

Box

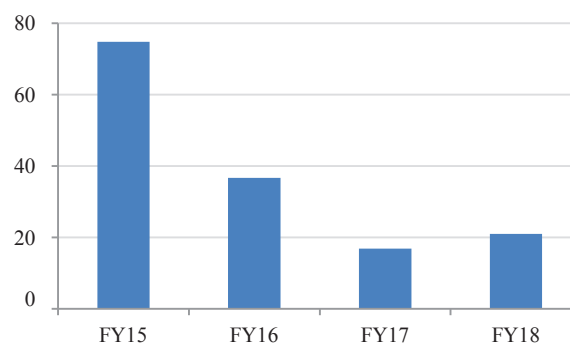
Box-1

Foreign Exchange Market Dynamics in Bangladesh"

Foreign exchange market dynamics in Bangladesh has been evolved overtime in tandem with increasing openness of the economy including import, export and remittances growth. During FY15-FY18, a mixed trend was observed in interbank foreign exchange transactions volume. The foreign exchange market is segmented in two categories based on market participants i.e. interbank and other than interbank. Authorized dealers (scheduled banks) and Bangladesh Bank are engaged in interbank transactions while both banks and money changers are engaged in transactions with the business entities and individuals. Currently 59 scheduled banks with 1010 branches and 225 money changers are doing their foreign exchange business in the country. Banks (authorized dealers) are the dominant player because remittance, exports and imports proceeds are solely transacted through banking channel, while a part of the foreign exchanges are transacted by the money changers within the country.

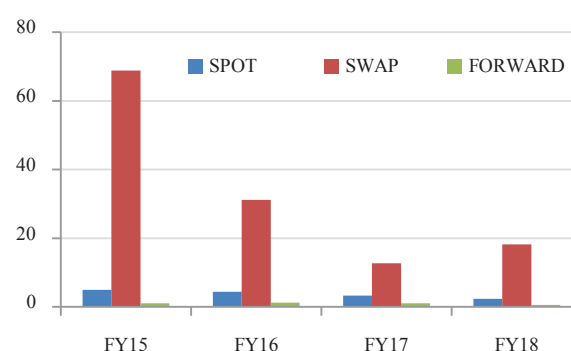
Transactions in the inter-bank market are comprised of spot, forward and SWAP basis. The SWAP is typically used for liquidity support and as a hedging tool against the market risks. Presently SWAP transaction occupies the major share (86 percent) in the interbank foreign exchange market of Bangladesh (Chart 2 and 3).

Chart 1: Volume of foreign exchange transaction in the inter-bank (In billion USD)



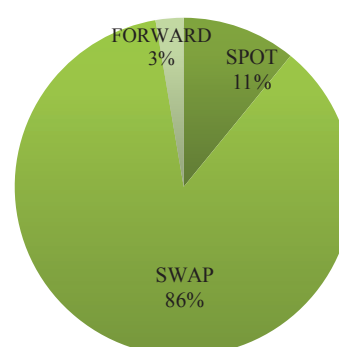
Source: Bangladesh Bank.

Chart 2: Interbank foreign exchange Transaction by Type (In billion USD)



Source: Bangladesh Bank.

Chart 3: Share of inter-bank transaction by type in FY18 (In percent)



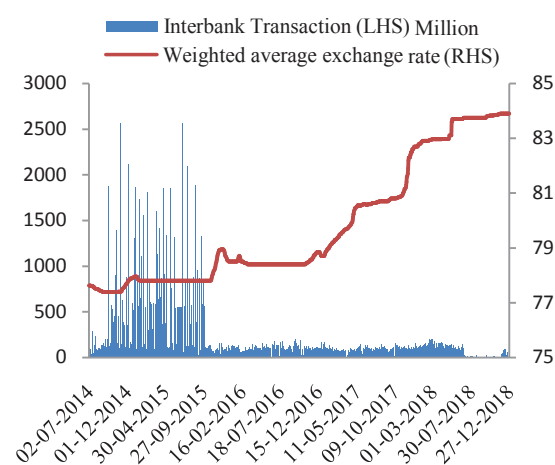
Source: Bangladesh Bank

* The note is prepared by a team comprising of Md. Sakhawat Hossain, Md. Yousuf and Md. Ezazul Islam of Chief Economist's Unit and Mohammad Iftakhar Awal Bhuiyan, Forex Reserve and Treasury Management Department. The views expressed in the paper are authors' own and do not reflect those of Bangladesh Bank..

Authorized dealers deal in some major foreign currencies mainly US dollars, euro, Japanese yen, and pound sterling in the interbank market. More than 95 percent currency transactions occurred in USD.

In order to avoid exchange rate volatility, BB actively participates in the foreign exchange market. BB updates foreign exchange transactions guideline on a regular basis to align the foreign exchange market with the economic fundamental. In FY18, BB sold USD 2.31 billion (net) in the market as against bought of USD 1.77 billion (net) in FY17.

Chart 4: Exchange rate movements and daily turnover foreign exchange transactions



Source: Bangladesh Bank

The movement of nominal exchange rate was negatively associated with current account balance (the coefficient of correlation is -0.7885) for the period of Q1FY14 to Q2FY19 in Bangladesh. The relationship between daily turnover and nominal exchange rate also found a negative association (the coefficient of correlation is -0.27)

The analysis (an ARCH estimation on daily transaction data for the period FY15-FY18) shows that both the exchange rate and transaction volume of Bangladesh in the foreign exchange market is less volatile than that of India. The volatility of the foreign exchange market depends on markets participants, size of market, product derivatives, and level of intervention for maintaining stability.

Although the foreign exchange market in Bangladesh is very swallow compared with neighboring countries in terms of turnover and product derivatives, evolving market dynamics gradually is noteworthy. It is likely that the depth of the market will increase in near future due to expanding openness of the economy.