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Exchange Traded Fund
A New Era of Hope for Investors

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The BICM Financial Market Review provides analytical insights about the performance of the financial market in Bangladesh on a monthly basis.

“With the march of economic restoration time period after COVID-19, the economy has been facing challenges from different country risks like wars and other disturbing economic issues, but Bangladesh is becoming resilient to these shocks with the course of time.”



Economy of Bangladesh

Main indicators at a glance

Countries	Nominal GDP (as of Apr, '22) (USD in billion)	Real GDP Growth (as of Apr, '22) (yearly % Change)	Inflation Point to point (%) (as of July, '22)	Current Account Balance: (% of GDP)	Interest Rates (%) 10-years Treasury Bond	Currency Exchange Rates (per USD)
Bangladesh	396.543	6.415	6.33	-3.74	8.345	102.33
Emerging Economies						
India	3,534.74	8.153	7.00	-1.09	7.232	81.61
China	19,911.59	4.373	2.50	1.79	2.636	7.12
Developed Economies						
USA	25,346.81	3.708	8.26	-3.57	3.200	1.00
UK	3,376.00	3.749	9.87	-2.59	2.910	0.88

Appreciation or Depreciation of Different Currencies against USD

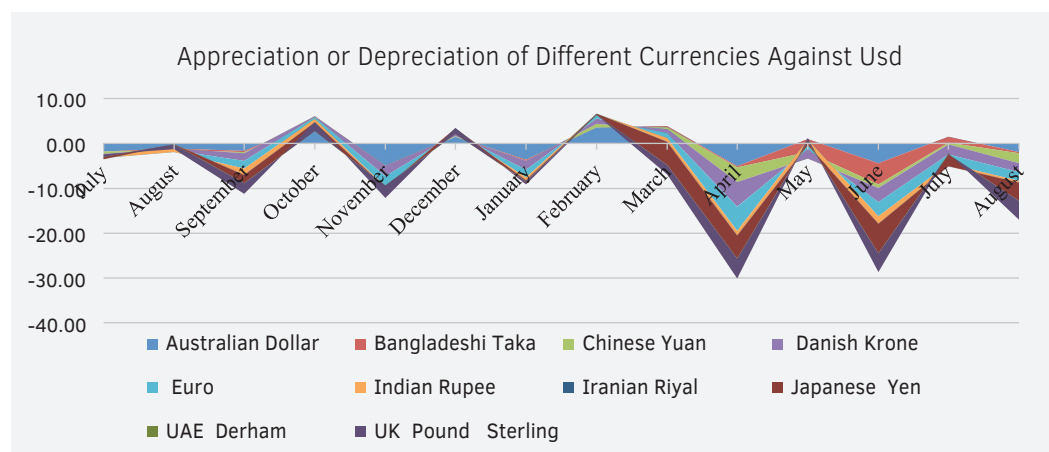


Figure 1: Appreciation or Depreciation of Different Currencies against USD

A visual tour of the key statistics

Import-Export Growth % upto July, 2022

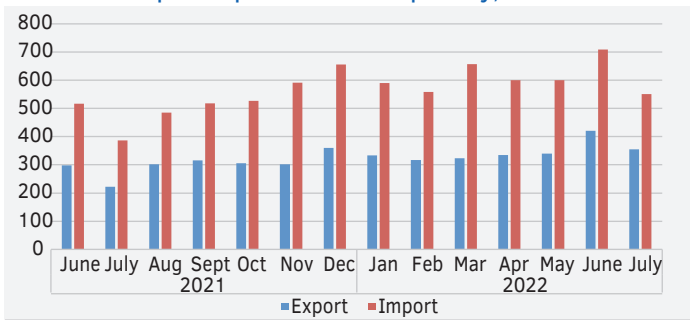


Figure 2: Import-Export Growth Percentage of Bangladesh

Percent change of Foreign Remittance of Bangladesh

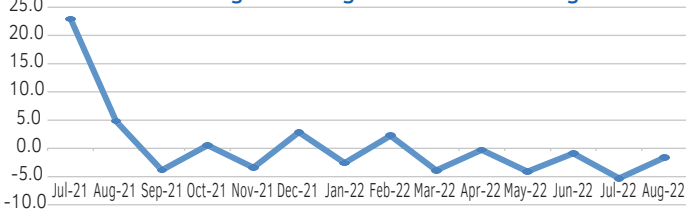


Figure 3: Foreign Remittance of FY 2021-22 (Year over Year Growth)

