



The state of our foreign reserves: Separating myth from reality

Thursday, Dec 8, 2022

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Representational image. Photo: Collected

The ongoing global economic climate has created significant economic turmoil for both developed and developing countries across the world. While citizens in developed countries are navigating a substantial increment in the price of goods and services, culminating in high inflation – economic actors within some developing countries are also navigating numerous changes, ranging from strong exchange rate fluctuations, high inflation and a moderate to a high balance of payment concerns.

For countries in South Asia, the problems have crossed the realm of inflation management as they have also imposed considerable pressure on the balance of payments – most noticeable from the recent economic turmoil in Sri Lanka and Pakistan.

Bangladesh, in this context, is no exception as it is currently experiencing a high-inflation climate, fluctuating exchange rates and noticeable pressure on the balance of payments, but unlike Sri Lanka or Pakistan – our position benefits from stronger internal conditions stemming from the buoyancy of our export and remittance sector after the outbreak of Covid-19.

Yet, in recent times, the public space has witnessed a large spike in gossip and uninformed speculations, which needs to die down to preserve our macro-economic stability. Thus, this article is an attempt to present some views that separate the myth from reality, so that economic actors do not articulate their decisions on irrational speculations.

But what are these myths?

First, there is strong speculation within the public space that the current pressure on the balance of payments has emerged from irresponsible foreign borrowing to finance mega infrastructure. As this article will underscore, this narrative is more myth than reality.

Second, the public space has also seen uninformed discussions concerning the Export Development Fund (EDF), especially what it is and to whom it is given. A modest aspiration of the article is to push this discussion on EDF to a more informed terrain.

Broad trend in foreign reserve

Bangladesh's foreign reserve management has come a long way after its war-ravaged inception in 1972. Its foreign reserves were approximately \$270 million in 1972, and it took Bangladesh nearly 18 years to cross the \$1 billion threshold in 1990.

Furthermore, when Prime Minister Sheikh Hasina assumed office in January 2009 – foreign reserves stood at approximately \$5.5 billion, allowing roughly 3.8 months of import coverage. Since then, foreign reserves have experienced sustained improvement – and it reached an all-time high in August 2021 when it was as high as \$48 billion.

This incremental improvement in foreign reserves also allowed Bangladesh to develop strong cushions for preserving macro-economic stability – as import coverage of foreign reserves reached as high as 9.2 months in FY17.

These improvements to the foreign reserve scenario over the last fourteen years have opened new possibilities for Bangladesh as the government was able to use this economic cushion to seek developmental cooperation from foreign governments to support a wide array of infrastructure projects.

Given that foreign loans from development partners add foreign debt to any country's portfolio, which needs to be settled within a stipulated time frame, Bangladesh's improvement in the reserve scenario acted as a strong signal for external actors to confidently engage with local economic actors and state authorities to support our economic

