State of the Bangladesh Economy in FY2010-11 and Outlook for FY2011-12

Centre for Policy Dialogue (CPD)

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CENTRE FOR POLICY DIALOGUE (CPD)
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The Centre for Policy Dialogue (CPD) was established in 1993 as a civil society initiative to promote an ongoing dialogue between the principal partners in the decision making and implementing process. Over the past 19 years the Centre has emerged as a globally reputed independent think tank with local roots and global outreach. A key area of CPD's activism is to organise dialogues to address developmental policy issues that are critical to national, regional and global interests with a view to seek constructive solutions from major stakeholders. The other key area of CPD activities is to undertake research programmes which are both serviced by and are intended to serve as inputs for CPD's dialogue process. Some of the major research areas of CPD include: *Macroeconomic Performance Analysis*; *Fiscal Policy and Domestic Resource Mobilisation*; *Poverty, Inequality and Social Justice*; *Agriculture and Rural Development*; *Trade, Regional Cooperation and Global Integration*; *Investment Promotion, Infrastructure and Enterprise Development*; *Climate Change and Environment*; *Human Development and Social Protection*; and *Development Governance, Policies and Institutions*. CPD actively networks with other institutions within and outside Bangladesh which have similar interests, and also regularly participates in various regional and international fora. In recognition of the track record in research, dialogue and policy influencing, CPD was selected as one of the awardees under the Think Tank Initiative (TTI) through a globally competitive selection process. TTI is supported by a number of governments and foundations, and is implemented by the International Development Research Centre (IDRC), Canada. CPD's current publication list includes more than 370 titles including Books, Monographs, Working Papers (Occasional Papers), Dialogue Reports and Policy Briefs. CPD outputs are available for sale at the Centre and also in selected bookstores in Bangladesh. CPD publications and other relevant information are also regularly posted on CPD's website www.cpd.org.bd

The views expressed in this volume are those of the CPD IRBD 2011 Team members and do not necessarily reflect the views of the CPD.

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Mr Towfiqul Islam Khan served as the coordinator of the CPD IRBD 2011 Team.

Preface

Independent Review of Bangladesh's Development (IRBD) has been the flagship programme of the Centre for Policy Dialogue (CPD) since 1995 when the programme was first initiated. A major objective of the IRBD programme is to examine and analyse the key macroeconomic performance indicators of the Bangladesh economy including fiscal-budgetary and monetary sectors and the real economy, both on the basis of interim assessments of the economy, and also for the entire fiscal year. The purpose of the IRBD exercise is to highlight major developments in the economy of Bangladesh, to flag emerging challenges confronting macroeconomic management, to raise awareness about key developmental issues and challenges facing the Bangladesh economy, and to stimulate an informed debate around these issues.

As in earlier years, the work on IRBD FY2010-11 volume has involved both analytical work, and dialogues including a number of discussion sessions with relevant experts and stakeholders. Thus, along with the CPD researchers, views of many stakeholders have also been reflected in this volume. The present volume also includes a number of interim outputs prepared under the IRBD 2011 programme at CPD.

Chapter 1 of the present volume presents an assessment of Bangladesh's macroeconomic performance in FY2010-11, and identifies the major achievements and the emerging pressure points at the end of fiscal year. This chapter also traces the early trends in FY2011-12 and flags four critical concerns for the Bangladesh economy as the new fiscal year unfolds: adverse spillovers from global economic situation, deepening stresses in public finance management, unabated price inflation, and increasing pressures on the external balances. In view of these emerging strains, the prospect of economic growth and challenges facing macroeconomic management in FY2011-12 have also been discussed in the chapter.

Chapter 2 of this volume provides an analysis of the national budget for FY2011-12 and the revised budget of FY2010-11, which were placed before the National Parliament on 9 June 2011. The chapter presents an in-depth analysis of the proposed revenue mobilisation targets and public expenditure plans of the government including sectoral allocations for the Annual Development Programme (ADP) for FY2011-12. In addition, this chapter examines the various fiscal proposals made in the budget, evaluates these against the expectations, highlights the outstanding areas that demand further consideration, and provides critical comments on the feasibility of implementation of the proposals.

Chapter 3 undertakes a critical assessment of the Monetary Policy Statement (MPS) of Bangladesh Bank for the second half of FY2010-11 (January-June 2011). This chapter was originally prepared and presented as the keynote paper for a CPD organised dialogue titled *Growth, Inflation and Monetary Policy: Challenges for Bangladesh in FY2010-11*, held on 13 February 2011. The chapter explores to what extent the policy stance, stated in the aforementioned MPS, was adequate to address the emergent macroeconomic challenges confronting the policymakers. The chapter also articulates the challenges facing monetary management in FY2010-11, and discusses the outlook for economic growth in view of the evolving macroeconomic situation and the proposed policy framework.

In 2011, a CPD research team conducted a study, in collaboration with the BRAC Advocacy Unit, to examine the efficacy of fiscal measures and public service delivery for the ultra poor. Chapter 4 includes a Policy Brief prepared based on the research findings of the above mentioned study. These findings were presented at a national dialogue on *National Budget 2011-2012: Allocation for Safety Net and Related Sectors to Eradicate Extreme Poverty*, organised by the All-Party Parliamentary Group (APPG) on Extreme Poverty, held on 4 May 2011. The chapter puts forward a set of recommendations emerging from the research findings which could be addressed by the Members of Parliament (MPs).

Chapter 5 presents an analytical review of the emerging situation with respect to overseas migration and the inwards remittance flow with focus on the state of affairs over the first six months of FY2011-12. The chapter identifies some of the key emerging challenges and proposes a set of immediate to mid-term doables which policymakers could consider as they grapple with the task of addressing the attendant issues.

The present IRBD volume also includes two dialogue reports as Annexes. Annex 1 is a report on the CPD organised dialogue on *State of Bangladesh Economy and Analysis of the National Budget FY2011-12*, held on 18 June 2011. Annex 2 is a report on the post-budget discussion held in Chittagong titled *An Analysis of the National Budget for FY2011-12*, which was organised by the CPD in association with the Bangladesh Economic Association (BEA), Chittagong Chapter on 25 June 2011. Keynote presentations at these two dialogues were made based on CPD's analysis of the national budget for FY2011-12. These presentations were followed by discussions by representatives of key stakeholder groups who shared their critical perspectives and views on a wide-ranging issues covering fiscal proposals, strategies for revenue mobilisation, proposals for development-related investments in the ADP, and the major challenges with regard to implementation of the budgetary proposals and raising the quality and efficacy of implementation.

Acknowledgement

I would like to register my deep gratitude to *Dr Debapriya Bhattacharya*, Distinguished Fellow, CPD who has provided leadership to the preparation of this volume. He has provided intellectual guidance and organisational stewardship which has enabled the CPD IRBD 2011 Team to implement the assigned tasks, keeping up with the high standard that is a distinctive feature of the IRBD exercise. This is also an opportunity for me to recognise the tireless work of all the research staff at CPD who have been involved with the IRBD-related work. *Dr Fahmida Khatun* has played her dual role most effectively as Head of Research, CPD. She has been instrumental in giving leadership to the IRBD Team, and as one of the key contributors to the volume, she has provided valuable substantive inputs in its preparation. I would like to particularly appreciate the dedication and hard work put in by *Mr Towfiqul Islam Khan*, Senior Research Associate, CPD in preparing the IRBD volume. The quality of Towfiq's work both as a contributor to the volume and as the coordinator of IRBD exercise calls for special mention.

I will be failing in my duty if I do not give due recognition to the valuable contribution of the large number of individuals and institutions who have supported preparation of this volume. I would like to express my sincere gratitude to researchers, members of the academia, leading policymakers, political leaders and members of the national parliament, government officials, business leaders, and representatives from grassroots and civil society organisations who have provided information to the IRBD 2011 Team, and shared their views at dialogues and brainstorming sessions that were organised by the CPD as part of preparation of the IRBD 2011 exercise.

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Taking advantage of this opportunity I would like to put on record my sincere appreciation to the concerned officials belonging to a number of institutions for their valuable support that the CPD IRBD 2011 Team has received in the form of access to relevant data and information. These included the Bangladesh Bank, Bangladesh Bureau of Statistics (BBS), Bangladesh Energy Regulatory Commission (BERC), Bangladesh Power Development Board (BPDB), Bureau of Manpower, Employment and Training (BMET), Board of Investment (BoI), Department of Agricultural Extension (DAE), Department of Agricultural Marketing (DAM), Dhaka Stock Exchange (DSE), Export Promotion Bureau (EPB), Ministry of Food and Disaster Management, National Board of Revenue (NBR), Petrobangla, and Planning Commission.

On behalf of the CPD IRBD 2011 Team I would like to most thankfully recall the support and cooperation that CPD has received from members of the print and electronic media of the country. Their generous support has allowed CPD to take the message of IRBD outputs to the broader sections of the society both in Bangladesh and beyond.

CPD's Dialogue and Communication Division plays an important role in the preparation of IRBD volumes. *Ms Anisatul Fatema Yousuf*, Director, CPD and her colleagues at the Division has put in hard work in organising the various dialogues and brainstorming sessions in connection with preparation of the IRBD outputs, and the preparation of the IRBD manuscript for publication. Contribution of the CPD Administration and Finance Division in facilitating the IRBD-related activities is also sincerely appreciated.

As in case of the earlier IRBD volumes, *Ms Nazmatun Noor*, Senior Dialogue Associate, CPD has worked with high dedication and motivation in undertaking the task of copy editing of the present volume. *Mr Avra Bhattacharjee*, Senior Dialogue Associate, CPD has worked with dedication for the cover and graphic works of the book, and has been in-charge of designing of the IRBD publication. *Mr Fazley Rabbi Shakil*, Publication and Print Associate, CPD and *Mr Md. Shaiful Hassan*, Programme Associate (DTP), CPD have provided able support to get the present volume in the pre-printing format. I would also like to recognise the valuable contributions of *Mr A H M Ashrafuzzaman*, Senior System Analyst, CPD for his technical support, and *Mr Hamidul Hoque Mondal*, Senior Administrative Associate, CPD for his valuable secretarial support.

Readers of successive IRBD volumes will know that the CPD's IRBD programme emerged from the pioneering initiative of *Professor Rehman Sobhan*, Chairman, CPD. Professor Sobhan's ideas and ideals continue to inspire the work of the IRBD Team. The IRBD 2011 Team has benefitted immensely from the advice of *Professor Sobhan*, and his critical views on draft IRBD outputs. I would like to take this opportunity to put on record our deep gratitude to *Professor Sobhan* for his guidance to the IRBD 2011 Team.

February 2012
Dhaka

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Executive Director
Centre for Policy Dialogue (CPD)

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Acronyms

ADB	Asian Development Bank
ADP	Annual Development Programme
AIR	Annual Information Return
AIT	Advance Income Tax
API	Active Pharmaceutical Ingredient
BAIRA	Bangladesh Association of International Recruiting Agencies
BAPEX	Bangladesh Petroleum Exploration & Production Company Ltd.
BASIS	Bangladesh Association of Software and Information Services
BBS	Bangladesh Bureau of Statistics
BCCRF	Bangladesh Climate Change Resilience Fund
BCCTF	Bangladesh Climate Change Trust Fund
BCIC	Bangladesh Chemical Industries Corporation
BDF	Bangladesh Development Forum
BDT	Bangladeshi Taka
BEA	Bangladesh Economic Association
BERC	Bangladesh Energy Regulatory Commission
BGMEA	Bangladesh Garment Manufacturers and Exporters Association
BIDS	Bangladesh Institute of Development Studies
BIFFCL	Bangladesh Investment Facilitation Fund Company Limited
BIISS	Bangladesh Institute of International and Strategic Studies
BMET	Bureau of Manpower, Employment and Training
BO	Beneficiary Owner
BOOT	Build-Own-Operate-Transfer
BOP	Balance of Payments
BPC	Bangladesh Petroleum Corporation
BPDB	Bangladesh Power Development Board
BSTI	Bangladesh Standards Testing Institution
CAD	Canadian Dollar
CBN	Cost of Basic Needs
CBU	Completely Built Unit
CCCI	Chittagong Chamber of Commerce and Industry
CD	Customs Duty
CHT	Chittagong Hill Tracts
CKD	Completely Knocked Down
CNG	Compressed Natural Gas
CNY	Chinese Yuan

ACRONYMS

CPD	Centre for Policy Dialogue
CPI	Consumer Price Index
CRR	Cash Reserve Ratio
CSR	Corporate Social Responsibility
DAP	Diammonium Phosphate
DCCI	Dhaka Chamber of Commerce & Industry
DDA	Directorate of Drug Administration
DDR	Doha Development Round
DEMO	District Employment and Manpower Office
EBA	Everything But Arms
EEF	Equity and Entrepreneurship Fund
ECF	Extended Credit Facility
EFA	Education for All
EFSF	European Financial Stability Facility
EGPP	Employment Generation Programme for the Poorest
EPB	Export Promotion Bureau
EPZ	Export Processing Zone
ERP	Effective Rate of Protection
ETP	Effluent Treatment Plant
EU	European Union
FAO	Food and Agriculture Organization
FBCCI	Federation of Bangladesh Chambers of Commerce and Industry
FDI	Foreign Direct Investment
FDR	Fixed Deposit Receipt
FFW	Food for Work
FOB	Free on Board
GATS	General Agreement on Trade in Services
GBP	British Pound
GCC	Gulf Cooperation Council
GDP	Gross Domestic Product
GNP	Gross National Product
GSP	Generalized System of Preferences
GoB	Government of Bangladesh
G2G	Government-to-government
HIES	Household Income and Expenditure Survey
HNPSP	Health Nutrition and Population Sector Program
HS	Harmonized Commodity Description and Coding System
ICT	Information and Communication Technology
IDCOL	Infrastructure Development Company Limited
IMED	Implementation Monitoring and Evaluation Division
IMF	International Monetary Fund
INR	Indian Rupee
IOC	International Oil Company
IOM	International Organization for Migration
IPP	Independent Power Producer
IRBD	Independent Review of Bangladesh's Development
KSA	Kingdom of Saudi Arabia
LDC	Least Developed Country

LGED	Local Government Engineering Department
LGRD	Local Government and Rural Development
LPG	Liquefied Petroleum Gas
L/C	Letter of Credit
MCCI	Metropolitan Chamber of Commerce and Industry
MDG	Millennium Development Goal
MENA	Middle East North Africa
MEWOE	Ministry of Expatriates' Welfare and Overseas Employment
MFI	Microfinance Institution
MIS	Management Information System
MP	Member of Parliament
MPO	Monthly Pay Order
MPS	Monetary Policy Statement
MT	Metric Ton
MTBF	Medium Term Budgetary Framework
MTMF	Medium Term Macroeconomic Framework
MW	Mega Watt
MoA	Ministry of Agriculture
MoF	Ministry of Finance
MoP	Muriate of Potash
M2	Broad Money
mmcfd	Million Cubic Feet per Day
NBR	National Board of Revenue
NGO	Non-government Organisation
NPL	Non-performing Loan
NRB	Non-resident Bangladeshi
NREGA	National Rural Employment Guarantee Act
NSD	National Savings Bond
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
OMS	Open Market Sales
PCB	Private Commercial Bank
PFDS	Public Food Distribution System
PKB	Probashi Kalyan Bank
POL	Petroleum and Other Liquids
PPP	Public-Private Partnership
PRGF	Poverty Reduction and Growth Facility
PSI	Policy Support Instrument
QIP	Quantum Index of Production
RADP	Revised Annual Development Programme
REB	Rural Electrification Board
RMG	Readymade Garments
RPP	Rental Power Plant
RoO	Rules of Origin
SAFTA	South Asian Free Trade Area
SCB	State-owned Commercial Bank
SD	Supplementary Duty
SEC	Securities and Exchange Commission

ACRONYMS

SFYP	Sixth Five-Year Plan
SIM	Subscriber Identity Module
SLR	Statutory Liquidity Ratio
SME	Small and Medium Enterprise
SRO	Statutory Regulatory Order
SSP	Social Security Premium
SoE	State-owned Enterprise
TIN	Tax Identification Number
TRQ	Tariff Rate Quota
TSP	Triple Super Phosphate
TTC	Technical Training Centre
TTI	Total Tax Incidence
TUF	Technology Upgradation Fund
UAE	United Arab Emirates
UK	United Kingdom
UP	Union Parishad
USD	United States Dollar
USITC	United States International Trade Commission
VAT	Value Added Tax
VGD	Vulnerable Group Development
VGF	Viability Gap Fund
VGF	Vulnerable Group Feeding
WTO	World Trade Organization

CHAPTER

1

Analytical Review of Bangladesh's Macroeconomic Performance in FY2010-11 and Early Signals of FY2011-12

1.1

INTRODUCTION

The present chapter seeks to trace the emerging trends in the Bangladesh economy in the fiscal year 2011-12 (FY2011-12). To this end, the study first establishes the benchmark conditions of the current fiscal year by sketching a consolidated picture of FY2010-11 with an analysis of the year-closing data. The chapter then attempts to analyse the early signals of the current fiscal year.

With a view to highlight the major challenges facing the Bangladesh economy in the FY2011-12, the paper focuses on four critical issues. These are the followings:

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

The chapter rounds up by drawing lessons from the foregoing analyses and by putting forward a number of policy suggestions to deal with the identified macroeconomic concerns.

The attempt of the present study has been structured around its key objectives. It builds on the Centre for Policy Dialogue's (CPD) earlier works on the subject, and uses the most recent information available from official sources to provide an up-to-date analysis of the current state of Bangladesh economy.

This is the first reading of the state of Bangladesh economy in FY2011-12 prepared under CPD's programme on *Independent Review of Bangladesh's Development (IRBD)*. It is planned to be followed up by two other assessments before the announcement of the national budget for FY2012-13.

1.2

ESTABLISHING THE BENCHMARK: AN EVALUATION OF THE FISCAL YEAR 2010-11

1.2.1 Growth Performance

A notable turnaround of the manufacturing sector (backed up by the export-oriented enterprises), strong performance of the crops sector, and anticipated momentum in public investment contributed to a high projection of 6.7 per cent of gross domestic product (GDP) growth by the Bangladesh Bureau of Statistics (BBS) for FY2010-11. A recovering global economy with attendant prospects of robust performance by the country's export and linked sectors was also a reason that informed this optimistic scenario. Indeed, if this turns out to be actually the case, the estimated GDP growth rate for FY2010-11 would be the highest ever achieved in post-independence Bangladesh. What is also remarkable is

Table 1.1

GDP Growth and Sectoral Share

(in Per cent)

Sector	Share		Growth		Incremental Share	
	FY2010	FY2011	FY2010	FY2011*	FY2010	FY2011
Agriculture	19.6	19.3	5.2	5.0	17.1	14.6
of which Crops	*11.0*	*10.9*	*6.1*	*5.0*	*11.1*	*8.3*
Industry	28.9	29.3	6.5	8.2	30.8	35.4
of which Manufacturing	*17.3*	*17.8*	*6.5*	*9.5*	*18.5*	*24.8*
Services	48.1	48.1	6.5	6.6	51.1	47.9
Import Duty	3.4	3.3	1.8	4.2	1.0	2.1
Total	100.0	100.0	6.1	6.7	100.0	100.0

Source: Bangladesh Bureau of Statistics (BBS).
Note: *Provisional estimates.

that, this high growth rate would have been achieved over the relatively high benchmark of 6.1 per cent in FY2009-10 (Table 1.1).

The impressive GDP estimates, however, are provisional and are likely to be revised. Actual growth performance would hinge on two critical factors: (a) robustness of investment projections, particularly of public investment, based on the Revised Annual Development Programme (RADP) when the GDP estimates for FY2010-11 were prepared; and (b) estimates of growth of the manufacturing sector which, in view of information on the actual performance over the first six months, appeared to be rather optimistic. As is known, even the reduced RADP could be implemented only to the tune of 91.5 per cent. However, it appears that growth in the manufacturing sector gained some momentum in the second half of FY2010-11. Driven by an upbeat export sector that posted a high 41.5 per cent growth, medium and large-scale manufacturing sectors posted a record 17.7 per cent growth in terms of quantum index of production (QIP). The QIP of small industries also marked 3.3 per cent growth, a significant upturn in view of the negative growth ((-) 6.1 per cent) in the first half of the fiscal year. Whether, in the end, the final GDP growth estimate for FY2010-11 manages to reach the record high growth projection of 6.7 per cent, is to be seen when BBS comes out with the final figures in a few months time.

1.2.2 Three Major Achievements

Export was Robust

Exports showed remarkable turnaround in FY2010-11 having experienced the adverse consequences of the global economic slowdown in FY2009-10. Bangladesh's global export in FY2010-11 posted a high growth of 41.5 per cent against only 4.1 per cent growth in FY2009-10, with both readymade garments (RMG) and non-RMG products registering significant growth rates of 43.4 per cent and 35.1 per cent respectively. Robust export performance helped maintain a foreign exchange reserve of USD 10,911.6 million at the end of FY2010-11, which matched the corresponding reserve levels at the close of FY2009-10 (USD 10,749.7 million). However, the attained growth was achieved over a low benchmark growth of FY2009-10, and could prove difficult to sustain in FY2011-12.

An important aspect of the impressive export performance in FY2010-11 was that along with growth in the volume of exports, average prices in the global market also appeared to have posted some rise. For example, growth rates in terms of export volume for knit and woven RMG were 19 per cent and 20 per cent respectively in FY2010-11, which would imply that price indices have also seen significant rise. However, rise in prices also reflected a significant increase in cost of production, particularly in view of high cotton prices in FY2010-11.

Collection of Tax Revenue Strengthened

In continuation of its commendable efforts in the recent past, the National Board of Revenue (NBR) has achieved a significant 27.2 per cent revenue growth in FY2010-11, far outpacing the targeted growth rate of 16.8 per cent (by Tk. 6,502 crore). Impressive growth rates were achieved for most of the components, particularly in case of income tax component (32.4 per cent). In the non-NBR tax component as well, an impressive 17.7 per cent growth was recorded in FY2010-11. Although this was lower than the annual target of 25.8 per cent, this is a significant improvement in view of the low growth of 3.4 per cent achieved in FY2009-10.

Turnaround in Manpower Export

Significant slowdown in the outward migration had emerged as a major concern for Bangladesh in FY2009-10. The adverse impact of this was quite obvious, particularly from the perspective of foreign exchange earnings, domestic employment situation, poverty alleviation efforts and foreign exchange reserve situation. As may be recalled, the number of people going abroad for jobs declined from about 0.65 million in FY2008-09 to 0.43 million in FY2009-10. It was somewhat of a relief that the decline appears to have been arrested in FY2010-11; as a matter of fact, the number of migrant workers leaving the country marginally increased to reach 0.44 million in this year. However, growth in remittance earnings further slowed to single digit (6 per cent) in FY2010-11 from the robust 13.4 per cent recorded in the previous year.

In spite of some of the positive achievements relating to a number of important macroeconomic performance indicators, several disquieting fault lines began to appear in the economy as FY2010-11 approached its finishing line. Inflationary momentum continued to sustain, overall BOP position went into a negative terrain, burden of subsidies started to pick up significantly, particularly in the backdrop of operationalisation of (quick) rental plants, and bank borrowings were rising as a consequence of lower utilisation of foreign aid and higher unplanned public expenditure. Sustained moderately high growth with macroeconomic stability, which was the hallmark of Bangladesh's economic performance during the last decade, came under serious threat as the economy moved towards FY2011-12.

1.2.3 Pressure Points of Macroeconomic Situation

Despite the high GDP growth in FY2010-11 and the success in terms of high export earnings, remittance flow and revenue collection, a number of pressure points developed in the overall macroeconomic scenario of the country. These worrying developments transmitted a cautionary signal with regard to the country's macroeconomic management in the near-term. A number of these developments were new, whilst some of the others were carried from the past only to have had aggravated in the process with the passage of time.

Prices Continued to Soar

Contrary to what one would have expected from the impressive growth in the crops sector, as noted earlier, food prices continued to soar and drove up the overall inflation rate in FY2010-11. Moving average inflation rate for the fiscal year stood at 8.8 per cent, higher than the set target of 7 per cent. Point-to-point inflation in June 2011 was 10.2 per cent compared to 8.7 per cent in June 2010. Food inflation rate was higher[1] than the general inflation rate. It appears that trends in food prices have become somewhat de-linked from the food production and availability situation. With no major production shocks in recent times, food price hike appears to reflect a transmission of the high global prices to the domestic market. As Table 1.2 would evince, in FY2010-11 production was better, import had increased, public foodstock was higher, and offtakes under Vulnerable Group Development (VGD), Vulnerable Group Feeding (VGF), Food for Work (FFW) and

[1] 12.5 per cent in June 2011.

Open Market Sales (OMS) were more than the previous year. Yet, prices continued to rise, in tandem with the rising world prices. In this connection, one may recall World Bank estimates which indicate a contemporaneous correlation between rice prices of Kolkata-Dhaka and Thailand-Dhaka to be 0.9 and 0.8 respectively, implying that they tend to move closely together.[2]

Table 1.2

Food Situation

(Lakh MT)

Year	Actual Production (Gross)	Net Production*	Foodgrains Import			Public Procurement	Public Distribution	Foodgrains Stock (End June)
			Government and Food Aid	Private	Total			
FY2009-10	332.3	292.4	5.6	29.0	34.6	8.1	19.6	5.3
FY2010-11	345.1	321.5	22.0	31.1	53.1	4.6	22.9	8.9

Source: Bangladesh Bank.
Note: *After 12 per cent deduction for FY2009-10, and 10 per cent for FY2010-11 for seed, feed, waste, etc.

In its attempt to control the inflationary pressure, the Central Bank resorted to intervening in the money market and bringing down the credit growth. The Monetary Policy Statement (MPS) (for July-December 2010 or the first half of FY2010-11)[3] of the Bangladesh Bank targeted to significantly reduce the growth in money and credit supply. However, reining in the credit growth proved to be difficult in the face of higher credit demand from both public and private sectors: total outstanding domestic credit increased by 27.4 per cent, while net credit to the government and to the private sector posted 34.9 per cent and 25.8 per cent growth respectively, in FY2010-11. Disbursement of term loan increased by 24.3 per cent, while that of agricultural credit increased by 9.6 per cent. Broad money (M2) supply also recorded a significant increase of 21.3 per cent over the last year. In response, Bangladesh Bank resorted to multiple increases in the policy rates.[4] At the same time, higher demand for trade financing originated from significant import growth of 41.8 per cent in FY2010-11. Growing investment demand, and more importantly, the bubble in the capital market also wiped out a large part of the excess liquidity in the system. This resulted in a decline in the level of the excess liquidity which stood at Tk. 20,660 crore at the end of January 2011. This was the lowest amount of excess liquidity in two years. The bust in the capital market, following the boom, however, helped ease the liquidity pressure on scheduled banks.

Subsidy Pressure Intensified

As a strategy to combat food price hike, the government decided to focus more on food import rather than domestic procurement, through increased public as well as private channels. Higher imports and more extensive distribution of foodgrains led to significant rise in food subsidy requirement. Initial subsidy allocation of about Tk. 1,200 crore was later revised upwards to about Tk. 1,650 crore. However, it was the fuel subsidy requirement that emerged as the critical issue. This was underwritten not as much by the rise in international prices than the fact of the growing demand for petroleum products in the backdrop of rising fuel needs to service the newly installed fuel-fired quick rental and rental power plants (RPPs). Loss of Bangladesh Petroleum Corporation (BPC), the sole importer of petroleum products, was to the tune of Tk. 2,300 crore in FY2009-10. In FY2010-11 BPC had incurred a loss of about Tk. 7,200 crore. This was way over the subsidy allocation of Tk. 4,000 crore kept for the BPC in the revised budget of FY2010-11.

[2]World Bank (2011).
[3]No change has been mentioned on this in the January-June MPS of FY2010-11.
[4]Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR) were raised twice, and Repo and Reverse Repo rates were increased thrice during FY2010-11.

ADP: Business as Usual

The implementation of Annual Development Programme (ADP) stood at Tk. 32,830 crore during FY2010-11, which was Tk. 5,670 crore less than the original target, implying an implementation rate of 85.3 per cent (of the original budget). This was about the same level of the last year (85 per cent). However, in Taka terms the implemented ADP was 26.7 per cent higher. As a result, ADP-GDP ratio in FY2010-11 was higher at 4.2 per cent, an improvement from the 3.7 per cent of the previous year. An added concern regarding the ADP had been the higher share of local financing in the absence of envisaged foreign financing. Of the implemented ADP of FY2010-11, about 70.6 per cent had to be financed from local sources; this was in the range of 60-65 per cent in the previous years. This led to a higher government borrowing from the banking system, putting pressure on credit availability for the private sector.

Non-Tax Sources of Revenue Remained as Low Performers

In continuation of the commendable performance of recent years, overall revenue collection increased by 20.3 per cent in FY2010-11.[5] However, this growth was singularly shouldered by NBR since non-tax component, constituting almost one-fifth of the total revenue target of FY2010-11, declined by 12.3 per cent compared to FY2009-10 (against the targeted growth of 25.2 per cent).

Low Offtake of Foreign Aid, Budget Deficit Squeezed

Budget deficit amounted to Tk. 31,013.2 crore (3.3 per cent of GDP against 5 per cent envisaged in the budget) in FY2010-11. However, one could argue that although the deficit remained under control, it was in part due to the wrong reason, i.e. the low level of ADP implementation. A major nagging concern in FY2010-11 was the low disbursement of foreign aid. In the backdrop of the expected project aid not having been materialised, government went on to finance a significantly larger proportion of the deficit through domestic borrowing, more specifically through bank borrowing. Against a negative net bank borrowing of (-) Tk. 2,092.5 crore in FY2009-10, the amount borrowed in FY2010-11 was Tk. 25,210.2 crore. As financing opportunities by way of both non-bank borrowing and foreign borrowing was low, as much as 81.3 per cent of the deficit needed to be financed from bank borrowing. To compare, in FY2009-10, about 27.6 per cent of the financing was made from foreign borrowing and 82 per cent from non-bank borrowing; indeed contribution from the banking sources experienced a decline (by (-) 9.6 per cent).

Collapse of the Capital Market

As was mentioned, excess liquidity of the scheduled banks declined quite dramatically and reached its nadir during December-January period of FY2010-11. This was accompanied by a significantly rising trend in market capitalisation in the share market. While excess liquidity declined by over 28 per cent between June 2010 and December 2010, market capitalisation increased by over 24 per cent during the same period. Evidence suggests that a large part of industrial, consumer and other credit money were diverted to the capital market. This contributed to drying up of liquidity in the banking system, contrary to the liquidity requirement ratios set by the Bangladesh Bank. When CRR was raised by Bangladesh Bank in December 2010, this led to forced selling of shares by the over-exposed banks to comply with the new requirement. This had a knock-on effect on the capital market which experienced a sharp downturn. However, as a consequence, liquidity situation improved also because Bangladesh Bank complemented this by injecting money

[5] Original target for revenue growth in FY2010-11 was set at 22 per cent, which was raised to 25.2 per cent in the revised budget.

into the market through the use of Repo auctions. Undermining of the nexus between banking sector and capital market has significantly weakened the management of monetary sector. Lack of prudential management by the Central Bank, particularly in the early stages of capital market boom, contributed to this and stability in the capital market was not restored till the close of the fiscal year in end-June 2011.

Balance of Payments under Pressure

BOP situation came under increasing pressure in FY2010-11. Current account balance experienced significant deterioration mainly because of the negative trade balance component with a deficit of USD 2.2 billion, and imports outpaced the robust export. Trade balance stood at negative (-) USD 7,328 million as against a negative balance of (-) USD 5,155 million in FY2009-10. Financial account also recorded significant deficit of (-) USD 1,584 million against a deficit of (-) USD 651 million in FY2009-10. This was driven by lower foreign direct investment (FDI) inflow (USD 768 million as against USD 913 million in FY2009-10), and reduction in net aid flow (USD 312 million against USD 902 million in FY2009-10). As a result, a deficit to the tune of (-) USD 635 million was recorded in the overall balance, deteriorating from a surplus of USD 2,865 million recorded in FY2009-10. The emergent BOP situation further necessitated the need to improve remittance flow and secure foreign financing to meet the rising investment demand.

1.3

FOUR CRITICAL CONCERNS FOR FISCAL YEAR 2011-12

1.3.1 Adverse Spillovers from Global Economic Situation

Uncertain Global Prospect

Nearly three years after the downturn observed in 2009, the developed countries in the North America, Europe and Asia still continue to grapple with an uncertain future and markets are agitated by trepidations of new setbacks, defaults and the possibility of a 'double-dip' recession. A number of factors are behind the current situation, including the high unemployment rate in the USA, the sovereign debt crisis in Europe, and decision by credit rating agencies to downgrade the ratings of some of the developed countries. Also, the tsunami and earthquake in Japan had transmitted shocks to the global economy. The fact that the European Union (EU) debt rescue package is in a vulnerable position due to the Greek referendum announcement, has further heightened the likelihood of a recession.

Uneven Recovery of Output

The growth of the world economy is expected to increase by 3.3 per cent in 2011, and in 2012 the rate may reach 3.6 per cent[6] – marginally higher than that was predicted earlier. For EU, the growth rate may remain stagnant in 2011 and 2012, at level lower than the pre-crisis benchmark. According to the latest forecast, USA is expected to grow in 2012 at a rate lower than that of 2011 (details in Table 1.3).

[6]UNDESA (2011).

Table 1.3

Growth of World Output and Trade (Annual Percentage Change): 2005-2012

Region	2005-2008 (Average)	2009	2010	2011	2012	2011*	2012*
World	3.3	-2.1	3.9	3.3	3.6	3.5	3.7
USA	1.9	-2.6	2.9	1.6	2.5	3.0	2.8
European Union	2.2	-4.2	1.8	1.7	1.9	1.8	1.8
South Asia	7.5	5.7	7.1	6.9	7.0	6.8	6.8
China	11.3	9.1	10.3	9.1	8.9	8.9	9.0
Least developed countries (LDCs)	7.7	4.1	4.7	5.6	5.8	5.5	5.7
World trade in goods and services	7.1	-11.1	11.9	7.1	6.8	7.6	7.1

Source: UNDESA (2011) and UNDESA (2011a).

Note: *2011 and 2012 figures were later updated; available in UNDESA (2011a).

The Federal Reserve has cut the GDP growth forecast for USA to 1.6 per cent in 2011, down from an earlier forecast of 2.9 per cent. The Reserve also predicted that the US economy would grow at 2.5 per cent in 2012 and by 3.5 per cent in 2013 (FOMC 2011).

Thus, the world economy continues to experience a faltering recovery. Moreover, the process is uneven as China, India, Brazil and other emerging economies are demonstrating impressive growth and fuelling the engine of global recovery, while developed countries are lagging behind.

Slowdown in Global Trade

Recent global trade expansion was mostly led by the Asian economies. World trade in goods and services expanded by about 12 per cent in 2010, more than what was previously estimated, after the steep decline of (-) 11 per cent in 2009. Yet growth of global trade is expected to fall, as per latest estimates, to 7.6 per cent in 2011, and further down to 7.1 per cent in 2012 (UNDESA 2011a).

Inflationary Trend

It needs to be further noted that the covariate shocks in Japan have undermined the world financial market, whereas unrest in Western Asia and North Africa have contributed to further increase in oil prices. Sustained high prices of foodgrains along with other commodities also pose a threat to the process of economic recovery. Soaring headline inflation is corroding real income of the common people across the world. This has compelled governments to safeguard consumers' interests through subsidies and cash transfer programmes, which in turn, is putting further pressure on the fiscal situation.

However, a weak Dollar is expected to help take some of the heat off the mounting oil and food prices in the world market. In addition, better harvests are expected to moderate food prices in the near-term. Nevertheless, all projections indicate that there is hardly any possibilities of food prices going back to their pre-2007 levels, although they may have come down somewhat.

Capital Flow

Net private capital flows to developing countries have increased as investors are shifting parts of their portfolios to emerging markets, mostly in developing economies, in the form of short-term equity investments and FDI. This trend has put upward pressure on the foreign exchange rate of the currencies of developing countries, putting pressure to undertake sterilisation measures to offset the risks allied with the influx of capital inflows.

Aid Prospects

In the backdrop of fiscal consolidation taking place in developed economies, and given the ongoing Eurozone debt crisis, the outlook for generous aid appears to be rather bleak; prospects of adequate financial support for implementation of the Millennium Development Goal (MDG)-related investments in the low-income countries also appears to be uninspiring.

Scope for Another Stimulus

Many of the developed countries had to prematurely discontinue their stimulus packages as a consequence of deteriorating fiscal situation. Thus, the scope for a second round of stimulus package appears to be bleak. High inflationary trend has also made pursuance of counter-cyclical policy difficult.

In sum, as the world economy braces for a possible second cycle of economic recession, opportunities to deploy counter-acting policy measures have reduced significantly. The developed economies have much less economic flexibility at present; to make a bad thing worse, new risks have appeared in the mean time. Indeed, the evolving adverse trends in the global economy are going to have cross-border spillover effects, affecting particularly the developing countries to various extent and degrees.

Outlook for South Asia

Dual Track

South Asia has been able to absorb the impacts of the global financial shocks rather well. The reason for this can be primarily attributed to the stellar economic performance of countries such as India and Sri Lanka. The South Asian economy is projected to grow at 7 per cent and 7.2 per cent in 2011 and 2012 respectively. Again, India is expected to be the major driver of this growth. The country with a population of 1.2 billion is expected to achieve GDP growths rates of 8.6 per cent and 9.1 per cent in 2011 and 2012. Sri Lanka is projected to grow at a slightly higher than the South Asian average growth rate of 7.8 per cent and 7.4 per cent over the next two years.

