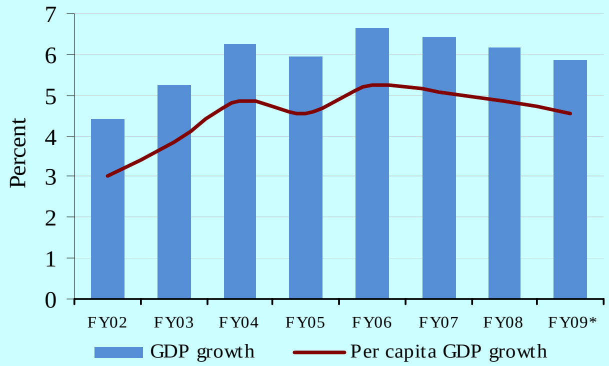
The target for production of wheat in FY09 is 1.0 MMT which is 18.5 percent higher than the level in FY08 Available reports suggest a good harvest. Among other cereals, significant increase has been achieved in the production of maize which has emerged as the fastest growing cereal over the last few years. The target production of maize has been set at 1.4 MMT in FY09, nearly 7 percent higher than the last year's production level (Table I.4). In the wake of high prices and buoyant domestic demand, the area and production level of non-cereal crops such as vegetables, oilseeds, potato, and sugarcane grew strongly in FY08 and this is likely to continue in FY09.

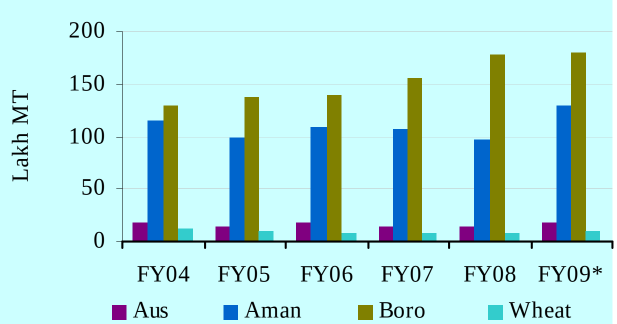
In order to support higher production levels, the annual target for agricultural credit disbursement is set at Tk. 93.8 billion for FY09, nearly 13 percent higher over FY08 disbursement, of which Tk. 69.1 billion was disbursed during the first three quarters of FY09 (9.4 percent growth over the same period of FY08). Of the total amount disbursed, Tk. 24.4 billion was given to the crop sector while Tk. 13.9 billion, Tk. 3.6 billion, and Tk. 3.3 billion went to poverty alleviation, livestock, and fisheries respectively. Overdue as a percentage of outstanding loans declined to 33.4 percent at the end of Q3 FY09 which was 36.0 at the end of Q3 FY08. In the recently announced fiscal stimulus package, another Tk.15.0 billion has been allocated to agricultural credit rescheduling scheme.

Chart I.1: Growth of Real GDP



* Provosional estimates of BBS

Chart I.2: Production of Major Crops



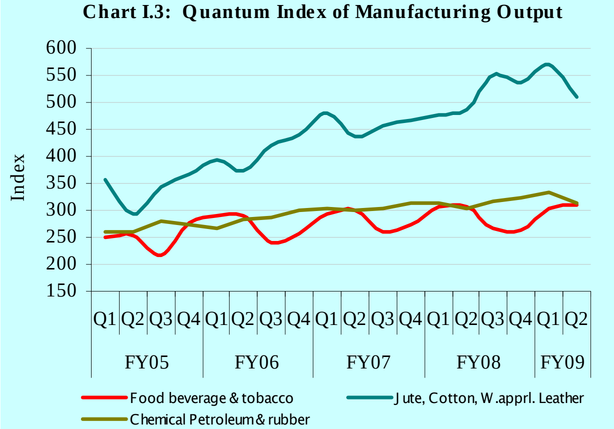
* Revised Target

Strong growth in private sector credit (by 17.2 percent in Q3 FY09 over Q3 FY08) and buoyant growth in industrial term lending (a disbursement of around Tk. 89.4 billion for long-term, mid-term, and short-term combined, during July-December FY09) has largely overcome last year's slower growth performance (6.9 percent in FY08) in the industry sector. Also, contribution of manufacturing products to total export growth during July-February FY09 indicates sustained growth of this sector over the period. The industrial quantum index including the index of major sub-sectors showed strong growth during H1 FY09. Available evidence shows the continuation of similar trend in H2 FY09 indicating strong expected contribution of the manufacturing sector to overall growth in FY09 (Tables I.3 and I.5). The industrial quantum index during Q2 FY09 achieved a growth rate of 4.8 percent over the same period of the previous fiscal which exhibited a mild moderation in the industrial sector growth especially in the medium and large scale manufacturing units. The two major sub-sectors in terms of relative weight, namely 'jute, cotton, RMGs and leather' and 'chemical petroleum, and rubber' grew at the rate of 4.6 percent and 3.5 percent respectively during Q2 FY09 where sub-sectors like 'non-metallic products' and 'basic metal products' showed significant growth of 17.1 percent and 17.0 percent respectively over Q1

FY09. Growth of 'food, beverage and tobacco', 'paper and paper products' and ' fabricated metal products' sub-sectors were also up to expectations.

The strong activities in manufacturing sector are also visible in strong export stimulus from the industry sector which is reflected in robust export growth (15.9 percent) during July-February FY09 over the same period of FY08. The performance of several other indicators during the period also suggests that manufacturing production is likely to grow at faster rates in the coming months. Growth of industrial loan by banks and non-bank financial institutions, growth of private sector credit and export-import situation were favorable for industrial activities. Disbursement of industrial loan experienced a robust growth of 15.7 percent over H1 FY09 and stood at Tk.316.0 billion which was Tk.273.1 billion during H1 FY08; especially there has been a remarkable growth of 28.4 percent in loan for working capital financing which indicates the possibilities of higher manufacturing production in the coming months. At the end of Q2 FY09 about 20.5 percent of total disbursed loan by banks and non-bank financial institutions (NBFIs) went to small and medium enterprises (SMEs) sector reflecting boost of activities in this sector which is a pre-requisite to attain higher productivity though building local capacity. Import of industrial raw materials, intermediate goods and capital goods has also become buoyant with 17.0 percent growth in overall imports L/Cs settlement in July-February FY09 over the same period of FY08 that are likely to expand industrial production base in the coming months of FY09. After the inception of new government, overall favorable investment climate is reported and also business confidence is likely to improving gradually resulted in higher growth in the industry sector. Nonetheless, to promote the industry sector, the prevailing shortages in power and gas supplies need to be improved urgently. New investment in bulk would be essential in the near term to ensure the required supply of power and gas. In this regard, higher dependence on local resources, public and private, would be best option.

