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By *Dr. Zaidi Sattar*

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Notwithstanding sound macroeconomic management for the past three decades, the external shocks originated from the Russia-Ukraine war have threatened the stability of the Bangladesh economy like that of many other developing nations. The country's economy, however, is still strong enough to face the threat and restore stability.

Eminent economist Dr Zaidi Sattar made these observations while taking to the Financial Express (FE) on the current economic challenges. He also endorsed the restrictive measures taken by the central bank to reduce unnecessary imports, maintaining that surge in imports has been a major source of higher inflation and depletion of reserves.

Dr Sattar, also the chairman of the Policy Research Institute of Bangladesh (PRI), a leading think-tank of the country, stressed uniform and flexible exchange rate to narrow the gap between the official and kerb market rates. He also claimed that the country's external debt situation is comfortable.

Here are the excerpts:

*Financial Express (FE). The global economy is under strain mainly due to Russian-Ukraine war and post-Covid supply chain disruptions, leading to price hikes in food and energy that have contributed to inflationary pressures on the one hand and threat of recession on the other. Bangladesh economy, like many other developing countries, is under severe macroeconomic pressure. What should be the appropriate response to such global developments?*

Zaidi Sattar (ZS): Whereas the Bangladesh economy was on a robust post-Covid recovery up to end December 2021, the Russia-Ukraine war and its repercussions in the global economy pretty much upended that recovery. It was a major unanticipated shock to the economy, upsetting the long sustainable trends in our balance of payments and also fuelling higher domestic inflation. Both internal and external macroeconomic stability has come under pressure, like in many other developing and emerging market economies. But make no mistake, having maintained a prolonged period of prudent macroeconomic management, Bangladesh is in a better position than many of its peers to address current macroeconomic challenges, albeit not without some pain.

First, let's acknowledge that the current macroeconomic challenges are externally driven. The main driver of the external imbalance was the import surge of 35 per cent (\$82 billion) in

FY2022. The export surge of 34 per cent (\$52 billion) and remittances of \$21 billion fell far short of the import bill thus resulting in a current account deficit (CAD) of \$18.7 billion.

*FE: How would you describe trends in the current account of our balance of payments. We understand the current account balance has been in a sustainable range for nearly 25 years. What makes the recent sharp rise in current account deficit so much of a problem?*

ZS: For the first time, Bangladesh’s CAD shot up to 4 per cent of GDP in FY2022, thanks to the import surge that was not matched by exports plus remittance inflows. This is untenable. A CAD of 3 per cent of GDP is the RED line that economies should not cross.

Cross-country and historical evidence reveals that persistent CADs of 3 per cent or higher for three years or more invariably leads to financial crises and eventual slowdown of the economy. So Bangladesh Bank was right in moving swiftly to stem the tide of imports by invoking two measures: (a) imposing administrative curbs on imports (e.g. clamping down on opening LCs of unproductive imports) and (b) substantial depreciation of the exchange rate which resulted in a steep rise in import prices. However, we believe the additional measure of introducing multiple exchange rates was unorthodox, should be deemed temporary, and abandoned sooner rather than later.

*FE: The US dollar has appreciated 20 per cent over the past year. Do you think the Bangladesh Bank has appropriately managed the exchange rate issue so far?*

ZS: The US dollar is by far the predominant means of international payments covering some 75 per cent of world trade. To curb domestic inflation, the US Federal Reserve (US Central Bank) has been tightening monetary policy by raising interest rates driving capital flows into the United States. This has strengthened the dollar by roughly 20 per cent in the past year. Unless the Taka/US dollar exchange rate depreciated by at least the same amount, our exchange rate would be grossly over-valued, thus hurting exports and making imports cheaper at a time when import surge had to be contained. So BB’s decision to finally let the exchange rate depreciate rapidly by about 20 per cent (averaging at Tk.103/US\$) was a sound move. However, introducing a multiple exchange rate system (e.g. a rate for exports, another for imports, still another for remittances) has created an untenable situation with no gain in sight. What needs to be done without further delay is to unify the exchange rate and make it flexible so that there is only marginal difference between the official and korb market rate.

*FE. Bangladesh’s foreign exchange reserves have now slipped to US\$36 billion as of October 2022. IMF also asked the central bank to update the reserve calculation in line with the fund’s standard guideline. It means, the actual amount of reserve will be much lower compare to*

*the reported one. What should be done to maintain a comfortable of forex reserves?*

ZS: Ever since the external shock reached our shores, Bangladesh’s official reserves of FE, called gross foreign exchange reserves, has been on the radar not only of the media but also of IMF, the multilateral institution that monitors FE adequacy across nations. Bangladesh’s FE reserves reached its peak of \$46.3 billion at the close of FY2021 with a coverage of almost eight months of projected imports. That comfortable situation evaporated with the onset of external pressures shortly after February 2022, on two counts: (a) import surge, and (b) abortive attempt of BB to shore up the exchange rate by reportedly shedding some \$10 billion out of official reserves until it became untenable.

