Part A: Economic and Financial Developments

Overview and Executive Summary

The Bangladesh economy started returning to normality in the third quarter of FY14 after facing prolonged pre-election political unrest during the previous two quarters. However various proxy indicator points to a moderate expansion of economic activity during this quarter with investors operating in a "wait and see" mode.

CPI inflation (point-to-point) increased to 7.48 percent in March 2014 from 7.44 percent in February 2014 mainly due to a rise in rice prices. Food inflation rose to 8.96 percent in March 2014 up from 8.84 percent in February 2014. On the other hand, non-food inflation declined from 5.53 percent in January 2014 to 5.26 percent in March 2014. After bottoming out at 6.06 percent in January 2013, average CPI inflation was on the rise and peaked at 7.60 percent in January 2014, and fell slightly to 7.55 percent in March 2014 due mainly to decrease in point-to-point non-food inflation.

Broad money (M2) growth slowed to 15.3 percent (y-o-y) in March 2014 from 18.1 percent in March 2013, and remained lower than the programmed growth of 17.5 percent for the period. Reserve money growth was 12.5 percent in March 2014. Private sector credit growth at end March 2014 was 11.5 percent which was lower than the 12.7 percent growth of March 2013 and the programmed growth of 16.0 percent.

Turning to fiscal issues, preliminary estimates show that total revenue increased by 4.4 percent, whereas total expenditure grew by 13.1 percent during Q3FY14 compared to that in Q3FY13. During the first three quarters (July-March) of FY14, revenue collection was 60.0 percent, while expenditure reached only 55.4 percent of the full year budget outlay respectively. Accordingly, the overall budget deficit for the first three quarters of FY14 amounted to 41.4 percent of the annual budgeted deficit or 1.9 percent of GDP which was very similar to the deficit of 1.7 percent of GDP in the first three quarters in FY13. Domestic financing and disbursement of net foreign financing grew faster during Q3FY14 compared to Q3FY13.

The current account balance moved into a small deficit, of USD 178 million, in Q3FY14 after posting positive figures for the previous two quarters. However the overall external balance was in surplus of USD 1.41 billion in Q3FY14 as a result of surplus in capital and financial accounts. Foreign exchange reserves continued its growth, reaching 19.29 billion at the end of Q3FY14 compared with USD 13.97 billion in Q3FY13.

After showing noticeable improvements during Q2FY14, banking sector indicators for Q3FY14 have again raised some concerns for a variety of reasons. The ratio of gross non-performing loans (NPL) to total outstanding loans increased from 8.9 percent at the end of Q2FY14 to 10.5 *percent at the end of Q3FY14. This is partly the 'return to trend' arising from the relaxation of loan rescheduling and classification policy in December 2013 which was formulated in order to cushion banks and their customers from the impact of the nationwide strikes over the second half of 2013. The ratio of net NPL of the sector has also increased from 2.0 percent at the end of December 2013 to 3.4 percent at the end of March 2014 partly due to the increase of gross NPL as well as increased shortfall in actual provision maintained by the sector. Interest rate spreads rose during Q3FY14.*

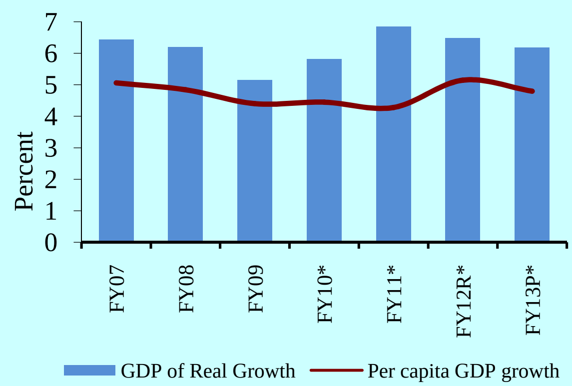
The rising trend of DSE indices and market capitalization continued during Q3 of FY14. At the end of Q3FY14, DSE broad index and DSE 30 index were at 4492.0 and 1603.5 which are respectively 5.3 percent and 9.4 percent higher than Q2 of FY14. Over the same quarter, market capitalization increased by 8.5 percent. The DSEX index and DSE 30 index have increased by 25.1 percent and 19.7 percent respectively compared to Q3FY13 level.

I Developments in the Real Economy

1.1 The Bangladesh economy started returning to normality in the third quarter of FY14 after facing prolonged pre-election political unrest during the previous two quarters. However the slow growth of some indicators, such as private sector credit (13.0%), export (6.4%), remittances inflow (0.01%) and negative growth of ADP utilization (-4.1%) point to a moderate expansion of economic activity.

1.2 The *aman* rice crop production, harvested in the second quarter, was 13.03 million metric tons (mmt), which was slightly lower (1.88%) than the annual production target of 13.28 mmt for FY14. *Boro* rice production, the major crop of Bangladesh which was planted in the third quarter, is expected to meet its annual production target of 18.92 mmts. Moreover, due to the benign weather conditions and increased acreage, production of wheat (13.75 mmt), potato (95.00 mmt) and onion (17.01 mmt) exceeded their respective production target of 12.81 mmt, 86.5 mmt and 14.88 mmt respectively for FY14 (Chart I.2). Similarly, production of other crops (e.g., pulse and vegetables) was on track in this quarter.

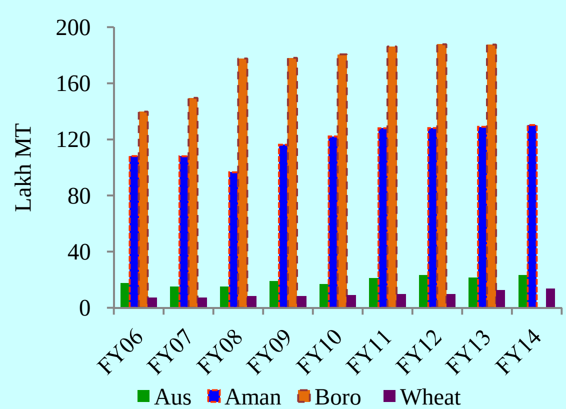
Chart I.1: Growth of Real GDP



P=Provisional estimates of BBS

* denotes GDP calculated based on 2005-06

Chart I.2: Production of Major Crops



* Figures of Boro in FY14 represent target set by DAE

1.3 Though data on industrial production is yet to be made available for Q3FY14, it is reasonable to expect that industrial production will show an uptick in this period with the resumption of normal economic activity. Moreover, positive growth of credit to the construction sector (9.5%) in Q3FY14, which was (-) 6.2% and (+) 8.9% in Q1FY14 and Q2FY14 respectively, also indicates a satisfactory growth of this sector. However, in Q2FY14, the production of large and medium scale manufacturing industries experienced somewhat moderate growth of 6.59% compared to the same quarter of previous fiscal year (Chart-1.3). Among various industry categories under medium and large scale manufacturing industries, apparel, pharmaceuticals, basic metals and food products registered positive growth of 9.58%, 10.84%, 17.19% and 5.25% respectively, while production of textile, paper and paper product, and chemical and chemical product registered negative growth of (-)1.76%, (-)12.01% and (-)7.16% respectively.

Chart 1.3: Quantum Index of Medium and Large-scale Manufacturing Industries, Mining and Electricity

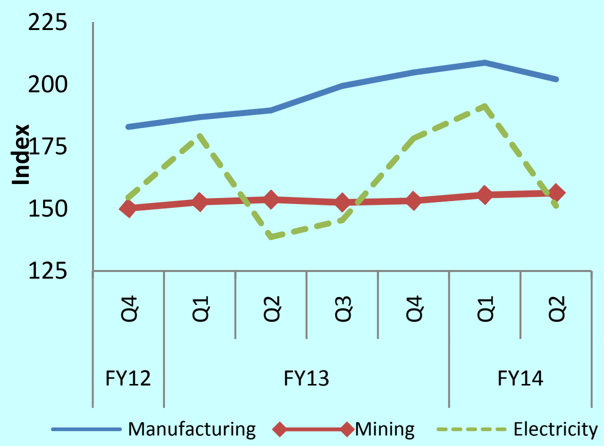
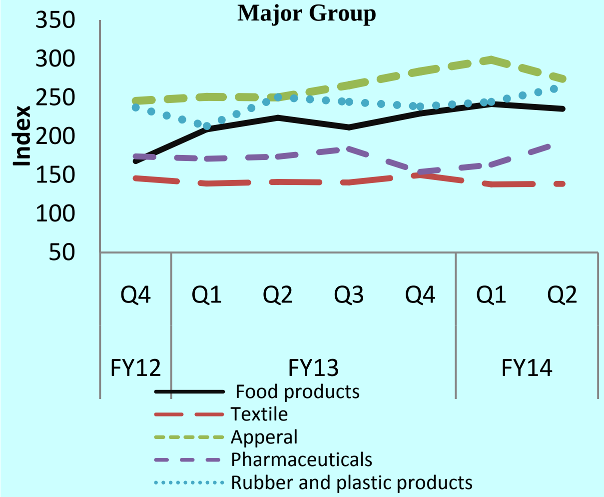