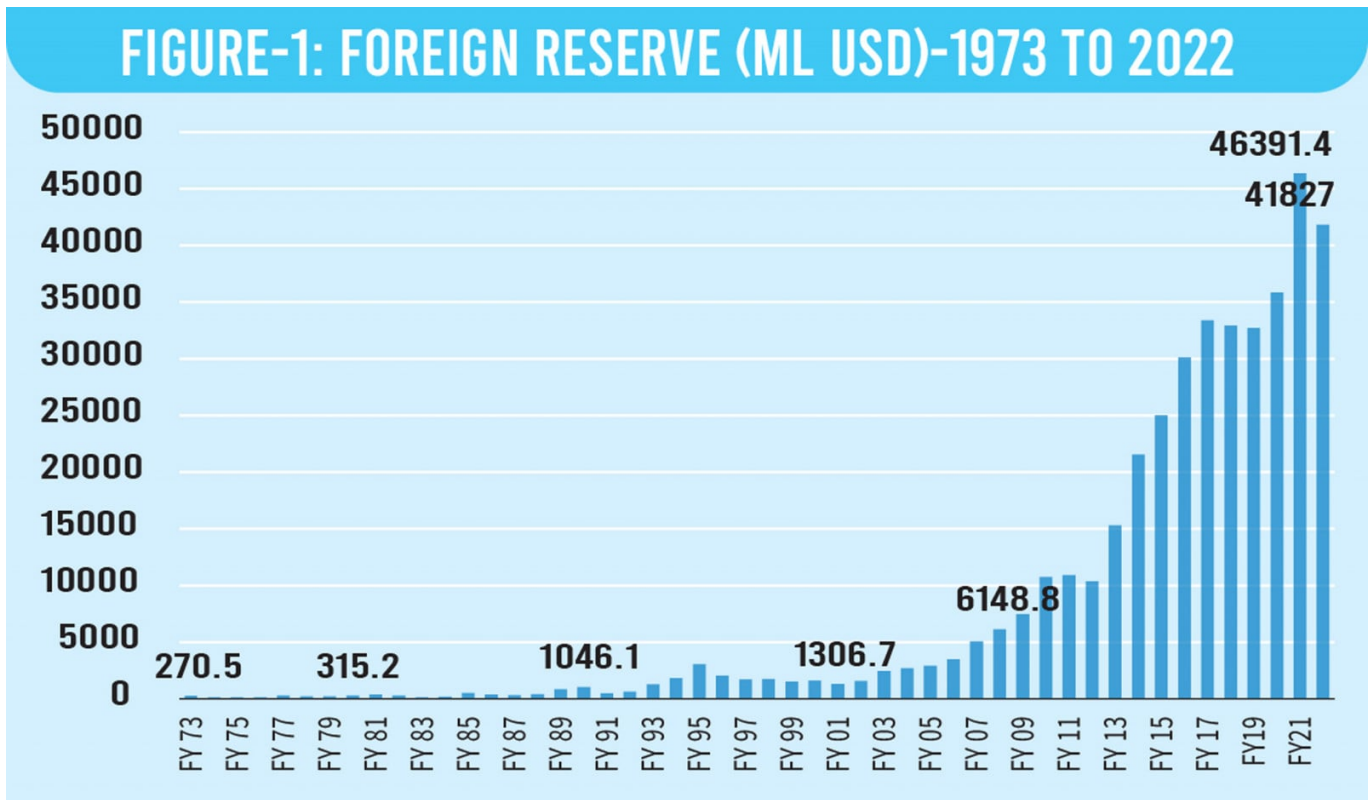
transformation.

Consequently, it is not surprising that between 2008 and 2022, Bangladesh was able to add nearly 18,000 MW to our generation capacity – and finance key transformational infrastructure projects such as the 6.15 km long Padma Multipurpose Bridge, 26 km long Dhaka Elevated Expressway, Dhaka-Chittagong four-lane expressway, Dhaka Metro Rail, LNG terminal, Payra Port, Rooppur Nuclear Power Plant, Rampal Coal Power Project, Matarbari Coal Power Project, Karnaphuli Tunnel, and numerous special economic zones, including the thirty thousand acre large economic zone in Mirsharai upazilas.

Once all these projects mature and start delivering economic dividends, there is little doubt that they will create strong supportive conditions for the private sector, enhancing Bangladesh's competitiveness in the global economy.

In fact, never in Bangladesh's history could one have anticipated that a country plagued with a chronic energy crisis and an acute dearth of acceptable infrastructure in 2006 would simultaneously mobilise such a significant amount of external resources and manage the execution of such a wide array of transformational infrastructure projects within a matter of a decade.

Accordingly, it is of no surprise that Bangladesh's per capita income experienced a sharp rise from less than \$800 in 2008 to approximately more than \$2800 in 2022 – marking Bangladesh's graduation from the category of Least Developing Countries.

