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Research Update:

Ratings On Bangladesh Affirmed At 'BB-/B', Outlook Stable

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Overview

- Although we assess Bangladesh's external liquidity as strong, the country faces the vulnerabilities of a low-income economy, fiscal constraints, and heavy development needs.
- We are affirming our 'BB-/B' foreign and local currency sovereign credit ratings on Bangladesh.
- The stable outlook balances healthy growth prospects and an improving external profile against fiscal weaknesses and development needs.

Rating Action

On May 13, 2015, Standard & Poor's Ratings Services affirmed its 'BB-' long-term and 'B' short-term sovereign credit ratings on the People's Republic of Bangladesh. The outlook is stable. The transfer and convertibility (T&C) assessment remains 'BB-'.

Rationale

The ratings on Bangladesh reflect the country's low economic development and limited fiscal flexibility owing to a combination of constrained revenue generation capacity, significant shortage of basic infrastructure and government services. The country's volatile political setting combined with administrative and institutional weaknesses represent additional rating constraints. We weigh these factors against a relatively modest external debt burden, reflecting support from substantial donor engagement, and large remittances from the Bangladeshi diaspora.

Low economic development, as represented by per capita GDP of US$1,250 for 2015, is Bangladesh's main rating constraint. This income level offers a weak and narrow revenue base, in turn limiting the fiscal and monetary flexibility needed to respond to exogenous shocks. Nevertheless, Bangladesh's real per capita GDP growth of about 5.2% is healthy and in line with peers' at this income level. Despite numerous structural impediments to growth, in particular the shortage of electricity, the economy has a record of steady growth with minimal fluctuation.

Bangladesh's fractious domestic political conditions distract from stable policymaking. In particular, widespread strikes and blockades have caused substantial economic disruption. Combined with a weak institutional setting and infrastructure deficiencies, Bangladesh's foreign direct investment have remained persistently low. Notably, opposition party-led strikes since the 2014 elections have significantly hurt GDP growth for the fiscal year ending June 30, 2015. Although economic activity has resumed, the confrontational stance between the incumbent Awami League and opposition Bangladesh Nationalist Party harbors the potential for conflict.

On the fiscal front, Bangladesh tends to run moderate deficits. We forecast the change in general government debt to average 3.4% of GDP annually over fiscal 2015-2018. However, many basic social and infrastructure needs remain unmet, which implies the need for higher outlays over the longer term. Although the government's debt burden is low, with net general government debt at our projection of 26% of GDP as of the end of fiscal 2015, its high interest expense at 18% of revenues limits fiscal flexibility. The government's increasing use of a costlier national savings certificates scheme rather than commercial bond issuances suggests that its debt-servicing ratio will not necessarily fall even if there is fiscal consolidation. In addition, almost half the total government debt is denominated in foreign currency. However, the availability of official concessional funding tempers these negative effects.

Bangladesh's narrow revenue base limits the government's flexibility to mitigate the effect of economic downturns or other shocks. It has only 2 million registered taxpayers (out of a population of 155 million). General government revenue was a low 10.9% of GDP in fiscal 2014. Nevertheless, numerous initiatives are underway to expand the tax base, most notably the plan to reform the complicated Goods and Services Tax (GST) system. The government has set a target to standardize the GST rate at 15% by fiscal 2016. However, the plan has been repeatedly delayed over the past years.

We view Bangladesh's monetary assessment as below average. The central bank's limited independence, multiple mandates, and underdeveloped capital markets hamper monetary flexibility. In addition, nonperforming loans remain high and capitalization low in the banking sector, particularly at the state-owned banks. However, the central bank has made progress in managing inflationary expectations. In the past two years, inflationary pressure subsided with reduced government borrowing from the banking sector. Inflation has stayed in the single digits since 2011.

Bangladesh's low external borrowings support the ratings. Remittance inflows averaging 9.1% of GDP over the past three years and an internationally competitive garment export sector generally ensure current account surpluses. Foreign exchange reserves (as of end March) stood at US$23.1 billion, equivalent to an estimated six months of imports. We expect Bangladesh's gross external financing needs to average 77.6% of current account receipts plus usable reserves over 2015-2018.

The country's significant reserve accumulation improved the narrow net external debt position, and we project it to average 5.6% of current account receipts over 2015-2018. We expect reserve accumulation to moderate due to lower remittance flows and stronger imports. Nonetheless, we believe external balance and liquidity will remain credit-supporting factors.

Bangladesh's external profile draws substantial donor support, ensuring that the bulk of public external debt is low-cost borrowing with long maturity. Additionally, donors and multilateral lenders condition policy formulation and provide direct budgetary support.

Outlook

The stable outlook reflects our expectation that Bangladesh's steady growth path and strong donor support will endure to raise average income and sustain the country's external profile over the next 12 months. These factors are balanced against lingering governance and fiscal weaknesses, infrastructure deficiencies, and inflation risks.

We may raise the ratings if measures aimed at expanding the revenue base and boosting collection efficiency materially improve fiscal performance. We may also upgrade Bangladesh if the government materially reduces energy, infrastructure, and administrative bottlenecks and boosts investment, leading to a durable increase in trend growth for real per capita GDP. Likewise, we may also raise the ratings if its monetary flexibility strengthens, evident in well-controlled inflation over a sustained period and deeper capital markets with market-based tools.

Conversely, we may downgrade the sovereign if fiscal slippages result in rising public debt and external donor support declines materially. We may also lower the ratings if Bangladesh undoes what it has achieved under the International Monetary Fund's Extended Credit Facility program.