However, countries such as Nepal (4.3 per cent and 4.6 per cent) and Pakistan (3.8 per cent and 4.2 per cent) are estimated to grow at a much slower pace. This is likely to be the story in the near future for South Asia – India will continue to grow with dynamism whilst the other South Asian countries will have mixed fortunes.[7]

South Asian Resilience

The slowdown in the regional GDP growth rates by nearly 3 percentage points[8] was the least pronounced among the developing regions. The adverse effects were nevertheless significant – large negative output shocks, job, income and wealth losses, erosion of confidence, stock market declines, indirect contagion effects propagated by domestic financial markets, losses in exports and tourism, and pressure on the already-weak fiscal, BOP, reserves and exchange rates. However, these extents of the damage were eventually contained.

The macro impacts of the crisis were most severe on countries with weaker macroeconomic fundamentals and higher external vulnerabilities. These included in Maldives, Pakistan and Sri Lanka. The crisis also affected India because of the contagion

[7] UNDESA (2011).
[8] From a peak of 8.9 per cent in 2007 to 6.3 per cent in 2009.

impact in terms of spending; there was limited negative impact in other countries including Bangladesh, Bhutan and Nepal.

Some key factors insulated South Asia's growth during the crisis and have helped its strong recovery performance. Sources of this resilience included remittance inflow, export expansion, good agriculture production, and strong policy responses.

Decline in External Demand and Weakened Macroeconomic Fundamentals

Continued recession in the developed markets is affecting external sectors of the South Asian economies. Exports from South Asia are slowing in most recent months, including key exports such as garments. Remittances, thus far a key strength, is showing some signs of slowing down as well. The number of returning workers is rising further accelerated by recent Middle East unrest, as in the case for Bangladesh and Nepal.

Inflation, fuelled by the surging commodity prices (particularly oil prices), is volatile which poses special challenges for South Asia as a largely import-dependent region. Central banks of several countries such as Bangladesh, Pakistan and India responded by tightening monetary policy further. However, if this continues, it is likely to weaken domestic demand and economic growth in the near future.

It may be difficult for the individual countries in the region to come up with response mechanisms as they did at the time of previous economic crisis because of the following reasons:

- Limited fiscal space, most of the countries have already implemented austerity measures;
- High levels of public debt compared to the pre-crisis level;
- Inflationary pressure have resulted in central banks in the region to rise the interest rates; and
- Weakening of the United States Dollar (USD) would mean that regional currencies would not undergo significant devaluation against the USD.

The impact of a possible double-dip recession will also be felt differently by the different South Asian countries because of their varying sources of resilience and vulnerability. Thus there is a need for the governments of these countries to design and implement policies relevant to their country's needs and susceptibility.

Challenges for Bangladesh

All economic risks are cross-bordered, and are by and large inter-dependent. Thus, Bangladesh is no less threatened from the global risks and uncertainties. Despite having an estimated growth rate of 6.7 per cent in FY2010-11, several growing downside risks arising from external economic environment are exerting added pressure on her economy.

The transmission channels of the implications of global economic downturn for the Bangladesh economy are primarily mediated through trade, remittances, foreign aid and FDI.

European countries account for 50 per cent of Bangladesh's export basket. Major export destinations in EU-27 are – Germany, United Kingdom (UK), France, Spain, Italy, Belgium and Netherlands. Thus the current Euro debt crisis is likely to have adverse implications for Bangladesh's exports in general, and exports of apparels in particular, in the EU. First signs of this are already there. In view of this, Bangladesh will need to focus on extra-EU markets, particularly markets in the developing countries.

The knock-on effect on remittances may not be very high since about two-third of the remittance flow originates from the Middle East. However, the spectre of double-dip crisis in the developed world and the after-effects of the turmoil in the Middle East are likely to weaken remittance flow in the coming months.

Bilateral aid from the European countries (and Japan) may get constricted as the governments of these countries opt for austerity measures. However, a number of countries (e.g. UK) promised to stick to their pledge to expand the volume of official development assistance (ODA), which is good news for Bangladesh.

Crisis on Hand

In the event of another cycle of global economic crisis, it will be difficult for Bangladesh to come up with response mechanisms as she did in 2008, due to weakened macroeconomic fundamentals informed by surging non-development expenditures, pressure on BOP and high level of prices. These factors have eroded the fiscal and monetary space. On the other hand, Bangladesh should also be prepared to take advantage of the opportunities that may emerge. In the backdrop of current global situation and global demand, prices of key commodities in the international market, including that of fuel and key intermediates, could come down. This could help Bangladesh's macroeconomic balance. Demand switching could help some types of garments exports. Thus, there is a need to remain alert to such possibilities.

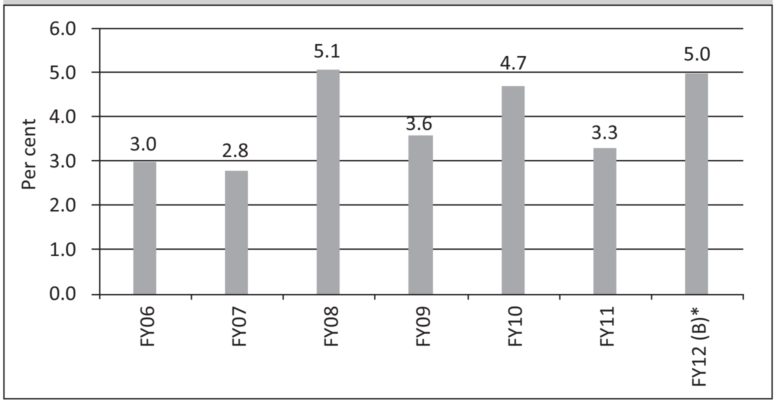
The global financial crisis that started in the US and Europe in 2008 had a lagged impact on the economy of Bangladesh resulting, by some estimates, in a 0.6 per cent loss of GDP growth.[9] It will be a challenge for the government to manage the economy in the current fiscal year in view of the emergent pressure points, whilst at the same time addressing the negative spillovers of the recent developments in the global economy.

1.3.2 Deepening Stresses in Public Finance Management

Managing Fiscal Deficit

Over the last few years, barring FY2007-08, fiscal deficit remained below 5 per cent of GDP. This has happened largely because of underutilisation of development funds underwritten by foreign (project) aid. In the budget for FY2011-12 a deficit of 5 per cent of GDP has been projected; total volume of the deficit being Tk. 45,204 crore. The projected deficit, in Taka terms, is 40.6 per cent higher than the actual deficit of the previous year. However, this proposed deficit figure remains within the trend (Figure 1.1).

Figure 1.1
Fiscal Deficit as Per cent of GDP



Source: Ministry of Finance (MoF).
Note: *B denotes Budget.

However, a major structural change has been envisaged in the financing plan of the budget deficit for FY2011-12 in comparison to the realised figures for FY2010-11. Concretely, 32.4 per cent and 67.6 per cent of budget deficit are to be financed

[9] Bhattacharya and Dasgupta (2011).

respectively from foreign and domestic sources in FY2011-12 (Table 1.4). The comparable actual figures for the previous year were 7.2 per cent and 92.8 per cent respectively. This means the government, in the current fiscal year, will have to secure foreign financing of almost six times more than the amount received in FY2010-11. The structural change programmed in the financing plan of the budget deficit relates to composition of the domestic sources of borrowing. If bank borrowing accounted for 87.6 per cent of the domestic sources of finance in FY2010-11, the comparable figures in the current fiscal year has been fixed at 69.7 per cent.

Table 1.4

Deficit Financing in FY2010-11 and FY2011-12

(Crore Tk.)

Source of Financing	Budget FY2011	Actual FY2011	Difference (Actual and Budget FY2011)	Budget FY2012
Foreign Borrowing (Net)	10834.4 (31.4)	2232.5 (7.2)	-8601.9	13058.0 (32.4)
Foreign Borrowing	15968.0 (46.3)	7659.7 (24.7)	-8308.3	18685.0 (46.4)
Amortisation	-5133.6 (-14.9)	-5427.3 (-17.5)	-293.7	-5626.7 (-14.0)
Domestic Borrowing	23679.6 (68.6)	28780.8 (92.8)	5101.2	27208.0 (67.6)
Bank Borrowing (Net)	15680.0 (45.4)	25210.2 (81.3)	9530.2	18957.0 (47.1)
Non-Bank Borrowing (Net)	7999.6 (22.2)	3570.6 (11.5)	-4429.0	8250.8 (20.5)
Total Financing	34513.9 (100.0)	31013.2 (100.0)	-3500.7	40266.0 (100.0)

Source: Ministry of Finance (MoF).

Note: Figures in parentheses indicate share in total financing.

Early figures for FY2011-12 suggest that both these programmed compositional changes are far from being on track. Indeed, inability to maintain these changes epitomise the current fault lines of fiscal management in Bangladesh economy. A closer look at these two critical variables will reveal the underlying entrenched problems of macroeconomic situation of the country.

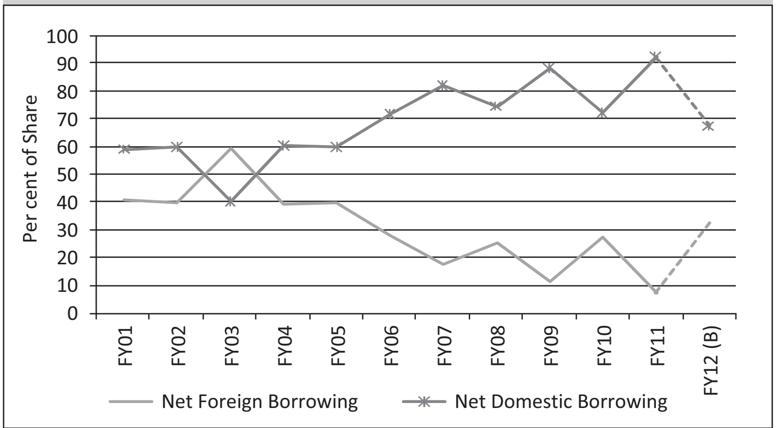
Marginalisation of Foreign Aid Inflow

Foreign aid inflow to Bangladesh economy has more or less steadily fallen during the current decade. This has led to an apparent fall in aid dependence of the country. However, development financing continued to remain critically dependent on foreign sources, particularly in the areas of social and physical infrastructure.

In FY2000-01, share of foreign sources accounted for about 40 per cent of the financing of fiscal deficit, which a decade later in FY2010-11, was only a little above 7 per cent of the same (Figure 1.2). The occasional rise in the share of foreign aid has been largely related to flow of humanitarian assistance during various natural disasters. This drop has very little to do with fall in aid commitment, as more than USD 13 billion remaining in the pipeline. Rather, it has mostly to do with the inability of government to keep up with the disbursement timeline due to failure in undertaking collateral preparations. Arguably, low absorption capacity of the economy is partly responsible for the emerging situation. The direct fall out of such a negative trend had been low utilisation of project aid, leading to low delivery of ADP. In some cases, it has led to substitution of foreign financing by domestic resources.

Figure 1.2

Sources of Financing



Source: Ministry of Finance (MoF).

During July-September 2011, Bangladesh received USD 246.2 million in aid, while amortisation accounted for USD 171.8 million resulting in net flow of only USD 74.4

million. This figure happens to be USD 98.6 million (57 per cent) less than the comparable figure for the preceding year.

Recent developments in Bangladesh government's relationship with the major development partners indicate that this trend may not improve readily. For example, large part of the programmed foreign aid inflow was attributable to release of early trenches of the foreign fund earmarked for the *Padma Multipurpose Bridge* which is currently facing a standoff. Postponement of the meeting of the Bangladesh Development Forum (BDF) signals the complexity currently afflicting the government's relationship with its international development partners. It may be safely underscored that without substantial increase in foreign aid flow, macroeconomic stability will remain under serious threats.

What are the options for the government in this regard? *First*, the government should put its best foot forward to get the committed foreign funds disbursed for the ongoing projects. Indeed, this will require project-by-project intensive monitoring jointly with the partners. A number of useful operational suggestions are available in this regard which only need to be acted upon with utmost urgency and sincerity.

Second, the government may intensify its effort to get budgetary support from the international and regional financial institutions. However, with the Padma Bridge impasse, World Bank will be hardly forthcoming to provide a budget support. The planned visit of the International Monetary Fund (IMF) Mission in December may decide on a programme loan. However, the fiscal and other conditionalities usually associated with such loans call for caution. One would suspect, given the dire state of public exchequer, the government will have little flexibility to cautiously consider the conditionalities associated with such loans.

Third, the government may be prompted to go to the global market to secure high cost commercial loan by issuing Sovereign Bonds. Getting loans from foreign private sources to finance fiscal deficits, brought about by high level subsidy offtake, will not be prudent. Indeed, this type of loans, carrying high foreign exchange risk, is not at all acceptable under the growing pressure on the BOP.

Beyond these above mentioned three avenues, Bangladesh can also improve her non-debt creating foreign sources such as export revenue, remittance flow and FDI. Whatsoever, without higher level of access to foreign financing in FY2011-12, Bangladesh economy is going to undermine not only its growth prospect, but also weaken further its macroeconomic stability.

Heavy Bank Borrowing

The second important destabilising factor for public finance in the current fiscal year is likely to be the high bank borrowing by the government. In fact, as mentioned in the earlier section of the review, this issue did emerge as a significant problem for macroeconomic management in FY2010-11; as high as 81.3 per cent of the fiscal deficit of FY2010-11 was financed through bank borrowing. If mitigating steps are not taken, this trend is apprehended to be heightened further in the current fiscal year.

The budget for FY2011-12 targets to finance 47.1 per cent (Tk. 18,957 crore) of the projected deficit through bank borrowing (Tk. 6,253.2 crore less than the actual borrowing in FY2010-11). However, there is every likelihood that this target will be missed by a significant margin. According to Bangladesh Bank, the government has already borrowed Tk. 9,470 crore till 10 October 2011, which is about 50 per cent of its total allocation for the year. In other words, the government has borrowed about Tk. 100 crore everyday to run its business.

Considerable rise in subsidy demand is likely to push up financing requirement. At the same time, existing high interest rates of the commercial banks undermines the potentials of mobilising fund from non-bank sources. If so happens, in this time of high inflation and high interests on credit along with weakened Taka against other currencies, further substantial rise in government borrowing from the banking system could lead to deterioration in all these indicators along with a crowding out effect for the private sector from their access to credit.

What are the options for the government in this regard? *First*, the government has to rein-in its financing requirement, particularly by downsizing its subsidy demand (discussed later). *Second*, the government may augment offtake from the untapped domestic resources. Non-tax revenue sources constitute a potential source in this regard (discussed later). *Third*, the government may seek to meet its incremental borrowing need from non-banking sources by increasing the sale of national saving instruments through increasing their yield rates. If all these are not enough, it may have to cut down its development expenditures.

Enhancement of Non-Tax Revenue Collection

While the overall revenue collection has been impressive in recent times, non-tax revenue collection has remained depressed. It may be recalled that in FY2010-11 non-tax revenue collection declined over that of FY2009-10 by (-) 12.3 per cent. In FY2011-12, this source is programmed to contribute more than 19 per cent of the total revenue collection. Against a target of almost doubling its collection (92.1 per cent target growth), actual intake during the first month (July 2011) had been (-) 12.3 per cent less compared to that of the first month of FY2010-11.

However, collection of license renewal and spectrum fees from the mobile network operators had already started to flow in, and the government is likely to get some relief in securing non-tax revenue from such fees this year. A total of Tk. 3,746 crore is to be paid by four telecom operators by 10 November 2011. Total revenue over the next one and half years, from these sources, is estimated at Tk. 8,000 crore, with the remaining to be paid.

As the NBR continued to deliver, achieving the overall revenue target for FY2011-12 will critically depend on improved non-tax revenue mobilisation and to a lesser extent on non-NBR taxes (accounting for about 5 per cent of the total intake).

Can the fiscal balance be strengthened given the realistic prospects of augmenting foreign aid flow, decreasing domestic borrowing requirement and fuller collection of revenue targets? Possibly not. One would possibly need to streamline elements of public expenditures to achieve the balance. Indeed, some of the adverse financing requirements are associated with the current public expenditure profiles, e.g. domestic borrowing and subsidy payments.

Rising Revenue Expenditure

A significantly high growth of 20.5 per cent in revenue expenditure has been envisaged in the budget for FY2011-12. Besides Block Allocation, high expenditure growth is to take place in case of Subsidies and Transfer (23.8 per cent), Interest Payments (20.4 per cent), and Goods and Services (19.7 per cent). In the first month of the current fiscal year higher offtake in case of a number of important expenditure items is evident, e.g. Pay and Allowances (19.6 per cent) and Interest Payments (21.7 per cent) (Table 1.5).

Table 1.5
Revenue Expenditures

(Crore Tk.)

Expenditure Category	Budget FY2011	Actual FY2011	Budget FY2012	Difference Actual FY2011 and Budget FY2011	Actual Growth FY2011 (%)	Target Growth FY2012 (%)	Actual Growth (July FY2012) (%)
Pay and Allowances	20374.6 (26.5)	19764.9 (27.1)	21640.0 (24.6)	-609.7	23.2	9.5	19.6
Pay of officers	1908.9 (2.5)	2071.4 (2.8)	2190.0 (2.5)	162.5	19.1	5.7	8.6
Pay of establishment	8656.4 (11.3)	8649.6 (11.9)	9154.0 (10.4)	-6.8	14.7	5.8	4.5
Allowances	9809.3 (12.8)	9043.9 (12.4)	10296.0 (11.7)	-765.4	33.6	13.8	54.4
Goods and Services	10413.3 (13.6)	9837.2 (13.5)	11772.0 (13.4)	-576.1	11.2	19.7	97.1
Supplies and services	7522.2 (9.8)	6842.7 (9.4)	8610.0 (9.8)	-679.5	11.0	25.8	99.0
Repairs, maintenance and rehabilitation	2891.1 (3.8)	2994.5 (4.1)	3162.0 (3.6)	103.4	11.5	5.6	25.0
Interest Payments	14708.8 (19.2)	14942.5 (20.5)	17997.0 (20.5)	233.7	0.5	20.4	21.7
Domestic	13270.7 (17.3)	13519.6 (18.6)	16519.0 (18.8)	248.9	0.2	22.2	21.7
Foreign	1438.1 (1.9)	1422.9 (2.0)	1478.0 (1.7)	-15.2	3.8	3.9	-
Subsidies and Current Transfers	29793.3 (38.8)	27972.2 (38.4)	34642.0 (39.4)	-1821.1	3.7	23.8	7.0
Subsidies	7661.2 (10.0)	7933.7 (10.9)	9286.0 (10.6)	272.5	5.7	17.0	-
Grants in aid	17951.8 (23.4)	14500.3 (19.9)	20290.0 (23.1)	-3451.5	-3.2	39.9	8.1
Contributions to international organisation	86.4 (0.1)	28.0 (0.0)	91.0 (0.1)	-58.4	-63.8	225.0	-
Pensions/gratuities/write-off of loans/advances	4093.9 (5.3)	5510.3 (7.6)	4975.0 (5.7)	1416.4	25.4	-9.8	5.3
Block Allocation	1472.5 (1.9)	362.5 (0.5)	1800.2 (2.0)	-1110.0	29.8	396.6	-133.3
Unexpected	1000.0 (1.3)	80.2 (0.1)	1100.0 (1.3)	-919.8	33.0	1271.6	-
Others	472.5 (0.6)	282.3 (0.4)	700.1 (0.8)	-4443.0	29.0	2382.3	-133.3
Non-Development Revenue Expenditure (not adjusted for recoveries)	76762.5 (100.0)	72879.3 (100.0)	87851.2 (100.0)	-3883.2	8.8	20.5	17.6

Source: Ministry of Finance (MoF).

Note: Figures in parentheses are shares of total non-development revenue expenditure.

What will be of crucial importance from revenue expenditure perspective in the coming months, is the developments in subsidy requirements. Economic classification of revenue expenditure, as reflected in Table 1.5, however shows low growth in subsidies. But this Subsidies and Transfers does not include subsidy sources such as BPC, Bangladesh Power Development Board (BPDB), agricultural and others in which major upturn in demand is noticeable.

Upsurge in Subsidy Demand

Total subsidy demand for the current fiscal year was initially estimated at about Tk. 22,500 crore, which is now anticipated to rise to about Tk. 47,400 crore, if no price adjustments are made. If that be the case, share of subsidy expenditures may increase to 29 per cent instead of 12.5 per cent of the revenue budget for FY2011-12. It would imply that subsidy payments will be equivalent to 5.3 per cent of GDP instead of 2.3 per cent as foreseen in the budget for FY2011-12. This will be a remarkable increase from 2.2 per cent of GDP in FY2010-11 (revised budget). In other words, about half of what is collected as revenue will go for paying subsidy.

Bulk of this subsidy originates from BPC, the soul merchandiser of petroleum products in the country. While the budget for FY2011-12 kept only Tk. 3,500 crore for BPC, it is now apprehended that BPC alone might require over Tk. 28,000 crore in subsidy (Table 1.6). During FY2010-11, a whoopping 69.7 per cent growth in total petroleum import was recorded. BPC report shows substantial increase in imports of furnace oil and diesel during FY2010-11, compared to FY2009-10. In volume terms, refined petroleum products (mostly diesel) contributed 55.5 per cent in the total petroleum import growth (incremental contribution) in FY2010-11. Another 20.5 per cent of the incremental growth came from import of furnace oil. In value terms as well, substantial part of the growth in FY2010-11 came from diesel (70.6 per cent) and furnace oil (9.6 per cent). To a large part, this growth structure reveals the additional demand originating from the rental and quick rental power plants. Starting from FY2009-10, 14 (quick) RPPs became operational till October 2011, adding 1,320 mega watts (MW) of power to the national grid. According to the original plan, a total of 24 rental plants are to be set up. Therefore, more liquid fuel demand will be adding up in near future, pushing the subsidy demand further up.

Table 1.6

Subsidy Requirements in FY2011-12

(Crore Tk.)

Sector	Revised Budget FY2011	Budget FY2012	Revised Requirement FY2012	Share of Total Subsidy (Revised Requirement) (%)
BPC	4000	3500	28014	59.1
Agriculture	5700	4500	6835	14.4
BPDB	4000	5200	5200	11.0
Export	2000	2200	2200	4.6
Food	1653	1677	1736	3.7
SoEs	358	3400	3400	7.2
Total	17711	20477	47385	100.0
Per cent of Budget	13.3	12.5	29.0	-
Per cent of GDP	2.2	2.3	5.3	-

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

It is pertinent to mention here that fertiliser subsidy is also on the rise due to over 100 per cent increase in international price. Besides, agriculture sector as a whole might require Tk. 6,835 crore in FY2011-12, i.e. an additional Tk. 2,300 crore more in subsidy than the original projection.[10]

On the other hand, BPDB placed a subsidy demand of Tk. 5,200 crore to the Ministry of Finance (MoF) for the current fiscal year[11] in line with the budget allocation for FY2011-12. Similarly, Tk. 2,200 crore will be necessary for payment of various export incentives, Tk. 1,736 crore for food operations, and Tk. 3,400 crore for the state-owned enterprises (SoEs).

What are the options for the government to deal with this unsustainable subsidy payment situation? The government will not be able to underwrite this mounting expenditure by incremental revenue collection. It is also not a sustainable proposition to resort to more domestic borrowing – either from bank or non-bank sources – to pay the subsidy bills. Thus, the government, as such, is left with no other viable policy choices to adjust fuel and power prices upward in a phased manner. The government may consider bringing up diesel, octane, kerosene and furnace oil prices in line with the prices in India

[10]Subsidy for agriculture sector include subsidy for fertiliser as well as for diesel and electricity used for irrigation.

[11]In its recent proposal for power price revision placed to the Bangladesh Energy Regulatory Commission (BERC), BPDB projected that the subsidy demand may reach over Tk. 7,340 crore, if no price adjustments are made.

(also to pre-empt smuggling out). Currently prices in India of these products are higher than those in Bangladesh, by on average, more than Tk. 10 per litre. However, such price enhancement may further aggravate the prevailing spiralling price situation. It is hoped that part of it will be off-set by reduced government borrowing, and better access of the private sector to bank credits for productive purposes, as well as stable agriculture production. However, in order to protect the farmers, subsidy on diesel and electricity may be supplied through designated cards.

Only bulk and rental price adjustment of energy products alone will not do the trick. Concerns also emerge from the fact that the government is planning to phase out the rental plants not before 2014. This will require new public plants to take over the production deficit. Although there are plans for new public plants, no visible progress in this regard is evident. In fact, power generation from public plants (other than rental, quick rental and independent power producer (IPP)) has declined by about 518 MW over the last one year. If the plan for new public plants does not materialise, then the heavy toll that the rental plants have had so far on the petroleum budget and will continue to have over the next few years, will all go in vain.

It needs to be emphasised here that there is a serious lack of information on both subsidy allocation and expenditure by the government. The Budget Documents do not provide any comprehensive subsidy estimate, other than some scattered information on agricultural subsidy allocation. Actual subsidy expenditure is also not published. Given the fact that subsidy expenditure has emerged as the core destabilising feature of the economy, greater transparency is required in this area for the citizens to appreciate the problem.

Check on Interest Payments and Public Debt

Both domestic and foreign interest payments, as share of revenue budget, declined during the last two fiscal years (FY2009-10 and FY2010-11) (Table 1.7). This happened largely because interest rates were low for domestic loans during this period. The budget for FY2011-12, however, projects significant rise in interest payments (by 20.4 per cent). In the first month of FY2011-12, significant increase (21.7 per cent) in domestic interest payments has been recorded. Heightened bank borrowing that was made in FY2010-11, and is likely to be made again in the current fiscal year, could lead to an increase in the share of domestic interest payments in the coming years.

Table 1.7

Share of Interest Payments in Total Revenue Budget

(in Per cent)

Interest Payments	FY2006	FY2007	FY2008	FY2009	FY2010	FY2011	FY2012 (B)
Total Interest Payments	14.3	14.0	15.0	15.7	14.6	12.1	11.0
Domestic	12.1	12.0	13.4	14.2	13.3	10.9	10.1
Foreign	2.3	2.0	1.5	1.5	1.3	1.2	0.9

Source: Ministry of Finance (MoF).

On the other hand, in the backdrop of much diminished flow of foreign aid, interest payments on foreign loans is eating up bulk of the inflow. For example, in FY2010-11 it was as high as 63.7 per cent of gross annual foreign aid.

While remaining concerned with the flow figures, one should not fail to look at the stock figures regarding foreign and domestic borrowings. Total public debt as a share of GDP from the recent peak of 53.7 per cent in FY2001-02 has come down to 38.7 per cent in FY2010-11. This encouraging trend is essentially underpinned by steady decline in Bangladesh's foreign debt. In contrast, domestic debt as a share of GDP is showing increasing trend. The concerned figure was 19.9 per cent of GDP in FY2010-11, up from 18.9 per cent of GDP in FY2009-10.

Given the recent experience with public debt stock, particularly in the developed countries, Bangladesh government will be well-advised not to lose the comfortable space in macroeconomic management which it currently enjoys regarding the public debt situation.

Delivering ADP

ADP expenditure has increased during the initial months of FY2011-12, owing to certain improvement in its implementation rate, from 9 per cent in the first quarter of FY2010-11 to 11 per cent during the same period in FY2011-12. Expenditure on account of project aid declined further during the first quarter of FY2011-12 to only 4 per cent from 5 per cent recorded in the corresponding period of the previous year. Accordingly, the incremental part of the implementation improvement, albeit marginally, was underwritten by domestic resources, adding to the government's borrowing requirement from the banking system.

In spite of the heightened importance of ensuring project aid flow in the current fiscal year, a further deterioration in the situation is evident. Table 1.8 bears this out clearly, reflecting the low implementation of aid component by the largest 10 recipients of ADP allocation. On the other hand, 15 per cent (Tk. 4,011 crore) of the Taka component has been utilised so far, which was 11 per cent (Tk. 2,518 crore) during the first quarter of the previous fiscal.

Table 1.8

Aid Utilisation by the Top 10 Recipient Ministries/Divisions during FY2011-12 (July-September)

(Crore Tk.)

Ministry/Division	Allocation of Aid	Expenditure of Aid	Rate of Aid Utilisation (%)
Bridges Division	3452	6	0.2
Roads Division	1461	14	1.0
Ministry of Water Resources	820	12	1.4
Energy and Mineral Resources Division	679	14	2.0
Local Government Division	5461	142	2.6
Power Division	2727	104	3.8
Ministry of Education	1503	90	6.0
Ministry of Primary and Mass Education	650	53	8.2
Railway Division	1245	141	11.4
Ministry of Health and Family Welfare	61	17	27.8
Total (Top 10 Recipients)	18059	594	3.3
Share in Total ADP (%)	39.3	3.2	-

Source: Implementation Monitoring and Evaluation Division (IMED).

Sustaining NBR Revenue Earnings

As was mentioned earlier, NBR continued with its robust performance in FY2010-11 (Table 1.9). For FY2011-12, a 16.2 per cent growth target has been set for the NBR. What is of concern is that during the first quarter (July-September) of the current fiscal year, some slowdown in NBR revenue collection is evident. This is particularly true for revenue collection at the local level, especially for VAT and supplementary duty (SD) collection, which could imply a slowdown in the domestic economy. Income tax collection, however, sustained its impressive trend.

Table 1.9

NBR Revenue Collection

(in Per cent)

Category	Actual Growth FY2011	Target Growth FY2012	Growth FY2012 (Jul-Sep)
Import Duty	22.8	8.8	18.7
VAT (Import)	19.9	11.1	0.3
SD (Import)	28.4	10.5	26.3
VAT (Local)	28.9	15.7	11.4
SD (Local)	27.8	21.5	16.0
Income Tax	32.4	21.4	24.9
Others	25.9	25.0	21.5
Grand Total (NBR)	27.2	16.2	15.2

Source: National Board of Revenue (NBR).

While NBR tax collection at the import stage has been quite impressive so far, this growth may suffer in the coming months as can be predicted from the recent slowdown in imports. As against 41.8 per cent growth in imports in FY2010-11, only 16.5 per cent growth has been recorded during the first two months of FY2011-12 over the corresponding period of the previous fiscal. Thus, it will be a matter of great interest to observe whether NBR continues to provide additional revenue to underwrite the government's increasing expenditure needs.

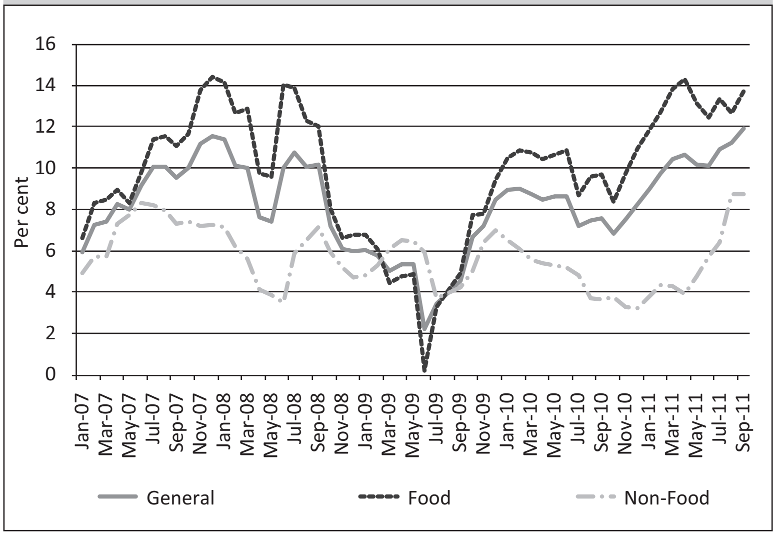
In fine, streamlining of public finance management has become an immediate priority so as to protect the medium-term growth prospect.

1.3.3 Unabated Price Inflation

Inflationary Trends

Inflation appears to have emerged as a permanent phenomenon in the economic landscape of Bangladesh over the recent past. It has started to increase since the second quarter of FY2009-10, and continued to rise throughout FY2009-10 and FY2010-11. During the first three months of FY2011-12 there has not been any change in the direction of inflationary movements. The 12-month point-to-point Consumer Price Index (CPI) inflation has reached as high as 11.97 per cent in September 2011 compared to 7.61 per cent in September 2010. This is the highest inflation in last one decade. As in most years, food inflation was higher than general inflation. Food inflation reached to 13.75 per cent in September 2011 as opposed to 9.72 per cent in September 2010 (Figure 1.3). High food inflation had a knock-on effect on non-food inflation as well, pushing it upward to settle at 8.77 per cent in September 2011 from as low as 3.69 per cent in September 2010. This reflects that prices of food and non-food items tend to move along the same direction, though at a different pace. Another feature of recent inflation in Bangladesh is that rural food inflation has been closer to urban food inflation which was not the case in Bangladesh till August 2010. The likely causes for high rural inflation could be increasing demand due to higher purchasing power of the rural population through rising agricultural production, higher labour wages, expanded social safety net programme, and inflow of remittances. If compared with other South Asian countries Bangladesh stands second, next to Pakistan, in terms of the record of inflation rate in the region. Despite higher food price in the international market, India has been able to keep its food price index down through higher production of major crops and by ensuring adequate supply in the domestic market. Pakistan epitomises the case of a conflict economy with a high inflation rate and a very low growth rate.

Figure 1.3
Point-to-Point Inflation Rate of Bangladesh



Source: Bangladesh Bureau of Statistics (BBS).

Underlying Causes of High Inflation

A widely discussed plausible cause of high inflation in Bangladesh is the impact of global price hike. As a food and petroleum-importing country, Bangladesh has to bear the brunt of global price hike of these items. Since the beginning of the current decade and up to 2008, global prices of fuel and food followed an increasing trend which got transmitted into the country's domestic economy. There has been some respite from high inflationary pressure towards the end of 2008 and 2009 due to the global meltdown and the resultant price fall of major commodities in the global market. With the turn around of the global economy from the recession towards the end of 2009 and beginning of 2010, inflation started to shoot up. This trend was also observed in Bangladesh.

The other major source of high inflation in Bangladesh is high food inflation. The reason behind this assumption is that food carries a large weight in the CPI of Bangladesh. The weight of food items in the CPI commodity basket of Bangladesh is as high as 58.8 per cent, of which the share of rice is 20.1 per cent. Hence the rise in food inflation affects the overall inflation significantly. Based on the BBS data, it has been estimated that the contribution of rice inflation to the overall inflation was 23.41 per cent during September of FY2011-12 (Table 1.10).

Table 1.10

Contribution of Food and Non-Food Items to General CPI Inflation

(in Per cent)

Year	General Inflation	Food Inflation	Non-Food Inflation	Food Contribution in Inflation	Rice Contribution in Inflation	Non-Food Contribution in Inflation
FY2000-01	1.94	1.38	3.04	41.86	14.30	58.14
FY2001-02	2.79	1.63	4.61	34.38	11.74	65.62
FY2002-03	4.38	3.46	5.66	46.48	15.88	53.52
FY2003-04	5.83	6.93	4.37	69.94	23.89	30.06
FY2004-05	6.49	7.90	4.33	71.62	24.47	28.38
FY2005-06	7.16	7.76	6.40	63.77	21.78	36.23
FY2006-07	7.20	8.11	5.90	66.28	22.64	33.72
FY2007-08	9.94	12.28	6.32	72.69	24.83	27.31
FY2008-09	6.66	7.19	5.91	63.52	21.70	36.48
FY2009-10	7.31	8.53	5.45	68.66	23.45	31.34
FY2010-11	8.79	11.33	4.15	75.85	25.91	24.15
FY2011-12*	11.41	13.28	8.00	68.52	23.41	31.48

Source: Based on the Bangladesh Bank data.

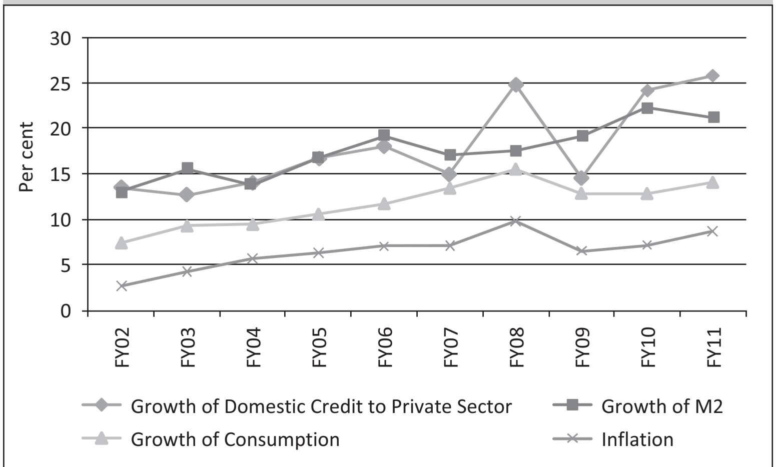
Note: Base: 1995-96=100. Weight: General=100; Food=58.84; Rice=0.1; Non-Food=41.16; Contribution of food/rice/non-food is calculated as the share (weight) of food/rice/non-food in general CPI, multiplied by food/rice/non-food inflation, divided by overall inflation rate.

*Up to September 2011.

Growth in money supply is considered to be another contributing factor of high inflation in Bangladesh. An examination of the trends of these factors during the last 10 years reveals that the relationship between growth in money supply and inflation has not been unidirectional all along. Though they moved along the same direction over the major part of the period between 2001 and 2011, no causal relationship could be established between growth of money supply and inflation in the short-run (Figure 1.4). However, in the long-run, a positive relationship is observed between these two variables (CPD 2011). The other two possible sources of high inflation could be growth in credit to the private sector and growth in consumption. As in the case of money supply these two factors do not follow the same growth path as inflation in the short period.