Chart 1.4: Quantum Index Manufacturing Industry by Major Group

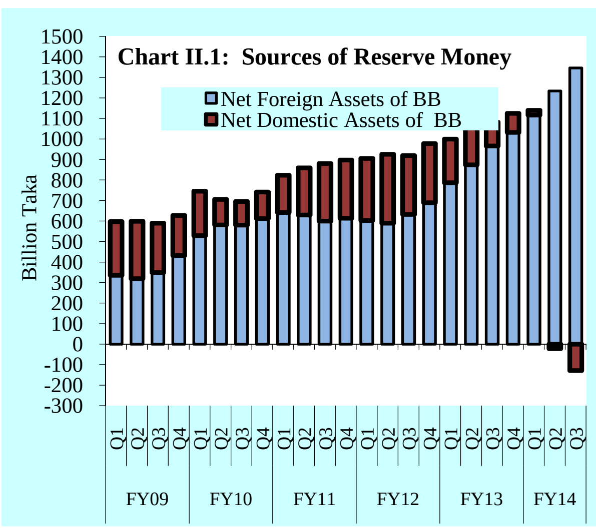


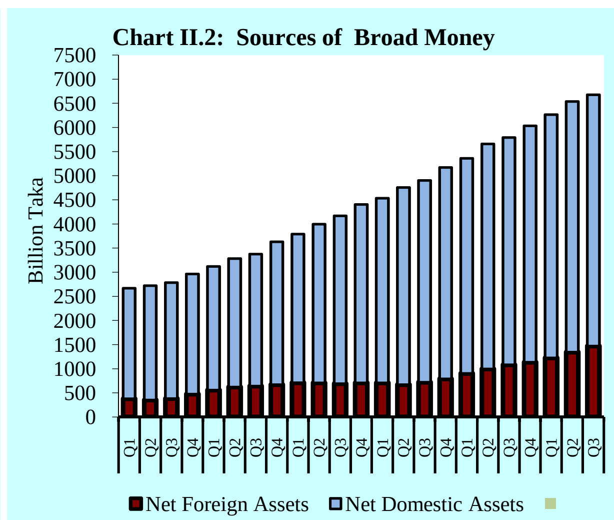
1.4 A number of proxy indicators (such as trade financing, bank advances to transport and communication sector, and the amount of cargo handled, etc.) reflect the recovery of service sector activities in the country during the third quarter of FY14. A healthy growth of Bank advances (outstanding) to trade and commerce sector (17.35 percent) signals that activities in this sector got some momentum in Q3FY14 (table 1.9 in appendix). Similarly, a pick up credit to the transportation sector (one of the sectors considered most adversely affected during the political unrest) indicates that this sector may also grow faster pace in Q3FY14 than the last two quarters. In this quarter, the amount of cargo handled by Chittagong port increased to 12.30 mmt from 9.85 mmt in Q2FY14, showing a strong rise of 25.84%. At the same time, hotel and restaurant business in the three cities (e.g. Dhaka, Chittagong and Sylhet) was benefited by the hosting of two T-20 cricket world cups (men and women) in the country in March 2014.

II. Money and Credit Market Development

2.1 Broad money (M2) growth slowed to 15.3 percent (y-o-y) in March 2014 from 18.1 percent in March 2013, and remained lower than the programmed growth of 17.5 percent for the period. The lower M2 growth resulted from slower growth in net foreign assets (36.2 percent compared with 49.9 percent in March 2013). However, net domestic assets increased slightly to 12.5 percent in March 2014 compared with 10.6 percent growth in March 2013 driven by a growth of 16.4 percent (compared to the growth of 8.2 percent a year earlier) in net credit to the government, due mainly to substantial increase of net sale of NSD certificates. Private sector credit growth at end March 2014 was 11.5 percent which was lower than 12.7 percent growth of March 2013 and the programmed growth of 16.0 percent.

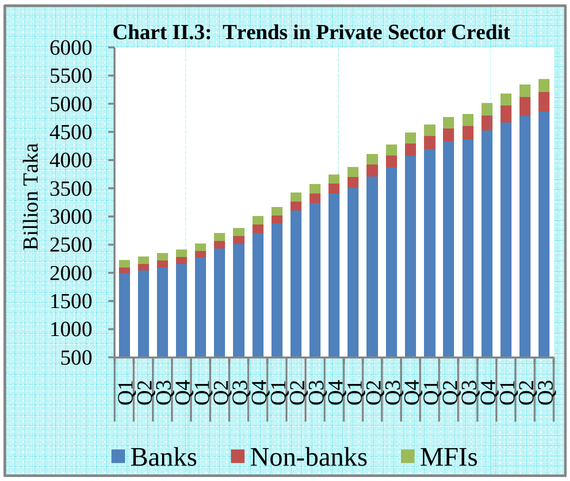
2.2 Reserve money growth slowed to 12.5 percent (y-o-y) in March 2014 from 17.7 percent in March 2013 due to sharp decline in growth of net domestic assets of BB by 211.7 percent compared with 59.9 percent decline in March 2013. The decline in NDA of BB was attributable to the large decline in lending to the public sector. The growth of NFA (39.4 percent) in March 2014 was mainly due to purchase of USD 1427 million by Bangladesh Bank during January-March 2014 to avoid a significant loss of external competitiveness

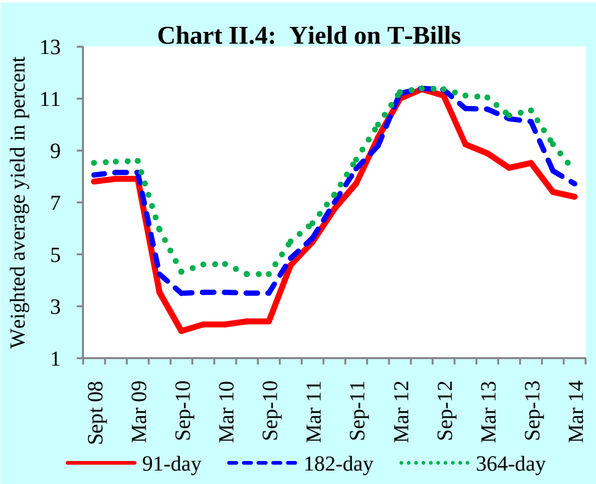


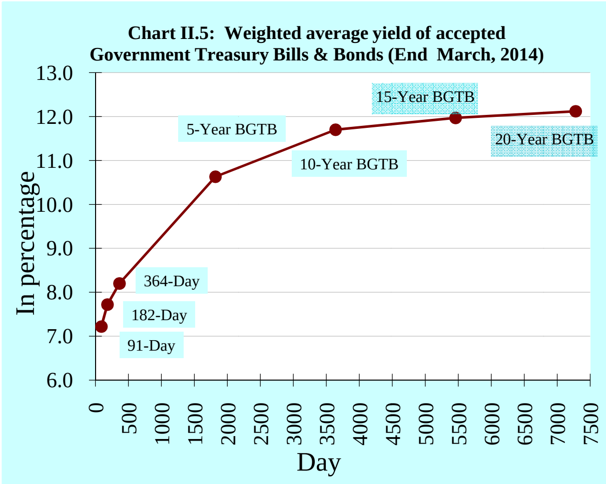


2.3 A look at the components of M2 shows that growth of currency slowed to 10.3 percent during Q3FY14 from 14.1 percent in Q3FY13. The growth in time deposit also slowed to 15.9 percent (y-o-y) during Q3FY14 compared with the growth of 20.1 percent in Q3FY13 but the growth in demand deposits increased to 16.0 percent (y-o-y) during Q3FY14 compared with the growth of 7.5 percent during Q3FY13. Slower growth of aggregate deposits could partly be due to an increase in demand for National Savings Certificates (NSC) as the yield differential between banks fixed deposits and NSC instruments widened over the past few months.

2.4 In Q3FY14, a slightly broader definition of private sector credit which includes micro-finance institutions (in addition to banks and non-banks) grew by 13.0 percent compared with 13.4 percent in Q3FY13. Bank advances to the transport and communication sector had negative growth of 7.0 percent in Q3FY14. Credit to industry increased by 7.1 percent of which working capital financing (excluding import & export financing) increased by 49.6 percent in Q3 FY14. Credit to the construction, and trade & consumer sectors were 9.5, and 17.3 percent respectively in Q3FY14. In the agriculture sector the supply of credit increased by 15.9 percent at end of Q3FY14 (of which crops increased by 14.9 percent and others by 27.0 percent). The highest share of bank advances went to the trade & commerce sector (39.0 percent) followed by industry (34.4 percent) and construction (9.5 percent) (Table I.9).







2.5 The BB repo and reverse repo rates remain unchanged at 7.25 and 5.25 percent respectively in March, 2014. The weighted average call money rate which was relatively volatile at the beginning of FY12 continued to hover around the middle of the policy interest rate corridor (Chart II.6). The call money rate came down to 7.16 percent at the end of March, 2014 which was 7.50 percent at the end of March, 2013 reflecting adequate liquidity in the money market. Government security rates also fell, including long term bond yields. The rate of 30-day Bangladesh Bank bills decreased to 6.92 percent in March 2014 from 7.62 percent in March 2013. Overall yields on short term treasury bills e.g., 91-day decreased to 7.22 percent in March, 2014 from 8.90 percent in March, 2013 and 182-day, 364-day treasury bills rates fell to 7.72 and 8.20 percent respectively at end of March, 2014 from 10.60 and 11.05 percent respectively at the end of March, 2013. Yields on long-term bonds such as 5-year, 10-year, 15-year, 20-year BGTB also decreased to 10.63 and 11.70, 11.97 and 12.12 percent at the end of March, 2014 from 11.82, 12.10, 12.38 and 12.48 percent respectively in March, 2013 (Table II.3). The spread between lending and deposit rates increased from 5.06 percent at end of Q3FY13 to 5.15 percent at the end of Q3FY14.

