Part A: Economic and Financial Developments

Overview and Executive Summary

Macroeconomic balances were under significant pressure in Q1 and Q2 FY 11, with high domestic credits growth trends of FY12 continuing in H1FY12, particularly in the public sector due to sudden sharp decline in net external financing inflows and rising fiscal burdens of energy and agricultural input price subsidies. Sharp spike in government borrowing from the banking system created severe liquidity stress on primary dealer banks with consequent stress on private sectors credit access from them.

Import and export growth came down from the very high Q4 FY11 levels (44 and 50 percent) towards trend levels in Q1FY12 (to 27 and 21 percent respectively), with the higher import growth from higher base sending current account balance to negative. Coupled with high domestic credit growth the worsened bop current account balance meant declining net foreign assets and foreign exchange reserve, with attendant depreciation pressure on Taka.

Annual average CPI inflation at double digit levels since March 2011 continued creeping upward in Q1 & Q2, FY 12, further away from single digit level targeted for FY 12.

Both fiscal and monetary authorities responded proactively in Q3FY12 with corrective measures to restore balance. The government raised administered user prices of energy in successive rounds to reduce fiscal subsidy burden; trimmed some ADP expenditure allocations and focused increased attention on utilization of foreign aid in pipeline. On the monetary front, BB's H2FY12 monetary policy stance actively pursued slowing down of domestic credit allowing the bulk of repo liquidity available only at 'special' rate 300 basis points higher than the usual 7.75 percent rate applied on liquidity support to primary dealers. Besides the higher cost of domestic credit, depreciation of Taka also helped trim credit demand, bearing down on non-essential imports. While adopting this tighter monetary stance BB's credit policies maintained a directional bias seeking to provide adequate credit for productive pursuits including those of farm and non-farm SME's while discouraging credit growth for unproductive uses and conspicuous consumption.

The cautious, restrained fiscal and monetary stance adopted in H1FY12 started showing positive result by Q3FY12. Fiscal deficit narrowed, with domestic financing coming down and foreign financing rising back from earlier low levels. On the monetary front domestic credit growth slowed to 22.45 percent in Q3FY12 from 25.94 percent of preceding quarter, with positive build up in net foreign assets. BOP current account balance turned back to positive in Q2FY12 and the overall balance also rose in Q3FY12, and exchange rate of Taka stabilized by February 2012 following substantial depreciation against USD in preceding months. Export growth continued weakening despite Taka depreciation, mainly due to demand weakness in the traditional European and North American markets.

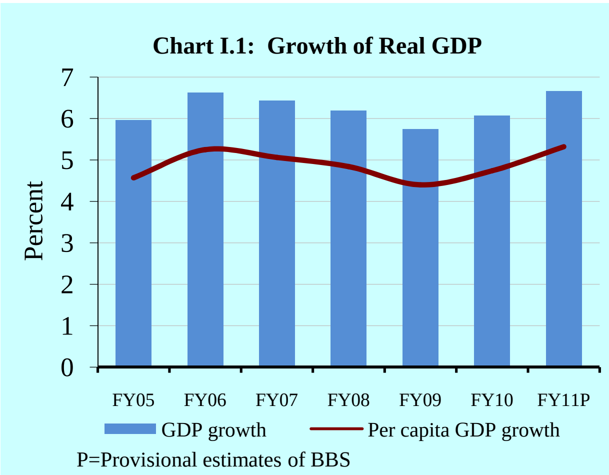
In the real economy, agricultural output activities remain healthy, aided by continuance of favorable weather. Despite slower growth in export related manufacturing, robust domestic demand has sustained positive growth in quantum index of manufacturing output, both in larger scale and small scale units. Import of capital machinery slowed down in Q2 and Q3 of FY12, but this may be of no immediate growth concern, with substantial spare installed capacity in manufacturing units. On the whole the economy remained on course in attaining the targeted real GDP growth of 6.5-7.0 percent.

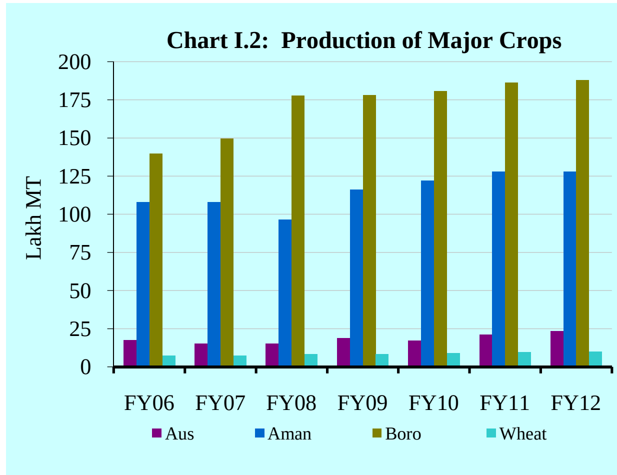
The impact of tightened monetary stance on CPI inflation has been slower to show up, particularly due to repeated rounds of hikes in administered user prices of electricity and gas, raising non-food CPI inflation, although food CPI inflation came down significantly by February 2012. Overall annual average CPI inflation has also started declining by March 2012, to 10.10 percent from 10.43 percent of the preceding month.

Both fiscal and monetary policies will need to continue on cautious stance for Q4FY12 and further on, until inflation settles down at single digit target level and until foreign exchange reserves rise back to ten billion plus levels. Policy and structural reforms to attract higher domestic and foreign investments for fuller realization of the economy's inclusive growth potentials will need to be pursued and hastened, for faster sustained growth in output and employment over the medium and longer term.

I. Developments in the Real Economy

1.1 During Q3 FY12, trends in major real economic indicators remained mostly stable reflected in bumper agricultural production and well supported by higher industrial production and foreign trade. Steady growth in exports and imports, inflows of worker remittances, increased financing in trade, working capital and term lending and construction, higher credit flows to agricultural sectors and SMEs including transport and communication contributed significantly to uphold the real sector activities. Strong domestic demand is likely to play its part to support expected real economic growth in coming year.





1.2 Agriculture sector showed a moderate output growth in Q3FY12, reflecting in bumper aus harvest with maintaining similar growth rate of aman production. Directorate of Agricultural Extension (DAE) estimates the production of *boro* rice crop at 18.78 mmt for FY12 as against yearly target of 18.7 mmt. Favorable weather condition, proper distribution of high quality seeds, adequate and timely supply of electricity, availability of fertilizers and pesticide, disbursement of agricultural input subsidy and better access to institutional agricultural credit contributed *boro* bumper production. In FY12, the actual production of wheat stood at 0.99 mmt, which was 2.06 percent higher than the actual production of FY11. Although jute and potato production recorded marginally lower growth, the production of *aman* and *aus* stood at 12.8 mmt and 2.33 mmt respectively in FY12 which were 0.08 percent and 9.4 percent higher over the actual production of FY11.

