

## **IMPACT OF THE GLOBAL FINANCIAL CRISIS ON BANGLADESH ECONOMY: A THEORETICAL APPRAISAL**

**Md. Hasan Uddin<sup>1</sup>, Md. Anisur Rahaman<sup>1</sup>, Mohammad Zoynul Abedin<sup>2</sup>,  
Md. Mamunar Rashid<sup>3</sup> and Md. Jamal Uddin<sup>4</sup>**

### **ABSTRACT**

The global financial crisis that started in the United State in September- October, 2008 has now turned into a full-fledged economic crisis that has pushed the European Union, Japan, Hong-Kong, Malaysia and others into recession. There is a saying that when America sneezes, the countries around the world get flu. This has been evident from the fact that the crisis is already beginning to have an impact on the real economy in poorer countries around the world. Bangladesh has been mostly insulated from the first round effects of the financial crisis. But the country is vulnerable to the second round effects of global financial crisis through export earnings, tourism receipts, remittance, capital market, labor market and external financing for infrastructure. Economists obviously do not have perfect foresight; so this work will not try to anticipate the future. But economist can do what doctors do after the outbreak of a contagious disease. They can tell how the disease might spread, so that someone can be prepared. This is the purpose of the article not to make a forecast of Bangladeshi economy, but to warn of possible dangers.

*Key words: Bangladesh, Global economic crisis, Government, Remittances, Slowdown*

### **INTRODUCTION**

The current global economic slowdown is of an unprecedented form one that has not been experienced since the establishment of the current world economic order after the end of the Second World War in 1945. The trajectory of the deceleration in global scale of trade, industrial production and financial flows has been extraordinarily rapid. Beginning with failures of large financial institutions in the United States, it rapidly evolved into a global crisis resulting in a number of European banks experiencing failures and declines in various stock indexes, and significant reduction in the market-value of equities (stock) down 27 per cent as of October 24, 2008 and commodities worldwide. The crisis has led to a liquidity problem and the de-leveraging of financial institutions, especially in the United States and Europe, which further accelerated the liquidity crisis. Political leaders and ministers of finance and central bank governors of the leading nations of the world have coordinated their efforts to reduce fears, but the crisis is persisting and undergoing changes in varying magnitudes and directions. The crisis has its roots in the sub prime mortgage crisis and can now be looked upon as an acute phase of the financial crisis of 2007-2008. The present scribe thinks the key reason for the global financial crisis, which is blamed on the sub prime mortgage crisis, is partially true. The US economy is basically a bankrupt economy, which depends largely on credit cards. Every citizen pays the price of commodities through credit card making their life debt-oriented. The economy of a country cannot stand on a sustainable level, if its public life remains debt-oriented instead of savings-dependent. Over and above, with the surge of inflation, especially for food and fuel, the cost of living has shot up throwing them out of liquidity and thereby triggering failures in settlement of debt installments one after another. Under such circumstances, the US banks faced an accumulated bad debts worth of billions of dollars which created credit crisis and the ultimate financial turmoil. The key difference from previous global slowdowns is in the substantial weakening of the

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<sup>1</sup>Lecturer, Department of Management Studies, Patuakhali Science & Technology University, Patuakhali, Bangladesh; <sup>2</sup>Lecturer, Department of Finance & Banking, Hajee Mohammad Danesh Science & Technology University, Dinajpur-5200; <sup>3</sup>Assistant professor, Department of Accounting, Hajee

Mohammad Danesh Science & Technology University, Dinajpur-5200; <sup>4</sup>Lecturer, Department of Marketing, Hajee Mohammad Danesh Science & Technology University, Dinajpur-5200, Bangladesh.

financial sectors in the United States and Europe, with consequent damaging implications for credit extension in the global economy. Although there are increasingly vigorous measures being taken in the United States and Europe to repair the financial institutions and re-start the flow of credit, these have been partial, patchy and incomplete. Without a swift rehabilitation of the global financial system, other measures such as fiscal stimulus and interest rate cuts may not succeed in reviving economic growth in key countries which are important markets for South Asia. However, overall, there is absolutely no reason to panic for Bangladesh. Bangladesh is relatively insulated from the financial side, but vulnerable to potential global economic slowdown, particularly in the US and EU. Against the background, Bangladesh cannot be immune from the global economic slowdown and is most likely to be adversely affected sooner or later. So the volatile situation is both a challenge and an opportunity for Bangladesh to show innovation and creativity to come out from the likely adverse effects of global economic crisis. Hence a research on this area is essential to overcome the relevant facts. This research study is an endeavor for the same.

### **RATIONALE**

The crisis began with the bursting of the US housing bubble and high default rates on subprime and adjustable rate mortgages, beginning in approximately 2005-2006. For a number of years prior to that, declining lending standards, an increase in loan incentives such as easy initial terms, and a long-term trend of rising housing prices had encouraged borrowers to assume difficult mortgages in the belief they would be able to quickly refinance at more favorable terms. However, once interest rates began to rise and housing prices started to drop in 2006-2007 in many parts of the US, refinancing became more difficult. Default and foreclosure activity increased dramatically as easy initial terms expired, home prices failed to go up as anticipated, and adjustable rate mortgage interest rates reset higher. Foreclosures accelerated in the United States in late 2006 and triggered a global financial crisis through 2007 and 2008.