Figure 1.4

Growth of Money Supply, Credit to Private Sector, Consumption and Inflation



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

Food Scenario: Production, Procurement and Prices

Food production during FY2011-12 is projected to increase by 3.5 per cent, of which the growth of rice will be 3.6 per cent. This year procurement of Boro rice by the government reached 8.12 lakh metric tonnes (MT) (during 5 June to 29 October 2011) exceeding the target of 6 lakh MT. Till 29 October 2011, storage of foodgrains was 15.18 lakh MT which is 97 per cent higher than that of the last year. There was a focus on public import of foodgrains instead of relying solely on private import. In FY2010-11, the share of foodgrains import by the government was approximately 41 per cent.

Prices of essential commodities have been on the rise since 2008 and the rice market in Bangladesh continues to remain volatile. However, the retail price of coarse rice in local market has shown a declining trend, and has reached Tk. 30-32/kg at present compared to Tk. 35.3/kg in January 2011, and Tk. 34.57/kg in April 2008. However, this is still higher than that of the recent past. In fact, since November 2009, rice prices started to decline and reached the lowest level at Tk. 20.42/kg in April 2010. Between July-May of FY2007-08 and July-May of FY2010-11 rice price increased by 23 per cent in the local market. However, prices crossed Tk. 30/kg again in July 2010 and the trend has persisted till now.

Policy Initiatives

Monetary Measures

In its MPS for the period of July-December FY2010-11, Bangladesh Bank targeted for an inflation rate of 7 per cent by the end of FY2010-11 primarily through discouraging credit flow to unproductive sectors (Table 1.11). At the time of the announcement of the MPS, monetary aggregates were already on increasing trends. In a move to control diversions and unproductive use of funds, Bangladesh Bank has been using its monetary policy tools more frequently in recent times than before. As was mentioned earlier, the CRR and SLR were increased twice, and rates of Repo and Reverse Repo have been raised thrice in the last fiscal year. To discourage loans to unproductive sectors and to control inflation, Bangladesh Bank has also withdrawn the lending cap for most sectors. These moves were not immediately effective in controlling liquidity expansion due to delayed response on the part of the Central Bank. However, there has been a moderate decline of M2 and credit to the private sector in September 2011 as a result of restraining monetary policy stance of Bangladesh Bank. The growth of credit to the public sector has, however, been significantly high between September 2010 and September 2011 (Table 1.12). Increased borrowing by the government from domestic sources has contributed to continuing high inflationary trend notwithstanding reduction in money supply.

Table 1.11

Monetary Policy Stances of Bangladesh Bank

Period	Monetary Policy Stance
January-June 2009	**Accommodative**; priority is given to providing credit support for creation and expansion of output capacities rather than for stoking of demand pressures
July-December 2009	**Accommodative**; greater directional emphasis on the credit needs of sectors like agriculture and small and medium enterprise (SME) that are typically underserved by the market
January-June 2010	**Accommodative**; special attention to programmes pursuing fuller financial inclusion of the economic activity segments (including agriculture and SMEs) and population segments that are underserved by the markets, towards fostering inclusiveness of economic growth
July-December 2010	**Accommodative**; special attention to financial inclusion of agriculture, SMEs, renewable energy, and ecological footprint minimising technology sectors
January-June 2011	**Accommodative**; in support of the government's goals of faster inclusive economic growth and poverty reduction besides maintaining monetary and price stability
July-December 2011	**Restraining**; in the context of unfolding near-term development and ensuring adequate credit flows to the productive sectors

Source: Monetary Policy Statements, Bangladesh Bank.

Table 1.12

Selected Monetary Indicators

(Crore Tk.)

Indicator	FY2011 (Sep 2010)	FY2012 (Sep 2011)	Change between September 2010 and September 2011 (%)	Change between September 2009 and September 2010 (%)
Domestic Credit	356498.70	449930.10	26.21	20.33
Credit to Public Sector	69256.10	99555.10	43.75	-0.28
Credit to Private Sector	287242.60	350375.00	21.98	26.65
M2	379095.60	453397.60	19.60	21.48
Reserve Money	82422.00	97013.90	17.70	10.48

Source: Bangladesh Bank.

Fiscal Measures

Major fiscal policy of the government towards addressing the high inflation rate and ensuring food security has been the reduction of import duty on rice and wheat, provision of credit to food importers at subsidised rates, cash transfer, allocation of funds to increase supply, and expansion of the operation of Public Food Distribution System (PFDS). Total distribution under PFDS has increased due to the higher level of distribution under priced channels, even though distribution under non-priced channels has decreased sharply. Distribution through priced channels has observed a significant rise due to government's intensive OMS and fair price drives. The government is also distributing foodgrains among the fourth-class government employees since February 2011. Foodgrains distribution is taking place among the Fair Price Card-holders across the country through which each cardholder can purchase up to 20 kg of foodgrains at a cheaper rate. During the period July to 20 October 2011, distribution of foodgrains amounted to 4.2 lakh MT which is reportedly an increase by 30 per cent compared to what was in the last year during the same period. During the last three fiscal years about 30 per cent of the total budget for social safety net programmes has been allocated for food security (Table 1.13).

Table 1.13

Food Security Budget as a Percentage of Total Safety Net Budget

(Crore Tk.)

Component	Budget FY2010	Budget FY2011	Budget FY2012
Food security budget	5877.81	5726.25	7102.57
Total safety net budget	17327.33	19496.99	22556.05
Food security as share of total safety net (%)	34.00	29.00	31.00

Source: Ministry of Finance (MoF).

There is no denying that PFDS has eased the pressure of high inflation on the low-income households. However, given the large number of people living below the poverty line and the limited nature of effort by the government, which is concentrated mostly within the periphery of urban centres, it is likely that significant number of poor people remains outside the coverage of PFDS. While efforts are needed to expand programmes to ensure food security, pre-emptive and decisive monetary policy should also be in place to rein the high inflation in. In view of the slower growth of money supply in the recent period compared to the last fiscal, the effectiveness of the contractionary monetary policy adopted by the Central Bank has been proved. This, however, is not a panacea to contain inflation, particularly in the medium-term, as the demand for domestic investment by the private sector remains high, and constraints to access credit will further affect the investment scenario which in turn will have adverse consequences for the overall growth of the economy. Monetary policy will also have to be coordinated with effective fiscal management (details in Section 1.3.2) if Bangladesh is to reduce the current inflationary pressure.

1.3.4 Increasing Pressures on the External Balance

Signs of Strains in Traditional Dependable Export Destinations

The extraordinary high export growth observed in FY2010-11 had started to slow down in the first quarter of FY2011-12, though the pace of growth is ahead of the target set for the current fiscal year. During the first three months of FY2011-12, total export earnings registered a 22.6 per cent growth (Table 1.14), which was impressive considering that this growth was attained over the aforesaid high benchmark.[12] A decomposition of export performance for the first quarter of FY2011-12 reveals that export growth of the dominant RMG sector was outpaced by that of non-RMG sector: RMG export increased by 21.2 per cent[13] while for non-RMG export the rate of growth was 27.6 per cent.

Table 1.14

Export Performance

(in Per cent)

Product	Growth Target for FY2012	Growth in FY2012 (Jul-Sep)	Growth in FY2011 (Jul-Sep)	Required Growth for Rest of the Year to Attain Export Target
RMG	13.7	21.2	31.0	11.5
Knitwear	*13.9*	*18.3*	*31.9*	*12.6*
Woven wear	*13.4*	*24.8*	*30.0*	*10.3*
Non-RMG	22.5	27.6	26.1	21.1
Raw Jute	*30.0*	*18.7*	*53.8*	*32.1*
Leather	*10.0*	*20.0*	*42.2*	*7.2*
Total	15.6	22.6	30.0	13.6

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

In the first quarter of FY2011-12, some progress was observed in case of export market diversification. Export earnings from new markets (other than US, EU and Canada) increased significantly[14], by 36 per cent over the corresponding figure for last year. Over the same period, export to EU and Canada increased by 28.8 per cent and 16.4 per cent respectively. Germany, UK, France, Spain, Italy, Belgium and Netherlands remained the major export destinations in EU-27. In spite of the crisis engulfing the Eurozone, significant export growth was attained in such crisis-impacted economies as Spain (48.3 per cent) and Italy (47.4 per cent).[15] The revised Rules of Origin (RoO) under the EU-GSP (Generalized System of Preferences) scheme may have contributed to this export boost in the EU, particularly favouring export of woven wear. Significant rise in exports to India, from USD 92 million to USD 143.1 million, may have originated from effective utilisation of the tariff rate quota (TRQ) of 10 million pieces.[16] Recently, India has downsized her sensitive list for least developed countries (LDCs) under the South Asian Free Trade Area (SAFTA), granting duty-free import of 46 items of which 45 are RMG. Bangladesh's global export of these 45 products accounted for 87.5 per cent of her total RMG export and 68.5 per cent of the total export. Hence, given Bangladesh's competitiveness in export of these 45 items globally, Bangladesh may be able to harness benefit by exporting these items to India.

On the other hand, in 2010, Turkey imposed a countervailing duty of 17 per cent on imports from LDCs. During the first quarter of FY2011-12, Bangladesh's export to Turkey decreased by (-) 0.4 per cent. Given the fact that Turkey is the fourth largest export destination for Bangladeshi products, there is a need for renewed attention to this particularly important export destination. It is important to note that, export to US, the second largest export destination for Bangladeshi products, decreased by (-) 1.7 per cent

[12] During the first three months of FY2010-11, total export posted a 30 per cent growth.
[13] This was 31 per cent during the first quarter of FY2010-11.
[14] During the first quarter of FY2011-12, total export to Japan increased by 72.1 per cent, India by 55.5 per cent, Australia by 56.6 per cent, and China by 94 per cent.
[15] Export to Ireland and Portugal also increased by 16.6 per cent and 17.6 per cent respectively in the first quarter of FY2011-12. However, export to Greece, the country in most fragile situation, declined by (-) 0.6 per cent.
[16] In 2010, India enhanced the duty-free TRQ from 8 million pieces to 10 million pieces for Bangladesh.

during the first three months of FY2011-12, when export of RMG declined by (-) 0.8 per cent[17] and that of non-RMG declined by (-) 12.4 per cent.[18]

However, it is notable that the export performance of September is transmitting some disquieting signals. Month-on-month analysis shows that in September FY2011-12, RMG export declined by (-) 6.6 per cent; indeed, export of knitwear decreased by (-) 12.3 per cent (Table 1.15). As a result, growth of export earnings in September 2011 was a mere 2.4 per cent. RMG export to US was particularly bad in September 2011, declining by (-) 17 per cent; export of knitwear declined by (-) 37.4 per cent.[19] As a matter of fact, Bangladesh's global export of knitwear for the month of September 2011 had declined in EU, her traditional market, as well as to the rest of the world. Such gloomy situation in RMG export (particularly knitwear) might have originated from lower price of cotton[20], which has reduced the price of garment products (particularly knitwear) in all important markets. RMG export shock came at a time when uncertainty is looming as regards any speedy recovery of the global economy. At the same time, new threats also evolved as India and Peru moved away from their position against Pakistan's claim for duty-free access to the EU under special consideration as part of the EU-GSP scheme.[21] Bangladesh needs to analyse the impacts of these developments taking place at the global level and formulate appropriate strategies to deal with attendant concerns.

Table 1.15

Bangladesh's Export Growth: FY2011-12

(in Per cent)

Product	World		US		EU		Rest of the World	
	Q1 FY12	Sep FY12	Q1 FY12	Sep FY12	Q1 FY12	Sep FY12	Q1 FY12	Sep FY12
Total Export	22.6	2.4	-1.7	-15.0	29.8	2.8	32.4	17.5
RMG	21.2	-6.6	-0.8	-17.0	30.0	-0.9	30.7	-5.9
Knitwear	*18.3*	*-12.3*	*-16.8*	*-37.4*	*25.7*	*-4.1*	*20.3*	*-21.1*
Woven wear	*24.8*	*0.5*	*6.0*	*-8.4*	*39.2*	*6.4*	*42.8*	*14.0*
Non-RMG	27.6	30.1	-12.4	6.6	28.2	24.6	34.1	35.8

Source: Estimated from the Export Promotion Bureau (EPB) data.
Note: Q1 refers to the first quarter (July-September period) of the corresponding fiscal year.

High Growth of Import Payments Inevitable

While the export earnings started to peak, demand for raw materials, capital machineries and fuel rose dramatically resulting in higher growth of import (41.9 per cent) in FY2010-11. The high import growth overshadowed the robust export sector performance resulting in a deterioration of the trade balance. This also put the BOP situation under pressure. However, during the first two months of FY2011-12, import growth somewhat slowed down to 16.5 per cent while imports of foodgrains, petroleum products and raw cotton saw a decrease (Annex Table 1.2). Major share of the foodgrains import was carried out by the government.[22] With public foodgrains procurement running well, in line

[17]Export of knitwear declined by (-) 16.8 per cent and export of woven wear increased by 6 per cent.

[18]Despite the fact that growth of global RMG import by US in the current year is somewhat lower than that of the previous year, other competitors of Bangladesh in the US market have performed much better in knitwear export. Total RMG import by US increased by 9.2 per cent during July-August, FY2011-12 (Annex Table 1.1), which was 17.8 per cent during the same period of the previous year. During July-August 2011, Bangladesh's growth in knitwear export was 0.6 per cent, whereas Cambodia and Sri Lanka attained 20.8 per cent and 30.5 per cent growth in the same period. Even China, India, Pakistan and Vietnam managed to attain significant growths. However, regarding export of woven wear, Bangladesh has performed much better than other exporters in the US market.

[19]Total export to US declined by (-) 15 per cent.

[20]International price of cotton is declining since March 2011. In the last six months, it declined by 49.1 per cent.

[21]Recently, according to a plea made by Pakistan, EU proposed for waiving tariff on 75 products originating from Pakistan. Eight out of these 75 items will be subjected to TRQ for two years; the rest 67 items were proposed to be exempted from any customs duty. A number of countries including India and Peru lodged official objections at the World Trade Organization (WTO) against the EU, opposing the waiver proposal. If Bangladesh's export to EU for those 75 products is considered, only two out of the top 10 are found to be protected by the TRQ. In view of this, Bangladesh proposed another list of eight tariff lines for exclusion from the EU-proposed list for Pakistan, or at least considering quota limits. Subsequently, EU proposed to add five more items in addition to the already included eight tariff lines to the list of products under TRQ. This newly proposed list of 13 tariff lines under TRQ now covers six of the proposed eight Bangladeshi export items.

[22]As of 20 October 2011, Bangladesh had imported 0.37 million MT of rice, 92 per cent by the government.

with the target[23] and promising outlook for the foodgrains production, it may be assumed that in the coming months, import of foodgrains is not likely to see a sharp upturn. Opening of import L/Cs (letters of credit) for foodgrains also shows similar pattern.[24] Import of fertiliser increased by 76.5 per cent; however, this growth was mainly driven by higher international price of fertiliser.[25] On the other hand, declining import growth of petroleum products is likely to increase in future as L/Cs opening for petroleum increased by 107.3 per cent in the first quarter of FY2011-12.[26] It also needs to be noted that four liquid fuel-based (quick) RPPs come into production in the course of the current fiscal year, which is likely to increase the demand for imported petroleum significantly.[27]

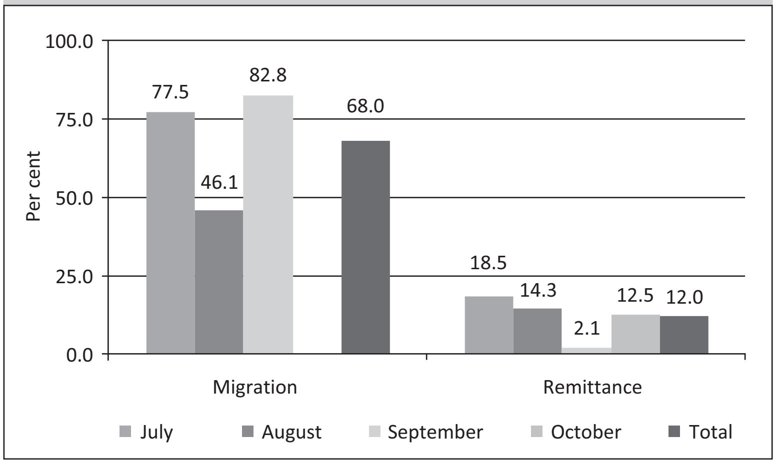
Import of capital machineries increased by 36.4 per cent during the first two months of FY2011-12 mostly due to higher demand from new power plants. Nevertheless, import L/Cs opened for capital machineries decreased by (-) 37.3 per cent in the first quarter of FY2011-12, indicating a possible stagnation of the investment sector in the coming months. Import of intermediate goods such as yarn and textiles and articles thereof also increased over the same period of FY2011-12.[28]

To maintain import growth within the target of 14 per cent for FY2011-12, growth of import in the next 10 months of fiscal year needs to slow down further to 13.5 per cent. As it stands, it will be difficult to contain import growth within the target set for FY2011-12.

Overseas Employment Picks Up but Remittance Slows Down

Remittance inflow during the first four months of the current fiscal stood at about USD 4 billion (Tk. 30,064 crore) which was 12 per cent higher than that of the comparable period of the previous fiscal (Figure 1.5).[29] Average monthly flow of remittances during the second half of FY2010-11 was USD 1 billion, which was maintained in the current fiscal year. In October, remittance inflow increased by 12.5 per cent. Growth of remittance inflow in the coming eight months of the fiscal year will need to be maintained over robust performance achieved during the second half of FY2010-11. To achieve the projected target of USD 12.7 billion for the current fiscal, inward remittances will need to register an average growth of 7.7 per cent during the remaining eight months of FY2011-12.

Figure 1.5
Growth of Migration and Remittance in FY2011-12 over FY2010-11



Source: Estimated from the Bureau of Manpower, Employment and Training (BMET) and the Bangladesh Bank data.

The number of migrant workers going abroad during the first quarter of FY2011-12 was about 0.15 million, which was about 68 per cent higher than that of

[23]As of 20 October 2011, 0.8 million MT of Boro rice had been procured and another 0.81 million MT contracted. The achieved procurement represents 97.8 per cent of the target, compared to a 46.9 per cent achievement of the target last year at the same time.
[24]Opening of import L/Cs for foodgrains declined by 62.7 per cent during the first three months of FY2011-12.
[25]International price of urea increased by 60 per cent between September 2010 and September 2011.
[26]Interview with concerned officials hinted that at present a number of vessels with imported petroleum are ready to offload.
[27]BPC projected that oil import bill for FY2011-12 may reach to USD 6.3 billion.
[28]New relaxed RoO in EU-GSP partially explains higher demand of imported yarn.
[29]In Bangladeshi Taka (BDT) terms, the growth of remittances is higher at 20.3 per cent, thanks to the accelerated depreciation of BDT against USD.

the comparable period of the previous fiscal. On average, 50,000 people have gone overseas in the first three months indicating a positive start for the current fiscal, a trend which has been missing since FY2008-09. Number of migrant workers from Bangladesh has increased in countries such as United Arab Emirates (UAE), Oman, Singapore, Kingdom of Saudi Arabia (KSA) and Jordan.[30] During July-September period of FY2011-12, about 80 per cent of Bangladeshi migrant workers went to the first three of the above mentioned countries. It is assumed that it takes three to four months for a migrant worker to get settled in the host country; presumably, the remittance inflow is not likely to increase till the last quarter of fiscal year. Hence, the remittance target for the current fiscal year also appears to be uncertain, even though in the medium-term this is likely to bring positive results for Bangladesh.

According to World Bank, remittance inflow in the developing world is likely to increase in 2012 and 2013 in a more sustainable way, compared to the period prior to the global financial crisis, with an annual projected growth of 7.4 per cent and 7.9 per cent respectively.[31] In case of Bangladesh, if the current situation persists and no other external shock affects overseas employment, remittance growth is likely to be more than 10 per cent in FY2011-12 compared to FY2010-11.

It is good to note that the cost of sending remittances from Saudi Arab and Singapore has declined by 12.7 and 3.9 per cent respectively in the third quarter of the calendar year 2011 compared to the first quarter of the same calendar year. According to World Bank, cost of sending remittances has been declining for South Asian countries like Bangladesh and Nepal owing to greater competition. However, anecdotal information suggests that due to higher spread between official and kerb market figures, sending of remittances to Bangladesh through *hundi* or *hawala* appears to have substantially increased in recent times. This needs further investigation and calls for an immediate policy attention.

No Promises Coming from Foreign Aid Front

Slowdown in foreign aid inflow has been a major concern for Bangladesh in FY2010-11. The trend continues this year as well. Since project aid is the overwhelmingly large component of foreign aid, its inflow is now directly linked to ADP implementation capacity. Availability of project aid is not the main concern.[32] During the first quarter, inflow of net foreign aid was only USD 74.4 million, whereas it was USD 173 million in the comparable period of the previous fiscal year. It appears that achieving the ambitious budget target of net foreign aid inflow to the tune of USD 2.5 billion will remain a far cry. Recently it has been proposed that the World Bank, the Ministry of Planning and the concerned ministries should sit together every three months to resolve contentious issues related to project implementation. On the other hand, government has urged the Bank officials to negotiate with their headquarter so that their local offices could get more power to expedite decision. At the same time, the latest indications suggest that USD 1 billion budgetary support from the World Bank is not likely to be finalised in the current fiscal year. The ongoing debacle over financing of the *Padma Multipurpose Bridge Project* is also likely to have an adverse impact in terms of foreign aid inflow to Bangladesh. Only 10 per cent of the total planned expenditure for the Padma Bridge (Tk. 20,507 crore) was actually earmarked for FY2011-12. However, project aid component of the Bridge accounted for 38.7 per cent of the total project aid planned for the transport sector, and

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[30] Government-to-government (G2G) initiative between Bangladesh and Jordan has facilitated migration of workers at a reduced cost of Tk. 10,000, which was previously Tk. 110,000. Heavy recruiting of female workers for RMG sector in Jordan (along with Mauritius) has been a major contributing factor.

[31] The corresponding growth figures for South Asia are estimated to be lower at 5.8 and 6.5 per cent respectively, reported due to slowdown in remittance inflow to India and Pakistan. For Bangladesh, the outlook is more promising.

[32] It is estimated that foreign aid to the tune of USD 13.5 billion is a waiting in the pipeline.

9.1 per cent of total project aid in ADP for FY2011-12. With uncertainty looming over the project's future, one may speculate that foreign aid inflow for the Padma Bridge project may not be realised any time soon. Overall, it can be expected that the BOP situation is not likely to get any respite with the help of its foreign aid component in FY2011-12.

Pressure on Balance of Payments Likely to Sustain

FY2010-11 ended with a negative overall balance and it was apprehended that this pressure would continue during FY2011-12. Monetary Policy Statement (July-December, 2011) of Bangladesh Bank projected even a wider deficit of trade balance for FY2011-12 coupled with low remittance growth. As a result, the Statement projected deficits in the current account balance and also overall balance (of (-) USD 884 million and (-) USD 439 million respectively). To contrast, the Sixth Five-Year Plan (SFYP) prepared earlier, had forecasted a strong surplus in the overall BOP (USD 902.3 million) anticipating higher inflow of FDI and foreign aid.[33]

In FY2011-12 (July-August), a low import growth had restrained, the trade balance at (-) USD 409 million. This, along with the increasing pace of remittance inflow helped to attain a current account balance surplus of USD 1,194 million (which was USD 625 million during the comparable months of FY2010-11). Negative balance in financial account continued, owing to a large extent, to the lower net inflow of foreign aid. Net FDI inflow registered promising growth of 66.4 per cent during the first two months of FY2011-12, but its volume was inadequate to restrain the deterioration of financial account balance.[34] Overall balance managed to maintain positive scale, for now, at USD 89 million. The government has once again sought for faster realisation of proposed IMF support to the tune of USD 1 billion for three years under the Extended Credit Facility (ECF) to tackle the apprehended uncomfortable BOP situation.[35] However, without acceleration in foreign aid utilisation, improvement in BOP situation can hardly be expected at this moment.

Weakened BDT may Fall Further

Growing BOP pressure got transmitted into depreciating exchange rate during the last fiscal year. The exchange rate of BDT against USD has been going down further and at a faster rate in recent months. Additionally, exchange rate management has become more difficult due to volatility in international exchange rate markets. BDT was appreciating against Euro between July-September 2011 period. However, in view of Euro's strengthening, BDT experienced marginal depreciation in October 2011. With a more acceptable agreement on debt crisis by EU leaders[36], the value of Euro has become more stable at the end of October 2011. As of October-end 2011, BDT depreciated against all major currencies[37] (USD, Euro, British Pound (GBP) and Chinese Yuan (CNY)), except for

[33]SFYP projected a trade balance of (-) USD 9,699.9 million and current account balance of (-) USD 192.1 million. The SFYP however looks forward to improve the BOP position by reducing deficit in trade balance through slashing dependence on imports and promoting export along with higher inflow of remittances.

[34]During July-August period of FY2011-12, net FDI inflow increased to USD 188 million, which was USD 113 million in the corresponding period of the previous fiscal year.

[35]Government is expected to ask for a Mission from the Fund to discuss the credit agreements soon. One may recall that the previous credit was tagged with a number of conditionalities by IMF including rationalisation of petroleum price. A number of these are already implemented by Bangladesh.

[36]On 26 October 2011, the EU leaders agreed to make a 50 per cent cut on the Greek debt. They also agreed to boost the European rescue fund (the European Financial Stability Facility – EFSF) from 440 billion Euro to 1 trillion Euro. The measures also included recapitalisation of European banks and IMF agreement to deploy its next instalment of 2.2 billion Euro for Greece's original bailout.

[37]During the last four months (between end of June to end of October), BDT lost its value vis-à-vis USD by 2.8 per cent, Euro by 0.8 per cent, GBP by 3.2 per cent and Canadian Dollar (CAD) by 0.5 per cent.

Indian Rupee (INR).[38] Depreciation of BDT would imply that export to US and EU will be benefited. However, greater depreciation against CNY would also mean costlier intermediate and capital goods imported from China.[39] Ceteris paribus, exporters may switch to importing raw materials from India (particularly for export of RMG products). Falling value of BDT put some pressure on prices of most of the imported consumer goods other than rice.[40] Accordingly, it may also create further strain on domestic price levels in the coming months. Currently, foreign exchange reserve is maintained at around USD 10 billion, which is equivalent to 3.6 months of import payments. Hence, there is hardly any room to use this reserve to contain BDT's value. The volatility in international foreign exchange market made foreign exchange policy making only harder.

Higher Utilisation of Foreign Aid Holds the Key

In the backdrop of falling growth of exports and remittances in September and lower levels of foreign aid disbursement in the first quarter, along with projected higher impacts in the coming months, the BOP is expected to remain under pressure in the coming months of FY2011-12. In this backdrop, BDT may witness further depreciation towards the end of FY2011-12. In the short-term, it appears that higher utilisation of foreign aid will be the key to maintaining balance in the external sector.

1.4

GROWTH PROSPECT AND CURRENT CHALLENGES

The current fiscal year kicked off on a relatively strong growth platform, although a number of tensions were becoming evident in the economy since the second half of the elapsed year. In its pre-budget analysis of the economy in June 2011, CPD identified a number of risks that loomed in the horizon as the country approached towards FY2011-12. The four risks that CPD pointed at, were: (i) financing risk; (ii) macroeconomic balance risk; (iii) institutional risk; and (iv) political risk. Our above observations validate that these risks are becoming stronger as the economy is moving forward in FY2011-12. Analyses presented in the foregoing sections of this chapter suggest that Bangladesh economy from the initial months in FY2011-12 has increasingly come under a complex set of stresses and strains emanating from multiple sources. Some of these growing pressures are manifestation of the structural problems of the economy, often aggravated by the nature of macroeconomic management; while some of the other pressure points are underpinned by adverse developments in the global economic environment. Under the circumstances, keeping the economy on a sustainable and inclusive growth trajectory and maintaining consolidated macroeconomic stability will be a very challenging task. Indeed, for Bangladesh economy, FY2011-12 will be, on many counts, one of the relatively difficult years in the recent past.

How does the economic growth prospect for the year look like, based on the performance indicators of the first quarter of FY2011-12? Early signals are not necessarily adequate predictors for overall economic growth for the full year. However, as the final GDP estimates for FY2011-11 are awaited, a number of reasonable assumptions lead us to suggest that attaining the target growth rate of 7 per cent in FY2011-12 will be quite

[38] Between end of June to end of October, BDT appreciated against INR by 6.6 per cent.
[39] China is the single largest source of imported capital machinery for Bangladesh.
[40] In Bangladesh, rice is generally imported from India. Prices of rice have also stabilised in international market in recent months.

difficult. Indeed, a number of international financial institutions have expressed similar view. The World Bank has maintained that it is 'uncertain' that the target GDP growth rate for FY2011-12 will be achieved, while the IMF has projected it to be 6.3 per cent. Nonetheless, it should not be missed that a 6 per cent plus growth rate is a pretty respectable figure given all the visible risks afflicting the Bangladesh economy.

What message does the present review send to the top policymakers of the country? Indeed, the first and foremost message is that the policymakers have to take into cognisance that the economy has entered a difficult period from the perspective of economic management. A denial syndrome will not help. This entails drawing up a transitional work programme and taking hard decisions. Given the electoral cycle, the government has little time in the margin to make mends before the next general election.

To operationalise the transitional work programme, the government would need to revisit at the earliest its targets for the current fiscal year relating to public finance. In fact, it should not wait till mid-year to produce the revised budget. Such a review of the public finance programme should identify a number of priorities, beyond the obvious ones.

While revising the budget, the government has to take note of the evolving trends in global economic recovery. Indeed, if a second dip actually takes place, the government has to be ready with a response plan. Admittedly, the government has much less fiscal space at this moment to finance counter-cyclical policies. This has been made more difficult by the prevailing high inflationary trend.

One of the overriding priorities should be to undertake all out efforts to increase the disbursement of the committed foreign aid, particularly for the ongoing projects. Such an approach will have multiple objectives including maintaining the growth momentum, reducing pressure on domestic borrowing, and alleviating pressure off the BOP situation. Budgetary support or BOP support may be negotiated with the international financing institutions at reasonable terms. Foreign financing on commercial terms, even for high profile national projects, may be avoided for the time being.

The other equally high priority should be to reduce the demands on subsidy payments. In fact, the country's subsidy basket needs to be scrutinised closely from the perspectives of both efficiency and distributive justice. Whatsoever, the government needs to adjust upward, in a transparent phased manner, the prices of all types of liquid fuels. Same applies to electricity prices. To support the poorer sections of the population, including the farmers, the government may pursue targeted approach in a manner which is efficient and effective. As the subsidy burden has become fiscally unsustainable, rationalisation of prices of energy products will help strengthen the fiscal balance. The consequent cost escalation-driven possible inflation will be partly offset by reduced government borrowing from the banks; banks will then have more resources to finance productive investment.

The government's claim on funds in the banking system has to be moderated and kept within the programmed target. Given the very low level of sales of national saving instruments, the government should consider revising their yield rates, and thus borrow from non-banking sources.

With a view to augment revenue intake, the government must concentrate on collections from non-tax sources as well as from non-NBR tax heads. The government also needs to remain vigilant regarding maintaining the robust performance of the NBR, particularly on the income tax front.

It has been mentioned by CPD on an earlier occasion that there is no 'magic bullet' for combating inflation. It may be expected that currently imposed restraints on credit growth, particularly on credit to government, may eventually have some sobering impact on the overall price situation. However, government will have to continue with public procurement of foodgrains, maintain adequate food stock, undertake open market operations when necessary, and broaden the safety net programmes to keep the food (rice) market stable. Nonetheless, inflation, particularly food inflation will continue to remain high in the remaining part of the current fiscal year. The creeping upward trend in non-food inflation may also gain momentum in the near-term.

As the export growth rate decelerates, efforts to diversify markets have to be intensified including by taking advantage of the recently announced trade concessions in the Indian market. Exploiting the new RoO in the EU, Bangladesh should also try to diversify her export basket.

In view of the slowdown of remittance growth, the government needs to take additional measures for market development and reduction of cost of migration. The BOP situation may get some relief due to slowdown of imports. Higher disbursement of foreign aid, greater inflow of export revenue and remittance income by expatriate workers could alleviate the situation further.

The government will need to keep under watch two other issues (not discussed in the report), namely – (i) the situation in the capital market, and (ii) issuance of new bank licences.

Regarding the first, it needs to be pointed out that the current attempts to rejuvenate the market are based on a misperceived 'liquidity approach.' The recent attempts to inject money into the market through launch of the 'Bangladesh Fund' and 'Stabilisation Fund' are going to yield little results. Indeed, such attempts and decisions like delayed adjustment of single borrower's exposure limit are only going to further complicate the interface between the banking sector and the capital market. Although, there had been, in the recent times, some initiatives to reform the market regulation and management, none of these touched upon the basic issues relating to transparency and accountability including strengthening of the surveillance capacity of the body responsible for oversight, i.e. the Securities and Exchange Commission (SEC). In this regard, the demand for implementation of the recommendations of the Probe Committee has now become a far cry.

The other subject of issuance of new bank licences is also a debatable proposition. Arguably, there is hardly any need for new banks – what the banking sector needs is strengthened oversight relating to compliance of Basel III, and possibly improvement of efficiency through competition and scaling up. Bangladesh Bank has drawn up a sound set of eligibility criteria for any new banks. If new licence(s) has/have to be awarded it should not be based on 'political consideration,' but on rigorous fulfilment of the eligibility criteria. In view of the revealed attempts to relax those criteria, particularly the requirement relating to Tk. 400 crore tax paid sponsors' fund, the Central Bank should remain committed to the criteria that itself has set. Under all circumstances there should be full disclosure regarding the applications and the award, as and when made.

Under the fiscal transparency requirements, the Finance Minister in FY2009-10 started the quarterly practice of reporting on the state of the economy to the parliament. Curiously, the Minister has not introduced such reports to the parliament during the last three quarters (two, if the Budget Speech is excluded). One may expect that the Minister will use his next reporting opportunity to deliberate on the package of measures that he thinks necessary to reboot the economic management for FY2011-12.

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ANNEX TABLES

Annex Table 1.1
RMG Import Growth of US in FY2011-12 (July-August)

(in Per cent)

Exporter	Knitwear	Woven Wear	Total RMG
World	10.5	7.5	9.2
Bangladesh	0.6	26.4	18.5
Cambodia	20.8	4.8	15.8
China	9.4	0.1	4.8
India	8.7	11.5	10.2
Pakistan	11.0	11.1	11.0
Sri Lanka	30.5	4.2	15.4
Vietnam	10.3	11.8	11.0

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

Annex Table 1.2
Import Growth of Selected Commodities

(in Per cent)

Item	FY2011 (July- August)	FY2012 (July- August)
A. Foodgrains	317.4	-19.0
Rice	7020.0	13.7
Wheat	104.9	-55.0
B. Other Food Items	104.3	34.8
C. Consumer and Intermediate Goods	90.9	6.1
Crude petroleum	-	-30.1
Petroleum and other liquids (POL)	16.8	-5.9
Fertiliser	539.4	76.5
Raw cotton	67.6	-21.8
Yarn	89.9	25.7
Textile and articles thereof	50.5	11.1
D. Capital Goods and Others	0.6	43.1
Capital machinery	21.8	36.4
E. Others n.i.e.	2435.6	9.1
Total (A+B+C+D+E)	132.5	17.0
F. Import by Export Processing Zone (EPZ)	78.0	7.6
Grand Total (A+B+C+D+E+F)	128.8	16.5

Source: Estimated from the Bangladesh Bank data.

2

CHAPTER

Analysis of National Budget FY2011-12

2.1

INTRODUCTION

The national budget for FY2011-12 and the revised budget for FY2010-11 were presented by the Hon'ble Finance Minister of Bangladesh on 9 June 2011. The budget was placed in the backdrop of rising pressure on macroeconomic management as signs of weaknesses began to appear in some of the key macroeconomic indicators towards the end of FY2010-11. In keeping with its tradition of putting the budgetary framework and proposals under close scrutiny, the Centre for Policy Dialogue (CPD) had earlier organised a series of events to project its views and perspectives on the progress made in the context of the various indicators relating to the FY2011-12 Budget.

CPD presented its immediate reactions on the national budget for FY2011-12 at a well-attended media briefing on 10 June 2011, the day after the budget was placed before the national parliament. CPD also organised a national dialogue on 18 June 2011 in Dhaka with participation of high level policymakers, Members of the Parliament (MPs), leaders of political parties, representatives from private sector, non-government organisations (NGOs) and civil society, academics and other stakeholders. CPD's presentation was based on an in-depth analysis of the various budgetary proposals and the fiscal stances taken by the government. Again, a regional dialogue was held in Chittagong on 25 June 2011 in collaboration with the Bangladesh Economic Association (BEA), Chittagong Chapter to take cognisance of views from the thinkers and stakeholders of the Port City. Participants at both dialogues shared their views on the analysis presented by the CPD, and commented on various aspects and measures proposed in the budget. Reports of these dialogues are included in this volume as Annex 1 and Annex 2.

FY2011-12 has been benchmarked by commendable revenue mobilisation by the National Board of Revenue (NBR), rebound in export earnings, and momentums in private investment and domestic demand. On the other hand, a certain degree of disquiet afflicted the economy with mounting pressure on foreign exchange reserves, slow down in remittance growth, underutilisation of foreign aid, and the urgency of maintaining food security. The budget for FY2011-12 is to tackle a number of challenges including soaring inflationary pressure, deteriorating balance of payments (BOP), apprehension with regard to liquidity in money market, and financing of the rising budget deficit.

