

# Turning Point

**Bank Job Aid**

**Focus Writing Module - 3**



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**Turning Point Job Aid**

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**A Complete Preparatory Package for Bank Job Written Part**

## Session Content

1. What are the major causes for foreign exchange reserve depletion?
2. What are the impacts of dwindling reserve on the economy?
3. What are the steps have been taken so far to address foreign exchange reserve depletion?

### Data Supplement for Trend Analysis

**Foreign Exchange Reserve (USD Billion)**

2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
10.36	15.32	21.51	25.03	30.17	33.49	32.94	32.72	36.04	46.39	41.83	19._*

**Remittance Earning and Forex Reserve (USD Billion)**

Particulars	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Remittance	12.84	14.46	14.23	15.32	14.93	12.77	14.98	16.42	18.21	24.78	21.03	22.61
Reserve	10.36	15.32	21.51	25.03	30.17	33.49	32.94	32.72	36.04	46.39	41.83	19._*

**Trade Gap (USD Billion)**

2018	2019	2020	2021	2022	2023
-18.18	-15.83	-18.57	-23.78	-33.25	-1.82*

**Export - Import Trend (USD Billion)**

	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Import	67.13	68.10	64.19	61.94	89.37	79.00
Export	37.61	41.43	36.05	40.64	52.47	55.56

**Current Account Deficit (USD Billion)**

2018	2019	2020	2021	2022	2023
-9.57	-4.49	-5.44	-4.57	-18.7	\$ 892 million *

## **Causes of Foreign Exchange Reserve Depletion**

Country highest net \$41 billion reserve in August 2021 plummeted to net below \$20 billion in October 2023 witnessed gradual erosion despite several regulatory attempts; there is no good hope in rebuilding reserve. Global supply chain disruption along with Federal Reserve's aggressive money market mechanism, multiple exchange rates in market, mounting trade gap and current account deficit, poor remittance and FDI growth let the official reserve to fall more than half in last one year and aggravated macroeconomic situation for Bangladesh. Major facts behind this reserve depletion are:

1. Exchange rate crumble in 2021 and introduction of multiple exchange rates in 2022 made the Central Bank's reserve as the cheapest source of dollar and thus Bangladesh Bank was bound to sale more than \$15 billion from reserve in last one year. Fundamental import necessity and global price hike of petroleum and food grains induced more dollar use and thus the reserve eroded in last two years. Because the official rate falls significantly below market rate, remitters resorted to informal channels to access higher rates and thus thinner remittance contributing less in reserve rebuilding.
2. Approximately \$33 billion trade gap and \$18 billion current account deficit put unbearable pressure on reserve position. This situation was aggravated by financial account deficit [*The reduction in foreign fund inflow turned the financial account to a deficit of \$4 billion in FY23 from a surplus of \$15 billion in FY22; Source: BOP, BB*] which bound the central bank to pay current account burden from the reserve position and thus it dwindled sharply. Moreover, approximately \$12 billion export proceed is yet to be repatriated which made a great difference in reserve position.
3. Interest rate cap in recent past kept money cheap, pulled import demand and raising interest rate in the global market resulted in decreased private sector borrowing from foreign sources, interest payment on borrowed fund raised, thereby putting pressure on reserve and obstructing its rebuilding process.

4. In order to keep inflation check, Federal Reserve raised interest rate 11 consecutive times and which is highest in last 22 years. Dollar became costlier globally as well as local currencies depreciated, raised demand pool pressure and thus atrophying foreign exchange reserve.
5. Slow growth in export and remittance income, almost stagnant FDI & lack of fresh foreign capital inflow, more overseas loan repayments by businesses than receipts, slower repatriation of export proceed, falling private sector loan from external sources made the dollar's supply side thinner. High cost and volume of basic importation, rising repayment of foreign debt, a surge in outflow of foreign portfolio, open market dollar sale for soothing dryness of dollar market etc. made the demand side thirsty which ultimately let the reserve being depleted in short time.

Dollar is also a commodity whose price and availability largely determined by the supply - demand mechanism prevailing in the market. Dysfunctional foreign exchange market mechanism and supply - demand mismanagement of dollar let the reserve position to be aggravated for Bangladesh which is expecting to regain its lost stability.