Percentage change of Foreign Reserve

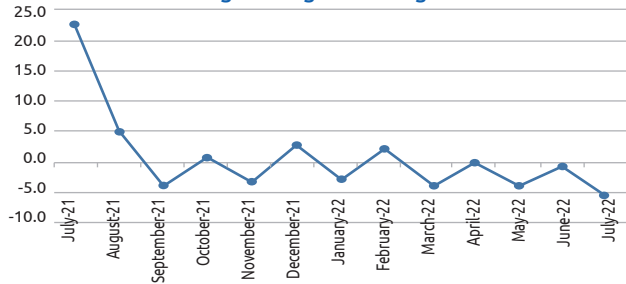


Figure 4: Percent Change of Foreign Reserve

Period Average Exchange Rate

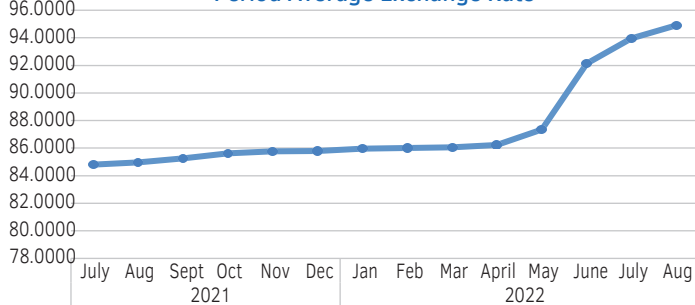


Figure 5: Percent Change of Foreign Reserve of Bangladesh

Country-wise Workers' Remittance

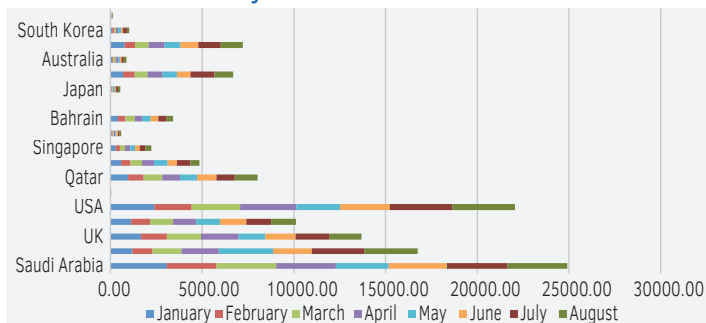


Figure 6: Country-wise Workers' Remittance

Total Domestic Credit

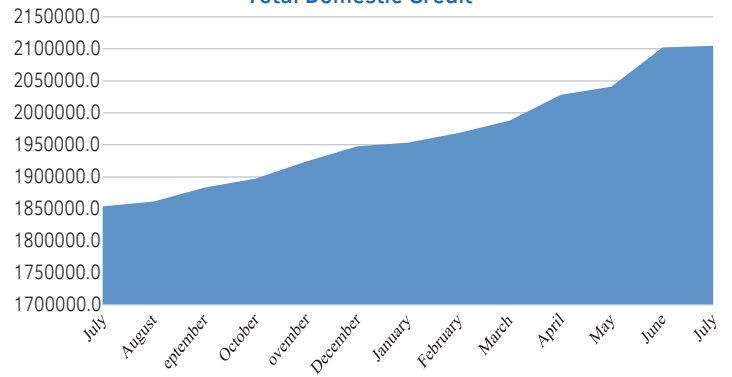


Figure 7: Total Domestic Credit

12- Month Average Inflation (In Percentage)

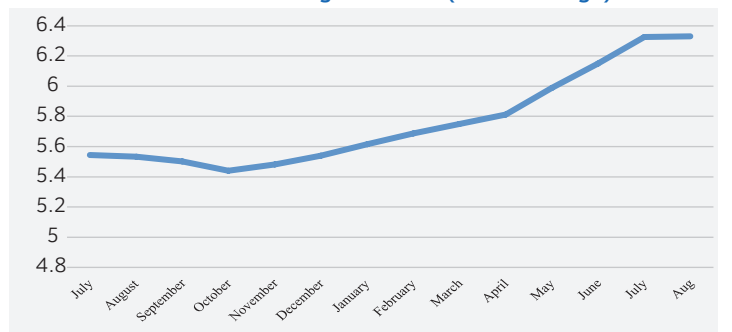


Figure 8: 12-Month Average Inflation (in %)

Numbers to Note

1. Comparing to the UK Pound Sterling, Japanese Yen, and Euro, BDT was quite resilient to the USD's sensitivity to change.
2. Both export and import reduced in July 2022. But the export increased higher than import comparing to previous month.
3. Foreign remittance growth reduced to 8.8% in this August 2022 comparing to a surging growth in July 2022 that was 12%.
4. The reserve is now 38.95 billion USD, a 1.6% decrease than previous month.
5. The average monthly exchange rate is now 94.91 Taka per USD.
6. The Debt to GDP percentage in 2021 is 21.8%, which was 19.5% in the previous year.
7. The inflation is 6.33%, which was 6.32% in the previous month.
8. Bangladesh gets its highest remittances from Saudi Arabia, the USA, and the UK.

Economic Challenges Ahead

1. As the Russia-Ukraine war is still ongoing, the turmoil may devalue BDT with respect to USD to a higher amount continuously.
2. The USD crisis in the global market may imbalance the export-import condition of Bangladesh.
3. As the oil price crisis is over evaluating the price surge to upper percentage, the inflation rate surge will follow up.
4. The reserve shortage increase is also a bad indicator, and 2023 may be a big challenge for meeting the external debt.
5. The issues of political imbalance with Rakhine and the military of Myanmar and the inclusion of China and India in it may pressurize Bangladesh and its economy.

