DHAKA TUESDAY MAY 31, 2022, JAISHTHA 17, 1429 BS ● starbusiness@thedailystar.net

Star BUSINESS

Convert export proceeds into taka fast

BB asks banks

STAR BUSINESS REPORT

Bangladesh Bank has asked banks to convert major export earnings of businesses into taka immediately as it looks to increase the supply of US dollars in the economy.

The rule will be applicable for the value-added portion of export earnings. The value-added portion refers to the export proceeds that are available to exporters after their import bills for back-to-back letters of credit have been met.

"It is observed that the value-added portion is not encashed into the taka immediately on the repatriation of export proceeds, resulting in delayed cash support to exporters for meeting working capital needs in the taka," said the central bank in a notice yesterday.

Banks have recently alleged that many exporters have not converted their dollars into the taka as the local currency has weakened drastically

Banks have recently alleged that many exporters have not converted their dollars into the taka as the local currency has weakened drastically.

The exporters thought that they would benefit more if US dollars are not converted immediately, intensifying the foreign exchange crisis.

The latest measure from the BB came after the foreign currency reserves fell to $42.29 billion on May 25 in contrast to $46.15 billion in December, driven by higher imports against moderate exports and lower remittance flows.

In Bangladesh, banks are allowed to retain repatriated export proceeds in a foreign currency in a single pool following the encashment of the local value-added portion. These funds are useable only for the settlement of back-to-back import payments of relative exporters.

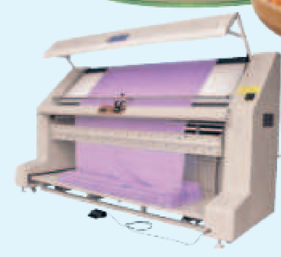
The retention of export proceeds in foreign currency facilitates exporters to settle back-to-back liabilities without facing exchange losses.

In another notice, the BB said exporters would have to sell their export proceeds to the banks through which they ship goods.

READ MORE ON B3

IF LENDING RATE CAP IS LIFTED...

- Interest rates on lending and deposit will go up
- Demand for loans including import financing will come down
- Imports will decrease
- Demand for dollar will fall
- Forex market may become stable
- Inflation will decline due to tight money supply
- Policy rate hike will be effective



WHAT'S WHAT

- BB imposed cap on lending rate in Apr 2020
- Inflation stood at **6.29**pc in Apr 2022
- Inflation target for FY22 is **5.3**pc
- Private sector credit growth **12.48**pc in Apr
- Annual private credit growth target **14.8**pc

EXPERTS SAY ON LATEST POLICY RATE HIKE

- Banks now face rising loan disbursement cost
- Credit demand from borrowers will not decrease

HIKE IN KEY INTEREST RATE

Case for lifting lending rate cap strengthens

AKM ZAMIR UDDIN

The case for withdrawing the lending rate cap, set in motion more than two years ago, has strengthened after the Bangladesh Bank hiked its key interest rate for the first time in a decade to cool inflationary pressures.

Experts urged the central bank to move away from the ceiling in order to bring back stability to the financial sector, which is facing a crisis owing to depleting foreign currency reserves and the devaluation of the local currency.

They described the hiking of the policy rate by the Bangladesh Bank by 25 basis points on Sunday as time-befitting and called on the BB to abolish the lending rate cap to make it effective.

The central bank imposed the interest rate cap on loans on April 1, 2020, as per the direction of the government. In August last year, it asked lenders not to set the deposit rates on fixed-term deposits below the inflation rate, as higher consumer prices have turned the actual return on such savings negative.

Ahsan H Mansur, executive director of the Policy Research Institute of Bangladesh, said that the taka would become dearer if the central bank withdrew the lending cap.

"Hiking the policy rate will not be able to reduce the credit demand unless the interest rate cap on lending is withdrawn."

The increase in the key lending rate of the BB, the repurchase rate at which a central bank lends money to lenders, to 5 per cent means banks will have to pay more to borrow. So, lenders will have to adopt a cautious stance while disbursing loans.

The policy rate hike will not tighten the money supply to a significant level, Mansur said.

But if the interest rates on loans go up, clients will not feel encouraged in borrowing from banks. Similarly, if the deposit rate increases in keeping with the lending rate, it will provide better returns to savers and allow banks to woo funds.

"This will make keeping the taka at banks attractive," said Mansur.

The withdrawal of the lending rate cap is also expected to bring back stability to the foreign exchange market.

Mansur also explained that the cost of funds for import financing would go up when the lending cap is withdrawn.

Banks are allowed to charge a maximum of 9 per cent for post-import financing.

"Importers will take a cautious stance when the interest rate on post-import financing moves higher," said Mansur, also a former official of the International Monetary Fund.

This will rein in import payments, which have gone up exponentially in recent months owing to the higher commodity prices in the global markets and the weakening of the local currency at home.

Bangladesh's import payments stood at $61.52 billion between July and March, up 44 per cent year-on-year, while exports grew 33 per cent to $36.61 billion.

The large import payments created a record trade deficit of $24.90 billion in the first nine months of the current fiscal year ending in June. This has compelled the central bank to inject more than $5.83 billion into the market, sending foreign exchange reserves low.

The reserves stood at $42.29 billion on May 25 in contrast to $46.15 billion on December 31.