Hussain Zahid (2008) pointed out that overall there is absolutely no reason to panic. Bangladesh is relatively insulated from the financial side, but vulnerable to potential global economic slowdown, particularly in the US and EU. The foreign exchange reserves of Bangladesh Bank and commercial banks have limited exposure to the securities markets and banking system risk in the US and EU. Foreign capital flows are largely in the form of concessional official lending. FDI and foreign portfolio investments are small. However, Bangladesh's economy relies heavily on garment exports. This is where the main risk lies. Remittances may also be vulnerable. Rashid Ur Harun (2008) noted that the export sector is potentially the most vulnerable in Bangladesh since it depends heavily on US and EU economies. Imam Hasan (2008) found that there is unlikely to be any direct immediate impact on remittances. Remittances in Bangladesh proved to be resilient during previous financial crises in the world. The bulk (over 60 percent) of Bangladesh's remittances come from the Middle East, and less than one-third come from the US, UK and Germany. Strong remittance growth (44 percent) has continued in the first quarter of FY09. However Uddin Alal Md. (2008) revealed that import is probably the one channel through which Bangladesh may benefit. Import payments in August have reportedly been US\$531 million lower than import payments in July. This decline in import payments is mainly due to the fall in prices of petroleum products, wheat and edible oil. Record high oil prices last year raised import payments to over US\$20 billion in FY08, compared to slightly over US\$15 billion in payments in FY07. The gains on account of reduced import payments can be sizable. Bhaskaran Manu(2008) mentions that with key donor countries in North America and Europe facing recession, Bangladesh could well see a lower disbursement of financial aid which has been key to Bangladesh's poverty alleviation

strategy. CPD-ILO study team (2009) stated that economic recessions tend to have adverse impact on all sectors and sections of the society; however it is the poor and working class which generally suffers from the most adverse consequences first. Recessions have negative impact on both employment and labor market.

A survey of literature pertaining to the East Asian financial crisis of the 1990s indicates that in the context of a global economic crisis the most vulnerable countries including Bangladesh are likely to be export-oriented sectors, manpower export, remittance and domestic resource mobilization. Aid inflow could also be hit by the crisis. So it is important that a review of the repercussions of the current crisis is carried out both at the level of Bangladesh's partners in the global economy, and also at the level of the domestic economy with its various sectoral dimensions. The central objective of the study is to assess the financial crisis on Bangladesh economy. To satisfy this central objective, the following are the specific objectives.

- a. To examine and analyze the impact of ongoing global economic crisis in the context of Bangladesh.
- b. To assess the initiative those are taken by the government of Bangladesh to address the attendant challenges.
- c. To develop policy suggestions by which these will both help the economies in the crisis times as well as build resilience for the future.

## METHODOLOGY

Keeping the objectives in the mind, the appraisal is designed to be carried out in two stages: firstly, an initial review that will lay down some basic issues based on preliminary findings collated from secondary sources, e.g, books, journals, news paper, and secondly, a detailed assessment of the crisis over a longer period based on unstructured interviews and consultations with government officials and other stakeholders. The collected data are analyzed through mathematical figures, charts, graphs, tables.

## DISCUSSIONS

The Bangladesh economy has been growing at a steady pace for the last five years. GDP grew by 6.2% in 2007/08 (Table -1). The Policy Analysis Unit (PAU) of the Bangladesh bank estimates growth in 2008/09 to register 6.0%, which is slightly slower than the previous years. This comparatively robust performance points to the country's resilience to the global economic crisis so far. The resilience is derived from the relatively small exposure to international financial markets, capital outflows and tourism. One important area of concern is the export industry which is dominated by low-cost apparel exports to the United States and Europe. However that should not be taken as an immediate concern.

Table 1. Bangladesh GDP breakdown by industry

% y/y	Weight age of GDP (2007/08)	2004/05	2005/06	2006/07	2007/08
GDP	100	5.9	6.6	6.4	6.2
Agriculture	20.9	2.2	4.9	4.6	3.6
Industry	29.7	8.3	9.7	8.4	6.9
Mining	-	8.4	9.3	8.3	8.6
Manufacturing	-	8.2	10.8	9.7	7.4
Utilities	-	8.9	7.7	2.1	4.9
Construction	-	8.3	8.3	7.0	5.9

Services	49.5	6.4	6.4	6.9	6.7
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Source: Bangladesh Bureau of Statistics

2008 has been an important year for Bangladesh. Certain important developments have helped shape the economy and are likely to impact the economy in 2009. Journal of Science and Technology, Vol. 6, 2008

**Change in political leadership:** The Awami League's (AL) landslide victory in the Dec 08 elections means a fresh political start for the country after several years of uncertainty and instability. The new democratic government is likely to enhance Bangladesh's investment attractiveness to foreign investors and could also help improve economic policy decision-making process in the country.