Chart I.3: Quantum Index of Manufacturing Output



The robust growth in exports and remittances inflow (15.9 percent during July-February FY09 and 24.4 percent during July-March FY09 respectively) shows the economy's high resilience to withstand the fallout effects of the global financial crisis and aided to grow the industry sector as well as related service at a higher rate. Global as well as domestic commodity prices have been declining including prices of fuel oil and other services sector inputs. The business climate has been improving and overall economic activities are picking up gradually. Thus positive impacts of these developments are likely to be felt in many services sector activities including financial intermediation, education, health and social works, and public administration and defense. On the other hand, several activities including wholesale and retail trade, transportation and telecommunication with significant development in mobile phone subsector, hotel and restaurants, and social and personal services have been gearing up aided by favorable weather condition and political environment and would contribute positively toward higher growth in the services sector in FY09. During the first 9 months of FY09, BB has expanded the spectrum of SME financing scheme by including broadband and IT, a sector with enormous possibilities of service oriented income and employment generation especially for the educated youth.

Furthermore, in the recent fiscal stimulus package, the allocation for house building fund has been increased by 200 crore taka to 500 crore taka which will boost service activities related to construction sector.

A large number of measures have also been taken in the recent fiscal stimulus package to facilitate the higher disbursement of credit to agriculture to achieve the target of domestic food grain self-sufficiency. Furthermore, new thrust sectors are targeting such as shipbuilding, IT, agro-processing, and export oriented industries to give required supports in order to accelerating real sector growth of the economy. Government has announced a two phased fiscal and financial incentive package along with policy support and administrative reformation to boost up domestic economy in the backdrop of global financial turmoil. Under this program a joint attempt has been taken by government and BB to promote export sector including increase of Export Development Fund (EDF) to US$150 million and extended financial facilities from banks and NBFIs for the adversely affected export oriented industries on a case to case basis. Thus under the current real sector outlook, the Provisional growth projection of 5.88 percent by the BBS for FY09 appears realistic. The buoyancy in economic activities that started in H1 FY09 has been strengthened in H2 FY09. For realizing the growth target and preparing the economy to move to a higher growth path, it would be important to strengthen existing growth supportive policies with additional policies to realize the potentials. The policy thrust would be to put adequate emphasis on rapid expansion of export oriented industries, SMEs and non-farm activities which will create more employment opportunities. The policy thrust should also be aimed to increase the investment rate and enhance productivity growth to boost growth friendly economic activities and encourage private sector led growth.

II. Monetary and Credit Market Developments

Monetary and credit market developments in Q3 FY09 were largely consistent with the monetary policy stance adopted by BB for H2 FY09. The thrust was to contain inflationary pressure on the one hand and ensure adequate liquidity to the productive sectors to facilitate growth of economic activities on the other. At the end of the quarter, monetary policy stance eased a little following lowering of inflationary pressure and inflation expectations. Besides, in order to weather adverse effects of global slowdown on the domestic economy through trade, remittances, aid, and investment channels, monetary sector developments were under constant vigilance of BB to ensure proper monetary management.

Chart II.1: Components of Reserve Money

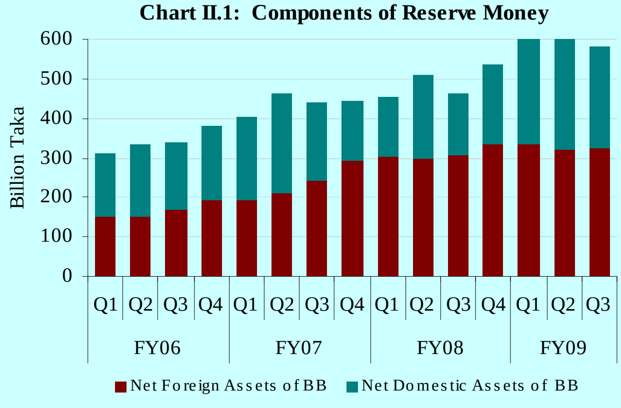
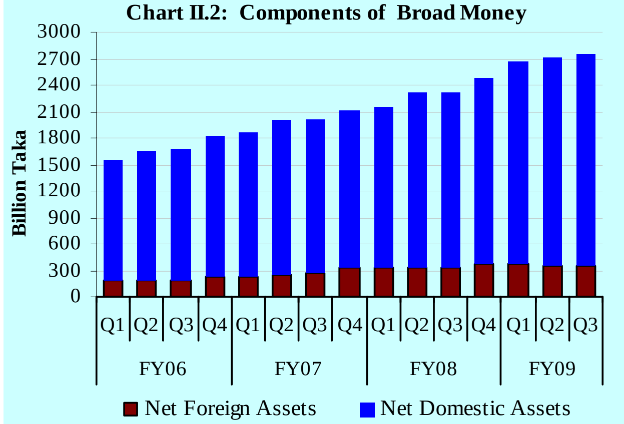
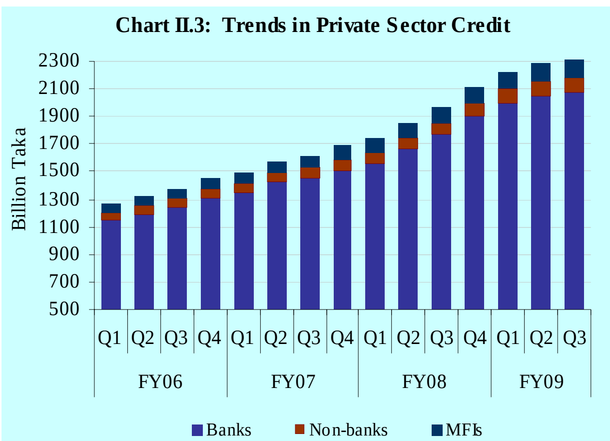