The Capital Market Circling Stagnant Index of 6500 in September 2022



Capital Market

In September 2022, the market demonstrated a 0.07% increase in the DSEX index compared to the previous month of August

It is apparent by analyzing the capital market snapshot of September 2022 that the DSE market indices demonstrated an analogous movement with a minor slide down in the second week of the month. The DSEX index has increased by 0.07% compared to that of the previous month. The prices of the majority of issues declined along with a large chunk of stocks being on the floor price as investors clustered towards only a few stocks. Other indices have also increased, whereas DSMEX weakened compared to those of August. During September, 97 issues were advanced, 144 issues were declined, and the remaining 132 issues were unchanged.

The market witnessed a quick correction in the second week along with a slow recovery in the last two weeks. Investment in the market dropped due to investors' inertia to invest in stocks in fear of having their investment stuck for a long time. Institutional and eligible investors inhibited their exposure, causing many of the stocks to be on the floor price. The decrease in the flows of foreign remittances, the widening trade deficit, along with the free fall in foreign exchange reserves to \$36 billion, has created a panic among investors to return to the capital market. The main catalysts for the stagnant market could be the presence of global inflationary pressure and geo-political turmoil.

DSE Market Indices

Index Name	1-Sep-22	31-Sep-22	Change	% Change
DSEX	6508.61	6512.89	4.28	0.07%
DSES	1409.19	1419.73	10.54	0.75%
DS30	2305.66	2330.42	24.76	1.07%
CDSET	1250.21	1269.15	18.94	1.51%
DSMEX	1922.13	1689.52	-232.61	-12.10%

Scripts Movement (Monthly Average)	Advance	Decline	Unchanged
	97	144	132

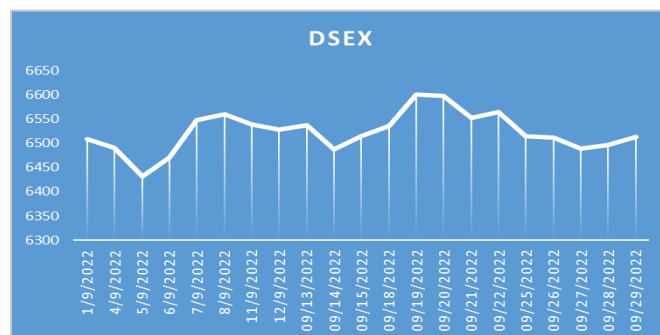


Figure 9: DSE Market Indices (Data Source: DSE Website)

Market Aggregates

	29 Sep 2022	31 Aug 2022	Change	% Change
Average Market Capital (TK Million)	5,208,715.69	5,108,563.70	100,151.9966	1.96%
Average Traded Value (TK Million)	16,895.35	12,736.20	4,159.154636	32.66%
Average Number of Trades	244,091.24	215,571.80	-(28,519.44)	-13.23%
Average Trade Volume	293,472,158.86	325,291,688.30	-(31,819,529.44)	-9.78%

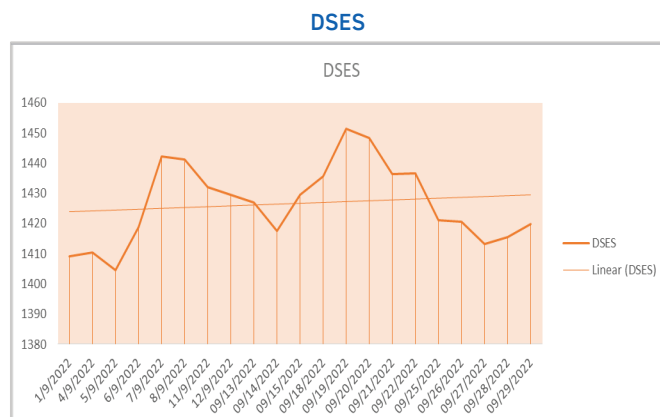


Figure 10: Market Aggregates (Data Source: DSE Website)

The AD ratio compares the number of stocks that increased in value to the number of stocks that decreased in value. By shedding light on the AD ratio of this month, it is evident that the 21-trading day denoted a downward trend in the market.

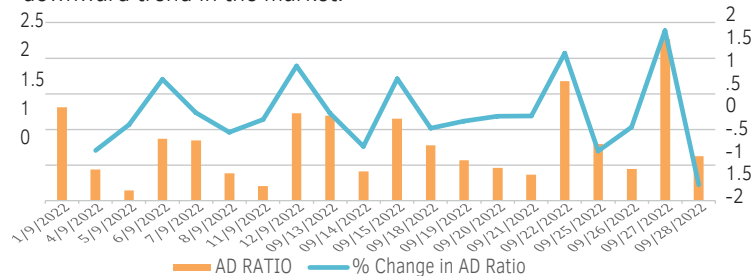


Figure 11: AD Ratio (Data Source: DSE Website)

The government's response to fighting these challenges with a higher policy rate aims to orchestrate the market. Most of the sectors in the capital market witnessed negative returns on average in September. The travel and leisure, IT and jute sectors of the market have contributed by a large percentage, whereas the textiles and insurance sectors experienced a downtrend in return.