**Reversal in inflation trend:** The Bangladeshi economy relies heavily on the imports of essential commodities. Thus, the fall in commodity prices in late 2008 will help alleviate inflationary pressures in the short term. However, the longer term risk of inflation remains a function of monetary policies.

**Growth maintained despite bleak global environment:** The ability of the economy to have withstood the crisis thus far is an encouraging trend as the domestic fundamentals in the economy appear to be strong.

Now a discussion will be made on the current and likely impact of the crisis, and then study the primary factors for resilience. Finally, discussion will be made on the policy measures adopted thus far.

#### The impact of the crisis

Bangladesh has been relatively unscathed from the crisis in the world economy. However, as the downturn accelerates further and spreads to other markets to which Bangladesh has significant important links, the indirect effects of the crisis are likely to affect Bangladesh's economy. Bangladesh is increasingly integrated with global economy in terms of trade, investment, flow of remittances; its degree of openness was about 57 per cent at the end of FY2007-08, where contribution of trade was the highest (43.4 per cent) followed by remittances (10 per cent) and ODA (2.4 per cent) (Table 2). About 85 per cent of Bangladesh's exports are destined to developed economies and about 60 per cent of imports are from those countries. If India, China and other emerging economies are also taken into consideration, the extent of exposure of the Bangladesh economy with crisis-driven developed and developing economies will be quite significant.

Table 2. Bangladesh's Degree of Openness and Extent of Globalizations (million USD)

	FY 1981	FY1991	FY 2001	FY 2007	FY2008
1. Export (X)	725	1718	6467	12154	14088
2. Import (M)	1954	3472	9335	17157	20217
3. Remittance (R)	379	764	1882	5978	7915
4. ODA Disbursed	1146	1733	1369	1565	1873
5. FDI (net)	n.a.	24	550	793	650
Total (1-5)	4204.0	7710.5	19603.4	37646.3	44743.8
GDP (Current Price)	19811.6	30974.8	47306.0	67714.0	78996.9
Degree of Openness (Export + Import as % of GDP)	13.5	16.8	33.4	43.3	43.4
Extent of Globalizations	21.2	24.9	41.4	55.6	56.6
X as % of M	37.1	49.5	69.3	70.8	69.7
(X+R) as % of M	56.5	71.5	89.4	105.7	108.8
ODA as % of GDP	5.8	5.6	2.9	2.3	2.4
ODA As % of Export	158.1	100.9	21.2	12.9	13.3

Source: CPD-IRBD Database

#### Gradual Slowdown in Export growth

Exports remain the most vulnerable sector in Bangladesh. The main exports out of Bangladesh are low-end manufactured goods such as textiles and footwear. Readymade textile products form over 63% of total exports from Bangladesh. Of the total exports over 70% are exported to the G7 countries. These figures suggest that even a minor contraction of exports is likely to hurt the economy and in the less likely case of a severe pullback, the consequences on Bangladesh may be worse. There might be a mild

slowing of exports given the relatively inelastic demand for the type of exports Bangladesh concentrates on. Figure 1 and Figure 2 do suggest some volatility of exports in the months leading up to October 2008. Exports of low-end apparels (accounting for 76 per cent of total export) have been less affected in spite of slowdown of import in both EU and USA (the so-called *Wal-Mart* effect). Export growth in the first six months of FY2008-09 (July-December, 2008), at 19.6 per cent, remain robust. However, slowdown is visible in recent months. Growth in Q2 of FY2008-09 (October-December, 2008) was 1.2 per cent, a first time negative growth in recent times.

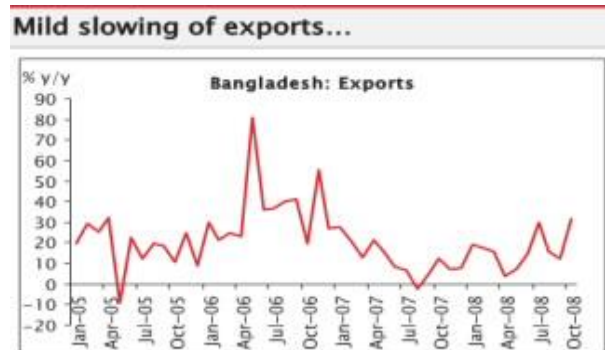


Figure 1. Volatility of exports

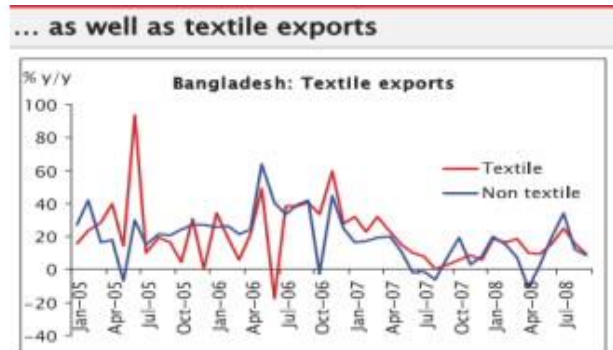


Figure 2. Textile export

Source: Bhaskaran Manu, (2008)

Exports of primary products such as frozen foods, raw jute, and leather have been adversely affected. Some of the promising sectors such as ship-building have seen orders cancelled. Some export diversion from China – but higher discount asked, and lower C&M charge offered by major buyers; at times orders being deferred.

