S&P Global
Ratings

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Research Update:

Bangladesh 'BB-/B' Ratings Affirmed With Stable Outlook

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Overview

- Bangladesh is experiencing a material economic slowdown owing to the COVID-19 pandemic, and we believe it will hit the government's fiscal performance.
- Nevertheless, the economy is resilient over the long term, and Bangladesh continues to benefit from modest external debt.
- We are affirming our 'BB-' long-term and 'B' short-term sovereign credit ratings on Bangladesh.
- The stable outlook reflects our expectation that the country's healthy growth prospects will overcome the risks associated with the COVID-19 pandemic over the next 12 months.

Rating Action

On Aug. 12, 2020, S&P Global Ratings affirmed its 'BB-' long-term and 'B' short-term sovereign credit ratings on Bangladesh. The outlook remains stable.

Outlook

The stable outlook reflects our expectation that Bangladesh's solid growth path will continue raising average income and prevail over risks associated with the COVID-19 pandemic in the next 12 months.

We may raise the ratings if the government materially improves its fiscal outcomes, including its very low revenue generation and increasing fiscal deficit.

We may lower the ratings if fiscal and external debt metrics weaken further. We could also lower the ratings if external debt and financing metrics worsen materially, such that narrow net external debt surpasses 50% of current account receipts plus usable reserves, and gross external financing needs exceed 100% of current account receipts plus usable reserves, on a sustained basis.

Rationale

The ratings on Bangladesh reflect the country's low economic development and diminished fiscal flexibility owing to a combination of limited revenue-generation capacity, elevated debt-servicing costs, and rising spending to address public service, infrastructure, and stimulus needs amid the COVID-19 pandemic. Administrative and institutional weaknesses represent additional rating constraints. We weigh these factors against a sound external position, reflecting support from substantial donor engagement, large remittances from overseas Bangladeshi citizens back to the country, and a globally competitive garment sector. Despite stout near-term economic hurdles, we expect Bangladesh to continue to achieve a higher-than-average rate of economic growth compared with its peers.

Institutional and economic profile: Economic resilience to be tested by COVID-19 downturn

- The Bangladesh economy decelerated significantly in the final quarter of the fiscal year ended June 2020, and will remain under pressure in the first half of fiscal 2021.
- However, Bangladesh has exhibited strong economic resilience over the past 10 years, and we expect growth to recover from the second half of fiscal 2021 onward.
- Bangladesh's political landscape constrains the effectiveness of institutions and impedes sound policymaking.

Bangladesh's economy has decelerated because of the COVID-19 pandemic, with a government-mandated lockdown from March-May significantly undermining activity in the April-June quarter. External demand, critical to Bangladesh's long-term growth prospects, has also fallen dramatically amid the pandemic, and may only recover gradually following an initial stabilization in June and July. Trade flows and associated employment in external-oriented industries, such as garment manufacturing, have been hit particularly hard. Garment shipments fell by 18.1% in fiscal 2020, with an aggressive decline in volumes in the April-June period. Employment in the garment industry is also likely to have suffered a serious blow over the same period, although recovering orders from June onward have likely led to rehiring by some firms.

After very strong growth in the first nine months through March 2020, preliminary estimates for the last quarter suggest a more modest expansion of 5.2% in fiscal 2020, the lowest in more than 10 years. We believe the drag on growth will persist in fiscal 2021, as external demand for Bangladeshi-made goods recovers at only a gradual pace. We have therefore lowered our real GDP growth forecast to 4.7% from 7.5% previously.

Low economic development, as represented by per capita GDP of about US$2,000 for 2020, remains one of Bangladesh's main rating constraints. This income level offers a weak and narrow revenue base, in turn limiting the fiscal and monetary flexibility needed to respond to exogenous shocks.

Despite the low income level and numerous structural impediments, particularly in infrastructure, Bangladesh's weighted average real per capita GDP growth of about 5.5% over 2014-2023 indicates consistently strong real economic growth. We assess its economic performance as being much stronger than sovereigns at similar income levels.

Bangladesh's economy has proven its resilience through a variety of political and financial crises over the past two decades, and we expect its strong trend growth performance to remain largely intact. The country's garment industry remains highly competitive on a global basis, with low unit labor costs and ample supply of labor. Demographics continue to favor the Bangladesh economy, and the government is working on strengthening access to key external markets ahead of its expected graduation from least developed country (LDC) status in 2024.

