Bangladesh Economy in FY2011-12

Third Interim Review of Macroeconomic Performance

A report prepared under CPD's programme on
Independent Review of Bangladesh's Development (IRBD)

Centre for Policy Dialogue (CPD)

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About CPD

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As part of the CPD IRBD tradition, CPD organised an Expert Group Consultation on 27 May 2012 at the CPD Dialogue Room. The working document of the *Analytical Review of Bangladesh's Macroeconomic Performance in Fiscal Year 2011-12 (Third Reading)* prepared by the CPD IRBD 2011-12 Team was shared at this in-house meeting with a distinguished group of policymakers, academics and professionals. The CPD Team is grateful to all of those present at the consultation for sharing their views, insights and comments on the draft report.

A list of the participants of the meeting is provided below *(in alphabetical order)*:

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Acronyms

ABB	Association of Bankers, Bangladesh
ACC	Anti-Corruption Commission
ADB	Asian Development Bank
ADP	Annual Development Programme
API	Active Pharmaceutical Ingredient
ASYCUDA	Automation System of Customs Data
BAPEX	Bangladesh Petroleum Exploration & Production Company Ltd.
BARI	Bangladesh Agriculture Research Institute
BBBF	Bangladesh Better Business Forum
BBS	Bangladesh Bureau of Statistics
BDT	Bangladeshi Taka
BEPZA	Bangladesh Export Processing Zone Authority
BIFF	Bangladesh Infrastructure Facilitation Fund
BLRI	Bangladesh Livestock Research Institute
BO	Beneficiary Owner
BPC	Bangladesh Petroleum Corporation
BPDB	Bangladesh Power Development Board
BTRC	Bangladesh Telecommunication Regulatory Commission
CAAB	Civil Aviation Authority of Bangladesh
CNY	Chinese Yuan
CPD	Centre for Policy Dialogue
CPI	Consumer Price Index
CTG	Caretaker Government
DAE	Department of Agricultural Extension
DAM	Department of Agricultural Marketing
DFID	Department for International Development
DLS	Department of Livestock Services
DSE	Dhaka Stock Exchange
ECF	Extended Credit Facility
EEF	Equity Entrepreneurship Fund
EGPP	Employment Generation Programme for the Poorest
EPB	Export Promotion Bureau
EPZ	Export Processing Zone
EU	European Union
FDI	Foreign Direct Investment
FFW	Food for Work
FRA	Financial Reporting Act
GBP	British Pound
GDP	Gross Domestic Product
GNI	Gross National Income
GSP	Generalized System of Preferences

GoB	Government of Bangladesh
G2G	Government-to-Government
HIES	Household Income and Expenditure Survey
HS	Harmonised System (of Coding)
HYV	High-yielding Variety
IDA	International Development Association
ICOR	Incremental Capital-Output Ratio
ICT	Information and Communication Technology
IMED	Implementation Monitoring and Evaluation Division
IMF	International Monetary Fund
INR	Indian Rupee
IPO	Initial Public Offering
IRBD	Independent Review of Bangladesh's Development
IT	Information Technology
LFS	Labour Force Survey
LPG	Liquefied Petroleum Gas
L/C	Letter of Credit
MOVE	Modernization of VAT Environment
MPS	Monetary Policy Statement
MT	Metric Ton
MTBF	Medium Term Budgetary Framework
MW	Mega Watt
MoF	Ministry of Finance
mmcm	Million Cubic Metre
M&E	Monitoring and Evaluation
M2	Broad Money
NBR	National Board of Revenue
NRB	Non-resident Bangladeshi
NSD	National Savings Bond
OECD	Organisation for Economic Co-operation and Development
OMS	Open Market Sales
PGCB	Power Grid Company of Bangladesh
POL	Petroleum and Other Liquids
PPP	Public-Private Partnership
PRGF	Poverty Reduction Growth Facilities
QIP	Quantum Index of Production
RADP	Revised Annual Development Programme
RMG	Readymade Garments
RPP	Rental Power Plant
RRC	Regulatory Reforms Commission
RoO	Rules of Origin
R&D	Research and Development
SAARC	South Asian Association of Regional Cooperation
SEC	Securities and Exchange Commission
SEZ	Special Economic Zone
SFYP	Sixth Five Year Plan
SME	Small and Medium Enterprise
SRO	Statutory Regulatory Ordinance
SSNP	Social Safety Net Programme
SoE	State-owned Enterprise
TIN	Tax Identification Number
TSS	Telephone Shilpa Sangstha
TUF	Technology Upgradation Fund
UNDP	United Nations Development Programme
USA	United States of America
USD	United States Dollar
USITC	United States International Trade Commission
VAR	Vector Autoregressive (Model)
VAT	Value Added Tax
WAN	Wide Area Network
WDI	World Development Indicator

Analytical Review of Bangladesh's Macroeconomic Performance in FY2011-12

*(Third Reading)**

*This report was released to the media by the Centre for Policy Dialogue (CPD) on 4 June 2012.

1. INTRODUCTION

The outgoing fiscal year FY2011-12 turned out to be quite daunting for Bangladesh in the backdrop of a number of national, regional and global economic developments. Some of the challenging issues that dominated the economic horizon were longstanding structural in nature, whereas others stemmed from more immediate circumstances. Throughout FY2011-12, issues relating to quality of macroeconomic management, particularly questions relating to government borrowing, foreign aid utilisation, implementation of the Annual Development Programme (ADP), and revenue generation figured prominently in the economic discourse. Extreme volatility in the capital market sent out shock waves across the economy and society. High level of consumer prices remained an enduring challenge. Crop production, safety net programmes and food security were on the policy radar screen. The sorry state of infrastructure – transport and communication, as well as gas and electricity supplies – dogged the policymakers, entrepreneurs and citizens alike. Reluctance of the World Bank to disburse funds for construction of the Padma Bridge had implications far beyond the economy. Along with these, the Indo-Bangla transit controversy and fallouts of the Eurozone crisis added new complexity to the existing policy challenges. Indeed, new dimensions were added to economic management as the government contracted a loan under an IMF (International Monetary Fund) programme towards the end of the year.

The Centre for Policy Dialogue (CPD), as part of its traditional exercise involving a review of the performance of the economy during a particular fiscal year and anticipating key emerging developments, had kept a close watch on the economy since the beginning of FY2011-12. CPD, in its first reading of the state of Bangladesh economy carried out under its *Independent Review of Bangladesh's Development* (IRBD) programme, released on 3 November 2011, highlighted the following four critical concerns for FY2011-12:

a. Implications of the new wave of global economic crisis
b. Deepening stresses in public finance management
c. Unabated price inflation
d. Increasing pressure on the balance of payments

The evolving state of the economy during FY2011-12 was captured by the second reading of economic development under the IRBD, which was published on 11 March 2012. This review, analysing the looming uncertainties in the short-term economic outlook, emphasised the following five areas of heightened concern:

a. Adverse spillovers from the uncertainties in the global markets
b. Public finance emerging as the weakest link of macroeconomic management
c. Monetary policy slowly going off the track
d. Trust deficit underpinning the capital market stabilisation
e. Balance of payments increasingly coming under seize

Thus, the present review, which is the third and last reading of the state of the economy in the current fiscal year, while puts focus on its defined scope, but also needs to be looked at as a product in a continuum. Thus, given the analyses presented in the two earlier editions, the present volume addresses, albeit in a rather compressed manner, in its section on macroeconomic performance, a number of important issues along with necessary updates. However, the main value of the present volume lies in three other core sections which discuss three themes of key importance for the Bangladesh economy at this present juncture: namely *investment, employment* and *reforms*. Identification of these three distinctive themes is dictated by the desire to take an in-depth look at the basic structural challenges confronting the Bangladesh economy – promoting investment, generating employment, and accelerating institutional and policy reforms. Admittedly, a stagnating, if not faltering, investment, is holding back the economy from achieving higher levels of economic growth. Arguably, basic objective of all public policy is generating additional gainful employment opportunities, but there is hardly any evidence-based real time picture of this that is available for scrutiny. The review of the reform initiatives of the present government – declared and/or implemented – has been undertaken to deepen our understanding about the institutional impediments to accelerating economic growth. The present review also contains a note on the state of crops production and its implications for food security. Indeed, as the incumbent government finishes the third year of its tenure, the current exercise intends to highlight the goal posts of the bigger picture of the economic canvas.

The present review, as in earlier occasions, has primarily depended on official statistics for its analyses. The conclusions derived were validated subsequently through field visits, debriefing of knowledgeable informants, and opinions of relevant experts.

2. THE MACROECONOMIC SCENARIO

2.1 Economic Growth Slows Down

Bangladesh successfully improved her economic growth performance over the last three decades. Average gross domestic product (GDP) growth rate increased sequentially by one percentage point in each decade (Figure 1). The present government aimed to increase GDP growth rate further to 8.0 per cent by FY2014-15, and 10.0 per cent by FY2020-21 (GED 2011). In course of the last two fiscal years (FY2009-10 and FY2010-11) Bangladesh economy was able to enhance its growth performance from 5.7 per cent in FY2008-09 to 6.1 per cent in FY2009-10, and the revised estimate for FY2010-11 indicates that Bangladesh managed to achieve her target growth rate of 6.7 per cent in that fiscal year.[1] Thus, such successive improvement in the overall economic performance of Bangladesh, notwithstanding all the impediments afflicting the economy, remained quite impressive.

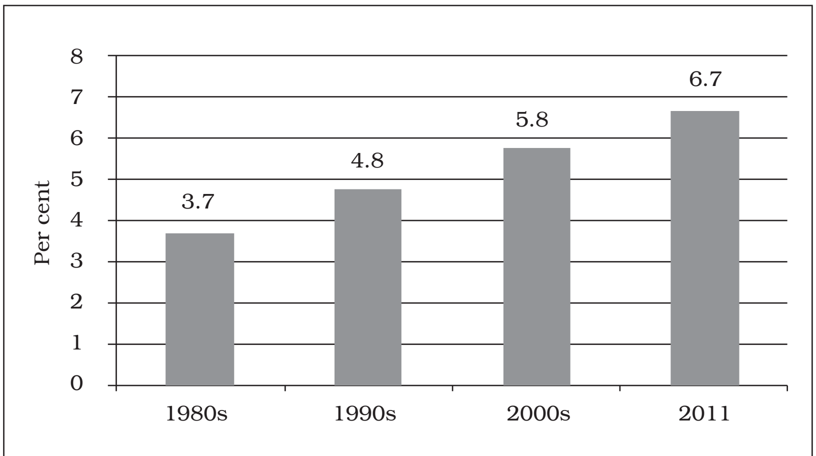


Figure 1

Average GDP Growth in Last Three Decades

Source: Calculated from the Bangladesh Bureau of Statistics (BBS) data.

Bangladesh Bureau of Statistics (BBS), however, has recently indicated that the economy will not be able to meet its GDP growth target of 7.0 per cent in FY2011-12. The provisional figure for GDP growth for the current fiscal year was limited to 6.3 per cent, i.e. 0.7 percentage points lower than its target.[2] This is

[1]In fact, recently released revised GDP growth shows marginal improvement (by 0.04 percentage points) over its provisional estimate. It may be recalled that CPD in its earlier annual review of Bangladesh economy raised questions about the robustness of GDP estimates in the country (CPD 2011b).
[2]The Asian Development Bank (ADB) projected a 6.2 per cent growth for Bangladesh in FY2011-12. The projection of IMF was even lower at 5.5 per cent (IMF 2012).

surely a setback for the present government's plan to move the economy towards a higher growth trajectory. To reach an eight-plus growth trajectory Bangladesh will need to address a number of unfinished agendas (Box 1).

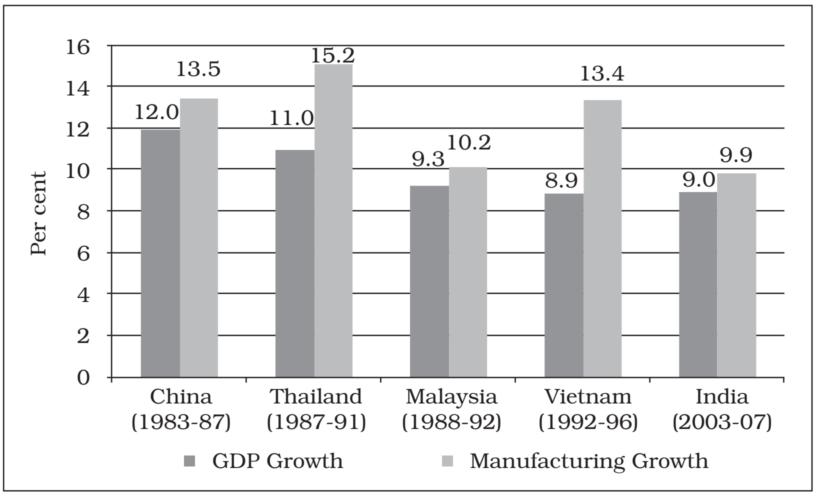
Box 1

Pre-Requisites of a Higher Growth Trajectory

Cross-country experiences suggest that economic growth of over 7-8 per cent in most developing countries was driven by industry sector, particularly the manufacturing component. Box Figure 1 shows that the five countries achieved an eight-plus per cent growth at different point of time but for all of them growth of manufacturing sector was faster than the overall GDP growth.

Box Figure 1

Structure of 8+ Per cent GDP Growth for Various Countries



Source: Calculated from the World Development Indicators (WDI) online data.

Economic growth was propelled in the East Asian economies by strong export-oriented manufacturing supported by strategic government policies and economic reforms. Policies geared towards promoting the competitiveness of exporters and removal of relevant biases could be done through uninterrupted access to imported inputs at global price, tax breaks, duty drawback programme, subsidised credit, privatisation of customs administration, bonded manufacturing warehouses, and provision of export processing zones (EPZs) (Radelet *et al.* 1997). On the other hand, after decades of tight protectionism accorded to local industries, India's industry level productivity grew 22 per cent in the 1994-1995 period (as compared to the pre-reform 1987-1990 period) following large-scale inflow of foreign direct investment (FDI). Trade liberalisation contributed 59 per cent increase to the aggregate productivity growth (Bollard *et al.* 2011).

While identifying the drivers for economic growth, Barro (1996) in his classic work on economic growth, used panel data on around hundred countries from 1960 to 1990 and found that economic growth rate is enhanced by higher initial schooling and life expectancy, lower fertility, lower government consumption expenditure, lower inflation, improvements in the terms of trade, and better maintenance of the rule of law.

Mahajan (2005) identified the following as factors holding back GDP growth in Bangladesh: failure to benefit from global integration, a lack of financial intermediation, and poor quality of governance, such as weak law and order or a cumbersome bureaucracy. Rahman and Yousuf (2010) also pointed out a number of constraints for Bangladesh's economic growth including low levels of human capital, poor infrastructure, market failures in specific sectors, low levels of trade, corruption and cumbersome regulations.

As it transpires from above, propelling Bangladesh to a higher growth trajectory would definitely require much more in the areas of inter alia, economic reforms along with better investment in physical infrastructure and human capital formation.

Per Capita Income

In FY2011-12, per capita GDP of Bangladesh has been estimated to be about USD 772, which is USD 24 more than that of the preceding year (Table 1). In Taka terms (1995-96 constant prices), the provisional GDP would indicate a per capita GDP growth of about 5 per cent in FY2011-12 over last year's benchmark.[3] On the other hand, per capita gross national income (GNI) also increased to USD 848 in FY2011-12 from USD 816 in FY2010-11, i.e. increase of USD 32.[4] One can see a slowdown in growth rate of per capita income (in USD terms). Moderate growth rates accompanied by stable exchange rate facilitated accelerated increase in per capita income (in terms of both GDP and GNI) between FY2008-09 and FY2010-11. Indeed, a faster depreciation of Taka against USD (by 9.9 per cent) restricted growth of per capita income in USD terms in FY2011-12.

Table 1

National Income and Per Capita Income

Indicators	Nominal				Growth (%)			
	FY09	FY10	FY11	FY12	FY09	FY10	FY11	FY12
Real GDP (million Tk.)	3401968	3608446	3850504	4093775	5.7	6.1	6.7	6.3
Nominal GDP (million Tk.)	6147952	6943243	7967040	9147842	12.6	12.9	14.7	14.8
Nominal GNI (million Tk.)	6706964	7589278	8692175	10047227	12.9	13.2	14.5	15.6
Per capita Real GDP (Tk.)	23587.9	24704.6	25730.1	27007.4	4.4	4.7	4.2	5.0
Per capita Nominal GDP (Tk.)	42628	47536	53238	60350	11.2	11.5	12.0	13.4
Per capita GNI (Tk.)	46504	51959	58083	66283	11.4	11.7	11.8	14.1
Exchange rate (BDT per USD)	68.80	69.18	71.17	78.18	0.3	0.6	2.9	9.9
Per capita GDP (USD)	620	687	748	772	10.9	10.9	8.9	3.2
Per capita GNI (USD)	676	751	816	848	11.1	11.1	8.7	3.9

Source: Calculated from the Bangladesh Bureau of Statistics (BBS) data.

2.1.1 Sources of Growth: Agriculture Holds Back

According to BBS statistics, a repeat of strong performance by the industry sector (9.5 per cent), particularly its manufacturing component (9.8 per cent) is expected to be the driver of the estimated GDP growth rate for FY2011-12 (Table 2). Construction sector surpassed its growth target for the current fiscal year (6.6 per cent) to attain a robust 8.5 per cent growth. On the other hand, agriculture sector, particularly crops production failed to maintain its remarkable track record of the last two fiscal years.[5] Services sector maintained its traditional 6 per cent plus growth rate, although it had been lower than the target.

To ascertain the sources of decline in GDP growth rate we have done a comparative decomposition of the GDP growth rates of FY2010-11 and FY2011-12. Such a scrutiny revealed that out of 6.3 per cent of overall growth (FY2011-12), only 0.5 per cent will be contributed by agriculture sector – which was 1 per cent in FY2010-11. The fall of agriculture sector's contribution is more than overall fall in GDP growth (0.4 per cent) (Table 3). Hence, it is easy to conclude that the decline in GDP growth has been predicted by the relatively depressed performance in agriculture sector growth, particularly its crop component. In contrast, industry sector, backed up by manufacturing and construction sectors, improved their growth

[3]It is important to note that population figure of FY2010-11 represents the new population figure from the census. However, it appears that BBS did not adjust the population figures for preceding years. Hence, a jump in population (by 3.6 million, which was 1.8 million between FY2008-09 and FY2009-10) is found. This has also influenced per capita income figures reported here.

[4]However, it should be noted here that these average income figures conceal the fact of highly skewed income distribution in Bangladesh. According to the latest Household Income and Expenditure Survey (HIES) 2010, gini coefficient for Bangladesh was 0.46 (BBS 2012).

[5]GDP of crops sector attained 6.1 per cent and 5.6 per cent growth in FY2009-10 and FY2010-11 respectively.

contribution. Indeed out of 6.3 per cent growth in FY2011-12, 2.8 per cent is expected from industry sector, the highest in the history. The services sector's growth contribution is expected to be limited to its regular level of 2.9 per cent. The contribution of import duty has remained in FY2011-12 at a modest level of only 0.1 per cent.

Table 2

Sector-wise GDP Growth

(in Per cent)

Sector	FY11	FY12 (Target)	FY12 (Provisional)
Agriculture	5.1	4.5	2.5
Crops	5.6	5.2	0.9
Industry	8.2	9.6	9.5
Manufacturing	9.4	9.8	9.8
Construction	6.5	6.6	8.5
Services	6.2	6.8	6.1
GDP	**6.7**	**7.0**	**6.3**

Source: Calculated from the Bangladesh Bureau of Statistics (BBS) data and GED (2011).

Table 3

Contribution to Growth

(in Per cent)

Sector	FY06	FY07	FY08	FY09	FY10	FY11	FY12[P]	Difference (FY11 and FY12)
Agriculture	1.1	1.0	0.7	0.8	1.0	1.0	0.5	-0.5
Crops	0.6	0.5	0.3	0.5	0.7	0.6	0.1	-0.5
Industry	2.6	2.3	1.9	1.8	1.9	2.4	2.8	0.4
Manufacturing	1.7	1.6	1.2	1.1	1.1	1.6	1.7	0.1
Construction	0.7	0.6	0.5	0.5	0.5	0.6	0.7	0.2
Services	3.0	3.3	3.1	3.0	3.1	3.0	2.9	-0.1
Import Duty	-0.1	-0.1	0.5	0.1	0.1	0.3	0.1	-0.2
GDP	**6.6**	**6.4**	**6.2**	**5.7**	**6.1**	**6.7**	**6.3**	**-0.4**

Source: Estimated from the Bangladesh Bureau of Statistics (BBS) data.
Note: P denotes Provisional.

The provisional estimate of GDP for FY2011-12 is expected to be revised at a later date based on data for full fiscal year. The proxy indicators available thus far indicate that a number of adjustments would be required. While there are reasons for the growth rates of manufacturing and construction sectors to be revised downward, crops sector's growth rate may be required to revise upward (see later in Section 2.1.3 for details).

2.1.2 Investment and Savings: Stagnation Continues

From the expenditure side, as in the past, the GDP of FY2011-12 is largely underwritten by private consumption expenditures (about 80 per cent)[6] (Table 4). The provisional figure on GDP from FY2011-12 projects a stagnating aggregate investment with a distinctive fall in private investment share. Curiously, the provisional figures also suggest an optimistic projection from the share of public investment. Analysis of various proxy indicators suggests that the public investment-GDP ratio may have to be revised downward from 6.3 per cent to 5.7 per cent. If our estimate is correct it will mean that not only the private investment, but also aggregate investment is expected to a decline as a share of GDP in FY2011-12. Our

[6]While reading these numbers one should keep in mind that there is a difference between GDP estimate based on expenditure method (known as GDE) and GDP estimate based on sectoral contribution. As a matter of fact, this statistical discrepancy increased substantially in FY2011-12.

estimate further shows that the momentum generated for augmenting the public expenditures in the first two years of this government is showing signs of running out of steam in FY2011-12.[7] The deficit in external resource balance (export minus import) in FY2011-12 has also seen remarkable expansion.

Table 4
Share of GDP Components by Expenditure Method

(in Per cent)

Component	Share		Incremental
	FY11	FY12	Share
Domestic demand	105.9	106.1	107.6
Consumption	80.7	80.6	80.1
Private	74.9	75.0	75.3
General Government	5.8	5.7	4.8
Investment	25.2	25.4	27.4
Private	19.5	19.1	16.7
Public	5.6	6.3	10.8
Resource balance	-8.7	-10.3	-21.2
Exports	22.9	25.0	39.1
Imports	31.6	35.3	60.4
Gross Domestic Expenditure at market price	97.2	95.8	86.3
Gross Domestic Product at market price	100.0	100.0	100.0
Statistical discrepancy	2.8	4.2	13.7

Source: Calculated from the Bangladesh Bureau of Statistics (BBS) data.

The Sixth Five Year Plan (SFYP) correctly mentioned that acceleration of investment is one of the primary pre-requisites for attaining targeted economic growth rates for the period FY2010-11 to FY2014-15. In FY2010-11, the aggregate investment-GDP ratio increased to 25.1 per cent from the earlier benchmark (FY2009-10) – 24.4 per cent. However, the high expectation about investment growth was belied in FY2011-12 (Table 5). As mentioned earlier the initial estimate of aggregate investment rate stood at 25.4 per cent of GDP in FY2011-12 which very well may be revised downward. The investment target for FY2012-13 has been set at 29.6 per cent of GDP. This would require a rise in investment as a share of GDP by more than 4.2 percentage points. Private investment, in this case, will have to rise to 22.7 per cent of GDP from 19.1 per cent. The current macroeconomic management can hardly assure this prospect.

Table 5
Investment-GDP Ratio and Incremental Capital-Output Ratio (ICOR)

Indicator	FY10	FY11		FY12		FY13
	Actual	Target	Actual	Target	Provisional	Target
GDP Growth (%)	6.1	6.7	6.7	7.0	6.3	7.2
Investment as a share of GDP (%)	24.4	24.7	25.1	26.8	25.4	29.6
Public Investment as a share of GDP (%)	5.0	5.3	5.6	6.6	6.3	6.9
Private Investment as a share of GDP (%)	19.4	19.5	19.5	22.2	19.1	22.7
ICOR	4.0	3.7	3.7	3.8	4.0	4.1

Source: Estimated from the Bangladesh Bureau of Statistics (BBS) data and GED (2011).

In addition to the present lacklustre situation in aggregate investment along with its two components, the concern over declining efficiency of capital, in terms of incremental capital-output ratio (ICOR), deepened further in FY2011-12. Estimates suggest that ICOR increased from 3.7 in FY2010-11 to 4 in FY2011-12. According to the SFYP target, ICOR is expected to be at this level (4.1) in FY2012-13. It implies that in

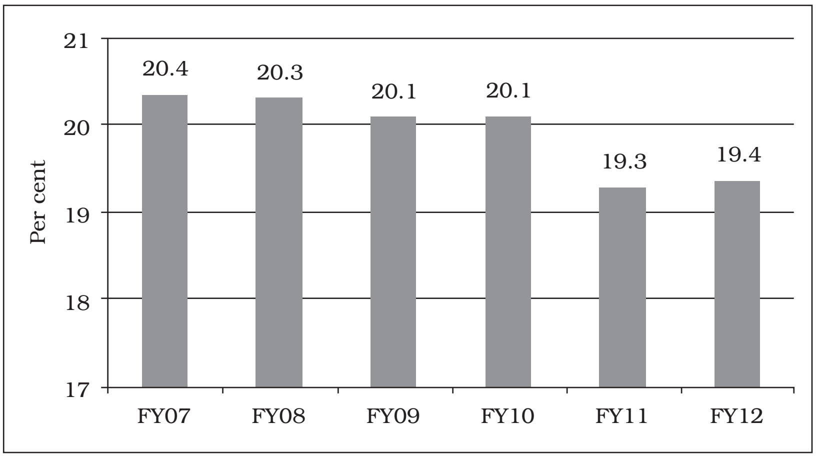
[7]See Section 3 for details.

absence of fast accumulation of investment from private sector and improved implementation of government investment plan (ADP), achieving the GDP growth in FY2012-13 will remain a far cry.

Domestic Savings

In FY2010-11 domestic savings as a share of GDP experienced a sharp decline – from 20.1 per cent to 19.3 per cent, i.e. by 0.8 percentage points. Stagnating share of domestic savings in the GDP continued to persist in FY2011-12, which stood at 19.4 per cent in FY2011-12[8] (Figure 2). Indeed, it could not recover the lost grounds of FY2006-07 when it was 20.4 per cent. It is not immediately evident to what extent this decline in domestic savings has been brought about by the changes in government savings, private-corporate savings and household savings. One wonders what the state of government sector savings is, as almost its assets (including the state-owned enterprises (SoEs)) are incurring loss. Rising prices of commodities, was perhaps a contributing factor affecting the household savings. The banking sector is also complaining about inadequate flow of deposits for them to cater the credit demand. Encouraging domestic savings needs special attention from policymakers, which would in turn help to finance the required investment for GDP growth.

Figure 2
Share of Domestic Savings as Per cent of GDP



Source: Calculated from the Bangladesh Bureau of Statistics (BBS) data.

Lower level of investment has always been a major impediment in way of achieving higher level of growth in Bangladesh. Compared to India and Vietnam, investment scenario in Bangladesh looks rather bleak; these countries invest around 40 per cent of their respective national incomes. Furthermore, the increase in ICOR means that more investment is required to attain a higher growth rate. A continuation of the current trend would imply lower than planned GDP growth rates. Indeed, the need for ensuring higher rate of investment to attain higher GDP growth rate and the necessity of taking adequate measures to raise capital productivity cannot be overemphasised. This also underscores the need for better implementation of public infrastructure development projects which could 'crowd in' downstream private sector investment. In addition to scarcity of infrastructure, high rate of interest on industrial loan is discouraging private investment.

In this connection, one can recall that the Association of Bankers, Bangladesh (ABB) curiously announced 'self-imposed' caps on interest rates for both deposits and advances at maximum of 12.5 per cent and 15.5 per cent respectively. One wonders what the central bank's stance is in this regard. However, business community has repeatedly complained that the interest rate on lending is not within this 'self-imposed cap'. According to their claims it varies between 17-19 per cent instead of 15.5 per cent.

[8]Domestic saving-GDP ratio in Bangladesh is lower compared to other developing countries including India (31.5 per cent), China (51.7 per cent), Malaysia (39.2 per cent) and Vietnam (28.6 per cent).

Increased interest rate on lending is also contributing to rising cost of production which will have an adverse impact on both economic growth and inflation. On the other hand, when higher than the announced interest rates on deposits were alleged to be offered by different commercials banks, the central bank reacted instantly by issuing notices. It is critical to ensure a balance between interest rates which can help augmentation of both domestic savings and investment for ensuring GDP growth. From policy perspectives, maintaining a reasonable spread between lending and deposit rates is an issue of critical importance in this context.

2.1.3 Revision of GDP (FY2011-12) Estimates: What to Expect

The provisional estimates for GDP are expected to be revised at a later date when data for the entire fiscal year will be available to the BBS.[9] One may reasonably expect a number of adjustments of the provisional growth figure when final estimates will be prepared. According to our analysis three areas of such critical importance are – public investment, and growth rates of manufacturing and crops sector.

As mentioned above, public investment figure will be revised downward as at least 10 per cent of Revised ADP (RADP) may remain unrealised at the end of the fiscal year (see Section 2.2 and Section 3 for details). Particularly, implementation of physical infrastructure-related projects is not up to the mark (see Section 3 for details). Hence, the construction sector's growth in the final estimate is expected to be lower.

Moreover, the estimated manufacturing growth may also require some downward adjustment. It is understood that figures of Quantum Index of Production (QIP) is treated as the proxy indicator of manufacturing sector's value addition. Currently QIP data is available for the first eight months of the fiscal year (July-February) which shows an 11.8 per cent growth of large and medium manufacturing production. On the other hand, production growth of small manufacturing during the first half of FY2011-12 had been 10.6 per cent. As exports during the last two months (March-April) declined by (-) 7.2 per cent, the production figures are also expected to decline. Moreover, the export earnings is declining particularly for knit garments products, which provides a higher value addition compared to woven garments products (see Section 2.4 for details). It implies, a higher loss in terms of GDP is expected. In the backdrop of falling export, domestic demand for Bangladeshi produced manufacturing products needs a boost to contain the growth of manufacturing sector at its provisional estimation level. It took a 17.7 per cent production growth to achieve a growth of 10.9 per cent in value addition (GDP) for large and medium manufacturing sector in FY2010-11. To attain a similar growth, one can assume a similar production growth will be required.

In contrast, the growth in agriculture sector may be revised upward in view of higher than expected production of Boro.

Since a number of sub-sectors within the services sector are linked with the real sectors and international trade activities, their growth may also see a decline during the second half the fiscal year.

Combining all these recent developments, a downward adjustment of GDP may be reasonably expected in the course of time.

2.2 Public Finance: Weakest Link

Fiscal management came under serious pressure in FY2011-12. Revenue expenditure went flying, subsidy demand increased significantly, foreign financing was not coming, and non-bank sources of financing

[9] As is known, for most of the indicators of national income accounts, provisional estimates are usually calculated on the basis of economic performance during the first half of the ongoing fiscal year.

remained limited. Combination of these factors led to heavy borrowing by the government from the banking system. Only cushion of comfort was provided by the National Board of Revenue (NBR), which surpassed its growth target during the first three quarters of the year, while the growth rate of non-NBR tax receipts slowed down.

However, a closer look at the actual fiscal developments in FY2010-11 and the expenditure targets set for FY2011-12 (Table 6) reveals that the fault line, to a large extent, emanated from the not so sound expenditure targets for FY2011-12 resulting largely from uncoordinated fiscal planning in relation to other sectors (particularly fuel and power). As for revenue mobilisation, NBR targets proved to be over cautious for two consecutive years (FY2010-11 and FY2011-12), whereas all expenditure targets appear to be over optimistically set at the low side, except for development expenditure (i.e. ADP) where the situation was quite opposite. The government was also over optimistic about accessing foreign and non-bank sources of financing. And, probably the most critical of them all, subsidy projection was not at all synchronised with the government's plan for the power sector including establishment of rental power plants (RPPs) and the associated rise in fuel demand. The following sub-sections will briefly discuss the specific developments in the area of public finance.

Table 6

Mismatch of Targets and Actual Developments in Fiscal Management

(in Per cent)

Targets	Actual Growth FY11	Target Growth FY12[a]	Actual Growth (July to Latest in FY12)
NBR	28.0	15.7	18.1
Revenue Expenditure	17.5	12.0	32.5
ADP	26.8	40.0	8.6
Subsidy Expenditure	52.1	18.5[b]	69.8[c]
Foreign Financing	-50.6	293.5	163.0
Bank Borrowing	-	-24.8	80.3
Non-Bank Borrowing	-72.2	65.8	Net Negative

Source: Ministry of Finance (MoF) and Implementation Monitoring and Evaluation Division (IMED) data.
Note: [a]Budgetary targets for FY2011-12 over actual FY2010-11. [b]Growth target over revised budget. [c]Revised budget growth over revised budget.