Chart II. 6: Policy Rates & Call Money Rate

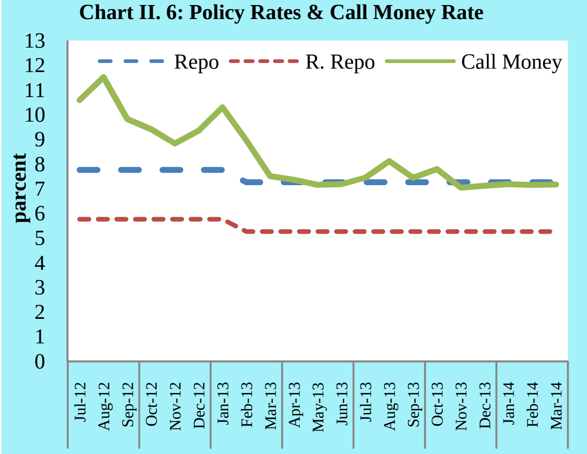
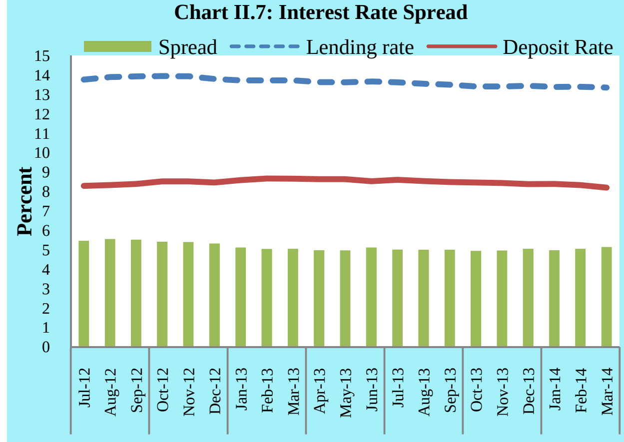


Chart II.7: Interest Rate Spread



III. Fiscal Developments

3.1 Preliminary estimates show that total revenue increased by 4.4 percent, whereas total expenditure grew by 13.1 percent during Q3FY14 compared to that in Q3 FY13. During the first three quarters (July-March) of FY14, revenue collection was 60.0 percent, while expenditure reached only 55.4 percent of the full year budgeted outlay respectively. Accordingly, the overall budget deficit for the first three quarters of FY14 amounted to 41.4 percent of the annual budgeted deficit or 1.9 percent of GDP which was very similar to the deficit of 1.7 percent of GDP in the first three quarters in FY13. Domestic financing and disbursement of net foreign financing grew faster during Q3FY14 compared to Q3FY13. (Table III.1 and Chart III.2).

Chart III.1: Trend in Government Revenue and Expenditure

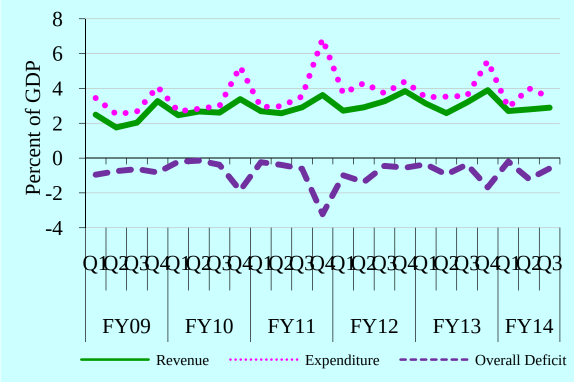
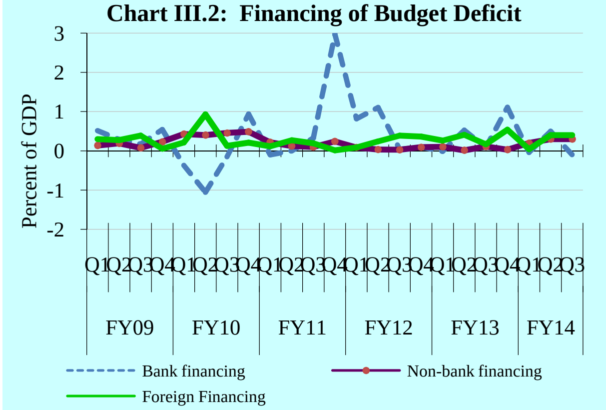


Chart III.2: Financing of Budget Deficit



3.2 Total NBR revenue increased by 2.0 percent to Tk. 288.4 billion (21.2 percent of the annual target of FY14) in Q3FY14 from Q3FY13. Revenue collection from value added tax (VAT), and other sources increased by 4.7 percent and 5.3 percent respectively during the quarter under review. Revenue from custom duties and income tax , on the other hand, decreased by 3.1 percent and 0.9 percent respectively during Q3FY14 due to lower import payment compared to Q3FY13. The overall NBR revenue collection during the first three quarters of FY14 reached Tk. 1004.5 billion (58.2 percent of the target of FY14), which is 8.5 percent higher than the level of the first three quarters of FY13.

3.3 During Q3 FY14, a preliminary estimate of total expenditure was Tk. 419.4 billion (18.9 percent of annual target) , which was 13.1 percent higher, in nominal terms, than that of Q3 FY13. The current expenditure grew by 42.4 percent to Tk. 232.1 billion in Q3 FY14. The ADP expenditure, on the other hand, declined by 4.1 percent to Tk. 103.4 billion (15.7 percent of annual ADP) compared to Q3FY13.

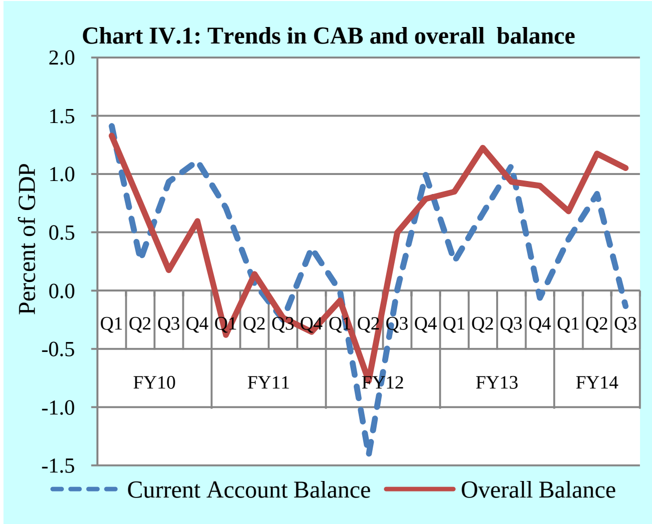
3.4 During the first three quarters of FY14, total government expenditure is estimated at Tk. 1232.5 billion (55.4 percent of FY14 target or 10.4 percent of GDP), which is 12 percent higher in nominal terms than the level of the first three quarters of FY13. During this period, current expenditure rose to Tk. 713.6 billion (65.4 percent of FY14 budgeted amount or 6.0 percent of GDP), which is 19.6 percent higher in nominal terms relative to the first three quarters of FY13. The Annual Development Program (ADP) outlay reached Tk.284.3 billion (43.2 percent of FY14 budget or 2.4 percent of GDP), which is 4.5 percent higher than it was in the same period of previous fiscal year but running behind the whole year target.

3.5 The overall fiscal deficit stood at Tk. 72.4 billion during Q3 FY14, representing 0.6 percent of GDP compared with Tk. 38.5 billion or 0.37 percent of GDP in Q3 FY13. Domestic financing of the deficit at Tk. 30.2 billion in Q3FY14 was much higher than Tk. 20.8 billion recorded in Q3FY13. Foreign financing of the deficit at Tk. 42.2 billion in Q3 FY14 was also higher than Tk17.8 billion disbursed in Q3FY13. Of the domestic financing sources, financing from the banking sector decreased to (-) Tk. 11.0 billion from Tk. 54.4 billion in Q2 FY14, and financing from the non-banking sector, on the other hand, increased to Tk. 41.1 billion from Tk. 31.9 billion in Q2 FY14.

3.6 The overall deficit financing during the first three quarters of FY14 amounted to Tk. 228.0 billion or 1.9 percent of GDP compared to Tk.175.2 billion or 1.7 percent of GDP, during the first three quarters of FY13. A look at the sources of financing, the deficit shows that Tk. 129.9 billion in the first three quarters (Tk. 85.6 billion in the same period of FY13), was accommodated from domestic sources that included bank financing of Tk. 38.6 billion and non-bank financing of Tk. 91.3 billion, while the remaining amount of Tk. 98.1 billion (Tk. 89.5 billion in the same period of FY13) came from foreign sources during the first three quarters of FY14. The growth in non banking sector domestic financing in the first three quarters of FY14, primarily through the sale of National Savings Certificate, is a key difference with the same period in FY13. The share of non-banking sector domestic financing in the total budget financing was 40.0 percent in the first three quarters of FY14 compared with 14.0 percent in the same period of FY13.

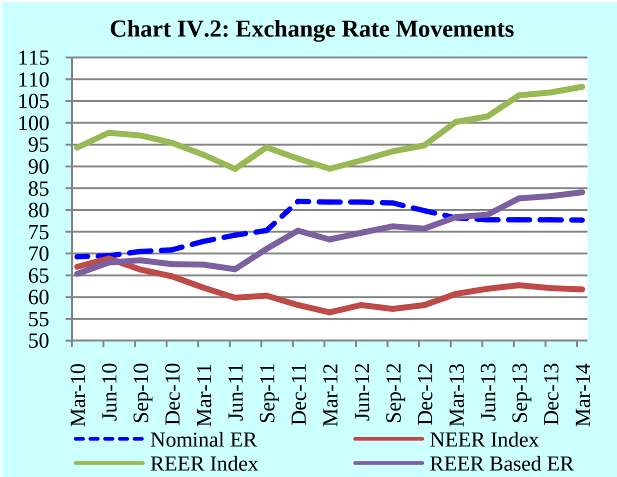
IV. External Sector Developments

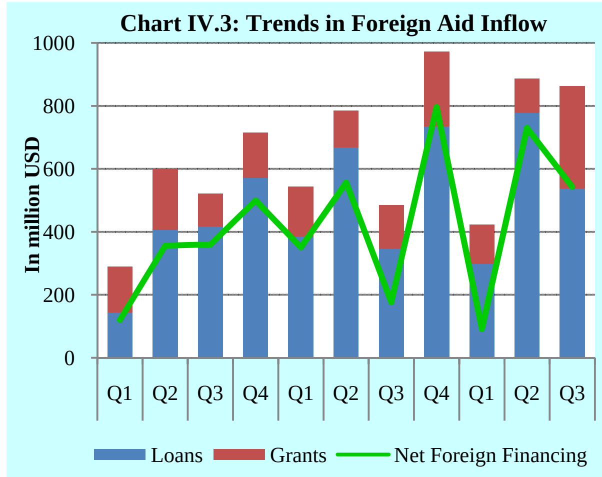
4.1 Current account balance moved into deficit, of USD 178 million, after posting positive figures for the last two quarters. Growth in import payments surpassed the growth in export earnings, and growth in remittances continued its negative trend. However the overall balance was in surplus of USD 1.41 billion in Q3FY14 as a result of surplus in capital and financial accounts. Foreign exchange reserve continued its growth, reaching 19.29 billion at the end of Q3FY14 compared with USD 13.97 billion in Q3FY13.