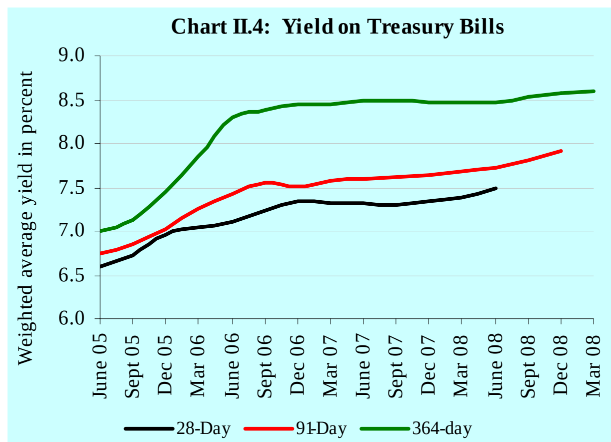
Chart II.2: Components of Broad Money



Total private sector credit by DMBs grew at 19.8 percent (y-o-y basis) in February 2009, which grew by 19.4 percent during the same period of the preceding year. The disbursement of agricultural credit during July-February FY09 stood at Tk. 59.4 billion which is 7.2 percent higher than the same period of the preceding year. On y-o-y basis, total credit growth to private sector from banks and micro finance institutions increased to Tk. 2,075.0 billion and Tk. 129.8 billion respectively during Q3 FY09 from Tk. 2045.3 billion and Tk.128.7 billion at the end of December FY09 reflecting increased overall economic activity during the period under review.

Among the monetary aggregates, broad money (M2) recorded a growth of 19.3 percent in February 2009 up from 15.3 percent in February 2008. This higher growth was caused mainly by increased growth of 22.1 percent in net domestic assets (NDA) although net foreign assets (NFA) showed a moderate growth of 3.3 percent. The rise in NDA was driven by growth of public sector credit by 21.8 percent and private sector credit by 19.8 percent respectively in February 2009 compared with 8.6 percent and 19.4 percent growth over the same period in the previous year. The growth of narrow money (M1) moderated slightly and grew by 14.3 percent in February 2009 which grew 14.6 percent over the same period in the preceding year.





An analysis of the components of M2 shows that currency demand and time deposits grew by 20.0 percent and 20.8 percent in February 2009 compared with 13.1 percent and 15.5 percent growth respectively recorded in February 2008. The growth rate of demand deposits, on the other hand, decelerated from 16.5 percent in February 2008 to 7.2 percent in February 2009. The money multiplier (M2/RM) declined to 4.7 in February 2009 from 4.9 during the same period of the preceding year due to larger increase in RM relative to M2.

The RM grew by 22.9 percent and stood at Tk. 581.7 billion in February 2009 showing 9.4 percent y-o-y growth in February 2008. This occurred despite a significant slowdown in growth of NFA (from 33.6 percent in February 2008 to 7.1 percent in February 2009).[1] On the other hand, NDA grew by 51.8 percent in February 2009 driven by a substantial increase in BB's claims on Government (31.1 percent in February 2009 compared with (-) 19.1 percent in February 2008), while the growth of BB's claims on DMBs decreased by 19.3 percent in February 2009 over the same period of the preceding fiscal.

[1] NFA refer to foreign exchange reserves in BB.

In December 2008, total advances by economic purposes increased by 21.88 percent and stood at Tk. 1,873.4 billion which was Tk. 1,537.1 billion during the same period in the preceding year. Bank advance by economic purposes shows that in Q2 FY09, credit for miscellaneous purposes increased by 37.05 percent, industry sector by 25.18 percent, construction by 22.60 percent, trade by 21.85 percent, agriculture by 15.36 percent (of which credit for crops rose by 15.13 percent and for others by 18.67 percent), working capital financing increased by 12.6 percent, transport and communication by 12.5 percent. These growth rates were 25.55 percent, 23.11 percent, 8.56 percent, 15.40 percent, (-) 1.7 percent (of which crop) (-) 1.28 percent and others 19.05 percent), 13.79 percent and 54.30 percent respectively during the same period of the preceding fiscal year (Table 1.8).

Chart II.5: Weighted average yield of accepted Government Treasury Bills & Bonds (End March, 2009)

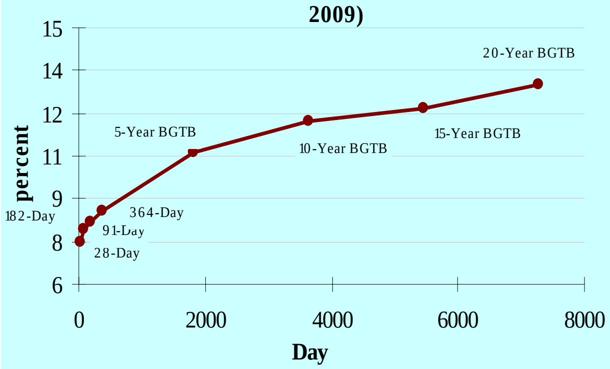
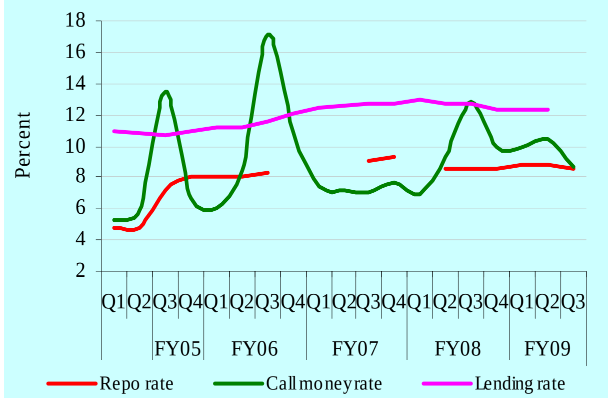


Chart II.6: Interest Rate Movements



The disbursement of term lending by banks and NBFIs decreased by 32.1 percent and stood at Tk. 39.9 billion in Q2 FY09 (y-o-y basis) which was Tk.58.8 billion during the same period in the preceding year. Between Q2 FY08 and Q2 FY09, term lending by SCBs decreased from Tk. 3.3 billion to Tk. 2.9 billion and that of PCBs decreased from Tk.41.2 billion to Tk.25.5 billion, while the decline for FCBs was from Tk. 7.3 billion to Tk. 6.1 billion. Term lending by NBFIs also declined from Tk.6.2 billion to Tk. 4.4 billion (Table I.11).

The rates of repo and reverse repo were reduced to 8.50 percent and 6.50 percent from 8.75 percent and 6.75 percent respectively on 11 March 2009. The call money rate remained mostly stable and stood at 8.68 percent at the end of March 2009. Overall, yields on short term treasury bills (182-day, 364-day) displayed slight increase in Q3 FY09 over Q3 FY08 although yields on long term bonds such as 5-year and 10-year BGTB remained unchanged while yields on 15-year and 20-year BGTB declined slightly over the same period of the preceding year (Table III.3). Outstanding stock of government treasury bills including NSD certificates increased slightly and stood at Tk.877.6 billion at the end of February 2009 compared with Tk. 852.0 billion at the end of December of 2008.