Rising trend in private sector credit growth brought it very close to the fiscal target of 14.1%



Money market section has been designed to make the readers comprehend regarding behaviors of key variables. The first section delves into the scenarios based on the most recent available data as well as the observations thereon. The second section, Key Takeaways, has been depicted to derive the possible explanations of the changes. Total Deposits as of July 2022 saw around 8.5% Year on Year (YoY) growth, where Demand Deposits added 14.26% and Time Deposits 7.74%. If we relate the growth to the previous month, total deposits grew negatively by 0.39, where Demand Deposits and Time Deposits contributed -4.78% and 0.25%, respectively. [Table-01]

Items	Jul 2022	Jun 2022	Jul 2021	Percentage Changes	
				Jul 2022 over Jun 2022	Jul 2022 over Jul 2021
Demand Deposits*	17,98,283	18,88,594	15,73,840	-4.78	14.26
Time Deposits*	1,28,54,406	1,28,22,175	1,19,30,498	0.25	7.74
Total	1,46,52,689	1,47,10,769	1,35,04,338	-0.39	8.5

Table 01: Deposits held in DMBS (Tk in Million)

Advances and Bills (Import & Inland Bills) saw a 14.12% and 33.42% YoY growth, respectively, as of July 2022. However, if we look at the monthly growth from July to June 2022, we see that it is 0.11% and 2.2%, respectively. Investments by banks saw a 12.94% YoY growth. However, it encountered negative growth of -1.09% compared to previous months. [Table-02]

Items	Jul 2022	Jun 2022	Jul 2021	Percentage Changes	
				Jul 2022 over Jun 2022	Jul 2022 over Jul 2021
Advances	1,32,64,525	1,32,49,422	1,16,64,915	0.11	14.12
Bills (Import & Inlands Bills)	3,49,234	3,41,725	2,40,246	2.2	33.42
Investments	35,66,775	36,05,922	32,04,832	-1.09	7.19
Total	1,71,80,534	1,71,97,069	1,51,09,993	-0.1	12.94

Table 02: Bank Credit (Tk in Million)

Note: *Excludes Interbank Deposits and Government Deposits

The interbank call money rate soared above 5.50%, with an average of 5.53% in September [Figure 01]. Both the nominal lending and deposit rate have been stagnant over the years, reaching an average of 7.14% and 4.02%, respectively. [Figure 02]

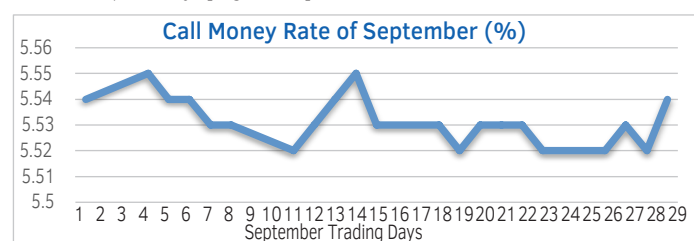


Figure 01: Call Money Rate of September

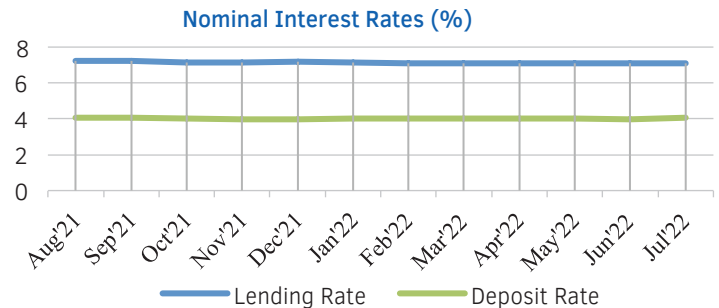


Figure 02: Nominal Interest Rates

Cost of funds for Non-Bank Financial Institutions showed up downward compared to June 2022, reaching 6.55% as of July 2022. A downward trend was also seen in the adjusted cost of funds, which is the interest-bearing funds minus the low-cost specific purpose plan funds, and it reached 7.52% as of July 2022 [Figure 03].

The target of Government borrowing from the banking sector has been set quite high at 1,06,334 crore Taka for FY23, which is around 46% higher than the actual figure of FY2022 [Figure 04].