4.2 The combined capital & financial account increased from a surplus of USD 572 million in Q3FY13 to a surplus of USD 1441 million in Q3FY14. Surplus in the capital account more than doubled from USD 129 million in Q3FY13 to USD 274 million in Q3FY14. On the other hand, the financial account recorded a surplus of USD 1167 million in Q3FY14, which was significantly higher than the surplus of USD 443 million in Q3FY13 as net trade credit recorded a surplus in the current quarter from a deficit in the same quarter last year. (Table IV.1).

4.3 Total foreign aid in Q3FY14 was USD 862.1 million, compared to USD 484.3 million in Q3FY13. Out of total aid, USD 537.4 was disbursed as MLT loan, whereas USD 345.3 million was disbursed under the same heading in Q3FY13. Grants increased sharply from USD 139.0 million to USD 324.8 million during the same period. In Q3FY14, Bangladesh made an amortization payment of USD 377.2 million, of which USD 318.9 million was paid as principal. As a result, net foreign financing in Q3FY14 was USD 543.2 million, much higher than USD 176.6 million received in Q3FY13 (Table IV.8).



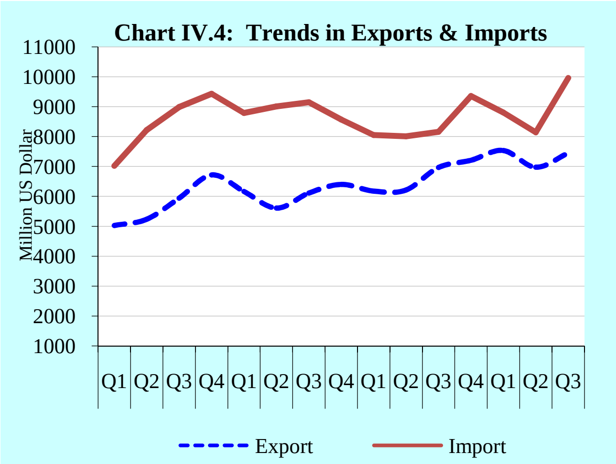


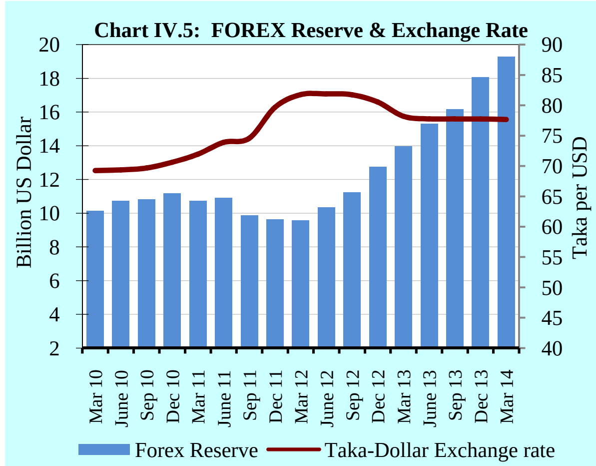
4.4 In the foreign exchange market, taka appreciated only marginally to Tk. 77.67 per USD during Q3FY14. Bangladesh Bank continued its intervention in the domestic foreign exchange market with a net purchase of foreign currencies amounting to USD 1.43 billion during Q3FY14. REER based exchange rate increased to Tk. 84.08 per USD at the end of March 2014 from Tk. 83.17 per USD at the end of December 2013.

4.5 According to the Export Promotion Bureau (EPB) data, export earnings increased by 6.9 percent to USD 7.5 billion in Q3FY14 from USD 7.0 billion in Q3FY13. RMG sector, which constitutes 81.0 percent of the export basket, spearheaded the growth. In Q3FY14, RMG exports grew by 6.8 percent as earnings from European countries grew at 13.1 percent while growth from the US market decreased by 7.8 percent. Export to "non-traditional destinations" showed an overall positive picture in Q3FY14. RMG related export increased in Turkey (+36.0 percent), and China (+86.0 percent). Non-RMG export to China (+105.0 percent), Turkey (+42.0 percent), Republic of Korea (+75 percent) increased. Among other major export items, earnings from leather and frozen shrimps and fish increased by 34.1% and 19.4% respectively. On the other hand, export earnings from raw jute and jute goods continued their downward trend, decreasing by -40.9% and -21.5% respectively over the corresponding quarter of the previous year (Table IV.2 and IV.5).

4.6 Import payments (using banking sector data) increased by 16.1 percent to USD 10.32 billion in Q3FY14 from USD 8.90 billion in Q3FY13 (Table IV.3). Import of food-grains increased sharply from USD 112.1 million in Q3FY13 to USD 420.5 million in Q3FY14. Import of rice was USD 130.2 million during Q3FY14, compared to USD 6.5 million in Q3FY13. Wheat import increased from USD 105.6 million in Q3FY13 to USD 290.3 million in Q3FY14. Import of other food items increased from USD 790.8 million during Q3FY13 to USD 842.3 million in Q3FY14. Among the other food items, the import of sugar (+22.6 percent), spices

(+27.2 percent), pulses (+12.9 percent), and milk & cream (+54.9) all increased, while edible oil (-8.3 percent) decreased (Table IV.3).





4.7 Imports of intermediate and consumer goods increased by 8.1 percent (y-o-y) to USD 4.86 billion during Q3FY14. Among the intermediate goods, imports of textile and articles thereof (+3.8 percent), pharmaceutical products (+2.8 percent), raw cotton (+21.1 percent), plastic and rubber articles thereof (+18.5 percent), crude petroleum (+0.4 percent), and yarn (+17.0 percent) increased, while imports of POL (-3.2 percent), and fertilizer (-9.2 percent) decreased. Imports of capital machinery recorded a growth of 21.0 percent in Q3FY14 over Q3FY13.

4.8 In Q3FY14, the opening of import LCs increased by 13.51 percent to USD 10.88 billion, of which consumer goods (+24.64 percent), intermediate goods (+22.22 percent), petroleum and petroleum products (+22.58 percent), industrial raw materials (+6.86 percent), machinery for miscellaneous industries (+29.76 percent) increased, while capital machinery (-7.35 percent), decreased (Table IV.9).

4.9 The overall inflow of workers' remittances was USD 3.72 billion in Q3FY14. Remittance from the Gulf region declined by 7.7 percent y-o-y as remittance from Saudi Arabia (-17.2 percent), UAE (-5.2 percent), Kuwait (-9.0 percent) all fell. On the other hand, remittances from Oman (+18.4 percent) and Bahrain (+31.6 percent) recorded positive growth. Remittance inflow from the Euro region (-2.5 percent) and the Asia Pacific region (+0.5 percent) exhibited small changes. Increase in the inflow of remittance from USA and other countries offset the fall in remittance earnings from the Gulf. Remittance inflow from the rest of the world, including the US, registered 27.0 percent growth. In absolute amounts, the major sources of remittance during the quarter was Saudi Arabia (USD 844.5 million), followed by UAE (USD 707.2 million), USA (USD 609.0 million), Malaysia (USD 276.5 million) and Kuwait (USD 275.5 million) (Table

IV.4). Overseas employment for Bangladeshi workers fell sharply by 11 percent in Q3FY14 as a total of 96,068 Bangladeshi emigrated compared with 107,626 in the corresponding period of FY13.

V. Price Developments

5.1 CPI inflation (point-to-point) increased to 7.48 percent in March 2014 from 7.44 percent in February 2014 mainly due to a rise in rice prices. Food inflation rose to 8.96 percent in March 2014 up from 8.84 percent in February 2014. According to Department of Agricultural Marketing (DAM), average retail rice price increased by 29 percent in the last month of Q2FY14 compared to same period previous year. This was at least in part due to higher distribution cost rising from transport blockades in December 2013. On the other hand, non-food inflation declined from 5.53 percent in January 2014 to 5.26 percent in March 2014.

Following the same trend as the national level, an upward trend of food inflation and a declining trend in non-food inflation were also observed in both the rural and urban areas during Q3FY14. As the charts below show urban inflation was higher than rural inflation. In March 2014, point to point inflation in urban areas was 7.98% (food was 9.98% and non-food 5.88%) while in rural areas point to point inflation was 7.21% (food was 8.53% and non-food 4.83%).

After bottoming out at 6.06 percent in January 2013, average CPI inflation was on the rise and peaked at 7.60 percent in January 2014, and fell slightly to 7.55 percent in March 2014 due mainly to the fall in point-to-point non-food inflation, which made up for the rise in food inflation during this period.