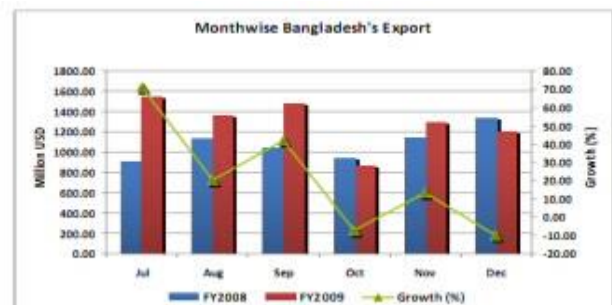
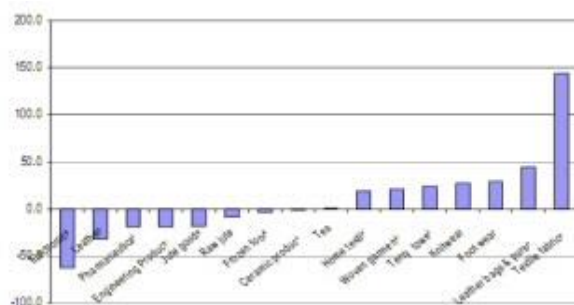


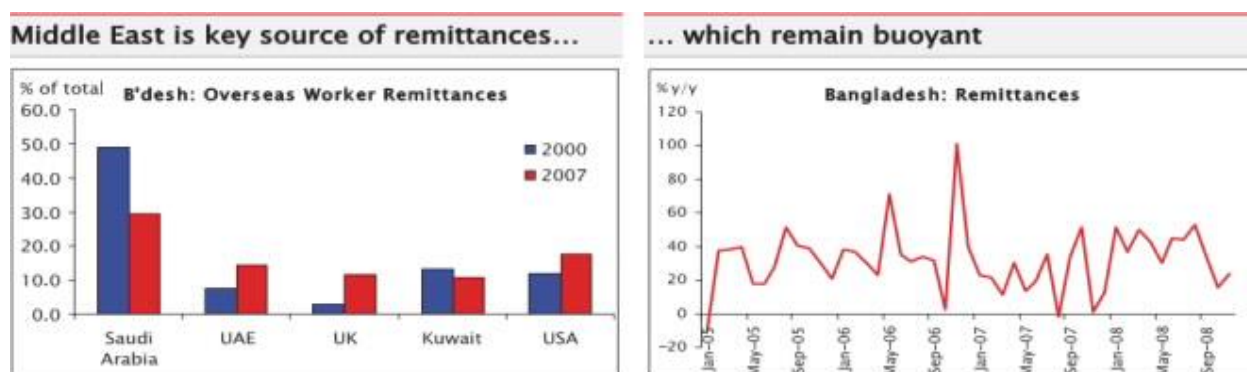
Figure 3. Changes in Export of Selected Commodities during July-December, 2008 and Over July-December, 2007

Source: CPD-IRBD Database

### Inward inflow of Remittances

Remittances from overseas Bangladeshi workers form a significant portion of incoming transfer payments in the current account balance. There are today about 981,000 Bangladeshi workers employed abroad, in a total population of 140 m. The ratio of remittances to GDP has also increased from 3% in 1993 to 9.7% in 2007. Remittances from Bangladesh are mainly sourced from two locations, the developed market comprising of the United States and United Kingdom, and Middle Eastern countries, namely Saudi Arabia, Kuwait and the United Arab Emirates (Figure 4). Workers in the United States and

United Kingdom have increased over the past few years as can be seen by the remittance flows from these countries. In the case of the Middle East, Bangladeshi laborers are employed in both construction as well as oil production projects.