The budget speech of the Finance Minister had set out with a slogan that said *Towards Building a Happy, Prosperous and Caring Bangladesh*. The speech featured a detailed narrative of achievements by the present government. The Document also presented a report card on some of the election promises of the Grand Alliance which was claimed to have been kept. For example, the speech recalled that net enrolment at primary level was targeted to be 100 per cent by 2010; it was reported that this had risen to 99.3 per cent. It is also important to mention that, as it appears from the speech, some of the election pledges were also revised. For example, the employment guarantee scheme was supposed to provide 100 days of employment per year for one youth from every family. The flagship employment generation programme of the government titled *Employment Generation Programme for the Poorest (EGPP)* was scaled down to 80 days. Some election promises remained unmet. The election manifesto's targets included supplying pure drinking water to all citizens by 2011. Though new water sources have been set up, not all citizens had access to arsenic-free pure drinking water. In view of this, a comparative matrix of promises and actual achievements would have been helpful to citizens to have a better understanding of the actual track record.

The budget for FY2011-12 also includes contextualisation of global trends and a revised Medium Term Macroeconomic Framework (MTMF) taking cognisance of the emerging realities. Growth target for FY2011-12 stands at 7 per cent and was set to increase to 8 per cent by FY2014-15 (Table 2.1). Growth projection for broad money (M2) was moderate, while inflation target for FY2011-12 remains moderately high. However, questions remained as to how the high growth targets in government borrowings (to finance budget deficit) would be accommodated with the envisaged moderate growth of M2! With respect to the external sector, in reference to the high benchmarks of FY2010-11, targets for export and import are set at a lower level. The target of foreign exchange reserve for FY2011-12 (USD 11.6 billion) was unlikely to be attained in view of expected slowdown in export and remittance growth with continuing high import and uncertainties about timely disbursement of foreign aid. In view of the missing links between various targets of MTMF, one wonders whether the presented Framework depicted a 'reality-based projection' or just an 'ideal set of targets?'

Table 2.1

Medium Term Macroeconomic Framework

Indicator	Revised	Projections				
	FY2011	FY2012	FY2013	FY2014	FY2015	FY2016
Real Growth (%)	6.7	7.0	7.2	7.6	8.0	8.2
Total Revenue (as % of GDP)	12.1	13.2	13.4	14.0	14.6	15.2
NBR Tax	9.6	10.2	10.8	11.4	12.0	12.6
Non-NBR Tax	0.4	0.4	0.4	0.4	0.4	0.4
Non-Tax	2.0	2.5	2.2	2.2	2.2	2.2
Total Expenditure (as % of GDP)	16.5	18.2	18.4	19.0	19.6	20.2
Budget Deficit and Financing (as % of GDP)	4.4	5.0	5.0	5.0	5.0	5.0
Domestic Financing	3.1	3.0	3.0	3.0	3.0	3.0
Banking System	2.3	2.1	2.2	2.2	2.2	2.2
Non-Bank	0.8	0.9	0.8	0.8	0.8	0.8
Net Foreign Financing	1.3	2.0	2.0	2.0	2.0	2.0
Inflation (Annual Average %)	8.0	7.5	7.0	6.5	6.0	5.5
Credit to Private Sector (% change)	27.0	20.0	18.0	18.0	18.0	18.0
Broad Money (M2) (% change)	20.0	16.0	16.0	16.0	16.0	16.0
Export (% change)	38.0	14.5	14.5	14.5	15.0	15.0
Import (% change)	45.0	14.0	14.0	14.5	14.5	15.0
Remittances (bln USD)	11.5	12.7	14.2	15.9	17.8	20.0
Current Account Balance (% of GDP)	-0.3	-0.2	-0.2	-0.3	-0.4	-0.6
FOREX Reserve (bln USD)	10.7	11.6	12.9	14.5	16.1	17.6

Source: Medium Term Macroeconomic Framework 2011, Ministry of Finance (MoF).

Note: GDP: Gross domestic product.

Before going into the detailed analysis of the Budget FY2011-12 one will need to keep in mind the four envisaged trade-offs for the government in FY2011-12: (i) growth vs. macroeconomic stability; (ii) subsidy requirement vs. other priorities; (iii) government borrowing vs. servicing private sector credit demand; and (iv) exchange rate: inflation vs. export.

The remainder of this chapter has six sections. Following the introductory section, the discussion sets off with a brief analysis of the envisaged public finance framework in the national budget for FY2011-12 in Section 2.2. Section 2.3 provides an overview of proposed fiscal measures, while a review of budgetary measures for different sectors are presented in Section 2.4. Section 2.5 and Section 2.6 deal with the budgetary allocations for social sectors and various safety net programmes respectively. The chapter rounds up with a few concluding remarks.

2.2

PUBLIC FINANCE

The national budget for FY2011-12 has envisaged an expenditure package of Tk. 163,589 crore which is 25.8 per cent or Tk. 33,578 crore higher than the revised budget for FY2010-11. The estimated growth target of 24.4 per cent for revenue mobilisation indicates a faster growth on the expenditure side when compared with the earning side. As percentage of GDP the proposed public expenditure (18.2 per cent of GDP) in FY2011-12 is about 1.7 percentage points higher than that of FY2010-11 (16.2 per cent in the revised budget). The proposed Annual Development Programme (ADP), to the tune of Tk. 46,000 crore, is equivalent to 28.1 per cent of total public expenditure; this was 27.6 per cent in the revised budget for FY2010-11. Overall budget deficit is projected at 5 per cent of GDP for FY2011-12. For financing of the deficit, the government has planned to rely on the banking system, which means the private sector may have to compete with the government for access to finance in the credit market. High foreign financing target (79.8 per cent growth over the revised budget of FY2010-11) is set with an anticipated gross foreign aid flow of about USD 3.3 billion. As the targets for both revenue earnings and expenditures are set on the high side in the revised budget, growth targets for FY2011-12 are likely to be higher when calculated over the actual figures of FY2010-11.[1] In order to have a better understanding of the budgetary proposals and fiscal stance, one may separate the four real defining elements in the framework – revenue earnings (NBR and non-tax), subsidy, ADP expenditure and foreign financing of fiscal deficit.

2.2.1 Revenue Earnings

Budget for FY2011-12 has targeted a revenue earning of Tk. 118,385 crore which implies that an additional Tk. 23,198 crore will need to be mobilised in FY2011-12 when compared to the revised budget target of FY2010-11. As a result, revenue-GDP ratio and tax-GDP ratio are expected to increase to 13.2 per cent and 10.6 per cent respectively in FY2011-12 from the previous year's revised matched figures of 12.1 per cent and 10 per cent respectively.

NBR Components

As it stands, in order to achieve the revenue earnings set for target FY2011-12, NBR will have to play the key role and contribute the largest share (70 per cent) of the additional revenue (Figure 2.1). The share of NBR in total revenue has decreased to 77.6 per cent for FY2011-12 from 79.4 per cent in FY2010-11 (revised). Overall, the NBR growth target for FY2011-12 is set at higher level, at 21.2 per cent, over the revised budget figure of FY2010-11. This growth rate was 26.5 per cent in FY2010-11 (revised).

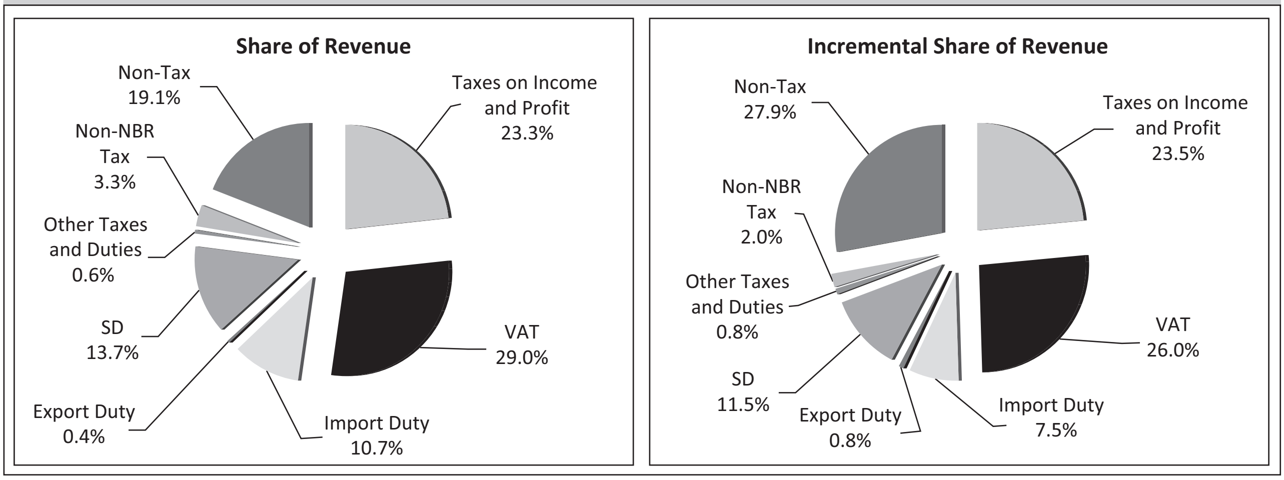
Within NBR, tax collection efforts from domestic sources (income tax, value added tax (VAT) and supplementary duty (SD)) will need to be intensified to attain the targets. The targets for FY2011-12 are set with reference to their recent performance particularly in view of the significant contribution of these sources in FY2010-11.[2] In fact the growth

[1] At the end of FY2010-11, actual revenue and expenditure growth targets turned out to be 29.6 per cent and 31.1 per cent respectively.

[2] At the end of FY2010-11, actual growth in income tax, VAT and SD turned out to be 33.3 per cent, 29 per cent and 27.8 per cent respectively.

Figure 2.1

Projected Share and Incremental Contribution of Sources in Revenue Growth: FY2011-12



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

targets set for these three sources (24.7 per cent for income tax, 21.3 per cent for VAT and 19.7 per cent for SD) are set on the lower side compared to their robust performances during the preceding fiscal year. The target for customs duty (CD) in FY2011-12 is somewhat conservative (16 per cent) against the revised budget for FY2010-11, as the import payments had gone up in recent months. In view of the proposed fiscal measures, expected improvement in revenue collection efforts and high price levels, it appears that the targets for NBR tax components should be within the reach.

Non-NBR Components

The budget predicts a significant recovery of non-NBR tax and non-tax revenues in FY2011-12. It is also projected in the revised budget of FY2010-11 that collection through these two revenue components will improve during the second half of FY2010-11. The performance during the first half, however, does not indicate this when a negative growth of (-) 12.9 per cent was achieved.[3] Such a shortfall in benchmark (FY2010-11) would mean a higher than stipulated growth targets for FY2011-12.[4] Within the additional Tk. 6,465 crore targeted from non-tax sources, Tk. 4,893 crore is expected to come from 'Other Non-Tax Revenue and Receipts.' It appears that, attainment of this target will largely hinge on the decision with regard to telecom spectrum fee and its timely collection.

2.2.2 Public Expenditure

A sector-wise analysis of total expenditure (development and non-development) reveals that the highest growth in terms of resource allocation has taken place in Public Services sector over the revised allocations of FY2010-11. Total allocation for Public Services is set to increase by 1.4 times, driven partly by subsidies (including for export), public-private partnership (PPP) and lump allocation for development programmes financed from the revenue budget. Expenditures on Industrial and Economic Services sector, and Transport and Communication sector are also projected to post significant growth of 40.2 per cent

[3] At the end of FY2010-11, in aggregate, revenue collection by non-NBR and non-tax components resulted in a shortfall by a margin of 23.4 per cent (Tk. 4,591 crore) against their joint revised target.

[4] This shortfall will mean that higher growth rates (76.8 per cent) will be required compared to what has been projected in the budget of FY2011-12 (35.4 per cent) to reach the target.

and 30.2 per cent respectively (Table 2.2). Interest Payments is also likely to post significant rise (by 23.5 per cent).

Revenue Expenditure

Revenue expenditure (augmented) as a percentage of GDP is set at 11.4 per cent which was 10.6 per cent in the revised budget for FY2010-11. Revenue expenditure target for FY2011-12 is set at Tk. 91,897 crore with a 13.6 per cent growth over the revised target of FY2010-11 (Table 2.3). Share of three major heads (Interest Payments, Pay and Allowances, and Subsidies and Current Transfers) stands at 80.8 per cent in FY2011-12 (83.2 per cent of FY2010-11). About one-third of the total incremental revenue expenditure (Tk. 10,977 crore) will be due to envisaged rise in interest payments, particularly from domestic interest payments. Interest payments is to increase by 23.5 per cent in FY2011-12 over the revised budget target. Interest payments for domestic borrowings is expected to make a significant growth of 25.6 per cent while foreign interest payments will increase by only 3.9 per cent. Expenditure on Pay and Allowances is set to rise by 5.7 per cent in FY2011-12. Expenditure on Subsidies and Current Transfers will contribute 37.7 per cent of total revenue expenditure and is set to increase by 7.4 per cent. However, it is important to note that, 'Subsidies and Current Transfers' reported in economic analysis of non-development revenue expenditure does not include all subsidy expenditures. Public budget documents also did not provide a detailed account of subsidy expenditures and contingent liabilities for FY2011-12. The MTBF Document reports that revised allocation for total subsidy in FY2010-11 was Tk. 16,085 crore (2.3 per cent of GDP). One can understand that subsidy allocation for FY2011-12 is set to rise by a substantial amount and may get close to 3-4 per cent of GDP, particularly due to rising subsidy demand from fuel (Bangladesh Petroleum Corporation (BPC)) and power sectors (Bangladesh Power Development Board (BPDB)).

Table 2.2

Sector-wise Distribution of Total Expenditure

Sector	Share (%)		Change in FY2012 (B) over FY2011 (RB)	
	FY2012 (B)	FY2011 (RB)	Crore Tk.	Per cent
Public Services	14.7	7.7	13992.0	140.1
Education and Technology	12.4	14.3	1741.0	9.4
Interest Payments	11.0	11.2	3419.0	23.5
Agriculture	7.7	10.1	-553.0	-4.2
Local Government and Rural Development (LGRD)	7.5	8.1	1783.0	17.0
Defence Services	7.3	7.2	2633.0	28.3
Transport and Communication	6.9	6.7	2618.0	30.2
Social Security and Welfare	6.8	8.0	627.0	6.0
Health	5.4	5.9	1252.0	16.4
Public Order and Safety	5.2	5.8	921.0	12.2
Fuel and Energy	5.1	5.6	1055.0	14.5
Recreation, Culture and Religious Affairs	1.0	1.2	83.0	5.1
Housing	0.9	1.0	205.0	15.7
Industrial and Economic Services	0.8	0.7	373.0	40.2
Others (Memorandum Items)	7.4	6.7	3429.0	39.6
Total Expenditur (in Tk. Terms)	100.0 (163589.0)	100.0 (130011.0)	33578.0	25.8

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

Table 2.3

Economic Classification of Revenue Expenditures

(in Per cent)

Indicator	Growth in FY2012 over FY2011 (RB)	Share FY2012 (B)	Share FY2011 (RB)	Incremental Share FY2012 (B)
Pay and Allowances	5.7	23.5	25.3	10.6
Goods and Services	7.6	12.8	13.5	7.6
Interest Payments	23.5	19.6	18.0	31.1
Domestic	25.6	18.0	16.3	30.6
Foreign	3.9	1.6	1.8	0.5
Subsidies and Current Transfers	7.4	37.7	39.9	21.7
Block Allocation	180.8	2.0	0.8	10.6
Deduct: Recoveries	-100.0	0.0	-2.2	16.4
Acquisition of Assets and Works	6.0	4.4	4.7	2.1
Total Augmented Non-Development Revenue Expenditure	13.6	100.0	100.0	100.0

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

Annual Development Programme (ADP)

The ADP for FY2011-12 has been targeted at Tk. 46,000 crore (5.1 per cent of the projected GDP). The new ADP will be 28.2 per cent higher than the Revised ADP (RADP)

Table 2.4

Sectoral Allocation for Top Five Sectors in ADP for FY2011-12

(in Per cent)

Sector	Share FY2011 (ADP)	Share FY2011 (RADP)	Share FY2012 (ADP)	Growth in FY2012 ADP over FY2011 RADP
Transport	14.30	14.90	16.85	47.83
Power	13.00	14.30	15.59	42.96
Education and Religious Affairs	13.50	14.40	13.31	21.18
Physical Planning, Water Supply and Housing	9.20	9.50	12.61	73.33
Rural Development and Institutions	11.50	13.00	9.57	-3.23

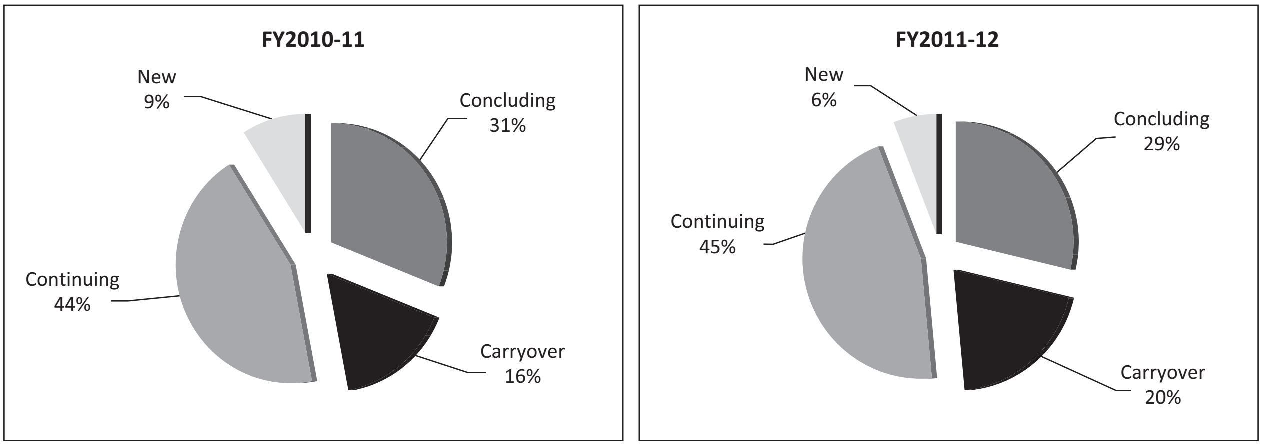
Source: Estimated from the Planning Commission data.

and 19.5 per cent higher than the original ADP of FY2010-11. Project aid component of the new ADP is targeted at 40.6 per cent of total (which was 33.3 per cent in the RADP and 39.7 per cent in the original ADP of FY2011-12). Five priority sectors in the ADP for FY2010-11 have received 67.9 per cent of the total allocation (Table 2.4). Allocation for Padma Bridge accounts for 28.2 per cent of the total allocation for the Transport sector, 78.2 per cent of this is expected to come from project aid.

In the FY2011-12 ADP, 77 new projects worth Tk. 2,251.91 crore have been included. This implies that only 5.7 per cent of total allocation is for new projects (Figure 2.2). Carryover projects consist of 19.9 per cent of the total allocation (which was 16 per cent in FY2010-11), while 325 projects with 28.6 per cent of total allocation is expected to be completed in FY2011-12. These to-be-completed and carryover projects will need to be prioritised in the process of ADP implementation. It is also important to know about the top 50 projects, which are under 'intensive monitoring.'

Figure 2.2

Structure of ADP in FY2010-11 and FY2011-12



Source: Based on the Planning Commission data.

An examination of the six priority sectors in the ADP shows that, similar to the overall structure, a high proportion of the ADP allocation is either for carried over projects from previous periods or are earmarked for completion in FY2011-12. 46.7 per cent, 39.5 per cent and 38.1 per cent of respective allocations for the Power, Oil, Gas & Natural Resources, and Social Welfare sectors are carrying over. Even though Power Division spent 107 per cent of its RADP allocation during the first eleven months of FY2010-11, considerable reallocation among the projects within power sector had to be made because of the underimplementation of some of the old projects. Lack of progress with regard to the latter projects could put under question the attainment of the set targets for the Power sector.

Some 259 development projects, worth Tk. 14,000 crore are in the pipeline, and are listed in the FY2011-12 ADP list (without allocation) to attract foreign financing. About 35.6 per cent of projects in this list are carried over from the FY2010-11 list of unapproved projects. If the related negotiations are successful, an additional USD 230 million (Tk. 1,690 crore) of foreign aid would come to Bangladesh annually over the next five years. In view of past record, this is highly unlikely.

In case of the ADP for FY2011-12, 16 new PPP projects are included, of which 13 were in power sector. Fiscal allocation for PPP in FY2011-12 is 1.8 per cent (Tk. 3,000 crore of the total budget: Tk. 2,500 crore for the Bangladesh Infrastructure Finance Fund Company Limited (BIFFCL); Tk. 400 crore as Viability Gap Fund (VGF); Tk. 100 crore for technical support). Except for the fast implementing Jatrabari-Gulistan flyover (under build-own-operate-transfer (BOOT) arrangement of PPP), the budget for these much-hyped PPP initiative remained mostly unutilised over the last two fiscal years. The PPP Office is yet to be fully functional although some recruitments were made. A PPP focal point has also been established in each of the line ministries, however, overall progress in PPP had been very slow to say the least.

2.2.3 Budget Deficit and Financing

The revised budget for FY2010-11 projects an overall deficit (excluding grants) of Tk. 34,824 crore (4.4 per cent of GDP) for the fiscal year. With the possibility of ADP not attaining its revised target, the final budget deficit figure for FY2010-11 was likely to be lower than the revised targets. For FY2011-12, once again, a larger deficit of Tk. 45,204 crore has been projected which is expected to be within 5 per cent of the GDP (Table 2.5). However, in view of the growing subsidy requirement and increased demand for investment on account of infrastructure, adoption of moderately higher deficit in FY2011-12 appears to be a justified policy choice. This was also needed to guard against any apprehension about the inflationary pressure from its financing nature.

Table 2.5

Fiscal Framework in Budget FY2011-12

Description	FY2011 (RB)		FY2012 (B)		Growth in FY2012 (B) over FY2011 (RB) (%)
	Crore Tk.	% of GDP	Crore Tk.	% of GDP	
Revenue Collection	95187	12.1	118385	13.2	24.4
Total Expenditure	130011	16.5	163589	18.2	25.8
ADP	35880	4.6	46000	5.1	28.2
Non-ADP	94131	12.0	117589	13.1	24.9
Overall Deficit (excluding Grants)	34824	4.4	45204	5.0	29.8
Financing					
Foreign Grants	4224	0.5	4938	0.5	16.9
Foreign Loan (Net)	5783	0.7	13058	1.5	125.8
Foreign Loan	10920	1.4	18685	2.1	71.1
Amortisation	5137	0.7	5627	0.6	9.5
Domestic Borrowing	24817	3.2	27208	3.0	9.6
Bank Borrowing (Net)	18379	2.3	18957	2.1	3.1
Non-Bank Borrowing (Net)	6438	0.8	8251	0.9	28.2
Total Aid Requirement (Net)	10007	1.3	17996	2.0	79.8
Total Aid Requirement (Net) (bln USD)	1.4	-	2.5	-	79.8
Total Aid Requirement (Gross)	15144	1.9	23623	2.6	56.0
Total Aid Requirement (Gross) (bln USD)	2.1	-	3.3	-	56.0

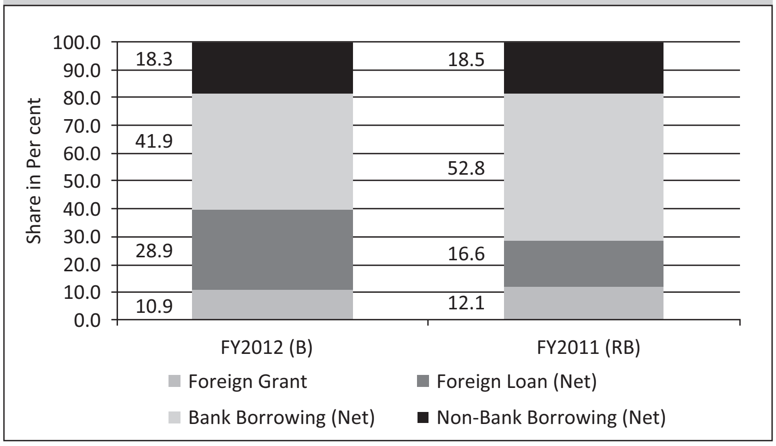
Source: Calculated from the Ministry of Finance (MoF) data.

With regard to financing of the deficit projected in the budget of FY2011-12, it may be noted that about 60.2 per cent of total deficit (Tk. 27,208 crore) is earmarked to be financed through domestic borrowing, of which Tk. 18,957 crore (69.7 per cent) is to come from the banking system (74.1 per cent in revised budget for FY2010-11), and Tk. 8,251 crore (30.3 per cent) to be mobilised through non-bank instruments (25.9 per cent in revised budget for FY2010-11).

The remainder 39.8 per cent is supposed to come from foreign sources that included foreign loans and grants (Figure 2.3). Gross foreign aid requirement is envisaged to be about USD 3.3 billion (USD 2.1 billion in revised budget FY2010-11) which is a challenging target particularly in view of the fact that only USD 1.4 billion was received during July-April, FY2010-11.

Figure 2.3

Sources of Deficit Financing



Source: Calculated from the Ministry of Finance (MoF) data.

The financing structure of budget deficit suggests that the government could not help but rely on bank borrowing. Thus, crowding out impact on private borrowing from banks should be monitored carefully, while inflationary impact needs to be considered as well. Much will depend on whether interest on National Savings Bond (NSD) certificates will be fixed at a level that matches market interest rates accrued from other savings alternatives (e.g. Fixed Deposit Receipt (FDR)).[5]

2.3

OVERVIEW OF FISCAL MEASURES

To meet the revenue expansion target, the budget for FY2011-12 has proposed a number of moves to expand the tax and VAT net. Some measures are also proposed to expedite the reform process in tax administration.

2.3.1 Direct Tax Measures

It may be recalled that the last adjustment in income tax threshold limit was made back in FY2008-09. Taking note of over 15 per cent inflation since then, income tax threshold limit has been raised to Tk. 180,000 from Tk. 165,000 in the budget for FY2011-12. Although this implies a 9 per cent upward shift of the exemption limit (lower than the recorded inflation in-between), the adjustment made in net terms appears to be logical considering the fact that significant growth in per capita income has also taken place during this time period (although the rate might have varied among income groups).

In line with the above revisions, exemption limits for individuals above 65 years, women and physically challenged people have also been raised, to various extents (from Tk. 180,000 to Tk. 200,000, and from Tk. 200,000 to Tk. 250,000 respectively). From the point of social justice, a differentiated tax slab for particularly vulnerable sections of people ought to be seen as a positive move.

[5]The interest rates of all NSD certificates were raised from 1 July 2011 along with a provision of Social Security Premium (SSP) at the time of maturity. The income tax at source (a flat 5 per cent rate) will be deducted before SSP payments. However, for most NSD certificates the interest rates are lower compared to interest rates on FDR.

Two distinctive initiatives proposed in the budget are notable with regard to personal income tax structure. *First*, 10 per cent surcharge on tax payable for those having wealth over Tk. 2 crore has been proposed. This is a welcome measure from the perspective of income distribution. *Second*, a bold and politically sensitive move to withdraw tax exemption for parliamentarians and government officials was also proposed.[6] This was a long awaited measure which would establish a semblance of equity between public and private sector employees.

The budget also proposes to impose a reduced rate of 5 per cent tax on the income from fisheries, poultries, etc. This was a move towards bringing the agriculture (non-crops) sector under the tax net and to further widen the tax net. However, one could question the timing of this move given the persistent high inflationary trend.

Another tax move proposed in the budget that appears to be unjustified relates to the deduction of tax at 10 per cent at the time of payment of service charges received from abroad by residents. There are two concerns in this regard. *First*, this particular income is tax-free and therefore the provision for deduction at source is contradictory. *Second*, the move may discourage the growing self-employment through catering to outsourced works from overseas. It may also encourage diversion of foreign earnings to bank accounts held in overseas by relevant clients.

The budget for FY2011-12, however, made no changes in corporate tax rates.

2.3.2 Special Tax Measures

The government in its budget proposals for FY2011-12 made a number of moves to improve savings and investment situation in the economy. For investment in national savings schemes, tax deduction rate has been brought down from 10 per cent to 5 per cent. This is likely to benefit smallsavers and pensioners. On the other hand, this could impact, albeit on a limited scale, the availability of non-bank borrowing sources of financing for the government.

The budget also maintained the provision of allowing investment in Bangladesh Infrastructure Finance Fund Limited (BIFFL) or Treasury Bonds, without questioning source of income, subject to payment of tax at the rate of 10 per cent. However, it is to be noted that BIFFL Bond was to be issued last year and this did not happen. The Finance Minister stated that the Bonds will be issued in three months.[7] In addition to this, the provision of lower than minimum usual tax rate (which is 15 per cent) creates moral hazard for regular taxpayers.

2.3.3 Custom Duties, Supplementary Duties and VAT

Given the inflationary pressure and in the backdrop of concerns about food security, the budget for FY2011-12 continues with the earlier fixed zero import duty on rice, pulse, wheat, sugar, edible oil, onion, fertiliser and seeds. This appears to be the right policy choice in the current context. The budget also continues zero import duty on life saving medicines which is indeed a major contribution to the health sector. It has also been proposed that SD on chewing tobacco be raised to 30 per cent from 10 per cent, driven by

[6] On 17 November 2011, the Cabinet decided to bring the salaries of the Prime Minister, ministers, state ministers and deputy ministers under the tax net. In view of this, the Cabinet approved the proposals for amending *The Prime Minister's (Remuneration and Privileges) Act 1975* and *The Ministers, State Ministers, and Deputy Ministers (Remuneration and Privileges) Act 1973*.

[7] In October 2011, the Bangladesh Bank has issued a license for BIFFL as a non-bank financial institute to facilitate the country's infrastructural development activities.

the ambition of curtailing its consumption. However, only a marginal increase in SD on cigarettes has been proposed.

Significant increase in SD on cars has been proposed which is likely to have positive implications from the perspective of both revenue generation and traffic congestion. However, this will only be applicable for the 'double cabin pick-ups' which will perhaps limit possible impact.

The budget has proposed the increase of SD on imports of all kinds of fabrics and readymade garments (RMG) articles from 20 per cent to 45 per cent. This is a welcome measure as it will improve the protection available for domestic market-oriented apparel industries. At the same time, the proposed measure to continue with 5 per cent regulatory duty on the import of finished products (along with 25 per cent import duty) is also likely to help protect the local industry and increase revenue collection.

While the proposed SD on cards incorporating a magnetic stripe and import tariff on SIM (Subscriber Identity Module) cards will generate revenue, the budget has reduced tax on SIM card (under VAT) from Tk. 800 to Tk. 600 which is likely to lead to a revenue implications of (-) Tk. 300 crore. One could apprehend that although there is a revenue consequence of the move for the government, there will be no impact on consumers as the tax burden tends to be usually absorbed by the service providers.

The budget has also increased CD on imported textbooks from 5 per cent to 12 per cent which will raise educational expenses for students, and as such, indeed amounts to taxing knowledge.

2.3.4 Export Tax

In the budget for FY2011-12, tax deductable at source for exports is raised to 1.5 per cent while the previous rate was in the range of 0.4 per cent to 0.5 per cent.[8] This will add to the cost burden of the exporters. Since the proposed change is not insignificant, it would have been more appropriate if this increase was made in a more gradual manner to help exporters to cope with the situation accordingly.

Export tax on tobacco (not stemmed, partly stemmed or wholly stemmed) has been reduced from 10 per cent to 5 per cent (Table 2.6). This is likely to encourage cultivation of tobacco leafs, resulting in diversion of agricultural land. Given the already threatened food security situation and the uphill task of further enhancing crop production (particularly of cereals) to keep pace with the population growth, the proposal does not appear to be rational.

Table 2.6

Some Selected Changes in Tax Rates

Item	Duty/Tax	FY2011 (%)	FY2012 (%)	Implication
Liquefied Petroleum Gas (LPG)	Import duty	5	0	Likely to increase the use and reduce pressure on domestic gas supply
All kinds of RMGs and similar articles	SD	20	45	Increased effective rate of protection (ERP) to local industry
Cotton waste	Export duty	0	25	Prevent export and support local textile industries

(Table 2.6 contd.)

[8]Later, the export tax rate at source was reduced to 0.6 per cent for the garments sector, and 0.7 per cent for other industries from the proposed rate of 1.5 per cent.

(Table 2.6 contd.)

Item	Duty/Tax	FY2011 (%)	FY2012 (%)	Implication
Cars: Cylinder capacity up to 1000 cc (double cabin pick-up)	SD	0	30	Reduce purchase of cars/traffic congestion; increase government revenue
Cars: Cylinder capacity of 1000-1500 cc (double cabin pick-up)	SD	0	45	
Cars: Cylinder capacity 4000+ and above (double cabin pick-up)	SD	0	500	
Particle board	Regulatory duty	5	0	Will protect the environment
Cigarettes (at different price level)	SD	33, 53, 56, 58	36, 55, 58, 60	Marginal increase; less likely to reduce consumption
Tobacco, partly or wholly stemmed/stripped	Export duty	10	5	Might encourage agricultural land conversion to tobacco cultivation
Rice, pulse, wheat, sugar, edible oil, onion, fertiliser, seeds	Import duty	0	0	Right move in view of current inflationary trend; will help to keep prices low
Motorcycles (completely built unit (CBU) condition)	SD	30	45	Should help the growing domestic motorcycle manufacturing industries
Motorcycles (completely knocked down (CKD) condition)	Regulatory duty	5	0	Helpful for domestic motorcycle assembling industries
Imported toilet paper and facial tissue	SD	20	30	Higher protection for the growing domestic industry

Source: Budget Document for FY2011-12, Ministry of Finance (MoF).

2.3.5 Tax Incidence

At the import stage, revenue collection during FY2010-11 (July-April) was Tk. 27,959.3 crore, which is about 35.4 per cent of total revenue collection. CPD has estimated that if import value for FY2009-10 is taken as a base year and the tariff structure for FY2011-12 is applied on the import value, proposed changes in CD, SD, regulatory duty and VAT (import) are likely to increase import-related revenues by 23.7 per cent. This appears to be consistent with the projections made in the budget for FY2011-12. This estimation was based on the assumption that import growth for FY2011-12 will be 14 per cent as proposed in the Medium Term Budgetary Framework (MTBF). Nevertheless, if the trend of high import growth (which was 41.8 per cent during FY2010-11) continues in FY2011-12, this will be higher. It also needs to be mentioned here that the estimated revenue collection is possible only under the circumstances that import grows at the rate projected and composition of import structure remains the same as in FY2009-10.

2.3.6 Tax Administration

In the previous fiscal year's (FY2010-11) budget, a number of measures geared towards strengthening of the tax administration were announced. Evidence suggests that noticeable progress has been made with respect to some of these announced measures. These include:

- *E-filing of income tax returns on a limited basis*. After a pilot programme, online filing and digitisation of tax return was scheduled to start from June 2011.[9]
- *Instalment of tax calculator software on the website of NBR*. This is to help taxpayers assess their own tax. The tax calculator is already in place on the NBR website.
- *Motivational programme for taxpayers of income tax and VAT*. A number of programmes such as tax fairs and regional dialogues were carried out during FY2010-11.

[9] However, as of November 2011, online tax filing facility was yet to kick-off outside the pilot project areas covering two tax zones.

However, it is to be noted that a number of measures that were announced for FY2010-11 did not see much (if any) progress. These are:

- *Restructuring of manpower and other facilities of income tax department*. A long standing issue for the NBR and yet to be resolved.
- *Introduction of 2-page Income Tax Return Form*. This was intended to simplify the tax form filling procedure. This is yet to be implemented.
- *Reforms in judicial process for easy settlement of VAT-related cases*. No move could be traced in this regard.
- *Reforms in VAT administration including setting up more VAT offices and recruitment of officials*. VAT offices are still suffering from manpower shortages as no initiative was visible in making fresh recruitments to meet the gap. Also, the proposal was to set up VAT offices in each upazila which did not materialise.

Tax Administration: Measures for FY2011-12

To remove some existing obstacles and strengthen the tax administration, budget for FY2011-12 announced a number of measures. For example, in view of nearly 19,000 pending cases and about Tk. 5,000 crore in taxes being stuck with those, 'alternative dispute settlement means' are proposed to be used to settle such cases outside of the court. This was a welcome measure in expediting the settlement process. However, there is a flipside to this, and hence caution should be practiced to avoid any malpractices in this regard.

The government also planned to expand online tax return filing facility which was introduced as a pilot project in two tax zones of Dhaka City. The budget announced that this facility will be expanded to another two tax zones in this fiscal year, with a plan to cover the entire country by 2013. Indeed, e-filing of tax return is a much awaited measure and is likely to help widen the tax net. The budget also announced for two Taxpayers' Information and Service Centres to be established in Dhaka and Chittagong, from 1 July 2011 to provide taxpayers all the relevant tax-related services. Withdrawal of the requirement of paying tax of Tk. 1,000 for Taxpayer Identification Number (TIN) registration has also been announced. To further motivate taxpayers, the budget announced that taxpayers who show 20 per cent higher income compared to the preceding year, in general, will not be audited. All these are positive measures and should contribute to a better tax administration.

Tax Administration: Concerns

Despite the measures during the last few years, a number of outstanding obstacles remain to be major concerns regarding the tax administration of Bangladesh. Only a few field officials were employed, and as such, acute shortage of manpower by the NBR continues to nag the functions of the institution. The budget for FY2011-12 also imposes the requirement of a quarterly withholding tax return submission (by institutions) in addition to Annual Information Return (AIR). There has been a concern that the measure could increase hassle for the taxpayers. Requirement for submission of AIR for certain financial transactions has also been proposed. While this will improve transparency of financial transactions, discretion should be applied on the basis of merit of the case.

The government is developing new *Direct Tax Act* and *VAT Law* which has been on hold in recent period. Indeed, these laws need to be reformed and revised, and there is no denying of the need to undertake this exercise. However, this should be done following due consultation with relevant stakeholders and experts; appropriate preparatory works ought to be undertaken before going for implementation of a number of these reforms.