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Table 5.1: Contribution @ of Food and Major Non-Food Items / Groups in CPI inflation(Point to Point)
Base Year 2005-06: 100

Months	Food beverage & tobacco	Clothing & Footwear	Gross rent, Fuel & Lighting	Furniture, Furnishing & Other	Medical care and Health Expenses	Transport & Communications	Recreation, Entertain-ment, Education	Misc. Goods & Services	Non-food
Weight	56.18	6.84	14.88	4.73	3.47	5.8	4.28	3.82	**43.82**
Jun-12	**24.36**	15.59	27.95	9.67	2.59	10.06	3.56	6.23	**75.64**
Jul-12	**22.30**	14.70	32.18	9.60	2.87	8.26	4.05	6.05	**77.70**
Aug-12	**23.74**	13.58	29.57	10.29	3.79	7.44	4.98	6.59	**76.26**
Sep-12	**18.12**	14.90	31.76	11.32	3.44	6.68	6.03	7.74	**81.88**
Oct-12	**22.28**	13.97	29.06	10.59	2.97	6.67	6.31	8.16	**77.72**
Nov-12	**32.24**	12.19	24.62	9.73	2.68	5.91	5.78	6.84	**67.76**
Dec-12	**40.56**	11.46	18.96	9.09	2.44	5.64	5.60	6.25	**59.44**
Jan-13	**41.75**	12.43	15.29	7.54	2.72	6.84	6.83	6.60	**58.25**
Feb-13	**53.38**	10.22	11.63	6.14	1.82	5.49	5.92	5.41	**46.62**
Mar-13	**54.75**	10.05	11.75	5.65	1.61	5.31	5.67	5.20	**45.25**
Apr-13	**58.73**	9.39	10.41	5.31	1.52	5.01	4.79	4.84	**41.27**
May-13	**57.65**	9.58	10.76	5.39	1.59	5.39	4.73	4.91	**42.35**
Jun-13	**58.07**	9.55	10.71	5.28	1.48	5.44	4.62	4.85	**41.93**
Jul-13	**58.92**	10.57	8.69	5.26	1.38	5.62	4.54	5.01	**41.08**
Aug-13	**62.38**	7.93	9.95	4.98	0.95	4.86	4.67	4.27	**37.62**
Sep-13	**63.54**	8.01	8.45	5.00	0.86	5.40	4.18	4.55	**36.46**
Oct-13	**68.48**	7.16	8.14	3.83	1.13	4.20	3.60	3.46	**31.52**
Nov-13	**68.63**	7.43	8.29	3.64	1.21	4.29	3.40	3.11	**31.37**
Dec-13	**70.59**	6.94	8.06	3.25	1.22	3.96	3.07	2.90	**29.41**
Jan-14	**67.34**	8.48	12.20	3.41	1.49	3.02	1.45	2.62	**32.66**
Feb-14	**68.07**	8.29	11.96	3.21	1.46	3.07	1.40	2.54	**31.93**
Mar-14	**68.72**	7.90	11.80	2.93	1.46	3.11	1.60	2.48	**31.28**

$$\text{@Contribution of ith Group} = \left(\frac{\text{Inflation in ith group} * \text{Weight of ith group in CPI basket}}{\text{Headline inflation}}\right) \times 100$$

Table 5.1 reveals that until January 2013, the main contributor of point-to-point CPI inflation was non-food inflation. After that, the scenario reversed and food inflation became an increasingly dominant contributor of point-to-point CPI inflation.

Chart V.1: 12 - Month Point-to-point CPI inflation(Base:2005-06=100)

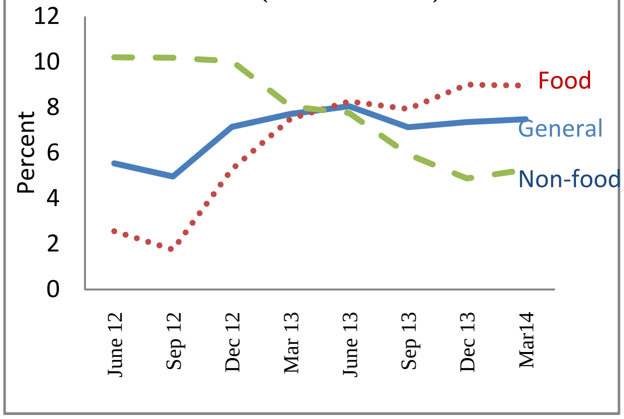


Chart V.2:12-Month Average CPI Inflation (Base:2005-06=100)

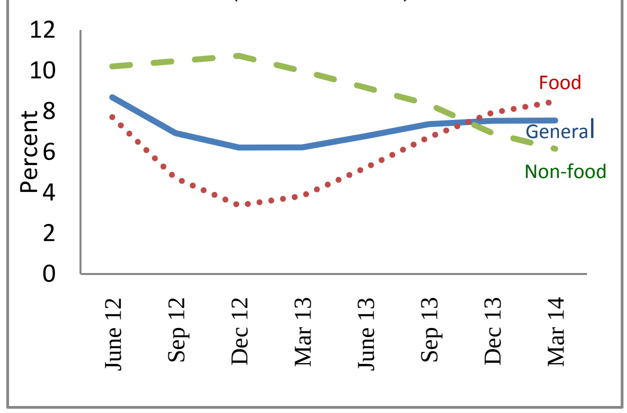


Chart V.3 : 12 Month Point-to-point CPI inflation for Rural (Base:2005-06=100)

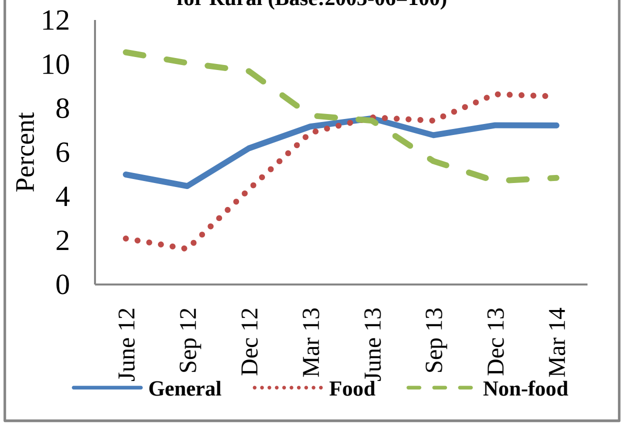


Chart V.4: 12 Month Average CPI inflation for Rural (Base:2005-06=100)

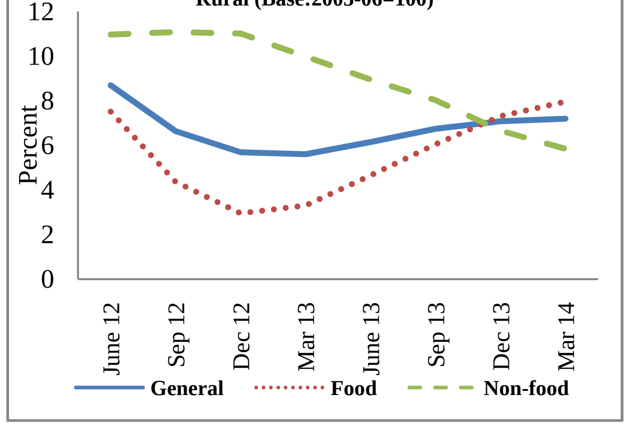


Chart V.5 : 12 Month Point-to-point CPI inflation for Urban (Base:2005-06=100)

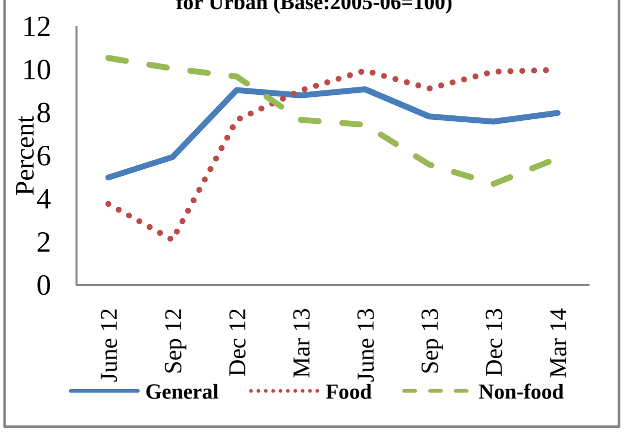
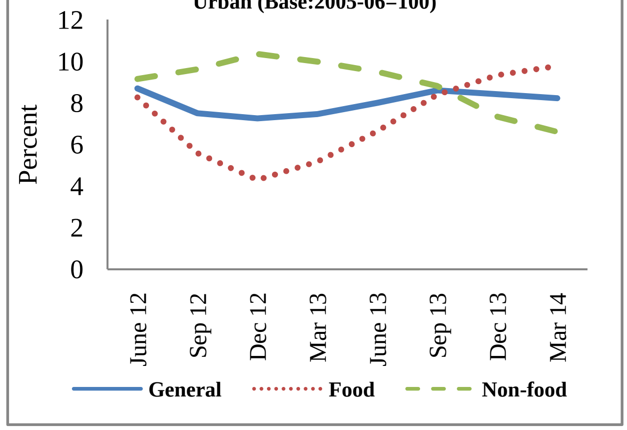


Chart V.6: 12 Month Average CPI inflation for Urban (Base:2005-06=100)



5.2 The point-to-point CPI inflation in our neighboring South Asian countries exhibits a mixed trend during the quarter under review. In India, after reaching a peak of 11.16 percent in November 2013, CPI inflation experienced a downward trend and after bottoming out at 8.03 percent in February 2014, it went back to 8.31 percent in March 2014. WPI inflation in India also experienced a similar trend and was 5.70 percent in March 2014. CPI inflation in Pakistan fell slightly to 8.5 percent in March 2014 as compared to 9.2 percent in December 2013. CPI inflation in Sri Lanka continued to decline since November 2013 and reached 4.2 percent in March 2014.