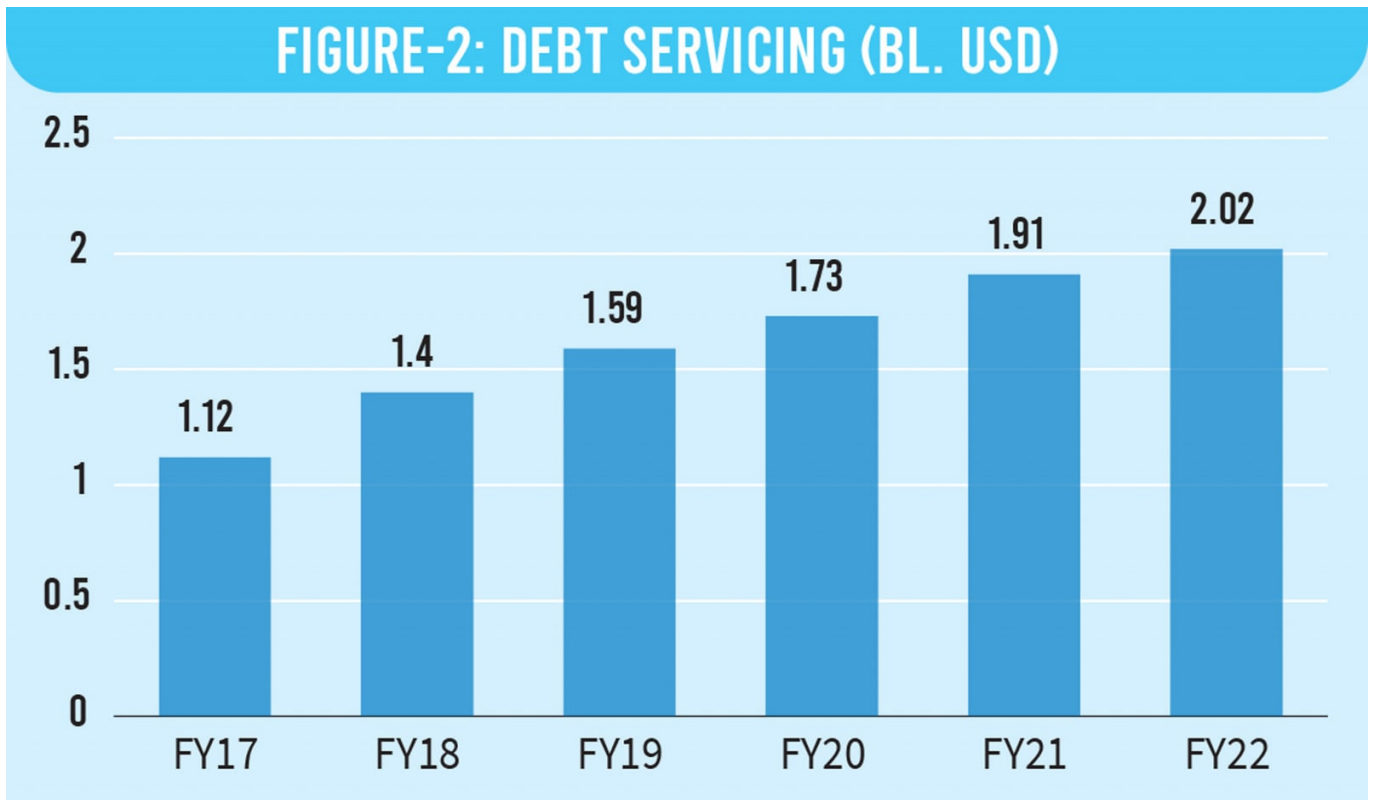


Infograph: TBS

In recent times, however, there have been strong speculations that existing pressure on the balance of payments has resulted from very high debt service obligations, which were incurred to finance the mega infrastructures.

This is a factually incorrect assessment of the existing pressure on the foreign reserves as foreign debt servicing in FY22 only amounted to \$2 billion. Furthermore, according to ERD data, Bangladesh has to pay \$2.77 billion, \$3.3 billion and \$4.02 billion for three fiscal years, which is unlikely to impose severe pressure on foreign reserves if our exports and remittances maintain double-digit growth.

There is, nonetheless, a need to underscore that while external borrowings to date have not created any major concerns for foreign reserves, it is advisable however that policymakers prioritise concessional loans from development partners over expensive bilateral financing options in the future.



