8.2 percent in FY14. Current expenditure in FY15 accounted for 8.4 percent of GDP which was 8.2 percent in FY14.

External Sector

1.24 The export earnings (including EPZ) continued to increase; from USD 29777 million in FY14 to USD 30768 million in FY15. During the same time total import payments increased from USD 36571 million to USD 40685 million. Trade deficit increased to USD 9917 million in FY15 from USD 6794 million in FY14. The services and income account including primary income and secondary income registered a surplus of USD 8271 million. Current account balance registered a deficit of USD 1645 million in FY15, which

Chart 1.7 Export and import growth

Chart 1.8 NEER, REER & Exchange rate

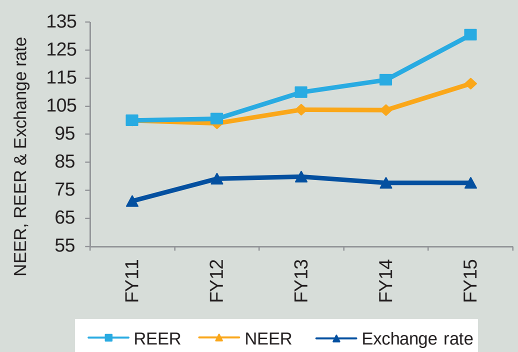
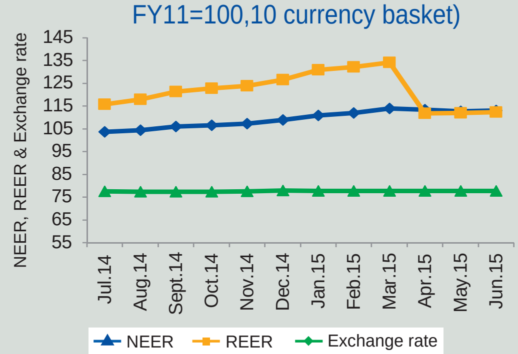


Chart 1.9 Recent movements in NEER, REER & Taka-Dollar exchange rate (base : FY11=100,10 currency basket)



was a surplus of USD 1406 million in FY14. The capital and financial account continued to register surplus and rose to USD 5791 million in FY15 from USD 3453 million in FY14. The overall balance of payments registered a surplus of USD 4373 million in FY15, which was USD 5483 million in FY14. Gross international foreign exchange reserves stood at USD 25021 million at the end of FY15 representing 7.4 months of import cover.

1.25 The growth of export earnings was lower from 12.1 percent in FY14 to 3.3 percent in FY15. Total export earnings as a percentage of GDP also decreased from 17.2 to 15.8 percent over the same period. While tobacco, chemical products, plastic products, jute goods, knitwear, woven garments, home textile, footwear and engineering products experienced a positive growth; some of the export items like fish, shrimps, vegetables, cut flower, fruits, petroleum by-products, leather, cotton & cotton products, raw jute, and specialised textiles experienced a negative growth.

1.26 Import payments as a percentage of GDP decreased from 21.2 percent in FY14 to 20.9 percent in FY15. Imports grew at a rate of 11.3 percent in FY15 compared with 8.9 percent growth in FY14. Total import bills for all items except milk & cream, oil seeds, edible oil, sugar, pharmaceutical products and raw cotton increased in FY15 compared to FY14.

1.27 The workers' remittance inflows experienced a moderate growth of 7.5 percent in FY15 compared to 1.5 percent negative growth in FY14.

1.28 Active foreign exchange intervention by BB continued in FY15 to keep the nominal Taka/USD exchange rate stable. As a result, the exchange rate of Taka against USD remained almost stable throughout the whole FY15. The nominal exchange rate of USD depreciated by 0.22 percent in FY15. It stood at Taka 77.80 as of end June 2015 compared with Taka 77.63 as of end June 2014. The nominal effective exchange rate (NEER) of Taka, calculated against a trade weighted 10 currency basket (base: FY11=100), appreciated by 9.16 percent in FY15. The real effective exchange rate (REER) of Taka also appreciated by 14.03 percent in FY15.

1.29 Outstanding external debt of Bangladesh decreased to USD 23488.6 million as of end of FY15 from USD 24387.9 million as of end of FY14. However, the outstanding debt-GDP ratio declined to 12.05 from 14.11 over the same period.

Near and Medium Term Outlook for Bangladesh Economy

1.30 GDP growth in Bangladesh will continue to grow at a stable rate, averaging annually 7 percent in the near to medium term. Moderate recovery in the euro area and USA will have positive effect on growth provided that domestic private investment picked up. The increase in the public consumption from the implementation of new pay scale, large infrastructure spending on power, road communication, transportation and establishment of Special Economic Zones (SEZ) will bring about a momentum of the GDP growth in the near to medium term.

CPI inflation will remain low in the short term. Moreover, low inflation is supported by supply factors and the declining import prices. Over the medium term the impact of these factors on inflation will gradually fade away, yet inflation is expected to remain below the Government projection (around 6 percent) made in the 7th Five Year Plan.

BB's monetary policy stance will support the momentum of inclusive, equitable and environmentally sustainable growth, further consolidating inflation moderation and macroeconomic stability. Banks and financial institutions are drawing on low cost refinance windows of BB against their financing of Micro Small and Medium Enterprise (MSME) output initiatives and environmentally benign green projects. Bangladesh Bank's supervisory oversight on credit disbursement and loan recovery disciplines in banks and financial institutions will intensify; with particular emphasis on risk management, internal audit and internal controls, accountability and transparency. The FY16 monetary programs projects 16.5 percent domestic credit growth against preceding year's 10.4 percent actual; to accommodate 7.0 percent real GDP growth with 6.2 percent inflation. The domestic demand growth is expected to pick up steadily in the near and medium term as a result of improvements in business environments. Moreover rapid growth in gross fixed capital formation in the public sector will continue to have a positive impact on growth of corporate capital expenditure. Investment will also be fuelled by the expected continuation of good financial standing of enterprises, allowing them to finance investment with their own funds.

BB remains active in support of a market-based exchange rate regime while seeking to avoid high exchange rate volatility. Low cost financial support from Export Development Fund (EDF) and other funds will be provided to the exporters to expand productive capacity in textiles, apparels and leather sectors in order to accelerate exports. Besides, recent sustained pick up in investment and consumption imports will ease appreciation pressures on Taka in the near future, enhancing its export competitiveness. The ongoing Government's efforts to boost overseas employment in Middle and Eastern Asian countries will accelerate inflow of remittances. BB expects 14 percent growth in imports, 7.5 percent growth in exports and 10 percent growth in remittances in FY16. The foreign reserves are projected to keep rising to reach USD 26 billion in FY16 from USD 25 billion in FY15. However, Bangladesh's aspiration to become an upper middle income country by 2030 might be realistic if its economy is going ahead overcoming difficulties supply side disruptions due to political and non-political factors, financial scams, and cumbersome overseas employment process, etc.