### **Impacts of Depleting Reserve on Economy**

Country highest net \$41 billion reserve in August 2021 plummeted to net below \$20 billion in October 2023 witnessed gradual erosion despite several regulatory attempts; there is no good hope in rebuilding reserve. Global supply chain disruption along with Federal Reserve's aggressive money market mechanism, multiple exchange rates in market, mounting trade gap and current account deficit, poor remittance and FDI inflow let the official reserve to fall more than half and aggravated macroeconomic situation for Bangladesh. Most vibrant impacts of depleting reserve are:

1. To restore Balance of Payment (BOP) stability as well as macroeconomic stability in the face of depleting reserve, Bangladesh had to take loan of \$4.7 billion from IMF by accepting 30 conditionalities and thus the country lost her policy independence.

2. Systematic import restrictions resulted in approximately 16% import decline in last FY and thus less capital machineries and raw material importation resulted in less output and thinner GDP growth in last FY which is expected to remain same in current year.
3. Less import and less production resulted in less supply of goods and services and thus fueling inflation. Moreover, exchange rate disruption caused by supply demand gap of foreign exchange made import costlier and fuelled rising inflation.
4. Bangladesh's long-term ratings downgraded by Moody's Investors Service, long-term rating outlook negative from stable by S&P Global Ratings, Outlook on Bangladesh to 'Negative' by Fitch Ratings due to hardship in satisfying foreign payment obligation has downgraded country image and investors' confidence.
5. Bangladesh is facing hardship in importing basic necessities like petroleum products, coal and LNG, food grain, industrial raw materials etc. which is threatening the existing production system, making production costlier and creating uncertainties in future investment.

Adequate reserve is a national confidence. Continuous reserve erosion couldn't be stopped though massive steps have been initiated in last one and half year which shaded country image and thus downgraded public confidence. Panic in market forces stakeholders being conservative and make the way difficult to restoring economic stability.

### **Steps taken for managing Foreign Exchange Reserve Depletion**

To address the issues behind depleting reserve and promote its rebuilding, Bangladesh Bank pursued various measures for exchange rate stability. Initiatives were taken to improve the current account balance by incentivizing foreign currency inflows and containing foreign exchange outflows. Major steps have been taken are:

1. BB has allowed the BDT to depreciate significantly (approximately 30%) along with supplying a huge amount (\$15 billion in last one year) of foreign exchanges to the market from its international reserves to mitigate the growing pressure on the exchange rate.

2. The Bangladesh Bank announced the unified exchange rate to comply with a condition of the International Monetary Fund (IMF). The objective of introducing a unified exchange rate was aimed at easing pressure on foreign exchange reserves.
3. To increase the supply of foreign currency, the bank's exports retention quota (ERQ) and net open position have been reduced, while borrowing from OBU is allowed by DBU.
4. BB has made a requirement to encash 50 percent of the balance held in exporter retention quota (ERQ) accounts.
5. To reduce the demand for foreign currency, BB increased annual interest on EDF loans from 4.00 to 4.50 percent for manufacturer-exporters. Moreover, BB has allowed importers to extend guarantees and the maturity of suppliers' and buyers' credit, and domestic banks to borrow from offshore operations to settle certain import payments.
6. In line with the government's austerity measures, BB increased overall LC margins and advanced payment requirements for non-essential and luxury goods imports.
7. Pre-authorization for LCs over USD 3 million has also been required to prevent over and under invoicing related trade-based money laundering.
8. Temporary restrictions were placed on government officials' overseas travel for training and study tours. Personal foreign visit, including training, workshop, seminar, and study tour of bank officials, has been restricted.
9. Banks now can provide incentives freely on foreign remittance. In order to boost foreign currency inflows, BB has implemented measures to ease fund transfers through Internet banking for remittances, removing previous ceiling on such truncations.
10. To further incentivize non-resident foreign currency deposit (NFCD), BB has raised NFCD rate. Additionally the cap on the interest rate for deposits made in non-resident foreign currencies has been eliminated, making it more attractive. Simplifying the process for wage earners' remittances, the documentation requirement has been eliminated, allowing for seamless transfer of any amount.