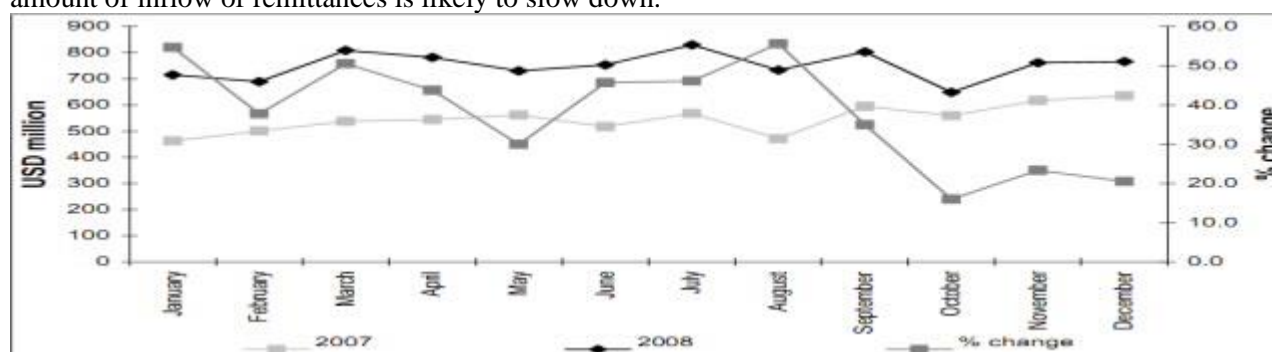


**Figure- d: Sources of remittance**

**Figure 5. Remittance over the period**

**Source:** Bhaskaran Manu, (2008)

Remittances are key drivers of household consumption. In Bangladesh, about 66% of remittances is used for family maintenance; 12% to purchase land and 14% to repay loans. Only 5% is used for business investment and just 3% is saved (Tasneem Siddiqui, 2003). In case of flow of remittances, though overall remittances in 2008 exceeded USD 9 billion, which was 37.3 per cent higher compared to the previous year; there is a deceleration in case of growth of remittance flow since August, 2008 owing to low outward migration of workers Figure 6. Month on month, number of workers traveling overseas have come down in 2008 compared to 2007. Although inflow of remittance per migrant was relatively higher (USD 1694) in 2008 compared to that in 2007 (USD 1476), unless more workers emigrated in 2009 this amount of inflow of remittances is likely to slow down.



**Figure-f: Flow of Remittances in 2007 and 2008**

**Source:** Data collected from the Bureau of Manpower Employment and Training (BMET)

**Foreign Direct Investment**

Bangladesh needs foreign direct investment (FDI) up to 28% per cent of GDP (almost 415 billion) every year to reduce poverty in the country. Whatever FDI was coming to Bangladesh was encouraging but it is likely to slow down considerably. No visible negative impact on FDI flow. Adverse impact on portfolio investment – net outflow.

**Table-3: FDI in Bangladesh (million Us\$)**

Foreign Investment	FY2006-07R	FY2007-08P	FY2007-08 July- Nov.	FY2008-09P July -Nov
Foreign direct investment	793	650	238	480
Portfolio investment	106	48	45	-34

**Source:** CPD-IRBD Database

**Foreign Aid**

Bangladesh has, till now, been able to maintain the trend of inflow of foreign aid amid the ongoing economic recession in its major development partner countries. While total foreign aid during FY2007-

08 was 20.4 per cent higher than that of FY2006-07, this increase for the July to October period of 2008 over the comparable period of 2007 has only been 1.6 per cent. It, therefore, gives a signal that if the recession continues, one may expect either a minimal rise in foreign aid over the remaining period of the current fiscal or, perhaps not so unlikely, even a negative growth. Nevertheless, overall balance of payment situation is still found at a healthy state.

**Table-4: Flow of Aid in Annual Development Program (ADP)**

ADP	ADP of FY2007-08 (July-December)	ADP of Fy2008-2009 ( July- December)
Total Aid disbursed for ADP(min US\$)	315.7	391.9
Share of Aid in ADP Utilization (%)	39.6	44.2

**Source:** CPD-IRBD Database

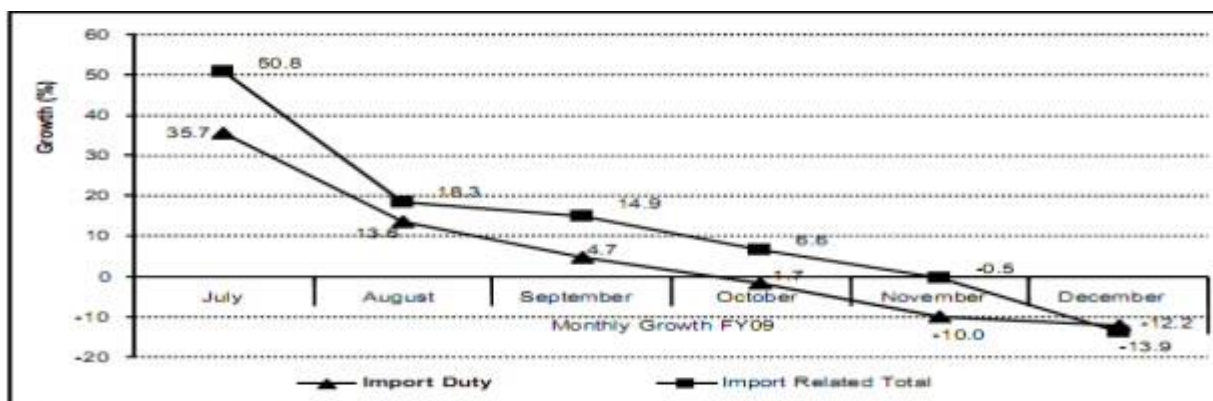
### **Capital Market**

A correction so far, not a crash one of the remarkable anomalies in the global financial meltdown has been the resilience of the Bangladesh stock markets. While other emerging economy stock markets have crashed, cut in half in a couple of months, the Bangladesh bourses have only experienced a mild correction - down 11 per cent from their peaks.