1.3 In order to boost up agricultural production for food security and generate employment in the rural area, BB has set targeted disbursement of agricultural credit of Tk. 138 billion for FY12 which is 9.38 percent higher than that of Tk. 126.2 billion for FY11. During nine months of FY12, about 66.6 percent of the yearly target of disbursement was achieved. Agricultural credit disbursement and recovery through commercial banks remained healthy in the current quarter. Disbursement of agricultural credit by commercial banks stood at Tk. 34.6 billion in Q3FY12 which was 18.1 percent higher than the actual disbursement in Q3FY11 (Table-I.10). Of this amount, Tk.14.5 billion went to crop sector, Tk. 4.6 billion to poverty alleviation, Tk. 2.9 billion to livestock, Tk. 2.7 billion to fisheries, Tk. 0.9 billion to agricultural equipment, Tk. 0.5 billion to grain storage & marketing and Tk. 0.4 billion to irrigation. Total recovery of loan stood at Tk. 24.5 billion during Q3 FY12 as against the recovery of Tk. 28.4 billion in the same quarter of the previous fiscal year. The outstanding of agricultural credit increased from Tk. 235.9 billion at the end of December 2011 to Tk. 242.7 billion at the end of March 2012.

Chart I.3: Quantum Index of Manufacturing Output

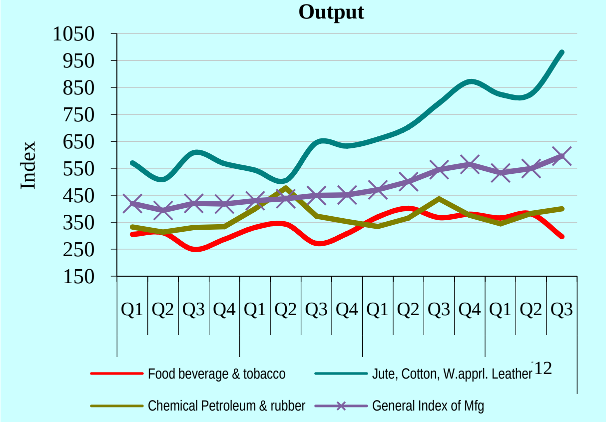
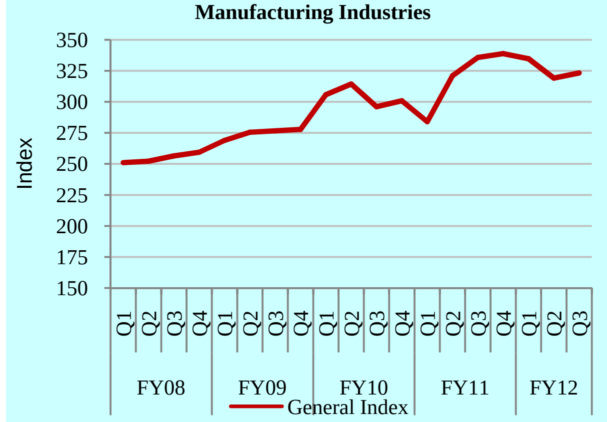


Chart 1.4: Quantum Index of Small Scale Manufacturing Industries



1.4 The buoyant activities of the overall industry sector's in Q2 FY12 also continued in Q3 FY12, reflecting in manufacturing production index. Industrial production, in terms of quantum general index (large and medium manufacturing), increased by 9.23 percent during Q3FY12 over Q3FY11 which is 8.4 percent higher than the previous quarter. The 'Jute, Cotton, RMG & Leather' subsector, the highest weighted subsector, grew by 23.9 percent during Q3FY12 over the level of Q3FY11. The 'fabricated metal product', 'paper and paper products' subsector increased by 13.95 percent and 4.1 percent respectively during Q3FY12 over Q3FY11 (Table-I.5). On the other hand 'Chemical petroleum and rubber', 'Food beverage and tobacco' and 'Basic metal' subsector' declined by 8.38 percent, 19.2 percent, and 13.9 percent respectively during the quarter under review over corresponding period of FY11. The quantum general index of small scale manufacturing industries grew by 1.27 percent to 323.28 in Q3 of FY12 as compared to 319.23 during the preceding quarter of FY12. Banks and financial institutions, disbursed Tk.77.55 billion of industrial term loan during Q3FY12 which was 2.53 percent higher over Q3FY11 (Table-I.12).

1.5 The disbursement target of SME loan has been set at Tk. 590.13 billion for 2012. Against this target, disbursement of SME loan stood relatively lower at Tk. 142.81 billion during January–March 2012 which is 24.2 percent of annual target. At the end of Q3FY12, outstanding position of SME loans stood at Tk. 886.70 billion as against the amount of Tk. 810.99 billion at the end of Q2FY12.

1.6 Service sector activities witnessed up trend during Q3 of FY12, reflecting as many as indirect indicators. Service sector activities largely depend on agricultural and industry sector performances. The increase of service sector activities in transport, storage and communication subsector was primarily due to increase in merchandise exports in Q3FY12. Bank advances on transport and communication registered an annual growth of about 73.3 percent in Q3FY12 as against the growth of 46.7 percent in Q3FY11. Trade financing grew by about 20.4 percent during the quarter under review over the level of Q3FY11. Cargo handled by Chittagong port shows that about 10.0 million ton imports and 1.26 million ton exports had been handled in Q3 FY12. In Q3FY12 disbursement of SME loan in service sector stood at Tk. 8.26 billion which is 17.54 percent higher than the level of Q3FY11. Transport, storage and communication sub-sector, constitute about 10.91 of GDP, activities grew during first nine months of FY12 compelled by particularly mobile phone services stemmed from increased consumer demand. The mobile phone subscriber reached 89.46 million at the end March 2012 from 85.46 million at the end December 2011.

II. Money and Credit Market Developments

2.1 Bangladesh Bank (BB) continued to pursue a cautiously restrained monetary stance adopted for FY12 to curb inflationary expectations and external sector pressures, while ensuring adequate private sector credit to stimulate production oriented inclusive growth during the second half of FY12. BB’s monetary policy specifically aimed to contain reserve money growth to 12.2 percent and broad money growth to 17.0 percent by June 2012 and credit to the private sector is programmed to remain at a 16.0 percent (January, 2012, MPS). As a result, the growth of various monetary aggregates (M1, M2), reserve money (RM), private sector credit slow down during Q3FY12 compared with the same period of the preceding year. However, domestic credit growth increased by 22.45 percent (y-o-y) in Q3FY12 compared with 28.95 percent growth during the same period of the preceding year. During Q3FY12, the total private sector credit by banks, non-bank and microfinance institutions grew by 18.8 percent (y-o-y) as against 27.9 percent during the same period of the preceding year. In view of containing inflation and inflationary expectations BB raised its policy rates, namely repo and reverse repo rates by 50 basis points in H2FY12 and also other short and long term Treasury bill rates, lending and deposits rates during the quarter under report.