III. Fiscal Developments

During the first three quarters of FY09, fiscal developments remained mostly in line with yearly targets set in the FY09 budget. During the period, preliminary estimates of total revenue and total expenditure, as percent of GDP, stood at 7.4 percent and 10.3 percent as against the yearly targets of 11.3 percent and 16.3 percent respectively for FY09. Overall fiscal deficit, as share of GDP, reached 2.9 percent in the first three quarters of FY09 as against the yearly target of 4.99 percent. During the period, total deficit financing amounted to Tk. 178.2 billion of which Tk.

118.4 billion was accommodated from domestic sources that included bank financing of Tk. 80.7 billion while the remaining Tk.59.8 billion came from foreign sources. [2]

The target for National Board of Revenue (NBR) tax revenue is Tk. 545 billion for FY09. As against the target, NBR collected Tk. 361.7 billion during the first three quarters of FY09 which is 13.2 percent higher than the level achieved during the same period of FY08. The tax revenue growth was led by value added tax (VAT), income tax, and other sources.[3] In the first nine months of FY09, tax revenue collected from VAT, income tax, and other sources, increased by 16.1 percent, 20.8 percent, and 9.3 percent respectively over the same period of FY08. However, revenue earnings from custom duty (18 percent share in total NBR revenue) slowed down in the first nine months of FY09 due to falling prices of imported commodities in the international market along with declining imports of consumer goods. In order to achieve the targeted revenue collection, various measures have been adopted such as strengthening tax collection efforts, identifying new tax payers, and enhancing transparency, accountability, and efficiency of tax administration, and introducing electronic cash register for retail sellers.

Chart III.1: Trend in Government Revenue and Expenditure

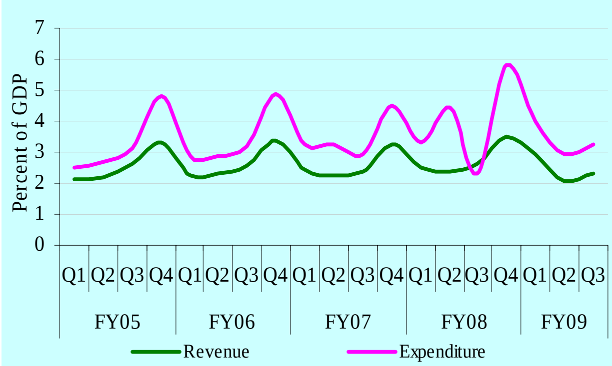
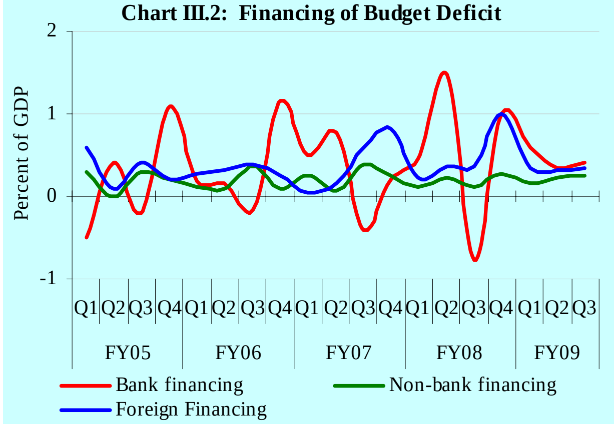


Chart III.2: Financing of Budget Deficit



In FY09, the targets for current expenditure and annual development program (ADP) expenditure have been set at Tk.667.6 billion (10.9 percent of GDP) and Tk.256.0 billion (4.2 percent of GDP). These targets are higher by more than one-third and 50 percent respectively than their actual levels in FY08. Against these targets, current expenditure in the first nine months of FY09 stood at 469.2 billion (70 percent of the annual target) which is 46.0 percent higher than the level of the same period of FY08. The increase has partly been contributed by payment of enhanced salaries to government employees and increased expenses on subsidies and debt services. The estimated data show that the implementation rate of ADP stood at 41 percent during the first nine months of FY09. Rapid implementation of ADP projects especially in social and physical infrastructure sectors like electricity, gas, agriculture, transport, education, health, and poverty reduction activities should be given priority in order to achieve the ADP target and promote desired growth. It may be added that the ADP utilization rate was 75.9 percent of the revised target in FY08.

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[2] In the absence of actual data up to March 2009, estimated data of revenue, expenditure, and financing have been used in the analysis of this section. As a result, the figures may differ from other sources.

[3] The share of VAT is around 41 percent in total NBR tax revenue. Other sources include supplementary duty (local and import), excise duty, turnover tax, and travel tax.

In FY09 budget, deficit financing from domestic and foreign sources is set at Tk.170 billion and Tk.72.4 billion respectively. Among domestic sources, Tk. 135 billion is expected to come from bank financing and Tk.35 billion from non-bank financing. During the first nine months of FY09, bank borrowing stood at Tk. 80.7 billion compared with Tk.62.0 billion in the same period of FY08. Non-bank borrowing stood at 37.7 billion in the first nine months of FY09 compared with 25.2 billion in the same period of FY08 (Table III.1 and Chart III.1).

IV. External Sector Developments

The current account balance (CAB) maintained a sizeable surplus during July-February period of FY09 due mainly to healthy growth in inflow of workers' remittances and export earnings. The slowdown of new manpower exports to some countries has been a source of concern and the government has taken steps to improve the situation so that inflow of workers' remittances can maintain its growth momentum. An important aspect of the external sector is that, in spite of global recession, Bangladesh has succeeded in maintaining external sector stability showing surplus in CAB as well as in overall balance of payments during July-February FY09.