2.2.1 Revenue Earnings

NBR Revenue: Surpassing Targets, Yet Again

Backed by strong revenue in-take from import duty, value added tax (VAT) (local) and income tax, NBR has surpassed its annual growth target of 15.7 per cent during the first three quarters of FY2011-12, posting 18.1 per cent growth. If the current growth rate sustains in the last remaining quarter, NBR could exceed its annual target of Tk. 91,870 crore by about Tk. 1,500 crore (Table 7). Indeed, for the second consecutive year, NBR revenue target has been adjusted upward; by Tk. 500 crore in the revised target for FY2011-12.

In FY2011-12, higher fuel imports to feed the RPPs have contributed to the increase in import duty collection. Most impressively, income tax collection on an average posted about 22 per cent growth during the last decade (FY2000-01 to FY2010-11). As a result, share of direct taxes in total tax revenue (NBR and non-NBR) rose to 28.1 per cent in FY2010-11. During the first three quarters of the current fiscal year income tax collection recorded an impressive 28 per cent growth.

Table 7

NBR Revenue: Growth Targets and Achievements

(in Per cent)

Particular	Actual Growth FY11	Annual Target FY12 (Crore Taka)	Annual Growth Target FY12	Achieved Growth FY12 (Jul-Mar)
Import Duty	28.4	12571.9	8.8	13.5
VAT (Import)	16.2	13748.8	11.1	7.4
Supplementary (Import)	24.8	4420.3	10.5	8.4
Export Duty		35.0	21.9	4.8
External Total	**22.4**	**30776.0**	**10.1**	**10.0**
Excise Duty	39.9	450.0	-7.4	51.1
VAT (Local)	29.1	20622.2	15.6	20.0
Supplementary (Local)	27.8	11784.8	21.5	17.5
Turn Over Tax	-22.3	5.0	37.7	4.4
Local Total	**28.8**	**32862.0**	**17.3**	**19.8**
Income Tax	35.0	27561.0	19.8	28.0
Travel Tax	6.8	670.8	62.8	8.8
Others	-42.9	0.3	212.5	-33.3
Total Direct Tax	**34.4**	**28232.0**	**20.6**	**27.6**
Grand Total	**28.0**	**91870.0**	**15.7**	**18.1**

Source: National Board of Revenue (NBR) data.

Non-NBR Tax and Non Tax Revenue: More Needs to be Done

Information on non-NBR[10] tax and non-tax[11] revenue is only available for the July-January period of FY2011-12. Data shows that collection of non-NBR tax revenue earnings slowed down quite considerably during the first seven months. Against an annual growth of 20.3 per cent in FY2010-11 and a target growth of 18.7 per cent for FY2011-12, this revenue head recorded only 11.1 per cent increase during the first seven months of FY2011-12 (Table 8).

Table 8

Growth in Non-NBR Tax and Non-Tax Revenue Collection

(in Per cent)

Particular	Actual Growth FY11	Growth Target FY12	Achieved Growth FY12 (Jul-Jan)
Non-NBR Tax	**20.3**	**18.7**	**11.1**
Narcotics and Liquor	8.6	11.1	2.9
Vehicles	5.4	42.8	9.4
Land	8.0	31.6	7.2
Stamp	29.6	8.5	12.6
Non-Tax Revenue	**0.2**	**68.1**	**61.8**
Dividend and Profit	-32.9	29.3	83.6
Post Office and Railway	1.5	27.7	5.6
Interest/Fees/Tolls and Other receipts	6.8	76.1	60.7

Source: Based on the Ministry of Finance (MoF) data.

On the other hand, impressive 61.8 per cent growth in non-tax revenue was due to collection of spectrum and license renewal fees from the mobile network operators. Around Tk. 4,000 crore is expected on this account in FY2011-12. The 3G license draft has recently been approved and the auction might take place in September 2012, which could once again play a vital role in augmenting the non-tax revenue in FY2012-13.[12]

[10] Contributes about 3.5 per cent to total revenue.
[11] Non-tax revenue accounts for about 14 per cent of total revenue intake.
[12] Bangladesh Telecommunication Regulatory Commission (BTRC) expects around USD 1.5 billion (about Tk. 12,000 crore) from the 3G spectrum fees.

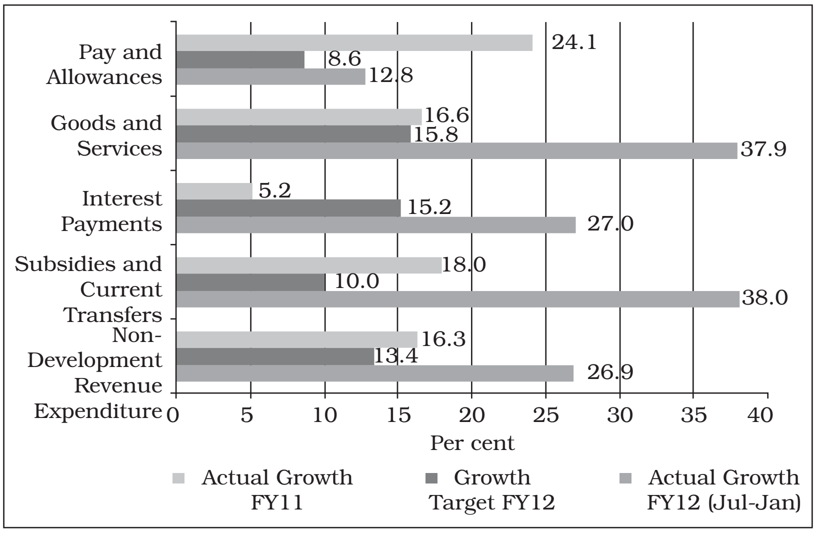
2.2.2 Public Expenditure

Revenue Expenditure: Defying Limits

During July-January period of the current fiscal year, all revenue expenditure heads recorded substantially higher growth than their programmed levels. Overall, non-development revenue expenditure recorded 26.9 per cent growth during the first seven months compared to the matching period of the previous year, while target growth for FY2011-12 was only 13.4 per cent (Figure 3). On the other hand, augmented revenue expenditure (which includes Acquisition of Assets and Works) posted a staggering 32.5 per cent growth. The most critical deviations from the (augmented) revenue expenditure targets were recorded for Acquisition of Assets and Works, Goods and Services, Interest Payments, and Subsidies and Current Transfers. Subsidies and Current Transfers contributed almost 50 per cent of the incremental revenue expenditure (excluding Acquisition of Assets and Works) during the period under review. Subsidies alone (excluding those to public institutions such as Bangladesh Petroleum Corporation (BPC) and Bangladesh Power Development Board (BPDB)) contributed 32 per cent in the growth.

Figure 3

Growth in Revenue Expenditure Components



Source: Ministry of Finance (MoF) data.

Note: Acquisition of Assets and Works, a part of augmented revenue expenditure, has not been included in the Figure, which posted 879.9 per cent growth during July-January period of FY2011-12.

Domestic interest payments, which is the fallout of the high borrowing of the government from the banking system, increased by 32 per cent and contributed 23.7 per cent in the additional revenue expenditure burden (excluding Acquisition of Assets and Works) during the first seven months of FY2011-12. Domestic interest payments accounted for 20.7 per cent of revenue expenditure during July-January period of FY2011-12.[13]

Expenditure on Subsidies: The Built-in Destabiliser

A major destabilising feature of the fiscal management in FY2011-12 has been the unforeseen growth in subsidy requirements. Original allocation for subsidy was of Tk. 20,447 crore for this fiscal. As the year progressed, this figure proved to be vastly underestimated. Along with the fiscal burden, demand for foreign exchange to underwrite liquid fuel import also increased. Mounting demand for resources proved to be too heavy to bear, forcing the government to maintain a large part of the installed capacity to remain

[13]Foreign interest payments accounted for 1.5 per cent of revenue expenditure (excluding Acquisition of Assets and Works).

unutilised by restraining the supply of fuel to them. Even after several upward adjustments in administered prices of fuel and electricity, and transferring Tk. 10,000 crore subsidy payments from the current fiscal year to FY2012-13, the revised subsidy budget for FY2011-12 is likely to be set at over Tk. 29,000 crore, according to media reports. This implies that total subsidy demand is estimated to approach Tk. 40,000 crore in FY2011-12. This will be about 4.4 per cent of the GDP – a remarkable increase compared to 2.2 per cent of FY2010-11.[14] On the other hand, the transfer of this year's subsidy payments to the next will result to a built-in instability in the budget for FY2012-13. Whatsoever, the subsidy episode – as an off short of deficient energy planning – by and large single handedly destabilised the public finance in FY2011-12.

According to media reports, the government is planning for a Tk. 34,533 crore subsidy allocation for FY2012-13, including the carryover of Tk. 10,000 crore from the current fiscal year. Therefore, the government is expecting much lower subsidy expenditure in the coming year, i.e. one-third reduction in current prices. This implies that the government will undertake energy price adjustments, as agreed with the IMF (as a part of the Extended Credit Facility (ECF) conditionalities), to allow 'full pass-through' of international prices in the domestic market by December 2012. It is, however, not yet clear in this context whether the government is going to maintain existing duties on fuel imports. Arguably, elimination of the mentioned duties will incur significant cost to the public exchequer, as duties on fuel import have been a sizable source of revenue. During July-April of FY2010-11, about Tk. 3,100 crore of revenue has been paid by the BPC in duties on fuel imports.

Although the full adjustment of fuel prices (if applied) will create considerable fiscal space for the government, major concern emerges from its potential impact on prices. As a decomposition of inflation sources reveals, between April 2011 and April 2012, the rise in inflation was associated more with non-food items. Within the non-food categories, i.e. gross rent, fuel and lighting, and transport and communication – items that bear the impact from fuel and power price adjustments more directly than others – were the major contributors to inflation (more on this in Section 2.3). Therefore, a full adjustment of domestic prices with international prices will possibly create significant inflationary pressure on the economy, which is unlikely to be offset by a growth reducing contractionary monetary policy, and could prove to be politically difficult to implement. The government will be well advised to prudently approach this issue.

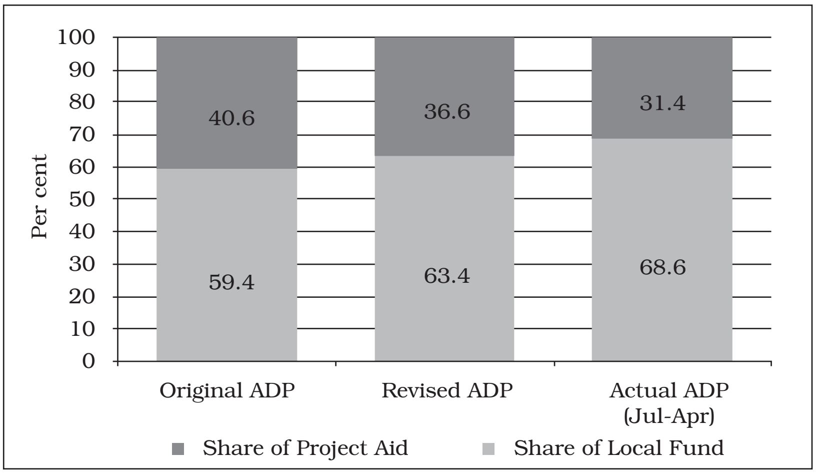
Annual Development Programme (ADP): Poorest Show in Recent Times

As in earlier years, low implementation of ADP during the first three quarters of FY2011-12 forced the government to revise the size of ADP downward by Tk. 5,000 crore resulting reduction of the size of ADP from Tk. 46,000 crore to Tk. 41,000, i.e. by 13 per cent). However, as the July-April implementation status indicates, this year the rate of ADP implementation has been the lowest in the tenure of the current government – only 55.4 per cent of the RADP as against 58.3 and 58.6 per cent respectively in FY2010-11 and FY2009-10.

Low disbursement of foreign funds leading to slower implementation of foreign aided projects brought down the share of foreign financing component of (revised) ADP to 36.6 per cent as against 40.6 per cent in the original ADP allocations (Figure 4). During the first ten months, only 47.6 per cent of the revised aid allocation has been utilised, forcing the share of local financing to 68.6 per cent in total ADP spending during this period.

[14]Actual subsidy spending for FY2010-11 is unavailable. Revised subsidy allocations have been used.

Figure 4
Financing Composition of ADP in FY2011-12



Source: Implementation Monitoring and Evaluation Division (IMED) data.

Larger projects in the ADP appear to be running relatively at slower pace. A CPD research involving the largest 20 projects that have been included in the ADP since January 2009[15] (with varying starting times and project durations, to be completed between 2012 and 2015) revealed on an average only 10.3 per cent cumulative implementation till November 2011 (Table 9). Within this list of 20 projects, seven are in their third year of implementation, nine are in second year of implementation, and the remaining four are in their first year of implementation. The list, however, includes the Construction of Padma Multipurpose Bridge (revised) project. If one excludes the Padma Bridge project from the exercise, the cumulative implementation rate marginally improves to 13.2 per cent for the remaining 19 projects. More interestingly, eight of these largest 19 projects are yet to spend any money since their inception, while another three had a cumulative expenditure of just 1 per cent.[16]

At the same time, since 2009 implementation of *aided projects* appears to have weakened further. The list of the largest 20 projects mentioned above include 11 aided projects, all of which are either in their third or second year of implementation, and are slated to be completed between 2012 and 2015. Cumulative implementation of majority of these projects is found to be extremely low: 0-1 per cent for seven projects, 4 per cent for two projects, 9 per cent for one project, and 70 per cent for one project.

A parallel CPD exercise on a separate list of 20 foreign aided projects with highest allocations and accounting for about 21 per cent of the RADP of FY2011-12 suggests similar story. On an average, only 34 per cent of the total allocations for these projects were spent during July-March period of FY2011-12 along with 35.7 per cent utilisation of comparable aid allocations. Performance was lower than overall ADP implementation of 50.3 per cent and overall aid utilisation of 40.9 per cent during this timeframe (Table 10). Thus, it is evident that slow pace of ADP implementation is mainly dictated by the large and foreign aid projects (they are largely coterminous).

As was mentioned earlier, during the first ten months of FY2011-12 only 47.6 per cent of the revised aid allocation has been utilised. In the RADP, aid allocation has been brought down by 19.7 per cent, and thus, FY2010-11 and FY2011-12 witnessed the highest downward revision since FY2001-02. If the current financing composition of project aid and local resources remains, it is estimated that this year's ADP will end up with the lowest aid utilisation rate since FY2000-01, i.e. less than 62 per cent of the original allocation (Table 11).

[15]Excluding the projects that are freshly included in the RADP of FY2011-12.
[16]Construction of Padma Multipurpose Bridge (revised) is showing 4 per cent cumulative spending till November 2011.

Table 9

Largest Projects Included in the ADP since January 2009

(Lakh Taka)

Name of Project	Project Duration	Project Cost		Cumulative Implementation up to Nov FY12 (%)
		Total	Aid	
Construction of Padma Multipurpose Bridge (rev)	2009-2015	2050720	1624952	4.0
Construction of 820 MW peaking power plant (rev)	2009-2012	695986		52.0
Priority based important rural infrastructure development project	2010-2013	469113		12.0
Bheramara combined cycle plant (360 MW) development	2010-2014	414048	322108	1.0
Revitalisation of community healthcare initiatives in Bangladesh	2009-2014	267749	50000	0.0
First class meterological observation centre at Panchagarh, Bandarban, Khagrachhari, Cox's Bazar	2009-2013	249696		0.0
Development of physical infrastructure of selected non-government high schools	2011-2014	211480		0.0
Construction of Siddhirganj 335 MW peaking combined cycle power plant	2009-2015	207781	150213	0.0
3G network technology establishment and extension of 2.5G network	2011-2012	190099	147700	0.0
Construction of meter gauge line at Dohajari-Cox's Bazar and Ramu-Gungdum	2010-2013	185235	118228	1.0
Feasibility study and railway construction from Khulna to Mongla port	2010-2013	172139	120231	0.0
Bibiana-Kaliakoir 400 KV and Fenchuganj-Bibiana 230 KV transmission line	2010-2013	172085	70000	9.0
Ekti Bari, Ekti Khamar project (rev)	2009-2013	149292		15.0
South-West rural infrastructure development	2010-2013	148072	107113	4.0
Renovation of ailed roads under Roads and Highways	2011-2012	141027		6.0
Rural electrification upgradation project (Rajshahi, Rangpur, Khulna and Barisal divisions)	2010-2015	132218	99554	0.0
Dredger and related machinery procurement for capital dredging of rivers of Bangladesh	2010-2012	130988		0.0
Construction of Siddhirganj 2*120 MW peaking power plant (2nd rev)	2009-2012	124363	7700	70.0
Asrayan-2	2010-2015	116918		0.0
Important urban infrastructure development project	2011-2014	115099		1.0
Total for the 20 Projects		**6344108**	**2817799**	**10.3**

Source: IMED (2012).
Note: Projects with aid component are shaded.

Table 10

Largest 20 Aided Projects in the Revised ADP of FY2011-12

(Lakh Taka)

Name of Project	Allocation			Expenditure			% of Allocation		
	Total	Taka	Aid	Total	Taka	Aid	Total	Taka	Aid
Introduction of 3G network technology and expansion of 2.5G network	70000.0	0.0	70000.0	29579.2	39.2	29540.0	42.3	0.0	42.2
Construction of Haripur 360 MW combined cycle power plant and associated sub-station (EGCB component)	69900.0	16000.0	53900.0	26953.4	3631.0	23322.4	38.6	22.7	43.3
Construction of Padma Multipurpose Bridge	61494.0	16205.0	45289.0	24953.2	10859.0	14094.2	40.6	67.0	31.1
2nd Local Governance Support Project (LGSP-2)	58834.0	24800.0	34034.0	0.0	0.0	0.0	0.0	0.0	0.0
Shahjalal Fertilizer Project	57200.0	2200.0	55000.0	0.0	0.0	0.0	0.0	0.0	0.0
Construction of Sirajganj 150 MW Gas Turbine Power Plant	55500.0	28500.0	27000.0	37720.1	11684.6	26035.5	68.0	41.0	96.4
Maternal, neonatal, child and adolescent healthcare	51700.0	5200.0	46500.0	0.0	0.0	0.0	0.0	0.0	0.0
Special Purpose Development Assistance	48623.0	15000.0	33623.0	0.0	0.0	0.0	0.0	0.0	0.0
Karnaphuli Water Supply Project	47482.0	9000.0	38482.0	19516.3	10692.2	8824.0	41.1	118.8	22.9
Second Rural Infrastructure Improvement Project (RIIP-2)	39500.0	15000.0	24500.0	30143.6	14436.3	15707.3	76.3	96.2	64.1
Saidabad Water Treatment Plant Project	38500.0	10000.0	28500.0	28087.4	7828.3	20259.1	73.0	78.3	71.1
Bangladesh Railway Sector Improvement Project (construction of double line up to Tongi-Bhairab including signaling component)	35200.0	12500.0	22700.0	16249.7	2756.7	13493.0	46.2	22.1	59.4
Secondary Education Quality and Access Enhancement Project (SEQAEP)	31393.0	3606.0	27787.0	11424.7	87.5	11337.1	36.4	2.4	40.8
Construction of Siddhirganj 2*120 MW peaking power plant	31277.0	14712.0	16565.0	18247.0	0.0	18247.0	58.3	0.0	110.2
Bangladesh Power Zone Distribution Project	30500.0	3000.0	27500.0	12937.6	801.9	12135.8	42.4	26.7	44.1
Procurement of single decker CNG buses	24747.0	4092.0	20655.0	0.0	0.0	0.0	0.0	0.0	0.0
School Feeding programme in poverty-affected area	23950.0	10400.0	13550.0	12569.0	2317.1	10251.8	52.5	22.3	75.7
Project for Infrastructure Development and Secondary City Management	23000.0	3000.0	20000.0	18275.8	1711.6	16564.2	79.5	57.1	82.8
Clinical contraception services delivery	22467.0	13800.0	8667.0	0.0	0.0	0.0	0.0	0.0	0.0
Primary Education Development Project-3	22381.0	21243.0	1138.0	0.0	0.0	0.0	0.0	0.0	0.0
Average for 20 projects	**843648.0**	**228258.0**	**615390.0**	**286656.9**	**66845.3**	**219811.5**	**34.0**	**29.3**	**35.7**
Overall RADP (Jul-Mar)	**4100000.0**	**2600000.0**	**1500000.0**	**2061700.0**	**1448800.0**	**612900.0**	**50.3**	**55.7**	**40.9**
Share of 20 projects	**20.6**	**8.8**	**41.0**	**13.9**	**4.6**	**35.9**	**-**	**-**	**-**

Source: Implementation Monitoring and Evaluation (IMED) data.

Note: EGCB denotes Electric Generation Company of Bangladesh.

Table 11

Revision and Utilisation of Aid Allocation in the ADP

Year	Absolute Revision (Crore Tk.)	Revision % of Original	Utilisation Rate of Project Aid (%)
FY2001	+13.0	+0.2	78.0
FY2002	-1399	-17.0	66.9
FY2003	-1181	-15.7	68.3
FY2004	-1484	-17.5	65.4
FY2005	-1400	-18.9	75.5
FY2006	-375	-5.0	83.4
FY2007	-800	-9.1	70.9
FY2008	-850	-8.7	71.2
FY2009	-1800	-15.0	65.9
FY2010	-1545	-12.0	74.1
FY2011	-3370	-22.0	64.1
FY2012	-3685	-19.7	61.7*

Source: Implementation Monitoring and Evaluation Division (IMED) data.
Note: *Projected.

Indeed, overall low implementation of larger and aided projects has been one of the critical factors underpinning the instability observed in fiscal management in FY2011-12, and has added significant pressure on local resources in financing the budget deficit. According to CPD estimates, projected shortfall in overall ADP implementation this year may amount to about Tk. 9,300 crore. This will imply a 79.8 per cent ADP implementation (of the original); 89.5 per cent of the RADP. If the projection comes true, the ADP-GDP ratio for this year will go down to 4 per cent, a reversal in the improving trend observed after FY2007-08.

2.2.3 Budget Deficit: In Desperate Need of Foreign Financing

With financing pressure emanating from overshooting revenue expenditures, overall budget deficit (excluding grants) stood at Tk. 10,253 crore during July-January period of FY2011-12 against a surplus of (-) Tk. 1,131 crore during the matching period of FY2010-11 (Table 12). However, modest level of net foreign financing and low contribution of financing from the non-banking sources made financing the deficit a major macroeconomic challenge in FY2011-12.

Table 12

Deficit and its Financing

(Crore Tk.)

Description	FY11 Actual	FY12 Budget	FY11 (up to Jan)	FY12 (up to Jan)
Deficit				
Revenue Collection	92790	118385	49336	62036
	(11.6)	(12.9)		
Total Expenditure	127793	163589	48205	72288
	(16.0)	(17.9)		
ADP	33091	46000	8772	12525
	(4.2)	(5.0)		
Non-ADP	94702	117589	39433	59763
	(11.9)	(12.9)		
Overall Deficit (excluding Grants)	***35003***	***45204***	***-1131***	***10253***
	(4.4)	***(4.9)***		

(Table 12 contd.)

(Table 12 contd.)

Description	FY11 Actual	FY12 Budget	FY11 (up to Jan)	FY12 (up to Jan)
Financing				
Foreign Borrowing (Net including Grants)	4573	17996	184	483
	(0.6)	(2.0)		
Foreign Grants	1306	4938	178	1363
	(0.2)	(0.5)		
Foreign Loan	8694	18685	3110	2482
	(1.1)	(2.0)		
Amortisation	-5427	-5627	-3105	-3362
	(-0.7)	(-0.6)		
Domestic Borrowing	29964	27208	-1296	7878
	(3.8)	(3.0)		
Bank Borrowing (Net)	25210	18957	5468	13377
	(3.2)	(2.1)		
Non-Bank Borrowing (Net)	4754	8251	-6764	-5499
	(0.6)	(0.9)		
National Savings Schemes (Net)	1802	6000	2204	-26
	(0.2)	(0.7)		
Others	2952	2251	-8968	-5474
	(0.4)	(0.2)		
GDP in current market price	796704	914784		

Source: Ministry of Finance (MoF) data.
Note: Figures in parentheses are GDP shares.

From the very onset of the current fiscal year, the government had to resort to borrowing from the banking sources which became alarmingly high, and reached over Tk. 21,000 crore in early December 2011, exceeding the budgetary annual target of Tk. 18,957 crore. The latest available information shows that on 21 May 2012, borrowing by the government from the banking system has come down and stood at Tk. 18,452 crore, i.e. closer to the annual target. It seems, with likely pick-up of ADP expenditure during the remaining one and half month of the current fiscal year, bank borrowing by the government will exceed its original budgetary target, but may remain within the limit agreed with the IMF, which is about 3 per cent of the GDP.

It is to be noted that higher bank borrowing by the government, particularly from the central bank, tends to leave a number of negative impact on the macroeconomic management, as has been identified by many empirical studies. One such important negative impact is its 'crowding out' effect on the private sector from the access to finance. As Emran and Farazi (2009) found from a cross-country econometric analysis involving 60 developing countries that each additional USD 1 borrowing by the government from the banking sector reduces credit available to the private sector by about USD 1.4. Whether the private sector will gain from the public spending in medium to long-term, offsetting the short-term loss, will obviously depend on the productive nature of the public spending.

On the other hand, according to Jácom *et al.* (2012), central bank financing to the government is considered to be a chronic source of inflation. This is so because central bank financing to the government essentially means printing of money, increasing the monetary base, and hence, the money supply. This also leads to erosion of purchasing power of the local currency and exchange rate depreciation, leading to imported inflation.

Given the multidimensional negative impacts of bank borrowing which are already visible in Bangladesh, mobilising foreign resources accumulated in the pipeline due to the non-implementation of aided projects has become a necessity. At the beginning of FY2011-12 this accumulated aid in pipeline amounted to about USD 14 billion.

To reduce pressure on bank borrowing and in order to improve the contribution from non-bank sources of financing, the government is planning to introduce five new saving schemes targeting elderly people, farmers, students and persons with disabilities. It is to be borne in mind that the relative yield rates of these government saving schemes as against commercial deposit rates offered by private banks are the most important factor determining the prospect of fund mobilisation through these instruments.

2.3 Monetary Policy: Hurting Economic Growth

2.3.1 Inflationary Pressure Continues: Non-Food Inflation in the Driver's Seat

Inflation during the last three years has been on the rise. The annual average inflation target for FY2011-12 was set at 7.5 per cent. In view of the reality, the most recent Monetary Policy Statement (MPS), issued on January 2012 optimistically hoped for a 'single digit inflation' at the end of the year (Bangladesh Bank 2012). At the end of first ten months of the fiscal year (July-April), there is hardly any sign of cooling down. General inflation (annual average) reached 10.9 per cent in April 2012 which was 8.5 per cent in April 2011 (Table 13). Indeed, during the last four months (January-April, 2012) average inflation remained stagnated at around 10.9 per cent.[17] In April 2012, food inflation was 11.4 per cent, while non-food inflation reached to as high as 10 per cent.[18] Within non-food commodities, prices of clothing & footwear, gross rent, fuel & lighting, and transport & communication experienced considerable increase.

Table 13

Category-wise Annual Average Inflation

(in Per cent)

Commodity	FY11 (April)	FY12 (April)
General	**8.5**	**10.9**
Food	**11.0**	**11.4**
Non-Food	**4.2**	**10.0**
Clothing & footwear	5.2	16.2
Gross rent, fuel & lighting	3.9	8.4
Furniture, furnishing, household	7.6	11.3
Medical care & health expenses	6.1	5.2
Transport & communication	5.4	11.1
Recreation, entertainment	3.7	2.2
Miscellaneous goods & services	4.2	13.0

Source: Estimated from the Bangladesh Bureau of Statistics (BBS) data.

A decomposition of inflation figures as on April 2011 and 2012 reveals that, of the 8.5 per cent inflation in April 2011, 7 per cent came from food inflation, while the rest – 1.5 per cent came from non-food inflation. Of 10.9 per cent inflation in April 2012, 7.4 per cent was contributed by food inflation and 3.5 per cent was accrued to non-food inflation (Figure 5). It implies, of the incremental inflation between the two periods, i.e. 2.4 percentage points – 2 percentage points (or 82.7 per cent) was originated from increase in non-food commodity prices. Among the sub-categories of non-food items, larger contributions

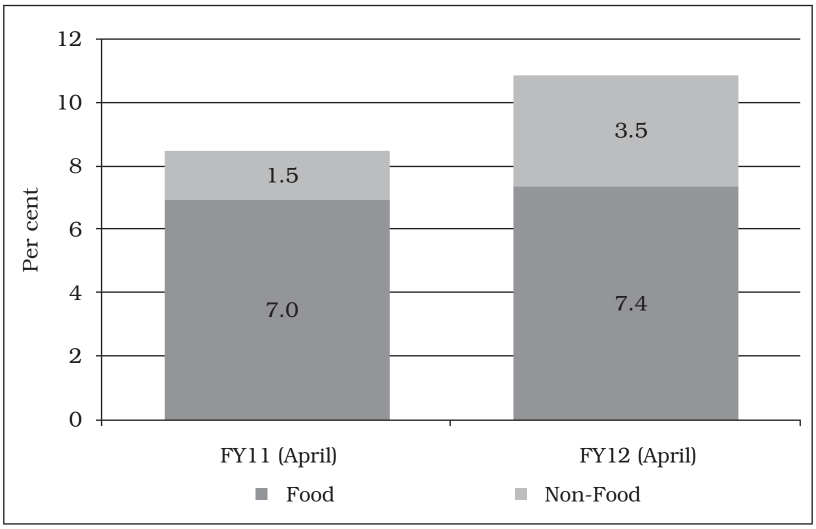
[17]When compared with her South Asian neighbours, Bangladesh tops the list in terms of having the highest rate of inflation in the current fiscal year. However, in India and Pakistan inflation rate remained at a higher level. Inflation rates in India, Pakistan and Sri Lanka were 10.4 per cent (April), 10.8 per cent (March), and 6.1 per cent (Colombo CPI, April) respectively.

[18]Since the mid-2000s price level of food items became the dominant contributor to inflation in Bangladesh. Point-to-point food inflation started to slow down since July 2011. On the other hand, non-food inflation surpassed food inflation in December 2011.

came from clothing & footwear (0.6 percentage points), gross rent, fuel & lighting (0.6 percentage points), and transport & communication (0.2 percentage points). Indeed, the adjustment of administered prices of petroleum products and electricity, depreciation of Taka, and increase in cost of production made a mark on price level of non-food items. However, one needs to be mindful that food inflation is still high and remains the major source of overall price level increase.

Figure 5

Sources of Annual Average Inflation



Source: Estimated from the Bangladesh Bureau of Statistics (BBS) data.

2.3.2 Inflationary Expectation to Continue

Before crafting a policy to rein in inflation it is important that its nature is properly diagnosed. Literature on inflation in Bangladesh mentioned about a number of determinants of price level increase.[19] CPD in its earlier macroeconomic review (March 2012) concluded that cost-push and structural factors have overwhelmingly underpinned the incremental inflation in recent times (for details, see CPD 2012). Among the cost-push factors, a number of issues were identified in the present context including upward adjustment of administered petroleum and electricity prices, increase in cost of production including wage rates, and depreciation of exchange rate.[20] Upward adjustment of recent electricity and fuel prices had impacts on inflation in both direct and indirect ways as they have an immediate knock on effect on other sectors such as transportation and housing, which are now reflected from the recent inflation figures. The extent of exchange rate pass-through into selling prices of imported commodities also needs to be assessed carefully. It is also expected that the administered prices of key intermediate products (electricity, petroleum products, natural gas, fertilisers, etc.) may be adjusted further in coming months. Simultaneously, value of Taka is not out of danger as balance of payments is expected to remain under pressure. The stagnation in investment situation also indicates that the cost of production is not going to decline anytime soon. All in all, inflationary expectation remains quite high.

[19] In empirical literature it has been identified that money supply growth has significant impact on inflation in Bangladesh (Mortaza 2006; Majumder 2006). While money supply could have a positive significant impact on inflationary trend, currency depreciation is seen to have not significant influence on inflation in Bangladesh (Hossain 2007). However, according to Osmani (2007) exchange rate have an impact on inflation in Bangladesh. Asides these, other factors such as food and oil prices in the international market, cost of production, shortage of agricultural commodities, inward remittances, government debt, inflation inertia are also important determinants of inflation in Bangladesh (Ahmed 2009; CPD 2011a).

[20] The cost of agricultural inputs, such as fertiliser, seed, wage rate and irrigation increased over time (see, *A Special Note on Crop Production and Food Security* for details). According to BBS data, during July-February, FY2011-12, average agriculture wage rate also increased substantially, by 25.8 per cent and 32.9 per cent for male and female workers respectively compared to the corresponding period of FY2010-11.

2.3.3 Contractionary Monetary Policy Pursued with Limited Success

Considering the inflation scenario in Bangladesh over the past periods, the monetary policy stance of Bangladesh Bank for FY2011-12 assumed inflation control as its core objective; if necessary, sacrificing the growth and investment prospect. Following a New Keynesian Framework, where the agents have rational expectations, market disequilibrium and sticky prices, contractionary monetary policy works through inflation adjustments. When the central bank declares their intention of monetary tightening, the agents adjust their actions accordingly so that it leads to a decrease in inflation in the short-run. The benefit of monetary tightening is that the central bank can send almost immediate signals to both the public and markets about their monetary policy stance of keeping inflation in check (Miskin 1997). Thus, the central bank operates within a flexible system that allows it to set the targets according to its short-term objectives (Clardia *et al.* 1999; Miskin and Posen 1997).