Key Statistics

Table 1

People's Republic of Bangladesh - Selected Indicators

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Nominal GDP (bil. US$)	92	102	115	124	129	154	174	198	225	255	289
GDP per capita (US$)	619	683	758	808	833	999	1,117	1,254	1,409	1,573	1,762
Real GDP growth (%)	6.0	5.0	5.6	6.5	6.5	6.0	6.1	6.4	6.5	6.5	6.7
Real GDP per capita growth (%)	4.9	4.0	4.4	5.3	5.3	6.7	4.7	5.0	5.1	5.1	5.3
Change in general government debt/GDP (%)	2.1	2.8	0.9	6.5	1.6	1.5	4.5	2.3	3.8	3.8	3.7
General government balance/GDP (%)	(4.5)	(2.8)	(3.4)	(3.3)	(4.0)	(3.7)	(3.1)	(3.4)	(3.5)	(3.5)	(3.4)
General government debt/GDP (%)	37.2	35.9	32.7	34.9	31.9	29.6	30.8	29.4	29.8	30.1	30.3
Net general government debt/GDP (%)	34.0	31.4	29.1	31.5	28.1	24.9	25.4	25.9	26.6	27.2	27.6

Table 1

People's Republic of Bangladesh - Selected Indicators (cont.)											
General government interest expenditure/revenues (%)	18.3	18.0	17.6	14.7	16.6	16.1	18.1	18.1	17.3	16.9	16.6
Other dc claims on resident nongovernment sector/GDP (%)	36.0	38.1	43.2	44.6	45.1	42.9	43.5	43.7	44.8	46.4	47.8
CPI growth (%)	8.9	5.4	8.1	10.7	6.2	7.5	7.0	6.7	6.2	6.0	6.0
Gross external financing needs/CARs plus usable reserves (%)	88.4	84.4	72.5	87.0	88.8	79.4	76.4	74.1	76.7	78.8	80.7
Current account balance/GDP (%)	0.8	2.4	3.1	(1.4)	(0.3)	1.6	0.9	0.6	0.1	(0.1)	(0.3)
Current account balance/CARs (%)	2.8	8.7	11.7	(4.5)	(1.1)	5.4	3.2	2.2	0.5	(0.3)	(1.0)
Narrow net external debt/CARs (%)	69.7	48.7	40.3	42.7	30.7	18.2	10.3	8.5	6.3	4.4	3.4
Net external liabilities/CARs (%)	86.2	64.5	57.9	57.6	44.5	35.3	27.6	26.8	25.1	23.5	22.8

Other depository corporations (dc) are financial corporations (other than the central bank) whose liabilities are included in the national definition of broad money. Gross external financing needs are defined as current account payments plus short-term external debt at the end of the prior year plus nonresident deposits at the end of the prior year plus long-term external debt maturing within the year. Narrow net external debt is defined as the stock of foreign and local currency public- and private-sector borrowings from nonresidents minus official reserves minus public-sector liquid assets held by nonresidents minus financial-sector loans to, deposits with, or investments in nonresident entities. A negative number indicates net external lending. CARs--Current account receipts. The data and ratios above result from Standard & Poor's own calculations, drawing on national as well as international sources, reflecting Standard & Poor's independent view on the timeliness, coverage, accuracy, credibility, and usability of available information.

Ratings Score Snapshot

Table 2

People's Republic of Bangladesh - Ratings Score Snapshot	
Key rating factors	
Institutional assessment	Weakness
Economic assessment	Weakness
External assessment	Strength
Fiscal assessment: flexibility and performance	Neutral
Fiscal assessment: debt burden	Weakness
Monetary assessment	Neutral

Standard & Poor's analysis of sovereign creditworthiness rests on its assessment and scoring of five key rating factors: (i) institutional assessment; (ii) economic assessment; (iii) external assessment; (iv) the average of fiscal flexibility and performance, and debt burden; and (v) monetary assessment. Each of the factors is assessed on a continuum spanning from 1 (strongest) to 6 (weakest). Section V.B of Standard & Poor's "Sovereign Rating Methodology," published on Dec. 23, 2014, summarizes how the various factors are combined to derive the sovereign foreign currency rating, while section V.C details how the scores are derived. The ratings score snapshot summarizes whether we consider that the individual rating factors listed in our methodology constitute a strength or a weakness to the sovereign credit profile, or whether we consider them to be neutral. The concepts of "strength", "neutral", or "weakness" are absolute, rather than in relation to sovereigns in a given rating category. Therefore, highly rated sovereigns will typically display more strengths, and lower rated sovereigns more weaknesses. In accordance with Standard & Poor's sovereign ratings methodology, a change in assessment of the aforementioned factors does not in all cases lead to a change in the rating, nor is a change in the rating necessarily predicated on changes in one or more of the assessments.

Related Criteria And Research

Related Criteria

- Sovereign Rating Methodology, Dec. 23, 2014
- Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers, May 7, 2013

- Methodology: Criteria For Determining Transfer And Convertibility Assessments, May 18, 2009

Related Research

- Sovereign Ratings And Country T&C Assessments, April 17, 2015
- Global Sovereign Rating Trends First Quarter 2015 Update, April 14, 2015
- Sovereign Risk Indicators at http://spratings.com/sri
- Asia-Pacific Sovereigns' Debt Stock Is Likely To Rise To US$16.5 Trillion In 2015, March 5, 2015
- Global Sovereign Debt Report 2015: Borrowing To Drop By 5.7% To US$6.7 Trillion, March 5, 2015
- Asia-Pacific Sovereign Debt Report 2015: Total Borrowing Is Likely To Remain Close To US$2.6 Trillion In 2015, March 5, 2015

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee agreed that the debt assessment has worsened. All other key rating factors were unchanged.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

Ratings Affirmed

Bangladesh (People's Republic of)	
Sovereign Credit Rating	BB-/Stable/B
Transfer & Convertibility Assessment	
Local Currency	BB-

Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at www.spcapitaliq.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.