The CAB showed a healthy surplus of USD 584 million in January-February period of 2009 as against a small surplus of USD 12 million in the corresponding months of 2008. In Q2 FY09, CAB had a deficit of USD 134 million. As a whole, CAB showed USD 816 million surpluses during July-February period of FY09. This surplus emerged due to healthy surplus in current transfers of USD 1609 million that included an inflow of workers' remittances of USD 1,643 million despite deficits in trade balance (USD 586 million), and income account (USD 444 million) during January-February 2009. The capital and financial account, on the other hand, maintained a small deficit (USD 216 million) during January-February 2009 against a surplus of USD 80 million during January-February 2008. Capital and financial account showed USD 9 million and USD 334 million surpluses during Q1 FY09 and Q2 FY09 respectively. The overall balance showed a surplus of USD 284 million during January-February 2009 compared with a deficit of USD 67 million during the same period of 2008 and a surplus of USD 64 million and USD 425 million in Q1 and Q2 FY09 respectively. Overall, the country's balance of payments showed a healthy USD 773 million surplus during July-February period of FY09.

Chart IV.1: Trends in Current Account and Overall Balance

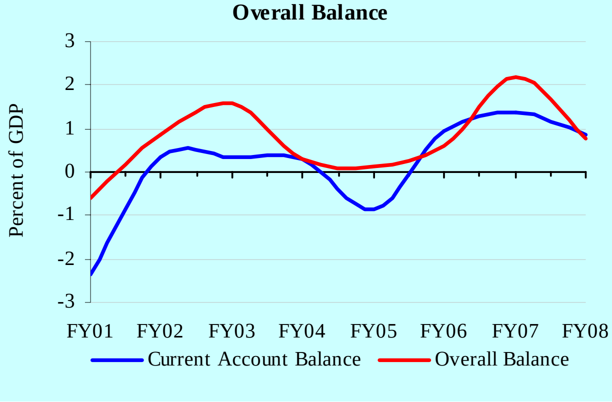
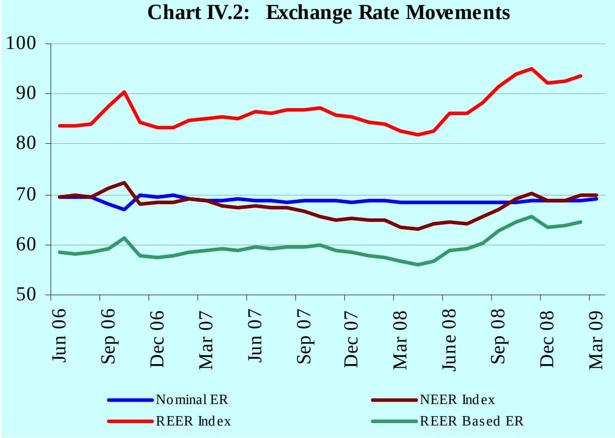


Chart IV.2: Exchange Rate Movements



The foreign exchange market remained mostly stable and Taka depreciated marginally by 0.14 percent against USD during Q3 FY09 and 0.72 percent during July-March period of the current fiscal due to healthy situation in the foreign exchange reserves (USD 5.95 billion at the end of Q3 FY09) and appropriate policy stance adopted by the government and the BB. The BB, as part of its pro-active monetary policy, remained active in the foreign exchange market and made necessary interventions showing a net purchase of USD 457.7 million in the inter-bank market during the first nine months of FY09.

Both the nominal effective exchange rate (NEER) index and real effective exchange rate (REER) index appreciated during January-February 2009. On the other hand, the nominal value of Taka depreciated marginally during the quarter. The nominal exchange rate remained higher than the REER based exchange rate and Bangladesh enjoyed reasonable competitiveness in the international market during the quarter under review (Chart IV.2).

Following the global recession, export earnings showed some dip in October 2008 but the country's overall export earnings bounced back and regained its momentum in November 2008. Export earnings registered a slower 5.5 percent growth during January-February period but the overall growth was 15.9 percent during July-February FY09 over the corresponding period of previous fiscal. During January-February period of FY09, RMGs (woven garments and knitwear products) which cover almost 80 percent of total exports registered higher exports but some other commodities like raw jute, jute goods, leather, frozen shrimps and fish, fertilizer, terry towels etc. registered shortfall over the same period of the last fiscal (Table IV.2). The exports of RMGs registered a 21.2 percent growth during July-February period of FY09.

Chart IV.3: Trends in Exports & Imports

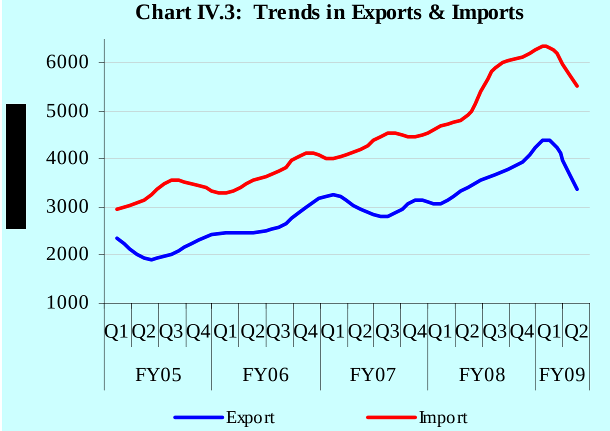
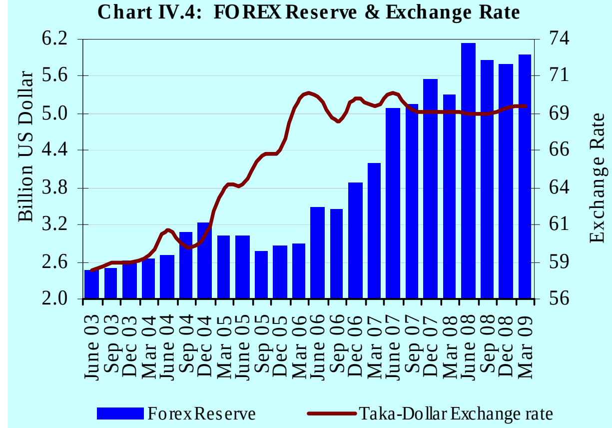


Chart IV.4: FOREX Reserve & Exchange Rate



According to the Export Promotion Bureau (EPB), during July-March FY09, several export commodities including RMG products as well as terry towel, textile fabrics, pharmaceuticals, handicrafts, computer services and chemical fertilizer recorded higher growth over the corresponding period of the last fiscal and achieved or exceeded their targets. The exports of foot wear, home textile, agricultural products and other manufacturing goods also recorded higher growth over the same period of FY08 but fell short of their targets. On the other hand, exports of raw jute, tea, jute goods, electronics, leather, ceramic products, frozen foods, petroleum bi-products and other primary commodities recorded declines over their corresponding period of FY08 levels as well as fell short of their targets (Table IV.6).