Two aspects largely determine the effectiveness of monetary targeting. First, it depends on the relationship between the goal variable and the targeted aggregate – inflation and money supply respectively in this case. If the relationship between the monetary aggregate and the goal variable is weak, then even if the targeted money supply growth is achieved, it may not provide the desired outcome (Miskin 1997). Restricting money supply can only address inflation originated from 'demand-pull' phenomenon. In contrast, it may be counter-productive for other natures of inflation. It needs to be noted that some inflation, arising from increase in aggregate demand, is required for economic growth itself (Nishimukai 1965). Hence, it is the incremental inflation beyond the tolerable level, that needs attention. As indicated earlier, currently the incremental inflation is largely attributable to cost-push and structural factors.

The second condition for the monetary tightening to work successfully relates to central bank's strong commitment to transparency and communication of the strategy of the monetary policy to the public (Miskin 1997). Therefore, central bank would have to have the credibility to create non-positive inflationary expectations and be able to control the targeted monetary aggregate. Bangladesh Bank has systematically missed its monetary targets in the recent periods (Bhattacharya and Khan 2010), and thus, has partly eroded its credibility. In FY2011-12 it may once again miss the targets.

In the recent MPS, Bangladesh Bank has reduced growth of credit flow to the private sector and expanded government borrowing targets (CPD 2012). The monetary policy for the second half of FY2011-12 set growth targets for private and public sector credit to 16 per cent and 31 per cent respectively; as of end March the comparable figures were 19.5 per cent and 34.5 per cent respectively (Table 14). Growth of broad money (M2) was 17.6 per cent against its target of 17 per cent. The lowering of private sector credit growth was underpinned by decline in industrial term loans. It implies that the monetary tightening came at an expense of reduced private investment, as reflected from national accounting data. Admittedly, the incremental growth of money supply beyond its target was largely due to excessive government borrowing from the banking sources. As the demand for local resources is going to rise during the last quarter proportionately to the ADP implementation, it remains to be seen whether the government can adhere to the limit given to it. Considering the evolving scenario in the monetary sector, the central bank is likely to have limited success on controlling, even though the economic growth may slow down.

Whatsoever, it is important to note that, movements of monetary aggregates during the third quarter (January-March) of FY2011-12 had been different from that of the first half (July-December). Until December 2011, private sector credit growth was on a declining path, whereas government credit was demonstrating incremental growth (Figure 6). Subsequently, target for private sector credit growth was revised downward and target for public sector credit growth was revised upward in the MPS for second half of FY2011-12. During the fiscal's third quarter, government managed to check its borrowing from banking system, which resulted in reducing growth of government borrowing. Concurrently, growth rate of credit to other public sector fell drastically and was in a negative figure. On the other hand, falling growth of private sector credit somewhat stabilised at around 19-19.5 per cent. Overall money supply growth came close to its target at the end of March FY2011-12.

Table 14

Growth of Monetary Aggregates

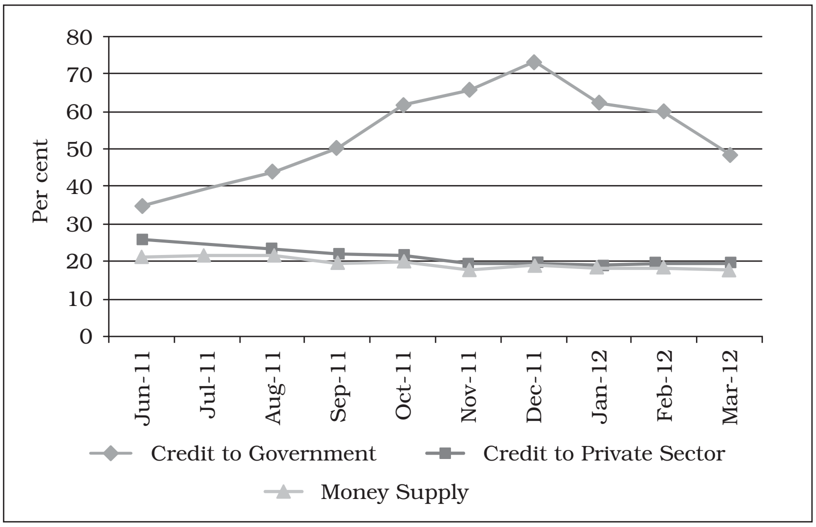
(in Per cent)

Monetary Aggregate	FY10	FY11		FY12		
	Actual	Target	Actual	Old Target	New Target	As of End March
Net Foreign Assets	41.3	-1.5	5.3	-1.6	-8.9	4.6
Net Domestic Assets	18.8	20.0	25.0	22.1	21.9	20.2
Domestic Credit	17.6	18.8	27.4	20.0	19.1	22.5
Credit to Public Sector	-5.2	29.2	33.6	28.1	31.0	34.5
Net Credit to Government Sector	-6.5	NA	34.9	NA	NA	48.6
Credit to Other Public Sector	21.1	NA	28.7	NA	NA	-8.4
Credit to Private Sector	24.2	16.5	25.8	18.0	16.0	19.5
Broad Money (M2)	22.4	16.0	21.3	18.5	17.0	17.6
Reserve Money	18.1	15.0	21.1	16.0	12.2	11.9

Source: Bangladesh Bank data.

Figure 6

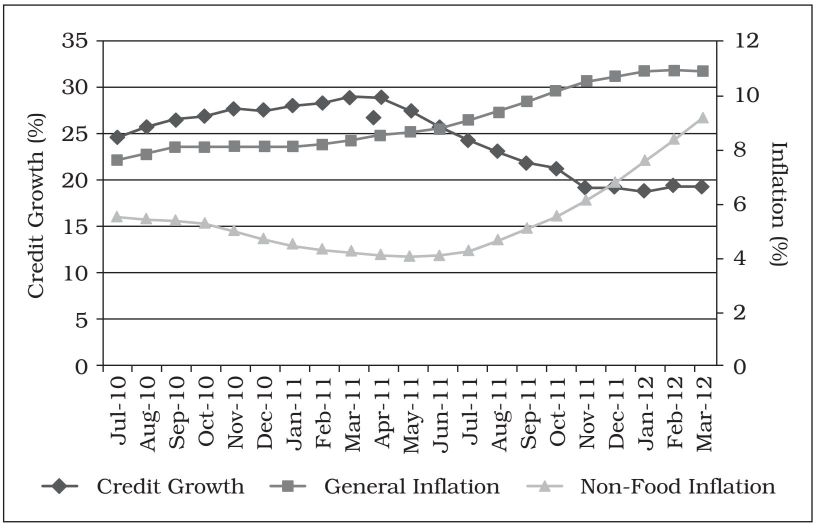
Growth of Credit and Money Supply (Year-on-Year)



Source: Estimated from the Bangladesh Bank data.

Figure 7

Private Sector Credit Growth and Annual Average Inflation



Source: Bangladesh Bank and Bangladesh Bureau of Statistics (BBS).

The monetary contraction was also found to be not effective in controlling the overall inflation as well as its non-food component. Non-food inflation continued to soar at a time when credit growth to private sector was on decline (Figure 7). Since April 2011, these two indicators are moving completely in opposite direction. A simple correlation suggests that there is strong negative relationship between private sector credit and non-food inflation (or general inflation).[21]

2.3.4 Monetary Policy Stance for FY2012-13: Bold Steps Warranted

CPD (2012) indicated that "... current macroeconomic policy stance may undermine potential economic growth and investment, but it will have a little success in controlling inflation." It appears that throughout FY2011-12 central bank's monetary policy prioritised inflation control over growth acceleration, and lost the battle in both fronts. In reality, the framework of forthcoming monetary policy of the Bangladesh Bank will largely depend on fiscal policy from the Ministry of Finance (MoF). Regrettably, it is known that, in Bangladesh, the central bank has limited control over government's demand for bank credit. No doubt, without restraining government's bank borrowing, discipline in the monetary sector will be difficult to attain. According to the IMF Country Report, the projections for private sector credit and money supply growths are 14.9 per cent and 15.4 per cent respectively (IMF 2012). The question is how these 'projections' are going to guide the upcoming MPS. Bangladesh Bank will need to consider the fact that GDP growth projection of IMF for FY2012-13 is also lower at 6.2 per cent. This target is even lower compared to the provisional GDP growth rate for FY2011-12, and about 1 percentage point lower than the GDP growth target of the government for FY2012-13. Hence, Bangladesh Bank is posed with a difficult choice between following a tight monetary policy and ensuring credit to the private sector to achieve the targeted growth. An independent central bank will not shy away from choosing the latter.

2.4 Balance of Payments: Not Out of Danger

All the macroeconomic correlates associated with balance of payments are moving downwards as the economy entered into the last quarter of FY2011-12. Export growth fell into negative terrain in recent months, while import requirement did not reduce by the same margin. Remittance inflow turned to be inadequate to keep up with the widening trade deficit. Despite making some improvements, foreign aid inflow remained below par. Although Bangladeshi Taka (BDT) has stabilised a bit against foreign currencies, yet pressure on it remains. Without support in the form of higher net inflow of foreign aid, balance of payments will continue to remain vulnerable. With the looming uncertainties in the developed world, external sector balances will likely to be under some pressure over the following months.

2.4.1 Export Earnings: Short of Target

Export earnings in FY2011-12 started to slow down in the second half and gradually fell short of the target set for the year. Against the targeted growth of 15.6 per cent, growth of export earnings was only 8.4 per cent during the first ten months of the fiscal year. To achieve the growth target set for FY2011-12, total export earnings will need to attain a 43.5 per cent growth in the last two months (May and June) (Table 15). As a matter of fact, growth of export earnings entered into a negative terrain during the last two consecutive months (March and April).[22] It is being speculated that the target for export earnings may be brought down to USD 23.7 billion from original target of USD 26.6 billion.[23] It implies, a (-) 15.6 per cent decline is expected over the next two months and growth figure for the full fiscal year may not be more than 3.5 per cent.

[21]Correlation figure for private sector credit growth and non-food inflation is (-) 0.7, whilst that for private sector growth and general inflation is (-) 0.9. The analysis considered monthly data between July 2010 and March 2012.
[22]Considering year-on-year estimation, growths of export earnings in March and April were (-) 7.2 per cent and (-) 7.1 per cent respectively.
[23]For details, see: http://www.thefinancialexpress-bd.com/more.php?news_id=130703&date=2012-05-25

Table 15

Growth Rates of Export

(in Per cent)

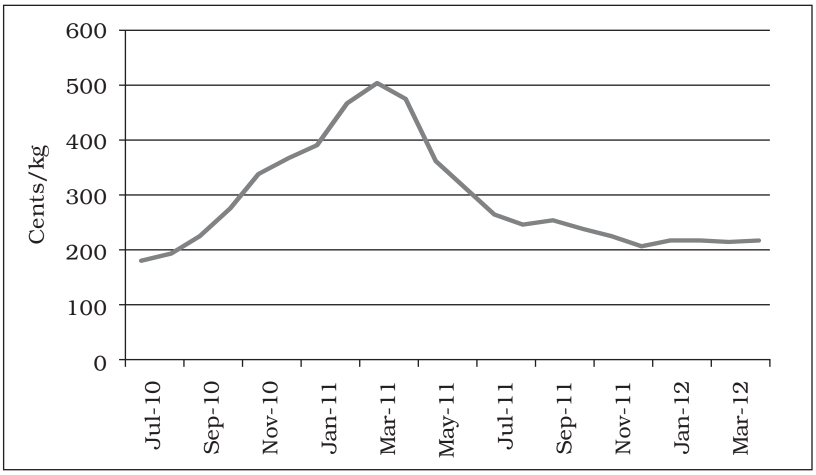
Product	Growth Achieved FY11 (Jul-Apr)	Growth Target FY12	Growth Achieved FY12 (Jul-Apr)	Required Growth for Rest of the Year to Attain Export Target
RMG	***42.4***	***13.7***	***9.6***	***29.1***
Knit	45.9	13.9	3.0	54.5
Woven	38.6	13.4	16.9	-0.2
Non-RMG	***36.0***	***22.5***	***4.4***	***100.7***
Raw Jute	69.2	30.0	-22.4	255.3
Leather	36.4	10.0	10.9	6.4
Frozen Food	53.6	16.2	-0.9	93.0
Total	**40.9**	**15.6**	**8.4**	**43.5**

Source: Estimated from the Export Promotion Bureau (EPB) data.

It is difficult to explain what leads to such a frustrating performance of export during FY2011-12. One could come up with a number of possible explanations. *First*, export growth was remarkable in FY2010-11. Attaining a higher growth on a high benchmark thus became difficult in the current fiscal year. *Second*, one can observe, in recent years export growth was resilient without a significant improvement in investment situation. As a result scope for using unused capacity (if any) may also have become limited in FY2011-12. Hence, it has been difficult for the exporters in FY2011-12 to expand their capacity to supply more (to attain growth) in the backdrop of stagnating private investment and inadequate infrastructure support during the recent years. *Third*, previous fiscal year's export growth may have been largely value-driven underpinned by rising unit prices as a result of significant rise in prices of raw materials. International price of cotton started to rise from July 2010. Indeed, average cotton price doubled in FY2010-11 compared to FY2009-10. Since March 2011, cotton price started to decline (Figure 8). The average cotton price during the first ten months of FY2011-12 (July-April) declined by (-) 29.8 per cent compared to the matching period of last fiscal. This should also be reflected in international prices of readymade garments (RMG) products. Thus, in value terms the export may have experienced a setback, but in volume terms the decline in growth may not have been that significant. *Fourth*, the performance of export sector is tied with the global developments, and grim global outlook affected the export orders. In this connection, one may recall that the government formed a high level committee to investigate the deteriorating performance of some of Bangladesh's export items (CPD 2012). Given the present context, a comprehensive response from this committee is warranted.

Figure 8

International Cotton Price



Source: World Bank Pink Sheet data.

Whatsoever, one can identify three disquieting features of recent export trends. *First*, export of knit RMG underperformed significantly compared to other exportables. In the first ten months of FY2011-12 (July-April), export of knit garment registered only 3 per cent growth; in contrast, woven garment export posted a rise of 16.9 per cent. In last two months (March and April) knit export declined by (-) 16.8 per cent. Growth of woven has also declined, albeit by a small margin, (-) 0.4 per cent. It is alarming that, in the United States (US) market, knitwear export decreased by (-) 11.2 per cent (Table 16). In European Union (EU), the traditional market for Bangladeshi knit products, export increased by 4 per cent. However, during March-April, export in EU also experienced a sharp decline, by (-) 19.1 per cent.

Table 16

Growth Rates of Knit Garment Export in FY2011-12 (July-April)

(in Per cent)

Export Destination	Jul-Aug	Sep-Feb	Mar-Apr	Jul-Apr
World	**29.6**	**0.8**	**-16.8**	**3.0**
US	-8.7	-11.3	-14.3	-11.2
Canada	19.0	-13.8	-18.8	-7.4
EU	36.5	1.4	-19.1	4.0
Germany	42.8	4.4	-21.1	6.4
UK	45.6	12.1	-9.5	13.4
France	23.0	-10.3	-38.0	-10.8
Spain	58.5	5.9	9.3	18.5
Italy	63.5	12.7	-20.9	15.3
Japan	211.8	93.7	51.4	97.7
Turkey	-20.7	-61.5	-71.8	-54.6
India	117.0	81.4	-9.7	65.9
China	334.5	89.6	47.1	110.0
Australia	121.0	56.0	28.4	57.3

Source: Estimated from the Export Promotion Bureau (EPB) data.

Second, export to the US market is in a weak situation and requires immediate attention. Export to the US market posted an insignificant growth of 0.2 per cent during the first nine months of FY2011-12, while export of RMG to the US market declined by (-) 2.3 per cent. Though growth of total RMG import by the US in the first nine months of FY2011-12 was low (3.7 per cent), some major competitors of Bangladesh, e.g. Vietnam, Cambodia, Indonesia, Nicaragua, Sri Lanka and Mexico managed to attain healthy growth.[24] Import of knit garment to the US from Bangladesh declined by (-) 10.8 per cent (Table 17). In contrast, her competitors achieved respectable growth – Nicaragua (39 per cent), Sri Lanka (28.3 per cent), Italy (20.2 per cent), Cambodia (13.8 per cent), Vietnam (9.6 per cent), Indonesia (9.8 per cent) and Guatemala (7.2 per cent). If competitors continue to perform better even in our dominant and dependable products in a traditionally important market, this certainly could become a matter of concern in the coming months. More importantly, considering the total export of top 10 Bangladeshi RMG products[25] where its major strength lies – contributing around 60 per cent of Bangladesh's RMG export to the US – global import by the US increased only by 0.2 per cent. The corresponding growth figure for import from Bangladesh was 8.4 per cent. Considering reduction in demand for these items in the US market, Bangladeshi exporters may need to diversify their products within the RMG sector in the US market.

[24]While export of Bangladesh increased by a mere 2.6 per cent, higher growth rates were attained by her major competitors in the US market such as Cambodia (9.3 per cent), Vietnam (8.9 per cent), Nicaragua (35 per cent), Indonesia (7.6 per cent), Sri Lanka (16.6 per cent) and Mexico (7.5 per cent). However, exports from China, increased by only 1.2 per cent, and India decreased by (-) 2.8 per cent.

[25]These products include seven woven and three knit items. The products are: men's or boys' shirts of cotton, knitted or crocheted (HS 610510); t-shirts, singlets and other vests, of cotton, knitted or crocheted (HS 610910); jerseys, pullovers, cardigans, waistcoats, knitted or crocheted (HS 611090); men's or boys' jackets and blazers of synthetic fibres (HS 620333); men's or boys' bib & brace trousers, breeches, shorts, of cotton (HS 620342); men's or boys' bib & brace trousers, breeches & shorts of synthetic fibres (HS 620343); men's or boys' bib & brace trousers, breeches & shorts of other textiles, nes (HS 620349); women's or girls' trousers, breeches, etc. of cotton (HS 620462); men's or boys' shirts of cotton (HS 620520); and men's or boy's shirts of other textiles, (exl. wool, cotton, manmade fibre) (HS 620590).

Table 17

Growth Rates of RMG Products Export to US in FY2011-12 (July-March)

(in Per cent)

Origin	RMG	Knit	Woven	Top 10 RMG Products
Bangladesh	**2.6**	**-10.8**	**7.5**	**8.4**
Cambodia	9.3	13.8	-0.7	-7.5
China	1.2	3.9	-1.7	-5.3
Guatemala	7.8	7.2	11.3	-4.2
India	-2.8	-9.7	3.1	-9.1
Indonesia	7.6	9.8	4.8	-0.1
Italy	18.3	20.2	17.1	6.5
Mexico	7.5	-0.1	11.8	7.5
Nicaragua	35.0	39.0	25.5	37.0
Sri Lanka	16.6	28.3	7.2	2.1
Thailand	-14.7	-16.8	-11.1	-22.0
Vietnam	8.9	9.6	7.9	0.8
World	**3.7**	**3.9**	**3.5**	**0.2**

Source: Estimated from the United States International Trade Commission (USITC) data.

Third, since January 2012 export earnings from the EU started to decline. One may recall, export earnings from the EU-27 withstood the Eurozone crisis until December, thanks to the new rules of origin (RoO) under the EU-GSP (Generalized System of Preferences) scheme. Exports to the EU-27 countries during January-April declined by (-) 1.2 per cent (Table 18). Particularly, during March-April export of knit garment to the EU declined by (-) 19.1 per cent. It implies that crisis in knit garment export is no longer limited to the US market.

Table 18

Growth Rates of Export to the EU in FY2011-12 (July-April)

(in Per cent)

Destination	FY12 (Jul-Dec)	FY12 (Jan-Apr)	FY12 (Jul-Apr)
EU	19.7	-1.2	10.5
Germany	24.1	0.8	13.5
UK	26.8	13.7	20.9
France	4.2	-21.7	-7.0
Spain	34.9	23.0	30.0
Italy	33.9	-0.1	18.6
Other	9.7	-10.8	0.9

Source: Estimated from the Export Promotion Bureau (EPB) data.

Meanwhile, export earnings from non-traditional markets of Bangladesh (i.e. other than US, EU and Canada) increased by 14.8 per cent during the July-April period of FY2011-12 (Table 19). Exports to Japan increased by 47.3 per cent, India by 7 per cent, Australia by 38.4 per cent and China by 30.2 per cent. This is certainly a positive development in terms of export market diversification for Bangladesh. But the combined share of these markets is too small to uphold the country's export growth. Moreover, slowdown in private investment may also hamper the export-oriented industries in the coming months. The apathetic global outlook coupled with the possibility of prolonged crisis in Eurozone and slower recovery of the US economy, garment exports growth will continue to face major challenge.

Table 19

Growth Rates of Export in Traditional and Non-Traditional Markets

(in Per cent)

Destination	FY12 (Jul-Apr)
World	8.4
Traditional Market*	6.7
Non-Traditional Market	14.8
Japan	47.3
India	7.0
China	30.2
Australia	38.4

Source: Estimated from the Export Promotion Bureau (EPB) data.
Note: *includes US, EU and Canada.

2.4.2 Import Payments: Demand for Petroleum Holds the Key

Throughout FY2011-12, higher import growth counteracted the weak export performance and robust remittance inflow, and put a significant pressure on the balance of payments position. During July-March FY2011-12, import registered a 12 per cent growth. Growth of import payments in the current fiscal year was primarily driven by the higher demand for imported petroleum as about one-third of the incremental import payments was on account of these products. Import of petroleum products registered 18.5 per cent growth in July-March of FY2011-12. In contrast, import payments for other commodities registered only 8.5 per cent growth. Regrettably import payments for capital machinery declined by (-) 6.1 per cent during the same period (Table 20) – indicating stagnation in investment situation in FY2011-12 (see Section 3 for details).

Table 20

Growth of Import Payments

(in Per cent)

Item	FY12 (Jul-Dec)	FY12 (Jan-Mar)	FY12 (Jul-Mar)
Total	**16.9**	**2.0**	**12.0**
Petroleum	53.5	39.2	18.5
Crude petroleum	8.1	90.3	34.4
Petroleum and other liquids (POL)	69.4	3.2	40.5
Other than Petroleum	12.9	-0.7	8.5
Foodgrains	-30.9	-69.1	-46.8
Rice	-8.2	-92.4	-49.6
Wheat	-44.6	-45.0	-44.7
Edible oil	34.9	168.2	69.9
Sugar	89.4	161.1	117.1
Chemicals	-0.4	-6.8	-2.7
Fertiliser	32.8	10.3	24.4
Plastics and rubber articles thereof	5.4	10.1	7.1
Raw cotton	-29.1	-40.6	-33.8
Yarn	37.4	-16.6	16.3
Textile and articles thereof	20.0	11.7	17.0
Iron, steel and other base metals	8.1	26.5	14.5
Capital goods	25.8	-3.0	15.8
Capital machinery	1.4	-20.0	-6.1
Other machineries	38.7	6.0	27.3

Source: Calculated from the Bangladesh Bank data.

However, the growth of import payments started to decline in recent months. During the third quarter of the current fiscal year, import payments increased by only 2 per cent. Indeed, import payments other than those for petroleum products declined by (-) 0.7 per cent. Refined petroleum import growth also increased by only 3.2 per cent. Slowdown in import payments can also be linked to decline in export. Uddin (2009) showed that in both short and long-terms, export from Bangladesh significantly determines her import growth.[26] Nevertheless, one can anticipate that the pressure arising from import payments during the rest of FY2011-12 and FY2012-13 will be largely determined by the demand for imported petroleum products. Indeed, in the backdrop of import pressure (along with subsidy requirement) the government is not fully utilising the capacity of liquid fuel-run quick RPPs (see Section 3 for details). It may be anticipated that the high growth of petroleum import will be maintained, as growth of letter of credit (L/C) opening for petroleum import stood at 75.9 per cent during the first three quarters of FY2011-12.

2.4.3 Remittances Inflow: Falling Short of Target despite Impressive Overseas Migration

Total remittance earnings during July-April, FY2011-12 stood at USD 10.6 billion registering a growth of 10.3 per cent. If the purchasing power of remittances adjusted for the domestic inflation, remittance growth would stand at 13 per cent for the same period. High level of petroleum oil price, and hence, renewed economic vibrancy in the Middle East countries along with depreciation of BDT against currencies of major migrant destination countries may have helped to attain this growth.[27] Such growth in remittance inflow was also accompanied by an upturn in the number of Bangladeshi workers going abroad. The number of total migrant workers going abroad during the first ten months of FY2011-12 (July-April) was 566,000, which was about 65.6 per cent higher than that of the corresponding period of FY2010-11.[28]

Although outlook for growth of remittance flows to South Asia is only about 7.4 per cent (Ratha 2012), the trends indicate that remittance inflow to Bangladesh may surpass her regional average. With the existing rate of remittance inflow, inward remittances will need to register an average growth of 18.3 per cent for the remaining two months of FY2011-12 to achieve the target of USD 12.7 billion. Hence, the final figure for remittance inflow in FY2011-12 may fall short of the target and remain close to USD 12.5 billion.

2.4.4 Foreign Aid: Inadequate Improvement

Slowdown in foreign aid inflow in FY2011-12 has hurt both fiscal balance and balance of payments. There has been some improvement in foreign aid inflow during the recent months. Gross foreign aid during the first ten months of FY2011-12 stood higher at USD 1.6 billion compared to the corresponding period of the last fiscal year (USD 1.4 billion). However, the disbursement is still low compared to the figure of FY2009-10 (USD 2 billion). Net foreign aid inflow during July-April, FY2011-12 (USD 1 billion) was USD 194 million higher than the disbursement of July-April, FY2010-11, but USD 459 million less than the corresponding period of FY2009-10. The present volume of foreign aid is also inadequate to restore stability in the balance of payments. As it stands, it is now highly unlikely that the budget target of USD

[26]According to Uddin (2009), there exists long-run bidirectional causality between export and import, and in short-run unidirectional causality exists from import to export. Moreover, bidirectional short-run and long-run causality exist between 'export-GDP ratio' and 'import-GDP ratio'.

[27]Regrettably, cost of sending remittances to Bangladesh has increased in the first quarter of 2012 compared to that of 2011 by 8.6 per cent for sending from Saudi Arab, and by 0.9 per cent from Singapore.

[28]Significant growth was posted for almost all major destination countries except for Bahrain and Malaysia. Libya is regaining as one of the major destinations with 7,500 workers migrating during the first four months of calendar year 2012. Recently Malaysia agreed to recruit workers from Bangladesh under government-to-government (G2G) arrangement in order to reduce the cost of migration. According to anecdotal information, under this arrangement cost of sending a worker to Malaysia would not be more than Tk. 50,000, which could be limited to Tk. 35,000 if any employer bears the air transport cost.

3.3 billion for FY2011-12 will be achieved. To attain maximum potential support from this component of the balance of payments, there is a need for a renewed effort to disburse and utilise the foreign aid growing in the pipeline.

2.4.5 Balance of Payments: Concerns Remain

The pressure on balance of payments sustained throughout FY2011-12. Deficit in trade balance widened rapidly as import payments increased at a faster rate compared to export earnings. Trade balance at the end of the fiscal year may go beyond the projected level. As remittances inflow may not achieve its target, current account balance may weaken further during the last quarter.

As a welcome development, foreign aid inflow gained some momentum in recent months. Indeed, at the end of the fiscal year, at the margin, government's ability to utilise its foreign resources awaiting in the pipeline will determine the final balance of payments figure.

Overall deficit remained at a better position ((-) USD 419 million) compared to the matching period of last fiscal (Table 21). The last quarter will also see receipt of the first tranche of IMF-ECF support, i.e. USD 141 million. It appears that for this fiscal year, balance of payments, notwithstanding being under continued pressure, has survived any major debacle.

Table 21

Balance of Payments

(Million USD)

Item	**FY11**	**FY12 (MPS Projection)**	**FY11 (Jul-Mar)**	**FY12 (Jul-Mar)**
Trade balance	-7328	-9034	-5826	-6586
Workers' remittances	11650	12815	8611	9532
Current Account Balance	995	-243	586	456
Capital account	600	300	463	401
Financial account	-1584	-1443	-1761	-1222
Foreign direct investment	768	850	571	551
MLT loans	1051	850	524	573
Errors and omissions	*-936*	*560*	*183*	*-54*
Overall Balance	**-925**	**-826**	**-529**	**-419**

Source: Compiled from the Bangladesh Bank data.

The government took a number of steps to maintain the balance of payments stability including IMF-ECF support which came against a long list of structural benchmarks. It is, however, unclear whether the government will be able to receive all the planned disbursements from IMF by fulfilling all the conditionalities.[29] The next disbursement is due in November 2012. Before that government is required to finalise its plan regarding implementation of an automatic adjustment mechanism for retail petroleum prices to ensure full pass-through of international prices. Given the political reality it may be difficult for the government to fully meet this condition; and hence, the government may have to look for alternative sources. One possible source could be the recent Indian offer of Balance of Payments Support for the SAARC (South Asian Association of Regional Cooperation) Members. Under this scheme Bangladesh may get a maximum amount of USD 400 million from this 'SAARC Swap Facility'.[30] Another offer relates to the

[29]One can recall that in September 2007, the IMF had set 20 conditions under a package of reforms for the government under a new Poverty Reduction Growth Facilities (PRGF) arrangement. However, Bangladesh government decided not to go for negotiation of the seventh and last installment of USD 123 million.

[30]Interest rate for this loan is LIBOR (for three months) plus 200 basis points, i.e. around 2.5 per cent.

Turkish government. In the present context, one may reiterate that the government is far better off by utilising the existing resources in the form of foreign aid awaiting in the pipeline.

2.4.6 Exchange Rate: Stabilised for the Moment

The first half of FY2011-12 experienced depreciation of BDT originating from a growing pressure on balance of payments. Since then the BDT value against the United States Dollar (USD) has somewhat stabilised. Exchange rate management has become even more difficult due to the volatility in the international foreign exchange markets. As of end January 2012, BDT depreciated against all major currencies, i.e. USD, Euro, British Pound (GBP) and Chinese Yuan (CNY), except for the Indian Rupee (INR).[31]

During the last ten months (July and April) BDT lost its value vis-à-vis USD by 10.7 per cent, Euro by 1.4 per cent, GBP by 9.2 per cent, and CNY by 17 per cent. In contrast, BDT appreciated against INR by 4.2 per cent.[32] During this period, Bangladesh also managed to withstand from any further depletion of foreign exchange reserve. Till end of April, Bangladesh Bank managed to maintain a foreign exchange reserve to the tune of around USD 10 billion (equivalent to three months of import payments). At present, there is no room for the Bangladesh Bank to use foreign exchange reserves for market intervention. The movements of balance of payment related correlates suggest a possible depreciation in coming months. Indeed, developments in the foreign exchange market will move along with the balance of payments situation.

3. INVESTMENT SITUATION

3.1 Introduction: Widening the Gap

Acceleration of investment has been identified as one of the major strategies for attaining targeted economic growth during the SFYP period (FY2010-11 to FY2014-15). So far the performance is unsatisfactory. Arguably, slow growth of investment, rising inefficiency of capital, unutilised productive capacity and adversities in business enabling environment would together constitute the major challenge for achieving the targeted level of GDP growth in the rest of the period of the SFYP.

3.2 Growth-Investment Linkage: Debates over Public and Private Investment

Growth-investment linkage is determined by the respective role played by public and private investments. Since public and private investments have differential impact on growth, it is not only the total investment that matters, but how this investment splits between public and private components, is also important (Khan and Kumar 1997). Public and private investment in developing countries often face the debates in terms of 'complementary' vs. 'competitive' relationship; nature and extent of 'crowd out' and 'crowd in' effects of public investment; and its 'short-term' vs. 'long-term' effects on private investment (Krueger and Orsmond 1990; Greene and Villanueva 1991; Khan and Kumar 1997). Moreover, what should be the desired level of public investment is also a debated issue in the classical and Keynesian schools of thoughts (Spencer and Yohe 1970). The level of public and private investments (as percentage of GDP) varies among developing countries depending upon, among others, their demand, availability of resources and relative level of indivisibilities and associated risks for provisioning the capital. Bangladesh's aggregate investment for FY2011-12 has been estimated to be 25.4 per cent of GDP of which 6.3 per cent

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[31]During the first half of the fiscal (between end of June to end of January) BDT lost its value vis-à-vis USD by 13.8 per cent, Euro by 3.2 per cent, GBP by 11.6 per cent, and CNY by 16.9 per cent. In contrast, between the end of June to end of December, BDT appreciated against INR by 7.2 per cent.

[32]In May 2012, INR experienced a sharp decline in its value against USD (by 6.2 per cent). On one hand, it will help Bangladeshi consumers as India is the second largest import source for Bangladesh after China. On the other hand, Bangladeshi exporters will face more competitions from their Indian counterparts.

(about 25 per cent of total) is public and the rest 19.1 per cent (75 per cent of total) is private investment. Although the attained level of investment in Bangladesh is higher than that of the average of low-income countries, but it is lower than that of the middle-income countries, particularly in case of public investment (Figure 9).