Foreign capital inflow into the Bangladesh stock market has been limited. One of the key drivers of growth in emerging market stock indexes over the last five years has been the influx of large foreign investments. In the positive phase of the credit cycle, foreign capital flowed into emerging markets driving up local stock indexes. But by the same measure, this capital is quick to flee when the risk premium increases. In the negative phase of the cycle, the same foreign investors are pulling out of these higher risk investments, leading to stock market crashes in emerging economies. This has happened in China (stock market down nearly 60 per cent in 2008), India (down over 50 per cent) and Vietnam (down close to 60 per cent), for Bangladesh this number is closer to 5 per cent.(Imam Hasan,2008).Banks, while a large segment of the stock markets, have been immune. Like many of their developed market counterparts, the Bangladesh stock indexes have a heavy concentration of financial institutions; banks and other financial institutions account for over 44.23 per cent of market capitalizations of the Dhaka Stock Exchange. However, unlike their foreign counterparts, Bangladesh banks have not been big casualties of the global financial meltdown, for reasons discussed earlier. This has meant that the Bangladesh stock markets have been spared the erosion due to banking sector collapse in foreign markets. Export-oriented sectors a small part of the index. The sectors that are likely to be the most negatively impacted by the financial crisis, the export oriented sectors and commodity importers are under-represented in the stock markets, accounting for less than 10 per cent of the market capitalization. As a result, even though these sectors are taking the first brunt of the negative consequences of the financial crisis, the impact on the stock market is relatively small.

### **Macroeconomic Management and Domestic resource Mobilization**

A large part of government's revenue comes from duties collected from imported commodities. Import and import related duties mobilized during July-December, 2008 were respectively 4.3 per cent and 11.8 per cent higher than those of the comparable period of 2007. However, month-on-month growth trend during the July-December of 2008 over 2007 shows a downturn in import duty (starting from 35.7 per cent in July, 2008 to a negative growth of 13.9 per cent in December, 2008) and in import related duty earnings (from 50.8 per cent growth in July, 2008 to the negative growth of 12.2 per cent in December, 2008), *Figure-g*.



Source: CPD-IRBD Database

Figure-g: Growth in Import and Import Related Duty Earnings (2008 Over 2007) Journal of Science and Technology, Vol. 6, 2008

### Employment and labor market

There is no real-time information with regard to the Bangladesh labor market; latest available data on employment and labor market was for FY2005-06. Based on this data set, a projection was made with respect to employment scenario in FY2007-08 by the BB (Table 5). According to the estimate, the size of the labor force was likely to be 51.8 million in FY2007-08; with 7.2 million in the industrial sector and 19.13 million in the services sector. Among the workers of the industrial sector, 5.27 million workers worked in manufacturing sector, and 1.7 million in construction sector. Among the workers in the service sectors, 8.46 million workers worked in trade, hotel and restaurants, and 4.21 million in transport, storage and communication sector. According to the projection, unemployment rate in fiscal year 2007-08 was estimated to be 3.98 percent. Female workers' participation was about 12.1 million which was 29.2 percent of the total female population under the same age category. Participation of workers in the informal sector was 37.2 million. However, it appears that under the changing scenario, with possible downward revision of growth of GDP, and changes in growth-employment elasticity, the composition of labor force in different sectors and the rate of unemployment may need to be reviewed

Table-5: Projected Employment in Major Sectors in FY2007-08

(in million) Sector	FY2005-06	FY2007-08 (estimated)
<b>1. Agriculture</b>	<b>22.83</b>	<b>23.41</b>
Crops and horticulture	20.93	21.37
Forestry	0.74	0.79
Fisheries	1.16	1.24
<b>2. Industry</b>	<b>6.90</b>	<b>7.20</b>
Mining and quarrying	0.10	0.12
Manufacturing	5.20	5.27
Electricity, gas and water supply	0.10	0.11
Construction	1.50	1.70
<b>3. Services</b>	<b>17.70</b>	<b>19.13</b>
Trade, hotel & restaurants	7.80	8.46
Transport, storage & communication	4.00	4.21
Finance, business services and real estate	0.70	0.75
Health, education, public admin and defense	2.60	2.86
Community, social and personal services	2.60	2.85
<b>Total</b>	<b>47.43</b>	<b>49.74</b>

Source: Bangladesh Bank (2008), Recent Employment Situation and Labor Market Developments in Bangladesh, Policy Paper 0807, Policy Analysis Unit, June.