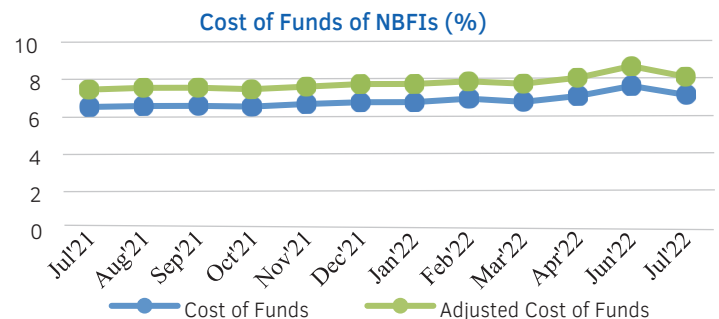


Figure 03: Cost of Funds of NBFIs

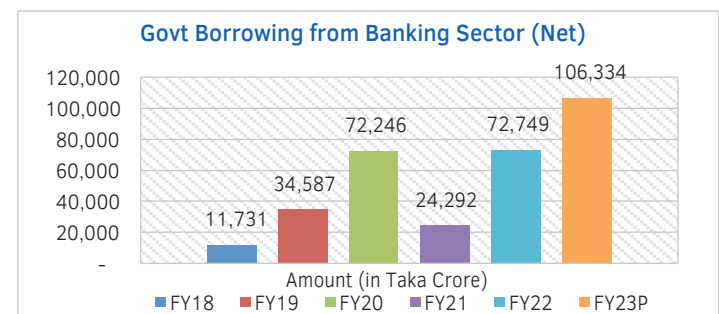


Figure 04: Govt. Domestic Borrowing

The private sector credit growth has been demonstrating a robust growth of nearly 14.07% as of August 2022 [Figure 05]. The foreign currency reserve has been facing a continuous downward trend, reaching 36.44 billion USD as of September, 2022 [Figure 06].

Private Sector Credit Growth (%)

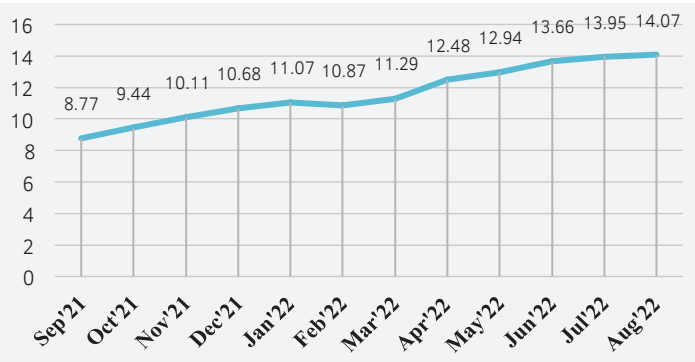


Figure 05: Private Sector Credit Growth

Foreign Currency Reserve (USD Billion)

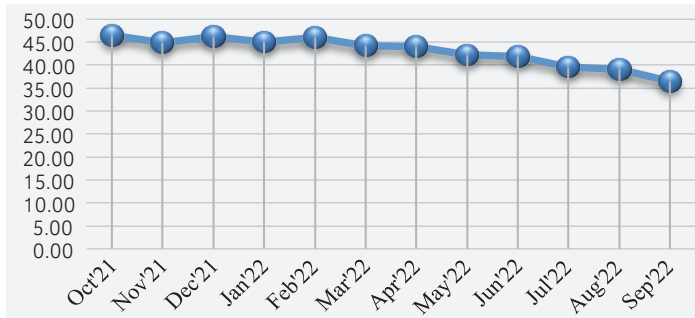


Figure 06: Foreign Currency Reserve

The yields on both T-Bills and T-Bonds have increased significantly over the years. As of September 26, 2022 [Figure 07], yields on T-Bills for 91, 181 and 364 days have reached 6.04%, 6.48% and 6.83%, respectively. Following the same trend, the 2-, 5-, 10-, 15-, and 20-year T-Bonds' yields reached 7.52%, 7.77%, 8.10%, 8.50% and 8.55% respectively [Figure 08].

Yields on T-Bills (%)

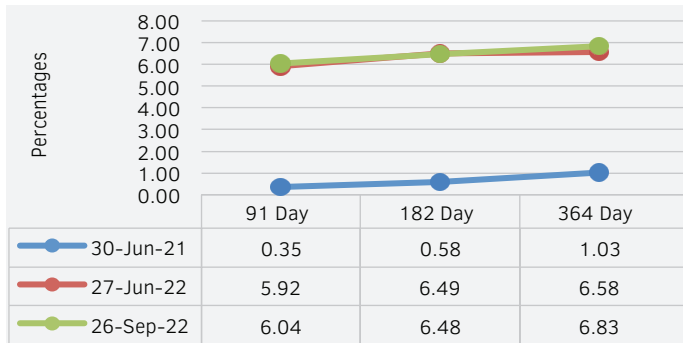


Figure 07: Yields on T-Bills

Yields on T-Bonds (%)

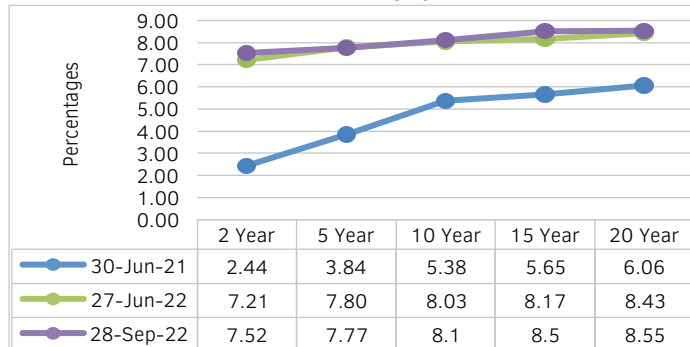


Figure 08: Yields on T-Bonds

Trends in Financial Inclusion and Digital Finance Statistics

As a part of digitalization, the number of internet banking users has reached 54,72,264 as of July 2022, a 2.18% increase compared to the previous month [Figure 09]. Gender-wise Mobile Financial Service (MFS) users give us a positive indication that male and female share almost equal percentages, nearly 58% and 42%, respectively as of July 2022 [Figure 10].