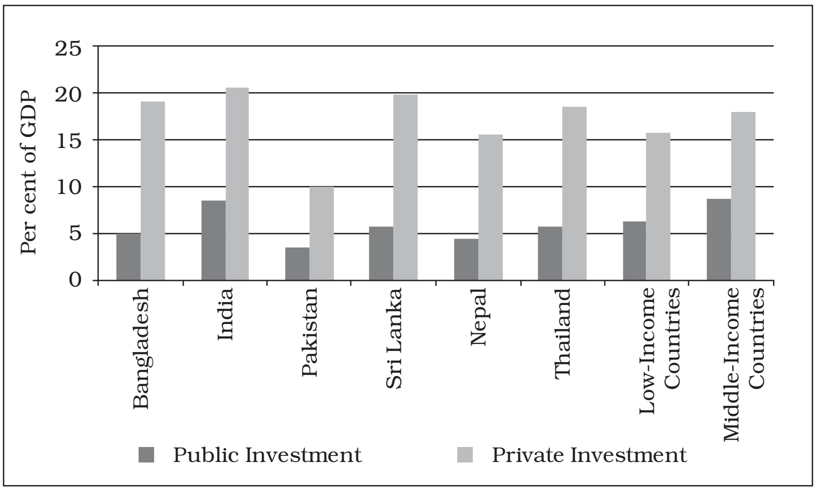


Figure 9

Investment in Selected Countries: 2010

Source: Based on the World Development Indicators (WDI), 2012.

This section seeks to address the following questions: a) Is aggregate investment in Bangladesh stagnating? If so, is this because of slowing down of private investment? b) Is the current trend in public investment failing to 'crowd in' private investment significantly? What are the major challenges for public investment to ensure significant 'crowd in' effect? c) Is there any liquidity crisis in the commercial banks from the perspective of investment financing? Is public investment in recent years 'crowding out' private investment? What are the major challenges in the financing pattern of public investment? d) Are there other factors that explain the slowing down of aggregate investment particularly private investment? What are those factors? How and to what extent are those factors affecting the investment?

3.3 Public Investment

The bulk of the public investment in Bangladesh takes place through the ADP, but it is also related with a number of non-ADP expenditures. The amount allocated in the RADP (at current market price) has experienced a rise of 26 per cent between FY2008-09 and FY2011-12. Once adjusted for price inflation, the growth of public investment during the above mentioned period was found to be not so significant (6.3 per cent). In fact, the RADP size at inflation adjusted value has actually shrunk between the period of FY2005-06 and FY2008-09. Moreover, actual expenditures under RADP had been always lower than the allocations. Thus the size of ADP in terms of actual expenditure did not increase notwithstanding the claims by the policymakers (Table 22).

Table 22

Trends in Allocation and Expenditure for Public Investment in Different Years

(Crore Tk.)

Component	FY08	FY09	FY10	FY11	FY12
Total RADP	22500.0	23000.0	28500.0	35130.0	41000.0
RADP after inflationary adjustment (base 1995-96)	11625.5	11141.8	12865.1	14575.6	15414.1*
Actual expenditure	18455.0	19701.0	25917.0	-	-
Difference between RADP and actual expenditure	4045.0	3299.0	2583.0	-	-

Source: Estimated based on the Ministry of Finance (MoF) data.
Note: *Estimated based on the Consumer Price Index (CPI) of April 2012.

3.3.1 Financing Public Investment

Accessing finance is a matter of major concern for the government of the low-income economies as they usually operate with deficit budget. Over the years, financing of RADP from domestic sources has increased from 56 per cent in FY2008-09 to 63 per cent in FY2011-12 (Table 23). Increasing use of local sources for financing ADP is often considered as a positive development from the perspective of reducing the dependence on foreign sources. At the same time, since borrowed local resources (in the absence of adequate revenue surplus) is usually found to be costlier compared to that of foreign aid, return accrued through the investments from former source has to be sufficiently higher in order to get positive effect on GDP growth.

Table 23

Financing of RADP

(Crore Tk.)

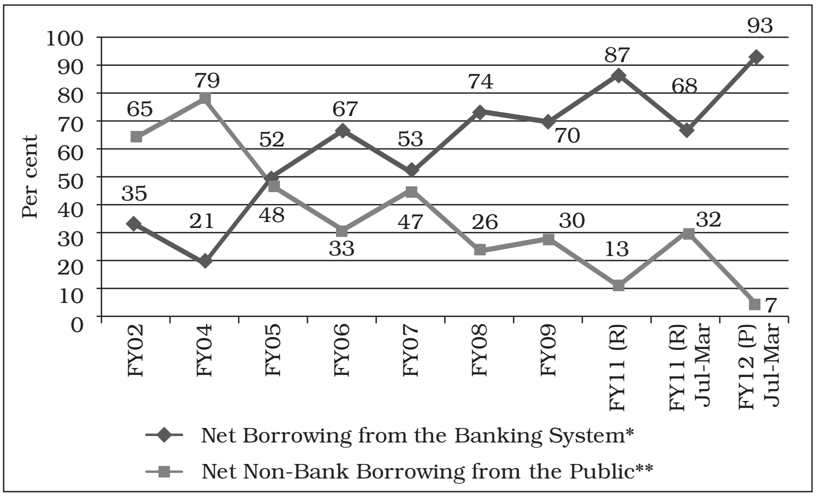
RADP	**FY07**	**FY08**	**FY09**	**FY10**	**FY11**	**FY12**
Domestic financing	11480	7973	12800	17200	23950	26000
Foreign financing	10120	14527	10200	11300	11930	15000
Share (%)						
Domestic financing	53	35	56	60	67	63
Foreign financing	47	65	44	40	33	37

Source: Implementation Monitoring and Evaluation Division (IMED) data.

Local financing of public investment (excluding revenue surplus) comprises of government borrowings from central bank, commercial banks and non-bank sources, and these borrowings have differential impact on growth and investment in short, medium and long-terms. Local financing of public investment through borrowing from the banking system has been increasing (Figure 10). During FY2007-08, the share of borrowing from the banking system was 74 per cent of total local finance, this increased to 93 per cent in FY2011-12 (July-March). Usually borrowing from commercial banks is preferred over borrowing from the central bank with a view to put less inflationary pressure on the economy. Whether and to what extent those public borrowings from the banking system are causing 'crowd out' effect in private investment is an issue for discussion.

Figure 10

Share of Banking and Non-Banking Sectors in Government Borrowing



Source: Estimated based on the Bangladesh Bank data.
Note: *Excludes interest.
**Excludes saving certificates held by the banks and includes T-bills and bonds held by the non-bank financial institutions; T-bills and bonds have been taken at face value.

Domestic credit growth in private and public sectors partly explain the nature and trend of overall investment. After embarking on the contractionary monetary policy by the Bangladesh Bank, overall growth of domestic credit has decelerated. Major share of domestic credit is supplied to the private sector (more than 75 per cent), which has declined over the years – from the peak of 79.6 per cent in June 2010 to 77.8 per cent in January 2012 (Table 24).[33] Domestic credit supply to the public sector, on the other hand, has increased. If commercial banks do not possess sufficient amount of 'excess liquidity', this rise in credit supply to the public sector may have a 'crowd out' effect on private investment. Excess liquidity in banks has significantly reduced from as high as 45 per cent of total liquid assets in June, FY2008-09 to 30.7 per cent in January, FY2011-12. A deceleration of 'excess liquidity' in the banking channel with shortages of credit supply to the private sector may partly indicate the 'crowd out' effect of public investment. But at the same time, all kinds of financial assets available to the bank in the form of 'excess liquidity' are not fully allowable for use as commercial credit. The issue needs further explanation.

Table 24

Distribution of Domestic Credit

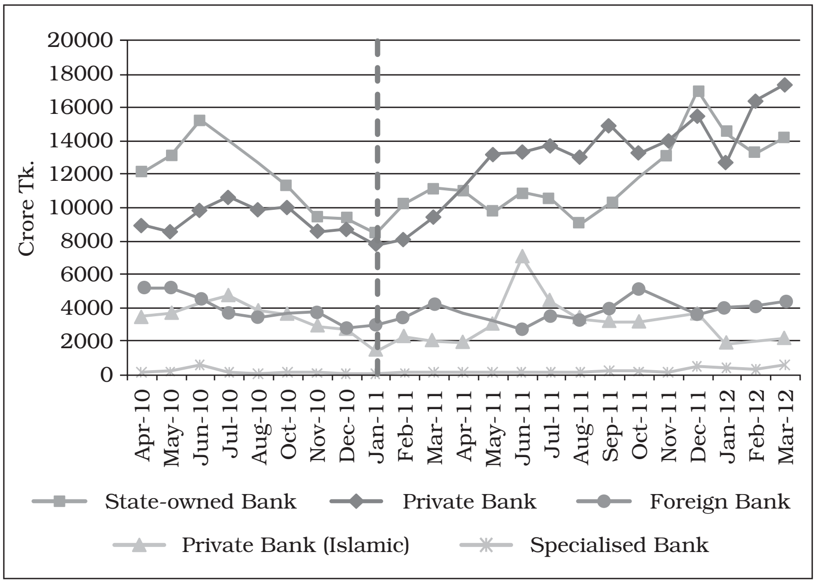
Component	June 2009	June 2010	June 2011 (R)	January 2012 (P)
Domestic Credit (Crore Tk.)	288552.3	340213.7	433525.9	481798.6
Share (%)				
Government	20.2	16.0	16.9	18.5
Other public sector	4.3	4.4	4.5	3.7
Private sector	75.5	79.6	78.6	77.8
Changes (over the previous period) (%)				
Total		17.9	27.4	23.6
Government		-6.5	35.0	62.4
Other public sector		21.1	28.7	-9.8
Private sector		24.2	25.8	18.9
Excess Liquidity				
Total (Crore Tk.)	34762.1	34498.7	34071.2	33337.2
% of total liquid assets	45.0	39.6	33.9	30.7

Source: Estimated based on the Bangladesh Bank data.

A number of other issues related to the financial market may be partly responsible for shortages of credit flow to the private sector. Excess liquidity in the scheduled banks has experienced fluctuations during 2009-2012, and there was a dip in January 2011, when share of 'excess liquidity' has reduced to as low as 25 per cent of total liquid assets (Figure 11). Perhaps this dip was linked with the collapse of the capital market in December 2010, which caused a significant decline of share prices affecting the money flow in the commercial banks.[34] Therefore, shortages of fund in the banking system in recent years is not only associated with public borrowing, but with other factors including low level of money flow to banks due to the collapse of the capital market. Moreover, rise in excess liquidity in recent period (though at a low pace) at a time of high government borrowing from the commercial banks further undermines the 'crowd out' effect argument.

[33]Domestic credit supply as of January 2012 was Tk. 481,800 crore.
[34]Overexposure of commercial banks in the capital market was partly responsible for the shortages of their loanable funds.

Figure 11
Excess Liquidity



Source: Estimated based on the Bangladesh Bank data.

3.3.2 Examining the 'Crowd Out' Effect of Public Borrowing

An analysis of long-term data reveals that public borrowing may not have significant 'crowd out' effect on private investment in Bangladesh. Majumder (2007) analysed public borrowing and private investment for the period of 1976 to 2006. The unit root test and Johansen co-integration test show that public borrowing did not have crowding out effect as long as excess liquidity prevails in the financial system. Similar exercise has been carried out by CPD using the data from FY1980-81 to FY2010-11.[35] Using a Vector Error Correction model, the investment function can be represented in the following equation[36]:

$$LRPI = -9.08 + 1.33.LRGDP^{***} - 0.14.LRPC - 0.06.RIR$$

The result suggests that there is a positive and significant relationship between private investment and GDP in Bangladesh. While the coefficient for public sector credit is negative, but it is not statistically significant – suggesting that the null hypothesis of public sector credit crowding out private investment cannot be rejected.[37] The result suggests that there is a positive and significant relationship between private investment and GDP in Bangladesh. While Majumder (2007) found a positive and significant result in case of the relationship of public borrowing with that of private investment; CPD (2012) on the other hand, found a negative but insignificant result. CPD's analysis therefore implies a 'crowding out' effect of public borrowing, but it is not significant. Perhaps differences in the coverage of data between the two studies are a possible reason for such different results. CPD's analysis has covered the data of the latest available years (2007-2010) when public borrowing has significantly increased, which might be reflected in the result. In other words, a persistent pressure of public borrowing in the future may cause negative and significant impact over private investment, causing 'crowding out' effect of public borrowing.

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[35]We have tested the hypothesis of public sector credit *crowding out* private sector credit in Bangladesh. The dependent variable used is private investment, while the independent variables include constant GDP, real public borrowing (transformed to real terms using GDP deflator), and weighted average of interest rates on advances charged by schedule banks adjusted for by the rate of inflation. All the variables except interest rate have been transformed into log-level.

[36]All the variables were found to be non-stationary, thus their first differences were used (which were found be stationary). Johansen co-integration test for estimating long-run relationship suggest that there are at least two co-integrating vectors between the dependent variable (LRPI) and the three independent variables-log of constant GDP (LRGDP), log of real public credit (LRPC) and real interest rate (RIR).

[37]Although the coefficient of real interest rate is negative, it is also not statistically significant.

3.3.3 Foreign Financing

Government usually tries to get the soft loan from the development partners for public investment. Although share of foreign finance has reduced in recent years, it continues to play a critically important role in case of physical infrastructure, social sector and human resource development in Bangladesh. All these investments have direct impact on private investment. It appears that government is not utilising foreign funds which are available in the pipeline, and the amount is increasing every year (Table 25). Enhancement of the country's development administration capacity in using the available foreign funds remains a major challenge.

Table 25

Foreign Aid in the Pipeline

(Billion USD)

Component	FY08	FY09	FY10	FY11	FY12
Opening Pipeline	7.29	8.68	8.86	9.43	13.86
Commitment	2.84	2.44	2.98	5.97	6.00 (P)
Disbursement	2.06	1.88	2.22	1.77	2.18 (P)

Source: The Daily Star (2012).
Note: P denotes projection.

3.3.4 'Complementary' Role of Public Investment

Given the underdeveloped status of physical and infrastructural facilities, public investment in Bangladesh is mainly focused on rural development, physical infrastructure and human resource development (Table 26). Over the years, there was not much change observed in the composition of the public investment. Taking the medium and long-term development priorities, several sectors got special priority in the government's public finance programme. Between FY2009-10 and FY2011-12, public investment has been consistently increased in infrastructure development, particularly in the power and transport sectors, and also in the rural development sector. During FY2011-12 the combined share of these three sectors in the RADP was 45 per cent. These investments are considered as 'complementary' in nature for private investment (Khan and Kumar 1997); admittedly, the level of complementarity depends on the quality of these investments.

Table 26

Sector-specific Allocation in RADP

Sector	FY08	FY09	FY10	FY11	FY12
Total RADP (Crore Tk.)	22500.0	23000.0	28500.0	35130.0	41000.0
Share (Top 10 sectors) (%)					
Agriculture	6.0	6.1	6.2	6.6	6.2
Rural development and rural institutions	14.1	15.6	14.1	13.0	12.3
Water resources	3.9	3.8	4.2	3.5	3.5
Industries	1.3	2.0	1.7	1.2	2.4
Power	13.8	11.6	9.3	14.3	17.6
Oil, gas and natural resources	2.0	0.9	3.8	3.1	1.8
Transport	11.5	11.0	13.3	14.9	15.1
Physical planning, water supply and housing	7.2	10.8	10.4	9.5	10.2
Education and Religious Affairs	13.6	14.1	15.7	14.4	11.8
Health, Nutrition, Population and Family	11.1	11.9	10.6	9.0	8.3
Public Administration	4.2	3.0	2.9	3.1	2.4

Source: Estimated based on the Ministry of Finance (MoF) data.

The 'complementary' role of public investment needs to be examined not only in terms of the volume of investment, but in terms of quality of these investments which includes appropriateness, effectiveness and timeliness. In power, oil, gas, natural resources and transport sectors, public investment is likely to have direct and immediate impact on private investment. Between FY2008-09 to FY2011-12, government increased allocations for these sectors; as a result their share in the RADP increased from 22.5 per cent in FY2008-09 to 34.5 per cent in FY2011-12. However, a number of qualitative issues related to these investments raised doubt about their extent of 'crowding in' effects. After a substantial amount of investment in the power sector (public and private) during FY2008-09 to FY2011-12, overall power generation capacity has increased by 3,380 mega watt (MW); but effective supply of electricity has increased only by about 50 per cent of the newly installed capacity. Investment in short-term, diesel-operated quick rental and peaking power plants caused huge import of diesel supplied at subsidised price to the power plants. This has created fiscal burden as well as put pressure on the balance of payments. To adjust these problems, government measures (including low level of supply of diesel to power plants, rise in diesel price, and further rationing of electricity supply) are found to be ineffective. Even the follow-up adjustment measures which are under consideration (such as adjustment of petroleum price at international market level in order to reduce the subsidy for diesel import) appear to be counter-productive. Thus, public investment in the power sector till date is likely to have very limited 'crowd in' effect to the private investment.

Investment in the transport sector during the last three years did not make significant improvement in the communication system. According to the Roads and Highways Department (ROHD), the average Roughness Index of national, regional and district level highways have significantly increased in FY2009-10. Investment in agriculture and rural development accounted for the largest share of RADP in recent years (18.5 per cent of RADP in FY2011-12); besides, agriculture subsidy provided under non-development expenditure is accounted for a large share in last several years. These investments have contributed to the supply of agricultural inputs at low price, which perhaps 'crowded in' private investment in agricultural production to some extent. For example, acreage of rice cultivation has increased in last three years – from 27,852,000 acre in FY2008-09 to 28,882,000 in FY2010-11. Besides, favourable market price for agricultural products particularly that of rice (e.g. from USD 254 in July 2009 to as high as USD 459 in February 2011, and then slowed down to USD 304 in March 2012) has also contributed to this rise in investment.[38]

Expenditure on industrial sector although directly linked with projects which have 'complementary' effect on the private investment, but have limited share in overall investment (2 per cent in FY2011-12). More importantly, the projects under those investments were not completed on time (only 3 per cent of total RADP allocation was completed in July-April, FY2011-12).[39] Low level of project implementation in general is a major weakness of public expenditure management, and in FY2011-12, level of implementation reached a new low (55 per cent in the first ten months). Slow implementation of public sector projects raises question about the viability and effectiveness of such public investment.[40]

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[38]For details, please see the *Special Note on Crop Production and Food Security* at the end of this report.

[39]Major projects currently implemented under the Ministry of Industries are: Leather Industrial Estate, Active Pharmaceutical Ingredient (API) Park, and BSCIC Industrial Estate in Sirajganj.

[40]The ADP expenditure in the current year (July-April, FY2011-12) has experienced the lowest level of implementation over the three year period under this government (55 per cent of total RADP vis-à-vis 58 per cent in FY2010-11, and 59 per cent in FY2009-10). This happened both in case of locally funded as well as project funded activities. A large number of ministries performed below the average level of implementation (55 per cent) – out of 54 ministries, division and departments, 32 have performed below the average. Even with the highest level of implementation (36 per cent recorded in last two months in FY2009-10) about Tk. 3,700 crore of the RADP would remain unspent (9 per cent for FY2011-12).

3.3.5 Examining the 'Crowd in' Effect of Public Investment: VAR Model and Sub-sequent Granger-Causality Test

To test the Granger-causality between public investment, GDP and private investment, the Vector Autoregressive Model (VAR model) is used. Aschauer (1989) showed that an increase in public investment could lead to higher rate of return for private investment.[41] Data for the RADP, investment and GDP for the period of FY1980-81 to FY2010-11 is used for this analysis. In order to remove the stationarity in data natural logarithm has been taken into consideration. Using the *Information Criterion* the optimum number of lags has been calculated which determines the relative goodness fit of the model.

The following VAR model is used for estimation:

$$lnX_t = \sum_{s=1}^{k} B_s \cdot X_{t-s} + u_t$$

Where, X_t= [*public investment on different sectors*$_t$, *GDP*$_t$/ *private investment*$_t$]

Analysis shows that most of the sectoral public investments have lagged positive effect on GDP (Table 27). Most significant positive causal relationship is found in case of agriculture, transport, physical planning and housing, public administration, health and social welfare. Table 28 presents causality between public and private investment. It is found that public investment has marginal impact on private investment, only significant relationship was found in case of industrial sector with a lagged effect of two years. Thus, the analysis found public investment with marginal 'crowd in' effect on private investment. Majumder (2007) analysed the data for the period of 1976-2006 and found significant crowd in effect of public investment in Bangladesh.

Table 27

Multivariate VAR on GDP (Optimum Lag: 1 Year)

Sector-wise Expenditure	Coefficient	P-Value	H0: Spending on Sector X does not Granger Cause GDP	P-Value
Agriculture	0.1733906	0.000	reject H0	0.000
Industry	0.0085611	0.148	fail to reject H0	0.297
Power	-0.0022255	0.806	reject H0	0.049
Natural resources: oil and gas	-0.0003254	0.457	reject H0	0.002
Scientific and technological research	-0.0156896	0.048	reject H0	0.001
Transport	0.1896090	0.000	reject H0	0.000
Communication	-0.0032583	0.772	reject H0	0.000
Physical planning and housing	-0.2119131	0.000	reject H0	0.000
Education and religion	-0.0634726	0.002	reject H0	0.000
Public administration	-0.0276062	0.000	reject H0	0.000
Health	-0.1185780	0.000	reject H0	0.000
Social welfare, women's affairs and youth development	0.0692395	0.000	reject H0	0.000
Manpower and labour	-0.0004954	0.0731	reject H0	0.000

Source: CPD estimations.

[41] Also see, Blejer and Khan (1984); Ghali (1998); Ghura and Goodwin (2000).

Table 28

Multivariate VAR on Private Investment (Optimum Lag: 2 Years)

Sector-wise Expenditure	Coefficient	P-Value	H0: Spending on Sector X does not Granger Cause Private Investment	P-Value
Agriculture	-0.1212516	0.188	fail to reject H0	0.389
Industry	0.1046276	0.045	reject H0	0.005
Power	0.1336832	0.417	fail to reject H0	0.581
Natural resources: oil and gas	-0.2215423	0.541	fail to reject H0	0.421
Scientific and technological research	-0.0647022	0.510	fail to reject H0	0.786
Transport	0.0218357	0.899	fail to reject H0	0.774
Communication	-0.0491347	0.591	reject H0	0.045
Physical planning and housing	0.0473939	0.805	fail to reject H0	0.508
Education and religion	0.1319379	0.494	fail to reject H0	0.610
Public administration	-0.1368023	0.106	reject H0	0.014
Health	0.2229237	0.115	reject H0	0.048
Social welfare, women's affairs and youth development	-0.0473430	0.499	fail to reject H0	0.060
Manpower and labour	0.0091274	0.153	fail to reject H0	0.304

Source: CPD estimations.

3.4 Private Investment: Is It Slowing Down?

3.4.1 Credit to the Agriculture Sector

Investment in the agriculture sector is examined by assessing the performance of disbursement and recovery of credit in major agricultural sub-sectors (Table 29). Growth of disbursement of agricultural credit showed a mixed trend between FY2008-09 and FY2011-12; more importantly, it has decelerated in July-March, FY2011-12 (6.2 per cent) compared to that of the same period of the previous year (16.6 per cent). Major share of credit which is distributed for cultivation (about 44 per cent of total agricultural credit) has experienced a moderate rise in this period (Table 30).[42] A considerable rise of disbursement of credit was observed in case of purchase of irrigation and agricultural equipments, and livestock development and fisheries sectors. Part of this rise is perhaps associated with rise of cost of inputs/machineries, and partly contributed by significant devaluation of BDT against USD during FY2011-12. Credit distributed for setting up grain storage and marketing has experienced a decline in the same period. A major rise of private investment particularly for rice cultivation is perhaps associated with considerable public investment and favourable market condition (e.g. high retail price at farmer's level).

Table 29

Disbursement and Recovery of Agricultural Credit

(Crore Tk.)

Year	Disbursement		Recovery	
	Total	Change (%)	Total	Change (%)
FY2008	8581	62.1	6004	28.4
FY2009	9284	8.2	8378	39.5
FY2010	11117	19.7	10113	20.7
FY2011	9155	-17.7	9028	-10.7
FY2011 (Jul-Mar)	7543	16.6	7611	28.4
FY2012 (Jul-Mar)	8007	6.2	7738	1.7

Source: Estimated based on the Bangladesh Bank data.

[42]Agricultural credit is distributed mainly for cultivation of different crops (mainly rice), purchase of irrigation equipments, agricultural equipments, livestock and fisheries, and grain storage and marketing.

Table 30

Change in Disbursement of Agricultural Credit during 2011 and 2012 (July-April)

(in Per cent)

Source	Crop Production	Irrigation Equipments	Agricultural Equipments	Livestock	Fisheries	Grain Storage and Marketing	Others	Total
Government Banks	9.6	12.9	-25.2	5.8	-8.2	-3.4	-29.0	-6.8
Foreign and Private Commercial Banks	67.0	158.7	59.4	88.0	54.9	-28.7	21.7	42.7
Total	18.4	129.2	40.1	42.9	16.6	-27.0	-20.0	5.7

Source: Estimated based on the Bangladesh Bank data.

3.4.2 Investment in the Manufacturing Sector

Private investment in the manufacturing sector is examined by analysing distribution of credit to the manufacturing sector, flow of FDI, and investment in the primary capital market.

Disbursement of industrial term loan has slowed down in the current year, after a significant rise in FY2009-10 and FY2010-11 (Table 31). During July-March, FY2011-12 total disbursement was Tk. 25,059 crore which was mere 2.3 per cent higher compared to the same period of the previous year. However, changes in the disbursement of credit would be insignificant if it is adjusted with the ongoing inflation rate and currency devaluation (i.e. BDT against USD). Credit to the small and medium enterprise (SME) sector is mainly comprised of trade credit (62 per cent). In January-March period, disbursement of total SME credit increased by 17 per cent (Table 32).

Table 31

Industrial Term Loan

Year	Amount (Crore Tk.)		Change (%)	
	Disbursement	Recovery	Disbursement	Recovery
FY2009	19972.69	16302.48		
FY2010 (R)	24487.71	19304.98	22.6	18.4
FY2011 (P)	32163.20	25015.89	31.3	29.6
FY2011 (Jul-Mar)	24487.70	19304.90	30.1	46.2
FY2012 (Jul-Mar)	25059.90	22347.90	2.3	15.8

Source: Estimated based on the Bangladesh Bank data.

Table 32

Disbursement of SME Credit

Period	Disbursement (Crore Tk.)				Change (%)			
	Services	Trade	Manufacturing	Total	Services	Trade	Manufacturing	Total
January-March 2010	736.1	7145.6	3124.9	11006.6				
January-March 2011	681.9	8137.8	3383.6	12203.3	-7.4	13.9	8.3	10.9
January-March 2012	826.9	8927.8	4525.9	14280.6	21.3	9.7	33.8	17.0

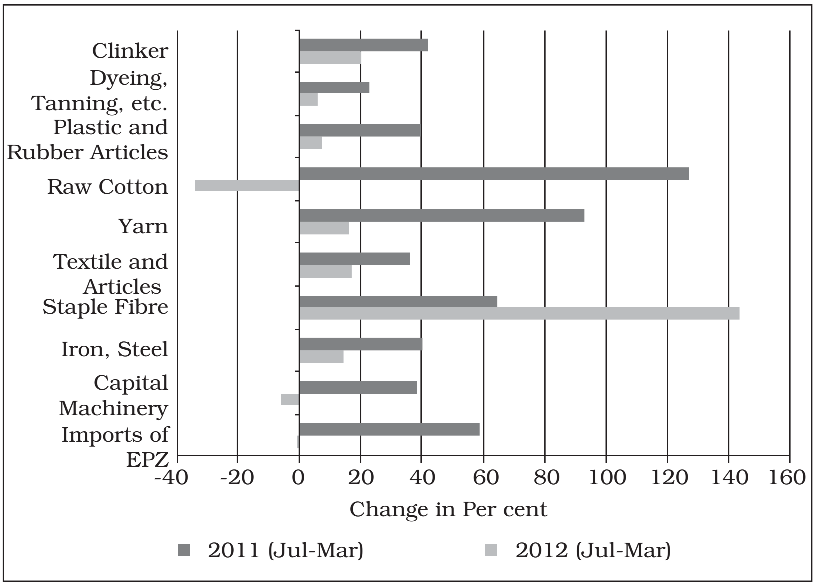
Source: Estimated based on the Bangladesh Bank data.

A significant growth of the manufacturing sector (9.8 per cent in FY2011-12 against 9.5 per cent in FY2010-11), as reported along with provisional estimates of GDP, in the backdrop of current slowdown of private investment has raised some confusion. On one hand, growth of the manufacturing sector could be explained as lagged effect of high growth of investment in the previous years. On the other hand, low growth of private investment, falling capital machineries import, and lack of electricity and gas supply have raised doubt about the reported high growth of this sector. If the private investment consistently slows down, manufacturing sector performance would experience lagged effect in the coming years.

Low level of industrial credit disbursement, particularly to the manufacturing sector is reflected in slow growth of import of raw materials, intermediate inputs and industrial machineries (Figure 12). It seems that slow growth in import will continue at least for some time in the coming months as growth of L/C opening for import of industrial raw materials, capital machinery, textile machinery and other machineries is found to be lower during July-January, FY2011-12 period compared to that in FY2010-11, except for petroleum and other machineries (Table 33). The exceptionally high rise in import of staple fibre in this year against the slowed down domestic production of yarn and textiles needs close examination in the coming years in order to understand the possible impact on local textile manufacturers.

Figure 12

Import of Major Raw Materials for Industrial Production



Source: Estimated based on the Bangladesh Bank data.

Table 33

Changes in L/C Opening in Different Years (July-January)

(in Per cent)

Item	2010 over 2009	2011 over 2010	2011 over 2010
Industrial raw materials	5.5	69.6	-9.3
Capital machinery	38.6	82.4	-33.2
Textile machinery	35.7	31.1	-28.3
Machinery for miscellaneous industry	21.8	55.5	10.8
Petroleum and petro products	5.4	5.0	93.3

Source: Estimated based on the Bangladesh Bank data.

3.4.3 Foreign Direct Investment (FDI)

Since FY2008-09, there was no major change discerned in inward flow of FDI (Table 34) – it was stalled at below USD 1 billion when other competing countries received several times higher (for example, India: USD 24.6 billion; Pakistan: USD 2.02 billion; China: USD 105.7 billion; Vietnam: USD 8.2 billion and Indonesia: USD 13.3 billion in 2010). There is a major shift in the composition of FDI stock of Bangladesh – shifting from using all kinds of FDI, i.e. equity capital, reinvested earnings and intra-company borrowings towards only one kind, i.e. equity capital (Figure 13). While this reflects pre-dominance of new investment in the Bangladesh's FDI basket, at the same time it also shows lack of reinvestment interest of existing foreign companies. This was reflected in huge amount of outward transfer of profit, dividend and royalties and other incomes of foreign-owned companies in recent years (i.e. USD 565 million, USD 553 million and USD 593 million in July-March period for FY2009-10, FY2010-11 and FY2011-12 respectively). Compared to the corresponding period of the previous year, FDI flow was coming down, during July-January, FY2011-12 registering a negative growth of (-) 3.5 per cent. If the outward transfers are deducted, net inward FDI flow will be negative ((-) USD 51 million). On the other hand, investment in EPZ is on the rise. Similarly, portfolio investment has started to

Table 34

FDI Flow during FY2008-09 to FY2011-12

(Million USD)

Component	FY09	FY10	FY11	FY09 (Jul-Mar)*	FY10 (Jul-Mar)*	FY11 (Jul-Mar)*	FY12 (Jul-Mar)*
Foreign direct investment	961	913	779	782	288	571	551
Of which EPZ	129	151	181	-	-	-	264
Portfolio investment (net)	-159	-117	-28	-98	-59	-43	118
Net FDI inflow after deducting outward transfers	-	-	-	-	-277	19	-42
Change (%)							
Foreign direct investment	-	-5.0	-14.7	-	-63.2	98.3	-3.5
Of which EPZ	-	17.1	19.9	-	-	-	-
Portfolio investment (net)	-	-26.4	-76.1	-	-39.8	-27.1	-374.4
Net FDI inflow after deducting outward transfers	-	-	-	-	-	-93.3	-326.5

Source: Bangladesh Bank and Bangladesh Export Processing Zone Authority (BEPZA).
Note: *indicates net FDI inflow.

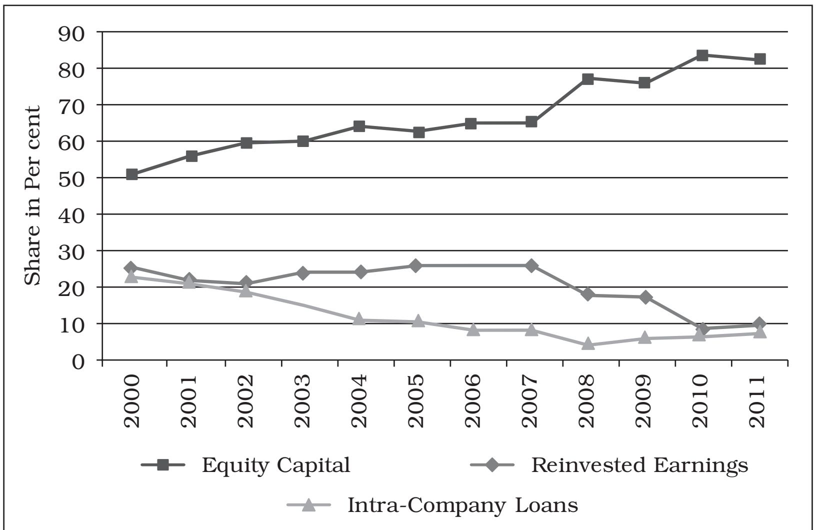
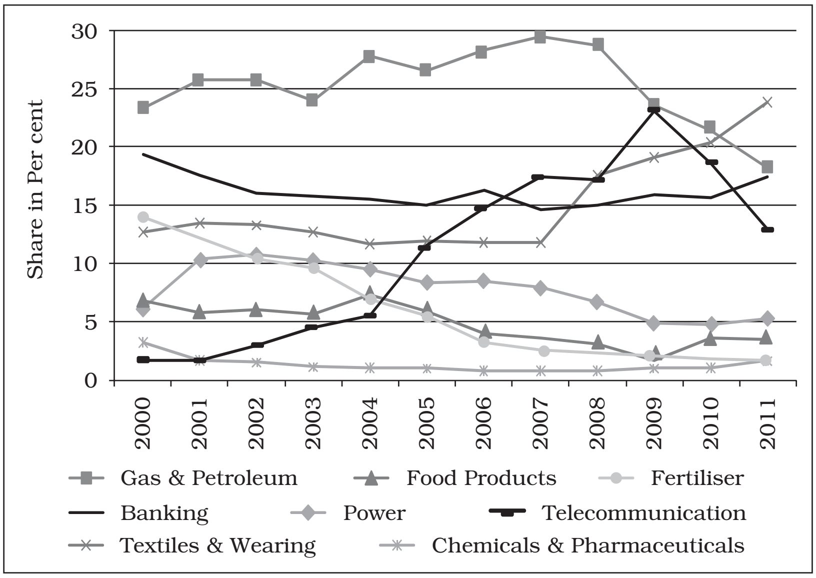


Figure 13

Distribution of FDI Stock in Bangladesh

Source: Estimated based on the Bangladesh Bank data.