Destination-wise trend of RMG exports is given in Table IV.5. The table shows that exports of woven categories increased significantly to US but fell sharply to EU regions during Q2 FY09 which recorded a higher growth in both regions during Q1 FY09. Exports of knitwear category recorded decline in both US and EU markets during Q2 FY09 which also recorded higher growth during Q1 FY09 in both markets. On the other hand, exports of both woven and knit category increased significantly in other than USA and EU markets during Q1 and Q2 of FY09. Overall export of RMGs increased by 12.4 percent to USA but declined sharply by 30.7 percent to EU markets while its export increased significantly by 337.7 percent to other than US and EU markets during Q2 FY09.

Total merchandise imports declined by 3.9 percent (on cif basis) during January-February 2009 compared with a 12.1 percent growth recorded in Q2 FY09 (Table IV.3). This decline in imports in January-February 2009 reflected decline in imports of food grains (-47.2 percent), consumer and intermediate goods (-11.2 percent) and imports by EPZ (-19.1 percent). Merchandise imports recorded a 15.6 percent growth during July-February period of FY09 over the same period of the previous fiscal. During July-February period, food grains imports decreased sharply by 40.2 percent of which rice import decreased by 62.5 percent and wheat import decreased by 8.1 percent. Imports of other food items decreased by 5.1 percent of which the decline in milk and cream was by 36.3 percent, spices by 35.3 percent, oil seeds by 13.4 percent, pulses by 54.2 percent. On the other hand, edible oil and sugar imports increased by 2.6 percent and 63.7 percent respectively during July-February period of FY09. Imports of consumer and intermediate goods recorded a high 23.8 percent growth during July-February period of the current fiscal. The import growth is largely accounted for by increased imports of POL (28.7 percent), pharmaceutical products (54.9 percent), fertilizer (113.1 percent), dyeing and tanning material (34.8 percent), and yarn (25.2 percent). The import of capital goods and others recorded 25.4 percent growth during July-February FY09. The higher growth in this sub-sector was mainly due to sharp increase in imports of iron, steel and other base metals (34.6 percent) and other goods and machineries (39.2 percent) in spite of decline in import of capital machinery (-12.4 percent).

The inflow of workers' remittances, the critical anchor for the current account balance, recorded 14.5 percent growth (USD 2.5 billion) during January-March FY09. During Q2 FY09, the inflow of workers' remittances recorded a growth of 19.7 percent to USD 2.2 billion. Overall inflow of workers' remittances recorded a strong 24.5 percent growth (USD 7.0 billion) during July-March period of FY09. During January-March 2009, the largest source of remittance was Saudi Arabia (USD 769.0 million) followed by UAE (USD 482.8 million) and USA (USD 428.4 million).

Maintaining a healthy balance of payments position including a stable and competitive par value of Taka requires continuous efforts to increase export earnings as well as well-conceived measures to ensure rising inflow of workers' remittances. In this context, strengthened initiatives are needed to explore new markets to diversify the country's export products and destinations. In order to capture new labor markets and sustain its position in the competitive global labor market, Bangladesh needs to formulate adequate policies and programs to impart appropriate training and skills to meet country specific labor demands.

V. Price Developments

Inflation has significantly subsided in Q3 FY09 which started in September 2008. The point-to-point (p-t-p) inflation stood at 5.04 percent in March 2009 down from 6.03 percent in December 2008 and 10.19 percent in September 2008. The 12 month average inflation was 7.69 percent in March 2009 which was 8.90 percent in December 2008 and 10.06 percent in September 2008. The decline in inflation during the quarter under review is mainly due to fall in the price of rice in the domestic market. Besides, prices of most imported items, particularly non-food items also declined in the backdrop of the ongoing global recession (Table V.1).

However, prices of several essential food items in the international market moved up during Q3 FY09 (January 2009) as compared to the end of Q2 FY09. The price of rice in the international market increased by around 12 percent in January 2009 compared to the price in December 2008. Prices of several other primary commodities e.g. wheat, edible oil, and sugar also increased in January 2009. The average price of crude oil (petroleum) increased in January 2009 and stood at USD 45 per barrel compared with USD 41.53 per barrel at the end of Q2 FY09. Overall, the price situation in the domestic market remained mostly under control during the quarter although prices of several food and non-food commodities increased in the international market (Table V.2).

Chart V.1: 12-Month CPI Inflation

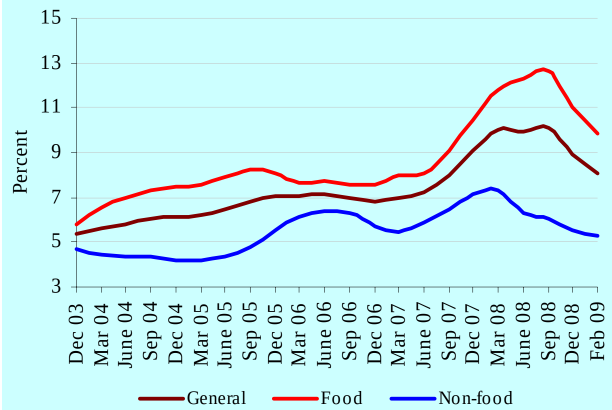
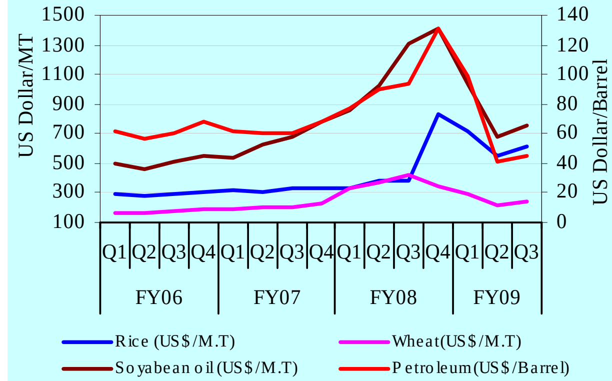


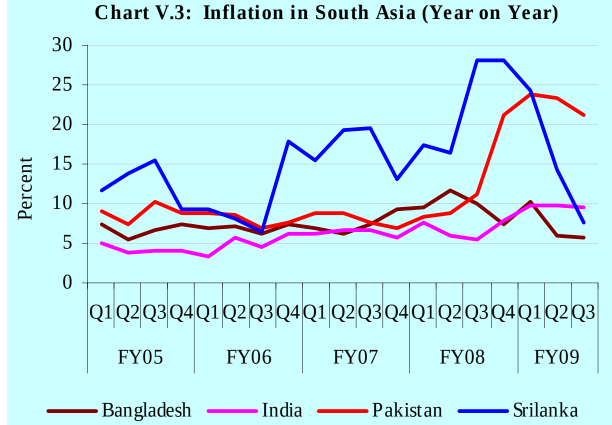
Chart V.2: Commodity Prices in International Market