2.3.7 Measures to Promote Overseas Employment

The budget for FY2011-12 announces some measures directed towards promotion of overseas employment. It has been announced that labour wings will be established in seven countries with high Bangladeshi labour concentrations. This is indeed a welcome measure, and there is a need to expand the initiative to all other countries in a phased manner.

The budget has made an allocation of Tk. 140 crore to the *Immigration and Skill Development Fund* for much needed skill development of potential overseas workers. The plan includes the establishment of 30 new Technical Training Centres (TTCs) and five new Marine Technology Institutes which is a positive initiative. However, the earlier project named *Skill Development Fund for Expatriate Returnees and New Entrants to Labour Market* has been discontinued in FY2011-12.

Overseas Employment: Gaps in Addressing Special Needs

Notwithstanding the measures proposed, there appears to be some gaps in addressing special needs of the overseas job sector. Despite much discussion, nothing has been mentioned about designing a 'Contingency Plan' to address the needs of Bangladeshi migrant workers in the host countries during times of crisis. One may recall here the experience from the Middle East and North Africa (MENA) crisis when necessities for such emergency support measures were critically felt. The budget also has not provided any indication towards giving special focus on skill development of aspirant female migrant workers.

2.4

SECTORAL MEASURES

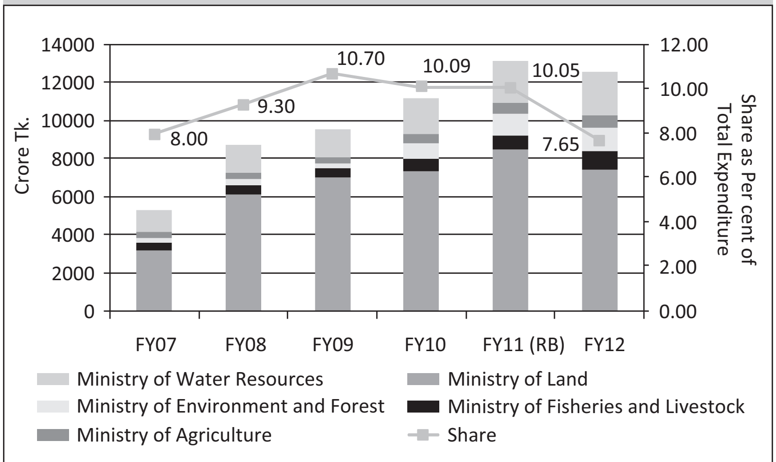
2.4.1 Agriculture

Allocation for Agriculture and Allied Sector

Though a lot of emphasis is given on the agriculture sector given its contribution towards food security of the country, the allocation for this sector has surprisingly been reduced in FY2011-12 compared to the previous fiscal year. In the proposed budget of FY2011-12, allocation for the Ministry of Agriculture in (MoA) total budget is 4.53 per cent, when this share was 6.49 per cent in the revised budget of FY2010-11. On the other hand, allocation for the agriculture and allied sectors (development and non-development) is (Tk. 12,516 crore), 4.23 per cent lower than the revised budget of FY2010-11 (Tk. 13,069 crore). This allocation is 7.65 per cent of total budget in FY2011-12 compared to 10.05 per cent in the revised budget of FY2010-11. However, allocations for a

Figure 2.4

Trend of Budgetary Allocation and Share (Development and Non-Development) of the Agriculture and Allied Sectors



Source: Budget Documents (various years), Ministry of Finance (MoF).

number of related ministries such as Ministry of Fisheries and Livestock, Ministry of Environment and Forest, Ministry of Land, and Ministry of Water Resources in FY2011-12 have increased by 23.05 per cent, 9.13 per cent, 16.41 per cent and 4.45 per cent respectively compared to the revised budget of FY2010-11. Allocation for agriculture and allied sectors is considered as public investment for its sectoral development. The declining trend in the allocation as a share of total proposed budget may have negative impact on the country's effort to achieve food self-sufficiency, and in ensuring food security. Figure 2.4 and Table 2.7 show allocation for agriculture and allied sectors.

Table 2.7

Changes in Budgetary Allocation and Share of the Agriculture and Allied Sectors

(Crore Tk.)

Ministry/Division	FY2012 (B)			FY2011 (RB)			Change between FY2012 (B) and FY2011 (RB) (%)	Share of Agriculture and Allied Sectors in Total Budget (%)	
	Non-Development	Development	Total	Non-Development	Development	Total		FY2012 (B)	FY2011 (RB)
Ministry of Agriculture	6368	1038	7406	7393	1042	8435	-12.20	4.53	6.49
Ministry of Fisheries and Livestock	509	468	977	492	302	794	23.05	0.60	0.61
Ministry of Environment and Forest	955	276	1231	942	186	1128	9.13	0.75	0.87
Ministry of Land	501	173	674	477	102	579	16.41	0.41	0.45
Ministry of Water Resources	721	1507	2228	689	1444	2133	4.45	1.36	1.64
Agriculture and Allied Sector	9054	3462	12516	9993	3076	13069	-4.23	7.65	10.05

Source: CPD calculation based on the Budget Documents, Ministry of Finance (MoF).

Agricultural Subsidy

In the budget of FY2011-12, the amount of subsidy for fertiliser has been reduced. The amount allocated amount for agricultural subsidy is Tk. 4,500 crore in FY2011-12 which is 26.66 per cent lower than the revised budget of FY2010-11, and 12.5 per cent higher than the original budget of FY2010-11. In April 2011, prices of diammonium phosphate (DAP), urea, triple super phosphate (TSP) and muriate of potash (MoP) were USD 617, USD 340, USD 536 and USD 414 respectively.

In view of the upward trend and volatility in international fertiliser market, actual subsidy for fertiliser may have to be revised as well over the subsequent period. CPD estimation based on imported price and projected demand of fertiliser shows that an amount of Tk. 5,732 crore may be needed in FY2011-12 as subsidy for fertiliser that is Tk. 1,232 crore higher than the allocated Tk. 4,500 crore in the proposed budget of FY2011-12 (Table 2.8).

Table 2.8

Projected Estimation of Subsidy Requirement for Fertiliser in FY2011-12

Fertiliser	Source	Price (USD/Ton)	Insurance and Freight Charge (USD/Ton)	Imported Cost (USD/Ton)	Cost (Tk./kg)	Administered Price (Tk./kg)	Quantity (Lakh Ton)	Subsidy (Crore Tk.)
DAP	China	617	50	667	48.6	27.0	6.5	1401
Urea	China	340	60	400	29.1	20.0	21.0	1915
	Bangladesh				9.5	20.0	9.0	-945
TSP	Tunisia	536	100	636	46.3	22.0	7.0	1701
MoP	Belarus	414	100	514	37.4	15.0	7.4	1659
Total	-	-	-	-	-	-	50.9	5732

Source: CPD estimation.

High market price in the international market is one of the factors contributing to this gap. According to Commodity Market Review of the World Bank Pink Sheet, international market prices saw substantial increment over the last year. Prices of urea, TSP, DAP and MoP increased by 24 per cent, 81 per cent, 44 per cent and 17 per cent respectively between January 2010 and April 2011. If the Government of Bangladesh (GoB) did not readjust the recent administered price of urea (from Tk. 12/kg to Tk. 20/kg), additional subsidy of Tk. 2,400 crore would be needed to meet the projected demand.

Fair Price for Agricultural Produce

In accordance with the Budget Speech FY2011-12, the government is planning to form additional 600 Farmers' Marketing Group and 6,200 Farmers' Club throughout the country to ensure fair prices for agricultural produces. Moreover, the government is taking steps to establish four agro-products processing centres which will facilitate agricultural marketing. The budget also mentioned that 'wholesale market infrastructure' in 15 districts and 'growers' market infrastructure' in 16 districts of the northern region have already been established. In addition, 490 Farmers' Marketing Group and 16,677 Farmers' Club have already been formed throughout the country. All these timely initiatives are needed to be continued to maintain fair price for agricultural produce in view of the formidable difficulties that farmers face in getting fair price in their end.

Agricultural Insurance

The proposed budget mentions that 'Crop Insurance' would be provided to small and medium farmers through crop price support in case of the yield damages caused by natural disasters such as flood and cyclone. Towards this, the state-owned Sadharon Bima Corporation has drawn up a pilot project in one upazila. However, no specific allocation has been made to initiate this scheme. In this regard, clarity in terms of modalities and procedures will be needed for implementation of the proposal in an appropriate manner.

Agricultural Research

In the proposed budget for FY2011-12, agricultural research fund is increased to Tk. 450 crore from Tk. 350 crore, mainly through interest (as profit) accumulation. The size of the fund is very small compared to the need and government's commitment towards agricultural development. Efficient allocation and use of these funds are important criteria to achieve quality and productive outcomes. Additional fund and adequate fund utilisation mechanism are also needed. *National Agriculture Policy 2011* and *Bangladesh Agricultural Research Council Act, 2011* should be finalised and enacted to support the agriculture sector and to strengthen research capacity in this sector.

Fisheries and Livestock

In FY2010-11, production of hilsha fish had indeed registered some increase, thanks to several programmes to prevent the netting of *jatka*. In the proposed budget, the government announced to finalise a draft Shrimp Policy to encourage environment-friendly shrimp cultivation. In this regard, a total of 22,175 shrimp farmers have been trained and 188 demonstration firms have been set up with the registration of 180,000 production firms. In FY2011-12, there is a plan to develop the livestock sector through initiatives including construction of 200 artificial insemination points, a semen production lab, setting up bull stations, and training programmes for farmers and volunteers. The budget also mentioned that required activities are in progress to increase meat and milk production by using improved variety and artificial technology. However, specific allocation is needed to implement these objectives. Allocation of Tk. 947 crore is proposed for the development of fisheries and livestock sector to carry out the development programmes.

2.4.2 Industrial Sector

During the new fiscal year FY2011-12, the industrial sector will find it increasingly difficult to maintain last year's growth (9.5 per cent in FY2010-11 vis-à-vis 6.5 per cent in FY2009-10, particularly the manufacturing sector) because of poor benchmark condition prevailing in the economy. This includes slow economic growth in the USA and debt crisis in a number of Eurozone countries, weak BOP situation, instability in the foreign exchange market, pressure on availability of credit for private sector, and high inflation rate. In this backdrop, one only hopes that the various fiscal and budgetary measures proposed in the National Budget 2011-12 will prove to be adequate to address the manifold challenges that the industrial sector is confronted with.

Tax Holiday

Government is likely to revisit the tax holiday facility provided to different categories of industries with a view to rationalise the structure of support for the industrial sector in a phased manner. In the 2011-12 Budget, government has proposed the structure of a revised tax holiday facility by including some new industries and replacing some of the existing ones, and also extending the timeline for eligibility for the facility till June 2013 (Table 2.9). The revision of the list of sectors to be eligible for tax holiday facility is,

Table 2.9

Coverage of the Thrust Sectors under the Proposed Revision of Tax Holiday Measures

Thrust Sector	Sectors under Existing Tax Holiday Measures	Sectors under Newly Proposed Tax Holiday Measures
Agro-based and agro-processing industry	Fertiliser, insecticide, pesticide, agro-machineries and agro-processing	Bio-fertiliser, insecticide and pesticide, and processing of locally produced foods and vegetables
Ship-building	Tax holiday present	N/A
Renewable energy and appliances	Solar energy plants	Energy-efficient appliances
Tourism	Residential hotels of 3-star standard	N/A
Basic chemicals	Basic ingredients of chemicals	Basic chemicals or dyes and chemicals
Information and communication technology (ICT) and ICT-based services	Computer hardware production	Basic ingredients of electronic industry (e.g. resistance, capacitor, transistor, integrator circuit), computer hardware
RMG, home textiles and handicrafts	High-value garments and textiles	Textile machinery
Active pharmaceutical ingredient (API), radio pharmaceuticals, pharmaceuticals	Pharmaceuticals, basic ingredients of drug and pharmaceuticals	Pharmaceuticals, API industry and radio pharmaceuticals industry
Radioactive industry	N/A	Tax holiday proposed
Development of polymer industry	Melamine, petrochemicals	Petrochemicals
Jute and jute products	Jute goods	N/A
Light engineering industry	Steel production from iron core, boilers, compressors, MS rod	Boilers, compressors
Plastic industry	Plastic	N/A
Ceramic	Ceramic and sanitary ware	N/A
Tissue grafting and biotechnology	N/A	Tax holiday proposed
Jewellery	Diamond cutting	N/A
Cosmetics and toiletries	N/A	Barrier contraceptive and rubber latex
Tea industry, herbal medicinal plants, hospital and clinic, leather and leather products, furniture, frozen fish, toys, human resources export	N/A	N/A

Source: National Budget Speech FY2011-12 and Industrial Policy 2010.

however, not always in consonance with the list of sectors mentioned as 'thrust sectors' in the *Industrial Policy 2010*. With a view to diversify the location of industries, the National Budget 2011-12 has offered tax holiday facility to the lagging regions which are outside the regions of Dhaka, Gazipur, Narayanganj and Chittagong. These initiatives are the continuation of existing differentiated tax holiday schemes for different regions. This may have some positive impact. However, till the time appropriate infrastructural facilities are developed in the targeted areas, including roads, supply of electricity and gas, other logistic facilities, linkage with the seaport, etc., the likelihood of tax holiday facility in being able to actually attract investment in those regions will remain doubtful.

Import Duty and Other Indirect Taxes

The budget of FY2011-12 has proposed some changes in the duty structure at import stage with a view to improve competitiveness of local industries. The reduction of duty on imported raw materials and intermediate products belonging to the sectors such as chemical, particle board and light engineering would cause a reduction of total tax incidence (TTI) within the range of 0.6 to 7.7 percentage points. Increase of duty on finished imported products, on the other hand, would likely to raise the price of domestic finished products as TTI will be increased by about 15 to 70 percentage points (for example in case of RMG, glass and furniture sectors), as shown in (Table 2.10).[10] It appears that these measures will have adverse impact on certain sectors in view of the likely shortages of fund for financing productive activities, attendant high interest rate, rising cost of import due to volatility in the foreign exchange market, and high inflation.

Table 2.10

Import-Substituting Sectors: Change in Total Tax Incidence

Sector	Difference in TTI between FY2012 and FY2011
Chemical (raw materials)	-0.6
Particle board (raw materials)	-7.7 to -0.6
RMG (intermediate/finished products)	38.0 to 70.0
Glass (intermediate/finished products)	14.8
Light engineering (raw materials/finished products)	-0.6 to 22.5
Furniture (finished products)	14.8

Source: CPD estimates.

Development of Standardisation System

In view of the need to maintain the required standards of local product, improvement of standardisation and testing facilities at the Bangladesh Standards and Testing Institution (BSTI) is exceedingly important. To this end, the ongoing project titled *Strengthening of BSTI* needs to be completed immediately. However, allocation for this project in FY2011-12 appears to be rather insignificant (Tk. 1.01 crore out of Tk. 72.9 crore). The likelihood of timely completion of the project in the coming fiscal year is rather doubtful under the circumstances.

Sector-specific Measures

Textiles and RMG

Although the Finance Minister has expressed concern with regard to the likely pressure on the backward linkage textiles sector, particularly given the adverse situation facing the sector in view of the changing Rules of Origin (RoO) in the EU-EBA (European Union's Everything But Arms), the developments in the industry should be put under close scrutiny. The government should be ready to provide support if there is a need to do so

[10]The FY2011-12 Budget announced measures related to import on following products: plastic, PET light sheet, LPG cylinder instruments, computer and related parts, pharmaceutical products, effluent treatment plant (ETP) and related parts, poultry industry, capital machinery, perfumes, woven fabrics, RMG, glass tube, fan, furniture parts, particle board, CKD motorcycles, sugar confectionary, spectacles.

(e.g. through a support package). On the other hand, proposed imposition of SD on imported fabrics (from 20 per cent to 45 per cent) should have some positive impact for the competitiveness of domestic market-oriented textiles mills. With a view to rise of the contribution of export-oriented industries in government's exchequer, the national budget for FY2011-12 has proposed to increase the rate of tax deduction at source for all export proceeds from 0.4 per cent or 0.5 per cent to 1.5 per cent. Given the diverse nature of industries in terms of volume of export, proceeds, size of firms, rate of profitability, etc., the governments should take phase-by-phase approach for full implementation of the initiative.[11] Extension of the timeline for renewal of bond licenses from one year to two years will reduce barrier to exporters.

As part of continuation of earlier initiatives to improve industrial waste management in the manufacturing sector, the national budget for FY2011-12 has proposed to bring down the duty on certain chemicals required for setting up ETP (not locally produced) to 3 per cent which contributes to reduce the set up cost of ETP by the industrial enterprises. Although various fiscal measures have been announced for last several years to make factories environmentally compliant, the fact of the low rate of setting up of ETPs by the enterprises remains a nagging concern.

Given the rising demand for professionals and skilled workers in the textiles sector, necessary allocation for the establishment of adequate number of textile institutes is important. Unfortunately, there is lack of sufficient allocation against the approved ADP projects announced in the budget. While two-thirds of the stipulated timeline of the projects will be over in FY2011-12, only 8.6 per cent of the total expenditure is likely to be used within that timeline. Necessary allocation for land and infrastructure development is required to complete the 'unapproved and unallocated' project titled *Garment Palli*. Allocation should also be made for construction of dorms for RMG workers.

Jute and Leather

In order to sustain the recent surge in the export of jute goods, adequate budgetary support is required for the improvement of the competitiveness of the jute manufacturing sector. The exclusion of jute industry from the tax holiday facility under the newly proposed scheme rather contradicts the government policy stance with respect to the sector. However, an accelerated depreciation in lieu of tax holiday is in effect for the jute manufacturing sector. In order to increase capital and labour productivity, a special *Technology Upgradation Fund (TUF)* is needed for the jute sector which could be used for technological restructuring. NBR and Bangladesh Tariff Commission should consider providing separate Harmonized Commodity Description and Coding System (HS) codes for machineries and spare parts imported for jute mills.[12]

The *Leather Industrial City* – a project currently being implemented with a view to establish an environment-compliant industrial zone for the leather sector needs to be completed on an urgent basis. As of December 2010, only 18.4 per cent of the project has been completed and another 27.7 per cent is to be completed in FY2011-12. This is a rather lengthy timeline. Government should actively think of removing bureaucratic and financial impediments including compensation for relocation of factories from their existing locations. Soft term loans should be made available for this purpose and for sharing of the cost burden connected with setting up of centralised ETP facilities.

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[11] Taking into account the concern raised by the exporters, the tax deduction at source has been raised to 0.75 per cent for all export proceeds.

[12] Currently machineries of jute mills are treated under the same HS classification applied for textile machineries.

Pharmaceuticals

Pharmaceuticals sector will enjoy tax holiday facility for new ventures (such as active pharmaceutical products and radio pharmaceutical products) along with ventures for basic ingredients of drugs. In this connection, the *Active Pharmaceutical Ingredient Industrial Park* project needs to be completed in an expeditious manner (as per the project timeline it is supposed to be finished by the end of December 2011). With the level of progress made so far (only 29.9 per cent of total cost of the project spent) and the proposed allocation for FY2011-12 (another 22.3 per cent), it is unlikely to be completed in accordance to the timeline. The sector also requires allocation for improvement of logistics and support facilities, particularly for establishment of drug-testing laboratory (as has been proposed, in Gopalganj), upgrading manpower in the other two drug-testing facilities, and setting up of appropriate storage facilities for the export of drugs and other ingredients.

Small and Medium Enterprise (SME)

The national budget for FY2011-12 has proposed reduction of annual turnover tax for SMEs to 3 per cent from the existing level of 4 per cent, keeping the turnover tax margin unchanged (Tk. 60 lakh). Whilst only a limited number of sectors are currently eligible to enjoy the benefits, the government may consider expansion of the eligibility criteria for SMEs from other sectors. Although the government has announced a number of measures in support of the SMEs, given the adversities in terms of high interest rate and high inflation, the possible implications of these measures are likely to be low.[13]

The coverage of Equity and Entrepreneurship Fund (EEF) implemented by the Bangladesh Bank is to be extended to silk, flowers and herbs.[14] The Fund could be made available for other potential labour-intensive industries as well, including light engineering, plastic, melamine and electronics. Currently import tariff on capital machinery is 1 per cent for the export-oriented industries and 3 per cent for the rest. It is advisable to set import tariff on capital machinery at 1 per cent across the board. The proposed reduction of import duty on some of the raw materials for iron and steel industry will reduce the production cost of the light engineering sector. Due to the lack of required supply of raw materials from the local ship-breaking industries, light engineering factories have been at a disadvantage. In view of this, import of cast iron shaft and cables will need to be encouraged.

Information and Communication Technology (ICT)

ICT sector will get an allocation of Tk. 2,300 crore in FY2011-12 which is equivalent to 5.5 per cent of total ADP allocation. This is in consonance with the annual allocation target envisaged in the *National ICT Policy 2009*. However, poor state of implementation of a number of important IT infrastructure projects (SASEC Information Highway, High Tech Park, etc.) has become a concern. Likewise, the delay in the establishment of the second submarine cable line which would help a faster linking with the global information highway has also been detrimental to the country's interest. The inordinate delay in finalising the policy guideline with regard to usages has not been helpful.

The National Budget 2011-12 did not propose any reduction of import duties on various computer parts, components, special networking parts and cables although the *ICT Policy 2009* had suggested this. Reduction of duties would have reduced the cost for repairing and assembling of computers and other IT components. There is also no announcement in

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[13]Recently the Central Bank has removed the lending cap on interest rates. At present interest rate on term/working loan is 10-18 per cent.
[14]Previously only agro and ICT industries were eligible for this facility.

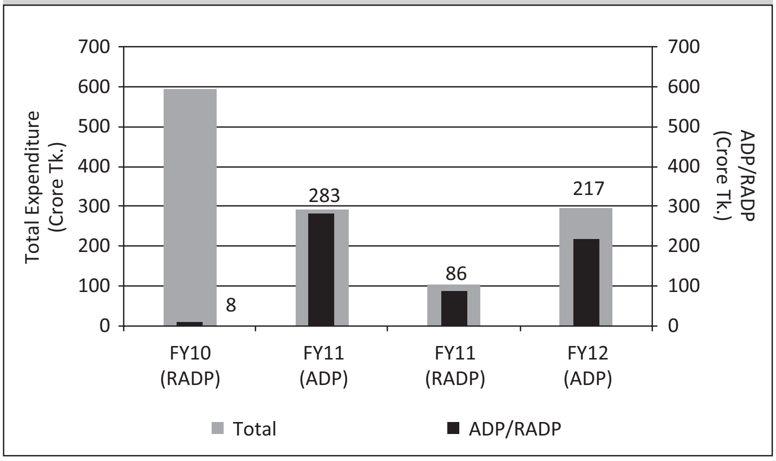
the budget to withdraw the VAT over the use of internet. This would have encouraged wider access to internet facilities. Like some others, IT sector will also enjoy the extended tax holiday facility up to 2013. Government should keep in mind that such facility will need to be extended further, till 2018, as per the recommendation of the *ICT Policy 2009*. It was expected that as per the policy guideline, a separate ICT authority would be set up with an allocation of 10 per cent of proposed fund (Tk. 700 crore); however, there is no mention about this in the budget. Likewise, there is no mention about the separate VAT code for IT and IT-enabled services in order to reduce the complexities in the VAT collection process.

Tourism

Despite the announcement of tourism sector as a thrust sector, there is inadequate reflection of this in the budgetary allocation of FY2011-12. The total allocation for the Ministry of Civil Aviation and Tourism in FY2011-12 is amounted to Tk. 296 crore, of which Tk. 79 crore is for non-development purpose and Tk. 217 crore is for development programmes. As a matter of fact, Ministry's revised budget for FY2010-11, particularly the development budget, has been drastically reduced to a mere Tk. 86 crore against an initial allocation of Tk. 283 crore (Figure 2.5). This has happened largely on account of the slow implementation of the single largest project under the Ministry, i.e. upgradation of the Hajrat Shahjalal International Airport. In fact, last year's unspent money for this project has been reallocated in this year's development budget for the Ministry. A number of tourism development projects were included in the ADP for FY2011-12 without any approval and specific budgetary allocation. This included, among others, development of tourism facilities at the Bangabandhu Mausoleum at Tungipara and the proposed Padma Bridge areas, and in Panchagarh and Noakhali districts. The provision for tax holiday for 3-star residential hotels has been withdrawn under the new scheme. Such facility should have continued particularly for tourist locations with high business potentials.

Figure 2.5

ADP and RADP in the Tourism Sector



Source: Estimated from the Planning Commission data.

Real Estate and Housing

Real estate sector has been confronted with a number of challenges in recent times. These included withholding of gas and electricity connections for newly constructed apartments because of supply shortages.[15] Since, the government is actively thinking of implementing the measure to set up solar panels in newly constructed apartments, subsidised credit facility for this purpose would encourage attainment of this objective. The national budget for FY2011-12 has revised the tax rates for registration of apartments and commercial spaces. Real estate companies will benefit from reduction of taxes for registration of apartments; however, for some, the cost will rise since tax rates for commercial spaces has been raised (Table 2.11).

[15]With the rise in the supply of electricity and gas under the ongoing projects, allocation for newly constructed apartments and commercial space should now be increased.

Table 2.11

Existing and Proposed Tax for Registration of Apartments and Commercial Spaces

Level	Apartment			Commercial Space				
	Existing Tax Rate for Category B (Tk. 2,000/ sq. m)	Proposed Tax for Category B (Tk. 1,800/ sq. m)	Reduced Tax Burden (Tk.)	Existing Tax Rate for Category A & B (Tk. 2,000/ sq. m)	Proposed Tax Rate for Category A (Tk. 20,000/ sq. m)	Proposed Tax for Category B (Tk. 15,000/ sq. m)	Increased Tax Burden for Category A (Tk.)	Increased Tax Burden for Category B (Tk.)
1000 sq. ft	185874	167286	18588	185874	1858736	1394052	1672862	1208178
1200 sq. ft	223048	200743	22305	223048	2230483	1672862	2007435	1449814
1500 sq. ft	278810	250929	27881	278810	2788104	2091078	2509294	1812268
2000 sq. ft	371747	334572	37175	371747	3717472	2788104	3345725	2416357

Source: CPD estimates.

Note: Category A includes: Gulshan, Banani, Baridhara, Motijheel and Dilkusha of Dhaka. Category B includes: Dhanmandi, Lalmatia, Uttara, Bashundhara, DOHS, Mohakhali, Dhaka Cantonment and Karwanbazar of Dhaka; and Khulshi, Agrabad, Nasirabad and Panchlaish of Chittagong.

Industrial Workers

A number of projects related to the development of human resources has been proposed in the national budget of FY2011-12; however, without any approval and allocation. Some of these are: establishment of five zonal and four regional training centres; 22 labour welfare centres and three industrial training centres; development of the National Institute of Labour Administration and Training at Tongi; project for skill development of *monga*-afflicted people in North Bengal; and reconstruction of Dhaka Divisional Labour Office. Funds need to be allocated for the existing 29 Worker Welfare Centres in order to make them operational. In view of the high food inflation, broadening of subsidised food distribution system for the RMG and textile workers through Open Market Sales (OMS) and other distribution mechanisms is a welcome initiative.

Capital Market

The capital market needs radical restructuring and reforms which must be geared to rescue the market from its current dysfunctional state. There were expectations that institutional as well as necessary fiscal and budgetary measures would be proposed in the budget to this end. In this connection, announcement of enactment of the *Financial Reporting Act*, establishment of the Financial Reporting Council, Clearing and Settlement Company, enforcement of demutualisation of stock exchanges, amendment of the *SEC Act* and *Security and Exchange Commission (Public Issue) Rules, 2006* would contribute positively towards improvement of governance in the capital market. Although injection of money in the capital market has been questioned by many, the government has announced provision for investment of undocumented/undisclosed money in the capital market and also for investing in BIFFL and treasury bonds, subject to payment of tax at the rate of 10 per cent. However, tax deductible at source for the commission charged by the brokerage houses has been raised from 0.05 per cent to 0.1 per cent.

Strengthening the surveillance system in the capital market has been a widely discussed issue. Although funds were allocated for the Asian Development Bank (ADB)-financed projects for strengthening of the capital market, but these were not actually disbursed within the stipulated time for reasons not known to the general public. This project has been revived and allocation has been made in order to implement the project by 2012. Besides, the government should make it mandatory to have TIN for all Beneficiary Owner (BO) account-holders with a view to ensuring transparency in transactions at the capital market.[16]

[16]Interested readers may like to consult CPD publication titled *State of the Bangladesh Economy in FY2010-11 (Second Reading)* for a more detailed discussion of the relevant issues, available on the CPD website (http://www.cpd.org.bd/downloads/IRBD_FY11.pdf).

2.4.3 Power and Energy

The allocation for power sector reflects the government's policy to strengthen power supply in the country. However, the allocation for energy sector appears to be low compared to the revealed demand, particularly when the issue of accelerating power generation in the long-run is considered.

In FY2011-12 Budget, the 'Power and Energy' sector received a total allocation of Tk. 8,311 crore (15 per cent higher than last year's allocation). Of this, Tk. 8,286.5 crore has been allocated under ADP and the remaining sum of Tk. 24.5 crore for non-development expenditure. If the GDP targets envisaged in the draft Sixth Five-Year Plan (SFYP) are to be achieved, there is a need to ensure about 10 per cent annual growth in energy consumption in the country during FY2011-12 to FY2014-15 period. The budget of FY2011-12 is unlikely to support such a 'big push' in energy consumption. Achieving the GDP targets projected in the SFYP will face problem in view of this.

Power

The revised target of producing 11,698 mega watts (MW) of additional power by 2015 (in place of 8,634 MW projected in the last year's plan) reflects the need of the economy. However, this appears to be rather difficult to achieve given the current rate of success and the resource constraints that the government faces. It is to be noted here that by the first week of June 2011, five quick rental power plants of 333 MW capacities failed to start their respective planned generation. On the other hand, the actual generation from the seven quick rental plants of 622 MW capacity was found to be about only 75 per cent in the month of May 2011 (due to mechanical problems, as noted by BPDB). This would mean that the current delay in generation and underperformance by power plants will put under threat the attainment of targets envisaged in the revised Power and Energy Plan.

The government is planning to generate 5 per cent of total power from renewable energy sources by 2015. This would mean that 610 MW of electricity will need to come from this particular source (given the production target of 12,197 MW by 2015). Attaining this will require huge resource allocation as renewable energy generation is costlier compared to primary energy-based power generation. Given this scenario, the target appears to be difficult to achieve by 2015.

The target of generating additional 700-800 MW of power from renovation of the aged plants appears to be an open-ended target since no timeline has been mentioned in the plan. Moreover, at present there are only two projects running under the ADP for renovation of aged plants in the country, and no new project has been proposed in FY2011-12. Given this, strengthening of the generation capacity of the aged plants by 700-800 MW through renovation appears to be a rather long shot.

Energy

An additional gas production of 1,920 million cubic feet per day (mmcfd) by 2013 appears to be a high target, particularly in view of the uncertainties surrounding the production of 1,000 mmcfd gas by the international oil companies (IOCs). 'Sunetra' could perhaps contribute to improving the situation. Additionally, the budgetary allocation for Bangladesh Petroleum Exploration & Production Company Limited (BAPEX) appears to be inadequate in view of the tasks ahead.

The need for a 'planned energy use guideline' to achieve 'energy use efficiency' is missing in the revised *Power and Energy Sector Road Map*, which is vital for the country to reduce the misuse of energy resources.

Risks and Challenges

There are a number of risks and challenges that the government is likely to face in the power and energy sector during the current FY2011-12. Increasing subsidy demand for power and energy may emerge as a major problem for the government. It is to be noted here that, the subsidy requirement for quick rental power plants alone in FY2011-12 might reach to the tune of Tk. 6,300 crore to Tk. 9,850 crore.

It is rather strange that the issue of this significant subsidy burden, in addition to the fuel subsidy which will need to be given, has not been mentioned in the budget. There is an urgent need to make the subsidy issue (both on account of sale of fuel and purchase of power) more transparent. Financing of this increasing subsidy should also be clearly spelt out. This is necessary not only from the perspective of sound macroeconomic management, but also to ensure long-term sustainability of power and energy sector growth in the economy.

Recommendations

Implementing the power plan and ADP projects efficiently will prove to be a challenging task for the government. Even if in the short-run the quick rental power plants are able to somewhat take care of the load shedding, in the long-run the accumulated oil import charges will put pressure on the BOP. Increasing domestic borrowing will be necessary which is likely to lead to higher inflation and undermining of macroeconomic stability. In view of this, the following initiatives demand special attention:

Resuscitate the National Coal Policy: According to the *Power Sector Master Plan*, by 2014 coal is envisaged to be a major source of energy in Bangladesh. Towards this, the *National Coal Policy* needs to be finalised on an urgent basis.

Renovation of old power plants: The allocation made in Budget FY2011-12 for the energy sector development may not be enough to achieve power generation targets. Renovation of aged power plants has not received due budgetary support that it deserves, although the target to achieve 700-800 MW additional power through augmentation of capacity has been mentioned in the *Revised Power and Energy Road Map*.

Ensuring quick rental power plants' efficiency: The deadline for achieving this target is also not clear. Some policy guidelines should have been provided to ensure that quick rental power plants generate the 'agreed' amount of power. Otherwise, the planned supply projected in the revised road map could come under threat.

Tariff rationalisation: The budget should have provided a sense with respect to the rationalisation of power tariff that the government was planning to implement.

2.4.4 Environment, Climate Change and Disaster Management

Though Bangladesh is considered to be one of the most vulnerable and adversely affected countries from the perspective of climate change, budgetary allocation does not reflect this concern. It is true that due to increasing awareness with regard to climatic vulnerability and environmental risks, the government is putting emphasis on comprehensive policy strategy for environmental care and disaster management. In order to mitigate the adverse affects of climate change, Bangladesh Climate Change Trust Fund (BCCTF) has been established for improving capacity building for disaster management. In line with the budget of the previous two years, Tk. 700 crore was allocated for BCCTF in FY2011-12. In FY2009-10 and FY2010-11, a total of Tk. 1,400 crore was allocated for 60 projects (worth Tk. 719.61 crore) initiated under this fund. Moreover, to ensure appropriate utilisation of the fund, the *Climate Change Trust Act, 2010* has already been enacted. In line with the same purpose, the government has also created another fund titled Bangladesh Climate Change Resilience Fund (BCCRF), which is worth of USD 113.5 million. This fund is supported by development partners.

Air pollution has emerged as a serious health threat in the country. One of the major reasons for air pollution is the brickfields which are primarily located in the adjoining areas of the capital Dhaka. The government has already set the deadline for improving their existing technology and has put a ban on export of brick. Moreover, in order to identify the sources of air pollution and to reduce the pollution in the Dhaka city to a minimum level, a special project titled *Clean Air and Sustainable Environment* has been undertaken. With a view to controlling air pollution in the export processing zones (EPZs) of Chittagong and Dhaka, the Infrastructure Development Company Limited (IDCOL) has granted funds for the installation of central ETP system. In order to manage the industrial waste in an environment-friendly manner, the *Solid Waste Management Rules, 2011* and the *Hazardous Waste and Ship Breaking Waste Management Rules, 2011* is expected to be enacted by FY2011-12. A proposal has been made to reduce tax by 3 per cent from the earlier 5-12 per cent on chemicals imported for ETPs. This is a welcome step.

Apart from these initiatives, a number of steps have been taken to update the existing laws, rules and regulations. In order to protect and preserve the existing environment, *Bangladesh Environment Preservation (Amendment) Act, 2010* and *Bangladesh Environment Court Act, 2010* have been enacted already. Moreover, to maintain ecological and environmental balance, the government has prepared the *National Action Plan 2020*, and formulated *Wildlife Protection Act, 2010*, which is in the process of finalisation. It is mentioned in the proposed budget that 20 per cent land of the country will be under afforestation programme by the year 2015.

Mitigating the risks of natural disaster and coping with the consequences of environmental hazard are some of the major challenges for a country such as Bangladesh. Though the government is implementing the second phase of *Comprehensive Disaster Management Project* and *National Disaster Management Plan 2010-15*, the internalisation of climate change concerns into development projects has not received a positive nod in the proposed budget. However, as per the promise in the previous budget to modernise the forecasting and warning system, an early warning system through cell phone networks of Grameen Phone and Teletalk in Cox's Bazar and Sirajganj districts has been initiated on a pilot basis. This is a positive move and more districts are expected to be covered in the coming year.

2.4.5 Rural Development and Local Government

Rural Development

A number of initiatives have been proposed in the budget of FY2011-12 to promote regional development and increase the effectiveness of the local government. A combined development and non-development budget allocation of Tk. 11,714 crore is proposed for rural development and local government, which is 18 per cent higher than the revised budget allocation of FY2010-11. For the upcoming fiscal year, 24 per cent of the development expenditure will go towards rural development. This includes total 68 projects, of which only five are new initiatives. All the new projects are under the Local Government and Engineering Department (LGED), and mostly geared towards infrastructure development, including construction of *Aila*-affected rural infrastructure. Another project which received a positive nod from the government relates to setting up of 2 lakh water sources by FY2012-13. For ensuring supply of arsenic-free water in rural areas, the government plans to design a policy to re-excavate and ensure at least one source of safe water supply in each village, with active support from the local government. Such a drive is likely to be given priority in the coastal belt, drought-prone and other disaster-prone areas in Bangladesh.