Chart II.1: Components of Reserve Money

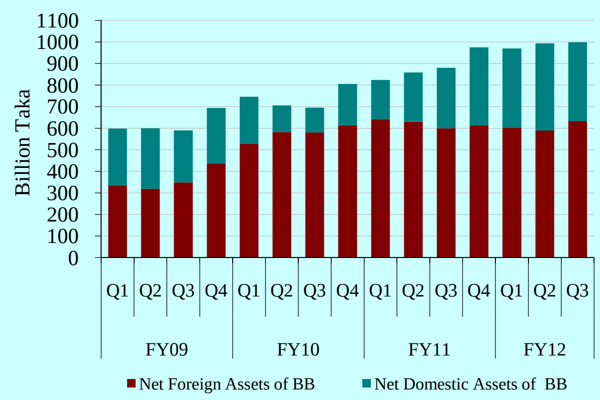
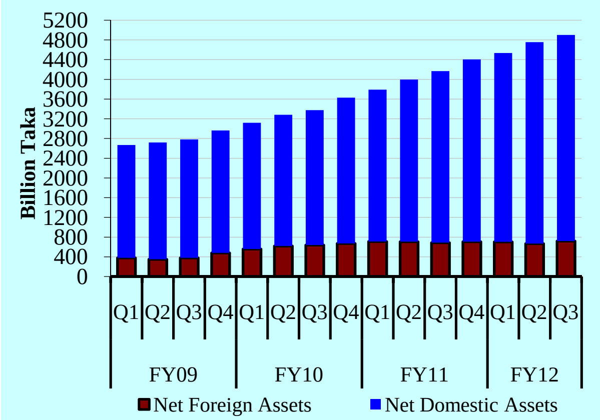


Chart II.2: Components of Broad Money



2.2 Provisional data show that M2 experienced a growth of 17.60 percent (y-o-y) and stood at Tk.4903.2 billion at end March, 2012 fueled mainly by 20.19 percent growth in NDA resulting from increased credit to the public and private sectors. The growth of M1 increased by 6.56 percent at end March, 2012 which increased by 28.90 percent during the same period of the preceding year mainly due to sharp decline in demand deposits growth rate of banks.

2.3 A look at the components of M2 shows that currency, demand deposits and time deposits increased by 11.91 percent, 0.62 percent and 21.09 percent (y-o-y) respectively during Q3FY12 as compared with 24.84 percent, 33.55 percent and 21.90 percent respectively during the same period of the preceding year. The money multiplier (M2/RM) increased by 4.26 in Q3FY12 from -3.09 during the same period of the preceding year. The increased of multiplier was influenced by the expansion of more M2 than RM.

2.4 The RM grew by 13.54 percent (y-o-y) and stood at Tk. 999.4 billion in March, 2012 which experienced a 24.87 percent (y-o-y) growth during the same period of the preceding year. This occurred due to significant growth in NDA by 30.88 percent despite moderate growth in NFA by 5.47 percent. The significant growth in NDA mainly resulting from a substantial increased in claims on banks and also claims on the public sector by 15.62 percent and 63.31 percent respectively in Q3FY12 which increased by 185.78 percent and 64.00 percent respectively during the same period of the preceding year.

Chart II.3: Trends in Private Sector Credit

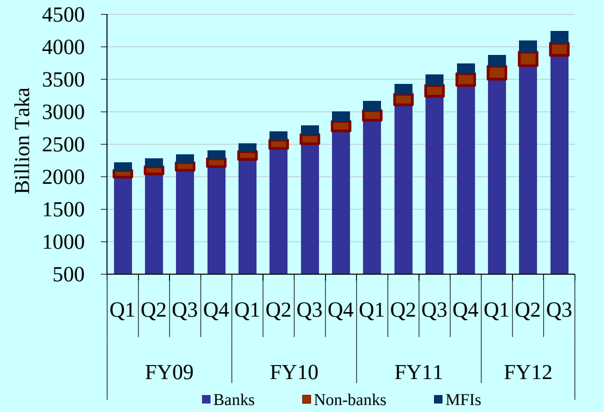
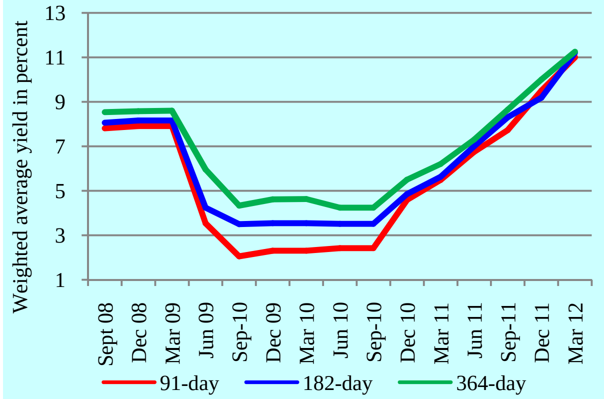
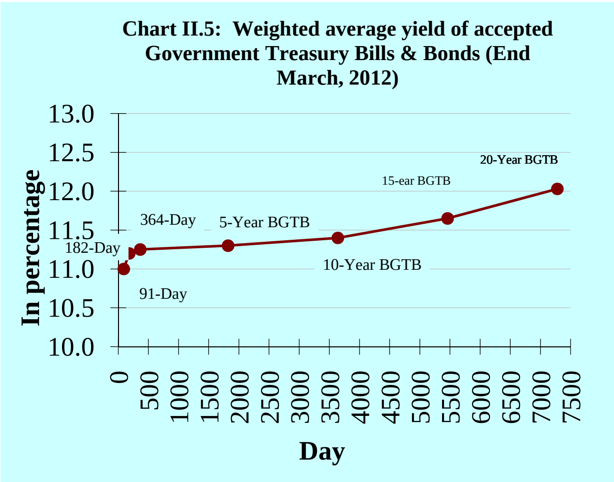


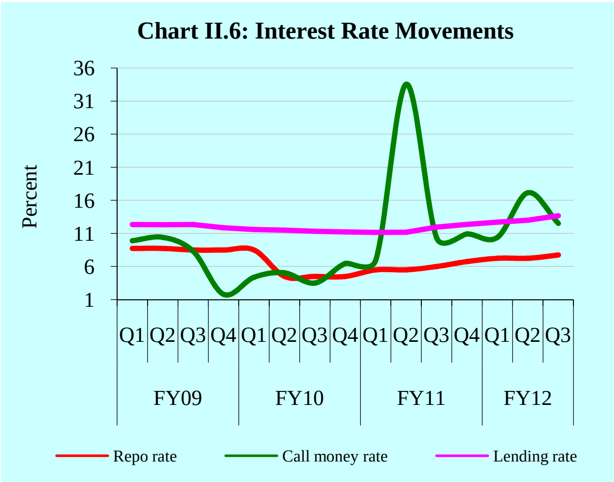
Chart II.4: Yield on T-Bills



2.5 The total advances by economic purposes increased by 19.9 percent and stood at Tk. 3533.7 billion in Q3FY12 which was increased by 28.1 percent during the same period of the preceding year. An analysis of trends of the bank advances to private sector shows that bank lending toward transport and communication, construction, storage, trade, industry sectors increased significantly during the current quarter. Bank advances to the transport and communication sector increased significantly by 73.3 percent compared with 46.7 percent during the same period preceding year. Credit to the construction and industry sectors increased by 36.5 percent and 20.1 percent respectively in Q3FY12 which increased by 40.7 percent and 24.3 percent during the same period of the preceding year. Credit to storage sector increased by 30.3 percent in Q3FY12, which was increased by 8.1 percent during the same period of the preceding year. Credit to the trade sector increased by 20.4 percent in Q3FY12, compared with 31.6 percent increase during the same period of the preceding year. The growth rate of credit to the agriculture sector remained the same (however, of which crops increased slightly by 0.3 percent and others declined by 2.5 percent) in Q3FY12, which increased by 26.7 percent (of which crops by 25.0 percent and others by 46.3 percent) in Q3FY11. However, on account of the first nine months of FY12 crops loan grew by almost 12.0 percent over the same period of the preceding year. Credit to the working capital financing increased by 10.7 percent in Q3FY12 as against 22.8 percent during the same period of the preceding year.