IMF has raised some issues regarding BB statement of FE reserves by their standard definition of net international reserves (NIR) — gross reserves minus short-term foreign currency drains — in determining adequacy. In this regard, the treatment of some \$8 billion export development fund (EDF), a revolving fund that finances short-term import of inputs used in exports (mostly RMG), was disputed, though not settled, as potential short-term drain. Thus far, EDF stocks have held well thanks to the regular servicing of loans by exporters who treated this mostly as short-term trade credit. Current gross FE reserves (including EDF) of about \$35.8 billion (end October) will cover about 5 months of projected imports which is reasonably adequate though addition of a few billion dollars would take FE reserves to a more comfortable zone. IMF commitment of \$4.5 billion to be disbursed over the next three years will do just that.

*FE: Bangladesh has been praised for its prudent macroeconomic management for the last three decades. Why is it that we now face problems in both internal and external balances?*

ZS: Despite sound macroeconomic management for the past three decades, the external shocks emanating from the Russia-Ukraine war with its global ramifications could not have passed without causing some disruption in the Bangladesh economy. Other emerging market and developing economies suffered even worse impacts in terms of debt distress, foreign reserve depletion, inflation and BOP imbalances. Bangladesh economy barely suffered from the impact of the Global Financial Crisis (GFC) of 2007-08. This time the external shock was far too strong and the Bangladesh economy is much more integrated with the world economy than it was in early 21st century. Both inflation (internal imbalance) and BOP disruption (external imbalance) were externally driven shocks. Imported inflation and import surge were the two main sources of the current problem.

*FE. Is Bangladesh’s debt situation really problematic as many critics point out? Is private external debt the main problem? If so, why?*

ZS: By all accounts, Bangladesh’s debt situation is comfortable, at the 38 per cent of GDP. This was the determination of the IMF-WB debt sustainability analysis that was reported in April 2022. Bangladesh’s external debt stock of \$70 billion in 2022 was 16 per cent of GDP, with external debt servicing at only 6 per cent of foreign exchange earnings. Bangladesh has never defaulted (or sought moratorium) on its debt payments and does not need to do so. Reports have been going around that private debt stock of \$26 billion has become an unsustainable burden. Actually, adding private and public external debt would be like adding apples and oranges. The fact is some leading Bangladeshi firms borrowed from the international capital market because of the low interest rates available. However, bulk of this loan is in the form of short-term trade credit taken by exporters who contemporaneously service them through export proceeds. Interest cost of this debt in the BOP current account is minimal and only \$1.6 billion showed up as trade credit (debit) in the overall BOP in FY2022. Not a problem.

*FE: To ease the pressure on foreign exchange reserve, the government has put some restriction on imports. Wouldn’t our exports and GDP growth be adversely affected due to the restrictive measure as much of our imports are destined for the productive sectors of the economy?*

ZS: The curbs on imports have one objective: to restore balance in BOP by reducing demand for foreign exchange while keeping exports and remittances growing at a healthy pace. The administrative curbs are in addition to the price effect on imports that arise from the sharp depreciation of the exchange rate. I assume the price effect was not enough to restrain demand for foreign exchange. True, these non-market measures cannot and should not be continued for too long. Otherwise, it would affect exports of goods and services as well as production for the domestic market.

*FE. How do you see our medium-term export prospects in the face of structural shifts in the global geopolitical and geoeconomic order?*

ZS: The world economy has been rattled by the war in Eastern Europe and its aftermath. The situation is still evolving. Tectonic shifts could take place in the geopolitical order that will surely have ramifications for the post-WWII geoeconomic order. Bangladesh is now far more integrated with the world economy. What happens in G20 economies is key to Bangladesh’s export prospects. IMF has been tracking global developments and has come up with sharp downward revisions of world trade and output growth in light of the latest geopolitical and economic developments. Nevertheless, there is a silver lining for Bangladesh to this gloom and doom. Despite the slowdown in the global economy the RMG sector, in particular, is

expected to remain buoyant on the back of redirected orders from China over the near to medium-term as most Procurement Officers of retailers in EU and US have cited Bangladesh as the No.1 sourcing country over the next 5-10 years upon the decoupling trends in Sino-US trade. We might see a pick up in apparel exports over the next few months.

*FE: We observed that BBS delayed the release of monthly inflation data of August and September as inflation jumped significantly in these months. Does not it give a wrong message that the government wants to hide some critical economic data?*

ZS: Official statistics should be completely de-politicised. High frequency data like inflation should be published regularly and on time without interference from official quarters. It is high time for the creation of a constitutional position of National Statistician who will have the authority to oversee timely publication of all national statistics without fear or favour.

*FE: twin crises of food and fuel are looming. What do you think? How Bangladesh can overcome the crises?*

ZS: One option of course is to practice austerity. But that cannot extend to the poorer population who suffer in times of inflation. The reported Government decision to provide 50 kg of rice to some 50 million people is just right. With respect to the food security situation the current year appears to be on track as food production has been nearly on target, public food stocks are adequate, and private stocks are reportedly even better. The outlook for global fuel supplies and prices appear to be floating in the region of uncertainty as long as the Russia-Ukraine war remains unresolved. We could start thinking of building strategic fuel reserves for bad times. But that is easier said than done.

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