The GoB is also sketching out a policy framework for *Integrated Land Use and Housing* to complete land zoning and to set up *Palli Nibash* (rural housing area) in union and upazila growth centres so that unplanned housing does not hamper arable lands. In this regard, *Protection of Cultivable Land and Land Use Act, 2011* has been finalised. It is expected that these initiatives would generate positive outcomes for the rural economy of Bangladesh. Moreover, the second phase of the *Chittagong Hill Tracts Development Project* is going to start in foreseeable future to improve the living standard of ethnic minorities in the Chittagong Hill Tracts (CHT) areas. An amount of Tk. 10 crore has been allocated for constructing a housing colony for Dhangar ethnic community in this region which has traditionally belonged to neglected segment of the society. In the coming years, such initiatives could be taken for many of the other ethnic communities living in the country to raise living standards of these neglected communities in our country.

Due to existing high demand-supply gap with respect to power generation, access to power persists to be a major problem in the rural areas of the country which often has to bear the brunt of power outages. In this regard, the Rural Electrification Board (REB) has set up a target of 14,408 home solar systems in the underprivileged rural areas which are not covered by the national power grid. On the other hand, IDCOL has installed bio-gas plants for about 20,000 households, and plans to add another 150,000 plants by 2016 under the *National Household Bio-gas and Fertilizer Program*. Respective government agencies have also taken steps to commercialise production procedures and use of bio-gas and bio-electricity by making use of poultry and dairy firm wastes. Such non-traditional measures, through appropriate government patronisation, can reduce grid-based electricity consumption in the country.

Local Government

Local Government (Union Parishad) Act 2009, Local Government (Pourashava) Act 2010, and *Local Government (City Corporation) Act 2009* were designed towards decentralisation of the governance system and with a view to strengthening people's participation in governance in the country. However, adequate resource allocation and real empowerment will be the real keys to getting the desired outcomes. Training has been provided to upazila parishad chairpersons and vice chairpersons so that they are able to discharge their responsibilities better. Moreover, audit has been conducted at the union parishad (UP) level to ensure transparency and accountability of public expenditures. All these initiatives are commendable, and continuation of such measures may be helpful in strengthening and empowering the local government system in the country.

The GoB has also taken initiatives to restructure the zila parishad. Additionally, necessary measures have been taken to formulate/amend laws to further strengthen the pourashavas and city corporations. However, no specific allocation has been made in the proposed budget of FY2011-12 to implement these measures.

2.5

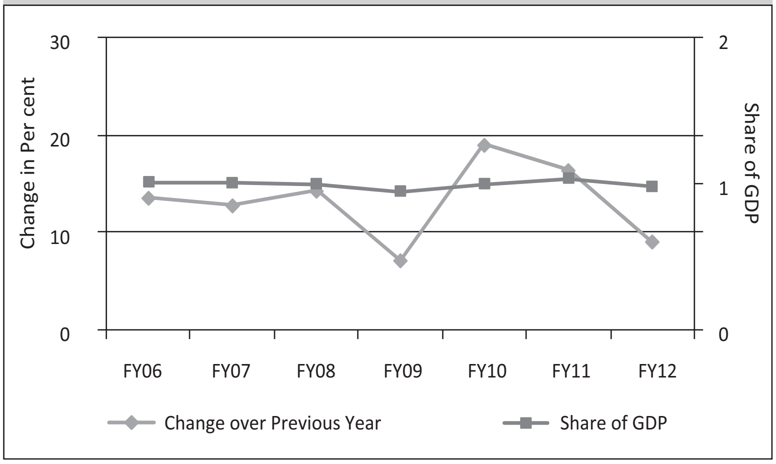
SOCIAL SECTOR

In view of the growth-poverty nexus in Bangladesh, the importance of strengthening various fiscal measures in social sectors can hardly be overemphasised. As is known, successive governments have tried to address this concern by way of allocating specific funds under the national budget every year. The budget for FY2011-12 has also continued with this endeavour. Such critically important sectors as health, education and social safety net, including food security and employment generation schemes have received significant allocations in the proposed budget. While some of the initiatives articulated in the budget appear to be supporting sustainable growth in these sectors, a large number of these measures are not complemented by the needed effective implementational modalities. This could undermine the expected outcomes.

2.5.1 Health

A total of Tk. 8,869 crore, accounting for about 5.4 per cent of the total budget has been allocated for the health sector in the national budget for FY2011-12. This is only about 1 per cent in terms of share in the GDP, and lower than that of the previous year in terms of year-on-year growth (Figure 2.6). Hence, it is doubtful that this allocation will be adequate to address the various health-related concerns in the country.

Figure 2.6
Allocation for Health in Various Years



Source: Budget Documents (various years), Ministry of Finance (MoF).

One important initiative proposed in this year's budget is the proposal to start a new phase of the *Health Nutrition and Population Sector Program (HNPSP)*. This new phase is to be implemented over the period of 2011 to 2016. From the perspective of attaining the health-related Millennium Development Goals (MDGs), this was indeed a welcome initiative. However, discontinuation of the *Micro-Nutrient Supplementation Programme* from social safety net somewhat contradicts the government's commitment to ensure nutrition for all. This could further aggravate the already weak prospect with regard to attaining the nutrition-related MDGs. Though the plan to employ alternative healthcare practitioners at district and upazila levels is a welcome initiative, budgetary implication of such measures is likely to surface as a concern. This was particularly relevant in view of the significant resources that would be needed for the development of necessary infrastructure and for providing salary to the concerned health personnel.

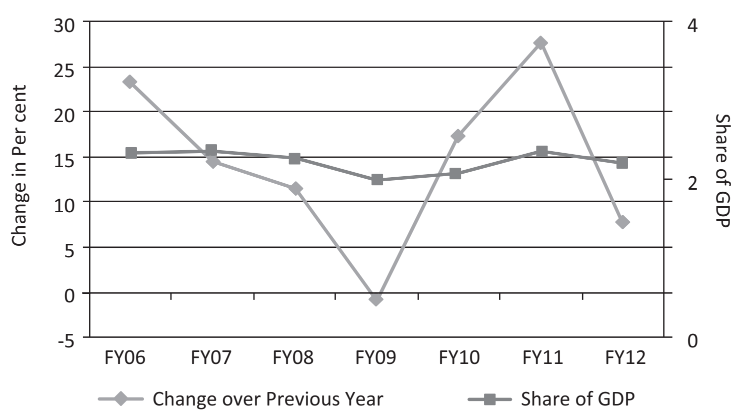
It is also somewhat disquieting that the budget for FY2011-12 did not address the issue of human resource scarcity in the Directorate of Drug Administration (DDA). Given the importance of this organisation in monitoring the quality control of the pharmaceutical and drugs production, as well as facilitating the export of pharmaceutical goods, there was a need to take a target-oriented policy initiative to strengthen this agency, with allocation of necessary funds.

2.5.2 Education

A major sub-sector in the social arena is education. Various line ministries under the education sub-sector has received a total allocation of Tk. 19,806 crore in the budget for FY2011-12 which is about 12.1 per cent of the total proposed budget for FY2011-12 and 2.2 per cent of the GDP (Figure 2.7). This allocation, however, is lower than the amount of the previous year. On a positive note, the budget has earmarked Tk. 1,000 crore for *Prime Minister's Education Assistance Foundation*, which is a commendable initiative. This proposed initiative should, however, be extended to post-graduate level, particularly for students coming from resource-poor families.

Figure 2.7

Allocation for Education in Various Years



Source: Budget Documents (various years), Ministry of Finance (MoF).

Amongst the other measures proposed in the budget speech, a laudable one has been the expansion of both coverage and allocation of additional funds for the *School Feeding Programme*. The decision to establish directorates of education at district level is a well thought out measure. However, no indication has been provided whether the existing education offices at district headquarters will be upgraded to the level of directorates.

The government has also proposed to initiate a *Talent Hunt* programme to identify bright minds to provide leadership in nation building in the 21st century. However, no allocation has been made for this purpose in the budget. There is no denying that implementation of such an endeavour will call for significant additional resources in many areas including setting up of institutions, delegation and development of human resources, etc. In addition to putting in place the above programme, the government has also proposed to revisit the entire Monthly Pay Order (MPO) system in the education sector. Though this is a bold step, the challenge will be to implement this without any undue partisan influence. On previous occasions, the MPO system has been criticised for nepotism and discrimination in institution selection process. It remains to be seen how the proposed reforms are carried out in the coming days.

2.5.3 Women Development

With a view to bring down gender-based discrimination and establish equal rights in all sectors of the economy, this year as well the government has continued with the tradition of preparing separate Gender Budgeting Report. This was the third consecutive year that the government has attempted to prepare a gender budget. The Gender Budgeting Report presented the gender disaggregated budget allocation and employment status for 20 ministries. In the previous year (FY2010-11), the gender reporting was presented for 10 ministries. Allocation for women's development has increased in 12 ministries and reduced in eight ministries in the budget for FY2011-12 when compared to FY2010-11. It is interesting to note that allocation for the Ministry of Women and Children Affairs is 0.76 per cent of the total budget for FY2011-12, which is 0.32 per cent lower than that of FY2010-11. It may be mentioned that the government has recently formulated the *National Women Development Policy 2011*. Clearly, the success of the women development policy will depend on adequate resources and their efficient utilisation. The budget for FY2011-12 has proposed a number of important measures towards women's development. Some of these are highlighted in Table 2.12.

Table 2.12

Some Commendable Programmes under Gender-Sensitive Budget

Measure	FY2010	FY2011	FY2012	Implications of FY2012 Budget
Gender equity expenditure	24.6 per cent of the total budget	25.9 per cent of the total budget	26.4 per cent of the total budget	Increase gender sensitivity by 2.3 per cent
Resource allocations for Gender Budget	Covering four ministries	Covering 10 ministries	Covering 20 ministries	10 more ministries reported; positive initiative
Women entrepreneur	Committed to ensure separate banking arrangements, loan and technical facilities	Directive has been issued to establish a 'Dedicated Desk for Women' in each bank and financial institutions for receiving easier loans	A programme has been introduced under PPP for marketing the products of women entrepreneurs	Name of the programme not mentioned
Daycare centres	No mention regarding this subject (18 daycare centres already exist increase in Dhaka city)	Decided to establish 10 more daycare centres (seven for lower income and three for middle income)	No new announcement for increase the number of the centres	Considering the increasing amount of working women, number of daycare centres should be increased

Source: Budget Documents for FY2009-10, FY2010-11 and FY2011-12, Ministry of Finance (MoF).

Some Other Measures

Creating Women-friendly Working Environment: Observing the demand at both local and foreign markets for female labour, in recent times a number of new training programmes have been initiated for women. These included housekeeping, mobile servicing and English language courses. The proposed budget for FY2011-12 also states that for promoting women entrepreneurship, a special marketing programme for products made by women entrepreneurs at the grassroots level has been initiated as part of PPP. This is a good initiative; however, there is no mention of the name or specific allocation, for this programme.

The share of ministry-wise gender equity expenditure in total budget has increased from 26.3 per cent to 26.4 per cent. The number of targeted beneficiaries for the scheme of *Maternity Allowances for Poor Working Mothers* has been proposed to be increased by 15 per cent for the rural areas and 15.8 per cent for the urban areas. The proposed total allocation for the scheme is Tk. 42.5 crore and Tk. 32.6 crore for rural and urban areas respectively. The increase in coverage and a separate budget allocation are positive initiative in support of working mothers; however, the allowance should be adjusted in view of the current inflationary pressure.

In the previous budget for FY2010-11, a decision had been taken to establish 10 more child daycare centres for lower income and middle income mothers. Of those, seven are already in operation and three centres are at the final stage of opening. In the proposed budget for FY2011-12, the government has decided to continue the programme 'well beyond its current remit' and does not mention establishment of any new centres. However, as the number of working women is increasing each year, the demand for daycare centres will be on the rise and there should be appropriate plans to cater to this rising demand.

Eliminating Violence against Women and Children: Total elimination of the violence against women and children is one of the declared priority concerns of the government. In line with this objective, the government has enacted relevant laws, i.e. *Family Violence (Prevention and Protection) Act 2010*. In the budget for FY2011-12, to support the existing laws and as part of the *Rehabilitation Programme for the Acid Burnt Women and Physically Disabled*, an amount of Tk. 11.95 crore is proposed to be allocated for social voluntary organisations under the Social Welfare Council. In addition with this initiative, for preventing the violence against women, National Forensic (DNA) Screening Laboratory with modern technology, which has already been established in six divisional medical colleges, is promised to be extended throughout the country from the year 2012.

Caring Maternal and Child Health: According to the available data from the Bangladesh Bureau of Statistics (BBS), the maternal mortality ratio per thousand live births is 3.37. That is why a significant reduction of the maternal and child mortality rate is one of the prime objectives of the government. Various projects have already been taken under ADP to improve maternal and child care. Moreover, two important programmes such as *Maternal Health Voucher Scheme* and *National Nutrition Sector Development Programme* have been included in the HNPSP from the FY2011-12, and an allocation of Tk. 271 crore is proposed to be allocated for this purpose.

Income Tax Limit: The income tax limit for individuals above 65 years and women has been raised from Tk. 180,000 to Tk. 200,000. This decision will hopefully benefit the cause of women entrepreneurship.

2.6

SOCIAL SAFETY NET PROGRAMME

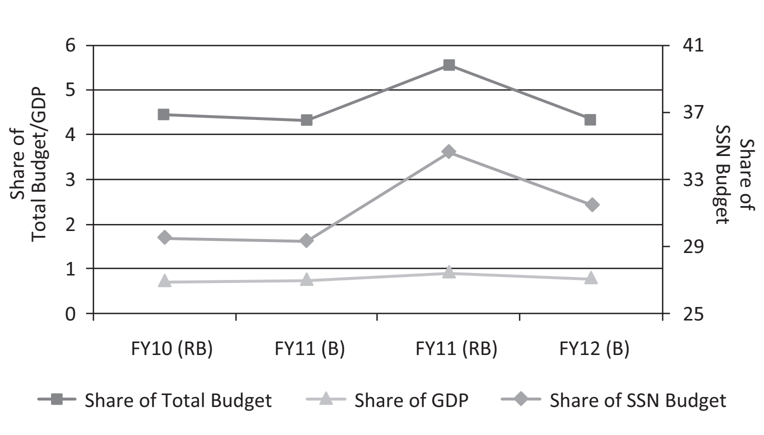
Social safety net programme is a protection shield for the poorest segments of the society against the threat of poverty. In the national budget for FY2011-12, this sector has received an allocation to the tune of Tk. 22,556 crore (13.8 per cent of total budget). The social safety net for this year includes 84 programmes; this excludes the five programmes which were discontinued though these were part of the previous budget of FY2010-11. Besides, two new programmes have been introduced in this year's budget. These are: *Universal Pension Scheme* and *Construction of Sweeper Colony*. Unfortunately, total number of beneficiaries for all the programmes under the safety net has come down by about 5 per cent (from 8.08 crore to 7.68 crore) in FY2011-12. Although the reduction in poverty levels may have induced this, it contradicts the declared commitment of the government to ensure social security for all. Increase in both allocation and coverage for various maternity allowances is, however, a commendable initiative.

It is discomforting to see that the budget for FY2011-12 has listed the programme titled *Vulnerable Group Development for Ultra Poor (Women)* twice in the document. Whilst in the first instance, under *Running Development Programmes* (D.1.18), there has been an allocation of Tk. 2.12 crore for FY2011-12; the same programme was once again listed under *New Development Programmes* (D.2.5) with an allocation of Tk. 121.93 crore. There is no clear indication whether these two programmes are different from one another. Apart from this, as in the previous budget, expansion of *Ghore Fera* programme has been announced without any allocation of earmarked funds. This raises question as to whether this programme will be actually implemented.

With regard to social safety net programmes to ensure food security for the poor and vulnerable community of the society, the budget for FY2011-12 has allocated Tk. 7,102.6

Figure 2.8

Share of Allocation for Food Security in Social Safety Net Programmes



Source: Budget Documents (various years), Ministry of Finance (MoF).
Note: SSN: Social safety net.

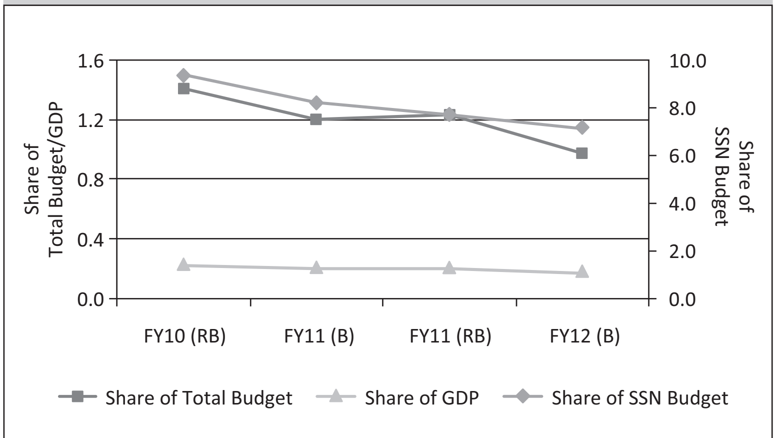
crore for various programmes. This amount is 4.3 per cent of the total budget, 31.5 per cent of the total social safety net budget, and 0.8 per cent as share of the GDP. It may be noted in this context that this year's allocation is on the lower side with respect to all the three indicators when compared to the revised budget for FY2010-11 (Figure 2.8).

Of particular concern in this context is the lower allocations for OMS and Food for Work (FFW), both of which would experience negative growth rates ((-) 16.3 per cent and (-) 1.4 per cent respectively), when proposed allocation for FY2011-12 is compared to the revised allocation for FY2010-11. It appears that this is a reflection of the government's understanding that there will be a fall in inflation and food prices in FY2011-12. If this does not come out to be so, effective benefits for the poor and the vulnerable will be lower than the last year.

Another key area in the social safety net programme is the Employment Generation Programmes for which the budget has allocated a total of Tk. 1,599 crore for FY2011-12. This total amount for the 11 programmes is less than 1 per cent of the total budget and less than 0.2 per cent as share of GDP for FY2011-12 (Figure 2.9).

Figure 2.9

Share of Allocation for Employment Generation Programmes



Source: Budget Documents (various years), Ministry of Finance (MoF).

Despite the increase in number of beneficiaries (from 54.9 lakh in the revised budget for FY2010-11 to 59.2 lakh in the proposed budget for FY2011-12), total allocation for the employment generation programmes is found to be about 0.4 per cent lower than that of the revised allocation for FY2010-11. In view of this, the question remains whether labour wage has decreased, or more small-scale projects are being taken up to implement these programmes. In either of the circumstances, the real income of per worker will be lower in FY2011-12. This certainly is not a desirable outcome, particularly since it is targeted towards benefit of the very poor people in the society. Hence, the government needs to look further into the matter and revise the allocations in this context.

2.7

CONCLUDING REMARKS

With regard to the implementation of the national budget for FY2011-12, the apprehension is that targets set out for non-ADP expenditure in the form of subsidy payments could overshoot. Revenue collection could be more than within the reach, but utilisation of foreign aid remains an area of nagging concern. Once again, full implementation of the ADP in quantitative and qualitative terms may fall short. The financing framework of budget deficit remains the key to reinstate the macroeconomic stability which has been the hallmark of Bangladesh in the recent past years. In its analysis, CPD has put forward four defining factors which will be critically important for a successful implementation of the budget for FY2011-12. *First* relates to the issue of financing of the budget deficit. While the flow of foreign aid has been low during the past few years, a number of large foreign-aided projects including the Padma Bridge have been earmarked for implementation in FY2011-12. Efforts to release foreign aid in the pipeline will need to be intensified. Ensuring good governance in the entire spectrum of activities in connection with the building of the Bridge will be crucial in this context. Government should also try to seek alternative sources of foreign aid in the form of grant and budgetary support to reduce the likely pressure on domestic credit market. *Second* is the maintenance of the macroeconomic balance. Prudent management of monetary and fiscal sectors will be necessary so that implementation of ADP can be ensured without crowding out the private sector. Adjustment of interest rate and management of exchange rate will also be necessary. *Third* concerns institutional strengthening. Strengthening of institutions that deal with development praxis will be critically important for effective management of the development administration. It will be essential to invest in development of the required human resources and capacity building, and raise the efficacy of all ministries and institutions related to ADP and budgetary implementation. In view of the increasing size of the ADP in recent years, this has acquired added importance. The *fourth* relates to the importance of maintaining political stability. A conducive political environment will be necessary to ensure that the budgetary proposals are implemented with efficacy and effectiveness.

3 CHAPTER

Monetary Policy Statement of January-June 2011

A Critical Appreciation

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This chapter was originally presented at a CPD organised dialogue titled *Growth, Inflation and Monetary Policy: Challenges for Bangladesh in FY2010-11* on 13 February 2011, at the CIRDAP Auditorium, Dhaka.

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3.1

INTRODUCTION

The macroeconomic scenario of Bangladesh has been undergoing significant changes in FY2010-11. A number of developments – related to both domestic and global economy – have led to presence of perceptible tensions in key macroeconomic balances. These strains are showing up in wide ranging areas including revenue mobilisation, implementation of public investment programmes, management of fiscal deficit, inflationary trends, conduct of the capital market, import growth, remittance inflow, foreign aid offtake, foreign direct investment (FDI) and balance of payments (BOP) status. A number of structural impediments – e.g. continued crisis in gas and electricity supply, are further aggravating the investment climate. The above mentioned trends have the potential to not only undercut the macroeconomic stability, but also weaken the growth prospect in FY2010-11. At the same time, the commitments that the government will likely make to access the International Monetary Fund's (IMF) credit, will have implications for policy contours. The recently announced Monetary Policy Statement (MPS) by Bangladesh Bank, announced on 30 January 2011, lays out some of the changes in the anticipated policy framework. Thus, it is reckoned that a serious revisit of the policy framework is necessary for ensuring macroeconomic management to confront the visible and emerging realities. This has become particularly important as the government positions itself for the preparation of the upcoming budget and the soon-to-be finalised Sixth Five-Year Plan (SFYP).

Taking note of the significantly changed economic backdrop and using the recently announced MPS as a policy reference point, Section 3.2 of this chapter seeks to highlight the nature of the macroeconomic challenges that the economy is going to experience in the near future. In Section 3.3, the study reviews the recent MPS to explore to what extent the policy stance is adequate in terms of addressing the emergent challenges, while Section 3.4 articulates the challenges for monetary policy in FY2010-11. The penultimate section discusses the outlook for economic growth in view of the present macroeconomic challenges and proposed policy framework. The chapter rounds up with a few closing observations.

3.2

EMERGING ISSUES IN THE MACROECONOMIC FRAMEWORK

3.2.1 Fiscal Balance

The FY2010-11 will be marked as a period, charecterised by significant rise in government revenue expenditure in the backdrop of rising commodity prices and higher than projected subsidy requirement. On the other hand, slow pace of implementation of the Annual Development Programme (ADP) will likely help the government, in a rather perverse way, to arrest the widening of the fiscal deficit. ADP implementation remained low in the first half of FY2010-11, particularly its component concerning foreign-funded projects. Only 27 per cent of an ambitious ADP of Tk. 38,500 crore has been implemented in the first six months of FY2010-11, while the implementation rate was 29 per cent in the reported period of FY2009-10. Expenditure of local fund (Taka) was 32 per cent[1] of

[1]Share of domestic resources in ADP is 60 per cent.

Table 3.1

ADP Implementation of Top 10 Ministries/Divisions during FY2010-11 (July-December)

(in Per cent)

Division/Ministry	Share of Allocation FY2011	Expenditure FY2011 (Jul-Dec)	Local Fund Expenditure FY2011 (Jul-Dec)	Project Aid Expenditure FY2011 (Jul-Dec)
Local Government Division	21.0	35.0	46.0	17.0
Power Division	13.0	18.0	17.0	20.0
Health and Family Welfare	9.0	23.0	21.0	25.0
Roads and Rail Division	9.0	19.0	25.0	9.0
Primary and Mass Education	8.0	41.0	46.0	33.0
Education	4.0	32.0	47.0	14.0
Water Resources	4.0	15.0	14.0	17.0
Bridge Division	3.0	6.0	14.0	3.0
Agriculture	3.0	31.0	32.0	24.0
Energy and Mineral Resources Division	2.0	15.0	13.0	25.0
Total ADP	100.0	27.0	32.0	18.0

Source: Authors' estimation from the Implementation Monitoring and Evaluation Division (IMED) data.

allocation, whereas only 18 per cent of project aid fund was implemented (Table 3.1). Failure of line ministries to negotiate, schedule, execute development schemes, and delays in pre-investigation on the part of the donor agencies, especially in case of foreign-funded projects, may be mentioned as reasons for this dismal performance. Lack of implementation of foreign-funded projects has also resulted in low foreign aid disbursement. This has not been very helpful in the backdrop of the tight BOP situation. Considering this implementation status, the Planning Commission is expected to lower the project aid budget by Tk. 3,000 crore to Tk. 12,300 crore, and at the same time bring down the total ADP allocation by the same amount. Thus, it is expected that at the end of the year, shortfall in ADP implementation would leave the total expenditure figure more or less unchanged despite a large upward revision of non-ADP expenditure.

It is encouraging to note that, the National Board of Revenue (NBR) is expected to exceed its stipulated target; however, the target for the overall revenue mobilisation may fall short. During the first half of FY2010-11, NBR achieved a significant 22.7 per cent growth, thanks mainly to the domestic sources of revenue (Table 3.2). On the other hand non-NBR tax and non-tax heads of revenue earnings are not likely to achieve their targets. The growth rate for non-NBR tax was to the tune of 8.3 per cent in the first quarter of FY2010-11 against an annual growth target of 25.8 per cent. Performance of non-tax revenue sources was rather dismal. Revenue collection from these sources declined by (-) 26.3 per cent against the formidable annual growth target of 27.4 per cent set for FY2010-11. In view of such sustained below-average mobilisation from non-NBR sources, NBR will need to continue with the current robust growth trend to compensate for the likely shortfall in the non-NBR component.

Table 3.2

NBR Revenue Growth

(in Per cent)

Indicator	Target FY2011	Growth FY2011 (Jul-Dec)	Achieved FY2010 (Jul-Dec)	Required FY2011 (Jan-Jun)
Customs Duty	14.2	13.4	4.3	14.9
VAT	12.9	28.6	19.8	0.3
Income Tax	22.9	34.0	21.6	17.0
Others	20.5	5.7	22.8	33.5
Grand Total	17.1	22.7	17.8	12.9

Source: Authors' estimation from the National Board of Revenue (NBR) data.
Note: VAT: Value added tax.

The size of the budget deficit itself should not be a matter of serious concern in FY2010-11. Rather it will be argued here that the composition of deficit financing could become a matter of debate and judicious choice. The overall budget deficit (excluding foreign grants) was 1.5 per cent of the gross domestic product (GDP) at the end of first quarter of FY2010-11 and remained well within the programmed limit (5 per cent of GDP) (Table 3.3). It appears that during the early months of FY2010-11, the government has mostly relied on domestic sources rather than foreign

Table 3.3

Financing of Budget Deficit in FY2009-10 and FY2010-11 (as Per cent of Total Deficit)

Source	FY2010	FY2011 (B)	FY2010 (Q1)	FY2011 (Q1)
Net Foreign Financing	47.5	39.8	92.6	31.8
Grant	19.0	12.2	80.8	27.0
Loan	49.8	40.6	73.5	40.5
Amortisation	21.3	13.1	61.7	35.7
Domestic Financing	52.5	60.2	7.4	68.2
Non-Bank Borrowing (net)	61.8	20.3	173.5	41.4
Bank Borrowing (net)	-9.3	39.9	-166.1	26.8
Total Financing as % GDP	3.3	5.0	0.9	1.5

Source: Authors' estimation from the Ministry of Finance (MoF) data.
Note: B denotes Budget; Q1 refers to the first quarter (July-September period) of the corresponding fiscal year.

financing and will likely continue to do so in near future. In making use of domestic resources for financing of the fiscal deficit, bank borrowing is expected to play a leading role when compared with the last fiscal.

In all likelihood the budget deficit is going to rise in the coming months as a result of the anticipated higher public expenditure requirements, including ADP implementation requirements, and more importantly, due to inflation resulting from food price hike. High level of oil prices[2] in the international market may call for more subsidy demand during the rest period of the fiscal year.[3] Thus the monetary policy may be required to play, over the remaining part of FY2010-11, a more proactive role to accommodate the envisaged public expenditure.

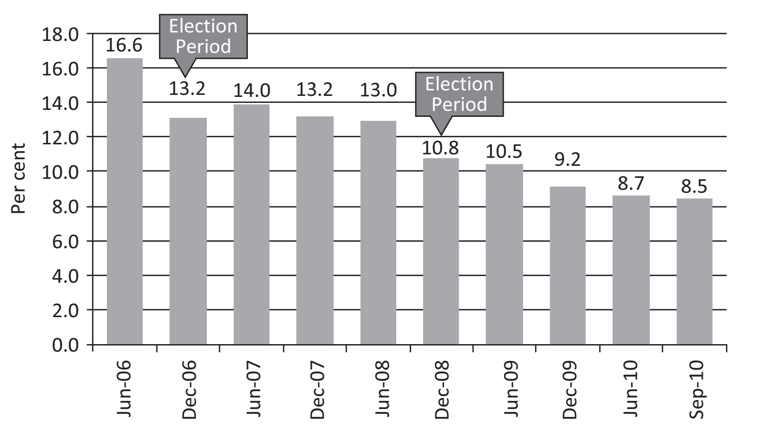
3.2.2 Financial Institutions

Financial sector in Bangladesh has been growing in tandem with the growth of the economy. 2010 has been a year of good profit for private commercial banks (PCBs), thanks to growing international trading activities and gains reaped from capital market. However, governance of financial sector came under scrutiny during the noted period. Evidence tends to suggest that credit in the form of industrial term loan, working capital and overdraft against workers' salary were diverted to the capital market.

Failure to address the issue of non-performing loans (NPLs) also led the financial sector under close scrutiny in recent times. The main reasons include higher flow of loans to unproductive sectors and risky exposure to capital market. Total classified loan at the end of first quarter of FY2010-11 (September 2010) stood at Tk. 8,978.2 crore (8.5 per cent of the total outstanding loan). This figure is 5.7 per cent lower than the corresponding figure of June end 2010. PCBs were able to limit their classified loan both in terms of total amount and with respect to the corresponding quarter of the previous fiscal. However, the overall recovery of default loans remained poor in case of the state-owned commercial banks (SCBs). A recent media report[4] informs that SCBs were able to recover only 12 per cent of the targeted Tk. 388 crore of bad debt from top 20 of their listed defaulters in 2010. More over, another media report quoted[5] an official from the Finance Division that two SCBs bought 25 bad loan cases from PCBs. Interestingly, it was found that only during the election period the recovery of NPL had been successful (Figure 3.1).

Figure 3.1

Percentage Share of Non-Performing Loan to Total Outstanding



Source: Authors' estimation from the Bangladesh Bank data.

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[2]International oil price, which is currently hovering around USD 100 per barrel, is expected to remain at a high level in the near future.

[3]The Finance Division has already estimated a higher demand for subsidy (an additional Tk. 3,200 crore) for energy, power and agriculture in view of the escalating global commodity prices.

[4]http://www.thedailystar.net/newDesign/news-details.php?nid=167412

[5]http://www.thedailystar.net/newDesign/news-details.php?nid=171651

3.2.3 Inflation and Price Trend

Successive monetary policies in Bangladesh in general were designed with a view to facilitate growth acceleration without losing the focus on containing inflationary expectations. No wonder, the ongoing inflationary pressure[6] has drawn considerable attention from the monetary authority when the recent monetary policy stance was formulated. *World Economic Outlook 2010 (October)* forecasted that commodity prices in advanced countries will remain at a high level in 2011. However, inflation in developing countries may ease to some extent, from 6.2 per cent in 2010 to 5.2 per cent in 2011 (IMF 2010). In spite of this, current global and national trends indicate that Bangladesh is not expected to experience any respite from the inflationary pressure at least in the short-run.

Evidence found in the academic literature concerning inflation in Bangladesh appears to be divided as far as determinants of inflation were concerned. Structuralists would argue that bottlenecks in the agriculture sector and the continuing BOP deficits were able to explain the rise in the price level. On the other hand, monetarists would claim that the persistence of inflation is the result of an exogenous expansionary monetary policy. Taslim (1982) found that neither the monetarist theory nor the structuralist theory alone is able to adequately explain the inflationary phenomenon in Bangladesh.

A number of studies concerning identification of the determinants of inflation in Bangladesh indicate that monetary aggregates have significant impact on inflation (Mortaza 2006; Majumdar 2006). Hossain (2007) also found that money supply tends to have a significant positive impact on inflationary trend, while devaluation of currency was found to have insignificant influence on inflation in Bangladesh. Osmani (2007), on the other hand, argued that exchange rate can have an influence on the inflation rate. Besides, inward remittances, government debt, inflation inertia, and food and oil prices are also found to be important determining factors driving inflation in the Bangladesh context (Ahmed n.d.). CPD (2011) found clear evidence of a positive relationship between inflation and foreign exchange reserve and domestic petroleum price. The study also found that inflation is negatively related to domestic rice production, while the relationship between money supply and inflation was found to be positive, but insignificant.

It can be argued that the current developments in the inflationary front in Bangladesh is not similar to the historical trend, and that econometric analysis using long-term time series data may not be adequate to explain current inflationary developments. In fact, the nature of current inflation is very similar to the one experienced by Bangladesh in 2007 and 2008, when inflationary trend was led by the food inflation. One can readily observe that the ongoing inflationary trend is also informed by some of these characteristics. Price hike in the global market has caught up with most of the countries in the world including Bangladesh. Bangladesh, being a small open economy, has experienced the influence of world prices for most of her daily essential commodities, even when particular commodities have not been predominantly dependent on imports. It has been seen that international oil price often dictates the overall inflation scenario to a large extent. The international price of oil has increased by 22.3 per cent in January 2011. Global Commodity Price Index maintained by the IMF also indicates a steady rise in global prices. The year-on-year growth in IMF's Commodity Price Index and Food Commodity Price Index in December 2010 stood at 23.4 per cent and 26.8 per cent respectively. One will need to consider that the level of inflation in Bangladesh has been lower compared to her other neighbours except for Sri Lanka. It is often stated that the inflation of Indian economy has a more pronounced and direct influence on commodity prices in Bangladesh. India has experienced a higher growth of inflation in recent years. However, this was the case in the

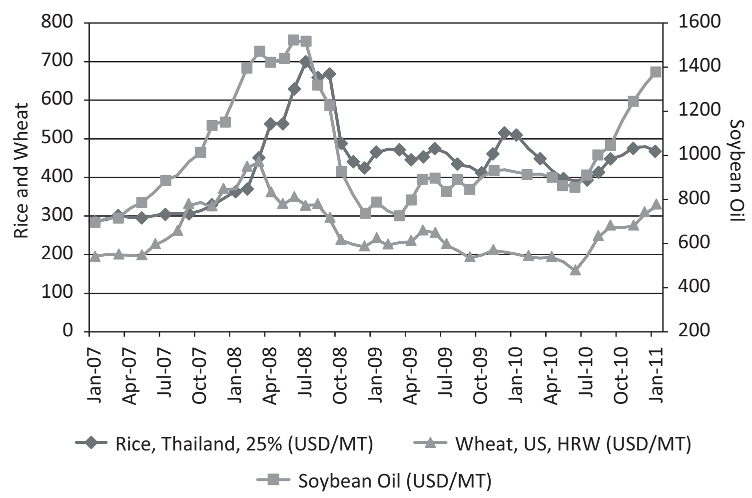
[6] In December 2010, average inflation was 8.1 per cent.

backdrop of higher pace of growth. On the other hand, Sri Lanka, with a lower growth rate of 3.5 per cent in 2010, had experienced a lower inflation rate. Pakistan has been a typical case of a conflict economy that had a higher inflation rate but a lower growth rate.

One may also argue that the overall inflation at present is driven by food inflation. In December 2010, the food inflation was 11 per cent whereas the non-food inflation was only 3.3 per cent. In fact the present non-food inflation is the lowest in last nine years! Given this, demand-side management can hardly work in view of the inelastic nature of demand for food items. Food inflation around the world is also on the rise. FAO Food Price Index has been increasing for the seventh consecutive month. The World Bank data suggests that international prices of rice, wheat and soybean oil increased in January 2011 by 16.2 per cent, 51.7 per cent and 37.9 per cent respectively, and heading towards the historical peaks of mid-2008 (Figure 3.2).

Figure 3.2

International Commodity Prices



Source: Authors' compilation from the Pink Sheet, World Bank.

At that point (mid-2008), Rahman *et al*. (2008) explained that the inflation was driven by significant rise in the international commodity prices besides supply-side constraints, as well as distortions in the domestic supply chain. Role of non-competitive market (syndication) behaviour is a much-discussed topic which is perceived to have aggravated the inflationary situation in Bangladesh (Rahman *et al*. 2008). Ahmed (n.d.) and Majumdar (2006) identified this as a major determining factor behind the high inflation in Bangladesh. However, Osmani (2007) did not observe any significant evidence of this variable in his study. There is no denying the fact that information asymmetry, lack of infrastructure and weak institutional capacity are key factors that limit the growth prospects of the Bangladesh economy. There is no short-cut solution to these issues. These will need to be addressed head on by facilitating information flows, through strategic market interventions and instituting effective market (global and domestic) monitoring mechanisms.

In recent times doubts have been raised with regard to supply and demand situation of foodgrains in the country. There is also a debate with regard to the figure of population in Bangladesh. CPD (2011) found that during the last few years domestic food production exceeded the demand for food in the country. It is thus surprising to find that even after a comfortable level of per capita food availability, rice prices have been constantly on the rise even during the paddy-harvesting season. The lower public stock of foodgrain is also not transmitting the right signal to the market. As is known, government was not able to meet its procurement target during the last Boro season. The government has decided not to procure Aman rice in the current season, instead plans to procure foodgrains from the international market. Rice imported from the global market will have to be procured at higher prices, and hence, government may have to continue to sell the foodgrains in the open market at a subsidised rate.