2.6 The disbursement of term lending by banks and NBFIs increased by 2.53 percent and stood at Tk. 77.55 billion at end Q3FY12, which was Tk. 75.63 billion during the same period of the preceding year. Between Q3FY11 and Q3FY12, term lending by PCBs actually increased from Tk. 52.26 billion to Tk. 52.80 billion, SCBs term lending increased from Tk. 8.92 billion to Tk. 11.44 billion, while term lending by FCBs decreased from Tk. 4.29 billion to Tk. 2.58 billion, and by NBFIs deceased from Tk. 7.98 billion in Q3FY11 to Tk. 6.32 billion in Q3FY12. However, the term lending by specialized banks increased from Tk. 2.19 billion to Tk. 4.40 billion during the same period.





2.7 In line with the policy stance of BB, the repo and reverse repo rates were increased by 50 basis points and stood at 7.75 percent and 5.75 respectively in March, 2012 making a total of 325 basis points increase in FY11-12 to contain inflation and inflationary pressure emanating from various domestic and international factors. Likewise, overall yields on short term treasury bills e.g., 91-day increased to 11.00 percent in March, 2012 from 5.48 percent in March, 2011, while 182-day, 364-day treasury bills rates also increased to 11.20 and 11.25 percent at end of March, 2012 from 5.63 and 6.20 percent respectively at the end of March, 2011. Long-term bond such as 5-year and 10-year increased to 11.30 and 11.40 percent at the end of March, 2012 from 8.26 percent and 9.36 percent in March, 2011 (Table II.3), while the yields on 15-year, and 20-year BGTB both also increased from 9.20 percent and 9.63 percent respectively to 11.65 and 12.06 percent in March, 2012. The call money rate was 12.51 percent at the end of March, 2012 which was 10.35 percent at the end of March, 2011 due to increased credit demand in the private sector. The outstanding stock of NSD certificates in March, 2012 stood at Tk. 634.6 billion against Tk. 640.2 billion in March, 2011 despite an increase in the 3-Year and 5-Year NSD certificate rate to 12.59 percent and 13.19 percent in Q3FY12 from 10.00 percent and 10.50 percent respectively in Q3FY11.

III. Fiscal Developments

3.1 During the first three quarters (July-March) of FY12, the pace of fiscal developments remained mostly in line with the yearly targets set in FY12 budget. During the period, preliminary estimates of total revenue collection and total expenditure, as percent of GDP, stood at 9.07 percent and 11.94 percent as against the yearly targets of 13.16 percent and 18.18 percent respectively for FY12. Preliminary estimate of overall fiscal deficit, during July-March of FY12 stood at Tk. 258.2 billion as against the yearly target of Tk. 452.0 billion (5.02 percent of GDP). The deficit financing during July-March of FY12 amounted to Tk. 258.2 billion of which Tk. 193.0 billion was accommodated from domestic sources comprising bank financing of Tk. 179.1 billion and non-bank financing of Tk. 13.9 billion while the remaining amount of Tk. 65.3 billion came from foreign sources.

Chart III.1: Trend in Government Revenue and Expenditure

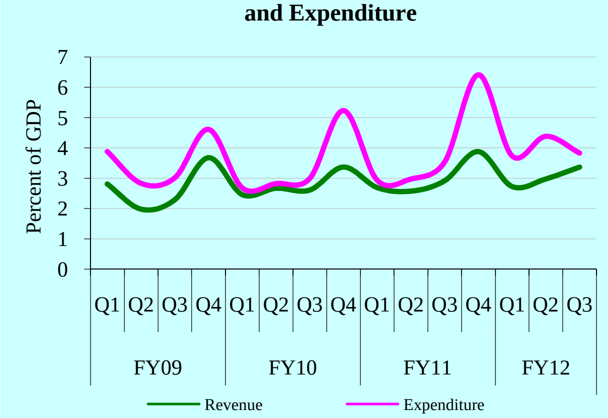
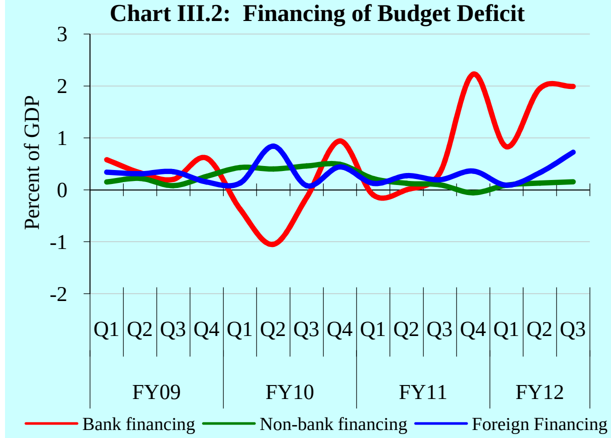


Chart III.2: Financing of Budget Deficit



3.2 During the first three quarters of FY12, NBR collected Tk. 629.0 billion tax revenue as against the yearly target of Tk. 918.7 billion for FY12, which is 18.4 percent higher than the amount stood in July-March, FY11. The tax revenue growth was led by income tax, other sources[1], custom duty, and value added tax (VAT). In the first three quarters, tax revenue

[1] Other sources include supplementary duty (local and import), excise duty, turnover tax, and travel tax.

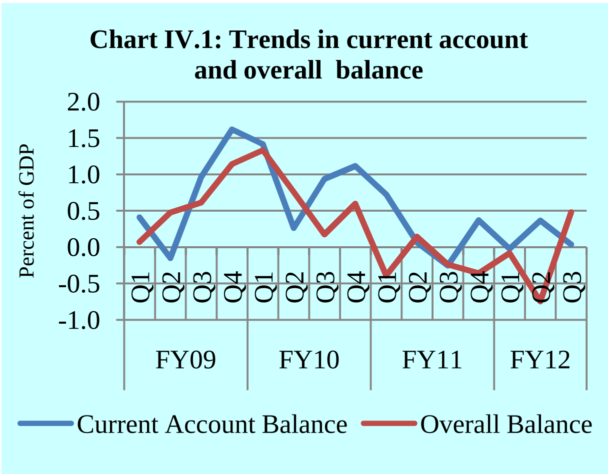
collected from income tax, other sources, custom duty and VAT increased by 27.8 percent, 19.3 percent, 14.7 percent, and 13.5 percent respectively over the same period of last year. Total revenue earning is estimated at Tk. 816.4 billion during July-March, FY12 as against the yearly target of Tk. 1183.9 billion, which is 26.7 percent higher than the actual level of July-March, FY11.