Chart V.7: Commodity Prices in International Market

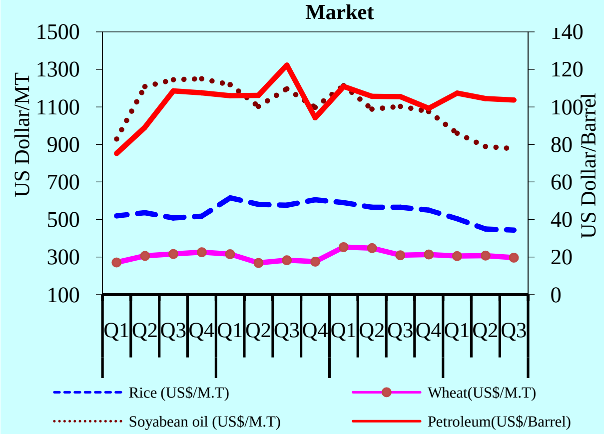
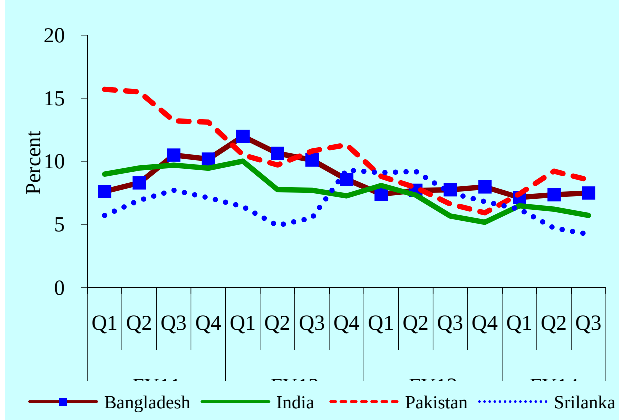


Chart V.8: Inflation in South Asia (Year on Year)



VI. Banking Sector Performance

6.1 After showing noticeable improvements during Q2FY14, banking sector indicators for Q3FY14 have again raised some concerns for a variety of reasons. The ratio of gross non-performing loans (NPL) to total outstanding loans increased from 8.9 percent at the end of Q2FY14 to 10.5 percent at the end of Q3FY14. The ratio of net NPL of the sector has also increased from 2.0 percent at the end of December 2013 to 3.4 percent at the end of March 2014 partly due to the increase of gross NPL as well as increased shortfall in actual provision maintained by the sector. During Q3FY14, the capital adequacy ratio (CAR) decreased slightly to 11.3 percent from 11.5 percent in Q2FY14. Among the profitability measures, return on asset (ROA) in the banking sector improved from 0.6 percent at the end of December 2012 to 0.9 percent at the end of December 2013 primarily due to increase in non-interest income of the sector (especially from investments in Government securities) and small provision deduction requirement for bad debt by the SCBs. Return on equity (ROE) of the banking industry also increased to 10.8 percent at the end of December 2013 from 8.20 percent at the end of December 2012. However interest rate spreads rose during Q3FY14.

6.2 During Q3FY14, the industry capital adequacy ratio (CAR) decreased slightly to 11.3 percent from 11.5 percent in Q2FY14 though still surpassing the minimum 10% regulatory requirement. Since Q1FY13, SCBs were gradually falling behind to fulfill the regulatory requirement of minimum capital before an injection of capital in Q2FY14 as the government fund allotted in the budget FY14 for their recapitalization in December 2013 (Chart VI.2). However CAR for SCBs has downfall again to 9.8 percent in Q3FY14 from 10.8 percent in Q2FY14. The ratio for PCBs decreased a little to 12.4 percent from 12.5 percent while for FCBs it increased to 22.4 percent from 20.3 percent during the period under consideration (Chart VI.1). During Q3FY14, CAR for specialized banks (SBs) deteriorated to (-) 12.4 percent from (-) 9.7 percent in Q2FY14.

Chart VI.1: Ratio of total eligible capital to risk weighted

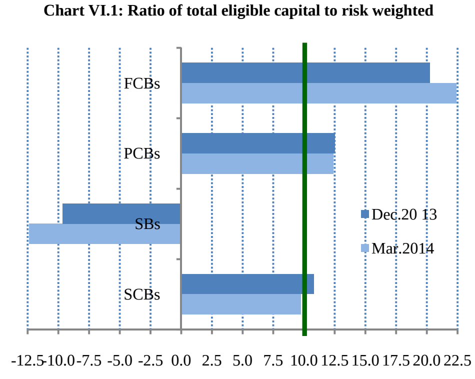
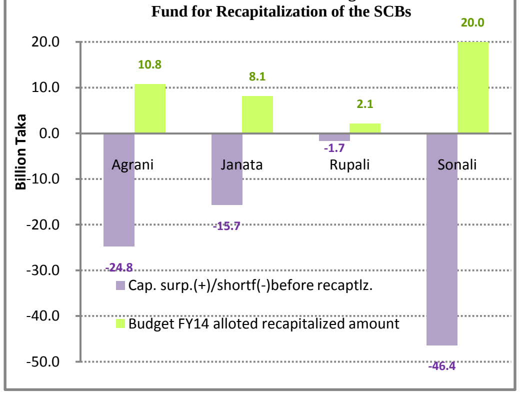
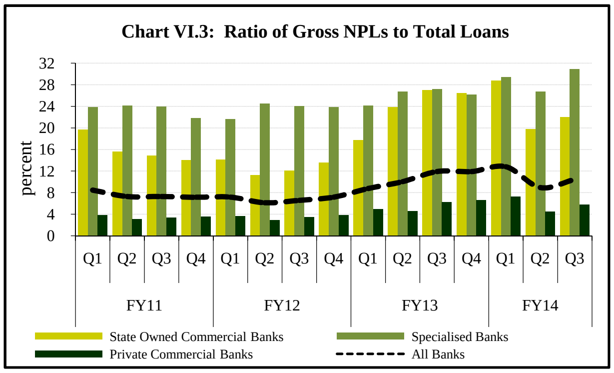
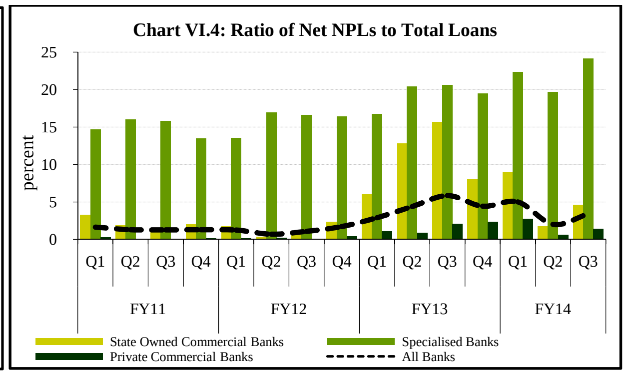


Chart VI.2: Disbursement from Budget FY14 Alloted Fund for Recapitalization of the SCBs



6.3 The ratio of gross NPL to total outstanding loans of the banking sector has gone up again at the end of Q3FY14 after recording a noticeable decrease during the previous quarter. Gross NPL ratio increased from 8.9 percent at the end of Q2FY14 to 10.5 percent at the end of Q3FY14 (Table VI.2 and Chart VI.3). There was an overall deterioration as the ratios for SCBs, SBs and PCBs increased to 22.0 percent, 30.9 percent and 5.8 percent respectively at end-March 2014 from 19.8 percent, 26.8 percent and 4.5 percent respectively at end-December 2013. However the ratio of FCBs has improved a little, decreased from 5.5 percent to 5.3 percent during the period.





Similarly, the net NPL ratio for all banks increased from 2.0 percent at the end of December 2013 to 3.4 percent at the end of March 2014 partly due to the increase of gross NPL as well as increased shortfall in actual provision maintained by the sector (Table VI.3, Chart VI.4 and Table 6.1). Provision shortfall of the sector as a whole increased sharply from Tk. 2.6 billion at the end of December 2013 to Tk. 24.3 billion at the end of March 2014. In Q3FY14 gross NPL ratio for SCBs and SBs increased by 2.2 percentage points and 4.2 percentage points respectively as these two groups of banks also had provision shortfall of Tk.0.3 billion and Tk.26.3 billion respectively. As a result, net NPL ratios for SCBs and SBs increased from 1.7 percent and 19.7 percent respectively at the end of December 2013 to 4.7 percent and 24.2 percent respectively at the end of March 2014. Net NPL ratio of PCBs has also increased from 0.6 percent to 1.5 percent during the period.

Table 6.1: Comparative Position of Classified Loan and Provision Maintained

(billion Taka)

Quarter	Items	SCBs	SBs	PCBs	FCBs	All Banks
Q1 FY14	Total classified loan	241.7	87.8	223.1	14.5	567.1
	Required provision	151.4	39.2	117.6	12.1	320.3
	Provision maintained	146.7	17.4	114.3	9.1	287.5
	Excess(+)/shortfall(-)	-4.7	-21.8	-3.3	-3.0	-32.8
Q2 FY14	Total classified loan	166.1	83.6	143.2	13.0	405.9
	Required provision	107.8	38.2	94.8	11.6	252.4
	Provision maintained	122.3	17.4	97.8	12.3	249.8
	Excess(+)/shortfall(-)	14.5	-20.8	3.0	0.7	-2.6
Q3 FY14	Total classified loan	186.9	97.3	185.3	12.3	481.7
	Required provision	120.6	44.0	107.3	11.1	283.0
	Provision maintained	120.3	17.7	109.1	11.6	258.7
	Excess(+)/shortfall(-)	-0.3	-26.3	1.8	0.5	-24.3

6.4 Return on assets (ROA) improved from 0.64 percent at the end of December 2012 to 0.90 percent at the end of December 2013. This was primarily due to an approximately 18.0 percent increase in non-interest income (especially from investments in Government securities) and small provision deduction requirement for bad debt by SCBs (Table 6.2) in 2013. SCBs required provision for bad debt for the year 2013 was only Tk. 5.9 billion, compared with Tk. 46.6 billion for 2012 in light of the loan rescheduling discussed above.