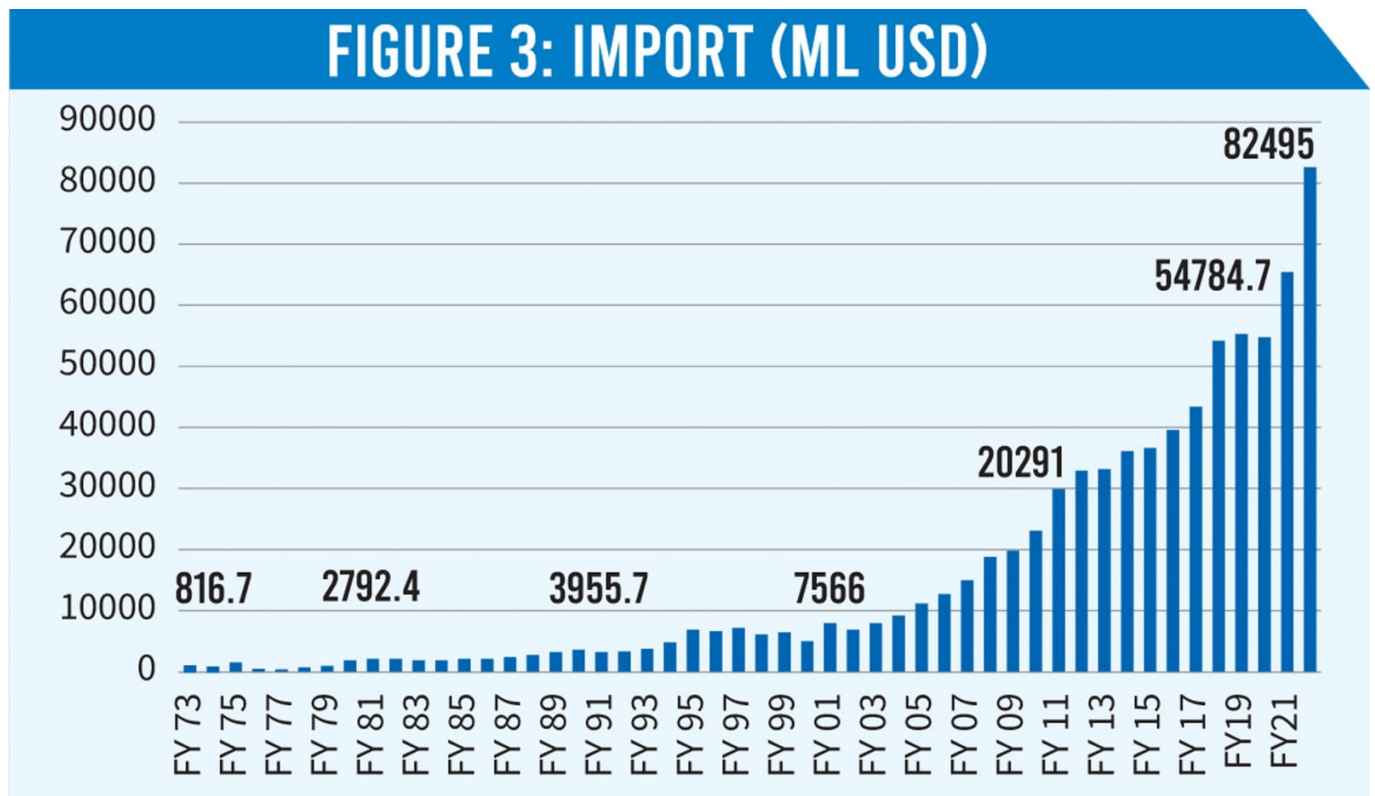
Infograph: TBS

Of course, if the high debt servicing obligation is not responsible for the existing pressure on our balance of payment, then what is? The changing global economic scene after Covid-19 and the outbreak of the Ukraine-Russia war created new complexities for the domestic economy.