Bangladesh's domestic political conditions distract from stable policymaking, and this can hamper policy implementation. The confrontational stance between the ruling Awami League and opposition Bangladesh Nationalist Party (BNP) harbors the potential for conflict. Given weak institutional settings, infrastructure deficiencies, and difficult business environment, Bangladesh's foreign direct investment has remained persistently low.

The country's polarized political landscape has evolved into a highly centralized decision-making environment, which could make future policy responses unpredictable. The Awami League-led coalition swept the elections held in 2018, winning more than 80% of the parliamentary seats. A period of uncertainty followed the election results with allegations of voting irregularities by the BNP. The opposition's subsequent decision to join parliament has brought some stability to the fractious environment.

That said, the opposition's representation in parliament remains extremely small, limiting checks and balances on the government. Nevertheless, strikes and politically motivated violence have not been overly disruptive to overall economic growth in the past.

Flexibility and performance profile: Pandemic will exacerbate government's weak revenue base and high cost of borrowing

- Garment exports and worker remittances hurt by depressed consumer goods demand, lower oil prices, and a weak global labor market.
- Fiscal revenue remains low despite value-added tax (VAT) revisions in 2019, and a slower economy entails further downward pressure.
- Higher fiscal deficits and lower economic growth will push net general government indebtedness above 30% of GDP over the next three years.

Bangladesh is likely to run higher fiscal deficits as the pandemic undermines revenue generation and expenditure needs rise. We forecast the change in net general government debt will average 5.5% of GDP annually over fiscals 2021-2023 (ending June 30), materially higher than our pre-pandemic projection of 4.2%.

The Bangladesh government has introduced a variety of measures aimed at mitigating the impact of the pandemic on individuals and businesses. These measures include direct cash assistance to vulnerable segments of society, lending schemes for exporters, and working capital facilities and interest subsidies for businesses.

Thus far, these measures total approximately US$13.1 billion (4.0% of GDP), although most of that will not be direct government spending. Despite higher pandemic spending and continued efforts to boost capital expenditure over recent years, many basic social and infrastructure needs in Bangladesh remain unmet, implying higher outlays.

We expect Bangladesh's higher fiscal deficits in fiscals 2020 and 2021 to lead to a material rise in net general government debt, which we project at 33.0% of GDP by the end of fiscal 2021, versus an estimated 29.3% in the prior year.

The government continues to fund itself partially through the issuance of costly national savings certificates (NSCs), with interest rates above the market rate. While we expect the government to continue its recent shift toward less costly bank borrowing, the outstanding NSC stock, and ongoing issuance of the same, will keep its debt servicing costs above 20% of its revenues over the next few years.

Bangladesh's narrow revenue base constrains the government's flexibility to mitigate economic downturns or other potential shocks. The introduction of additional fiscal stimulus would be difficult, in our view, owing to the very limited scale of the government's revenue program.

Bangladesh has only approximately 5 million registered taxpayers (out of a population of approximately 160 million). General government revenue was less than 10% of GDP in fiscals 2018 and 2019--among the lowest of rated sovereigns globally. The government has outlined numerous initiatives to expand the tax base, culminating most notably with the introduction of new VAT rules in July 2019. The program has different VAT rates for imports, depending on economic classification, contrary to initial proposals for a single, harmonized rate.

We do not expect significant revenue increases from the initiatives to expand the tax base. In our assessment, contingent liabilities from financial institutions have a limited risk. The banking sector remains small with assets less than 100% of GDP, which informs our view of the contingent risk it poses. We classify Bangladesh's banking sector in group '9' under our Banking Industry Credit Risk Assessment (with '1' being the highest assessment and '10' being the lowest).

Although the private sector banks are in better shape, significant risks reside in state-owned commercial banks (SOCBs). SOCBs account for about 30% of total banking sector assets, and their nonperforming loans ratio is considerably higher than that of peer commercial banks.

Bangladesh's credit profile benefits from low external borrowings. The country has large remittance inflows and an internationally competitive garment export sector, resulting in a gradual decline in its current account deficit over recent years.

However, Bangladesh faces important risks to its external profile related to the COVID-19 pandemic. These risks include the weak state of the global labor market, and depressed external demand conditions. High global unemployment could undermine the generation of overseas Bangladeshi remittances back into the country. This risk is particularly acute in the Gulf states, where many Bangladeshi overseas workers reside, following the steep decline in oil prices this year. In addition, the long-running construction booms in locations such as Qatar and Dubai are nearing completion.