The global meltdown also had some moderating effect on inflationary pressure in other South Asian countries. The CPI inflation (p-t-p) in India slightly eased to 9.6 percent in February 2009 compared with 9.7 percent in December 2008. Inflation in Pakistan as measured by changes in CPI (p-t-p) came down to 21.1 percent in February 2009 which was 23.3 percent in December 2008. In Sri Lanka, inflation as measured by Colombo consumer price index (CCPI) declined by 6.8 percentage points to 7.6 percent in February 2009 as compared with 14.4 percent in December 2008 (Table V.3).

In the backdrop of global recession and backed by improved domestic supply conditions, the softening of inflationary pressure is likely to continue in the coming months. However, it is important to keep in view that the current price fall in the global commodity market is largely due to changes in demand side factors while global supply situation has remained relatively unchanged. As such if the major economies, especially the advanced ones, succeed in recovering from the crisis within a relatively short period, the commodity markets may again experience tight conditions for which Bangladesh needs to adopt appropriate policies.

Chart V.3: Inflation in South Asia (Year on Year)



VI. Health of the Banking System

Major indicators of health of the banking system showed improvements during the quarter under review. The risk-weighted asset to capital ratio for the banking system as a whole stood marginally above the regulatory requirement of 10 percent. The ratio of non-performing loan

(NPL) to total loan for the banking sector, in both gross and net terms, declined. Return on asset (ROA) and return on equity (ROE), two important measures of bank profitability increased. The interest rate spread (IRS) for all banks also reduced. The country's banking sector remained shielded from the global financial turmoil mainly due to the low level of global integration and good health underpinned by prudent regulation and sound management. It would however be important to refresh banking sector surveillance and revisit financial sector management to counteract any potential adverse impact on the country's banking sector.

The risk-weighted capital asset ratio (RWCAR) for all banks increased to 10.1 percent in December 2008 from 9.5 percent in June 2008, reflecting positive changes in the ratio from 6.3 percent to 6.9 percent for SCBs; from 10.9 percent to 11.4 percent for PCBs; from (-) 5.6 percent to (-) 5.3 percent for SBs, and from 22.9 percent to 23.8 percent for FCBs. This is partly the result of corporatization of three SCBs (Sonali, Janata and Agrani) by the government as well as policy measures implemented by BB. The RWCAR, however, remained significantly above the regulatory requirement of 10 percent only for FCBs and marginally higher for PCBs (Table VI.1).[4] In view of the growing share of PCBs in the overall banking activities, it would be prudent to encourage the PCBs to further augment their capital ratio to acquire higher capacity to successfully weather any episode of systemic shocks in the banking sector.

The ratio of gross NPL to total loans of the banking sector declined from 12.3 percent during end September 2008 to 10.8 percent in end December 2008. During the period, gross NPL ratio for SCBs declined from 29.3 percent to 25.4 percent which contributed significantly in reducing the overall ratio. The ratio for the FCBs increased marginally to 1.9 percent during end December 2008 from 1.6 percent at the end of September 2008 (Chart VI.1). For the PCBs and SBs, similar ratios decreased from 5.4 percent to 4.4 percent and 26.2 percent to 25.5 percent respectively (Table VI.2).

Chart VI.1: Ratio of Gross NPLs to Total Loans

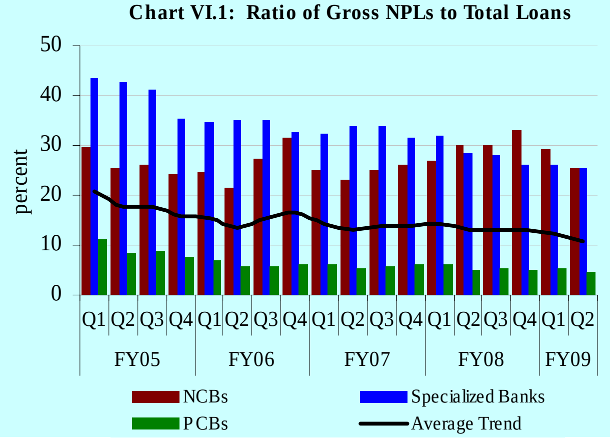
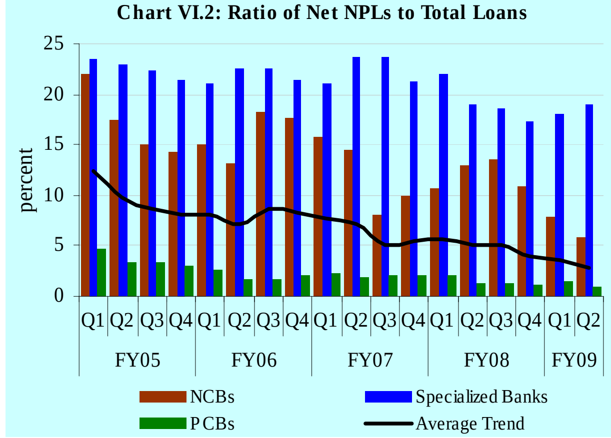


Chart VI.2: Ratio of Net NPLs to Total Loans



On the other hand, the net NPL ratio for all banks declined to 2.8 percent in Q2 FY09 from 3.7 percent in Q1 FY09 led by healthy improvement in the ratio of SCBs from 8.0 percent to 5.9 percent. Similarly, the ratio decreased from 17.9 percent to 16.9 percent for SBs; from 1.5 percent to 0.9 percent for PCBs; and from (-) 1.9 percent to (-) 2.0 percent for FCBs (Table VI.3 and Chart VI.2).

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[4] As per BB's BRPD Circular No. 05/2007 of 14 May 2007, banks are required to maintain capital to risk-weighted asset ratio of 10 percent at the minimum with core capital not less than 5 percent.