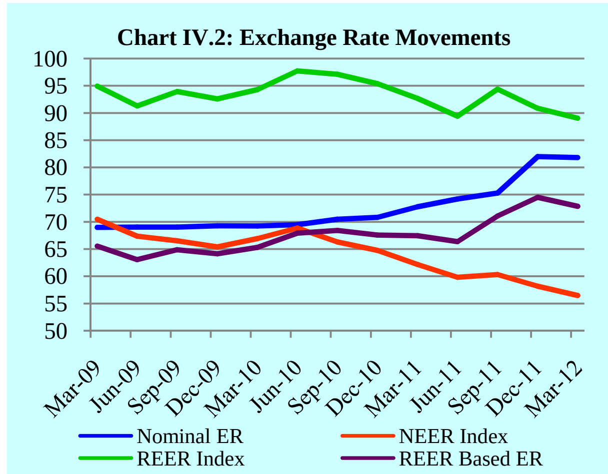
3.3 During the first three quarters of FY12, total government expenditure is estimated at Tk. 1074.7 billion (against annual target of Tk. 1635.9 billion) which is 45.0 percent higher than the amount stood in July-March FY11 and 65.7 percent of annual target. In Q3 of FY12, current expenditure increased by 11.1 percent over the same period of FY11 due mainly to increasing expenditure on subsidy for both agricultural and export sector. Provisional data on ADP expenditure show that Tk. 206.2 billion was utilized during first three quarters (July-March) of FY12 which is 44.8 percent of the annual allocation of Tk. 406.0 billion and 17.5 percent higher than the same period of previous year.

3.4 During Q3FY12, overall fiscal deficit stood at Tk. 41.4 billion which is .46 percent of GDP. Of which Tk. 5.9 billion came from domestic sources including bank financing of Tk. 3.3 billion and non-bank (through NSD) financing of Tk. 2.6 billion while the remaining Tk. 35.5 billion came from foreign sources.

IV. External Sector Developments

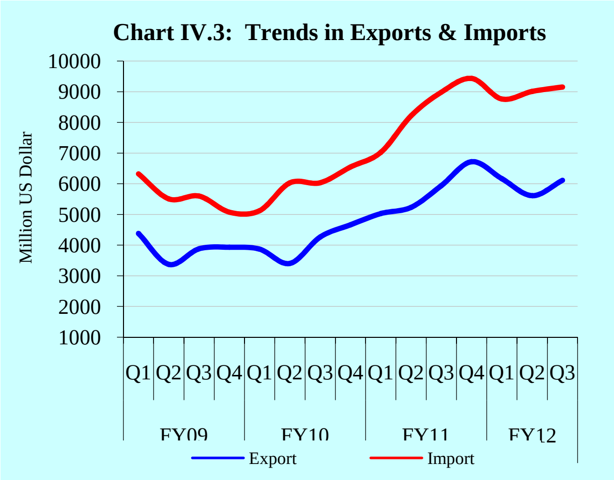
4.1 The current account balance (CAB) remained in the surplus position in Q3FY12 due to higher inflows of current transfer. During Q3FY12, surplus in the current transfer increased to USD 3.46 billion compared to USD 3.08 billion of Q3FY11. Workers' remittances, contributed most of total current transfer amounting at USD 3.46 billion in Q3FY12 compared to USD 3.06 billion in Q3FY11. As a result, despite the deficit trade balance (USD 2.39 billion), the CAB recorded USD 0.04 billion surplus during the quarter (January-March FY12) against USD 0.44 billion surplus during the previous quarter and USD 0.28 billion deficit during the same quarter of FY11. The net services account showed a deficit of USD 0.62 billion during Q3FY12 against a deficit of USD 0.64 billion in the same quarter of previous fiscal. Deficits in income account increased to USD 0.41 billion during the quarter under review compared to a deficit of USD 0.34 billion in Q3FY11. Deficits in the capital and financial account stood at USD 0.10 billion during Q3FY12 against a deficit of USD 0.53 billion in Q2FY12 while in Q3FY11 it was in the surplus position of USD 0.04 billion. Overall, the balance of payment maintained a surplus of USD 0.58 billion during Q3FY12 against a deficit of USD 0.26 billion during the same period of FY11 and thus the foreign exchange reserve stood at USD 9.58 billion at end March 2012.

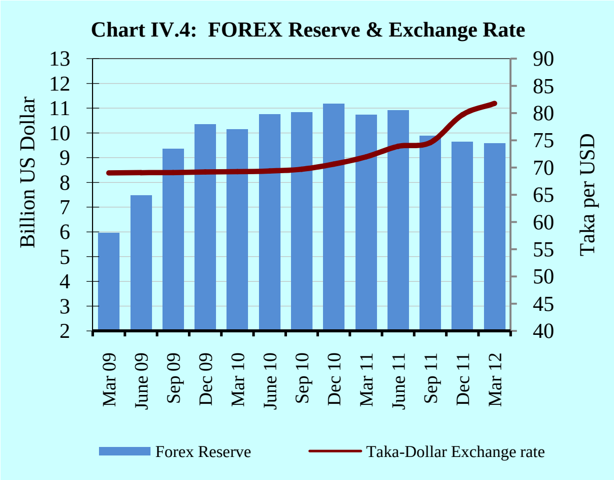




4.2 Despite some movements, the foreign exchange market remained mostly stable during Q3FY12. The Taka-Dollar exchange rate got higher in January'12 with a depreciating pressure on Taka against major international currencies due to increased demand for foreign currencies due to high import payments especially high fuel/oil import cost in the context of less than expected growth of exports and remittance inflow. Since February'12 Taka-Dollar exchange rate started moderating and continued till the end of March 2012. The weighted average nominal exchange rate stood at Taka 81.76 per USD at the end of March'12, against Taka 79.67 per USD at the end December'11 and Taka 73.88 per USD at the end of June'11. The REER based exchange rate decreased to Taka 72.87 per USD at end March'12 from Taka 74.51 per USD at end December 2011, indicating sufficient room of external trade competitiveness during Q3FY12 in spite of appreciating tendency of Taka against USD at the end of March 2012.

4.3 Export earnings registered only 1.9 percent growth during Q3FY12 and stood at USD 5.83 billion (on adjusted fob basis) against USD 5.72 billion recorded during the corresponding quarter of the previous fiscal year. During Q3FY12 the export of woven garments (+14.0 percent) recorded higher growth while exports of raw jute (-12.0 percent), jute goods (-21.9 percent), tea (-36.9 percent), frozen food (-16.8 percent) and terry towels (-21.5 percent) declined at various degrees compared to corresponding quarter of FY11 (Table IV.2).





4.4 Import payments recorded 1.5 percent growth (on adjusted fob basis) to USD 8.22 billion during Q3FY12 compared to USD 8.10 billion imports recorded during corresponding quarter of FY11 (Table IV.3). Import of food grains decreased sharply by 69.1 percent during Q3FY12 to USD 167.3 million compared to USD 541.9 million recorded during Q3FY11 resulting in 92.4 percent (USD 20.90 million against USD 275.9 million) rice import decrease and 45.0 percent (USD 146.4 million against USD 266.0 million) wheat imports decrease during the period. On the other hand, imports of other food items increased by 114.9 percent during the quarter under review of which imports of milk & cream (+26.0 percent), spices (+14.3 percent), oil seeds (+47.6 percent), edible oil (+168.2 percent) and sugar (+161.0 percent) increased while imports of pulses decreased (-40.2 percent).