No. of Internet Banking Customers [July, 2022]

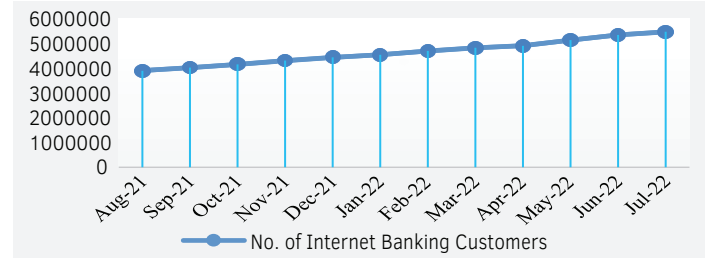


Figure 09: Number of Internet Banking Users

Gender-wise MFS Users [as of July, 2022]

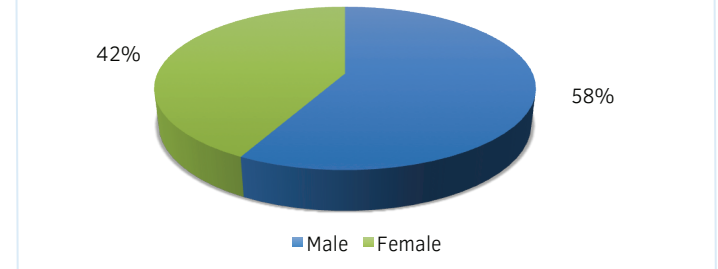


Figure 10: Gender-wise MFS Users

In recognizing the interaction with e-banking and e-commerce gateways, we observed that around 71.81% of transactions took place through Automated Teller Machines (ATMs), 11.33% in Point of Sale (POS), 8.20% in Cash Recycling Machine (CRM), and 8.66% in e-commerce [Figure 11]. In terms of the kinds of services offered by the agent banks, rural people outpaced urban [Figure 12].

E-Banking and E-Commerce Transactions [as of July, 2022]

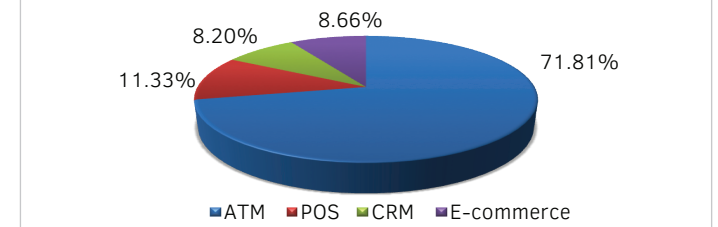


Figure 11: E-Banking and E-Commerce Transactions

No. of Agent Banking Transaction (July 2022)

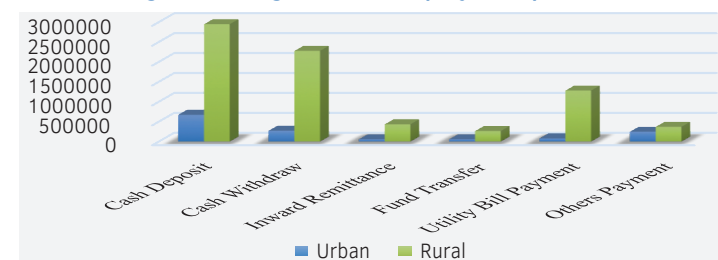


Figure 12: Number of Agent Banking Transactions

Key Insights:

- ▶ Despite low deposit rates in comparison to inflation, total deposits increased by nearly 8.5% due to people's trust in the banking sector and lack of investment opportunities. The rise of the middle-income group and,

subsequently, the expansion of the workforce have also contributed to this growth.