Table 6.2: Profitability Position of Banks

(In Billion Taka)

Bank Groups	Net Intt. Income	Total Non Interest Income	Operating Income	Non-Intt. Exp (Operating Exp.)	NIBPT	Bad Debt Prov.	Tax Prov.	NIAPT	Total Assets	Return on Assets (ROA)	Capital/ Equity (AdjustedTotal Capital)	Return on Equity (ROE)
1	2	3	4=2+3	5	6=4-5	7	8	9=6-7-8	10	11	12	13
Dec-13												
SCBs	-5.4	65.1	59.7	33.1	26.7	5.9	8.3	12.5	2108.5	0.6%	143.3	8.7%
SBs	3.8	5.9	9.6	8.0	1.6	2.3	0.9	-1.6	454.8	-0.4%	5.2	-35.0%
PCBs	118.2	124.2	242.5	114.4	128.1	34.0	46.9	47.2	4948.2	1.0%	440.9	10.7%
FCBs	15.7	24.6	40.3	10.6	29.7	3.9	11.3	14.5	488.7	3.0%	82.4	17.6%
All Banks	132.3	219.8	352.1	166.0	186.1	46.1	67.4	72.5	8000.2	0.9%	671.7	10.8%
Dec-12												
SCBs	14.9	56.2	71.1	28.6	42.6	46.3	6.5	-10.2	1831.9	-0.6%	86.0	-11.9%
SBs	4.7	4.3	9.0	6.7	2.2	0.7	1.3	0.2	385.4	0.1%	-20.5	-1.1%
PCBs	114.7	107.2	221.8	97.7	124.1	37.0	47.0	40.2	4371.5	0.9%	395.3	10.2%
FCBs	19.6	18.7	38.3	10.0	28.3	2.5	11.4	14.4	441.8	3.3%	83.6	17.3%
All Banks	153.8	186.4	340.2	142.9	197.3	86.4	66.2	44.7	7030.7	0.6%	544.3	8.2%

NIBPT= Net Income Before Provision & Tax /Operating Profit

NIAPT= Net Income After Provision & Tax

The ROA for SCBs and PCBs improved from (-) 0.6 percent and 0.9 percent at the end of December 2012 to 0.6 percent and 1.0 percent respectively at the end of December 2013. However, the ratio for FCBs and SBs declined from 3.3 percent and 0.01 percent to 3.0 percent and (-) 0.4 percent during the same period. Return on equity (ROE) of the banking industry increased to 10.8 percent at the end of December 2013 from 8.2 percent at the end of December 2012. The ROE for SCBs increased to 8.7 percent at the end December 2013 from (-) 11.9

percent at the end of December 2012 mainly due to the positive net income and small bad debt provision deduction for the year 2013. This ratio for PCBs and FCBs slightly improved from 10.2 percent and 17.3 percent to 10.7 percent and 17.6 percent respectively during this period (Table 6.2 and VI.4). However, ROE for SBs decreased from (-) 1.1 percent to (-) 35.0 percent during the same period[1].

Table 6.3: Deposit and Advance Position of Scheduled Banks (end of the month)

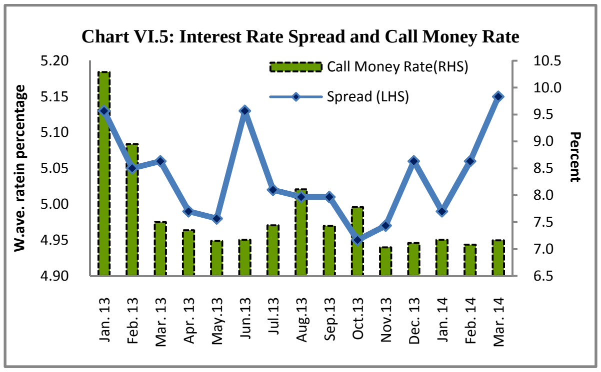
Bank groups	Year-on year growth of deposit (excluding interbank)		Year-on year growth of advances (excluding interbank)		Advance Deposit Ratio (ADR)	
	Mar.14	Dec. 13	Mar.14	Dec. 13	Mar.14	Dec. 13
SCBs	14.6%	18.4%	-4.0%	-4.6%	56.6%	55.6%
SBs	24.8%	31.8%	14.5%	14.9%	77.3%	77.5%
PCBs	16.3%	14.8%	12.9%	11.5%	75.6%	77.7%
FCBs	11.9%	9.9%	-0.1%	-0.6%	58.6%	64.5%
All	16.1%	16.3%	8.5%	7.4%	69.9%	71.2%

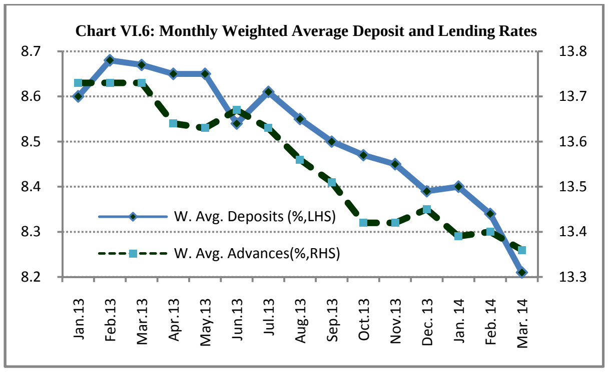
Table 6.4: Liquidity Position of the Scheduled Banks (Tk. in billion)

	As of end June, 2013[R]			As of end March, 2014[P]		
	Total Liquid asset	Required liquidity	Liquidity: excess(+) /shortfall(-)	Total Liquid asset	Required liquidity	Liquidity: excess(+) /shortfall(-)
SCBs	534.7	264.3	270.3	704.7	304.6	400.0
SBs	50.8	30.7	20.1	44.2	37.9	6.3
PCBs (other than Islamic)	795.2	475.4	319.8	911.4	526.6	384.7
Private Banks (Islamic)	218.4	113.0	105.4	233.1	128.6	104.5
FCBs	142.7	64.0	78.8	181.6	68.0	113.6
All	1741.7	947.3	794.4	2074.9	1065.8	1009.2

Here , required liquidity is the sum of CRR (6%) and SLR (13% for conventional banking and 5.5% for islamic banking)

6.5 At the end of Q3FY14, the growth rate (year-on- year) of deposits remained higher than that of advances. As a result, advance-deposit ratio (ADR) remained far below the maximum regulatory ceiling as well as its average value for the last eight years. The growth rate of deposit decreased marginally from 16.3 percent at the end-December 2013 to 16.1 percent at end-March 2014. On the other hand, the growth of advances has turned around from its declining trend up to Q2FY14 and it rose from 7.4 percent at the end of Q2FY14 to 8.5 percent at the end of Q3FY14. The advance - deposit ratio (ADR) decreased further to 69.9 percent at the end March 2014 from 71.2 percent at the end of previous quarter (Table 6.3). Accordingly, the liquidity position of all bank groups except SBs and Islamic Banks improved at the end of March 2014 compared to that in June 2013, leading to a further easing of money market conditions (Table 6.4).





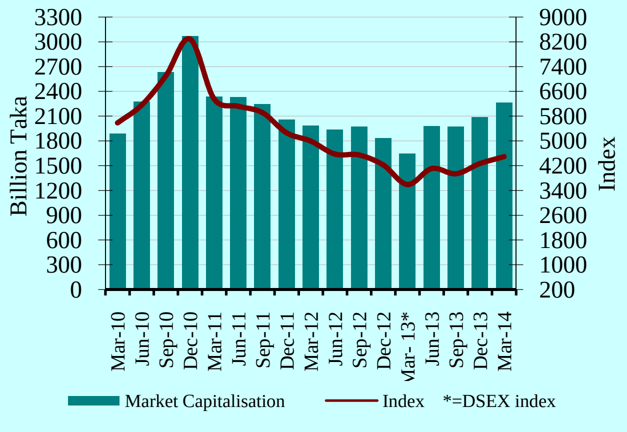
[1] It is simple arithmetic outcome of SBs' negative net income and adjusted capital during this period (Table 6.2). Total capital of SBs increased to Tk.5.2 billion in December, 2013 from (-) Tk.20.5 billion in December 2012 after adjustment while the bank group made net loss of Tk.1.6 billion compare to Tk. 0.2 billion net profit during the same period.

6.6 Monthly interest rate spread for all banks, measured as the difference between monthly weighted average rate of advances and deposit, came down to 4.99 percent in January 2014 from 5.06 percent in December 2013 but rose again to 5.15 percent by the end of Q3FY14 (Chart VI.5). In Q3FY14, due to low investment demand and easing money market conditions banks were forced to cut both deposit and lending rates. However, bank wise data show that most banks reduced their weighted average deposit rates more than their weighted average lending rates which caused a sharper decline in the overall weighted average deposit rate than that of in lending rate and the increase in spread during Q3FY14 (Chart VI.6). Monthly weighted average call money rate rose slightly from 7.11 percent in December 2013 to 7.16 percent in March 2014.