3.2.4 Balance of Payments

Decelerated remittance receipts and swelling import payments had put pressure on the BOP situation in FY2010-11 despite a relatively broad-based export growth. In the

Table 3.4
Export Growth

(in Per cent)

Product	Target FY2011	Growth FY2011 (Jul-Jan)	Growth FY2010 (Jul-Jan)	Required Growth FY2011 (Feb-Jun)
RMG	10.0	41.3	-6.9	-26.1
Knitwear	*10.0*	*43.2*	*-6.9*	*-30.0*
Woven wear	*10.0*	*39.1*	*-7.0*	*-22.1*
Non-RMG	28.2	35.1	4.1	19.9
Raw jute	*30.0*	*91.8*	*39.6*	*-52.5*
Leather	*30.0*	*29.9*	*-0.8*	*30.1*
Total	14.2	39.8	-4.6	-15.7

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

Table 3.5
Balance of Payments

(Million USD)

Items	FY2010 (July-November)	FY2011 (July-November)
Trade Balance	-1976	-2752
Export FOB (including EPZ)	6107	8299
Import FOB (including EPZ)	-8083	-11051
Services	-653	-978
Receipts	777	1024
Payments	-1430	-2002
Income	-601	-547
Receipts	16	44
Payments	-617	-591
Of which: Official interest payments	*-81*	*-87*
Current Transfers	4904	4840
Official transfers	9	44
Private transfers	4695	4796
Of which: Workers' remittances	*4659*	*4581*
Current Account Balance	1674	563
Capital Account	114	125
Financial Account	890	-873
FDI (net)	285	320
Portfolio investment	-34	56
Other investments	639	-1249
Errors and Omissions	-522	-399
Overall Balance	2156	-584

Source: Bangladesh Bank data.
Note: FOB: Free on board; EPZ: Export processing zone.

backdrop of the low export growth in FY2009-10, export was able to turn back during the early months of FY2010-11 and registered a robust 39.8 per cent growth in the first seven months. Readymade garments (RMG) export growth during this period was an impressive 41.3 per cent, while non-RMG exports posted a 35.1 per cent growth (Table 3.4).[7]

However, increased demand of import in the first five months of FY2010-11 (with a growth of 36.7 per cent) underwritten by the augmented demand for raw materials for export, industrial investment, and food price hike were the reasons that made trade balance situation uncomfortable during this period. A sluggish remittance inflow[8] could not help maintain the current account surplus that Bangladesh had enjoyed over the last five fiscal years. Current account surplus came down to USD 563 million during the first five months of FY2010-11 while the overall balance turned negative in the concerned period of FY2010-11 (Table 3.5). Stagnating net FDI[9] and low inflow of foreign aid[10] have also put further strains on the BOP position of Bangladesh. A further widening deficit may become evident by the end of the fiscal year if the current trends continue.

The relatively high foreign exchange reserves could provide some cushion against any sudden fall in foreign exchange earnings or rise in foreign exchange demand. Foreign exchange reserves stood at USD 10.4 billion at the end of January 2011, which was equivalent to payment of 4.2 months of import. This level of foreign exchange reserve does allow Bangladesh to maintain stability of the exchange rate and to cope with larger BOP deficit in the short-run.

The stability of exchange rate is also important from the perspective of balancing the tension between inflationary targets and export competitiveness. Historic trends indicate that the exchange rate of Bangladeshi Taka (BDT) against the United States Dollar (USD) has been somewhat stable over the last couple of years, but BDT is now showing some tendency to depreciate. Between end of June 2010 and end of January 2011, BDT depreciated against USD and Euro by 2.2 per cent and 11.8 per cent respectively. This has certainly helped export competitiveness of Bangladesh and provided inducement for

[7]However, given the slow pace of global recovery coupled with the lagged impact of the global economic crisis, the targets for RMG (both knit and woven) were set on a conservative mode.
[8]Remittance inflow increased by only 0.4 per cent in July-January, FY2010-11.
[9]Net FDI flow was USD 320 million in July-November, FY2010-11 against USD 285 million in July-November, FY2009-10.
[10]Foreign aid was USD 818.5 million in July-December, FY2010-11 against USD 1,481 million in July-December, FY2009-10.

higher remittance flows. However, BDT has also depreciated against Indian Rupee (INR) and Chinese Yuan (CNY) by 3.9 per cent and 5.7 per cent respectively during this period. This would put some pressure on prices of imported consumer goods as well as intermediate and capital goods. Thus, in view of ongoing global developments, there is a need to remain constantly vigilant regarding the exchange rate movements.

3.3

A DECONSTRUCTION OF THE RECENT MONETARY POLICY STATEMENT

In past, monetary policy was aimed to provide directions to the behaviour of various macroeconomic variables and the policy instruments. These instruments include the volume and direction of credit and the interest rates. At the same time, administrative import allocations were also kept under investigation in order to ration excess demand for foreign exchange. As may be recalled, in mid-2003 the currency peg mechanism was abandoned by introducing the managed floating exchange rate. At present, the monetary policy framework includes the near-term outlook for domestic demand, external trade, inflation and exchange rate stability. Basically Bangladesh Bank formulates MPS by targeting several monetary aggregates in addition to core macroeconomic variables including inflation and economic growth. Bangladesh Bank puts greater reliance on monetary targeting by focusing on the reserve money, and thus via the money multiplier, on the broad money (M2).

The most frequently used instruments to control money supply and credit by Bangladesh Bank include Repurchase (Repo) and Reverse Repo, and outright transactions in government securities (in the form of open market operations). Repo and Reverse Repo instruments were introduced by Bangladesh Bank in 2003 to streamline the liquidity management, and as tools to control money supply more effectively. Other institutional instruments that Bangladesh Bank make use of include directed credit, administered interest rates and policy rates. During the early 1990s, Bangladesh Bank frequently changed the Cash Reserve Ratio (CRR), Statutory Liquidity Ratio (SLR) and the Bank Rate, and used other instruments prior to implementing the financial sector reforms (Bhattacharya and Khan 2010). Later, CRR and SLR were considered as more effective medium-term policy instruments. Recently, the Central Bank changed these policy rates in the backdrop of high level of excess liquidity (Table 3.6).

Table 3.6

Status of Monetary Policy Instruments

Instrument	Current Rate (%)	Last Rate Changed
CRR	6.0	Increased from 5 per cent to 5.5 per cent in May 2010 and again in December 2010
SLR	19.0	Increased from 18 per cent to 18.5 per cent in May 2010 and again in December 2010
Repo	5.5	Increased from 4.5 per cent in August 2010
Reverse Repo	3.5	Increased from 2.5 per cent in August 2010

Source: Compiled by the authors.

3.3.1 Trends in Monetary Aggregates: Targets and Achievements

Bangladesh Bank's targets for monetary aggregates have systematically failed to match the actual outcomes. The targets set for FY2010-11 are also unlikely to be close to reality. For example, the target for money supply growth has been set at 15.2 per cent (Table 3.7). The target can be regarded rather conservative in the context of expanded monetisation in the economy; this was also significantly lower than last year's growth rate of 22.4 per cent. As a matter of fact, the average growth rate of broad money supply during the last five years was 19.1 per cent. Similarly, the targets for the components of money supply

Table 3.7

Targets and Achievements of Monetary Indicators

(in Per cent)

Indicator	FY2009		FY2010		FY2011	
	Target	Actual	Target	Actual	Target	Nov 2010 over Nov 2009
Net Foreign Assets	14.3	27.2	27.9	41.3	4.2	10.8
Net Domestic Assets	18.1	17.8	13.1	18.8	17.6	24.9
Domestic credit	20.4	15.9	15.6	17.9	17.9	24.2
Credit to public sector	27.3	20.3	11.9	-1.7	25.3	9.6
Credit to central government	-	23.2	13.8	-6.5	-	-
Credit to other public sectors	-	4.5	0.0	21.1	-	-
Credit to private sector	18.5	14.6	16.7	24.2	16.0	27.8
Broad Money Supply	17.5	19.2	15.5	22.4	15.2	22.2

Source: Compiled from the Bangladesh Bank data.

were also found to diverge widely when compared to the actual outcomes. This once again puts into question the approach of targeting the monetary aggregates pursued by the Central Bank.

Targeting the monetary aggregates reduces uncertainty and ensures transparency in policy making (Crockett 2004; Lindsey and Wallich 1989). Bhattacharya and Khan (2010) argued that in Bangladesh the Central Bank practices targeting the aggregate money supply while its components are distributed accordingly. However, Ramey and Ramey (1995) argued that it would be more efficient to target the components to achieve objectives and let the aggregate adjust automatically. Taslim (2010) argued that failure of central banks to contain the monetary aggregates within their target bands is not unusual. And hence, many of the central banks in developed countries have abandoned the policy of monetary aggregates targeting.

Rebound of export-oriented industrial production coupled with higher demand for import-oriented trade credit is expected to lead to high level of private sector credit demand in the course of the current fiscal year. A surge of government sector credit (i.e. for subsidy, ADP expenditure acceleration, import bills, etc.) is also already anticipated for the later half of FY2010-11. As a result, other than credit to government sector, all other monetary aggregates are likely to surpass respective targets set for the end of the current fiscal year. A revision of the monetary targets was thus expected from the recent MPS. It was somewhat surprising to observe that Bangladesh Bank did not rationalise the growth target for private sector credit flow in view of the growth record actually attained till December 2011.

3.3.2 Policy Stance for Second Half of FY2010-11

The MPS for the second half of the FY2010-11 (Bangladesh Bank 2011) indicates that Bangladesh Bank has programmed the monetary aggregates to accommodate 6.7 per cent GDP growth with 7 per cent inflation. Reviewing the MPS, one may highlight the following policy stances:

- Bangladesh Bank's monetary policies in the second half of FY2010-11 vowed to support growth and preserve price stability simultaneously.
- The Central Bank conceded that monetary policy had insignificant impact on inflationary trends and domestic food price inflation. Fiscal initiative in the form of subsidised foodgrain sales may be needed in order to ease hardship suffered by low-income earners.

- In view of the apprehension of possible adverse impact of monetary expansion, in line with growth in the real economy, the policy emphasised on keeping the non-food Consumer Price Index (CPI) inflation low and stable. It was, however, surprising to see that the Central Bank did not take cognisance of the fact that non-food inflation is already at its lowest.
- The Central Bank also admitted that the industrial and SME (small and medium enterprise) loans were being diverted to the overheated asset markets. At the same time, the policy expressed its belief that it would be able to bring back the discipline in financial sector by enforcing "*a firmer grip on monetary expansion*."
- The MPS also mentioned that:
  "Supervisory vigil on lending and loan administration discipline in banks will remain stricter, lapses and laxities in lending banks will be dealt with sternly, eschewing forbearance" (Bangladesh Bank 2011).

3.4

CHALLENGES FOR MONETARY POLICY IN FY2010-11

Servicing the Credit Demand

A major task of the central bank is to service and regulate the credit demand of the government and the private sector. In Bangladesh the Central Bank in general tries to accommodate all credit needs of the government as is needed. On the other hand, to stabilise the exchange rate, the growth of net foreign assets in M2 is largely determined by the BOP situation. If we recall the experience of last two fiscal years, one would find that the Central Bank allowed the growth of net foreign assets to surpass beyond the projected level. For FY2010-11, the falling current account balance has kept the growth of net foreign assets in control. However, it is expected that there will be a surge in government credit demand during the second half of the fiscal year. This would mean that restraining the growth of private sector credit remains the only avenue to reduce the monetary growth. The MPS has also stated its intention to have a firm grip on private sector credit. It is evident that industrial loan and SME loan have been diverted to the non-productive sectors (capital market and asset market). However, it will be difficult to stop this ill-practice by constraining the credit flow. As of September 2010, the overall growth in bank advances stood at 25 per cent, whereas growth figure for construction (including real estate activities) and flat purchase were 30.4 per cent and 63.7 per cent respectively. Credit for import financing of food and petroleum products has also increased by around 70 per cent during the reported period. The Central Bank repeatedly indicated its willingness to restrict credit for consumer loans, and direct it towards growth-friendly productive sectors. An active supervision will be required to achieve this goal. The Central Bank also ought to be flexible to service the productive private sector as well as the government.

Limited Role of Monetary Authority in Response to Inflation

In view of the soaring commodity prices the Central Bank has revised its inflation target from 6.5 per cent to 7 per cent for FY2010-11. As is mentioned, the present inflationary phenomenon is largely driven by external and structural forces. The MPS also realised that: *"monetary policy actions will have little leverage on rising food prices. In view of this situation, fiscal measures by way of subsidised foodgrain sales from public stock may need to be expanded to ease the hardships faced by low-income population segments."*

However, in contradiction, the Central Bank also aimed to control monetary expansion to control inflation. The Bank has cited similar moves by the neighbouring countries such as India. However, one should also consider that India revised its policy rates in response to the crisis.

It is also pertinent to mention here that monetary expansion is largely related to the non-food inflation rather than food inflation owing to the inelastic nature of food items. Since the non-food inflation is already at its historical low, the possible contradiction may result in adverse supply-side response to aggravate inflationary pressure. It may also have further adverse implications for growth and employment in the long-term.

Interest Rate is Set to Increase

High lending rate remains one of the major impediments to investment in Bangladesh. The Central Bank, in the face of global crisis, introduced a cap for industrial credit of 13 per cent with a view to revitalise investment. Following IMF conditionality, the Central Bank indicated its intention to phase out the cap on interest in near-term future. One can recall that this provision was introduced at a time when there was a high level of excess liquidity. The commercial banks, at that time, had responded by lowering the interest rate on deposits. The money market situation has changed in recent times – the level of excess liquidity is coming down due to higher demand for credit and subsequent upward revision of policy rates. Commercial banks have been forced to increase the interest rate to attract deposits. Banks are also expecting to increase their interest rates on lending. However, the issue, regrettably, was not mentioned in the most recent MPS.

Exchange Rate Management will be under Scrutiny

In view of growing pressure on BOP, after two years of stability, BDT started to depreciate against USD along with other major currencies. BDT is expected to depreciate further in the coming days. The volatility in the global currency market has started to put pressure on developing economies including Bangladesh. The MPS mentioned that net selling of USD by Bangladesh Bank stood at about USD 84 million during the first half of FY2010-11 to arrest further depreciation of the Taka. In the current context, a prudent exchange rate management will be required to ensure competitiveness of the export-oriented sectors without undermining the interests of consumer's welfare. Bangladesh Bank has to play a more proactive role in managing foreign exchange reserves, and decide as to how far it can use the reserves to maintain a balance between the aforementioned conflicting interests.

Role of Financial Institution in Capital Market

The capital market in Bangladesh has been the centre of attention for some time now given the recent volatility and the consequent developments in the market. Since 2006, capital market related indicators, e.g. price index, trade volume and market capitalisation, have registered significant rise. As a result a large number of small investors entered the market with a view to making lucrative short-term capital gains. CPD (2011) noted that lack of investment opportunities in the productive sector and huge inflow of new investors to participate in the *Keynesian Beauty Contest*, have been the major reasons driving such behaviour. The volatility in the capital market and the possibility of market manipulation is now under the scrutiny of the recently formed Probe Committee.

The role of financial institutions, particularly of the commercial banks, has been criticised in connection with the volatility seen in the capital market in recent times. The Finance Minister has also asked that the commercial banks' involvement in capital market be reduced. According to *Bank Company Act 26(2)*, a commercial bank is not allowed to invest more than 10 per cent of their deposits in the stock market. A total of 12 commercial banks have been identified by Bangladesh Bank which have violated this rule. Credits in the form of industrial term loan, working capital and over-draft against workers' salary are reported to have been diverted to the capital market. Some have suggested that the role of Central Bank should also be examined when capital market scrutiny is carried out. In the latest MPS, the Central Bank has tried to defend itself by arguing that the recent volatility was not a result of monetary contraction pursued by it. However, the role of Central Bank as a supervisory body of all financial institutions needs to be revisited in view of the emergent situation.

Addressing Non-Performing Loans

As is well-known, significantly large amount of NPLs have been afflicting the financial sector of Bangladesh for a long time. Given the debate with regard to the high cost of borrowing, it was expected that the MPS would provide some policy guidelines about dealing with the existing bad debt overhang. This issue is also important for the financial sector from perspective of implementing the Basel II.

Integrating Microfinance

While not being a part of mainstream monetary sector, microfinance has been a major supplier of credit to the private sector, particularly in the rural economy. At the end of FY2009-10, total outstanding microcredit from top five microfinance institutions (MFIs) was about 5 per cent of the total credit to private sector (private sector plus microfinance), and 2.2 per cent of GDP. Even though the MFIs are regulated by a separate authority, it is time that microfinance variables are integrated in monetary aggregates. In fact this would also help the policymakers who have indicated their intention to mainstream and regulate microfinance. Regrettably, the MPS, which demonstrated high level of sensitivity to financing the rural poor, opted not to integrate the issues relating to microfinance within its policy framework.

Impact of IMF's Extended Credit Facility (ECF) of USD 1 Billion

A credit deal, equivalent to about USD 1 billion, for the next three years (FY2012-14) between Bangladesh Bank and IMF is being finalised at the moment. The loan under IMF's Extended Credit Facility (ECF) arrangement is expected to get the nod soon. Since the termination of the Poverty Reduction and Growth Facility (PRGF) arrangement in 2007, this will be the first time that Bangladesh is opting for an IMF programme. According to the IMF factsheet, as in case of its predecessor, the PRGF, the ECF supports a country's economic programmes aimed at *"moving toward a stable and sustainable macroeconomic position consistent with strong and durable poverty reduction and growth."* Bangladesh Bank's decision to go for such another IMF arrangement brought a surprise to many quarters. One may recall the melancholic experience of the IMF-supported structural adjustment programmes (including those under PRGF), and the lessons drawn from the recent global financial and economic crises (CPD 2011).

The last time, Bangladesh Bank received about USD 467 million in six instalments under IMF's PRGF programme. In September 2007, IMF placed 20 conditions under a package of reforms for the government. The then-government decided not to go for further negotiation for the instalment of USD 123 million. Since then, Bangladesh Bank at different times rejected at least four IMF recommendations over a four-year period, including the adoption of Policy Support Instrument (PSI), introduction of a tight monetary policy, raising CRR for the scheduled banks, and opening of the capital account.

The IMF arrangement comes with a set of conditionalities aimed at liberalising economic policies. In order for the loan under ECF to Bangladesh to be disbursed, 11 steps will have to be taken by the country as per agreed conditionalities. They include: raising prices of compressed natural gas (CNG) and furnace oil (to cut back on energy subsidy); establishing a framework to monitor losses of state-owned enterprises (SoEs) such as the Bangladesh Petroleum Corporation (BPC), Bangladesh Chemical Industries Corporation (BCIC) and Bangladesh Power Development Board (BPDB); phasing out of bank lending rate ceilings; placement of the new VAT and income tax laws that will draw on IMF technical assistance; introducing a debt management strategy to reduce budget deficit; further liberalisation of tariff level; and pursuing of demand-side management in the form of contractionary monetary policy to check the inflationary pressure.

The Finance Minister has ruled out any conditionalities from the IMF side for securing the credit, and stated that the reforms agenda has been prepared locally. VAT laws is expected to be finalised in January 2011, while new income tax law will come in June 2011, with a view to strengthen to mobilisation of domestic resources. A rise in CNG prices has also been hinted by the Finance Minister, and adjustment of furnace oil price has already been announced. As is known, the Central Bank has already raised the policy rates (CRR and SLR) twice in six months to have a firmer grip on the monetary expansion.

Conditionalities that inform the IMF loan may give rise to the cost of doing business, limit government's fiscal operation, limit scope for strategic support to domestic industries and push towards a contractionary monetary policy. Thus, on the one hand, this may constrain the policy space of the government in undertaking the supply-side measures for sustained high economic growth, on the other hand, this could further aggravate the inflationary and BOP pressure. Overall, the economic policies may be directed towards a low-level equilibrium rather than moving on to a higher growth trajectory. However, such policies are also contradictory to the suggested policy in post-crisis global economic order (Box 3.1).

Box 3.1: Policy in Post-Crisis Global Economic Order:
Reflection from United Nation's World Economic Situation and Prospects 2011

After two years of recession and uncertainty, the global economy has started to recover albeit at a slow and differentiated manner. The crisis transmits a number of important lessons for the global economic order. While it has signalled the need for rebalancing global economy, it has also called for a reordering the global economic policies. The policy measures taken by various governments during the early stage of the crisis have no doubt helped to stabilise the economy, but their effectiveness has weakened in recent times. In this backdrop, the United Nation's *World Economic Situation and Prospects 2011* report has placed a number of recommendations (UNDESA 2011). The report forecasted that shifting towards fiscal austerity by many developed countries may adversely affect global economic growth in next couple of years while the developing countries will continue to drive the global recovery. The report also concluded that inflation does not pose a 'serious and present danger,' except in parts of South Asia, where increasingly strong inflationary pressures reflect a combination of supply and demand-side factors. It was advised that enough fiscal space was still available in many countries, and that additional fiscal stimulus was required in the short-run to boost the global recovery. However, fiscal policies will need to be redesigned to strengthen their impact on employment and aid in the transition towards promoting structural changes in the economy for more sustainable growth. A prudent policy to target public investments with a view to alleviating infrastructure-related bottlenecks that mitigate growth prospects is also cited a pre-requisite. Social protection policies are mentioned as another crucial element in cushioning the impact of economic shocks, boosting aggregate demand and contributing to the sustainability of economic growth. The report also put emphasis on greater synergy between fiscal and monetary stimulus. In the current context, maintaining an accommodative monetary policy could be supportive of additional fiscal stimuli in the short-run. Counter-acting damaging international spillover effects in the form of increased currency tensions and volatile short-term capital flows have also been highlighted in the report. The exchange rates among a number of major currencies experienced high volatility during 2010, and hence, escalated tension spread rapidly to other currencies. For now global leaders have agreed to avoid any

(Box 3.1 contd.)

(Box 3.1 contd.)

possible currency war. The failure to maintain exchange rate stability among the three major international reserve currencies has also affected currencies of other developing economies. The surge in capital inflows to emerging economies, due to the quantitative easing in developed countries and portfolio reallocation by international investors, in addition to the weakening of the Dollar, has led to an upward pressure on the exchange rates of some emerging economies. Many developing countries responded by intervening in the currency markets. Some of them imposed capital controls to avoid soaring exchange rates, loss of competitiveness and inflating asset bubbles. Overall the report called for a renewal of pledges to intensify and broaden macroeconomic policy coordination among the global leaders. Drawing lessons from the above context, it is thus once again emphasised that Bangladesh will require to maintain an infrastructure and employment-friendly expansionary fiscal policy, while the monetary policy stance will have to be accommodative.

3.5

PROSPECTS FOR ECONOMIC GROWTH IN THE NEAR-TERM

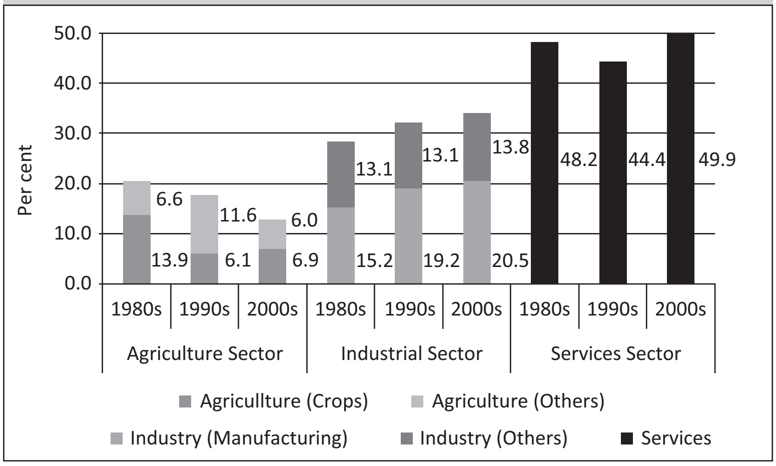
3.5.1 Growth for Structural Change

For a sustainable inclusive development, Bangladesh economy needs to usher in structural changes based on promotion of productive sectors. Growth experience of Bangladesh in the past three decades reveals two broad phases. These are: (a) GDP growth during 1980s and 1990s that had originated from rapid growth of the manufacturing industries; (b) In 2000s, it was the services sectors which had provided a substantial base to augment additional national income, while manufacturing and crops sector held and consolidated their positions (Figure 3.3).

Outline Perspective Plan of Bangladesh 2010-2021: Making 2021 A Reality has rightly emphasised on higher contribution of the manufacturing sector in GDP (Table 3.8). Admittedly, attaining these challenging targets will require considerable acceleration of manufacturing production.

Figure 3.3

Incremental Share of GDP by Broad Sectors



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

3.5.2 Required Sectoral Contributions for Attaining Growth Target

In view of current structure of the GDP in Bangladesh, economic growth beyond 5 per cent is in large part determined by manufacturing sector's level of output. The last time a 'more than six-and-half per cent' growth was achieved in FY2005-06. In that year, the manufacturing sector was able to

Table 3.8

Sectoral Share of GDP

(in Per cent)

Sector	FY2010	FY2015 (Target)	FY2021 (Target)
Agriculture	19.5	16.0	15.0
Industry	28.9	35.0	40.0
Manufacturing	*17.3*	*26.0*	*30.0*
Services (including Import Duty)	51.6	49.0	45.0

Source: Bangladesh Bureau of Statistics (BBS) data and Planning Commission (2010).

Table 3.9

GDP Growth Rate by Sectors

(in Per cent)

Sector	FY2006	FY2007	FY2008	FY2009	FY2010	Required in FY2011 (CPD Projection)
Agriculture	4.9	4.6	3.2	4.1	4.7	4.6
Crops	*5.0*	*4.4*	*2.7*	*4.0*	*5.1*	*5.0*
Industry	9.7	8.4	6.8	6.5	6.0	8.5
Manufacturing	*10.8*	*9.7*	*7.2*	*6.7*	*5.7*	*10.0*
Services	6.4	6.9	6.5	6.3	6.4	6.8
Total	6.6	6.4	6.2	5.7	5.8	6.7

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

post a growth rate of 10.8 per cent (Table 3.9). An analogous performance will need to be attained by the manufacturing sector in FY2010-11 to achieve the 6.7 per cent overall growth target. The contribution from agriculture sector has to be as good as in FY2009-10. CPD has projected that about 6.8 per cent growth will need to be attained by the services sector in FY2010-11 if the overall growth target was to be reached.

3.5.3 Growth Outlook for FY2010-11

At the halfway mark of FY2010-11, several indicators suggest that the economy was gaining some momentum, particularly thanks to the surge in external demand. Buoyant export growth also indicates the possible upbeat in the manufacturing growth. Greater investment demand is reflected in strong industrial credit flow and growing import demand for capital machinery and other production inputs. The outlook of crops sector is also expected to match the recent past performance. The production of Aus and Aman in the ongoing fiscal year have been satisfactory, while optimistic outcome is being forecasted for the Boro yield by concerned quarters. In general, a steady performance of services sector consistent with the energetic performance of the real sectors is to be expected. Thus, in the final analysis, the ability to generate a broad-based manufacturing growth will define the final growth outcome in FY2010-11.

However a couple of disquieting developments may subdue the GDP growth figure in the current fiscal year. The performance of small manufacturing industries has not been able to match the growth of large and medium manufacturing industries.[11] Moreover, a stagnated implementation of ADP was unable to provide the much needed infrastructure to meet the needs of development, and is consequently holding back private investment plans. The emerging power supply situation may not be adequate to accommodate the potential expansion of agriculture and manufacturing sectors in the coming summer season. The government has already indicated that new connections of power and gas supply will be deferred till next April. Slow progress in the energy and power sector is emerging as a binding constraint for the growth and competitiveness of the processing activities. Unhealthy trend in the domestic capital market is also diverting funds and attention from the development of real sectors. Given the current context, it will be challenging to attain the GDP growth target of 6.7 per cent at the end of the fiscal year if the manufacturing sector does not experience a broad-based boost, promoting the needed structural change in the economy.

[11] Production of small manufacturing industries has declined by 9.2 per cent during the first quarter of FY2010-11. As of now, the data for large and medium manufacturing industries is available for only one month; the production index registered 15.3 per cent growth compared to the matching month of previous fiscal year.

3.6

CONCLUDING REMARKS

The monetary policy for the second half of FY2010-11 has been announced at a time when macroeconomic fundamentals are under considerable stresses and strains. Government's revenue collection is turning out to be inadequate to complement the rising expenditure demands whilst overall BOP has entered into a negative terrain. The plan to control money supply to arrest sustained inflationary pressure appears to be not very successful as yet. Implementation of the announced monetary policy will face enormous challenge in achieving its twin objectives of servicing growth and controlling inflation simultaneously. It appears that, at the margin, attainment of a broad-based growth in manufacturing sector will determine the overall growth outcome for FY2010-11. The present macroeconomic developments may have important implications for attaining the economic growth objective. It is apprehended that the loan arrangement under negotiation with the IMF may limit the growth-supportive policy space that the government would otherwise have. A number of conditionalities of the aforementioned loan may be at variance with the declared development policy framework of the government. If fully executed, the conditionalities may curb necessary fiscal expansionary stance and reduce subsidies to critical sectors. It is extremely important that conditionalities that inform the soon-to-be finalised IMF programme are disclosed which is followed by a broad-based public discussion. The policy framework needs to be designed in a way where fiscal policy takes the lead with monetary policy being accommodative to its need. Given the circumstances, the policymakers should not get overly preoccupied with concerns about stability; rather all possible policy measures should lead to broad-based, inclusive and accelerated growth.

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4 CHAPTER

National Budget for the Ultra Poor

Policy Recommendations Submitted to the Members of Parliament

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This chapter was prepared as a Policy Brief for the Members of Parliament under the CPD-BRAC Advocacy Unit (BAU) study on *An Analysis of National Budget: Ultra Poor's Perspective*. The study is detailed on the publication titled *National Budget for the Ultra Poor: An Analysis of Allocation and Effectiveness* (forthcoming).

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Sustainable poverty reduction requires employment generating economic growth with an emphasis on the development of human capital to empower the poor to participate in the growth process. Mobilising resources for poverty reduction programmes may not bring expected results unless policy making and implementation processes ensure empowerment of the poor through a participatory approach. Bringing the poorest sections of society into mainstream economic activities is challenging due to a number of factors which marginalise them, such as lack of skills, lack of community involvement and networks, disabilities, minority status, homeless status, etc. Generally, these people are confined to informal, insecure, low-wage occupations.

Policymakers need to address the needs of the poorest by recognising the factors that have led them to their extreme marginalisation and chronic poverty. As such, the poorest section of the people need a different set of approaches and fiscal provisions, separate from what is set aside for the poor in general. A disaggregated analysis of poverty is also required to better understand the complexities of the problem. Government policies may take more proactive and pragmatic steps to design a pro-poorest approach in the fiscal policy.

Members of Parliament (MPs) are the representatives of the people, and are involved in policy making and finalising the national budget. Thus the MPs can contribute to a great extent in ensuring that the budget addresses the needs of ultra poor citizens of Bangladesh more effectively.

4.1

SUMMARY OF OBSERVATIONS

- Poverty as a concept could not break-off the narrow approach, as the existing conceptualisation based on income/consumption is inadequate. The use of a poverty line approach to define the concept overlooks the multifaceted nature of poverty. Policymakers need to engage with the poor community leaders and others working with these groups to recognise the various dimensions of poverty.
- The current government statistics are prepared based on the Cost of Basic Needs (CBN) criteria, and hence the government policies, do not recognise the concept of *ultra poor*.
- Designs of various fiscal programmes provide very limited scope to differentiate between the poor and the poorest. For example, most of the designated poverty programmes set the criteria of *landless* in targeting their programme participants.
- Poverty reduction has gained some momentum in recent times. But this trend is not perpetuated among all sections of people, particularly the hardcore poor.
- The achievement in poverty reduction so far, has not been equally apparent in terms of all indicators of poverty incidence either. These findings clearly raise the question as to whether the prevailing economic trend is good enough to reach the poorest.
- Rapid urbanisation and rising migration of the poor to urban areas raise the concern about the outlook of poverty reduction. Fiscal policies should also take cognisance of the changes in poverty dynamics in Bangladesh.
- Deepening regional disparity emerges as the new challenge in development paradigm. A number of poverty pockets may slow down the future progress of poverty alleviation. Spatial dimensions include rural-urban poverty, regional disparity (an emerging East-West Divide), and extreme poverty pockets such as *monga*-prone areas, *haor-baor*, *char* areas, etc.
- The tax structure of Bangladesh had little impact on equalising income between the richest and the poorest sections of the society.
- The current budget formulation process has very limited scope to ensure participation of the poors of the society.
- Following the definition by the Finance Division, poverty reducing expenditure as percentage of total expenditure and gross domestic product (GDP) remained more or less stagnant. However, this notion of budget's pro-poorness can be criticised on a couple of grounds. *First*, the definition of the poverty reducing spending is too broad. *Second*, some activities considered under this category, may not always reach the ultra poor.
- The poorest section of the society faces considerable structural barriers to access public services.
- Designs of social safety net programmes are inadequate to prioritise the poorest section. In fact, a number of programmes hardly recognise the ultra poor as a special class among the poor section of the society.
- A small portion of the ultra poor are covered by the social safety net programmes in Bangladesh. Even with the recent rise, Bangladesh seems to be spending far less for them than other countries.

- Given the scarcity of resources, geographical targeting can be one approach which can improve the coverage of social safety net programmes. However, little evidence on effective addressing of regional issues is found in the overall social safety net programme design.
- Currently practiced poverty reducing strategies and programmes do not effectively empower the poorest section. As a result, they fail to participate at the higher end of the market channels. This, in turn, makes it difficult to lead their way out of poverty.

4.2

POLICY RECOMMENDATIONS

Development strategies of Bangladesh have, all along, been focusing on poverty reduction, which is reflected in almost all the planning documents of the country. Despite such efforts, Bangladesh is still known to be the home of a large number of poor people. Programme-based assistance does not address the root cause of poverty – the structural injustice of society that disempowers the poor, and prevents them from having access to productive resource and participating in the decision making. With this end in view, the recommendations of this chapter are made from two perspectives – empowerment of the poor, and effective delivery of the budget.

The following recommendations are placed before the hon'ble MPs regarding issues on which they can directly contribute.

Participation of the MPs in Budget Making Process

The budget making process in Bangladesh is so far bureaucratic in nature. Public representatives, especially the MPs, need to participate actively in this process. Through regional estimation of poverty and resource demand, MPs can then put forward the needs for their administrative areas during the budget preparation phase. Even for special programmes designed for poverty reduction (e.g. social safety net programmes), they can place demands for their respective areas which would in turn help in doing estimation and making allocation of total resource under that programme.

Participatory Budget Making

There is a need to involve all relevant stakeholders, including the ultra poor, in the budget making process for transparency and accountability of the national budget. The government has begun a process of pre-budget consultation with the business community, professionals, civil society organisations, non-government organisation (NGOs), academics and experts. However, the voice of the absentee – the poorest – is still to be heard by the policymakers. While the budget is known to be the most crucial instrument for pro-poor economic growth, it is of utmost importance that the poor, especially the ultra poor, participate in the preparatory process of the budget. Involvement of the political parties in budget preparation is also important to make the process more participatory, which is currently not in practice. Several local NGOs have attempted to simulate a local government's budget making process involving the wider community at the local levels. Such endeavours can be mainstreamed.

Resource Gaps

To make growth sustainable, resource allocation for social protection is essential. On the other hand, a sustainable growth can increase the coverage of social protection. Due to the definitional ambiguity between poor and extreme/ultra poor, it is difficult to come up with a number to indicate how much resource is exactly allocated for the poor and the ultra poor. Currently, only 2.5 per cent of the GDP and 14.8 per cent of the total budget is allocated for the social safety net programmes. However, the definition of these programmes pursued by the government at present also includes *Pension for Retired Government Employees and their Families*, consisting more than 20 per cent of the total allocation for social safety net. In the absence of universal pension scheme, this allocation should not fall into this category. Without this programme, the above mentioned figure will be only 2 per cent of the GDP and 11.7 per cent of the total budget. The allocation for social safety net programmes in FY2014-15 is planned to increase to 3 per cent of GDP. The inadequacy of resources is reflected in two ways. *First*, there is not enough money to reach all those who need it. *Second*, each person receiving support is not receiving enough. Such constraint in resource availability calls for an efficient targeting.

Targeting the Poorest

Targeting is a key factor in implementing any social safety net programme. For effective targeting, target group needs to be clearly defined. Coverage needs to be designed carefully with latest poverty maps or Household Income and Expenditure Survey (HIES). Local NGOs often develop local resource maps and poverty maps with grassroots level information. Synchronisation with these NGOs, by involving them in design, implementation and monitoring process would enhance the efficiency of these programmes. Design and implementation mechanism should be made participatory where voices of the poorest/target group would be heard by the policymakers.

Partnership with NGOs

The practice of GO-NGO collaboration in implementing social safety net programmes is not new in Bangladesh. Vulnerable Group Development (VGD), one of the most prominent such programme in Bangladesh, is being implemented by private organisations like RDRS and BRAC. Many NGOs have identified that the poorest group of the society are less benefited from government interventions (e.g. social safety net). Several development organisations have started programmes specifically targeting the ultra poor. BRAC's *Challenging the Frontiers of Poverty Reduction: Targeting the Ultra Poor* is one such programme, which covers 100,000 households from 15 districts in Phase 1 (2002-2006), and 860,300 households from 41 districts in Phase 2 (2006 and onwards). *Shiree* is another programme which works with 150,000 extremely poor households across the country. The government can build partnership with such organisations to implement and evaluate programmes for the ultra poor.