Among the profitability measures, overall ROA increased from 0.9 percent to 1.2 percent during 2008 because of healthy profits earned by PCBs; while ROE for the same period increased from 13.8 percent to 15.6 percent due mainly to sharp growth in ROE for SCBs: from nil to 22.5 percent. Both ROA and ROE turned negative for SBs over the last few years. The figures show similar poor performance in 2008. Since BB requires that taxes and provision shortfall be accounted for in determining net income, net returns of SCBs turned negative since 2006.[5] Hence both ROA and ROE for the group have been administratively set at zero for 2007. But in 2008, both ROA and ROE increased to 0.7 percent and 22.5 percent respectively for the SCBs which is the result of corporatization of the three NCBs under which the amount of loss of the banks were converted into goodwill and shares were issued equivalent to the amount in favor of the government. Another feature is that the ROE figures for FCBs and PCBs have narrowed down to 17.8 percent and 16.4 percent in 2008 compared with the 20.4 percent and 16.7 percent respectively in 2007. The ROA for FCBs, on the other hand, decreased from 3.1 percent in 2007 to 2.9 percent in 2008; the group still remains the front runner compared with other bank categories (Table VI.4).

During end December 2008, the interest rate spread (IRS) stood at 5.00 percentage points for all banks; lower than 5.17 percentage points in end September 2008. During Q2 FY09, the deposit rate increased to 7.31 percent from 7.17 percent in Q1 FY09 while the lending rate decreased from 12.34 percent to 12.31 percent over the same period. However, IRS increased from 2.95 percentage points to 3.12 percentage points for SBs while the same decreased from 4.54 percentage points to 3.96 percentage points for SCBs; from 4.76 percentage points to 4.70 percentage points for PCBs; and marginally from 9.34 percentage points to 9.33 percentage points for FCBs. This shows the result of BB's persistent effort in persuading the banks to reduce the spread in a rational manner (Table II.3).

At the end of Q2 FY09, total deposit (excluding inter-bank) of the banking sector stood at Tk. 2,527.6 billion which was 5.1 percent higher than Tk. 2,404.5 billion in end Q1 FY09. Similarly, total advances (excluding inter-bank) increased by 2.8 percent from Tk. 1,910.8 billion to Tk. 1,963.9 billion over the same period. During Q2 FY09, among different bank categories, SBs recorded the highest deposit growth of 6.1 percent over Q1 FY09; the growth was 5.5 percent for PCBs; 6.0 percent for SCBs; and (-) 1.0 percent for FCBs. In the case of advances, PCBs recorded 3.4 percent growth during Q2 FY09 over Q1 FY09 compared with 3.3 percent growth for SCBs; 3.0 percent for SBs and (-) 3.9 percent for FCBs.

Thus most of the indicators of health of the banking sector have shown improvement over the recent past. This may largely be attributed to the BB's regulatory framework as well as cautious monitoring and supervision of the banking sector. On the other hand, the country's banking sector possesses low level of global integration. The banking sector in Bangladesh still remained largely immune to the current global financial crisis more particularly, the crisis in the global banking sector. Under these circumstances, being the regulator of the banking and financial sector, it will be prudent for BB to augment the regulatory framework for the banking sector to avoid any episode of global shocks to be transmitted in the country's banking system.

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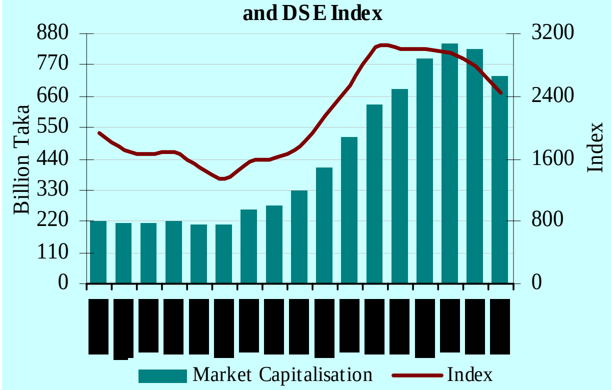
[5] It may be noted that the net income was negative even without accounting for the provision shortfall during the calendar year 2004. But in 2006, income before provision was positive, but it turned negative after allowing for the provision shortfall.

VII. Capital Market Development

The downward trend of DSE general index along with some volatility continued during the quarter. All indicators except turnover of capital market showed weaknesses as evidenced by declines in general price index and market capitalization. During Q3 FY09, DSE general index and market capitalization declined by 12.5 percent and 11.1 percent respectively (Chart VII.1 and Table VII.1). Year-on-year position of DSE general index declined significantly by 18.9 percent while market capitalization increased by 7.2 percent.

The liquidity situation in the capital market improved significantly during the quarter vis-à-vis the previous quarter. Total turnover increased to Tk. 217.8 billion as compared with Tk. 152.4 billion in the previous quarter recording a healthy growth of 15.8 percent. On a year over year comparison, the increased turnover shows robust growth of 67.5 percent. The number of listed securities was 301 in December 2008 which increased to 306 in March 2009, while the value of issued equity and debt increased merely by 4.1 percent during the quarter under review (Table VII.1). Five new companies were listed in the capital market during Q3 FY09.

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



Sector-wise DSE data show that during Q3 FY09 market capitalization increased everywhere except for banks, investment and the cement sector. During Q3 FY09, market capitalization of the banking sector declined by 35.4 percent while issued capital of the sector increased by 3.0 percent. The domination of banks, power, and pharmaceuticals in total market capitalization with significant contribution from cement industries continued up to end of September 2008. At the end of Q3 FY09, the share of banking (including NBFIs) sector in total market capitalization declined to 32 percent from 45 percent in Q2 FY09 mainly due to sharp decline in prices of banking sector stocks.

A major weakness of the country's capital market is its inability to reflect company fundamentals adequately along with the danger of insider trading in manipulating market prices. Along with measures to address these weaknesses, it would be important to reduce volatility in the market which has shown increasing trend in recent times. For sustaining the development of the capital market, it is necessary to attract nonresident Bangladeshis in increasing numbers to invest in the capital market.

VIII. Near-Term Economic Outlook

In the backdrop of the ongoing global economic crisis, the growth prospects for the developed as well as the emerging countries have deteriorated significantly over the last few months. This is mainly due to significant downturn in economic activities in the advanced economies. According to the recent update of the World Economic Outlook (WEO, March 2009 IMF), it is apprehended that advanced economies would experience their sharpest contraction in the post-World War II period. The IMF predicts that real activity could contract by 2.6 percent in the USA, 3.2 percent in the euro area, and by 5.8 percent in Japan. Though more resilient than in previous global downturns, emerging and developing economies would also suffer serious setbacks. However,