First, FY22 saw a surge in imports mostly stemming from pent-up demand and a large increment in logistic costs. This in effect meant that Bangladeshi traders clocked record imports crossing \$82 billion in one single fiscal year, which was nearly \$17 billion higher than the previous year. As a result, the trade deficit in goods reached as high as \$33.25 billion in the noted fiscal year.

Second, the outbreak of the Ukraine-Russia war fundamentally changed LNG prices globally. From roughly \$4.6 per mmBtu in July 2019, LNG prices exponentially increased to approximately \$38 per mmBtu in March 2022 - reaching as high as \$54 per mmBtu in August 2022.

This substantial increment in LNG prices meant that Bangladesh could no longer afford to purchase LNG from the spot market and any attempt to import LNG to meet our energy demands would cost us more than \$10 billion, which our foreign reserves cannot support. This, of late, has resulted in acute gas shortage-induced power cuts that have caused substantial economic panic among economic stakeholders.



Infograph: TBS

Subsequently, these changes have collectively meant that our foreign reserves have been cushioning these adverse external changes and have therefore been decreasing since August 2021 - and as of November 15th 2022 - it reached \$34.24.

Moreover, there is also a new debate which notes that nearly \$8 billion of the stated \$34.24 billion-dollar foreign reserve should not be categorised as a 'useable' foreign reserve given \$7 billion has been committed to the Export Development Fund, \$200 million to Sri Lanka in the form of currency swap, \$200 million to Green Transformation Fund, 77 million Euros to Payra Port Authority, \$385 million to long-term financing facility, etc.

In short, IMF argues that the ‘useable foreign reserves’ stand at \$27.5 billion since the funds that are committed to different usage should not be considered as foreign reserves – as the standard definition dictates that “reserves consist of official public sector foreign assets that are readily available to and controlled by the monetary authorities”.

Furthermore, IMF’s position conforms to standard accounting standards – and it is satisfactory to see that Bangladesh Bank is no longer disputing IMF’s position that the net reserve estimates must not accommodate allocations that are tied up in different economic usage.

Even so, Bangladesh’s net reserves are enough to secure more than four months of import coverage, which should be enough to categorise the so-called ‘Sri Lanka Syndrome’ narrative as weak and devoid of any real economic logic.

Myths and realities surrounding Export Development Fund (EDF)