Figure 14
Sectoral Distribution of FDI Stock



Source: Estimated based on the Bangladesh Bank data.

rise in recent months; during July-March, 2012 it was about USD 118 million. As a result net FDI flow (after deducting the outward transfers) during the last three years was meagre or even negative (Table 34). It is found that investment in some of the major traditional sectors has decelerated which include gas and petroleum and telecommunication; on the other hand, share of FDI stock has increased in textiles and banking (Figure 14).

3.4.4 Capital Market

Capital market is passing a transitional phase after the collapse in December, 2010. Although various kinds of initiatives for stabilising the market have been undertaken, volatility in the market is continuing. Lack of appropriate measures taken by the regulatory authority to address the structural and operational problems and weaknesses of the market is the main reason for this unstable situation. It is found that number of new initial public offerings (IPOs) offloaded in the market and their public offers are less in July-February, FY2011-12 compared to that of July-March, FY2010-11 (Table 35). Number of IPOs for offloading mutual funds has decreased in FY2011-12, whereas IPOs for manufacturing and other service sector-related companies are gradually increasing.

Table 35
IPOs Offloaded in the Primary Market

Sector	FY11 (July-March)		FY12 (July-February)	
	Number	Public Offer (Crore Tk.)	Number	Public Offer (Crore Tk.)
Pharmaceuticals and chemicals	2	42.0	0	0.0
Cement	1	334.8	0	0.0
Fuel and power	2	580.0	0	0.0
Engineering	1	16.0	1	60.0
Mutual Fund	8	575.0	4	500.8
Corporate Bond	1	300.0	0	0.0
Insurance	0	0.0	1	12.0
Financial institutions	0	0.0	1	50.0
Textiles	0	0.0	1	50.0
Food and allied	0	0.0	1	29.4
Total	15	1847.8	9	702.2

Source: Dhaka Stock Exchange (DSE).

3.5 Business Enabling Environment: Less Improvement

The slowdown of private investment is often related with adversities of business enabling environment (Greene and Villanueva 1991; Hassan and Salim 2011). This adversities occur due to, inter alia low level of electricity supply, poor growth in gas production, poor roads, rail and port facilities, high inflation, high lending rates of commercial banks, and weakness of local currency.

3.5.1 Low Level of Electricity Supply

Gap between demand for and supply of electricity in April 2012, according to BPDB, was as high as 1,200 MW (Table 36). Both public and private investment in the power sector has contributed to addition of 3,330 MW during FY2008-09 to FY2011-12, thus creating a total generation capacity of 6,807 MW. However, as of 13 May 2012, only 1,644 MW additionally, in active use. This has happened because of closure of power plants and reduction of production capacity of the power plants. The amount of loss of electricity generation capacity has increased over the years, and it was doubled between the period stated above (from 1,557 MW to 3,028 MW) (Table 37). The reduction of productive capacity occurs mainly because of lack of regular maintenance of power plants, low level of gas pressure, limited supply of fuel and some other factors.

Table 36

Electricity Generation

(Mega Watt)

Period	Maximum Demand	Maximum Generation	Average Generation	Gap
	1	2	3	4 =1-3
July 2009	4700	4201	3956	744
January 2010	4500	3921	3679	821
July 2010	5150	4170	4055	1095
January 2011	4200	3855	3637	563
July 2011	5600	4936	4702	898
January 2012	5214	5214	4950	264
April 2012	6000	5141	4800	1200

Source: Bangladesh Power Development Board (BPDB); Power Grid Company of Bangladesh (PGCB).

Table 37

Reasons for Low Level of Electricity Supply

Type	Reason	Amount of Supply Loss (MW)			
		13 May 2009	13 May 2010	13 May 2011	13 May 2012
Shut Down	Limited gas supply	38	-	-	40
	Others	162	48	1077	910
Capacity Reduction	Low water level	40	-	-	-
	Under maintenance	795	1033	185	1046
	Low gas pressure	100	115	79	285
	Limited amount of fuel supply	-	-	-	464
	Problems in coal supply	156	-	-	-
	Others	266	472	1347	283
	Total	**1557**	**1668**	**2688**	**3028**

Source: Bangladesh Power Development Board (BPDB).

Between January 2009 and April 2012, a total of 2,379,000 new connections were provided to different categories of consumers which increased domestic connections by 20 per cent, industrial unit connections by 12 per cent, connections to the irrigation pumps by 111.6 per cent, and commercial units by 12 per cent. Overall situation has further aggravated in the backdrop of rising demand and the failure of electricity production to keep up with this pace.

3.5.2 Limited Gas Supply

Between FY2008-09 and FY2010-11, total supply of gas has increased by 1,131 mmcm (million cubic metre); and between February 2011 and February 2012 the rise in supply was 3.83 per cent. This slow rise in supply is not commensurate with the high rise in demand every year; thus the deficit of supply has gone from 6,016 mmcm in FY2009-10 to 13,861 mmcm in FY2010-11. Given the limited supply, demand for gas has been adjusted by shifting a part of supply from one activity where gas is less urgently needed (e.g. fertiliser production) to other activities. Most importantly, the supply to industrial sector decreased by a considerable amount (Table 38). Anecdotal information shows that a large number of new industrial units did not get the gas connection, and therefore, could not start their operation.

Table 38

Gas Supply to Different Sectors

Sector	2009		2010		2011		2012	
	Amount (mmcm)	Share (%)	Amount (mmcm)	Share (%)	Amount (mmcm)	Share (%)	Amount (mmcm)	Share (%)
Power	7272	39.8	8017	40.0	7567	39.0	5181	41.6
Fertiliser	2119	11.6	1832	9.2	1569	8.1	913	7.3
Captive power generation	2694	14.7	3189	15.9	3317	17.1	2044	16.4
Industrial	2960	16.2	3364	16.8	3305	17.1	2093	16.8
Commercial	212	1.2	229	1.1	228	1.2	135	1.1
CNG	878	4.8	1046	5.2	1047	5.4	678	5.4
Domestic	2136	11.7	2341	11.7	2345	12.1	1423	11.4
Total	**18270**	**100.0**	**20018**	**100.0**	**19378**	**100.0**	**12467**	**100.0**

Source: Petrobangla data.

3.5.3 Poor Condition of Roads and Ports

Physical infrastructure related to domestic and external trade did not improve much although a significant amount spent under public investment in these sectors. The national, regional and district level highways/roads were not in good condition since average Roughness Index of these roads has significantly increased in FY2009-10 compared to the previous years. Some important highway development projects (e.g. Dhaka-Chittagong four lane highway project) were stalled because of many irregularities in project implementation process. The condition of Chittagong Port is not up to the mark (Table 39). The positive changes with respect to equipment availability and berth occupancy at the port could not reduce the adversities caused by the rise in turnaround time and low productivity in gang hour.

Table 39

Condition of the Chittagong Port

Criteria	FY08	FY09	FY10	FY11
Turnaround time of vessels (days)	5.10	5.50	5.20	6.90
Productivity per gang hour (no. of containers)	14.42	15.11	15.07	15.05
Equipment availability (%)	44.61	44.78	43.50	46.50
Berth occupancy (%)	66.15	62.21	66.05	81.98

Source: Chittagong Port Authority.

3.5.4 Inflation, Interest Rate and Exchange Rate

The financial market is not at a stable state for the last few years which is reflected in wide fluctuation in three important market-related factors, i.e. inflation, interest rate and exchange rate (Figure 15). A part of

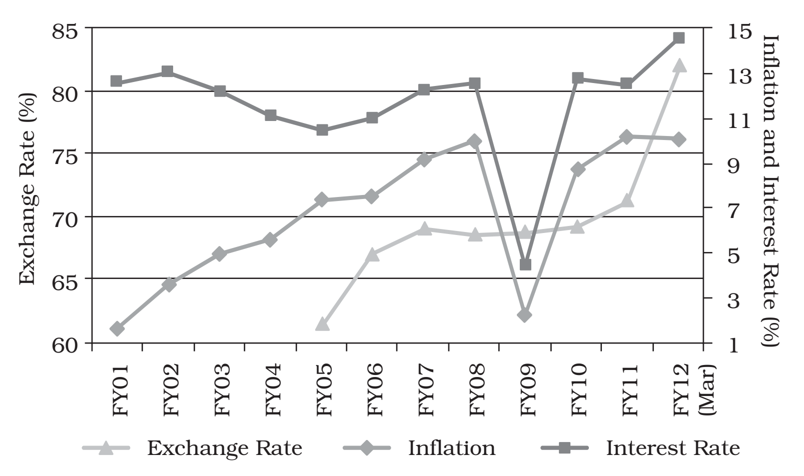


Figure 15

Interest Rate, Inflation and Exchange Rate

Source: Bangladesh Bank data.

this volatility is responsible for government's unwise expenditure on petroleum subsidy for short-term power plants. It is also related to the collapse of the capital market where huge anomalies in financial transactions (as reported in the Probe Committee Report) have created shortages of investible fund at the commercial banks. The weak balance of payments situation particularly due to rise in import of petroleum, against slowdown of export, owing to global economic downturn, has caused significant devaluation of local currency within one year.

Such adversities in business enabling factors put the existing businesses in pressure which may be reflected in their weak performance in repayment rates of credit from the commercial banks in the recent past. It is found that absolute amount of substandard, doubtful, bad and classified loans have increased in FY2011-12 (December 2011), and even share of substandard loans has increased (Table 40). This is perhaps also associated with a number of other factors including anomalies in the transaction of credit in the commercials banks, irregularities related to transaction in the capital market, transfer of fund for unproductive purposes, and increasing transaction for fake business activities. Weak oversight of the regulatory authorities (i.e. Bangladesh Bank, Securities and Exchange Commission (SEC) and Ministry of Finance) is responsible for such irregularities and anomalies.

Table 40

State of Loan Disbursed from the Commercial Banks

(Crore Tk.)

Period	Types of Loans								
Summary	Substandard Loans (Amount)	Substandard Loans (As Percentage of Total Loan)	Doubtful Loans	Doubtful Loans (As Percentage of Total Loan)	Bad Loans	Bad Loans (As Percentage of Total Loan)	Classified Loans	Classified Loans (As Percentage of Total Loan)	Total Loans
As of 31 March 2010	2839.6	1.1	1977.5	0.8	18774.4	7.5	23591.5	9.4	250610.25
As of 31 March 2011	3495.1	1.1	2440.3	0.8	17816.6	5.5	23751.9	7.3	326505.06
As of 31 March 2012	4651.7	1.2	2734.6	0.7	17903.2	4.7	25289.4	6.6	385126.38

Source: Bangladesh Bank data.

Box 2

Major Problematic Factors for Doing Business in Bangladesh: FY2009-10 to FY2011-12

Leading entrepreneurs and business bodies have expressed their opinions with regard to the problems associated with doing business in Bangladesh in the Executive Opinion Survey 2012, which was conducted by CPD during February-April, 2012. The Survey shows problems ranked among the top three are also the same as those that are found to be most important by the business bodies, as their share in the total weighted response has been increasing over the years (i.e. 45 per cent in 2010, 46 per cent in 2011, and 48.2 per cent in 2012) (Box Table 1). Similar to the earlier two years (2010 and 2011), poor infrastructure was regarded as the most important problematic factor in 2012 for doing business in Bangladesh. High level of corruption was regarded as another major problematic factor for business which was elevated to the second position since 2011. Lack of access to finance had re-emerged in 2012 after some time as one of the top three most important problematic factors (it held rank 6th and 5th positions in 2011 and 2010 respectively). Overall perceptions expressed during the survey corroborate the findings of the analyses presented earlier.

Box Table 1: Top Problematic Factors for Doing Business in Bangladesh in 2010-2012

Problematic Factor	2012		2011		2010	
	Weight	Rank	Weight	Rank	Weight	Rank
Inadequate supply of infrastructure	20.6	1	22.6	1	23.8	1
Corruption	17.6	2	18.5	2	12.6	3
Access to finance	10.0	3	5.2	6	8.5	5
Inefficient government bureaucracy	9.4	4	17.4	3	15.4	2
Policy instability	8.5	5	7.0	4	9.3	4
Inflation	8.4	6	5.0	7	2.7	10
Government instability/coups	5.7	7	2.2	12	4.7	8
Foreign currency regulations	4.2	8	4.0	8	2.8	9
Tax rates	4.0	9	2.4	11	2.1	13
Inadequately educated workforce	3.9	10	6.0	5	6.7	6
Complexity of tax regulations	2.3	11	3.9	9	5.2	7
Poor work ethics in national labour force	1.7	12	1.6	13	2.6	11
Crime and theft	1.7	13	3.2	10	2.5	12
Restrictive labour regulations	1.1	14	0.9	14	0.8	14
Poor public health	0.8	15	0.3	15	0.4	15

Source: Executive Opinion Surveys 2010, 2011, 2012.

Summary

Investment targets set forth in the SFYP faced a major hurdle in view of the declining investment growth in the second year of the Plan period in FY2011-12. Unless a significantly high growth can be attained over the subsequent years, the existing gap between the realised benchmarks and the target is likely to widen further in the coming years. Over the years, financing of the ADP through bank borrowing has been on the rise. Analysis of a Vector Error Correction model conducted by the CPD shows that public borrowing may not have significant 'crowd out' effect on private investment in Bangladesh. Similarly, exercise of Vector Autoregressive model found insignificant 'crowd in' effect of public investment on private investment.

Adversities in business enabling environment are found to be responsible for slowing down of private investment. This is perhaps related to inadequate supply of electricity and gas, poor physical infrastructure, high inflation, high lending rates of commercial banks, devaluation of local currency against USD, and difficulty with regard to access to finance. These adversities are likely to cause high cost of production with consequent negative implication for competitiveness of business both in local and foreign markets.

In this backdrop, the central bank should revisit its monetary policy in order to ensure that the interest of the private sector with respect to access to credit is not undermined. A strong coordination is required between fiscal measures and budgetary targets with the benchmarks set in the financial sector. Given the limited level of 'crowd in' effect of public investment, the government should put priority on assessing the quality of public sector projects. Appropriate and timely measures on the part of the regulatory authorities (i.e. Bangladesh Bank, SEC and Ministry of Finance) are needed in order to restore discipline in the financial sector.

4. EMPLOYMENT GENERATION

4.1 Employment Scenario in Bangladesh

With a reasonably high GDP growth, Bangladesh economy has experienced a structural change during the last several years. It has gradually moved from an agrarian to a more industry and services sector-based economy. However, the growth of the economy has not been accompanied by adequate employment creation and the number of unemployed people has increased over the years. A recent report reveals that Bangladesh is the only country in South Asia[43] where growth in labour force outpaced growth in employment during the last decade (World Bank 2012).

However, unemployment rate remained remarkably low in Bangladesh (4.5 per cent in 2010) mostly due to definitional reasons. Unemployment rate for 2010 becomes as high as 24 per cent if underemployment is added to unemployment rate (Table 41).

Table 41

Labour Force and Employment Trends

Criteria	LFS 2000			LFS 2002-03			LFS 2005-06			LFS 2010		
	Total	Male	Female	Total	Male	Female	Total	Male	Female	Total	Male	Female
Labour Force (million)	40.7	32.2	8.6	46.3	36.0	10.3	49.5	37.3	12.1	56.7	39.5	17.2
Employed population (million)	39.0	31.1	7.9	44.3	34.5	9.8	47.4	36.1	11.3	54.1	37.9	16.2
Unemployed population (million)	1.7	1.1	0.7	2.0	1.5	0.5	2.1	1.2	0.9	2.6	1.6	1.0
Unemployment rate (%)	4.2	3.4	8.1	4.3	4.2	4.9	4.3	3.4	7.0	4.5	4.1	5.8
Underemployment (million)	6.5	2.3	4.2	15.1	8.0	7.1	11.6	3.9	7.7	11.0	5.5	5.5
Underemployment rate (%)	16.6	7.4	52.8	34.0	23.1	72.7	24.5	10.9	68.1	20.3	14.4	34.2
Unemployed and Underemployed (per cent of Labour Force)	20.0	10.5	56.6	36.9	26.3	74.0	27.7	13.7	71.0	24.0	17.9	38.0

Source: Estimated based on the Labour Force Surveys (various years).

One of the encouraging developments in the employment scenario of the economy has been the increase of female participation in the labour force. Between 2000 and 2010, female labour force doubled, against a 39.3 per cent growth in the overall labour force. At the same time, against a 38.7 per cent growth in total number of employment during this time period, female employment grew by 105.1 per cent. The share of women in labour force in 2010 stood at 30.3 per cent (29.9 per cent in total employment) which was 21.1 per cent (20.3 per cent in total employment) in 2000 (BBS 2011).

It is to be noted that while growth is important for employment generation, it may not be a sufficient condition. Studies (e.g. Auer and Islam 2006; Islam 2010) have indicated that the sectoral composition of growth influences the extent and nature of employment creation. For example, manufacturing,

[43]Countries include Sri Lanka, India, Bangladesh, Nepal and Pakistan.

construction and services sectors usually demonstrate higher employment elasticity compared to sectors like agriculture, mining, utilities, etc. Though the composition of growth trend in Bangladesh suggests a positive shift towards a modern economy, the pace of the shift is yet to get adequate momentum. It is observed from Table 42 that annual employment growth in recent years has been higher in agricultural sector than the services sector in Bangladesh. This is probably due to high underemployment in the agriculture sector which absorbs more of the incremental labour force even though the sector is burdened with surplus labour.

Table 42

Sectoral Distribution and Growth in Employment

(in Per cent)

Sector	FY06 GDP	FY10 GDP	LFS 2005-06 Employment	LFS 2010 Employment	Annual Growth in Employment between 2005-06 and 2010
Agriculture	21.0	19.6	48.1	47.3	3.1
Industry	27.9	28.9	14.5	17.6	8.7
Of which Manufacturing	16.4	17.3	11.0	12.4	6.5
Services	47.3	48.1	37.4	35.1	1.9

Source: Estimated based on the Labour Force Surveys (various years).

Low level structural shift in the domestic economy has resulted in a deteriorated labour force scenario. As Table 43 indicates, between the last two Labour Force Surveys (2005-06 and 2010), although rate of employment creation has been higher than the increase in working age population, the pace of employment generation has been slower than the growth of labour force. As a result, in absolute numbers, unemployment (in traditional definition) as well as number of unemployed working age population have increased.

Table 43

Changes in Working Age Population, Labour Force and Employment

(in Per cent)

Criteria	Change between 2006-2010			Annual Growth (2006-2010)		
	Total	Male	Female	Total	Male	Female
Working age population (15+) (million)	11.0	4.8	6.2	3.1	2.7	3.5
Labour Force (million)	7.2	2.1	5.0	3.5	1.4	9.1
Employed population (million)	6.7	1.8	4.9	3.4	1.2	9.4
Gap between additional working age population and employment (million)	4.3	3.0	1.3	-	-	-
Gap between additional Labour Force and employment (million)	0.5	0.3	0.1	-	-	-

Source: Estimated based on the Labour Force Surveys (various years).

It is thus important to pursue a strategy objective towards further enhancement of the share of the manufacturing sector for employment generation. The current government in its election manifesto set the target to increase the share of modern sectors in the GDP. This is also reflected in the medium-term targets laid down in the SFYP. The following sub-section discusses employment targets divulged in the strategic documents of the government.

4.2 Employment Targets in the Strategic Planning Documents

The unemployment numbers mentioned in the election manifesto of the current government is not based on any Labour Force Survey (LFS). However, the target of the government has been set to reduce unemployment by more than 50 per cent by 2021. This is to be achieved by a compositional change in the GDP, with modern sectors (industry and services) having to contribute more. Thus the share of agriculture sector is aimed to be brought down to 15 per cent by 2021 from the current rate of 18.6 per cent.

The Sixth Five Year Plan (FY2010-11 to FY2014-15) though promotes such changes in its targets it seems to be less optimistic in a number of ways. According to SFYP targets, unemployment rate is not going to decline compared to FY2009-10 until the very last year of the plan period (only marginally by 0.3 per cent) (Table 44). In fact, total number of unemployed people is projected to increase in the next few years (till FY2013-14), and is expected to return to the FY2009-10 level in FY2014-15. However, as a share of labour force, unemployment will be lower, as the labour force is expected to grow by 1.8 per cent a year (SFYP).

Table 44

Employment Targets of the Sixth Five Year Plan

Sector	FY10	FY11	FY12	FY13	FY14	FY15
Agriculture (% share)	44.3	42.5	40.9	39.2	37.5	35.7
Manufacturing (% share)	11.6	12.4	13.3	13.9	14.6	15.7
Construction (% share)	3.6	3.9	4.1	4.3	4.5	4.7
Services (% share)	40.5	41.2	41.6	42.7	43.4	43.8
Total employment (million)	52.4	54.1	55.8	57.6	59.5	61.6
Employment growth (%)	-	3.2	3.1	3.3	3.2	3.2
Total unemployment (million)	2.1	2.1	2.2	2.3	2.3	2.1
Unemployment rate (%)	4.0	4.1	4.0	4.0	4.0	3.7
Labour Force (million)	54.5	56.2	58.0	59.9	61.8	63.7
Labour Force growth (%)	-	3.1	3.2	3.3	3.2	3.1
GDP growth (%)	6.1*	6.7*	6.3*	7.2	7.6	8.0

Source: Based on the Sixth Five Year Plan (SFYP) targets.
Note: *Actual growth.

On an average, during the remaining three years of the SFYP period (FY2011-12 to FY2014-15), 1.9 million additional employments generation per annum has been targeted. The actual employment trend in the LFSs between 2005-06 and 2010 reveal that about 1.7 million employments have been created annually. It thus appears that SFYP aims improvement in employment intensity of growth in the medium-term, but not in any significant way.

4.3 Employment Creation during the Last Three Years and Prospects for SFYP Targets

Recently it has been claimed by the government that about 6.8 million jobs have been created during the last three years, of which about 0.45 million has been employed in the public sector.[44] In the absence of annual labour force (employment) survey, it is difficult to discuss the incremental changes that have been in the employment situation over the last three years. However, the standard procedure is to estimate the employment elasticity of growth which can be used to derive approximate estimates of employment generation. The accuracy level of employment estimates is better if employment elasticities of growth are calculated at the sectoral levels instead of the aggregate level.

Based on the sectoral elasticity approach CPD has estimated that during the last three years (end of F2008-Y09 to FY2011-12) about 5.8 million employments have been created (Table 45), i.e. an annual

[44]On 24 April 2012, it was reported in the Financial Express that the Prime Minister while addressing a reception, accorded to her by the Bangladeshi community living in Qatar, at the Diplomatic Club in Doha, told that 6.8 million jobs have been created by the present government.

average of 1.9 million.[45] This figure is one million less than that of the official claim. About 41 per cent and 26.7 per cent of the incremental employment came from the agriculture sector and manufacturing sector respectively while other sectors generated 35.2 per cent of the new jobs.

Table 45

Estimated Employment during the Last Three Years

(Million)

Criteria	FY10	FY11	FY12
Labour Force	56.7	58.5	60.3
New employment	1.9	2.1	1.8
Total employment	54.1	56.2	58.0
Unemployment	2.6	2.3	2.3
Unemployment rate (%)	4.6	3.9	3.8

Source: Estimated based on the Labour Force Surveys (various years).

Hence employment generation targets set by the SFYP appears to be rather conservative compared to the estimates done by CPD. Estimates of employment elasticities based on the GDP projections of SFYP shows that if the economic growth projections materialise, by FY2014-15 the traditional employment concerns will be eliminated, but underemployment will continue to prevail as a major concern.

It is also to be borne in mind that given the present composition of the economy, achievement of the growth targets (e.g. 8.0 per cent by FY2014-15) will be a challenging task. Indeed, as the provisional estimate of the BBS shows, GDP growth in FY2011-12 has missed the SFYP target by quite a significant margin (6.3 per cent against the target of 7.0 per cent).

4.4 Way Forward

With three years left for the implementation of the SFYP, any significant change in the GDP composition may be an over optimistic target to be fulfilled within the Plan period. Although the contribution of the agriculture sector in gross output is gradually declining, it is unlikely to reach 15.5 per cent by FY2014-15 as targeted in the SFYP. However, the government can try to achieve the aggregate growth projection. This is a difficult, but not impossible task given the performance that Bangladesh economy has demonstrated over the years.

Apart from the efforts to accelerate growth, the government can emphasise two areas of intervention to leave a direct impact on the employment situation. First, the government can directly engage in employment generation through its social safety net programmes (SSNPs) for the poorest section. Major employment generating programmes of the government include: Employment Generation Programme for the Poorest (EGPP), Food for Work (FFW) and National Service. In FY2011-12 the EGPP created over 3.3 million, FFW about 3.8 million and National Service programme another 1.5 million man-month of employment. These programmes are, therefore, contributing significantly to the improvement of the employment scenario. The challenge however is to achieve incremental job creation through SSNPs in order to have any significant improvement of the unemployment situation. This is all the more important given the resource constraint. It is to be noted that the three above mentioned programmes targeted only 0.5

[45]The estimate follows the methodology suggested by ILO (2002). According to this methodology the changes in sectoral employment can be defined as: $\Delta Ei = (hi)(li)\Delta Yi$

Where, ΔEi is the changes in employment in sector i; hi is the sectoral employment elasticities; li is the average labour intensity (employment per unit of value added) in the i-th sector; and ΔYi is the change in value added in sector i over the period of projection.

This method is particularly useful for projecting employment changes in countries like Bangladesh where employment data is generated with a lag. Adding up all the sectors would bring the overall change in employment of the economy. Assumptions: 1) Relationship between employment and output remains consistent over the medium-term. 2) Structural changes within industries are adjusted for a broad sector in the medium-term. 3) No change in production technology.

million man-months of incremental employment in FY2011-12. Targeted employment generation for the EGPP and the FFW programme remained the same in FY2011-12 compared to FY2010-11 (GED 2011).

The wage implications of the employment generating programmes have increasingly become an important factor in job creation. Due to the absence of a competitive wage rate a modest increase in allocations did not yield any significant incremental employment contribution from these programmes. As the current government is committed to enhance social protection and employment generation through the safety nets, resource allocation for these programmes will need to be enhanced.

The second important area of intervention is the outflow of overseas migrant workers. Surprisingly, migrant workers are neither included in the labour force, nor counted in total employment. However, the outflow of workers does reduce the pressure on the growth of labour force and the overall employment generation effort. During FY2005-06 to FY2009-10 (between the last two LFSs), 2.9 million people went abroad for jobs from Bangladesh. This number is about 40.2 per cent of the incremental labour force during this period, a fact that signifies the impact of overseas workers on the labour force and employment scenario of the country. Thus as part of the employment generation strategy of the government and in order to supplement domestic employment generation efforts, due emphasis should be given on the exploration of opportunities for overseas employment. Apart from strengthening diplomatic relations, this also calls for reducing cost of migration and skill enhancing training programmes, catering for the needs of the overseas markets. The *Comprehensive Migration Policy* and *Overseas Employment Act 2011* needs to be finalised through specification of appropriate modalities for ensuring full compliance with the law by the recruiting agencies.

Indeed, enhancement of economic growth should be at the centre of an employment strategy, which will be intertwined with the ultimate aim of poverty reduction through employment generation. However, the major impetus for increased employment has to come from the private sector. Enhancing growth and employment creation in Bangladesh will of course require removal of obstacles such as infrastructural bottlenecks, institutional weaknesses and political instability.

5. REVIEW OF POLICY AND REFORM INITIATIVES

5.1 Introduction

The need for undertaking reforms and policy initiatives, as a continuing activity to raise the efficacy of developmental practice and the quality of developmental outcomes, is a generally accepted wisdom as far as developing countries are concerned. Whilst in the 1990s many developing countries have pursued first generation reforms that led to opening up of their economies, it was subsequently felt that without a second generation reforms and strengthening of institutions and institutional capacities, developing countries would not be able to move towards the accelerated growth trajectory they aimed for. In view of this, in the recent past many developing countries have started to pursue regulatory and institutional reforms in an attempt to accelerate economic growth and development. In the context of Bangladesh, an attempt to undertake reforms, as a part of the broader developmental strategy, was witnessed during the time of the Caretaker Government (CTG) (2007-2008) which took a decision to initiate a series of reforms programmes in some key areas of governance and development. As one would recall, the CTG had set up two important bodies towards this. Bangladesh Better Business Forum (BBBF) and Regulatory Reforms Commission (RRC) with a view to undertake policy initiatives and reforms measures in the areas of macroeconomic management and sectoral development. The newly elected government that came to power in January 2009, also committed itself to undertaking the much-needed policy initiatives and reforms in a number of areas, in line with its election manifesto and the Perspective Plan 2021 document.

As a concept 'reforms' generally allude to major departures in policies which are undertaken with a view to going beyond the 'business as usual' mode of doing things (Alesina *et al.* 2006), and are pursued with the goal of raising efficacy and effectiveness of institutions in performing their respective mandated tasks. The objectives of policy initiatives and reforms, in the context of developing countries such as Bangladesh, are to raise the quality of macroeconomic management, enhancing institutional efficacy and higher mobilisation, and better utilisation of resources which would be reflected in better developmental outcomes, good governance, higher accountability and greater transparency. It may be recalled in this connection that the *Mohajot Government* took the helms of power on 6 January 2009 in the backdrop of high expectations on the part of an electorate that gave it an unprecedented mandate through elections to the Ninth Parliament. The newly elected government promised that it would undertake important policy initiatives and reforms in a number of key areas of the economy in order to ensure a qualitative change in the way government worked in Bangladesh.

Indeed, the manifesto of the ruling Awami League, the *Rupokolpo 2021*, and a number of subsequent documents including three budget speeches, the Perspective Plan 2021 and Sixth Five Year Plan, did mention about a number of important policy initiatives that the government was planning to undertake as part of addressing bottlenecks and improving the quality of management of the economy. The overarching declarative goal was to raise the quality of overall economic governance with a view to alleviating poverty and accelerating the pace of economic growth. As the tenure of the present government draws to a close, it is perhaps an opportune time to review the progress that has been made in this context, and undertake an exercise to assess the performance of the government in this regard.

As is known, the *first generation* of serious reforms in Bangladesh, that took place in the late 1980s and early 1990s, were pursued through policies of liberalisation, deregulation and privatisation and by putting in place market-oriented exchange and interest rates. The period subsequent to these reforms saw an acceleration in the pace of growth of the Bangladesh economy and faster poverty alleviation, although there had been criticism with regard to pacing, phasing and sequencing of these reforms. There is a wide consensus that a modernising economy such as Bangladesh, in order to graduate to the next phase of development, will need to undertake new policy initiatives in key areas of economic management and development. It is increasingly felt that Bangladesh needed a *second generation* of reforms to consolidate the results of the *first generation* of reforms; it is also felt that some of the first generation reforms would not be able to generate the intended outcomes if the second generation of reforms were not put in place in the first place. For example, reforms initiatives to open the capital market were unlikely to generate the expected results if institutional reforms, such as those towards strengthening of the regulatory mechanisms and the Institution of the Securities and Exchange Commission, were not adequately addressed as a *necessary condition.*

In this backdrop, there was an increasingly felt urgency to the effect that Bangladesh needed policy initiatives and reforms that would raise the efficacy of institutions, improve resource mobilisation and utilisation capacity of the state and improve the quality of macroeconomic management with less corruption, better governance, higher accountability and transparency, and better developmental outcomes in the form of faster growth, accelerated poverty alleviation and inclusive development.

It may be recalled here that during the tenure of the 2007-08 CTG, BBBF and RRC had proposed and implemented a number of important reforms and policy changes to improve governance, accountability and transparency in macroeconomic and sectoral management. Important reforms were also carried out in the areas of electoral process. The RRC, established in October 2007, was mandated to recommend reforms in such areas as better business regulation, stimulating investment and capacity building in government agencies. The RRC put forward a total of 135 recommendations of which 46 (34 per cent) were implemented by the CTG during its two years tenure. A few examples can be cited to illustrate the positive outcomes of these reforms: the Bonded Warehouse Licensing Reform led to savings of more than USD 1,700 for an average firm; administrative reforms led to reduction in land registration fees in the range of 10-12 per cent; automation of the Dhaka Customs House led to significant reduction in the time needed for customs related-work (Rahman 2009).