4.5 Imports of intermediate goods mainly used for manufacturing output increased by 0.3 percent during Q3FY12. Among the intermediate goods imports of clinker (+17.3 percent), crude petroleum (+90.3 percent), POL (+5.5 percent), pharmaceutical products (+35.0 percent), fertilizer (+10.8 percent), dyeing and tanning materials (+1.2 percent), plastic and rubber articles thereof (+10.1 percent), textile and articles thereof (+11.5 percent) and staple fibre (+122.0 percent) increased while imports of chemicals (-7.2 percent), raw cotton (-40.5 percent) and yarn (-16.6 percent) decreased. Imports of capital goods and others recorded 0.2 percent decline in Q3FY12, of which imports of iron, steel and other base metals increased by 26.7 percent while imports of capital machinery (-19.8 percent) and other capital machineries (-1.4 percent) decreased.

4.6 The inflow of workers' remittance increased by 13.2 percent to USD 3.46 billion during Q3FY12 compared to USD 3.06 billion in Q3FY11. In spite of some risk factors like political unrest in some countries, the inflow of workers' remittance managed to rebound in the double digit growth (10.7 percent) during July-March period of FY12. During Q3FY12 remittances from Gulf region recorded 21.6 percent growth of which Saudi Arabia recorded 22.7 percent, UAE recorded 24.5 percent, Oman recorded 21.7 percent, Bahrain recorded 79.1 percent, Qatar recorded 10.5 percent and Kuwait recorded 5.9 percent growth. Remittances from the euro region recorded 21.0 percent growth and Asia pacific region recorded 39.8 percent growth while remittances from rest of the world (including USA) decreased by 19.2 percent of which remittance from USA declined by 27.3 percent during the quarter under review. The major sources of remittance during the quarter was Saudi Arabia (USD 1005.8 million) as usual, followed by UAE (USD 665.9 million), USA (USD 388.0 million), Kuwait (USD 290.9 million), and UK (USD 275.9 million) (Table IV.4).

V. Price Developments

5.1 Point to point CPI inflation continued its declining trend since the closing month of Q3 of FY12 (March, 2012) resulted a decline in twelve-month average CPI inflation in the closing month of Q3 of FY12 though remained elevated at double digit level. Point to point CPI inflation declined to 10.10 percent in March 2012 from 10.63 percent in December 2011 due mainly to declining food inflation. Point to point food inflation declined significantly from 10.40 percent in December 2011 to 8.28 percent in March 2012. On the other hand, with continuation its upward surge non-food inflation climbed to 13.96 at faster pace in March 2011 from 11.38 percent in December 2011. Food inflation was more acute in urban areas whereas non food inflation was

Chart V.1: 12-Month Average CPI Inflation

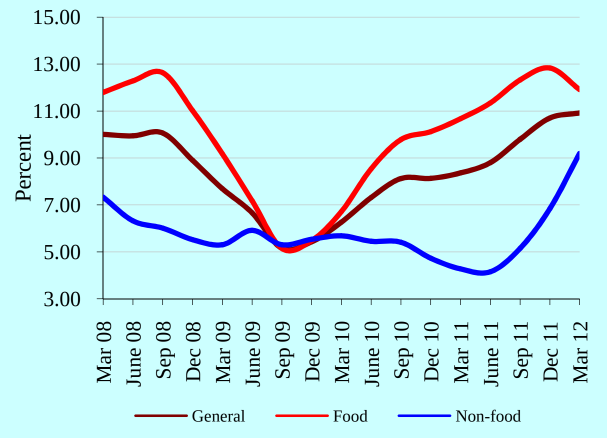
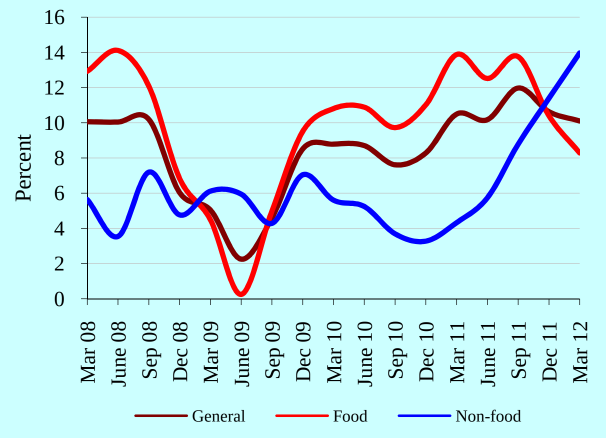


Chart V.2: 12-Month P-to-P CPI Inflation



more pronounced in rural areas. Though 12-month average CPI inflation started to declined since the closing month of Q3 FY12 (March 2012), still it was higher at 10.92 percent compared to 10.70 percent in the last month of previous quarter, as point to point inflation remained elevated for a long time.

Table-5.1

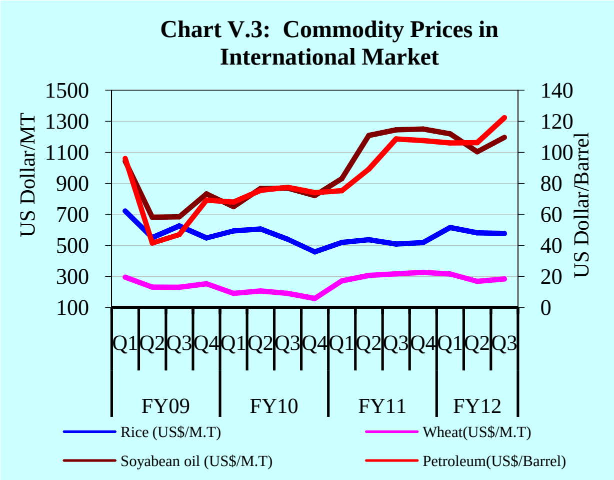
Contribution@ of Food and Major Non-Food Items / Groups in CPI inflation(Q-o-Q)