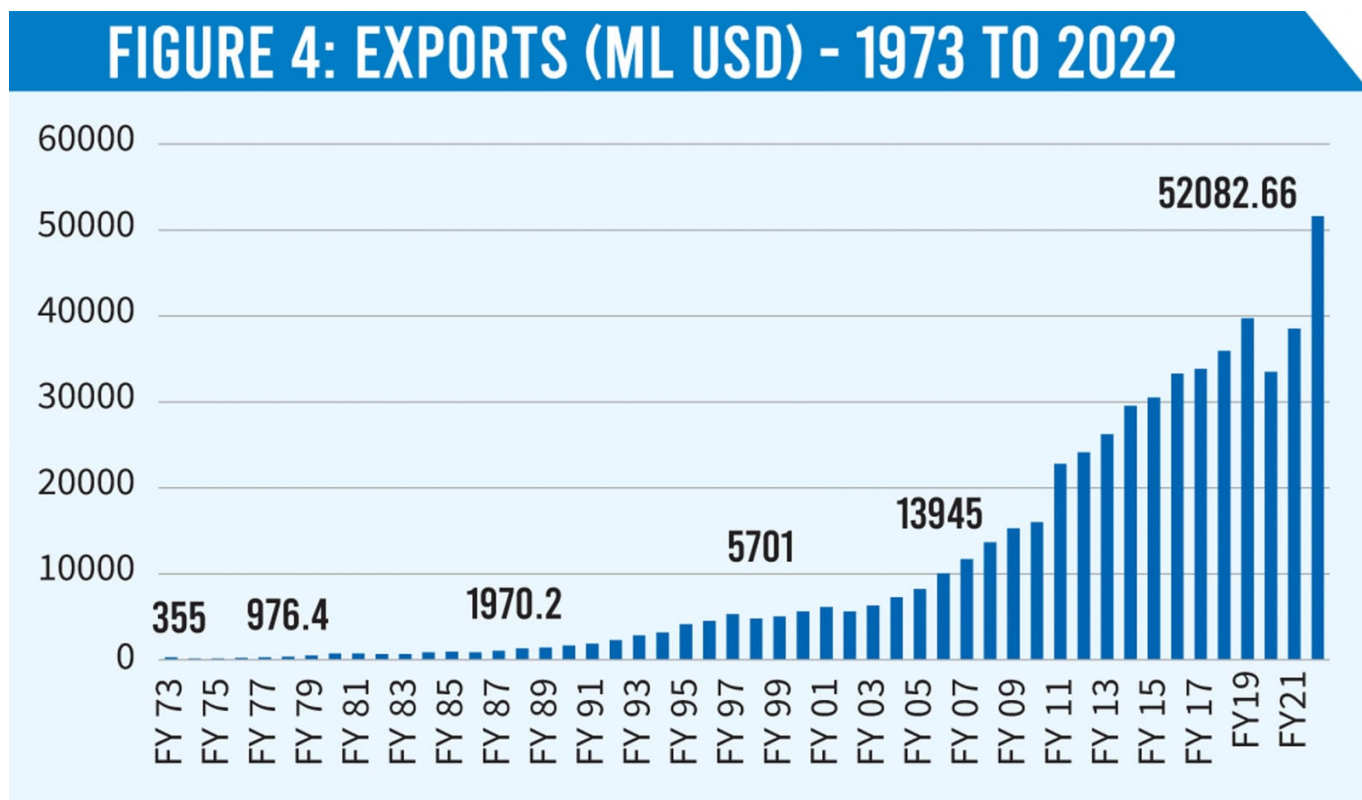
The Export Development Fund has recently received wide public scrutiny concerning what it is and how it is spent. Yet, a good share of this discourse is based on clumsy information and an incomplete understanding of the issue.

First: EDF funds are not given to a handful of politically connected firms. It is a revolving fund that is only given to exporters to ensure that they can procure necessary inputs for a cheaper interest rate. Furthermore, over the last two years, more than 1,700 exporters have used this policy instrument to make their exports competitive in the global market – and cumulative defaults under this scheme is less than 1.5%.

It is also essential to note that single exporter exposure has not exceeded \$30 million, which stands in contrast to the popular myth that only a few large borrowers took advantage of this policy scheme.

Second, the EDF fund was originally introduced in 1989 but when the present government assumed office in 2009 – allocations under this policy instrument remained below \$300 million. However, as our foreign reserves increased in size, the resources which we could devote for such specialised economic use also increased.

Hence, under the present government, resources devoted to EDF were increased to about \$7 billion, where exporters are expected to settle their borrowing in foreign currency within 360 days at an interest of 4%. Accordingly, it is not an accident that our exports have shown strong resilience and growth over the last 14 years - increasing from approximately \$14 billion in 2008 to \$52 billion in 2022.



Infograph: TBS

Light at the end of the tunnel

As policymakers operating on the economic front keep looking for passages and policies to navigate the adverse global economic scenario, a recent agreement with the IMF for a \$4.5 billion loan is likely to be instrumental in bringing much-needed resilience to our balance of payment.

Note, while the proposed support committed is not very large, the agreement with the IMF works as a strong signal to international financial institutions that Bangladesh is committed to economic reforms that will improve its economic fundamentals. Further, this should aid

Bangladesh in securing an additional \$2 billion which it is currently discussing with the World Bank and ADB.

Collectively, these economic measures along with the current tightening of the import regime have helped inject some stability into the balance of payment scenario. And while the ongoing war will demand cautionary macro-economic decisions from policymakers culminating in an economic slowdown, recent trends help keep us cautiously optimistic that Bangladesh will navigate the current global economic storm with some bruises but no deep wounds.



Dr Ashikur Rahman. Illustration: TBS

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