Migrant workers have tended to suffer from the ongoing financial crisis (Figure 4). Although number of workers going abroad in 2008 (875,055) was 5 per cent higher compared to the previous year, the number substantially declined when compared to the growth in 2007 over 2006 (118 per cent). More importantly,



month-on-month number of migrant workers has started to decelerate from January, 2008 (140 per cent growth) and reached its lowest level in December, 2008 (-40 per cent) (BMET, 2008). Growth of migration in major markets is mixed. While in some of the Middle East and South East Asian countries it was substantially high in 2008 compared to 2007 (85.2 per cent in the UAE, 47.6 per cent in Singapore, 200.6 per cent in Oman, and 68.9 per cent in Qatar), in other markets of these region it was negative (-35.3 per cent Saudi Arabia, and -51.77 per cent Malaysia). Since 2006, UAE and Malaysia had been two key destinations for Bangladeshi workers followed by Saudi Arabia. It is important to mention here that currently Saudi Arabia and Kuwait have stopped issuing work permits to Bangladeshi workers, while these two destinations comprises of 39.7 per cent of total migrant workers from Bangladesh. Thus, growth of outward migration will not be sustained unless recruitment of workers in Saudi Arabia and Kuwait can be ensured.

There is dearth of adequate information about return migrants, since information on return migrants are not maintained in a systematic manner. However, evidence suggests that workers in the affected countries are experiencing retrenchment (though on a limited scale). Malaysia has announced retrenchment of about 45,000 workers by January, 2009, of which a substantial number appears to be migrants; it was reported in the national dailies that retrenched migrant workers in Indonesia held processions in Jakarta demanding jobs in Malaysia. It would be a challenge for Bangladesh to retain the growth of migration in 2009. In all likelihood, the pace of growth will slow down.

#### ***Supporting policy in regime/ Policy response***

There has been little in the way of policy changes made by the Bangladesh government and regulatory bodies. The need for a stimulus package has not arisen yet but businessmen, economists and consumer groups are pushing for more anticipatory and preventive action from the government.

#### **Measures Taken by the Government**

In January 2009, the government decided to constitute a broad-based national committee to follow the developments related to the ongoing economic crisis and suggest measures to address the adverse impacts on Bangladesh economy. (Addressing fallouts of global recession in Bangladesh', The Financial Express, 1st February 2009)

A high-powered technical committee was earlier formed in early November, 2008 to closely monitor the impact on the country's economy from the fallout of the current global financial crisis and take instant remedial measures. The committee is expected to examine proposals which demand increasing cash incentives for apparel exporters. The Ministry of textile and Jute will be coordinating with the Finance Ministry to form a plan to protect and safeguard exporters. Government undertook a seven-point strategy to ensure the well being of the Bangladeshi workers abroad and to explore new manpower export markets. The government has been active in the remittance front by signing agreements with other countries on manpower exports. An agreement with Libya has already been signed while deals with Jordan and Bahrain are under discussion (Bangladesh, Libya to sign manpower export agreement', New Age, 31st October 2008). Certain tax exemption schemes on interest income earned by the non-resident Bangladeshis have also been introduced.

#### **Measures Taken by the Central Bank (Bangladesh Bank)**

The Bangladesh bank has set up a *Forex Investment Committee* to monitor and manage the currency composition of forex reserves. BB prudently withdrew about 90 per cent of its total investment from international banks which were perceived to be at risk. When the early signals started to blip on the radar screen in 2008, the BB took speedy and energetic steps to safeguard the country's reserves (USD 5.98 billion in October, 2008), and also those of the commercial banks of the country (about USD 490.0 million kept at the time with overseas financial institutions). Bangladesh bank has advised commercial banks to be cautious about such investments.

Bangladesh bank has recently instructed banks to take measures to reduce the time and cost of transferring remittances by cutting down time and costs of transferring remittances, bringing remittances through legal channels, creating opportunities for investment of remitted money, and ensuring welfare of expatriates. It directed the bank branches or exchange houses overseas to keep their organizations open on holidays to help expatriates remit funds. In addition, BB has continued with its policy of intervention in the inter-bank foreign exchange market by selling and buying US dollar directly and providing short term facilities to the banks aiming to keep the market stable. BB has allowed settlement of import payments in Euro alongside the US dollar among the Asian Clearing Union (ACU) member countries. In view of the losses incurred by importers as a result of the fall in global commodity prices (e.g. wheat, edible oil and pulses) and the difficulties faced by importers in honoring L/Cs, BB has relaxed the

conditions for opening fresh letters of credit (L/Cs) from the existing 90 days' time to 150 days. BB will continue its foreign currency support to the commercial banks mainly for making payments of fuel oils, fertilizer and food grains import. The BB, in its *Monetary Policy Statement* for July-December, 2008 and that of January-June 2009, has provided its policy stance envisaging possible impact of global economic meltdown on the domestic economy.

The Bangladesh bank has mentioned that it will give priority to unhindered flow of private sector credit to productive sectors, with agriculture, SMEs, and the rural economy being the prime targets. Engagement in agriculture lending has been made mandatory for all private and foreign banks. BB will continue monitoring the liquidity situation in the banking system and adopt appropriate measures to overcome any temporary pressure on liquidity. BB has also indicated that it would conduct 'surprise inspections' on banks and exchange companies to ensure compliance with foreign exchange regulations and provisions of the Anti-money Laundering Act. BB report mentions that measures would be taken to divert increasing amount of remittances toward investment in productive sectors to ease the potential demand pressure and expand the economy's productive capacity. For facilitating more efficient import of essential goods, BB has made available forward hedging mechanism to importers. In view of collapse of house price bubbles in major economies, BB has taken up an initiative to construct a house price index using time series data.