Although we expect export momentum to stabilize and improve after a very difficult March-June quarter, demand for Bangladeshi exports may not recover fully until 2021. Nevertheless, concomitant import compression, especially of intermediate and capital goods, should keep help to rein in the current account deficit. We forecast Bangladesh's current account deficit to remain roughly stable this fiscal year at nearly 1.5% of GDP.

In our view, Bangladesh's external balance sheet and liquidity will remain key credit-supporting factors. We expect gross external financing needs to stabilize around 87% of current account receipts plus usable reserves over 2020-2023.

This implies that the gap between the country's external debt and its liquid external assets is unlikely to reduce. Likewise, we project Bangladesh's narrow net external debt to average approximately 47.6% of current account receipts throughout the forecast period. Much lower oil prices, and an expected rebound in export demand from 2021 onward, should mitigate the gradual erosion of Bangladesh's external buffers.

Bangladesh's external profile draws substantial donor support, ensuring that the bulk of public external debt is low-cost borrowing with long maturity. Additionally, donors and multilateral lenders have in the past provided some degree of direct budgetary support, which may carry conditions for policy formulation. Since the onset of the pandemic, Bangladesh has secured considerable official creditor financing, including US$732 million in emergency assistance under the IMF's Rapid Credit Facility and Rapid Financing Instrument facilities.

We view Bangladesh's monetary assessment as a neutral factor to the rating. The central bank's limited independence, multiple mandates, and underdeveloped capital markets hamper monetary flexibility. We consider Bangladesh's exchange rate regime as a managed float, which provides some flexibility to mitigate external shocks. However, despite gradual depreciation in the exchange rate since 2015, Bangladesh's real effective exchange rate (REER) has been rising, reflecting the currency depreciation of its trading partners.

Should the REER continue to rise, it could strain the competiveness of the country's export garment sector. Bangladesh's central bank has made progress in managing inflationary expectations. Since 2015, inflation has generally remained below 6% annually.

Key Statistics

Table 1

Bangladesh - Selected Indicators

Economic indicators (%)	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**
Nominal GDP (bil. LC)	13,437	15,158	17,329	19,758	22,505	25,425	28,271	31,287	35,486	40,324
Nominal GDP (bil. $)	173	194	221	246	270	301	332	365	411	465
GDP per capita (000s $)	1.1	1.2	1.4	1.5	1.7	1.8	2.0	2.2	2.4	2.7
Real GDP growth	6.1	6.6	7.1	7.3	7.9	8.2	5.2	4.7	7.0	7.1
Real GDP per capita growth	4.9	5.4	5.9	6.1	6.7	7.0	4.2	3.5	5.8	5.9
Real investment growth	9.9	7.1	8.9	10.1	10.5	8.4	7.0	5.5	7.8	8.0
Investment/GDP	28.6	29.6	29.6	30.6	31.5	31.1	31.8	32.0	32.0	32.1
Savings/GDP	29.4	31.0	31.6	30.0	27.9	29.4	30.3	30.5	31.0	31.3
Exports/GDP	19.0	17.3	16.6	15.0	14.8	15.3	12.7	12.7	12.4	11.9
Real exports growth	3.2	(2.8)	2.2	(2.3)	8.1	10.9	(8.2)	6.0	5.5	4.5
Unemployment rate	3.5	3.5	4.2	4.2	4.0	4.0	4.0	4.0	4.0	4.0
External indicators (%)										
Current account balance/GDP	0.8	1.5	1.9	(0.5)	(3.5)	(1.7)	(1.5)	(1.5)	(1.0)	(0.8)
Current account balance/CARs	2.9	5.8	8.1	(2.6)	(17.0)	(8.0)	(8.3)	(9.0)	(6.3)	(5.3)
CARs/GDP	27.7	25.6	23.7	20.8	20.9	21.2	17.6	17.0	16.6	15.9
Trade balance/GDP	(3.9)	(3.6)	(2.9)	(3.9)	(6.7)	(5.3)	(5.4)	(4.8)	(4.4)	(4.0)
Net FDI/GDP	0.9	0.9	0.6	0.7	0.7	0.9	0.5	0.5	0.6	0.8
Net portfolio equity inflow/GDP	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross external financing needs/CARs plus usable reserves	76.6	75.0	70.8	74.7	85.1	85.5	85.9	86.5	86.9	86.5

Table 1

Bangladesh - Selected Indicators (cont.)