In the above backdrop, there was a genuine demand on the part of the citizens of the country for a qualitatively developmental governance in Bangladesh which would lead to more efficient service delivery for citizens and better outcomes. One may recall that, a number of policy initiatives needed in this context were articulated in CPD's Vision 2021 document which was prepared in 2006 through a wide-ranging consultation process involving citizens from all cross-sections of the society, across the country. The aspiration of citizens for change also got reflected in the Awami League's election manifesto titled *Din Bodol*. The manifesto promised to bring about fundamental changes in a number of areas including in regulatory and business environment, tax administration, local government, civil service and environment. The *Din Bodol* document mentioned about five priority areas: (a) arresting price hike of essential commodities via policy measures; (b) combating corruption; (c) developing a comprehensive long-term policy on electricity and energy; (d) eradicating poverty and inequity; and (e) promoting good governance. The document mentioned that necessary policy initiatives would be undertaken to attain these objectives. The Awami League election manifesto concluded: "Let us put a permanent end to persecution, deprivation, inequity, and mis-governance. Let us construct a just and democratic society and build a happy, prosperous, golden Bengal."

The three budget documents presented before the parliament, in view of the budgets for FY2009-10, FY2010-11 and FY2011-12, also reiterated the need for policy changes and new policy initiatives and reforms. Each of these policy documents came up with various proposals to be undertaken by the government as a sign of departure from business as usual. In his first budget speech the Hon'ble Finance Minister stated that the Grand Alliance was elected "with a charter for change, with a promise to create an environment where people can live with dignity and with determination to build a prosperous and caring Bangladesh." This commitment was also reiterated in the ten-year Perspective Plan titled, *Perspective Plan of Bangladesh 2010-2021: Making Vision 2021 A Reality*, and the Sixth Five Year Plan. It mentions: "The Government understands that without fundamental reforms of core institutions, improvement in public administration capacity and a strong anti-corruption strategy, the ability to implement Vision 2021 and the underlying five year development plans will be seriously compromised."

In view of the above commitments and declarative statements, as the government's tenure enters its finishing line, there is a heightened need to assess the progress made in undertaking the policy initiatives and reforms in various areas which the government had promised to its citizens. This is the motivation of the present review. Thus, the purpose of the present exercise is to: (a) document the policy initiative and reform propositions of the government in key areas of – (i) economy-wide policies, (ii) economic governance, and (iii) development administration; (b) undertake an assessment of the progress made so far with regard to the relevant policies and laws/acts/regulations/ordinances, etc. (preparation of drafts, enactment of laws by the parliament); and (c) comment on the state of follow-up actions to pursue and implement the policy initiatives in the aforesaid areas. To facilitate the analysis, a matrix was first prepared with respect to the above three areas to help identify the policy initiatives proposed by the government, and to track the state of progress in this context (the matrix is included in the Appendix of the chapter). The Appendix has been developed as a *tracer study* pertaining to various pronouncements made by the government. It needs to be stated upfront that these groups are not mutually exclusive groups and there are significant overlaps. However, effort has been made to disaggregate these three categories to the extent possible, though interpretational ambiguities persist. For instance, Public-Private Partnership (PPP) could be placed under any of the three categories but since its primary objective pertains to improving resource mobilisation, this was put under the economic reforms category. Similarly, e-governance could be placed under governance or administration, but this was placed as an economic reform because one of its objectives was also to augment revenue earnings by making use of information and communication technology (ICT) in tax-related transactions.

The present review makes an attempt to study whether proposals relating to policy initiatives and reform measures have actually been followed up with concrete actions in terms of enacting laws, amending rules and regulations and undertaking institutional measures. Making an assessment of whether the policy initiatives, if and when these were implemented, have been able to generate the expected results, will require a more detailed and disaggregated in-depth work focusing on success, bottlenecks and unfinished agendas. As evidence suggests and experience of the developed world with reforms illustrates, it takes a long time to achieve fundamental changes. Schacter (2000) cites the example of civil service reforms in the UK which took thirty years to eliminate patronage as the *modus operandi* for recruitment in the public sector. On the other hand, the International Development Association (IDA) showcases a powerful story of how public sector reforms led to concrete results in the infrastructure, health and education sectors. Their 'Results Profile' on public finance reform in Bihar, India illustrates how reforms in public finance management, with greater delegation of financial powers, resulted in a three-fold increase in development expenditures in such areas as roads, health and education.

The next sub-section has been prepared with two objectives in mind. The first objective is to identify the key policy initiatives and reform measures as has been proposed by the government, based on an analysis of various budget and plan documents. The second objective is to review the progress made till now with regard to these proposed areas based on a review of documents and discussion with relevant stakeholders. The section also attempts to anticipate some of the key cross-cutting reforms that will need to be pursued during the next two years of the current government, and also beyond, based on perceptions of CPD on developmental priorities facing Bangladesh in the coming days.

5.2 Identification of Core Reform Areas

The present government adopted several initiatives aimed at improving governance for delivering better developmental outcomes. It has reverted back to the Five-Year Plan system and introduced the Sixth Five Year Plan (FY2010-11 to FY2014-15) which has been approved by the cabinet; so has been the ten years Perspective Plan titled *Outline Perspective Plan of Bangladesh 2010-2021: Making Vision 2021 A Reality*; thus far, three fiscal budgets have been put into effect. In this section an attempt has been made to categorise the reforms through an in-depth examination of the initiatives as identified in the accompanying matrix. A majority of the policy initiatives, however, fall under the category of economic reforms and covers a fairly wide spectrum of issues. The focus of this particular report has been on *economic policy* and *reforms proposals*. The related policy initiatives have been categorised in three groups: (a) Strengthening Economic Management; (b) Improving Governance, Accountability and Transparency; and (c) Raising the Efficacy of Development Administration. Economic reforms proposed by the government covered a number of areas which have been mentioned in dedicated sub-sections. In certain cases progress had been made in terms of following up on those intentions and proposals and relevant acts and laws have been made. In other cases drafts have been prepared and being discussed; in other cases initiatives are yet to be taken. Where concrete steps have been taken, the challenge remains to follow up on the reforms that have been implemented.

5.2.1 Strengthening Economic Management

In its policy documents, the government had proposed a number of initiatives to strengthen the management quality of the economy through various macro and sectoral measures. These covered such areas as improving fiscal discipline, greater mobilisation of domestic resources, and raising the quality of economic management.

Consolidation of Fiscal Management

Revenue mobilisation remains a major concern in Bangladesh with the tax-GDP ratio being low even by South Asian standards. With a view to reforming policies towards better fiscal effort, the first budget talked of bringing changes to the Value Added Tax (VAT) Act, 1991 and its related Statutory Regulatory Orders (SROs). Similarly, proposals were made to amend a number of sections of the Customs Act, 1969, and to revise the Income Tax Ordinance, 1984. The third budget proposed that the VAT and Direct Tax Act would be put into effect by December 2011. It mentioned that all ministries and divisions will be brought within the ambit of the Medium Term Budgetary Framework (MTBF). Enactment of the Public Finance and Budget Management Act 2009 was also announced. An NBR Modernization Plan (2011-16) and Modernization of VAT Environment (MOVE) were also proposed.

Review of Current Status

With regards to the finalisation of the VAT Act and Direct Tax Act, the drafts have been prepared and this will perhaps be reported in the budget speech for FY2012-13. However, there is a need for broader public discussion on these particularly keeping in view the need for undertaking appropriate preparatory work, introducing of the needed operational and accounting practices and logistic arrangements along the value chain. To discourage capital flight and address the problems associated with transfer pricing, the draft is proposing introduction of a separate chapter in the Income Tax Ordinance 1984 and putting in place a separate Transfer Pricing Cell. However, the draft in this context will need to be further strengthened in a number of areas (Rahman *et al.* 2011).

All ministries at present have been brought under the purview of the MTBF. However, the capacity of the ministries to perform according to the needs of the MTBF is yet to be strengthened in a commensurate manner. This lacuna is also reflected in the inability of most of the line ministries to implement the ADP both in terms of quality and quantity. There is lack of coherence between the processes for planning and management of strategic plans, MTBF and ADP. The move towards a comprehensive budget process covering both the development budget and ADP also implies reform of the ADP, and in particular, the phasing out of those procedures that duplicate the line ministry budget preparation procedures under the MTBF (World Bank 2010).

The Public Finance and Budget Management Act was made effective as of July 2009. This was a welcome step from the perspective of providing greater transparency in the policy making and implementation process. It may be recalled that, earlier, the need for real time information with regard to the performance of the economy had been highlighted by CPD in its successive reviews. According to the Article 15 (4) of the aforesaid Act, the Finance Minister is mandated to present a quarterly report to the parliament regarding performance of the economy. Since the enactment of this legal obligation, during the last 11 quarters (July 2009-March 2012), the Finance Minister has placed only five such reports before the Parliament. This practice now needs to be formalised alongside introducing a Reform Reporting System for tracking the progress of reforms proposals.

Introducing E-Governance

The Perspective Plan 2021 mentioned about adopting the e-governance model. Here, ambition was to promote *Digital Democracy* and *Digital Government* and empower citizens through more intensive and widespread use of ICT. This was to be done through wider access to information, better and speedy delivery of public services and government decisions, promoting paper-less transactions, digitisation of the work of the government agencies in various areas through more intensive use of ICT. The government set the target of initiating e-commerce by 2012 and graduating to e-governance by 2014. Ambition was set to transform administrative works in the public sector into e-government/digital government. The third budget document noted that Digital File Tracking System had been introduced on a test basis. Also, the National Information and Communication Technology Policy 2009 was approved by the government.

Review of Current Status

A number of initiatives have been taken to introduce e-governance including introduction of Automated System for Customs Data (ASYCUDA) and computerisation of Chittagong Customs; steps to bring local governments under computer network; e-filing of tenders; and income tax returns. The Digital File Tracking System has been introduced albeit only on a test basis. However, much will need to be done to make appropriate use of ICT in terms of generating revenue and bringing transparency in the public administration system. For example, not much headway has been done with regard to digitisation of the land registration system, a key aspect of e-governance.

Land Administration and Food Security

The Perspective Plan 2021 called for preparing an integrated programme of food procurement, storage and distribution. It also mentioned about formulating a Land Use policy. The SFYP espouses these aspirations through plans to prepare and use Land Zoning Maps for use of land; along with rationalisation of land acquisition act and policy. Additionally, in line with the commitment towards *Digital Bangladesh*, the SFYP set the ambition of computerisation of land records and automatic land mutation. In case of food security, the SFYP mentions that it is to be achieved through implementation of the National Food Policy and Plan of Action (NFP/POA) supported by the Country Investment Plan (CIP) 2010-2015.

The first budget mentioned about the implementation of the National Food Policy Capacity Strengthening Programme. It also mentioned about preparing a policy to integrate *Khas* Land Distribution, Housing, Employment Facilities, *Adarsha Gram* and *Asrayan*. The third budget set the target of finalising the National Agriculture Policy 2011 and talked of introducing Crop Insurance Scheme on a pilot basis. It also mentioned that a draft was under preparation with regard to City Area Planning and Land Use Management Act 2011.

Review of Current Status

A draft titled Protection of Cultivable Land and Land Use Act 2011 has been prepared by the government as per the commitment made in the Perspective Plan 2021. The government has enacted the *Balu Mahal* and Field Management Law 2010 to tackle the problems related to leasing of land. The Vested Properties Return (Amendment) Bill 2011 has been passed although not all demands of the stakeholders were address in this bill.

The National Agricultural Policy 2011 and the National Food Policy have been formulated, and are being implemented. Progress is yet to be made in terms of preparing that a policy to integrate *Khas* Land Distribution, Housing, Adarsha Gram and Asrayan, as declared in the first budget speech. The Crop Insurance Scheme was expected to be introduced on a pilot basis in four upazilas; however, no progress has been made with regard to its implementation.

Resource Mobilisation through PPP

The SFYP mentions that under the PPP initiative and the associated investment guideline, the procedures for PPP investment have been streamlined and a new PPP Office established to promote PPP projects.

Simultaneously, the Bangladesh Infrastructure Finance Fund (BIFF) was created to strengthen PPP initiative and to attract investment from home and abroad.

One of the key policy initiatives mentioned in the first budget was the introduction of PPP as an important strategy towards investment promotion. The first budget mentioned that steps were being undertaken to establish the PPP Office. Indeed, in anticipation of this, a Tk. 3,000 crore was set aside in the budget for FY2009-10 for projects under PPP. The second budget also reiterated that steps were being taken for the establishment of a PPP Office. The third budget indicated that PPP guidelines were being prepared by incorporating new policies, strategies and procedures. It confirmed about the BIFF's transformation into a company, which was expected to commence investment function in FY2011-12.

Review of Current Status

Introducing PPP had been a key commitment of the government in attracting private sector capital for stimulating investment. However, the process of getting the PPP going has been very slow. Though the PPP Policy came into effect in 2010, the Office of the PPP is still to be made a full-fledged and functioning entity. The guidelines for PPP projects have been designed; however, attaining concrete results with regard to use of the allocated funds for PPP will now need to be prioritised by the government. The BIFF is yet to make any impact to showcase its potential for promoting PPP as a model for attracting investment.

Managing the Industrialisation Process

The Perspective Plan 2021 mentions that industrial parks, dedicated private sector industrial zones, EPZs and special economic zones (SEZs) were to be established with the objective of stimulating industrial growth. New policies will be put in place to get these off the ground. The SFYP talks of reforming the SoEs to reduce losses and improve efficiency.

The budget for FY2009-10 mentioned about revisiting and reforming the industrial policy, and setting up a new investment financial institution, dedicated for industrialisation, through merger of Bangladesh Shilpa Bank and Bangladesh Shilpa Rin Sangstha. The second budget informed that the Bangladesh Economic Zones Act 2010 was being formulated and that the draft Industrial Policy 2010 was being finalised, and that the government was at the final stage of formulating the Competition Act. The third budget stated about setting up economic zones under the Bangladesh Economic Zones Act 2010. Towards greening the economy, a number of steps were mentioned including passing of the enactment of the Hazardous Waste and Ship Breaking Waste Management Rules, 2011 by FY2012-13.

Review of Current Status

The Special Economic Zone (SEZ) 2010 bill was passed in 20 July 2010; the Economic Zones Act 2010 has also been enacted. A Hi-Tech Park Authority Law, 2010 has also been enacted to help promote the software industry in the country. Private sector has now come forward with proposals for establishing SEZs in association with the government under the PPP model. Industrial Policy 2010-2014 was approved by the government in August 2010, which provided opportunities for local as well as foreign entrepreneurs to invest under the PPP arrangement. At present, the Competition Policy Law is with cabinet awaiting approval. The Bangladesh Development Bank Ltd. came into effect with the merger of ailing Shilpa Bank and Shilpa Rin Sangstha in 2010 (at one stage, the government considered privatising the two SoEs but instead opted for a new bank through merger). In May 2012, the government decided to sell the Rangamati Textile Mills Ltd. and Magura Textile Mills Ltd.

Capital Market Management

According to the Perspective Plan 2021, the capital market was poised to be further liberalised, reformed and deepened to create opportunities for raising equity to support Bangladesh's efforts to modernise and develop the industrial sector. Particularly after the boom and bust of the capital market in December 2010, the government declared that it will take a number of initiatives towards restructuring the market, raising its functioning efficacy, promoting transparency and eliminating possibilities of manipulations and insider trading, and strengthening the overall governance in the country's capital market. It was also mentioned at various times that a Financial Reporting Act (FRA) will be formulated; demutualisation of the two stock exchanges was proposed to be completed at an early date; and, that the SEC will update the Small Investor Protection Law. The SFYP mentions about reforms in the capital market with the objective of promoting private investment and strengthening the oversight functions of the SEC. Sight was also set on setting up a Capital Market Institution.

The first and second budgets indicated that steps and plans were being undertaken to establish the Bangladesh Institute of Capital Market. In the latest budget, it was mentioned that in order to separate the ownership, management and trading of stock exchange and to contain manipulation in the capital market, the process of demutualisation in Dhaka and Chittagong Stock Exchanges had begun. The latest budget also indicated that steps were bring taken to amend the SEC Act, various rules guiding the functioning of the SEC and the Companies Act.

Review of Current Status

In view of the developments in the capital market, in particular the report of the investigation committee and demand from stakeholders towards good governance in the capital market, there was an expectation that speedy reforms will be undertaken to improve the functioning of the country's capital market. Although the government and the reconstituted SEC have undertaken a number of steps to address the attendant issues, some of the key reforms are still to happen. These include, among others, formulation of the FRA to improve quality of accounting and auditing disclosure by listed companies, demutualisation of the two stock exchanges to ensure better corporate governance, and upgradation of insider trading rules. As it stands now, the FRA is yet to be drafted whilst the work is in progress with regards to demutualisation and insider trading. It is necessary to expedite this work with due priority in order to restore investor confidence of the private sector in the capital market.

Developing the Energy Sector

As is known, the power and energy sectors have become the Achillees' heels of the Bangladesh economy. The Perspective Plan 2021 calls for formulating a long-term policy on electricity and energy. It also mentions about preparing a policy for energy conservation. Many initiatives have been mentioned under the SFYP and one of such key reforms is to ensure proper pricing of power based on a review of good international practices.

The first budget mentioned that work was near completion with regard to the finalisation of the Energy and Coal Policy as a step towards long-term energy sustainability of the country, a crucial policy initiative from the perspective of the country's economic growth. The third budget mentioned that the government was working towards finalising the Sustainable Energy Development Authority Act, 2011 to oversee long-term energy-related interest of the country.

Review of Current Status

Reforms in the energy sector to accelerate production of electricity and fixing price of electricity and gas remain a key area of interest in Bangladesh. To create a competitive market for gas supply through participation of the private sector and timely payment, the government enacted the Gas Law in July 2010. The government also passed the Power and Energy Fast Supply Enhancement (Special Provision) Law, 2010 which allowed taking steps towards accelerated energy production, though critics say that it has been at the cost of due diligence. In spite of the pitfalls of pursuing the current policy of overdependence on fuel-powered electricity, the government has not been able to finalise the coal policy. It may be recalled that, the government had repeatedly declared its intention to establish *Khani Bangla* and prepare the National Coal Policy. At present, the National Coal Policy is pending approval of the parliamentary committee.

Financial Sector Management

The first budget affirmed the enactment of the Money Laundering Prevention Act 2009. Subsequent budgets put forward a number of proposals towards good governance, and promoting greater transparency and accountability in the monetary sectors. These included drafting the FRA and an Audit Act, amending Bank Companies Act, Financial Institutions Act and Insurance Corporation (Amendment) Act, and enactment of the Insurance Act 2010 and Insurance Development and Regulatory Authority Act 2010.

Review of Current Status

In 2012, the Money Laundering Prevention Act 2009 was revised with the passage of the Anti-Money Laundering Law 2012 by the parliament. Money laundering issues will also be dealt through the amended Income Tax Ordinance. In the budget speech 2011-12, the Finance Minister underlined the necessity of implementing an Audit Act. It is to be recalled here that a draft Audit Act was submitted to the Finance Ministry in 2008. However, till now, there has not been any headway in finalising the draft.

5.2.2 Improving Governance, Accountability and Transparency

The government indicated that it would take a number of initiatives towards institutionalisation of good governance in the economy. In view of the developments preceding the elections in 2008, improving the state of governance became a key demand of citizens. The urgency of undertaking governance reforms were reiterated in all government documents. However, significant rhetoric-reality gaps remain in this context.

Establishing the Institution of Ombudsman

The commitment to establish an *Office of Ombudsman* was made by successive governments in Bangladesh. This is also a constitutional obligation. The Perspective Plan 2021 mentions that the post of Ombudsman should be filled, and he/she is to be provided full autonomy to function effectively and independently. The SFYP, likewise, calls for the appointment of an Ombudsman with adequate support as guaranteed by Article 77 of the Constitution. This has not happened as yet although a number of positive steps were taken by the present government to establish institutions that promote transparency and accountability. The National Human Rights Commission Law, 2009 has helped establishment of the National Human Rights Commission. The Right to Information Act, 2009 was enacted with a view to making public agencies accountable and subsequently, an Information Commission was set up by the government to service citizens need for information. It is to be noted that both these initiatives were introduced as ordinances by the previous CTG and subsequently enacted as laws by the current parliament.

Review of Current Status

It may be recalled that an Ombudsman Act was enacted in Bangladesh in 1980. There was no serious follow-up till 2005, when a Tax Ombudsman was appointed as part of a watered-down initiative. The Awami League had also committed to establish the Office of the Ombudsman. However, these were not followed up, and on the contrary, the Tax Ombudsman was abolished through the Tax Ombudsman (Avoidance) Law 2011.

In a number of developing countries, the Ombudsman acts as the destination of last resort for redressing grievances of the common citizens. One can assume under what potential load of petitions and pressure such an office will function in a populous country like Bangladesh! Some have argued that Ombudsmen should be appointed also at sub-national (divisional) level to deal with complaints in a speedy manner (Mollah and Uddin 2004).

Strengthening the Anti-Corruption Commission (ACC)

The Awami League manifesto mentions about taking effective measures to tackle corruption as one of the five priority initiatives. The Perspective Plan 2021 underlines a commitment towards a corruption-free society; it also speaks of an Anti-Corruption Commission (ACC) that would be able to function with constitutional guarantees, free of any constraint by the executive. The SFYP also mentions about putting the ACC on a strong footing, enabling it to execute its mandate with the highest degree of efficacy and independence. The SFYP seeks to provide the ACC with complete independence in carrying out its investigations and prosecution in order to ensure that its actions are politically neutral and targeted towards enhancement of public welfare. Budget speeches proposed that some amendments would be made to the ACC Act to address loopholes in the existing law.

Review of Current Status

The government had declared several times that the ACC would function independently without the requirement of government's permission to carry out investigations against civil servants, and it will be able to file case anytime, as and when any complaint was received. However, no law or policy has been adopted yet to institutionalise the declarative intention of making the ACC independent.

Institutions to Promote Reforms

The Perspective Plan 2021 envisages establishment of a number of institutions to maintain momentum of the reforms agenda. It stipulates establishment of a permanent Pay, Services and Regulatory Reforms Commission (PSRRC) for strengthening the regulatory environment; a Perspective Plan Management Office (PPMO) at the Planning Commission to coordinate the execution of the Plan; and an Independent Vision 2021 Council to regularly refine the Perspective Plan and track progress in an objective manner. However, these are yet to be followed up with concrete actions.

Review of Current Status

Although no actions have been taken to give effect to the aforesaid intentions, it is, nevertheless, good to see that the government has taken an initiative to review the progress made with regard to the reform measures it has proposed in its various policy documents. A committee has been formed which is to report to the Finance Ministry. However, it may be recalled that the government, as part of its ECF, had promised the IMF to undertake wide-ranging reforms in a number of areas. One hopes that this committee was not set up in view of the reports to be made to the IMF, but to undertake a serious review of the progress made with regard to reform proposals in its various policy documents, monitor progress and suggest measures to implement reform measures in a manner that supports poverty alleviation, economic growth and inclusive development.

5.2.3 Raising the Efficacy of Development Administration

It is recognised that the closer the people are to public resources, the higher are its efficacy in terms of delivery (Lewis and Hossain 2008). To a large extent, efficiency of development administration determines how allocated resources are appropriately utilised. A number of initiatives were mentioned at various times in this regard. The importance of reforms in civil service and centre-local relations has been underlined by both the Perspective Plan and the SFYP.

Raising Efficacy of Public Administration

The effectiveness and efficiency of a country's public sector is vital to the success of its development activities (World Bank 2008). At various times the government indicated its willingness to enhance transparency and accountability in bureaucracy and public administration. The Perspective Plan 2021 directs preparing a composite set of agency performance indicators for ministries and agencies to facilitate public disclosure of performance data for individual agencies. The SFYP calls for formulating a Civil Service Act. Alongside the provisions for fiscal devolution, the Perspective Plan 2021 and the SFYP calls for reforms in the education and health administrative systems. The Perspective Plan stipulates that the administration, particularly for secondary and college education, should be decentralised. Also, health sector administration was to be greatly decentralised by delegating greater authority and responsibility at each level.

There was some progress made in terms of introducing performance indicators in the second budget speech. It mentioned that Performance Based Evaluation System had been introduced in the Ministry of Establishment on pilot-basis. The third budget speech indicated that the draft of Civil Service Act was in the process of finalisation and that all ministries/divisions were going to be connected to the budget database through Wide Area Network (WAN) to facilitate better coordination of their activities. The government enacted the Public Servants (Retirement) (Amended) Law in 2012.

Review of Current Status

With a view to putting in place "a modern, efficient, corruption-free and service-oriented public administration," the government has prepared a draft Civil Service Act in connection with which opinion was sought from citizens. The Act is now being finalised to be presented before the Parliament.

Decentralisation of Public Administration

The Perspective Plan 2021 calls for devolution of power, responsibility and financial management to the upazila and other local government tiers for better utilisation of public resources. The SFYP sought to reform the property tax base in order to strengthen the financial autonomy of city corporations and municipalities. The first budget speech mentioned about government's intention about preparing a District Budget by FY2010-11.

The first budget also indicated about transforming all union headquarters into planned rural townships. It also committed to turning upazila headquarters into pourasabhas (municipalities) with modern amenities which are to be developed as planned townships. The first budget speech also talked of decentralising police administration and setting up a Public Representative Board. The second budget mentioned about steps that were being taken to reform upazila parishad legislation and frame its terms of reference. The third budget provided a list of laws which were enacted in reforming the local government structure, namely, the Local Government (Union Parishad) Act 2009, the Local Government (Paurasabha) (Amendment) Act 2010 and Local Government (City Corporation) Act 2009.

Review of Current Status

The government is yet to make any significant impact on reducing the centre-local conflict of interest over public provisions. There has been talk of establishing a National Decentralisation Policy and Decentralisation Commission. A well thought out Decentralisation Policy in this direction may help to put the country on the right track to move forward.

Although the first budget speech had mentioned about decentralisation of the police administration, the Police Reform Act is yet to be finalised and appropriate laws enacted.

It has been suggested that in order to materialise the reforms relating to decentralisation in the SFYP and the Perspective Plan 2021, a pilot programme could be launched to try out two key aspects of decentralisation in education – devolution of authority and resources to local levels involving local government, and devising institutional models with greater academic, management and budgetary responsibility with accountability at the institutional level.

5.3 Priorities for the Next Two Years and Beyond

It needs to be noted and appreciated that not all reforms initiated by the government, necessarily serve the aspirations of the citizens. Some reforms, whilst needed in view of the demands of the changing times, could be designed in a manner that could undermine the interests of the common citizens or do not adequately service the demands medium-to-long term developmental prospects and interests of inclusive growth. The local government reforms and the attendant proposed role of parliament members and local government elected leaders have been contested by many as not going far enough in ensuring actual devolution of power. Many apprehend that the initiative to formulate a new law to guide activities of the NGOs could stifle their freedom if stakeholders' concerns are not appropriately reflected. So the interest, design and implementing modality should remain a point of interest for any assessment of policy initiative.

As the analysis presented in the preceding sections indicate, many of the policy proposals of the government are at various stages of follow-up actions, whilst in respect of others, initiatives are yet to be taken.

There are also some areas where reforms are needed but have not been proposed. Public expenditure is one where reforms are needed to raise its efficacy by tying outcomes to resource allocation and disbursement, but no attempt has been made to tackle the issue. A thorough review and reforms in the subsidy policy could be cited as another area.

In view of the emergent needs of the economy and the necessity to raise the capacity of resource mobilisation and resource use, one would suggest that priority in the next two years of the current government and indeed beyond ought to be given, but not delimited, to the following areas:

Capital market reform: The capital market remains a key area to raise investible resources through raising equity. However, the capital market has experienced significant volatility, malgovernance and insider manipulation in recent times. A number of reforms measures were suggested by the investigation committee and subsequently policymakers as well have come up with a number of proposals including strengthening of the functions of the SEC as a regulatory body, demutualisation in the two exchanges, measures against insider trading, enactment of FRA, etc.

Civil service reform: Another area which appears to be important, particularly in view of the need to raise the quality of public service delivery in Bangladesh, relates to civil service reforms. The Perspective Plan 2021 and the SFYP underlined the importance of reforming the civil service from the perspectives of good governance and sustainable development. It is being increasingly felt that if Bangladesh is to achieve its ambition of double-digit growth rates, the efficacy and effectiveness of government bureaucracy will need to be significantly enhanced. All these require important reforms in the way the government machinery functions. Finalisation of the Civil Service Act, now under consideration, with its provisions of cadre deployment, clustering of ministers, promotion, incentive structure and delegation of authority, is thus seen as another priority area.

Reforms towards decentralised governance: Strengthening local government institutions and actual devolution of power and vesting of greater responsibilities to local authorities will be key to raising the utilisation efficacy of resources and instituting an accountable, participatory and inclusive government. Whilst some initiatives have been taken in this area, some of the key areas of reform including resource mobilisation by local governments, division of responsibilities between various tiers of local government and members of parliament, and exercise of power of local government bodies over developmental projects implemented in their respective areas remain a matter of concern. Reforms in safety net programmes aimed at gradually moving towards a social protection scheme, where local authorities would assume the lead role, should also be perceived as an important area of reforms.

5.4 Conclusion

The aforesaid review of the progress made with regard to government's initiatives in the areas of reform and policy changes indicate that the present government has indeed undertaken a number of the initiatives in the course of three and half years it had been at the helms of power. However, the review of the government's track record in this regard clearly evince that the success of its reform efforts was rather limited owing to a number of factors. *Firstly*, the government's policy and reform efforts failed to address a number of key areas that were crucial to raising the efficacy of developmental efforts in Bangladesh. Some of these were related to reforms in public expenditure, the SoEs, civil service and administration, land reforms, subsidy management. *Secondly*, in areas where reforms and policy initiatives were indeed introduced, the pace of such reforms were rather slow, and where progress were made, these were not supported by other measures which were needed to ensure success of the reforms and to deliver the expected results. For example, the policy initiatives in the areas of PPP and MTBF have attempted to raise resource mobilisation capacity and enhance the quality of resource utilisation. However, the appetite for energetic follow-up activities in terms of undertaking the next steps to take advantage of the initial reforms, had failed to match the expectations of citizens. Consequently, the envisaged results are yet to become visible. *Thirdly*, some of the reforms and policy initiatives, whilst good and necessary on their own rights, have suffered because of apparently conflicting interests of key stakeholders. For example, in spite of reforms and policy initiatives in some of the related areas, real decentralisation and devolution of power have not taken place because issues related to remit of power and responsibilities of various elected representatives (local and at various tiers above) are yet to be addressed in a clear and precise manner leaving room for interpretative ambiguities and tensions. *Fourthly*, in case of some of the proposed policy initiatives and reforms, concerns remain with regard to the preparatory homework that would need to be undertaken for the reforms to be effective. For example, the VAT law, already approved by the cabinet and to be implemented from July 2015, will require substantive preparatory work over the interim period if the desired results are to be achieved. Concerns also remain with regard to continuity of particular reform initiatives across various political regimes. *Fifthly*, some of the policy initiatives, which have been accepted in principle, and remain important from the perspective of good governance, transparency, accountability and efficiency, are not being dealt with the urgency that they deserve. For example, in the area of financial management, the Financial Reporting Act is yet to be drafted although this is the key to bringing transparency and accountability in the capital markets. Also, proposed initiatives towards demutualisation (separation of ownership, management and trading rights at the exchanges) and strengthening of measures in relation to insider trading are making only slow progress. *Sixthly*, opposition from powerful vested interest groups have at times been able to get the upper hand and thwart reform efforts. For example, enactment of appropriate reforms in civil service and other areas have faced resistance from vested groups bent on upholding narrow coterie interests. *Seventhly*, a general criticism with regard to the laws enacted to implement reforms and policy measures has been that some of these were not being done with due diligence. This has led to weak drafts, frequent revisions and amendments of the law, and hence, delayed implementation. Absence of wide-ranging stakeholders' consultation, and in some instances, a lack of the needed drafting capacities in place, has led to a need for repeated amendments of the law. For example, the telecommunication law was enacted in 2006, revised in 2010 and is being further revised now. Same can be said of Union Parishad and Municipality Acts and the Jute Act which had undergone frequent changes. Whilst the need for changing laws in view of the changing demands of time cannot be denied, ensuring the quality of the laws which is crucial to ensuring the expected outcomes, remains a challenge.

The upshot of the above discussion is that, although the present government have taken policy initiatives and reforms in a number of areas, its efforts were undermined by an inability to undertake the needed reforms in some of the key areas and delays and slow progress when it had, with reforms, inability to undertake associated measures to make the reforms more comprehensive and effective, weak preparation and last but not least, effective follow-up efforts. All these have meant that, in spite of its good intentions articulated in various declarations and policy documents, government's reform efforts have stalled. On the other hand, it is becoming increasingly clear that without successful second generation reforms towards good governance, better accountability, higher transparency, higher efficacy of resource mobilisation and better resource utilisation, Bangladesh cannot aspire to have the developmental outcomes which is needed for putting the economy on to a high gear and growth trajectory which is essential to attaining double digit growth rates in the medium-term. In view of this, there is a heightened need for Bangladesh's policymakers to take a serious review of the reform measures and policy initiatives and energetically act on the unfinished agendas in this context. It is hoped that the committee constituted by the Ministry of Finance recently will endeavour to do exactly this.