### **Measures Protecting the Poor and the Vulnerable**

Under the public food distribution system (PFDS), government provides in-kind support to poor people and those affected by natural calamities and disaster. Total food grains distribution in FY2008-09 (01 July-20 November) through PFDS was 697.89 thousand metric tons. Government has recently introduced the *Rural Employment and Road Maintenance Programme* for the ultra poor and destitute women of some of the crisis prone districts, namely *Panchagarh* and *Rangpur* districts. At the end of five years' guaranteed employment, each will get cash worth of Tk.70,000 (USD1,020). During the project period, 52,000 destitute women will be employed to work in the maintenance of 90,000 kms of road network in the northern part of the country. Under the national budget for FY2008-09 government has introduced a new programme titled '*100 Days Employment Generation Scheme*' with an allocation of Tk.2,000 crore (USD291.5 million) to generate employment for 20 core man-days (2.92 million) to combat *Monga* (seasonal chronic food shortage among the absolute poor in selected areas) in greater *Rangpur* and *Dinajpur* districts.

### **Supporting Productive and Sustainable Enterprises to Safeguard Employment**

A new programme has been introduced under the national budget for FY2008-09 with a monetary support of Tk.20 core (USD 2.92 million) to provide support to low-income workers particularly for working mothers of the garment factories. Under the national budget for FY2008-09, government has continued Second Primary Education Development Programme (PEDP-II); as part of which 5.5 million primary students are receiving stipends on annual basis. Total outlay for this programme is Tk.1, 800 cores (USD 262.4 million). Under the national budget for FY2008-09, government has allocated an endowment fund (known also as 'credit whole selling') of Tk.100 core (USD 14.6 million) for the *SME Foundation* to provide credit to SMEs through private commercial banks. The *SME Refinancing Scheme* of BB has been allocated Tk.500 core (USD 72.9 million) in FY2008-09 from Tk.300 core (USD 43.7 million) in FY2007-08.

## **CONCLUSION**

In conclusion, we are in the midst of a violent unwinding of a decade long cheap credit cycle, and the dust has yet to settle. While Bangladesh has side-stepped the financial sector meltdown and sharp stock market corrections being experienced by other nations, we remain vulnerable to the longer-term global economic slowdown. It is prudent, in these times, to make informed and thoughtful reforms to our economic policies and regulatory framework, but we must not give in to the impulse of isolationism. Given our stage of development, Bangladesh can benefit enormously from the influx of foreign capital and intellectual property into both the capital markets and the real economy. Integrating into the global economic cycle, while painful sometimes is the only way forward to sustain prosperity. The policy implications of what is under our eyes are given below:

- Policy makers have to make sure that markets do not panic by continuously providing evidence on the economy's resilience in various sectors. They must proactively monitor the channels through which the global financial turmoil may start creeping into the Bangladesh economy and take appropriate mitigation measures.
- Against the background, private sectors are likely to shed employees in the country and as a result, unemployment is likely to increase in the country. The government's principal aim is to keep unemployment in check. A careful look at expenditure priorities is in order. Public spending that creates jobs, especially for the poor, will be essential. Important examples include rural and other infrastructure (rural roads, irrigation facilities, rural power); basic urban services; and well-designed safety net programs.
- Purchasing power must be increased of vulnerable groups by directly giving money or food for works so that their basic needs are met.
- It is also apparently clear that the flow of foreign aid and donation in our annual budget will decline because of the global crisis. But our national priority should be to reduce the dependency on foreign aid. We have to ensure our self-esteem in the world as a self-dependent nation. We must create food safety net and energy safety net right now to ensure our national growth to withstand the challenges.
- New business friendly policies may be adopted to attract foreign investment and a cut in interest rate by Bangladesh Bank is an option to be considered to boost investment by private sectors.
- The ongoing efforts to increase the efficiency and effectiveness of the banking sector must continue. These measures should aim to lower intermediation cost, reduce non-performing loans, improve banking services, and strengthen prudential regulations.
- Real estate developers and garment manufacturers may be given more incentives in cutting taxes and customs duties in importing raw materials so that engine of growth is maintained.
- Policy attention needs to focus on creating as much additional fiscal space as possible to prop up the domestic economy while preserving macro economic stability. As noted, the decline in global fuel and food prices has provided a welcome opportunity to regain the loss in fiscal space owing to previous higher prices. This gain should not be wasted in reversing the policy changes made in aligning domestic prices better to the global prices, especially domestic fuel prices. Additionally, efforts must intensify to raise public revenues.
- Finally, in an environment of constrained resources, greater attention to improving implementation capacity and corruption prevention in public spending becomes even more important.

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