Economic indicators (%)	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Narrow net external debt/CARs	22.7	13.6	12.0	17.4	33.9	39.0	46.8	49.9	47.9	44.9
Narrow net external debt/CAPs	23.4	14.4	13.1	17.0	29.0	36.1	43.2	45.8	45.1	42.7
Net external liabilities/CARs	39.5	37.0	35.4	44.8	59.4	65.1	78.3	82.6	81.5	80.6
Net external liabilities/CAPs	40.7	39.2	38.6	43.6	50.8	60.3	72.3	75.8	76.7	76.6
Short-term external debt by remaining maturity/CARs	8.4	14.4	16.1	19.4	18.6	20.4	25.6	28.2	27.7	26.5
Usable reserves/CAPs (months)	4.7	5.7	6.9	7.4	6.1	5.6	6.2	6.4	6.1	6.0
Usable reserves (mil. $)	22,317	27,494	32,285	33,434	32,029	32,694	36,372	37,065	38,711	41,499
Fiscal indicators (general government; %)										
Balance/GDP	(3.1)	(3.4)	(3.7)	(4.5)	(5.6)	(5.4)	(5.5)	(6.5)	(5.2)	(4.7)
Change in net debt/GDP	1.6	1.5	3.1	2.9	3.5	5.4	5.5	6.5	5.2	4.7
Primary balance/GDP	(1.0)	(1.4)	(1.8)	(2.7)	(3.8)	(3.5)	(3.4)	(4.3)	(2.9)	(2.3)
Revenue/GDP	10.9	9.6	10.1	9.1	8.7	10.0	11.0	10.0	10.0	10.5
Expenditures/GDP	14.0	13.0	13.8	13.6	14.3	15.4	16.5	16.5	15.2	15.2
Interest/revenues	19.2	20.4	18.9	19.7	21.4	19.5	18.9	22.0	23.3	22.7
Debt/GDP	29.6	27.9	27.7	27.6	28.3	30.9	33.3	36.7	37.6	37.8
Debt/revenues	271.1	289.9	274.6	304.3	326.5	309.7	303.1	366.9	376.0	360.4
Net debt/GDP	24.1	22.9	23.1	23.2	23.8	26.5	29.3	33.0	34.3	34.9
Liquid assets/GDP	5.5	5.0	4.6	4.5	4.5	4.4	4.0	3.7	3.3	3.0
Monetary indicators (%)										
CPI growth	7.0	6.2	5.5	5.7	5.5	5.6	5.5	6.0	6.0	6.0
GDP deflator growth	5.7	5.9	6.7	6.3	5.6	4.5	5.7	5.7	6.0	6.1
Exchange rate, year-end (LC/$)	77.95	78.50	78.70	82.70	83.90	84.90	85.50	86.00	86.50	87.00
Banks' claims on resident non-gov't sector growth	18.0	14.0	16.7	19.3	13.2	9.8	13.0	13.0	13.0	13.0
Banks' claims on resident non-gov't sector/GDP	45.2	45.7	46.6	48.8	48.4	47.1	47.8	48.8	48.7	48.4
Foreign currency share of claims by banks on residents	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

Table 1

Bangladesh - Selected Indicators (cont.)

Economic indicators (%)	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Foreign currency share of residents' bank deposits	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Real effective exchange rate growth	4.3	14.2	5.7	2.4	(1.7)	5.1	0.0	0.0	0.0	0.0

Sources: Bangladesh Bureau of Statistics, International Monetary Fund (Economic Indicators); Bangladesh Bank, Central Bank of Bangladesh, International Monetary Fund (Monetary and External Indicators); Ministry of Finance (Fiscal, Debt Indicators).
Definitions: Savings is defined as investment plus the current account surplus (deficit). Investment is defined as expenditure on capital goods, including plant, equipment, and housing, plus the change in inventories. Banks are other depository corporations other than the central bank, whose liabilities are included in the national definition of broad money. Gross external financing needs are defined as current account payments plus short-term external debt at the end of the prior year plus nonresident deposits at the end of the prior year plus long-term external debt maturing within the year. Narrow net external debt is defined as the stock of foreign and local currency public- and private- sector borrowings from nonresidents minus official reserves minus public-sector liquid claims on nonresidents minus financial-sector loans to, deposits with, or investments in nonresident entities. A negative number indicates net external lending. N/A--Not applicable. LC--Local currency. CARs--Current account receipts. FDI--Foreign direct investment. CAPs--Current account payments. The data and ratios above result from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information.