The surge in imports, which are needed to feed the economy rebounding from the pandemic-induced slowdown, has also created tremendous pressure on the taka, compelling the central bank to depreciate the local currency seven times this year alone.

The latest devaluation came on Sunday when the taka was allowed to lose value by 1.25 per cent to Tk 89.

A BB official said that import financing was one of the main reasons behind the recent upward trend of credit growth in the private sector. The credit growth stood at 12.48 per cent in April, albeit slower than the BB's target of 14.8 per cent for the current fiscal year.

The curb in imports may lead to a decline in domestic demand, which will ultimately go on to help the government tame inflation, which rose to an 18-month high in April.

Salehuddin Ahmed, a former governor of the central bank, says that the central bank should withdraw the interest rate cap on lending as it will help ease the inflationary pressure.

He also suggested the central bank not impose any ceiling on the exchange rate of the taka against the US dollar.

Mustafizur Rahman, a distinguished fellow of the Centre for Policy Dialogue, urged the government to revisit the rates on loans and deposits.

Senior bankers also voiced concerns that lenders would face difficulties in running banking operations unless the lending rate ceiling is removed.

Profitability in banks will decrease because they have to borrow at a higher rate from

READ MORE ON B3

Financial market liberalisation may be derailed

Frequent regulatory interventions to blame

AHSAN HABIB

Bangladesh set out for financial sector reforms in the 1980s.

The interest rates were partially deregulated in 1989 to bring flexibility in determining the deposit and lending rates. In 1992, the interest rate bands for lending were removed for all sectors, except agriculture, small industries, and exports.

It took a step further in 2003 when the government adopted a free-floating exchange rate regime to determine the value of the local currency on the basis of demand and supply, which forms the theoretical basis of modern economics.

Still, regulatory intervention in the markets has not become a thing of the past, posing a threat to the progress that the country has attained so far in financial liberalisation.

Sometimes, regulatory measures are taken on an ad hoc basis. And every now and then, they are put in place, due to, economists say, a lack of knowledge and good governance, in absence of empirical analysis, and often to provide undue advantage to a few big players.

In the money market, the interest rates of banks are determined, not by the market forces, but by the Bangladesh Bank's order. The central bank also controls the foreign exchange market strictly.

In the stock market, the Bangladesh Securities and Exchange Commission (BSEC) even goes further. It tries to control the market movement by imposing a floor price or reducing the limit of the circuit breaker although it is not its core task.

"Nothing is market-determined in the financial market of Bangladesh," said Zahid Hussain, a former lead economist of the World Bank's Dhaka office.

"The interest rate is determined by the central bank. The minimum wage of employees is also set by the regulator. Fees and charges limit of financial services are also dictated. Even sector-wise, credit targets are also given."

"So, there is no free market anymore in the financial sector. The companies are doing business based on the volume only."

Selim Raihan, executive director of the South Asian Network on Economic Modeling, blames market imperfection for the intervention.

READ MORE ON B3

STOCKS

DSEX ▲	CASPI ▲
0.30%	0.29%
6,388.65	18,702.78

COMMODITIES

Gold ▲	Oil ▲
$1,856.25 (per ounce)	$115.73 (per barrel)

ASIAN MARKETS

MUMBAI	TOKYO	SINGAPORE	SHANGHAI
▲ 1.90%	▲ 2.19%	▲ 0.26%	▲ 0.60%
55,925.74	27,369.43	3,238.92	3,149.06

UK to lend $450m in five years

PORIMOL PALMA

British International Investment (BII) has embarked on an ambitious plan of lending $450 million to Bangladesh over the next five years, finding that the country has a stable government and policy support for private sector development.

Private sector financing in the areas of renewable energy and green factories will be the focus of the fund, said top officials of the BII, the development finance institution of the UK government.

The plan was made public during BII Chief Executive Officer Nick O'Donohoe's visit to Bangladesh last week.

"We focus on the countries that have a strategic alliance with the UK, with ongoing development challenges, and ideally, having a stable government and stable economic policies that create jobs," said O'Donohoe.

"All of these are present in Bangladesh," he said in an interview with The Daily Star at the British high commission in Dhaka.

Currently, the BII has a portfolio of about $300 million in Bangladesh, supporting 11 businesses and two funds, across a variety of sectors, including financial services, infrastructure, manufacturing and food processing.

British International Investment

Following a visit to Dhaka in 2019 by the officials of the then Commonwealth Development Corporation, which is the former name of the BII, it has already established its Bangladesh office in Dhaka.

This shows the increasing interest of the development financial institution in Bangladesh where the private sector is rapidly expanding.

O'Donohoe said the BII keeps green financing a top priority in line with the UK's commitment to climate finance.

Given the lack of adequate wind and land, the country does not have much scope on investing in wind or solar power. Therefore, it will look to invest in green factories and projects, he said.

"Another important area is commercial industrial application. Individual industries or hospitals can set up solar power systems. Bangladesh is one of the target countries for this."

He thinks Bangladesh can attract more foreign direct investments by better focusing on its digital transformation.

Unlike some of the African countries and also countries like Pakistan and Nepal, Bangladesh is already active in digital transformation and the BII could find more opportunities in the sector.

On the potential of Bangladesh in terms of foreign investments, BII Country Director M Rehan Rashid said there were positive moves from the government side.

The investment process needs

READ MORE ON B2