6. OUTLOOK FOR FY2012-13

Although the economy has clocked a 6.3 per cent GDP growth (provisional estimate) in FY2011-12, the foregoing analysis indicates that, from economic perspective, this had been the weakest of the three years of the present government. This weakness manifested itself in a major way, in continued stagnation, if not fall, in the aggregate investment rate including both its components, viz. public and private. Slowdown in investment had been underpinned by, among others, decreased flow of industrial and agricultural credit, slump in import of capital machineries, decreased industrial use of electricity, negative net flow of FDI and lower flow of IPOs to the capital market. Record low level of ADP implementation as well as foreign aid utilisation has aggravated the situation further. Indeed, the investment targets of the SFYP are increasingly moving out of reach. Thus, the single most important objective for the next fiscal year should be revamping the investment situation with a view to attain the targeted GDP growth rate.

The analysis presented in this paper also reveals that the lax macroeconomic management has been greatly responsible for many of the recent economic woes. This relates particularly to the shabby public resource management. Notwithstanding the steady above-the-trend performance of the NBR, the government could not tap adequately the non-NBR tax and non-tax sources for additional revenue. More importantly, increasing inability to effectively access the committed foreign aid has given rise to a number of serious tensions in financing the development expenditures. Consequently, the government has to greatly lean on the banking sector for additional resources, particularly to meet the unplanned subsidy demand. Accordingly, restoring fiscal discipline would be another major challenge in FY2012-13.

One of the major sources of weaknesses of macroeconomic management in FY2011-12 related to the energy sector. Inadequate understanding about the implications of massive use of RPPs not only created serious destabilisation in the fiscal as well as balance of payments management, it also defeated the very purpose of the initiative, i.e. quick and steady supply of electricity. One definitely needs to revisit this initiative in FY2012-13 so as to limit its negative spillovers on government exchequer, and at the same time, rigorously pursue implementation of the big power generation projects along with attempts to bring more gas supply on stream. However, it seems the government has lost the opportunity to finalise the Coal Policy in its present tenure.

Subsidy management would remain a tricky issue for the government in FY2012-13 as well. By deferring Tk. 10,000 crore of subsidy payment to the upcoming budget and allocating unsustainably low amount for subsidy and transfer, the government has created a built-in destabiliser in the budgetary management. Prudent management of subsidy will continue to be a vexing issue in the upcoming fiscal year.

While the recent MPS has brought in some discipline in the conduct of monetary aggregates, controlling the government's borrowing demand will be the central bank's one of the important pre-occupations. What would be also important for the Bangladesh Bank is to create adequate space for the private sector's access to credit so as to meet the revealed investment demand. One will have to wait for the announcement of the next MPS to understand whether the central bank will seek to undermine economic growth prospect in its bid to control inflation through monetary contraction. From all indications, it seems that inflationary pressure will sustain in the upcoming fiscal year. It is to be seen whether the successive bumper productions of foodgrains along with high level of stock holding is going to bring down the level of food inflation. The fall in global foodgrain price is supposed to facilitate this process. On the other hand, 'cost push' brought about by the expected upward revisions of energy products will possibly enhance the non-food inflation. The government will need to energise its supply-side interventions (beyond safety net programme and open market sales (OMS) of foodgrains) to enable investment and create more jobs to augment purchasing power of the consumers.

One of major tasks for FY2012-13 will be strengthening the balance of payments situation. Along with streamlining the import demand, the government will have to enhance its foreign exchange receipts by getting more export earnings, remittance flow, FDI and most importantly, disbursement of foreign aid. Maintaining a stable exchange rate will be a corollary of this exercise.

Our review maintained that the current employment situation at the aggregate level is not so disconcerting as the investment scenario. However, the need to generate decent jobs with reasonable wages, particularly for the youth, remains another yet-to-fulfil promise of the present government. Arguably, this is about more than sending people abroad and providing temporary employment through safety net programmes. Indeed, this has to do more with the rejuvenation of the investment flow, as mentioned earlier.

The wide ranging reform initiatives espoused by the ruling party and the government are yet to provide necessary support towards accelerating the inclusive growth in the economy. As the government approaches its finishing line, it has to concentrate on a number of some quick-yielding and/or demonstratively visible reform initiatives.

In fine, the government in its fourth year of tenure has to, on the one hand, consolidate its achievements, and on the other, aspire to attain newer heights during its last full fiscal year of the tenure. To that end, it will have to target to keep the economy stable as it strives for higher level of growth. Admittedly, peaceful and predictable socio-political environment can provide one of the most critical pre-requisites for performing such feat.

A SPECIAL NOTE ON CROP PRODUCTION AND FOOD SECURITY

The objective of self-sufficiency in food production requires rice production to grow in a manner that matches the growth in population of the country. No doubt Bangladesh has been successful in adopting new technologies in agriculture including high-yielding varieties (HYVs), chemical fertilisers and irrigation. The track record in terms of foodgrains production has led Bangladesh to attain near self-sufficiency in rice production. However, continued import of foodgrains along with surplus production poses somewhat of a paradox, and has raised questions as regards reliability of relevant data including the actual size of population. Whether the growth record of the recent past years could be sustained in the future and whether Bangladesh has reached a technological frontier, are also questions that are being asked. The issue of long-term food security has thus remained as a concern for the policymakers.

Increase in Aman production in FY2011-12 has been insignificant and this was a concern. Although cultivated area for Aman was down by 1.1 per cent, a somewhat positive growth (albeit of only about 0.05 per cent) in production was achieved, thanks to the productivity growth of about 1.2 per cent. The early estimate of Boro shows a growth of about 0.3 per cent. However, there are indications that actual production of Boro will be higher than the early estimate. Import of foodgrains was low in FY2011-12 compared to earlier years. During July-March FY2011-12, total import of foodgrains was 2.38 million metric tonnes (MT), which was about 44 per cent lower than that of the last year. Since FY2005-06, annual rice consumption has always been lower compared to the net production in Bangladesh indicating a net surplus in availability. According to a CPD estimate, in FY2011-12 a total amount of 5 million MT rice was available as production surplus, which was 5.7 million MT in FY2010-11.

Low coverage, delayed start of government procurement (partly due to lack of storage space) along with relatively low market price in the post-harvest season in FY2011-12, may have created a disincentive for the farmers. The government undertook a number of projects under the ADP to increase storage capacity through construction of new silos. However, thus far, no new storage capacity has been added in the last three years. In this backdrop, a failure to reach the procurement target could push the price of paddy/rice further down, and thereby, could seriously undermine farmer's interest and create disincentive for them.

Upward adjustments of administered prices of such inputs as fertiliser, diesel and electricity and the increasing labour cost were major contributing factors which pushed up the cost of Boro production this year. A CPD field visit survey revealed that, the production cost of Boro was 18 per cent higher this season compared to that of the last year. In the present context, it is quite unlikely that farmers will get the financial return that they were hoping for, and in view of the procurement price and prevailing market prices, farmers could even suffer losses. The government decided to procure 0.9 million MT of rice (at 28 Tk./kg) and 1.5 million MT of paddy (18 Tk./kg) from 3 May which will continue until 30 September. The procurement price of rice (or paddy) is just enough to meet the cost of production. Regrettably, in general, farmers in Bangladesh do not have the capacity to sell their crop directly to the government. As a result, at present, on an average, farmers tend to incur a loss of Tk. 150 per maund (app) of paddy.

Rice price in the international market showed a declining trend since September FY2011-12 in contrast to the upward trend observed during the same period of the last year. With favourable climatic conditions in FY2011-12 in major rice producing countries, India's return as a regular exporter after having lifted the three-year long ban, have played a positive role in this context. Thanks to a good harvest and large carry-over stocks by major importers, world price is expected to decline further in the coming days. In Bangladesh, owing to a good Boro harvest and a comfortable level of stock dependence on import from the international market is likely to be lower this year. This declining trend is already visible in the form of lower import figure.

The issue of subsidy is under the spotlight this year. The indication is that present level of subsidy for agriculture sector will be continued in FY2012-13. In the budget for FY2011-12 about Tk. 4,500 crore was allocated on account of agriculture sector's subsidy. However, the requirement increased to about Tk. 10,000 crore of which Tk. 6,500 crore will be accommodated in the revised budget for FY2011-12, and the rest (Tk. 3,500 crore) will be deferred to the next year's budget. If as reported Tk. 6,000 crore (plus Tk. 3,500 crore) will be allocated as agriculture subsidy for FY2012-13. This would imply that the government in due course has to either enhance the allocation or undertake radical price adjustments of inputs, in case it does not want to go below the FY2011-12 benchmark. To ensure distributional justice and allocative efficiency of the subsidy expenditure, it is important to revise the beneficiary list of the farmers on a regular basis.

Initiatives with regard to rice procurement, including fixation of price, will need to be taken in a timely manner. It is important to accelerate implementation of ADP projects relating to putting in place the new storages facilities. At the same time, community-based storage facilities, to be set up by farmers, could be encouraged. In this regard, capacity building of farmers with regard to maintaining improved storage facilities as well as pursuing better methods of storage, should be given due attention. Special attention should be given towards innovation and promotion of improved salt and submergence-tolerant varieties in the southern districts and also water efficient varieties. Cultivation of high value crops including maize, spices, oilseeds, pulses and orchards in the Northern districts should be encouraged. This is particularly important considering the possible adverse impact of climate change, with attendant implications for agro-practices which calls for a serious rethinking about repositioning of the Bangladesh agriculture in the coming days.

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Appendix

Mapping Matrix on Policy and Reform Initiatives and State of their Implementation

Appendix Table A: Strengthening Economic Management

Perspective Plan 2021	Sixth Five Year Plan	First Budget	Second Budget	Third Budget	Comments
A1. Consolidation of Fiscal Management					
	▪ The government will put in place some key reforms, such as introducing legislation and practices that will enhance the transparency of fiscal operations of the government	▪ Amendments of the Value Added Tax Act, 1991 and its related SROs	▪ Proposal to amendment of the Value Added Tax Act, 1991 and its Rules	▪ VAT and Direct Tax Act to be presented by December 2011	▪ VAT and Direct Tax Act have been drafted. Cabinet approved the law in March 2012. FY2012-13 budget likely to mention its introduction from FY2014-15. However, concerns remain whether the proposed law will have flexibility to address concerns of SMEs and whether the needed institutional capacities will be in place before the law is put into operation
		▪ Amendments of the Customs Act, 1969	▪ Proposal to amend a number of sections of the Customs Act, 1969 to make it up-to-date		▪ Amendments have been made
		▪ Revision of Income Tax Ordinance, 1984	▪ Plan to revise the Income Tax Ordinance, 1984		▪ The revised Ordinance will have a separate chapter dealing with capital flight and address the problems associated with transfer pricing
				▪ Bring all ministries and divisions under the coverage of MTBF	▪ All ministries have been brought under the MTBF. However, the capacity of ministries to perform according to the demands of the MTBF is yet to be strengthened accordingly. This serious lacuna is undermining the utilisation of resources by the respective ministries both in terms of quality

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(Appendix Table A contd.)

Perspective Plan 2021	Sixth Five Year Plan	First Budget	Second Budget	Third Budget	Comments
					and the extent to which resources are being actually implemented ▪ World Bank (2010) has called for budget integration (planning and management processes) for moving the MTBF forward
				▪ Enacted Public Finance and Budget Management Act 2009	▪ Budget Management Act has been effective since 9 July 2009, but it needs to be formalised, alongside introducing a Reform Reporting System
				▪ Presented NBR Modernization Plan 2011-16 ▪ A project named Modernization of VAT Environment (MOVE) to be launched shortly to bring more VAT offices under automation	▪ A number of pilot projects running under the NBR plan
A2. Introducing E-Governance					
▪ The e-governance model will be developed and implemented. It will begin with e-tenders and e-bill payments	▪ The e-governance vision for SFYP is that citizens will be able to receive comprehensive information and conduct most simple transactions with government agencies using ICT			▪ Digital File Tracking System has been introduced on a test basis	▪ Introduction of ASYCUDA and computerisation of Chittagong Customs House; steps to bring local governments under computer network; e-filing of tenders; and income tax returns ▪ The Digital File Tracking System has been introduced. However, till now this has been done only on a test basis
▪ Promoting 'Digital Democracy' and				▪ Approval of National	▪ Science and Technology Development Trust Law, 2011

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(Appendix Table A contd.)

Perspective Plan 2021	Sixth Five Year Plan	First Budget	Second Budget	Third Budget	Comments
'Digital Government'				Information and Communication Technology Policy 2009	
A3. Land Administration and Food Security					
▪ Preparing an integrated programme comprising of food procurement, storage and distribution	▪ Food security to be achieved through implementation of the National Food Policy and its Plan of Action (NFP/POA), alongside the Country Investment Plan (CIP) 2010-2015	▪ To implement National Food Policy Capacity Strengthening Programme		▪ The National Agriculture Policy 2011 will be finalised	▪ The CIP was revised and updated in 2011 ▪ The National Agriculture Policy 2011 and National Food Policy have been formulated and are being implemented
▪ Plan to formulate Land Use Policy	▪ Planned use of land according to Land Zoning Maps	▪ A policy will be in place to integrate *Khas* Land Distribution, Housing, Employment Facilities, *Adarsha Gram* and *Asrayan*	▪ Formulating *Balu Mahal* and Field Management Law 2010	▪ Draft prepared on City Area Planning and Land Use Management Act 2011	▪ No initiative has yet been taken to integrate *Khas* Land Distribution, Housing, Employment Facilities, *Adarsha Gram* and *Asrayan* ▪ Enacted *Balu Mahal* and Field Management Law 2010
	▪ Land records will be computerised and land mutation will be made automatic ▪ Land acquisition act and policy would be rationalised				▪ Passed the Vested Properties Return (Amendment) Bill 2011, although not all demands of the stakeholders were addressed in this bill ▪ Not much headway with regard to digitisation of the land registration system ▪ Land zoning of 21 districts is ongoing and it will be completed by 2013. Land zoning of rest of the 40 districts will need two more years to be completed

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(Appendix Table A contd.)

Perspective Plan 2021	Sixth Five Year Plan	First Budget	Second Budget	Third Budget	Comments
A4. Resource Mobilisation through Public-Private Partrnership (PPP)					
	▪ Under the PPP initiative and the associated investment guideline, the procedures for PPP investment have been streamlined and a new PPP Office established to promote PPP projects	▪ Establish PPP Office	▪ Steps are being taken for the establishment of a PPP Office	▪ Preparing PPP guidelines by incorporating new policies, strategies and procedures	▪ Though the PPP Policy came into effect in 2010, the institutional set up is yet to be completed. Necessary steps need to be taken in order to expedite operation of a full-fledged PPP Office ▪ The government has recently approved three guidelines for PPP projects with Tk. 100 crore funding support
	▪ To strengthen PPP initiative and to attract investment from home and abroad, the Bangladesh Infrastructure Finance Fund (BIFF) has been created			▪ The BIFF has been transformed into a company and the company will commence its investment function in FY2011-12	▪ BIFF commenced but no progress
		▪ Bangladesh Better Business Forum will be reconstituted ▪ The Better Business Forum will continue to function			▪ Bangladesh Better Business Forum was dissolved in 19 August 2010
A5. Managing the Industrialisation Process					
▪ Infrastructural support in the form of establishment of industrial park,	▪ Industrial policy would be made flexible to support investment in	▪ Revisiting the industrial policy	▪ Framed the Bangladesh Economic Zones Act 2010	▪ Economic zones to be established under the Bangladesh	▪ Industrial Policy 2010-2014 approved ▪ The government is implementing the new economic zone regime

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(Appendix Table A contd.)

Perspective Plan 2021	Sixth Five Year Plan	First Budget	Second Budget	Third Budget	Comments
dedicated private sector EPZs and SEZs will be put in place to stimulate industrial growth	lagging regions. Industrial zones would be established in lagging regions with all adequate infrastructural facilities so that entrepreneurs can get benefit from economies of scale		▪ Finalised the draft on Industrial Policy 2010 ▪ Final stage of formulating Competition Act, 2010	Economic Zones Act 2010 ▪ Formulated Compulsory Use of Jute for Packaging Commodities Act, 2010 ▪ The Hazardous Waste and Ship Breaking Waste Management Rules, 2011 will be enacted by the next fiscal year	with support from the World Bank and Department for International Development (DFID) ▪ Private sector keen to establish SEZ under the PPP model ▪ Enacted the Economic Zones Act 2010 ▪ Competition Act awaiting cabinet approval ▪ Ship Breaking and Hazardous Rules 2010 drafted ▪ Hi-Tech Park Authority Law, 2010 enacted
	▪ Reforming the SoEs to cut losses and improve efficiency	▪ A new financial investment institution, dedicated for industrialisation, will be set up in the next fiscal year by merger of the Bangladesh Shilpa Bank and Bangladesh Shilpa Rin Sangstha			▪ The Bangladesh Development Bank Ltd came into effect with the merger of ailing Shilpa Bank and Shilpa Rin Sangstha in 2010
A6. Capital Market Management					
▪ The capital market will be further liberalised, reformed and deepened to create opportunities for raising equity to support industrial sector growth	▪ Capital market reforms to promote private investment, including strengthened surveillance by the SEC will be implemented			▪ In order to separate the ownership, management and trading of stock exchange and to contain manipulation in the capital market, the process of demutualisation in Dhaka and	▪ Regulations related to the SEC and also the Companies Act are currently under review ▪ Initiative of the SEC to increase the number of independent directors in companies is a good move ▪ Slow progress with regard to demutualisation (only a draft concept note has been submitted to MoF)

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Perspective Plan 2021	Sixth Five Year Plan	First Budget	Second Budget	Third Budget	Comments
				Chittagong Stock Exchanges has begun ▪ Steps taken to amend the Securities and Exchange Commission (SEC) Act, different rules and Companies Act	▪ Strengthening of rules related to insider trading is yet to be put in place ▪ National core committee for amending the Companies Act formed in 2011 ▪ The Financial Reporting Act (FRA) is yet to be drafted
	▪ Establishment of a capital market institute	▪ Steps have been taken to establish a capital market institute	▪ Plan adopted to build the Bangladesh Institute of Capital Market		▪ Bangladesh Institute of Capital Market established in December 2010
A7. Developing the Energy Sector					
▪ There must be a deliberate policy of energy conservation	▪ A key policy reform is to ensure proper pricing of power based on a review of good international practices		▪ Use of solar power in National Building Code, install solar panels in government organisations, replace incandescent bulbs with compact fluorescent lamp (CFL) bulbs, and change conventional street lights with lead as well as to solar bulbs	▪ Working to finalise the Sustainable Energy Development Authority Act, 2011	▪ The government has approved a draft law titled Sustainable Renewable Energy Development Authority Act 2011 ▪ Bangladesh Gas Law, 2010 ▪ Power and Energy Fast Supply (Special Provision) Law, 2010
▪ Formulating a long-term policy on electricity and energy		▪ Energy and Coal Policy is nearing finalisation			▪ A National Coal Policy is pending for approval of the parliamentary committee

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(Appendix Table A contd.)

Perspective Plan 2021	Sixth Five Year Plan	First Budget	Second Budget	Third Budget	Comments
A8. Financial Sector Management					
	▪ Bangladesh Bank's Strategic Action Plan 2010-2014 to enhance regulatory and supervisory framework against money laundering	▪ Money Laundering Prevention Act 2009 enacted		▪ To frame Financial Reporting Act ▪ To frame an Audit Act ▪ Steps have been taken to prepare the draft for the amendment of Bank Companies Act and Financial Institutions Act ▪ Enacted Insurance Act 2010 and Insurance Development and Regulatory Authority Act 2010 ▪ To amend Insurance Corporation (Amendment) Act ▪ Reformulated Money Laundering Prevention Act 2009 and Anti-Terrorism Act 2009	▪ The draft Audit Act was submitted to the MoF in 2008. But till now, there has been no headway in finalising the draft ▪ Anti-Money Laundering Law 2012 enacted

Appendix

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Appendix Table A: Strengthening Economic Management

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		▪ Amendments of the Customs Act, 1969	▪ Proposal to amend a number of sections of the Customs Act, 1969 to make it up-to-date		▪ Amendments have been made
		▪ Revision of Income Tax Ordinance, 1984	▪ Plan to revise the Income Tax Ordinance, 1984		▪ The revised Ordinance will have a separate chapter dealing with capital flight and address the problems associated with transfer pricing
				▪ Bring all ministries and divisions under the coverage of MTBF	▪ All ministries have been brought under the MTBF. However, the capacity of ministries to perform according to the demands of the MTBF is yet to be strengthened accordingly. This serious lacuna is undermining the utilisation of resources by the respective ministries both in terms of quality

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Perspective Plan 2021	Sixth Five Year Plan	First Budget	Second Budget	Third Budget	Comments
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				▪ Enacted Public Finance and Budget Management Act 2009	▪ Budget Management Act has been effective since 9 July 2009, but it needs to be formalised, alongside introducing a Reform Reporting System
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A2. Introducing E-Governance					
▪ The e-governance model will be developed and implemented. It will begin with e-tenders and e-bill payments	▪ The e-governance vision for SFYP is that citizens will be able to receive comprehensive information and conduct most simple transactions with government agencies using ICT			▪ Digital File Tracking System has been introduced on a test basis	▪ Introduction of ASYCUDA and computerisation of Chittagong Customs House; steps to bring local governments under computer network; e-filing of tenders; and income tax returns ▪ The Digital File Tracking System has been introduced. However, till now this has been done only on a test basis
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Perspective Plan 2021	Sixth Five Year Plan	First Budget	Second Budget	Third Budget	Comments
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▪ The capital market will be further liberalised, reformed and deepened to create opportunities for raising equity to support industrial sector growth	▪ Capital market reforms to promote private investment, including strengthened surveillance by the SEC will be implemented			▪ In order to separate the ownership, management and trading of stock exchange and to contain manipulation in the capital market, the process of demutualisation in Dhaka and	▪ Regulations related to the SEC and also the Companies Act are currently under review ▪ Initiative of the SEC to increase the number of independent directors in companies is a good move ▪ Slow progress with regard to demutualisation (only a draft concept note has been submitted to MoF)

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▪ There must be a deliberate policy of energy conservation	▪ A key policy reform is to ensure proper pricing of power based on a review of good international practices		▪ Use of solar power in National Building Code, install solar panels in government organisations, replace incandescent bulbs with compact fluorescent lamp (CFL) bulbs, and change conventional street lights with lead as well as to solar bulbs	▪ Working to finalise the Sustainable Energy Development Authority Act, 2011	▪ The government has approved a draft law titled Sustainable Renewable Energy Development Authority Act 2011 ▪ Bangladesh Gas Law, 2010 ▪ Power and Energy Fast Supply (Special Provision) Law, 2010
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Appendix Table B: Improving Governance, Accountability and Transparency

Perspective Plan 2021	Sixth Five Year Plan	First Budget	Second Budget	Third Budget	Comments
B1. Establishing the Institution of Ombudsman					
▪ The post of Ombudsman should be filled and the incumbent provided full scope to function effectively and independently	▪ Appointment of an Ombudsman with sufficient staff as guaranteed by the Article 77 of the Constitution				▪ Tax Ombudsman appointed in 2005 but no provision made for the Ombudsman envisaged under the Constitution ▪ In late 2009, some indications were made but not followed up later ▪ Tax Ombudsman (Avoidance) Law 2011 ▪ National Human Rights Commission Law, 2009 ▪ Right to Information Act, 2009 ▪ Establishing Divisional Ombudsmen
B2. Strengthening the Anti-Corruption Commission (ACC)					
▪ The ACC should function with constitutional guarantees for its powers, free of any constraint by the executive and lower judiciary	▪ The ACC will be put on a more sustainable footing by providing it with clear independence to carry out investigations and prosecute, but with high levels of accountability to other public authorities to ensure that its actions are unbiased and in the public interest	▪ Proposed some amendments to the Anti-Corruption Commission Act		▪ The proposed amendments will address the loopholes in the existing Anti-Corruption Commission Act	▪ ACC Act amendment underway ▪ Public Interest Related Information Disclosure (Protection) Law, 2011
B3. Institutions to Promote Reforms					
▪ A permanent Pay, Services and Regulatory Reforms					▪ Similar to the Bangaldesh Better Business Forum, the Regulatory Reforms Commission has

(Appendix Table B contd.)

(Appendix Table B contd.)

Perspective Plan 2021	Sixth Five Year Plan	First Budget	Second Budget	Third Budget	Comments
Commission should be set up					disappeared from the political radar ▪ A committee has been constituted in May 2012 to undertake a review of the progress with regard to reform proposals in various documents
▪ Establishment of a Perspective Plan Management Office at the Planning Commission may be envisaged to coordinate the execution of the Plan					▪ No progress made
▪ An Independent Vision 2021 Council will be created to continuously refine the Vision 2021 and the Perspective Plan and track progress in an objective manner					▪ No progress made

Appendix Table C: Raising the Efficacy of Development Administration

Perspective Plan 2021	Sixth Five Year Plan	First Budget	Second Budget	Third Budget	Comments
C1. Raising the Efficacy of Public Administration					
▪ A composite set of Agency Performance Indicators will be initiated for ministries and agencies to facilitate public disclosure of performance data for each and every agency	▪ Formulations of the Civil Service Act and the Public Administration Reform Road Map (2010-2014) underway		▪ Performance Based Evaluation System has been introduced in the Ministry of Establishment on pilot-basis	▪ The draft of Civil Service Act is in the process of finalisation ▪ All ministries/ divisions will be connected to the budget database through WAN	▪ Ministry of Public Administration sought public opinion over the draft in May 2011 ▪ Public Service Act now being finalised to be presented before the parliament
C2. Decentralisation of Public Administration					
▪ Devolution of power, responsibility and financial management to the upazila and other local government tiers are necessary	▪ Property tax base will be reformed to strengthen the financial autonomy of city corporations and municipalities	▪ Hope to present district-level budget in the national budget for FY2010-11 to increase transparency and accountability ▪ All union headquarters will be turned into planned rural townships ▪ All upazila headquarters and flourishing centres of trade and industry will be converted into pourasabhas (municipalities) with modern amenities and will also be developed	▪ Steps have been taken to reform upazila parishad legislations and frame its terms of reference	▪ Formulated the Local Government (Union Parishad) Act 2009, Local Government (Pourasabha) (Amendment) Act 2010, and Local Government (City Corporation) Act 2009	▪ Preparing a National Decentralization Policy and Decentralization Commission ▪ A well thought out Decentralization Policy and subsequent reformulation of an umbrella law in this direction may help to put the country on the right track to move forward

(Appendix Table C contd.)

(Appendix Table C contd.)

Perspective Plan 2021	Sixth Five Year Plan	First Budget	Second Budget	Third Budget	Comments
		as the planned townships			
▪ The administration, particularly for secondary and college education, will be decentralised	▪ Decentralisation of Directorate of Secondary and Higher Education ▪ Reform of existing examination systems in secondary level education				▪ A pilot programme may be launched under the SFYP to try out two key aspects of decentralisation in education – devolution of authority and resources to local levels involving local government, and devising institutional models with greater academic, management and budgetary responsibilities with accountability placed at the institutional level
▪ Health sector administration to be decentralised by delegating greater authority and responsibility at each level					▪ Progress yet to be made
		▪ Decentralising police administration and setting up a Public Representative Board			▪ Draft Police Reform Act prepared; yet to get approval of cabinet

Annex

A Set of Proposals for the National Budget FY2012-13*

*This set of proposals was released to the media by the Centre for Policy Dialogue (CPD) on 7 May 2012.

1. THE MACROECONOMIC FRAMEWORK

Bangladesh economy entered into a difficult period from the perspective of macroeconomic management in FY2011-12. The fiscal management came under serious pressure due to unprecedented rise in subsidy requirement. Conversely, the expenditures under the Annual Development Programme (ADP) remained lacklustre. The growth in revenue collection failed to keep pace with the incremental growth of public expenditures. Although the size of the fiscal deficit may remain in the safe zone due to a possible cut of development expenditure, its financing emerged as a major concern. Throughout the fiscal year, borrowing from banking system remained the only reliable source of financing budget deficit. The economy continued to experience inflationary pressure, for both food and non-food items, and the contractionary monetary stance of the central bank made a little impact. The deteriorating balance of payment situation has contributed to depreciation of the domestic currency, adding further tension in the price situation. The investment scenario, as well as the economic growth prospect, has also suffered a setback in FY2011-12.

The national budget for FY2012-13, to be announced on 7 June 2012, will be the penultimate budget of this government's present tenure. As a matter of fact, this is the last national budget which will be completely implemented during the present government regime. In the backdrop of present macroeconomic scenario and political realities, the design of the forthcoming national budget is under the spotlight. The government is at a stage where it may have to choose among a number of alternatives. The forthcoming budget may try to restore macroeconomic stability at the cost of economic growth. Alternatively, it may try to promote structural reforms to make a qualitative difference in economic governance for achieving higher level of inclusive growth. Or, even in the face of the growing adverse circumstances, the budget may resort to a set of populist measures that have little significance for strengthening growth fundamentals of the economy. Regrettably, at present the government has very little policy spaces to consolidate these alternative choices.

1.1 Structure of the Budget

- The indications received thus far suggest that the size of the budget (or its expenditure side) will be about Tk. 190,000 crore (16.1 per cent higher than the budget for FY2011-12). As a share of the gross domestic product (GDP), the size of the public expenditure thus may not change to any significant margin.

- The total size of public expenditure is experiencing a significant increase in FY2011-12 due to substantial rise in subsidy payments. The estimation of subsidy requirement had serious miscalculatation in its initial submission; and it became clear within three months of placement of the national budget for FY2011-12 that subsidy estimates were severely underestimated. Accordingly, on 13 September 2011, a revised estimate of subsidy requirement was prepared which revealed that the actual requirement was almost 2.75 times higher than the original budget figure, Tk. 47,385 crore as against Tk. 17,261 crore. An amount of Tk. 4,500 crore was allocated for the current fiscal year for agriculture, but the figure is expected to reach up to Tk. 10,000 crore in the revised budget. In course of the fiscal year the government revised the administered prices of fuel and power a number of times to reduce the subsidy burden. The government has already issued bonds worth Tk. 2,700 crore for the Bangladesh Petroleum Corporation (BPC) to clear its liabilities with the state-owned commercial banks. The total subsidy bill on various accounts for the current fiscal will be Tk. 40,000 crore, of which Tk. 29,000 crore will be provided from the current fiscal year's budget, and the rest will be carried forward to the next fiscal year. Hence the forthcoming budget will not only have to cater its own requirement, but will also have to carry this year's burden. While the government is expected to release the revised figures regarding subsidy allocation for FY2011-12, the composition and actual allocation of subsidy requirement for the forthcoming fiscal year also needs to be released. The Finance Minister has already announced his plan to reduce subsidy expenditure in FY2012-13. Indeed if the government complies with the conditionality of the Extended Credit Facility (ECF) offered by the International Monetary Fund (IMF), an automatic adjustment mechanism for retail petroleum prices will be adopted to ensure full pass-through of international prices by December 2012. If this will be the case, a serious implication can be expected on cost of production and commodity price levels. In this context, a detailed disclosure of information regarding the estimated requirement and subsidy policy are warranted in the forthcoming budget.

- ADP for FY2012-13 may be around Tk. 54,300 crore, of which only 36.9 per cent will be financed from the project aid. In FY2011-12 the share of project aid in original ADP was 40.6 per cent which may come down to 36.6 per cent in the Revised ADP (RADP). It implies that the reliance on domestic sources for ADP financing may continue in the coming fiscal year. The expenditures in productive sectors as envisaged under the ADP, thus far, have not shown any breakthrough in terms of either quantity or quality. Hence, the implementation capacity of the government needs to be improved significantly to achieve the goal.

- Project-wise action plans should be prepared for timely completion of all the ongoing projects. To start with, the government may put emphasis on preparing action plans for a number of important projects. Power and infrastructural projects should get the highest priority while preparing the list. These action plans should be prepared by the respective project authorities and be approved by the head of their implementing agencies.

- The revenue mobilisation target for the National Board of Revenue (NBR) may be set at Tk. 112,350 crore which is 22.3 per cent higher than the target for FY2011-12. The revenue collection trend during the first three quarters of this fiscal year suggests that NBR may surpass its collection target for the second consecutive year in FY2011-12. Considering the recent performance of NBR, changes in tax structure and ongoing reforms according to the modernisation plan for NBR, the target for FY2012-13 may be achievable. On the other hand, non-tax revenue in FY2011-12 has been blessed with spectrum fee from the telecom companies, which augmented around Tk. 4,000 crore for the national exchequer. To receive a similar boost this year under the non-tax revenue, the licensing process of 3G for telecom industry needs to be expedited.

- The economy is growing but the government assets are not paying enough returns. There is a need to revisit decades old government rates including the various fees, rents, stamp duties, etc. Public properties including land and waterbodies should be leased in a competitive manner to tap potential revenue.

- Performance of dividend and profit from state-owned enterprises (SoEs) is also below par. The efficiency of public enterprises needs to be revamped particularly considering government's decision in favour of any new privatisation effort. A more comprehensive plan needs to be in place in order to estimate the reinvestment requirement for these enterprises and give a clear indication to the prospective private investors.