- ▶ Advances, a component of bank credit, has demonstrated a robust growth owing to the fixed interest rate regime and the revival of the economy from the pandemic. Rising import payments and the strong dollar have propelled the strong YoY growth in bill payments.
- ▶ The call money rate has been in strong position, soaring above 5.50% in September. Possible reasons may include the high purchase of USD by banks to settle import bills as well as the government borrowing from the banking sector. Furthermore, nearly 62 percent of the banking sector's excess funds in Bangladesh are concentrated in just nine banks, leaving the remaining cash-strapped banks to rely on the call money market to meet their immediate liquidity needs. This further pushed the rate up.
- ▶ Due to the fixed band of interest rates, both the lending and the deposit interest rates are in a stable position, thus the spread between them demonstrates stagnant.
- ▶ Though both the cost of funds and adjusted cost of funds decreased slightly in July, the yearly averages of both the variables hovered around 6.55% and 7.52%, respectively. The high cost of funds of NBFIs may have resulted from the liquidity squeeze, lack of digitization and automation.
- ▶ The actual government borrowing from the banking sector for FY22 was 83.34% of the revised target of Tk 87,287 crore. However, the proposed target for FY23 is around 2.4% of GDP. Such borrowing to meet the budget deficit results from lackluster performance in collecting revenues as well as sharp falling investment in savings certificates.
- ▶ Rising trend in private sector credit growth brought it very close to the fiscal target of 14.1%. Despite the central bank's third attempt to raise the policy rate in four months, credit growth has kept on rising. Possible explanations may include the lending rate cap on banks and NBFIs by 9% and 11%, respectively, as well as the resumption of the economy after the pandemic. In addition, the depreciation of Taka as well as the high import payments further aggravated the growth.
- ▶ Foreign exchange reserve endures the downward pressures despite the various measures taken by the central bank. The rising import payments as well as the \$1.73 billion payment to the Asian Clearing Union on September 8th squeezed the reserves further.
- ▶ Both T-bills and T-bonds are the instruments that the government uses to borrow from the banking sector. Compared to one year ago, the yields on both of the rates have increased significantly as the government has been borrowing from the banking sector. According to experts, such high yields may cause the banks to be unwilling to lend to the private sector because they can obtain similar yields by simply lending to the government.
- ▶ The outbreak of COVID-19 in 2020 accelerated internet banking manifold as account holders were forced to do banking from home. The use of internet banking has been continuously prevailing on an upward trend, registering 122.60% growth in FY22. The monumental growth has taken place owing to fast-growing internet users as well as the wide acceptability of smartphones and digital services.
- ▶ Mobile Financial Service (MFS) has reshaped the entire payment system of Bangladesh. There are around 18 crore account holders where male and female ratios are almost the same, conducting nearly 2 crore transactions through MFS daily.
- ▶ Through the adoption of cutting-edge technology, banks have been continuously trying to uplift their customers' experiences. Uses of ATM, POS, CRM and E-commerce sites are the vibrant examples of it.
- ▶ Just a decade ago, access to financial products for the remote areas of Bangladesh was unavailable and unaffordable. Thus, the introduction of agent banking saw a remarkable growth in rural areas. For example, there is a sharp 43% increase of transactions in FY22.

Data source: Bangladesh Bank Website



Imran Mahmud



Insights

Exchange Traded Fund A New Era of Hope for Investors

Exchange Traded Fund (ETF) is not a new concept for the capital market regulators of Bangladesh. BSEC has been trying to launch ETFs since 2015 and has come up with regulations, namely “Bangladesh Securities and Exchange Commission (Exchange Traded Fund) Rules, 2016” to promote the market.

After all these years, the Dhaka Stock Exchange Limited (DSE) announced that an ETF will debut in the market in September-October 2022 with investments in just 30 companies included in the DS30 index. With the arrival of the news, a series of queries emerged among the investors concerning the nature, mechanism, stakeholders, and benefits that the product would bring to the investors.

ETFs, as the name implies, are hybrid investment products that consist of a basket of stocks that are traded on exchanges like any other share. In 1993, the first U.S. ETF was launched to follow the S&P 500 index. Since then, it has not seen any downtrend in its journey (Figure 29).

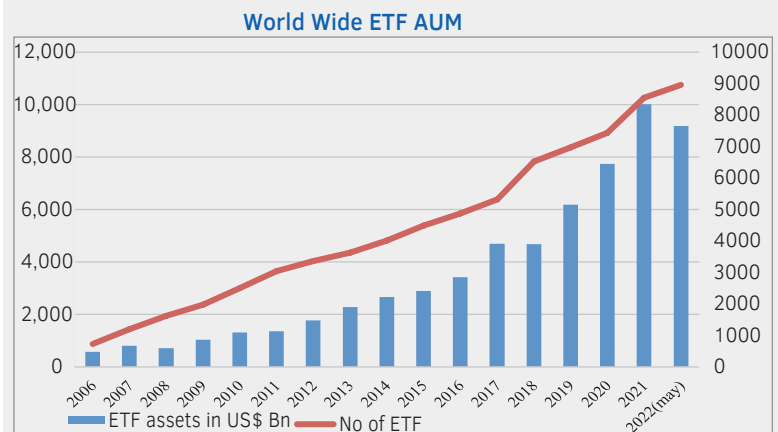


Figure 29: Worldwide ETF Asset under Management (Source: etfgi.com)

ETFs will be managed by an Asset Management Company (AMC) for a fee according to the Exchange Traded Fund Rules 2016. With the introduction of ETFs in DSE, there will be a lot of confusion among investors regarding the comparison of different securities existing in the market. Table 3 depicts the key differentiating factors among similar securities.

Issue of Comparison	Open Ended Mutual Fund	Closed -End Mutual Fund	Exchange Traded Fund
Fund Size	Can be extended or contracted back	Fixed	Flexible and can be extended or contracted
Value Disclosure	Weekly	Daily	Real-Time
Sale Price	Purchase or sold at NAV	Traded premium or discount to NAV	Trade very close to actual NAV
Place of availability	AMC itself	Through Exchanges (DSE or CSE)	Through Exchange were listed or fund itself
Management fees	Higher than ETF but lower than Closed End MF	Higher with implicit charges	Lower than Closed End and Open -End MF
Disclosure of Portfolio constituents	Monthly	Monthly	Daily or real time
Intra-day trading	Not possible	Not possible	Possible at low cost

Table 4: ETF Key Features Compared with Open-Ended and Closed-Ended Mutual Fund

Mechanism of ETF

ETF units are not offered for sale to the general public for money, which distinguishes them from mutual funds. Instead, the asset management company that sponsors the ETF (Fund) purchases shares of the companies that make up the index from a variety of investor types, including institutions, large investors, and Authorized Participants (AP). It then grants them a sizable block of ETF units in return.