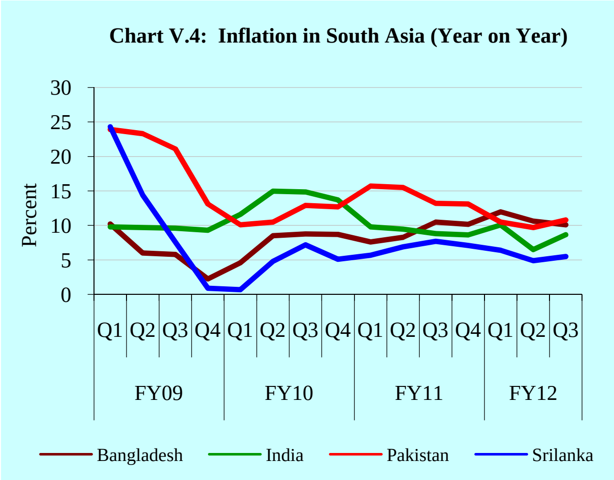
Base Year (1995-96)=100

Months	**Food beverage & tobacco**	Clothing & Footwear	Gross rent, Fuel & Lighting	Furniture, Furnishing & Other	Medical care and Health Expenses	Transport & Communications	Recreation, Entertainment, Education & Cultural Services	Misc. Goods & Services	**Non-food**
Weight	**58.84**	6.85	16.87	2.67	2.84	4.17	4.13	3.63	**41.16**
Jan-11	76.22	4.86	4.29	3.37	1.17	2.35	2.34	5.40	23.78
Feb-11	80.05	4.76	5.15	1.29	1.12	2.87	1.59	3.17	19.95
Mar-11	72.04	6.43	7.22	1.54	1.80	4.38	2.14	4.45	27.96
Apr-11	68.04	7.65	10.03	2.64	2.09	5.20	1.22	3.14	31.96
May-11	-60.68	36.06	29.64	14.00	10.79	41.65	3.33	25.21	160.68
Jun-11	33.82	14.89	10.93	5.07	2.77	18.51	1.08	12.92	66.18
Jul-11	64.82	10.45	5.06	2.30	1.29	8.57	0.51	7.00	35.18
Aug-11	64.55	14.24	10.17	2.10	0.58	3.82	0.55	3.98	35.45
Sep-11	72.86	11.26	8.87	1.76	0.53	2.23	0.43	2.06	27.14
Oct-11	65.37	12.89	12.55	2.57	0.70	3.53	0.53	1.87	34.63
Nov-11	63.38	6.42	18.22	2.77	0.93	4.98	0.57	2.75	36.62
Dec-11	-49.69	24.70	82.82	10.14	5.07	13.15	2.59	11.22	149.69
Jan-12	6.96	10.48	64.35	4.50	3.46	3.49	1.16	5.60	93.04
Feb-12	-17.39	12.24	75.44	7.01	6.66	6.70	2.03	7.31	117.39
Mar-12	17.61	8.10	49.41	5.05	5.72	4.76	1.75	7.60	82.39

@ Contribution ith Group=(Inflation in ith group*Weight of ith group in CPI basket/Headline inflation)*100

5.2 One of the major causes of current inflationary pressure was high petroleum price in world market and successive upward adjustment of administered fuel and energy prices in domestic market. Moreover, high import demand for petroleum product is partly due to feed the gas-guzzling rental power plants. Recent depreciation of Bangladeshi Taka against US dollar is also exerting upward pressure on domestic price level through increase in prices of imported commodities and second round effect through increase in prices of domestically produced goods and services using imported inputs. In order to curb inflationary pressure, Bangladesh Bank has already taken a cautiously restrained monetary stance for H2 FY12, while ensuring adequate private sector credit to stimulate inclusive growth.



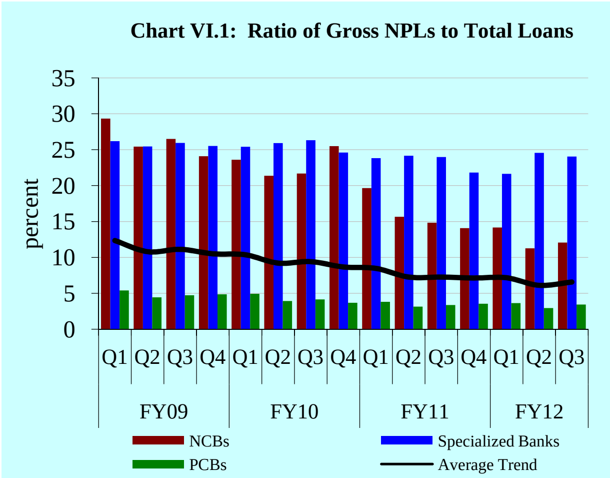


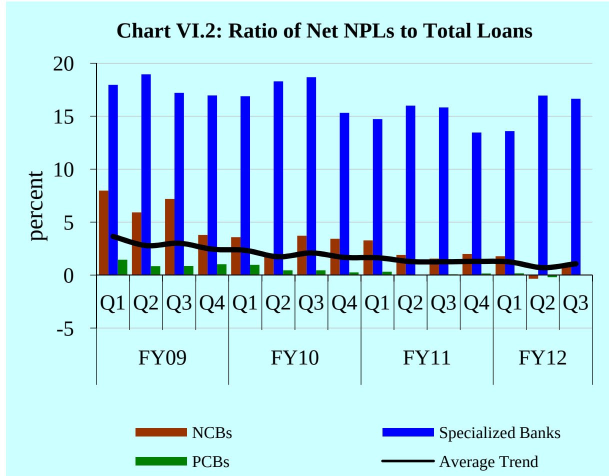
5.3 Given the current inflationary trends, the attainment of the single digit level of inflation seems possible assuming that the moderation in global food and non food prices will continue and BB's stance for limiting the money supply growth and stable benign domestic environment with no major supply disruption will be maintained. Due to bumper *aman* and *boro* crop production in last season along with stable food price in world market and restrained monetary policy, inflation in Bangladesh already has shown the signs of moderation.

5.4 Inflation in other South Asian countries showed mixed trends during the quarter under review. In India, due to continual monetary contraction point-to-point CPI inflation decreased to 5.32 percent in January 2012 from 6.49 percent in December 2011 then increased to 8.65 percent in March 2012. In Pakistan, point-to-point CPI inflation increased to 10.80 percent in March 2012 from 9.70 percent in December 2011. In Sri Lanka, inflation decreased significantly to low level of 2.7 percent in February 2012 from 4.9 percent in December 2011 then increased significantly to 5.5 in March 2012.

VI. Banking Sector Performance Trends

6.1 Performance of major indicators of banking sector reflecting in movement of the risk weighted capital asset ratio, the gross NPL ratio and the net NPL ratio, ROA and ROE for all banks during the third quarter of FY12 was mostly remained at a comparable level relative to the second quarter of Q2FY12. The gross NPL ratio and the net NPL ratio of overall banking sector slightly increased and the risk weighted capital asset ratio declined to some extent during Q3FY12 as compared to Q2FY12.





6.2 The risk weighted capital asset ratio for all banks was recorded at 11.31 percent at the end of Q3FY12, slightly lower than that of 11.35 percent during Q2FY12. This was due to decrease in the ratio for SCBs and FCBs to 11.68 percent and 20.97 percent at the end of Q2FY12 in comparison to 11.48 percent and 20.87 percent respectively at the end of Q3FY12 while that ratio for PCBs remain same at 11.49 under the mentioned period.

6.3 The ratio of gross NPL of the banking sector increased marginally to 6.57 percent in Q3FY12 from 6.12 percent in Q2FY12. This ratio for SCBs, PCBs and FBs were recorded at 12.06 percent, 3.44 percent and 3.2 percent respectively at the end of Q3FY12 higher than that of 11.27 percent, 2.95 percent and 2.96 percent respectively at the end of Q2FY12 despite SBs was registered lower ratio of 24.05 percent in comparison to 24.55 percent during the quarter under review (Chart VI.1). On the other hand, net NPL ratio for all banks exhibited an increase of 1.07 percent at the end of Q3FY12 in comparison to 0.70 percent during Q2FY12. This was due to significant increase of this ratio for SCBs, PCBs and FCBs to 0.78 percent, 0.03 percent and (-) 1.46 percent from (-) 0.34 percent, (-) 0.20 percent (-) 1.81 percent and respectively though the same factor for SBs witnessed a decrease to 16.64 percent from 16.95 percent during the same period (Chart VI.2).