- The budget deficit is expected to be within 5 per cent of GDP. Although the size of the fiscal deficit remains in the safe zone, its financing is emerging as a major concern. The government, in the face of low offtake of committed foreign aid, has been resorting to heavy borrowing from the banking sector. Under the revised target, the government may borrow about Tk. 27,900 crore from the banking system against the original budgetary target of Tk. 18,957 crore in FY2011-12. The government needs to reduce its dependence on banking system for its budget deficit financing in next fiscal year. The much delayed upward revision of the yield rates of the National Savings Bond (NSD) certificates did not lead to any major improvement of non-bank financing of the fiscal deficit. The government has also sought budgetary support of USD 300 million from the Asian Development Bank (ADB). To maintain macroeconomic balance, the government will have to intensify mobilising foreign resources to finance its budget deficit.

- Coordination among relevant parts of the government coupled with policy leadership by the Ministry of Finance (MoF) is required for effective macroeconomic management and implementation of economy-wide policies.

2. GENERAL FISCAL MEASURES

2.1 Value Added Tax (VAT)

- The proposed *Value Added Tax (VAT) Act 2012* is a positive initiative. The Act is expected to improve VAT collection through enhanced efficacy and higher transparency. It is expected that the new VAT Act will be passed by the parliament during this budget session and will come into force in July 2015. The new VAT Act is likely to introduce a single VAT rate of 15 per cent for all products. In this connection, the government may consider keeping provisions for differentiated rates for strategic interventions in the economy. At the same time, appropriate preparatory measures should be undertaken well in advance, before implementing the VAT Act. The Act itself should be implemented in a phased manner.

- Unification of tax administration is necessary in order to avoid duplication, harassment, reduce corruption and improve transparency and efficiency in the process of tax collection. This requires a modern information technology (IT)-based tax administration which will have online integration of the various components including the VAT, income tax and customs duty departments.

- Evasion of customs duty could be reduced significantly if data on revenue collection could be passed on to the NBR monitoring cell on a regular basis through online network between the customs points and the NBR. The forthcoming budget for FY2012-13 should allocate funds to digitise all the customs points.

2.2 Income Tax

- Given the inflation fixation of last year, the level of tax-free income rates deserves a review and revisiting. Thus, tax exemption limit may be revised upward to Tk. 200,000 for individuals (from Tk. 180,000), Tk. 220,000 for female assessees (from Tk. 200,000) and Tk. 275,000 for assessees with disability (from Tk. 250,000) considering the current high rate of inflation in the economy. The minimum threshold of tax could be raised to Tk. 2,500 at the same time (from Tk. 2,000).

2.3 Transfer Pricing

- The government is considering to introduce a separate chapter in the present *Income Tax Ordinance 1984* to deal with the issue of transfer pricing. This is a welcome initiative. According to estimates made in a recent UNDP study, Bangladesh loses equivalent of USD 1.8 billion per year due to transfer mispricing.

- It is good to note that the Ministry has created a position for looking at the issues of transfer pricing and money laundering. Additionally, NBR has created a Transfer Pricing and Anti Money Laundering Cell/Task Force. Allocation of required funds and building the needed expert human resources should be prioritised in the forthcoming budget.

- Recent incidents suggested, in addition to transfer mispricing and trade mispricing, misdeclaration of imported products is also causing substantive revenue losses. NBR needs to be strengthened to avoid these losses.

- The consolidated direct tax law is a welcome step since the present tax measures are being implemented on the basis of the 1984 Ordinance. The proposed Draft Direct Tax Act provides opportunities for transfer pricing legislation, but misses some essential components of a standard legislation. A recent CPD study identified a number of missing components, and cited the example of the Direct Tax Code of India with a view to designing a comprehensive Act (Annex Box 1). In addition to the changes in the present ordinance, the forthcoming Direct Tax Act needs to accommodate transfer pricing provisions.

Annex Box 1

Suggestions for Inclusion in the Proposed Direct Tax Act 2012

Area of Transfer Pricing Legislation	Related Sections of Direct Tax Code, India	Related Sections of Draft Direct Tax Act, Bangladesh
Scope	105, 106	202, 203
Definition of terms	113	missing
Reference to transfer pricing officer	130, 284	missing
Transfer pricing documentation	83	missing
Furnishing information/filing	149	missing
Administrative procedures	160	missing
Assessment procedure	162	missing
Penal provision	226	missing

Source: Rahman *et al.* (2011).[1]

2.4 Legalisation of Undisclosed Income

- NBR has already expressed its intention to offer opportunity to legalise undisclosed income provided a payment of 10 per cent tax is made. This proposal may have been considered in light of the stagnated investment environment and with a view to attracting new money for investment purposes. However, this runs counter to the principle of rewarding conscientious taxpayers and punishing tax evaders and people with undisclosed income. At the same time, one would recall that such initiatives in the past had little success in mobilising additional revenues and in attracting investment. If at all, income may be allowed only with payment of a certain percentage of additional tax as a penalty.

3. AGRICULTURE AND FOOD SECURITY

3.1 Crop

- There is no doubt that input subsidies and price support schemes put pressure on government's fiscal expenses; on the other hand, rationalisation of related administered prices and cash subsidies is likely to raise production cost for the farmers. It has been assured from the top policy making body that subsidising agricultural production (particularly foodgrain production) will be continued in FY2012-13.

[1]Rahman, M., Ahmed, M.S. and Khan, T.I. 2011. *Adopting Transfer Pricing Regime in Bangladesh: Rationale and the Needed Initiatives.* CPD Working Paper No. 94. Dhaka: Centre for Policy Dialogue (CPD).

It is important that the Finance Division undertakes a comprehensive study to assess the impact, distributional justice, distribution of allocation within the sector (for different inputs including fertiliser and irrigation, and for price subsidy of output) and currently practiced distributional mechanism relating to the subsidies given in the agriculture sector. The study will be able to guide the future subsidy policy of the government with a view to raising allocative efficiency.

- Evidence suggests that Bangladesh has been successful in adopting new technologies in agriculture including high-yielding varieties (HYV), chemical fertilisers and irrigation. Technological diffusion is also warranted to support crop production in unfavourable zones (including submersible, flood-prone and drought-prone areas). In this context, special allocation should be made to innovate and promote improved salt and submergence-tolerant varieties in the southern districts, and water efficient varieties and other high-value crops including maize, spices, oilseeds, pulses and orchards in the northern districts. This is particularly pertinent because of the adverse impact of climate change and its possible implications for agro-practices.

- For ensuring fair price both at the consumer and at the farmers' levels, funds should be allocated for strengthening the Department of Agricultural Marketing (DAM) to provide improved marketing services such as ensuring fair returns to the growers, improving market condition, reducing cost of marketing and ensuring fair market practices. In this regard, to attain the Sixth Five Year Plan (SFYP) targets, funds should be allocated for setting up an Agricultural Price Commission, under the umbrella of DAM, to forecast price of agricultural commodities.

- Till now, crop insurance, planned to be initiated on a pilot basis in a number of upazilas to protect farmers from shocks, was able to make only insignificant progress. This initiative should be given due priority and other sub-sectors such as poultry, livestock and fisheries should also be brought under its ambit. Appropriate funds need to be allocated for this.

- More funds should be allocated for research on improved variety of seeds for wheat and jute, to identify international market opportunities and to examine emerging consumer preferences. In this regard, research organisations such as Bangladesh Agriculture Research Institute (BARI) should be further strengthened through higher allocation to enable it to undertake research and coordinate the related activities.

- Low disbursement of farm credit could result in harming the cause of ensuring food security in the medium-term, and could adversely affect farm productivity. Unutilised funds should be disbursed to support small infrastructure facilities in the agriculture sector. Funds should also be allocated to support the increasing cost of doing business in the thrust sectors with the help of microfinance institutions.

- Construction of cold storages for potato and potato seeds in the bumper producing areas should be given priority. To encourage community-based storage, fund should be allocated for training and technical assistance to the farmers to implement improved methods of storage.

- To encourage export of agricultural commodities, crop diversification should be one of the major prioritised areas for allocation. Women farmers can be targeted for high-value production such as fruits, vegetables, oilseeds, legumes and spices which have export potentials with appropriate training on insect and pest management. Loans may be offered to those who also want to graduate into commercial farming to support the supply chain of export-oriented industries.

- Overexploitation of ground water for irrigation of Boro rice farming has led to overshooting of the capacity of annual recharge of aquifers causing rapid depletion in the ground water level. In this regard, funds should be allocated for re-excavation of canals and ditches to increase the navigability and also for renovation of dams to hold the surface water to be used for irrigation purpose.

- Discrepancies in the data provided by Department of Agricultural Extension (DAE) and Bangladesh Bureau of Statistics (BBS), particularly for minor crops, create confusion for researchers and policymakers. Valid methodology will need to be developed by these institutions to service the requirements at field and monitoring levels. Funds should be allocated to enhance the strength and capacity of these organisations.

- Integrated research fund, with the support of major donors, should be allocated for new projects such as *Support to Research for Climate Change Adaptation in Bangladesh* for developing and disseminating successful indigenous technologies among the coastal farmers to develop their capacity to adapt to the changing situation originating from climate change.

3.2 Livestock and Poultry

- At present income from poultry is exempted from tax up to 30 June 2013, subject to investing at least 10 per cent of the exempted income that exceeds Tk. 150,000, in government securities or bonds. Because of spread of avian influenza virus attack, a large number of poultry farms had to be shut down. The tax exemption may be extended up to 2015 for helping the revival of this sub-sector. Poultry feed mills may be considered for inclusion in tax exemption list along with poultry farms. Credit may be offered to bird flu affected farms at a concession rate.

- At present bird flu detection kits are not allowed to be used at farm-level. Farms should be allowed to use these kits and duty on this item should be waived off, so that avian influenza can be detected as early as possible at the farm-level. Funds should be allocated to Department of Livestock Services (DLS) for undertaking training of poultry farmers in the use of the detection kit. Along with these, government should allow zero duty on medicines and vaccines used in poultry, livestock and fisheries sector.

- To encourage local producers, existing 25 per cent custom duty on import of chicks and eggs should be continued.

- Maize is one of the important elements for poultry feed. Current 5 per cent advance tax on maize import may be considered for elimination.

- Due to the scarcity of grazing land, the area devoted to fodder cultivation for livestock is rather insignificant at present. The problem of feed shortage will be more acute in the coming days unless steps are taken to increase the fodder supply. More funds will be required for research to develop feed technologies and improve the extension services to transfer germplasm to farmers. In this regard, Bangladesh Livestock Research Institute (BLRI) and DLS will need to be further strengthened.

3.3 Fisheries

- Strengthening of fish preservation, processing and marketing infrastructure needs due consideration. Capacity of Bangladesh Fisheries Development Corporation needs to be enhanced further to preserve and process fish during harvesting season which is to be marketed during lean period.

- Export-oriented shrimp farms should receive technical support and training for detecting waterborne virus outbreak. This will prevent huge loss suffered by the farms due to lack of timely detection of diseases. Funds should be allocated for training of shrimp farmers.

- Due to the alarming level of pollution of the open waterbodies in Bangladesh, ecosystem of the rivers, canals and ditches are now under great risk. Urgent actions are needed in this context. Establishing industrial waste treatment plant should be made mandatory and pollution tax should be imposed on violators to address this problem.

3.4 Agro-based Industries

- Seasonal surpluses of perishable items demand that agro-processing industries be developed in adequate number to prevent post-harvest losses and ensure farmers' profitable return. Agro-processing units based on domestic production of potato, tomato, vegetables and fruits should get cash incentive to encourage them to go for export. All exportable agricultural products can be given a unique number to identify the origin of the product and its grower to ensure modern agricultural practice. This number will be helpful to ensure compliance requirement, particularly when the products go to export market.

- Government has recently lifted the three years ban from aromatic rice export in view of the good stock and taking into cognisance its export potential in the markets of United States of America (USA), England, Italy and Saudi Arab. Number of specialised aromatic rice mills in Bangladesh is very few. Large scale specialised mills such as rubber roller mills in the bumper producing areas may help to increase production of export quality rice. Private entrepreneurs should be encouraged to do this through availability of credit.

- The existing 3 per cent customs duty on capital machineries used by the agro-processing industries may be considered for waiver to promote establishment of these industries.

4. INDUSTRY

FY2012-13 will be a challenging time for the industrial sector in view of the ongoing developments which are likely to continue over the next year (e.g. uncertainties in the global economy and the recession and its likelihood in many OECD (Organisation for Economic Co-operation and Development) countries; tightening credit market with high interest rate; high inflation; excessive government borrowing from the banking sector; devaluation of Bangladeshi Taka (BDT) against United States Dollar (USD); contractionary monetary policy). Furthermore, emergence of new issues and concerns has also added to these emergent challenges (rising political instability is one). National budget for FY2012-13 should take specific fiscal and budgetary measures to help address these tasks and stimulate the industrial sector.

It is hoped that the Finance Minister will announce the framework for a Comprehensive Trade Policy in the National Budget 2012-13 as the present trade policies (export policy, import policy order) are going to expire in June 2012. In order to seize new opportunities emerging in the domestic and global markets in addition to addressing the existing challenges, there is a strong rationale to enact a Strategic Trade Policy for Bangladesh. The new trade policy should highlight the following issues: putting in place trade supportive macro policies; ensuring better governance of trade-related activities; improving business processes; undertaking initiatives for product and market diversification; strengthening linkages with global value chains; strengthening trade-investment linkages through promotion of foreign direct investment (FDI); improving trade facilitation; ensuring better trade diplomacy; enhancing the capacity and efficiency of trade institutions; and addressing new issues related to trade.

The announcement of fiscal and budgetary measures in the national budget for FY2012-13 targeted to different manufacturing and services sectors should take into account the ongoing and emergent issues and concerns.

4.1 Readymade Garments (RMG), Textiles and Leather

- Allocation of necessary funds for speedier completion of the *Garments Palli* project is required. Establishment of this *Palli* will help to set up new state-of-the-art factories and also to relocate factories from the Dhaka city.

- Government may consider allocation of fund for setting up dormitories for industrial workers in major industrial clusters of Dhaka, Gazipur, Savar, Narayanganj and Chittagong.

- In view of rising cost of living due to high inflation, government should reintroduce operation of food rationing facilities for industrial workers in major industrial clusters. In this context, discussion for the revision of minimum wage for industrial workers may need to be initiated in the next year.

- In view of the difficulties faced by the backward linkage textile industries and to help these maintain their competitiveness against imported fabrics, this industry may need to be supported. Reduction of VAT on certain utility items may be considered in this context.

- Establishment of *Leather Industry City* remains well behind the stipulated timeline. Development works for this project should be expedited with adequate allocation of funds in the next budget.

- In order to reduce industrial pollution, government should allocate adequate funds to the concerned authorities (i.e. Ministry of Environment) to strengthen their monitoring and law enforcement activities.

4.2 Jute

- Government may consider establishment of a *Technology Upgradation Fund (TUF)* to support productivity increasing and efficiency enhancing efforts in the jute manufacturing sector. The proposed fund will help enterprises to undertake restructuring and reform initiatives and access loans at reduced rate. Indian jute and textile mills are benefitting from this type of fund.

- In order to create skilled workforce in the jute manufacturing sector, adequate budgetary allocation is required for the establishment of a *Skill Development Fund* which could be used to train workers.

- In order to reduce ambiguity between jute and textile sectors, machineries and spare parts used in the jute mills should have separate Hermonised Systemed (HS) codes which are at present put under the same HS codes that are applied for textiles sector.

- Improvement of quality of jute seeds and jute fibre are considered to be one of the major factors for better productivity and product quality. Government should consider increased budgetary allocation for research and development (R&D) activities in the jute sector. Dedicated efforts are also needed to take forward Bangladesh's achievements in decoding the jute plant draft genome.

- Government should consider jute manufacturing industry as agro-based industry which has been recommended by the Jute Commission.

4.3 Ship-Building Industry

- Buyers operating in the ship-building sector prefer to provide Payment Guarantee to the manufacturers which is endorsed/reconfirmed by international banks. Such a practice raises manufacturers' cost burden due to payment of charges both to local and international banks. Bangladesh Bank should explore the possibility to introduce alternate mechanism for endorsement of Payment Guarantee in order to reduce the cost imposed on the manufacturers.

- Government should take initiative to formulate a policy for the ship-building sector with a view to provide future policy directions to the entrepreneurs.

- There should be a special zone for the ship-building industry with adequate infrastructural and logistic facilities.

4.4 Pharmaceuticals

- Establishment of the Active Pharmaceutical Ingredient (API) Park has fallen behind the projected timeline (31 December 2011). Since about half of the development work is yet to be completed, necessary allocation of fund for the project and its speedy implementation are urgently needed.

- Appropriate storage facilities in the form of temperature controlled area for life saving drugs and vaccines should be set up at country's international airports.

4.5 Small and Medium Enterprise (SME)

- Allocation for the Equity Entrepreneurship Fund (EEF) needs to be increased in order to expand its coverage beyond the existing sectors (e.g. agro, agro-processing, information and communication technology (ICT), silk, flowers and herbs) to cover other potential labour-intensive sectors (e.g. light engineering, plastic, melamine and electronics).

- At present import duty on capital machineries is zero for 100 per cent export-oriented industries, but 3 per cent for other industries. Domestic market-oriented industries will be benefitted if this rate is reduced, perhaps to 1 per cent.

- Finance Minister may like to continue with the commitment to attain the target of 15 per cent of SME loans to be disbursed to women entrepreneurs, as was set out in the *Industrial Policy 2010*.

- In order to provide better financial access to SMEs, government may take the initiative to launch flexible loan sanction policy for SMEs under the authority of the Bangladesh Bank.

4.6 Light Engineering

- Government should take initiative to set up a separate industrial park for the light engineering industries. This has been a longstanding demand of the entrepreneurs. This park could be established under the public-private partnership (PPP) arrangement.

- In order to be competitive, local manufacturers should put more focus on R&D, machinery upgradation and skill development activities. As in India (Opportunities Venture Fund), a special fund could be introduced in this regard to provide low interest credit facility to the manufacturers.

4.7 Information and Communication Technology (ICT)

- Completion of some of the important ICT projects are well behind the stipulated timeline including *Establishment of SASEC Information Highway* and *Hi-tech Park at Kaliakair*. Adequate allocation of fund and speedier implementation of these projects are urgently required.

- In order to ensure wider accessibility, VAT charged over the use of internet service (15 per cent) could be reduced.

- Import duty on computer parts and accessories that are mostly used in academic institutions, such as connecting cables, cooling fan, webcam, CD/DVDs, multimedia projectors, etc. could be reduced to zero.

- NBR should consult the stakeholders to resolve the ambiguity in the HS codes applicable for computer accessories. Necessary initiatives should be taken in this regard.

- A separate VAT code could be useful for IT and IT-enabled services. NBR should take initiative in this regard.

- Efforts should be made to set up a separate ICT Authority and ICT Development Fund as per the *ICT Policy 2009*.

- A PPP model should be used to introduce 3G in Bangladesh. 3G data solution will also promote other areas of development such as remote healthcare.

- The government should give more attention to developing the software industry, in particular where investors and institutions can collaborate to support needs of the industry.

- Incentives should be given to non-resident Bangladeshis (NRBs) to invest in the country's ICT sector. Bangladesh Bank has also called for the establishment of a fund for research on banking sector software and security system.

- The government should establish training centres for computer literacy to strengthen human resource for the ICT sector. On that note, the recent release of the locally manufactured Doel laptop by state-owned Telephone Shilpa Sangstha (TSS) is commendable. Government assistance to TSS in diversifying its product is recommended.

4.8 Real Estate

- In the face of the ongoing slump in the housing sector, government may put directives for reinstating 'housing loan' at low interest rate for individual buyers buying homes, particularly in peripheral areas/in the outskirts of the Dhaka city.

- Import of safety equipments such as fire alarm, fire extinguisher, etc. should be allowed without any duty.

4.9 Capital Market

- Submission of Tax Identification Number (TIN) should be made mandatory for all Beneficiary Owner (BO) accountholders in the capital market in order to bring transparency in the transactions as well as to ensure proper reporting of earnings from the secondary market trading in individual's tax return.

- Introduction of capital gain tax on individual accountholders should be taken into consideration in order to discourage short-term trading activities.

- Government may consider issuance of Infrastructure Bond in order to support big infrastructure projects with the provision for participation of foreign investors.

- In order to modernise the operation of the Securities and Exchange Commission (SEC) by strengthening human resources and improving technical capacities, necessary allocation of fund is required for the organisation, both under revenue and development budgets.

- The Finance Minister should announce specific timeline for preparation and enactment of important bills (Financial Reporting Act, Controlling the Insider Trading and Demutualization of Stock Exchanges). Enactment of these bills is important in order to improve the governance in the capital market.

5. ENERGY AND POWER

- In view of the ongoing power crisis in Bangladesh, the government should place greater importance on medium (100-200 MW) and large (500 MW) base load power plants in lieu of smaller oil-based rental and quick rental power plants (RPPs) to reduce the huge subsidy burden and to secure long-term power supply.

- To achieve the target proposed in the *Power System Master Plan 2010* timely, there is a need to initiate more coal-based power plants instead of gas or oil-based ones. The Coal Policy needs to be finalised on an urgent basis.

- Aged power plants lose generation capacity and efficiency over time. Accordingly, adequate allocation for regular upgrading and renovation of aged power plants is necessary for generating maximum capacity from the existing plants.

- To secure long-term energy security, cross-border electricity trade would be an option; but power pricing, transmission and distribution mechanisms require more effective methods and efficient technologies. Regional energy cooperation could be an important strategy in this context.

- Rationalisation policy of power tariff at end-user level should be adjusted, keeping in mind the consequences of power tariffs on the economy and at consumer levels.

- Rural electrification should be enhanced through various alternative energy technology, i.e. bio gas.

- Adequate budgetary allocation is necessary for building capacity of the Bangladesh Petroleum Exploration & Production Company Limited (BAPEX) to carry out onshore gas exploration (old and new fields) and to conduct seismic surveys (2D and 3D) in order to meet the increasing demand.

- As the price of liquefied petroleum gas (LPG) is higher than fixed retail price and availability is low, retail price and supply of LPG should be regulated.

- The upcoming budget should continue tax exemption declared in the last budget for renewable energy and energy efficient technologies and apparatus.

- Coal-based power plants are the most cost effective option for power generation and there are huge proven coal reserves in Bangladesh. In this regard, there is a need to design an integrated coal policy which will also deal with extraction of local coal.

- Development of terminals and pipelines for import of gas will require additional funding from the budget.

- Allocation of funds is needed to enhance the storage capacity of BPC to secure fuel supply for oil-based power plants.

- The Government of Bangladesh (GoB) has plans to import electricity from the SAARC (South Asian Association of Regional Cooperation) countries, especially Bhutan, India, Nepal and Myanmar. Establishing regional energy cooperation, in this regard, will be a vital policy imperative to enhance cross-border power trade for maintaining long-term energy security of Bangladesh. The standards for fixation of power tariffs, wheeling charges, property rights, transmission and distribution systems, as well as operation and maintenance services will have to be considered thoroughly.

- Since the hydropower potential of the country is low compared to that of the other countries, bilateral cross-border hydropower trade with Bhutan and Nepal will help mitigate Bangladesh's power deficit. In addition, appropriate steps should be taken to import gas from Myanmar.

- Promoting the use of energy efficient technologies in industrial and residential sectors can significantly reduce the demand for electricity.

- Establishing Bangladesh Energy Research Council should be a priority and adequate funds should be allocated towards this.

- The Bangladesh Infrastructure Facilitation Fund (BIFF) of Tk. 1,600 crore should be utilised via private partnerships as soon as possible.

6. TRANSPORT, CONNECTIVITY AND CONSTRUCTION

6.1 Roads and Highway

- Development of the road network is particularly urgent. All major roads need to be expanded to four lanes and be able to bear load capacity up to 15-18 tonnes, compared to current capacity of 8-10 tonnes. Budgeting for rural roads, regional highways and feeder roads must be synchronised with the long-term sectoral master plans.

- Revenue for repair work can be generated by charging tolls as well as fines for speeding and other violations. The government may look into the harmonised scheme for road transport charges introduced by members of the Common Market of Eastern and Southern Africa in 1991.

- The combination of country's heavy rainfall and irregular maintenance of roads is responsible for the poor condition of the roads. Additional money should be allocated for routine maintenance, especially of the major highways, as well as for R&D of construction technology to improve the durability of the roads. Low-cost year-round maintenance is also a cost effective measure to curb road accidents compared to large-scale restoration projects.

- Better feasibility exercise will help maintain longevity of bridges which suffer from river erosion and other adversarial environmental factors.

- Enforcement of road regulations as well as tracking of invalid licenses must be taken into consideration when planning the road and highway budget. Non-compliance, such as speeding and plying of heavy vehicles that exceed the load capacity of the road, is a major factor behind the deteriorating condition of the roads. The Meghna Bridge, a crucial link between Dhaka and

Chittagong, is a case in point. The government must invest in better driving schools to ensure that individuals are qualified to drive on the road.

- The number of highway police and monitoring personnel in the country is inadequate to maintain safety. In addition, cautionary signals are essential in dangerous locations. The Accident Research Centre has identified 209 such 'black spots', including 38 in the Dhaka-Aricha highway and 35 in the Dhaka-Chittagong highway. Budgetary allocation is needed to address this problem.

6.2 Traffic

- Isolated projects will not improve the traffic situation; rather coordinated and strategic planning is needed to resolve the ongoing problems.

- Traffic jams can be alleviated by imposing mandatory bus services at all schools, which are the epicenters of traffic during rush hour.

- The public transportation network and facilities should be strengthened to reduce the number of private cars on the road. City planners should expedite the establishment of a Bus Rapid Transit, as was envisioned in the Strategic Transport Plan in 2008. Though this new system is perhaps not possible to be introduced immediately, funds should be channeled gradually towards implementation of the plan.

- The drivers of small unauthorised vehicles, which the government is trying to clamp down in order to reduce traffic, must be compensated, preferably in the form of alternative employment.

6.3 Railway

- Since Bangladesh is a land-scarce country, 70 per cent of transit traffic should be carried through rail routes, 15 per cent through water, and the rest by roads. This calls for improvement of the country's railway system on an urgent basis.

- Aside from fund shortage, the government also has not increased train fare since 1992, as a result revenue generation for development of the railway sector has been rather insignificant. The recent proposal by the Bangladesh Railway to hike the train fares needs serious consideration, but it is advisable to introduce the new fares gradually and in phases.

- Integration of the railway with road and water transport systems as well as the development of facilities for transit purposes will allow for smoother movement of traffic. This will need careful consideration and appropriate budgetary allocation.

6.4 Waterway

- The major barriers to inland waterway transit include high level of siltation, bank erosion, inadequate navigational aids, and insufficient facilities and equipment. Bangladesh needs to spend a significant amount of money to dredge rivers in order to reduce siltation and make waterways suitable for transportation. Adequate budgetary allocation will be needed for this. These investments should be taken into consideration when fixing fees on transport movement to ensure cost recovery.

- Unauthorised trading of sand and illegal structures are responsible for narrowing down of traditional waterways. Enforcement agencies should be enhanced and be given greater incentives to monitor the important routes.

- The Chittagong and Mongla Ports, country's two existing ports, are currently operating below their capacities. More funds should be channeled toward the development of these two ports to enable them to handle increased future cargo and business originating from possible transit trade.

- The underdeveloped Chittagong and Mongla Ports, along with the low capacity of the Ashuganj-Akhaura road, are hindering operation of the Ashuganj River Port, a potential focal point for trade between India and Bangladesh. Investment by the private sector should be encouraged to develop the necessary infrastructure in Ashuganj and the connecting road to Akhaura. Appropriate fees should be fixed to ensure good returns on investment. Here PPP could play a key role.

6.5 Airway

- More investment is necessary to strengthen the Civil Aviation Authority of Bangladesh (CAAB), which was downgraded from Category 1 to Category 2 by the US Federal Aviation Administration. As a result, Bangladeshi airlines cannot operate flights to the USA.

- The capacity of the present airport in Dhaka will need to be significantly expanded if Dhaka is to become a regional air traffic hub.

6.6 General

- Comprehensive feasibility studies covering the aforesaid transportation modes needs to be conducted. Feasibility and preliminary studies should be systematic so as to avoid overlooking important details. This will require considerable funding and the involvement of relevant government ministries. The government may consider inviting tenders for transportation projects through Design-Build system, which will free the government from spending its own money.

- The government should allocate funds for the integration and harmonisation of the different modes of transportation in order to facilitate a more efficient and fluid movement of traffic.

- While regional connectivity is still being considered, these steps towards international standards will also facilitate improved trade within the country.

7. SOCIAL SAFETY NET

- Detailed information on the safety net programmes (including implementation status of the last year) should be made public during the announcement of the national budget proposals. These should include information about allocations and coverage (district-wise and phase-wise, where applicable), for at least the major programmes.

- Bangladesh should gradually move towards a more comprehensive social safety net with a view to designing a social security programme in future. For this consolidation and coordination will be required.

- The government took a step to build a database of safety net beneficiaries in order to avoid duplications. Pilot project was taken at Shibalaya upazila of Manikganj district. A nationwide programme should be taken to list all the beneficiaries.

- Geographic distribution of poor and ultra poor has changed remarkably between 2005 and 2010, as indicated by the Household Income and Expenditure Surveys (HIES 2005 and HIES 2010). However, geographical distribution of safety net coverage maintained its trend of focusing more on the western regions. To facilitate a review of the existing structure of safety nets in Bangladesh, a district-level survey of poverty prevalence needs to be carried out.

- The second phase (March-April 2012) of the Employment Generation Programme for the Poorest (EGPP), which is currently being implemented, is to cover all the 64 districts of the country. The programme should focus only on the highly poverty-stricken areas rather than the entire country, and widen the beneficiary coverage in those areas.

- For EGPP in FY2012-13, the current geographical distribution of poverty pockets should be included in targeting the beneficiaries. It is to be noted in this connection that, according to HIES 2010, significant improvements were achieved in terms of poverty reduction in those areas of the country that were found to be lagging behind in HIES 2005.

- Daily wage rate for the EGPP were increased by Tk. 25 each year and now stands at Tk. 175. Given that the average non-agriculture labour wage in the market is above Tk. 200 at present, daily wage rate for the EGPP in FY2012-13 may be adjusted upward taking into account the current inflation rate.

- In FY2011-12 allocation for safety net programmes was increased by about 16 per cent over FY2010-11. However, to achieve a resource allocation to the tune of 3 per cent of GDP by 2015, as stipulated in the SFYP, higher annual growth in allocations will be necessary in the next three fiscal years. From the current (FY2011-12) safety net allocation (equivalent to 2.5 per cent of GDP), the programmed safety net allocation for FY2014-15 will be over 77 per cent higher. To achieve the goal, required annual average growth in safety net allocations for the next three years will be around 21.1 per cent. From these estimates, a safety net budget of around Tk. 27,300 crore will be needed in the budget for FY2012-13.

8. INSTITUTIONAL CAPACITY FOR DELIVERY

8.1 Building Professional Capacity

- One of the major factors influencing the delay in implementation of the development projects, and subsequently the sharp decline in foreign aid disbursement, is lack of adequate and appropriate capacity of the line ministries. It is proposed that in line with the Medium Term Budgetary Framework (MTBF), ministries should delegate some responsibilities to directorates and offices under them by establishing a result-based monitoring and evaluation (M&E) system.

- Weak institutional capacity is evident from the fact that the project aid utilisation is low, despite availability of foreign aid in the pipeline. The technical capacities of the MoF and the Planning Commission will need to be significantly strengthened through proper staffing and training to ensure timely implementation of the ADP projects. Steps should be taken to ensure that project-related forms (e.g. Draft Project Proforma) can be completed in a timely manner.

- The MTBF has restricted ministries' space for undertaking independent initiatives by setting limits on their future spending. It is suggested that ministries should be permitted some degree of flexibility in putting forward their budget proposals to the Planning Commission. This will allow them to go for higher budgets in view of emergent needs in the relevant sectors.

8.2 Decentralising Fiscal Structure

- Budgetary transfers from the centre are the most important sources of financing for most local governments in Bangladesh, accounting for about 50-60 per cent of local government income. The FY2012-13 Budget should come with a more transparent system for inter-governmental fiscal transfers which will make these more predictable. In particular, fiscal transfers through ADP will need to be made more transparent and based on rational criteria (e.g. poverty incidence).

- There is a wide variation in terms of revenue composition of individual cities. The upcoming budget should consider offering incentives to reward high performers (e.g. Chittagong). It could empower leading performers by increasing their sources for generating own revenues, thereby increasing their autonomy in public expenditures.

- The FY2012-13 Budget could propose a timeline and institutional framework for designing modalities with the objective of moving towards a District Budget, by taking into cognisance the performance variation of local bodies in terms of revenue generation.

8.3 Reinvigorating PPP

- The PPP, as a model for attracting new resources, is yet to make any significant impact to showcase its potential. The absence of profit-sharing provisions in the *Policy and Strategy for Public-Private Partnership (PPP) 2010* should be considered by the upcoming budget, since private sector's interest in participating in such arrangements has tended to remain further mute.

- To promote private participation in the budget implementation stage, the upcoming budget could consider the PPP arrangement for establishing a result-based M&E framework. A block allocation may be earmarked for the Office of the PPP to execute the M&E framework for ongoing projects. This proposal is in conjunction with the objective of the SFYP where such arrangements are called for monitoring development outcomes.

- Though the PPP Act was enacted in 2010, the institutional set up is yet to be completed. The Office of the PPP is in operation headed by a Chief Executive Officer and four managers. It is proposed that necessary steps be taken to expedite operation of a full-fledged PPP office/secretariat.