Ratings Score Snapshot

Table 2

Bangladesh--Ratings Score Snapshot

Key rating factors	Score	Explanation
Institutional assessment	5	Future policy responses are difficult to predict because of increasingly centralized decision-making. Respect for the rule of law is not assured, owing to high perceived corruption and interference by political institutions.
Economic assessment	4	Based on "GDP per capita (US$)" as per Selected Indicators in table 1.
		Weighted average real GDP per capita trend growth over a 10-year period is significantly higher than peers, and among the highest in the world.
External assessment	2	Based on Narrow Net External Debt and Gross External Financing Needs/(CAR + usable reserves) as per the Selected Indicators table above.
Fiscal assessment: flexibility and performance	6	Based on "Change in net general government (GG) debt / GDP (%)" as per Selected Indicators in table 1.
		The sovereign faces shortfalls in basic services and infrastructure, as reflected, for instance, by its low ranking on the U.N. Development Program's human development index.
		The sovereign has limited ability to raise GG revenues compared with sovereigns with a similar level of development due to large informal economy and limited revenue reforms.
Fiscal assessment: debt burden	5	Based on net general government debt (% of GDP) and GG interest paid / GG revenues (%) as per Selected Indicators in table 1.
Monetary assessment	4	Bangladesh's exchange rate regime is classified as a crawl-like arrangement.

Table 2

Bangladesh--Ratings Score Snapshot (cont.)

Key rating factors	Score	Explanation
		Bangladesh Bank's operational independence is limited by perceived political interference and structural issues in monetary policy transmission.
Indicative rating	bb-	As per table 1 of "Sovereign Rating Methodology."
Notches of supplemental adjustments and flexibility	0	
Final rating		
Foreign currency	BB-	
Notches of uplift	0	Default risks do not apply differently to foreign- and local-currency debt.
Local currency	BB-	

S&P Global Ratings' analysis of sovereign creditworthiness rests on its assessment and scoring of five key rating factors: (i) institutional assessment; (ii) economic assessment; (iii) external assessment; (iv) the average of fiscal flexibility and performance, and debt burden; and (v) monetary assessment. Each of the factors is assessed on a continuum spanning from 1 (strongest) to 6 (weakest). S&P Global Ratings' "Sovereign Rating Methodology," published on Dec. 18, 2017, details how we derive and combine the scores and then derive the sovereign foreign currency rating. In accordance with S&P Global Ratings' sovereign ratings methodology, a change in score does not in all cases lead to a change in the rating, nor is a change in the rating necessarily predicated on changes in one or more of the scores. In determining the final rating the committee can make use of the flexibility afforded by §15 and §§126-128 of the rating methodology.

Related Criteria

- Criteria | Governments | Sovereigns: Sovereign Rating Methodology, Dec. 18, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- General Criteria: Methodology: Criteria For Determining Transfer And Convertibility Assessments, May 18, 2009

Related Research

- Asia-Pacific Sovereign Rating Trends Midyear 2020, July 31 2020
- Global Sovereign Rating Trends Midyear 2020: Outlook Bias Turns Negative As Governments Pile On Debt To Face COVID-19, July 30 2020
- Sovereign Risk Indicators, July 14, 2020.
- Sovereign Ratings History, July 8, 2020
- Sovereign Ratings List, July 8, 2020
- Sovereign Ratings Score Snapshot, Aug. 5, 2020
- 2019 Annual Sovereign Default And Rating Transition Study, May 19, 2020
- Sovereign Ratings And The Effects Of The COVID-19 Pandemic, April 17, 2020
- Up Next: The Complicated Transition From COVID-19 Lockdown, April 17, 2020
- COVID-19 Deals A Larger, Longer Hit To Global GDP, April 16, 2020

- Sovereign Debt 2020: Global Borrowing To Increase To $8.1 Trillion Amid Favorable Financing Conditions, Feb. 20, 2020
- Bangladesh 'BB-/B' Ratings Affirmed; Outlook Stable, May 30, 2019

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

Ratings Affirmed	
Bangladesh	
Sovereign Credit Rating	BB-/Stable/B
Transfer & Convertibility Assessment	BB-