6.4 The ROA for overall banking sector turned up to 1.54 percent in December 2011 compare with June 2011 low of 1.31 percent. This was due to increase of ROA factor for SCBs, SBs and PCBs to 1.34 percent, 0.30 percent and 1.59 percent from 0.62 percent, (-) 0.30 percent and 1.57 percent respectively during the mentioned period while it declined for FCBs to 3.24 percent from 3.62 percent registered in June 2011. On the other hand, overall ROE for all banks was recorded at 17.02 percent in December 2011, higher than that of 15.45 percent in June

2011due to significant rise in this factor for SCBs and PCBs to 19.66 percent and 15.69 percent in comparison to 10.01 percent and 15.58 percent respectively despite the same for SBs and FCBs reduced to (-) 0.92 percent and 16.58 percent from 5.15 percent and 20.19 percent respectively during the same period.

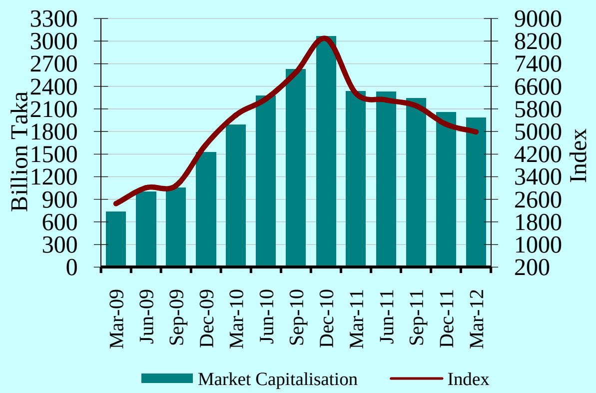
6.5 Excess liquidity in scheduled banks went up to Tk. 386.65 billion at the end of March 2012 in comparison to 270.88 billion at the end of March 2011.The excess liquidity of Tk. 141.83 billion was held by SCBs at the end of March 2012 which was Tk. 173.48 billion for PCBs (excluding Islamic banks) and 43.34 billion for FCBs.

6.6 The weighted average lending rate for all banks increased to 13.67 percent from 12.99 percent and the weighted average deposit rate for all banks increased to 8.07 percent in comparison to 7.56 percent during the same period. As a result, the interest rate spread (IRS) increased to 5.60 percentage points for all banks at the end of Q3FY12 in comparison to 5.43 percentage points at the end of Q2FY12. The real deposit rate for all banks was negative due to high inflation of 10.10 percent (p-o-p) at the end of Q3FY12. The interest rate spread for PCBs, SBs and FCBs increased to 5.59, 2.55 and 9.21 percentage points respectively from 5.40, 2.18 and 8.89 percentage points respectively during Q2FY12 though the spread for SCBs decreased to 4.48 percentage points from 5.01 percentage points during the above mentioned period.

VII. Capital Market Development

7.1 Despite several measures, the downward trend with significant volatility of DSE general index has been continued till March2012 due partly to lack of broad based investors' confidence. At the end of Q3 FY12, DSE general index and market capitalization decreased by 5.08 percent and 3.35 percent respectively (chart VII.1 and Table VII.1).Year-on-year position DSE general index and market capitalization declined by 21.43 percent and 14.21 percent respectively .

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



7.2 However, the liquidity situation in the capital market improved during the current quarter vis-à-vis the previous quarter. The volume of total turnover also increased to Tk. 230.14 billion as compared with Tk. 201.03 billion in previous quarter recording strong growth by 14.48 percent. Year over year comparison the total turnover declined by 55.66 percent. The “number of listed securities” was 280 in December’11 increased to 283 in March’12, while the value of “issued equity and debt” increased by 6.03 percent during the quarter under review (Table VII.1).

7.3 Sector-wise DSE data shows that during the Q3 FY12 market capitalization declined across the board except mutual fund, fuel & power, cement and telecommunication sector. The domination of banks, power, pharmaceuticals and telecommunication in total market capitalization with significant contribution from cement industries is continued till March’12. The share market capitalization of banking sector stood at 28.79 percent in Q3 FY12 against 29.74 percent in Q2 FY12.

7.4 Market overall price earnings ratio came down to 13.53 in March 2012 from 29.16 in December’ 2010. On the basis of price earnings ratio market is more attractive now requiring active participation of institutional investors to regain the investors’ confidence for stabilizing the market. Aggressive participation of the Bangladeshi expatriate in the capital market is also required to improve liquidity condition of capital market.

VIII. Near and medium term outlook

8.1 Despite of the multiple rounds of international instabilities like very recent global financial crisis followed by euro-zone debt crisis, the near-term economic outlook of Bangladesh economy remain favorable mainly because of strong output activities in industrial sector with solid supports of the agriculture and services sectors. This positive outlook is underpinned by strong domestic demand due to continuous supportive macroeconomic policies, steady growth in exports and imports, inflows of worker remittances, increased financing in trade, working capital and construction, higher credit flows to SME and agricultural sectors including transport and communication. Strong domestic demand is likely to play its part to support expected real economic growth in coming year.

8.2 Gross Domestic Output (GDP) growth is estimated to be 6.3 percent as against the projection of 6.5-7.0 percent in the FY12. A BBS analysis of sub-sectoral growth rates suggests the overall growth for the agricultural sector is likely to be 2.0 percent in FY12, the principal contribution coming from the crop sub-sector. It is also believed that industrial growth for FY12 would be the main driver of the growth and estimated to grow by around 10.0 percent, well in excess of the average recorded over the past five years. Further, the service sector in FY12, the largest component of the economy, is expected to build on the past year's performance, and yield a growth rate of 6.0 percent. In FY13, however, the real GDP of Bangladesh it is retargeted to grow by 7.2 percent with CPI inflation of 7.5 percent (Budget Speech, FY2012-13).

8.3 Data for the quantum index of manufacturing output show the signs of dynamism reflecting strong growth in jute, cotton, RMG & leather and fabricated metal products industries. These appetites for domestic investment would be increased significantly by a rapid pace of reform in the investment climate addressing inadequacies in energy supply and the quality of communication system.

8.4 Inflation is still a major concern for the economy as the higher inflation may impacts the domestic demand negatively and thus affects output growth in the near term. Ensuring the sufficient flow of funds to the productive sectors, Bangladesh Bank has been pursuing a cautiously restrained monetary policy stance raising its policy rates during the second half of FY12 in view of containing the current uptrend of inflation. The increased flow of bank advances (private sector) to the productive sectors such as transport and communication, construction and storage indicate development in infrastructure and connectivity in the country; therefore, the recent moderate growth of private sector credit directed to selective productive purposes while decreasing growth of public sector credit could ease the inflationary pressures in the coming months.

8.5 In view of supporting inclusive and pro-poor growth strategy, Bangladesh Bank has been taking steps to improve the stability and outreach of the financial system promoting specific products targeted to the needs of the unbanked populations. Accordingly, BB strongly emphasizes, among others, on an effective and monitoring based agriculture and SME lending program.

8.6 The near-term economic outlook of Bangladesh depends on various internal and external factors. Global growth prospects in 2012 remain highly uncertain in key trading partner countries, particularly in euro area due to the unfolding sovereign debt crisis in several euro area countries and the increasing related risk of a global recession. The IMF latest update forecasts that global recovery stalls and downside risk intensify. Global output is projected to expand by 3.25 percent in 2012-a downward revision of about 0.75 percentage points to the September 2011 WEO (WEO Update, January 2012). In this backdrop the higher growth of exports, remittance and flow of foreign aid are the key challenges for the economy to grow further. The movements of current domestic high inflationary pressure may pose a downside risk in economic growth and investment.