VII. Capital Market Development

7.1 The rising trend of DSE indices and market capitalization continued during Q3 of FY14. At the end of Q3FY14, DSE broad (DSEX[2]) index and DSE 30 index were at 4492.0 and 1603.5 which are respectively 5.3 percent and 9.4 percent higher than Q2FY14's indices. Over the same period, market capitalization increased by 8.5 percent (Chart VII.1 and Table VII.1). The DSEX index and DSE 30 index have increased significantly by 25.1 percent and 19.7 percent respectively as compared to Q3FY13 level. Over the previous 12 month period, the DSE Market capitalization increased by 37.5 percent i.e. between Q3FY14 and Q3FY13.

Chart VII.1: Trends in Market Capitalisation and DSE Index



7.2 The average price earnings ratio of the DSE reached 15.81 in March 2014 which was 90 basis point higher than 14.91 in December 2013. Total turnover value in the Dhaka Stock Exchange increased significantly by 20.3 percent from Tk. 255.9 billion in Q2FY14 to Tk.307.9 billion in Q3FY14. The liquidity situation in the capital market improved as measured by Turnover Velocity Ratio (TVR)[3], which increased to 54.4 percent in Q3FY14 from 48.1 percent in Q2 of FY14. The number of listed securities increased marginally to 311 in March'14 from 308 of December'13. The value of "issued equity and debt" increased by 1.0 percent (Table VII.1) and three new companies were listed in the capital market during Q3 FY14.

7.3 The sector-wise DSE data shows that during Q3FY14 market capitalization decreased in banks, engineering, textile industries, and corporate bonds sectors (Table VII.2). All together these sectors contributed 26.1 percent of the total market capitalization. Market capitalization of the other sectors like, fuel & power, food & allied product, pharmaceuticals & chemicals, cement industry, telecommunications, etc. however, increased during Q3FY14. The contribution of the banking sector decreased to 18.8 percent at the end of Q3FY14 from 20.3 percent in the previous quarter. The relative contributions of all other sectors in total market capitalization remained almost unchanged during the last two quarters.

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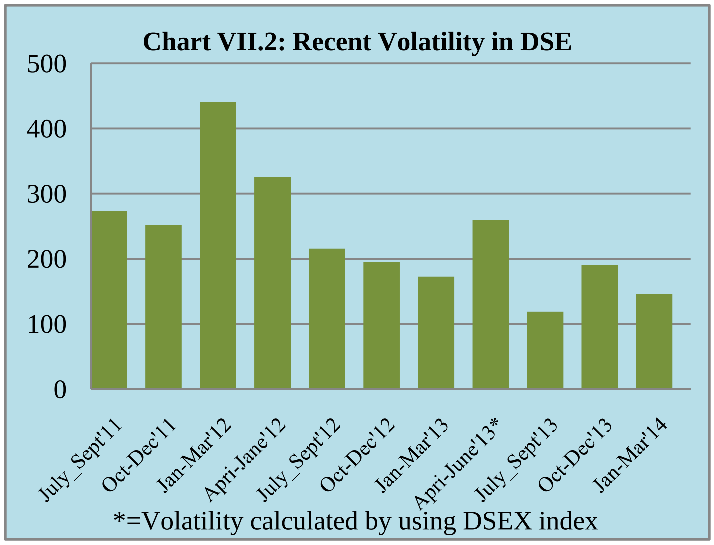
[2] DSE general index discontinued from 1st August 2013.

[3] TVR = (Turnover during the quarter/Quarter-end Market capitalization)*4



7.4 During Q3FY14 the new investment on share purchases by foreign and non-resident Bangladeshi investors increased to Tk. 9.4 billion from TK. 7.2 billion in the previous quarter. At the same time, total share sales by foreign and non-resident Bangladeshi investors also increased to Tk. 5.4 billion from TK. 1.5 billion in the previous quarter. As a result, net investment of foreign and non-resident Bangladeshi during Q3FY14 decreased to Tk. 4.0 billion from TK. 5.7 billion in the previous quarter. Foreign investment still has a limited, though growing, contribution in total turnover of DSE. During Q3 FY14 total turnover by foreign investors increased to 4.8 percent of total turnover from 3.4 percent in the previous quarter. The volatility in the DSEX index, measured by standard deviation, decreased to 146.1 during Q3FY14 compared to 190.3 in Q2FY14.

7.5 Cross country data shows that price earnings ratio of Bangladesh capital market is comparatively lower than some South and East Asian countries while dividend yield of Bangladesh is more than some South and East Asian countries (Table 7.1).

Table 7.1: Comparison among regional capital markets- March 2014

Country	Price Earnings ratio	Dividend Yield
Bangladesh	15.81	3.29
India	17.87	1.39
Sri Lanka	15.93	1.96
Thailand	12.00	3.30
Malaysia	17.00	3.0
Taiwan	17.00	2.80
Hong Kong	15.00	2.70
China	9.00	3.20
Singapore	13.00	3.40

Source: Monthly Review, Dhaka Stock Exchange

Part B: Boxes/Annexes

Chronology of Major Policy Announcements: January- March 2014

BRPD Circular No.01 01 January, 2014 Amendment of Guidelines on Risk Based Capital Adequacy (RBCA)	BB has made amendment in the Guidelines on Risk Based Capital Adequacy (RBCA) and developed a 'Credit Rating Methodology for Small and Medium Enterprises' which will ensure uniformity, larger levels of transparency of external credit assessment and thereby determine the relative creditworthiness of entities belonging to this segment and thus establish credit discipline in the banking industry. In this manner, BB has launched SME ratings for banks in Bangladesh.
BRPD Circular Letter No.02 16 January, 2014 Regarding avoidance of High Expense for Luxurious Vehicles and Decoration	The negative effect of high expenses and usage of luxurious car by Bank's Chairman, Chief Executives and other high officials by bank company's money created concerns. Therefore, a circular has been issued containing few instructions; a. Motor car (Sedan) costing more than Tk. 50 lac and sport Utility Vehicle costing more than Tk. 1 crore shall not be bought with bank company's money. b. Floor space more than 5000 square feet for urban branch and 2000 square feet for rural branch would not be used for establishing new branch or shifting of existing branch. c. Expenditure on per square foot (for vault, interior decoration, office furniture, electric/electronics etc.) should not exceed Tk.1500 for new branch and Tk.1000 for shifting branch except for IT expenditure.
FE Circular No.04 22 January,2014 Regarding advance payment against imports	With a view to further liberalizing foreign exchange regime, it has now been decided to enhance the limit of advance payment from USD 2,500 to USD 5,000 for import of books, journals or life saving medicines without repayment guarantee.
FE Circular No.06 30 January,2014 Pledging of collateral in	. 01. As per the Guidelines for Foreign Exchange Transactions (GFET)-2009, Volume-1, it is mentioned that ADs may not, without prior approval of Bangladesh Bank, furnish guarantees to or hold collateral on behalf of overseas bank branches or

favor of overseas bank branches and correspondent	correspondents in respect of credit facilities or guarantees to be extended by them or for any other purpose. 02 It has now been decided that ADs may, without prior approval of Bangladesh Bank, hold collaterals on behalf of overseas bank branches or correspondents in respect of external borrowing by industrial enterprises as approved by Board of Investment.
FE Circular No.08 18 February,2014 Regarding remittance of cost of training and consultancy services	It has now been decided that, like industrial enterprises (engaged in manufacturing or processing or assembling), service sector industries which are within the purview of Industrial Policy in force may remit through their nominated ADs upto 1% of annual sales as declared in their previous years' income tax return towards costs of training and consultancy services as per relevant contract with the foreign trainer/consultant.
FEID Circular Letter No.08 19 February,2014 Inward Remittance against agency services on one-off basis	In order to benefit the customers concerning liberalization in foreign exchange regime, it has been decided that ADs may encash inward remittances against agency services on one-off basis without permission of Bangladesh Bank after satisfying themselves with the genuineness and bonafide nature of the requests from their customers through relevant documents such as invoices, agreements, etc. and after deducting all applicable taxes.
FE Circular No.11 10 March,2014 Regarding revision of Business travel quota entitlements	1.(i) Exporters, importers and producers for the local market will be entitled to foreign exchange quota for travel abroad @ USD 400 per diem, subject to limits of USD 4,000 per trip and USD 10,000 over a calendar year. Besides, exporters will also be entitled to use balances in their foreign currency retention quota account for their business visits abroad. (ii) Senior level (top two tiers) expatriate foreign nationals employed in business organizations in Bangladesh with valid visas and work permits will be entitled to the same business travel quota as Bangladesh nationals; which can be used through

	international credit/debit cards held by them. 02. Genuine requirements beyond the entitlements enumerated above will be accommodated by Bangladesh Bank upon submission of application supported by documents establishing bonafides of the additional requirements.
FE Circular No.12 11 March,2014 Term lending in Taka to foreign owned controlled companies in Bangladesh.	Given the prevailing comfortable liquidity situation in the local markets, it has been decided that foreign owned/controlled companies engaged in manufacturing or services output activities for three years or longer in Bangladesh can access Taka term loans from the domestic market regardless of local content in their equity; subject to adherence by banks/financial institutions to all applicable credit norms and prudential parameters including single borrower exposure limit, debt-equity ratio and so forth.
FE Circular No.13 11 March,2014 Foreign owned/controlled industrial enterprises access to short term interest free loan from parent companies/shareholders abroad	Foreign owned/controlled industrial enterprises in Bangladesh have indicated occasionally arising urgent necessity of short term borrowing for business needs other than inputs procurements, for which working capital financing from the local market has not yet been lined up. To help foreign owned/controlled industrial enterprises get around such difficulties, it has been decided that they may henceforth access interest free loans from parent companies/shareholders abroad for upto one year without any prior approval, subject to post facto reporting to Bangladesh Bank.