To put it another way, a 'Creation Unit' – a sizable group of ETF units – is traded for a 'Portfolio Deposit' of equities and a 'Cash Component.' The APs can also use the reverse process – creating a Redemption Unit – to convert their ETF units into 'Portfolio Deposit' of equities based on market demand. The APs can hold the ETF or sell those in the secondary market (Figure 30).

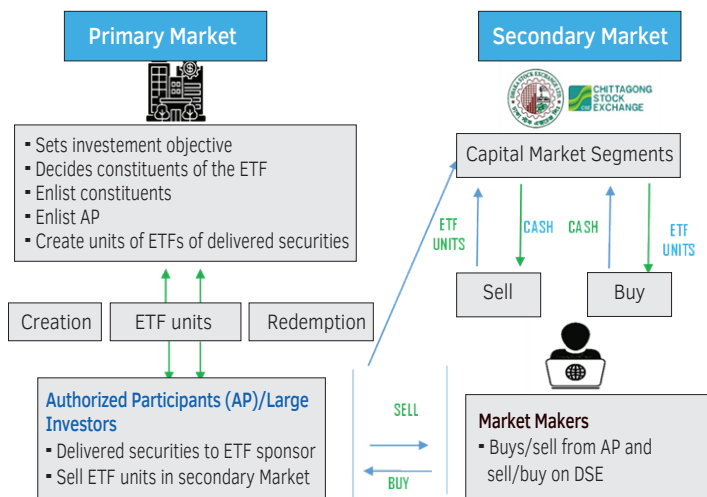


Figure 30: ETF Participants, Structures and Mechanism of Primary and Secondary Market

Added Benefits to ETF Investors

There are broadly four distinct benefits an investor can enjoy from investing in ETFs. These are:

1. Access to disparate asset classes and sub-asset-class slices based on style, size, and sector that were not available before.
2. Transparency in the ETF fund portfolio on a real-time basis provides a huge leap forward, regaining investors' confidence when they are skeptical about the existing closed-end mutual funds. In developed countries, ETF sponsors publish their NAV every 15-seconds, fostering arbitrage activity and lowering tracking errors.
3. ETF ensures liquidity and price discovery even in times of financial crisis, providing a safe venue for investors.
4. ETFs generally are able to provide in-kind redemptions by delivering a basket of securities and thus rarely need to make capital gain distributions. This feature allows most ETFs to avoid taxable events, providing tax efficiency that arises from selling securities for cash within the fund.

Findings from the US Market on Positive Impact of ETF

1. ETFs managed to avoid the 2008 global financial crisis, the 2013 Taper Tantrum, the 2015 sell-off in high-yield bonds, and the stressors brought on by the coronavirus. In June 2013, amid the so-called Taper Tantrum, bond ETFs stepped in to

stabilize the unstable bond market. Up to 25% of the underlying market's trading volume was placed in the largest high-yield bond ETFs.

2. Trading in ETFs picks up as market volatility increases. The average daily trading volume for US-listed ETFs was about \$256 billion, or about three times the volume for all of 2019.
3. Since 2011, ETF primary market activity has made up 5% of all US stock trading, while ETF secondary market activity has stayed nearly steady at 25%. (Source: CFA society Research on ETF)

BSEC (Exchange Traded Fund) Rules, 2016

According to the ETF Rules 2016, an ETF fund can be either 'passively managed ETF' or 'actively managed ETF.' It can be operated as a general index fund or an Islamic index fund. The following criteria must be met if any AMC or sponsor wants to create and maintain an ETF fund:

1. Minimum fund size at formation shall be at least TK five hundred million and subscription by the sponsor(s) shall not be less than 10% of the fund's target size;
2. Minimum investment by the asset manager shall be at least 2% of the fund's target size;
3. Investment of the sponsor and asset manager shall have a lock-in period of 02 years since the listing date of the fund with a continuous investment of 1/10th of its initial contribution;
4. The fund shall determine an annual fee for the Commission at 0.07% on year-end fund size;
5. For index-based ETFs, subscriptions must be done through private placement;
6. A registered asset manager shall be eligible to apply to be an asset manager of ETF; if it has completed a successful operation of at least 03 (three) years and has experience in fund management for at least one registered mutual fund or collective investment scheme;
7. The asset manager shall be entitled to get an annual fund management fee up to 0.75% (zero-point seven five percent) of the weekly average NAV of the fund for managing 'passively managed ETF';
8. The AMC must appoint at least 2 APs (each having minimum 5 years of experience in being a stock broker-dealer) and at least 1 market maker;
9. The ETF must invest at least 95% of the fund size in constituent securities if it is a general index fund;
10. The annual operating expenses of an ETF shall not be above 3% on the weekly average of the net asset value of the fund for the index fund.

Conclusion

ETF is the most innovative product among the various capital market instruments that provide a safety cushion in terms of uncertainties as well as a long-term stable growth opportunity. The genesis of ETF in Bangladesh is hoped to bring emancipation to our stagnant market boosting the confidence of the general and institutional investors.

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