Include Social Safety Net in the Corporate Ventures

A number of corporate entities are involved in various corporate social responsibility (CSR) initiatives. MPs may pursue to add some selective safety net programmes as the new sectors in the existing CSR list. This can reduce the fiscal burden of the government.

Conceptualisation of Ultra Poor

'Ultra Poor' is not a distinctly defined group in the government's policy documents. The closest nomenclature could be the 'extreme poor' or 'lower level poverty.' The draft Sixth Five-Year Plan (SFYP) uses 'extreme poor' and 'absolute poor' to differentiate between various levels of poverty. Given the importance of targeting as a determinant factor of efficacy of any safety net programme, it is extremely crucial to define the target group clearly. With a clear definition of different poverty groups, MPs would be able to perform a needs assessment for the ultra poor and place demand for resources. In this context, MPs may take proactive role to resolve this fundamental issue of defining and including ultra poor while finalising the SFYP.

Conceptualisation of Social Safety Net Programmes

Globally, the philosophy of social protection/social safety net is inclining towards conditional transfers. Access to social safety net programmes should be highlighted as the 'right' of the poor rather than 'relief.' For example, in case of *Employment Generation Programme for the Poorest (EGPP)*, an essence of 'relief' still prevails. It is crucial that the resource is 'transferred' to the appropriate target group in a 'condition' that they earn it 'through labour.' The philosophy should be: "enhance income and social development through employment generation." It is now time to transform social safety net programmes into more demand-driven ventures instead of supply-driven.

Maintain a Database

A centralised database for social safety net programmes and their benefeciaries has become essential to reduce overlapping of coverage, and maximise the utilisation of resources.

Impact Assessment

It is important to evaluate and assess the impact of the government's programmes to ensure transparency and accountability. The government on its own and a third party institution can conduct the impact assessment of these programmes. This process is not only important for assessing efficacy of the programmes, but is also crucial to set a benchmark that determines graduation strategy and departure points of the participants.

Another set of recommendations is attached as an Annexure to arm the hon'ble MPs with more knowledge so they may advocate for those to different stakeholders including the other government agencies.

4.3

ANNEXURE

4.3.1 General Recommendations

Participation in the Market

- It is the structural injustice that has been resisting the poorest to participate in the market. Approach to 'assist' the poor/extreme poor provides temporary solution. It is important to design programmes that empower the poorest through upgradation of skills so they can contribute to their own development and move to the higher ends of market channel.

Design and Implementation

- *Mainstreaming of the Programmes:* Social safety net programmes should be part of the mainstream development plans. Emphasis should be given on achieving higher implementation of the Annual Development Programme (ADP). Increase in ADP implementation will mean more employment generation for the poor.
- *Preparation and Groundwork:* Adequate time needs to be allocated for proper designing and planning, and pre-implementation groundworks. Similar programmes which are being operated in other countries need to be explored to draw lessons. Officials involved in mid-level and field-level implementation, monitoring and record-keeping need to be trained up properly.

Addressing Urban Poverty

- Most of the social safety net programmes are designed for the rural poor. However, given the increasing rate of urban poverty, specially designed programmes are of great need to assist the urban extreme poor as well.

Grievance Readdress

- A systemic method for grievance recording is highly recommended. Consultation and discussion sessions can be held between participants and delivery/ implementation authority on a regular basis, to this end.

4.3.2 Programme-specific Recommendations

Employment Generation Programme for the Poorest

Institutional Issues

- *Legal Basis:* The programme is still not enacted through any legal act. If the programme is to be made effective and sustainable, it needs to be enacted to guarantee employment for the poorest.

Revisiting the Programme's Status Quo

- *Timeframe:* The programme operates in two lean seasons of a year to assist the rural ultra poor, most of who are agricultural day-labourers, at times when they cannot find job. However, as crop cycles vary in different agro-ecoregions, the lean periods do not prevail uniformly across the country. In this backdrop, rather than following a stringent timeframe, the programme should cluster districts according to agro-ecological pattern and run the programme accordingly. Local crop-cycle, seasonal variability and cropping patterns need to be taken under consideration. In view of this, a bottom-up approach in decision making, where operational timeframe would be designed by local experts, implementation authority involving local people, is required.
- *Selection Process: National Rural Employment Guarantee Act (NREGA)* of India and *Trabajar* of Argentina, two most successful public work programmes operate in a flexible and demand-driven manner where worker groups come to the implementation authority to apply for employment, at times when they fail to get jobs in the market. Despite the fact that for Bangladesh, it is difficult to operate in such an approach where the demand group is extremely large, a similar participatory approach can be piloted in selected districts where potential participants will form a group and apply for work. The selection process of projects also needs to be conducted in a more participatory approach. Active participation of the local community and civil society members needs to be ensured in the consultation process. With the use of that resource, there remains a scope to diversify the type of projects by including social afforestration, waste management, and cleaning and maintenance of local public assets.
- *Non-wage Cost:* Currently EGPP runs with the provision of 10 per cent non-wage or material cost. This is commendable in view of durability of the projects. However, this non-wage cost is allocated from the wage cost by cutting down number of participants. To widen the coverage, separate resource needs to be allocated for non-wage costs.
- *Wage Rate:* Wage of EGPP is and should be kept below market rate to filter non-target groups. The average market wage rate needs to be monitored regularly, and if that changes, EGPP wage rates should be revisited accordingly (on annual basis).
- *Mode of Payment:* Centre for Policy Dialogue (CPD) has long been advocating for payment through banking system in these kinds of projects.[1] EGPP has introduced wage payment through bank accounts, which is a commendable step. However, the associated banks are facing problems in dealing with such a huge workload. In view of this, manpower of the banks needs to be enhanced, while in remote

[1]For details, please see Khatun *et al*. (2009) and Khatun *et al*. (2010).

areas, where access to bank is difficult, mobile branches/stations should be established. CPD has also been suggesting to introduce mobile banking system on a pilot basis to find and deal with associated constraints.

- *Use of Management Information System (MIS):* As can be observed for the case of NREGA, a flagship public work programme in India, all relevant information regarding allocation, expenditure, participant selection process, approved and running projects can be found in the website which is updated regularly. EGPP can also follow the same example for better transparency and efficacy.

Stipend Project for Primary Schools Students

- *Revisiting Selection Criteria:* To continue receiving stipend for the next year, one student needs to secure at least 33 per cent marks in all subjects in the annual examination, and have to attend 85 per cent classes throughout the year. For a student from poor family, it is often difficult to maintain such criteria. As a result, the beneficiary quota is filled by students with better results, in most cases with students from non-poor families who can afford supplementary educational expenses (e.g. private tutor, coaching, etc.). Hence, it is important to make the selection criteria flexible to ensure that students from poorer families derive more benefits.
- *Targeting and Coverage:* The programme, targeting to deliver primary education to all children which demands notes of appreciation, currently covers 60-90 per cent of primary students of any approved primary school throughout the country. To make the programme more directed towards the poorest section of the society, it needs to prioritise the poorest regions of the country. Latest poverty map and HIES can be used to locate the these regions, and coverage can vary as per the regional poverty status.
- *Payment:* The current coverage has the provision to cover all students irrespective of their economic condition. Raising the amount of monthly stipend while lowering number of participating students will benefit the poor students more.
- *Implementation Design and Monitoring:* Design and implementation mechanism needs to be more participatory. Strong and close monitoring involving education officers, members of civil society and NGOs can enhance efficiency of implementation.

Maternity Allowance for the Poor Mothers

- *Design and Preparation:* Programme beneficiary selection, fund release process and implementation mechanism are extremely slow. In cases, the mothers receive the allowance after birth of the child. As a result, expected impact of the programme is not up to the mark which calls for a faster delivery mechanism.
- *Selection Process:* Selection of programme beneficiary is conducted only once-a-year (usually during September-October), and consequently, only those mothers who are pregnant at that time get enlisted. The programme can be redesigned in a way that beneficiary selection process will be conducted in two phases over the year.
- *Involvement of Relevant Agencies:* Local Family Planning and Health Services Offices have complete and regularly updated lists of population (by age, sex and marital status), number of pregnant mothers, newborn children, family planning activities and health-related information. To ensure better, timely and effective selection and implementation of this programme, it needs to be synchronised with those agencies.
- *Awareness:* Awareness among the participants and potential participants is extremely low about the availability of this scheme and its benefits. Relevant information need to be disseminated through workshops, public notices and mass media to increase awareness regarding selection process, allowance disbursement mechanism, duration, frequency of payment and eligibility criteria.
- *Monitoring:* There is no effective monitoring system. The implementation process needs to be monitored closely. Monitoring the participants is also required to ensure that the allowance is appropriately utilised by them. Cases are found where male family-head has used the money. The participants need to be ensured with ownership of the scheme through proper monitoring and awareness raising. A process of regular health check-up of pregnant mothers and the newborn child can be added up in the implementation process.

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5

CHAPTER

Migrant Workers Outflow and Remittance Inflow

Current Trends, Challenges and Future Options for Bangladesh

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5.1

INTRODUCTION

Remittances earned from overseas Bangladeshi migrants have traditionally played an important role from the perspective of replenishing the foreign exchange reserves of Bangladesh. Contribution of remittances in maintaining healthy overall balance of payments (BOP) situation of the country is well documented (Table 5.1). Remittances also played a significant role in the economy when export was experiencing deceleration during the post-Global Financial Crisis period.[1] The positive impact of remittances on consumption and poverty alleviation is also supported by extensive literature.[2] Remittances generate large multiplier effects as these are "more likely to be spent on domestically produced goods" (World Bank 2008). Besides, the welfare impact of international migration, both in terms of reducing pressure on the domestic labour market and injection of foreign currency into the domestic economy is well established.[3] Latest figures show that since independence more than 7.7 million[4] people had left Bangladesh for jobs abroad through formal channels only.[5] A cumulative USD 90.8 billion has been sent to the country by migrant Bangladeshis as remittances since 1976, through the formal channels.[6]

Table 5.1

Importance of Overseas Migration and Remittance for Bangladesh Economy

Year	Remittance (Million USD)	No. of Expatriates ('000)	Cumulative No. of Expatriates ('000)	Remittance as Per cent of				
				Total Export	Total Import	Total ODA	GDP	FOREX Reserve
FY2000	1949	248	2865	33.9	3.0	362.0	17.8	99.1
FY2005	3848	250	4051	45.6	1.9	565.7	21.8	131.3
FY2007	5979	564	4906	49.2	3.3	745.4	25.1	117.8
FY2008	7915	981	5887	56.2	4.5	683.4	27.2	128.7
FY2009	9689	650	6537	62.2	43.0	524.5	10.8	129.7
FY2010	10987	427	6964	67.8	46.3	507.7	11.0	102.2
FY2011	11650	439	7403	50.8	34.6	655.5	10.5	108.6

Source: Calculation based on the Bangladesh Bank and the Bureau of Manpower, Employment and Training (BMET) data (several years).
Note: ODA: Official development assistance; GDP: Gross domestic product.

In the context of prospects of future remittance flows to Bangladesh, a number of factors including gender and skill-mix of migrant workers, cost of migration, catering to the demands in the global labour market, and impact of the crisis in the Middle East and North Africa (MENA) have emerged as major concerns in recent times. Whether or not the

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[1]Increase in oil prices and expansion of economic activities in the Gulf Cooperation Council (GCC) countries helped Bangladesh maintain a decent performance in manpower export and remittance earnings during that period.

[2]According to Khondker and Raihan (2007), growth in remittances accounted for 1.7 per cent out of a 9 per cent decline in headcount poverty during 2000-2005. The study also found that the probability of a household becoming poor decreases by 5.9 per cent if it receives remittances.

[3]About 2.2 million people get into the Bangladesh labour market each year. Capacity to absorb this number within the domestic economy is rather limited. Migrant workers account for between 20-30 per cent of the annual incremental labour force. Thus, manpower export contributes to both poverty alleviation and economic security of the country.

[4]Data till December 2011.

[5]Total number of migrant workforce from Bangladesh at present, however, remains somewhat unclear as many have left through various informal channels and some have also come back.

[6]The cumulative remittance inflow since January 1976 till March 2011 was USD 81.7 billion. This was 1.6 times the foreign aid (USD 51.4 billion) received by Bangladesh during the same period.

upheaval in the MENA countries has had any significant adverse impact on Bangladesh's labour export and remittance earnings, needs careful investigation. However, the volatile situation following the uprising in MENA countries has once again redirected attention of labour-exporting countries such as Bangladesh with regard to the likely uncertainties emanating from this type of development.

The following discussion presents an analytical review of the emerging state of overseas migration and remittance situation of Bangladesh with focus on the first six months of FY2011-12.

5.2

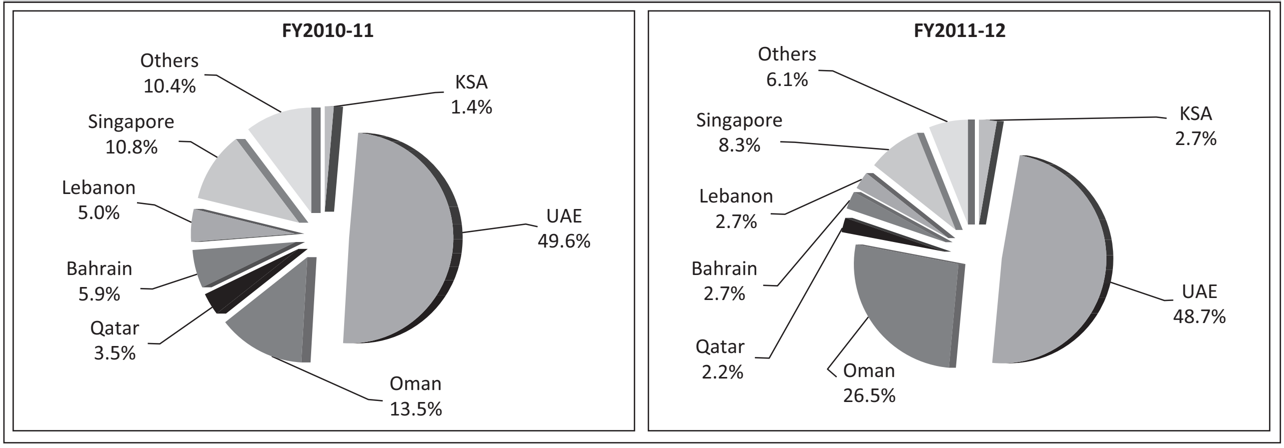
OVERSEAS MIGRATION: REBOUND IN FY2011-12

Official data show that the total number of migrant workers who had gone abroad during the first six months (July-December) of the current fiscal (FY2011-12) was 316,565. This is about 68.5 per cent higher than that of the corresponding period of the previous fiscal when a total of 187,878 workers went abroad. Indeed, the indicator is significantly better than the (-) 16.3 per cent negative growth registered during July-December period of FY2009-10 over the same period of FY2008-09. However, one may recall that number of peoples going abroad from Bangladesh had continued to fall since FY2007-08 till FY2010-11; this was in sharp contrast to the secular rise in the number which was experienced during the period between FY2001-02 and FY2007-08.[7] One may also recall here that with a total of 0.44 million people migrating abroad for work in FY2010-11, the target set out in the national budget (0.58 million) could not be met. Hence, the upturn in overseas migration in the first half of FY2011-12 shows some signs of respite in terms of regaining the lost momentum in manpower export from Bangladesh.

Market concentration of Bangladeshi migrant workers has also shown certain variations in recent times. Figure 5.1A and Figure 5.1B reveal that while share of some of the

Figure 5.1

Change in Market Composition for Manpower Export from Bangladesh: FY2010-11 and FY2011-12 (July-December)



Source: Based on the Bureau of Manpower, Employment and Training (BMET) data.

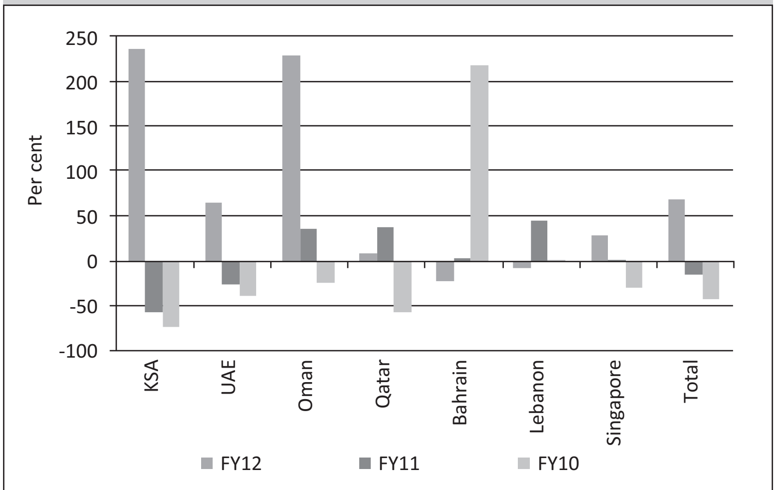
[7] There was some decline in FY2004-05; however, in FY2007-08 a record 0.98 million people had gone abroad from Bangladesh.

traditional markets (such as United Arab Emirates (UAE), Qatar and Bahrain) in terms of manpower export by Bangladesh has declined during the July-December period of FY2011-12, a number of other countries (including Oman and Kingdom of Saudi Arabia (KSA)) have witnessed a rise in their respective shares. Particular mention may be made here of Oman for which the share increased by about 13 percentage points. It may be noted here that while Libya hosted about 6 per cent of total overseas migrant workers from Bangladesh during the first six months of FY2009-10, there was no or insignificant migration to this country over the same period of the next two fiscal years.[8] Indeed, the evolving situation in Libya has raised demand for a *Contingency Plan* to address the needs of the migrant workers in times of crisis in the host countries (more on this in Box 5.2).

Apart from Libya, continued deceleration in overseas migration to Malaysia appears to be a major concern. While Malaysia took about 73,500 (more than 18 per cent of total) Bangladeshi workers during the July-December period of FY2008-09, the number for the corresponding period of the three successive fiscal years were a mere 237, 628 and 308 respectively. As a result Malaysia's share became negligible during the respective first six months of FY2009-10, FY2010-11 and FY2011-12. In a welcome development, some negotiations have recently been initiated by the governments of Bangladesh and Malaysia to facilitate labour migration from Bangladesh through government-to-government (G2G) arrangements.[9] However, the process is yet to bring any tangible outcome.

Bangladesh has experienced negative growth in manpower export also to Bahrain (-22.4 per cent) and Lebanon (-8.5 per cent) during July-December, FY2011-12 as against the same period of FY2010-11 (Figure 5.2). The corresponding growth rates for FY2010-11 vis-à-vis FY2009-10 were 2 per cent and 45 per cent respectively. A large part of the recent decline in overseas migration to these two countries could be attributed to a shift in preference of aspirant migrant workers towards Saudi Arab, UAE and Oman. It is notable that while overseas migration from Bangladesh to both Saudi Arab and UAE during the first half of FY2010-11 registered negative growth ((-) 57.7 per cent and (-) 26.8 per cent respectively) when compared to the same period of FY2009-10, the situation has reversed during the July-December period of FY2011-12. With more than 8,600 people going to Saudi Arab during the first six months of the current fiscal, the growth over the corresponding period of the previous fiscal has jumped to 237 per cent. As for UAE, the growth has been an encouraging 66 per cent. Singapore has also contributed to the positive upturn during the first half of FY2011-12 by posting a growth of 28.6 per cent over the corresponding period of the previous fiscal.

Figure 5.2
Comparative Growth in Overseas Migration: July-December



Source: Based on the Bureau of Manpower, Employment and Training (BMET) data.

[8]According to official data, there was no migration from Bangladesh to Libya during July-December period of 2010. During the same period of 2011, only 89 Bangladeshi workers migrated to that country.

[9]Under the G2G arrangement, Malaysia will take workers from Bangladesh through the Bureau of Manpower, Employment and Training (BMET). The initiative also envisages sending workers to Malaysia at a migration cost not exceeding Tk. 84,000. The Government of Bangladesh (GoB) is currently in the process of finalising the necessary modalities with registered recruiting agencies (though they initially disagreed with the proposed migration cost), so that the offer by the Malaysian government can be meaningfully made use of.

As is known, Saudi Arab has recently expressed its willingness to take workers from Bangladesh under four categories, namely drivers, gardeners, doormen and domestic help. Besides, the island countries of Maldives and Mauritius are reported to be interested to host increased number of migrant workers from Bangladesh in the coming days.[10] While demand in the former is known to be for skilled and professional manpower specially doctors, nurses and teachers, preference of the latter is semi-skilled and skilled workers in garments, construction and fish processing industries. Reports suggest that UAE is planning to invest USD 1.5 trillion in hotels and travelling businesses over the next five years. If so happens, this can turn out to be an important opportunity for export of skilled and semi-skilled manpower from Bangladesh. From the perspective of sustainable development of manpower export, these offers will need to be appropriately considered and follow-up actions will need to be taken.

5.3

REMITTANCE INFLOW: SOME UPTURN BUT LOWER GROWTH COMPARED TO THE RECENT PAST

Remittance earnings have increased more than five times during the past decade and it is currently the single largest foreign exchange earner for Bangladesh. Inward remittances to Bangladesh during the first six months of FY2011-12 stood at about USD 6.1 billion which is 9.3 per cent higher than the comparable period of the previous fiscal; as a matter of fact, much higher than the 0.3 per cent growth that was achieved during July-December of FY2010-11 over the corresponding period of FY2009-10. Hence, in quantitative terms there has been a significant increase in remittance inflow in the first few months of the current fiscal. With the existing growth rate, it is estimated that at the end of FY2011-12 total remittance inflow will stand at around USD 12.7 billion, compared to the USD 11.6 billion of the last year. It may be noted here that the target for remittance earnings in FY2011-12, as set out in the Medium Term Macroeconomic Framework (MTMF), is also USD 12.7 billion. If the average monthly remittance inflow during the July-December, 2011 period is sustained over the second half of the current fiscal, total remittance could turn up to be to the tune of USD 12.1 billion, or on average USD 1 billion every month.

According to the Bangladesh Bank data, growth in remittances in FY2010-11 over FY2009-10 was about 6 per cent. Indeed, this has been much lower than growth rates registered in the recent past (13.4 per cent in FY2009-10, 22.4 per cent in FY2008-09, 32.4 per cent in FY2007-08, and more than 24 per cent in both FY2006-07 and FY2005-06).

As is known, Bangladesh could only manage a mere 2.7 per cent growth in remittances in 2010 over 2009.[11] This was well below 8.2 per cent, which was the World Bank projection for average annual growth in remittances for South Asia for the calendar year 2010 (Mohapatra *et al*. 2011). However, Bangladesh surpassed the projected growth rate for 2011 when the annual growth in remittances stood at 10.5 per cent. It may be noted here that in this instance, the World Bank projection was 9.1 per cent.

In view of the above, Bangladesh needs to design appropriate strategies to consolidate further her manpower export sector in order to be able to access the emerging

[10] http://www.newstoday.com.bd/index.php?option=details&news_id=28982&date=2011-06-01
[11] Comparison between calendar years.

opportunities and ensure sustainable growth in remittance inflow. The following discussion highlights some of the major concerns in the context of overseas migration from Bangladesh.

5.4

CURRENT CHALLENGES IN THE MANPOWER EXPORT SECTOR

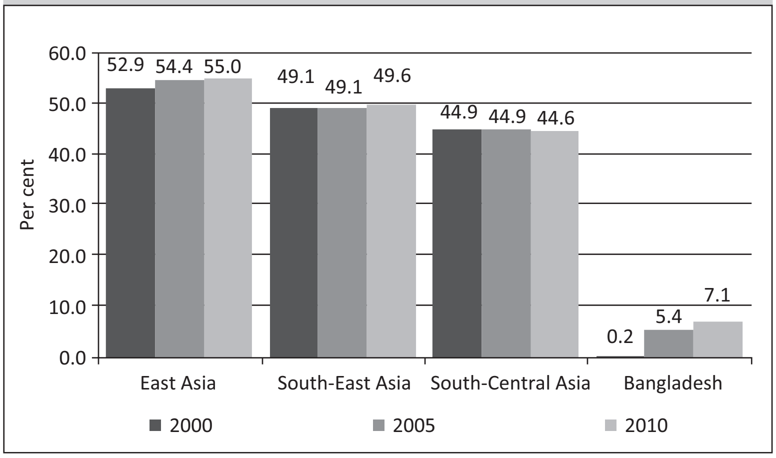
5.4.1 Gender Dimension of Migration: Some Emerging Opportunities

In terms of gender composition of migrant workers from Bangladesh, share of women has consistently remained dismally low compared to their male counterparts. In a welcome change, there appears to be some positive changes in this regard in recent times.

Available data suggests that a total of 182,558 female workers went overseas during 1991 to 2011 period, accounting for a paltry 2.6 per cent of the total overseas migration during the last 21 years. In 2000, share of female migrants in total overseas migration from Bangladesh was only 0.2 per cent which increased to 5.4 per cent and 7.1 per cent respectively in 2005 and 2010 (Figure 5.3). To compare, these figures for East Asia were 52.9 per cent, 54.4 per cent and 55 per cent respectively for the corresponding years. As for the first six months of FY2011-12, about 14,269 female workers went abroad which was roughly 4.7 per cent of the male migrants, and about 4.5 per cent of the total workers (male and female combined) going overseas during the said period. UAE, Jordan, Lebanon and Mauritius were the most important host countries for female workers originating from Bangladesh in recent years.[12]

Figure 5.3

Share of Female Migrants in Total Overseas Migration Across the Region



Source: Adapted from IOM (2010).

In view of the recent Saudi proposition for hosting female workers as domestic help, and also the growing demand for nurses and caregivers in the European countries, there is a need to give dedicated attention towards skill development of women to enhance their share in overseas migration from Bangladesh. Discussion with BMET officials reveals that the Saudi government has proposed to pay an advance of USD 800 per female worker to facilitate their migration in the domestic help category.[13] As per the proposal, this cost of sponsorship will be later adjusted with the wages of the respective workers in the host country.

[12] Rate of female worker migration to Saudi Arab fell drastically since 2009 when only 386 female workers went to the country from Bangladesh compared to more than 4,000 in 2008.

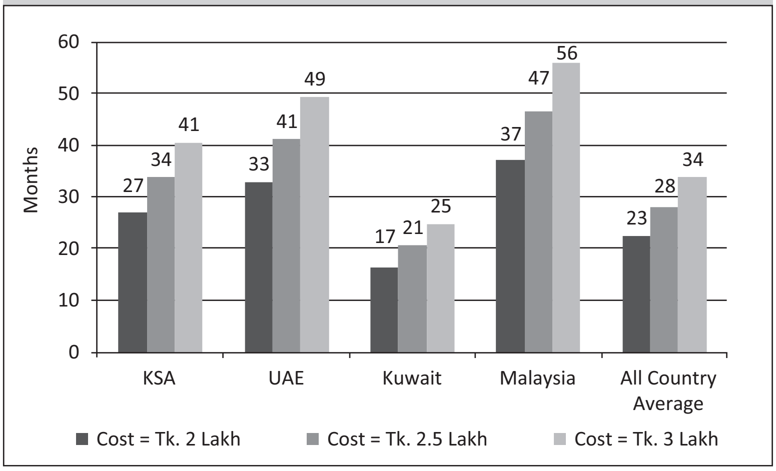
[13] A similar initiative has been reported to be in place on earlier occasions, but malpractice by some recruiting agencies in the form of charging additional fees from aspirant migrant workers inhibited success of the endeavour.

5.4.2 High Cost of Migration: Reduction is the Call of the Day

Average cost of migration from Bangladesh to most countries is known to be between Tk. 2-3 lakh.[14] When this cost is compared with the per capita monthly remittance earnings by the migrant workers, one gets some idea with regard to the approximate recovery period of the cost incurred by these workers to go abroad.[15] CPD estimates, based on the official data on migration and remittance inflow taking place through formal channels show that if a Bangladeshi migrant worker had to spend Tk. 2 lakh to go to Saudi Arab in 2010, it would have taken him/her about two years to recover the cost (Figure 5.4).[16] On the other hand, if the migration cost was Tk. 2.5 lakh the recovery period would have been about three years, and for Tk. 3 lakh it would be about 3.5 years. However, the actual figure could be significantly different as official data for both the stock of migrant workers in the particular country (because of workers returning, and also going through informal channels) and the flow of remittance (because of transfer of remittances through informal channels) often fails to capture the real picture.

Figure 5.4

Recovery Period of Migration Cost for Selected Destinations in 2010



Source: Authors' calculation.

Regrettably, a large number of aspirant migrant workers become victims of unethical profit-seeking motive of a section of recruiting agencies, operating in collaboration with the so called *dalals* (middlemen), and are forced to pay an excessively high price for the visa and migration-related other expenditure heads. Anecdotal information suggests that there are more than 50,000 middlemen currently active in the manpower export sector of Bangladesh. These people intermediate between the aspirant migrant workers and the recruiting agencies. Often the migrant workers 'change hands' several times with attendant cost escalation at each stage. There is a need to raise awareness amongst migrant workers about not taking assistance from the middlemen through various awareness raising campaigns. Recruiting agencies should also be asked to provide necessary information to aspirant migrant workers in a more comprehensive manner. District-level BMET offices (known as District Employment and Manpower Office or DEMO) will have to play a lead role here. Assistance may also be sought from local non-government organisations (NGOs) in this regard.

GoB has been trying to address the issue of migration cost through various ways. The government has recently set up the *Probashi Kalyan Bank* (Expatriate Welfare Bank) which is providing low interest loans to these people (see Box 5.1 for details). Besides, recent information suggests that the government is in the process of consultations with the Bangladesh Association of International Recruiting Agencies (BAIRA) to finalise destination-specific maximum cost of migration. However, any decision on this will need to be backed up by appropriate legislative initiatives. Reduced migration cost, coupled with cash support,

[14] This is more than double the cost incurred by workers going overseas from other South Asian countries.

[15] As a matter of fact, the recovery period will be higher as part of the money spent is collected through borrowings at exorbitantly high interest rate.

[16] Per capita monthly remittance earning from Saudi Arab is estimated to be about USD 107 (Tk. 7,384.5) for 2010. The recovery period is calculated by dividing migration cost by per capita monthly remittance earning. Similar calculations have been done for the other countries.

loan on easy terms, and financial assistance programmes for aspirant migrants will help migration from poor families and also poverty-prone areas, and help reduce the existing regional disparity in the context of overseas migration from Bangladesh.[17]

Box 5.1: Probashi Kalyan Bank (PKB): A Commendable Initiative

Bangladesh government has established the state-run Probashi Kalyan Bank (PKB) to fund workers going abroad for employment, facilitate sending remittances, and reduce migration cost. The PKB was inaugurated on 20 April 2011, on the eve of the 4th ministerial level conference of the Colombo Process. The initiative goes back to May 2010, when the Cabinet gave nod to introduce an 'Expatriate Welfare Bank' to serve the needs of the expatriate workers. In July 2010, the draft Expatriate Welfare Bank got approval from the Cabinet, and the Jatiya Sangsad (National Parliament) passed the Act in October 2010. The paid up capital of the PKB is Tk. 100 crore of which Tk. 95 crore came from the Wage Earners' Welfare Fund and the rest from the government exchequer. The authorised capital for the bank has been proposed at Tk. 500 crore.

The bank provides soft loans to aspirant overseas migrant workers to meet travel/processing cost at 9 per cent interest rate which is lower than that of any other commercial bank. Currently the bank is providing loans to jobseekers to UAE, Bahrain, Lebanon, South Korea, Oman and Mauritius. It has been reported that up to 70 per cent of their total cost is provided as loan. There is difference in the amount of PKB loans for male and female expatriates. According to BMET, cost of migration for male workers is higher than the female workers, as in most cases the cost of visa fees/air fares for female migrant workers are paid by the employers from destination countries.

Another important objective of this bank is to finance returnees to start new business after returning home. The PKB will collaborate with Bangladesh Post Office in order to reach the poor people in rural areas enabling them to collect their remittance from post offices. The new bank also envisages to collaborate with different money/remittance transferring agencies (e.g. Western Union, Moneygram, etc.) in order to reduce the cost of sending remittances.

5.4.3 Fluctuating Purchasing Power of Remittances

Growth figures often do not reflect the actual purchasing power, in local currency, of the remittance sent back home because of domestic inflation. Table 5.2A bears this out very clearly. As the Table indicates, there was indeed a negative growth in remittances sent to Bangladesh in calendar year 2010 in terms of domestic purchasing power (depreciation vis-à-vis inflation rate). This has also been the case for South Asia as a region and a number of other countries. However, the Bangladesh scenario took a positive turn in 2011 (as against 2010) when growth in remittances in terms of domestic purchasing power stood at 9.5 per cent (Table 5.2B). Indeed, this has been possible due to the continuing depreciation of Taka in recent times compared to the inflation rate.

Table 5.2A

Growth of Remittance in 2010 in Local Currency Terms Adjusted for Inflation

Region/Country	Remittance Inflow in 2010 (Billion USD)	Growth of Remittance in 2010 over 2009 (%)		
		USD Terms	Local Currency Terms	Local Currency Terms Adjusted for Inflation
South Asia	81.2	8.2	4.6	-6.3
Bangladesh	11.0	2.7	3.6	-4.5
China	51.3	5.3	4.3	1.0
India	53.1	7.4	1.5	-10.4
Pakistan	9.7	11.1	15.8	3.7
Philippines	21.4	8.1	2.3	-1.4

Source: Mohapatra *et al*. (2011).
Note: Data updated for Bangladesh.

Table 5.2B

Growth of Remittance in 2011 in Local Currency Terms Adjusted for Inflation

Region/Country	Remittance Inflow in 2011 (Billion USD)	Growth of Remittance in 2011 over 2010 (%)		
		USD Terms	Local Currency Terms	Local Currency Terms Adjusted for Inflation
Bangladesh	12.2	10.5	20.2	9.5

Source: Authors' calculation based on Mohapatra *et al*. (2011).

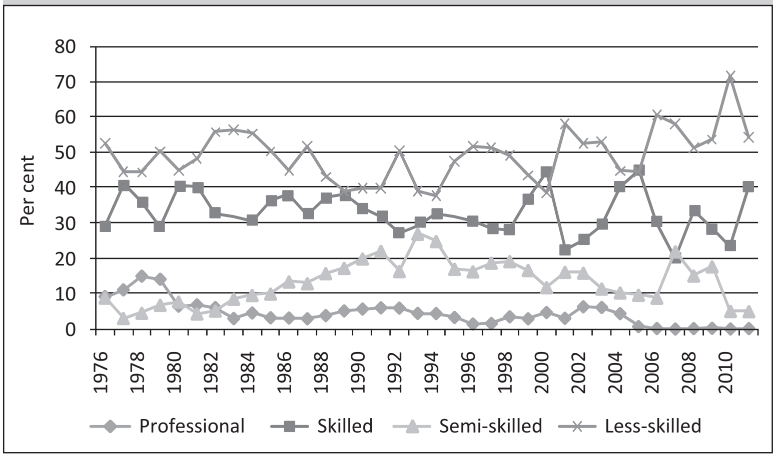
[17] An analysis of the Household Income and Expenditure Survey (HIES) 2005 data indicates that Barisal, Khulna and Rajshahi, the three divisions with higher poverty rates in 2005, received comparatively lower levels of remittances than the relatively more developed rest three divisions of Dhaka, Chittagong and Sylhet (Rahman and Hossain 2011).

5.4.4 Skill Composition of Bangladeshi Migrant Workers: Need for Skill Development

Another key aspect in overseas migration is the skill composition of the workers. As is known, Bangladesh has traditionally been an exporter of workers in the semi-skilled and less-skilled categories. The scenario barely changed over the last two decades (Figure 5.5). This is also reflected in the lower average per capita remittance sent by Bangladeshi workers when compared to other countries.[18] However, some improvements in the skill composition took place in 2011. The proportion of less-skilled workers alone in 2011 was about 54.4 per cent[19], while the rest comprised of semi-skilled, skilled and professional workers. It is noteworthy that the proportion of skilled workers increased significantly in 2011 (40.3 per cent) when compared to 2010 (23.2 per cent). However, low per capita remittance earning (about USD 1,580 for 2011) still demands further move towards skilled and professional categories.

Figure 5.5

Skill Composition of Bangladeshi Migrant Workers since 1976



Source: Based on the Bureau of Manpower, Employment and Training (BMET) data.

The average share of less-skilled workers rose from 52.4 per cent during 2001-2005 period to about 59.8 per cent during 2006-2010. The comparable figures for semi-skilled (from 12.5 per cent to 13.1 per cent), skilled (30.5 per cent to 27 per cent), and professional workers (4.7 per cent to 0.2 per cent) suggest that relatively lower number of skilled workers and professionals have gone overseas from Bangladesh in recent times. From the demand side, this has been particularly due to the slowdown of the building and construction sectors in the traditional markets, particularly in the Middle East. On the other hand, growth in the less-skilled category is partially explained by the growing demand for workers in the agriculture sector both in the Middle East and non-Middle Eastern countries (including Lebanon, Jordan, Sudan, Egypt and Brunei).

Demographic momentum of the Organisation for Economic Co-operation and Development (OECD) countries, characterised particularly by the growth in ageing population resulting in increased demand for caring services and shortage of workers in the healthcare sector, is likely to create significant job opportunities for developing countries, particularly in such areas as physicians, nursing, medical technicians and caring services (Aminuzzaman 2007; OECD 2008; Simoens *et al*. 2005; Kumar and Simi n.d.). This reinforces the need to create more skilled and professional migrants. At the same time, with new opportunities arising in countries such as Saudi Arab, Maldives and Malaysia, technical training centres (TTCs) should be strengthened both in terms of manpower and logistics. It may be noted here that the government has recently allocated about Tk. 900 crore to set up 36 new TTCs across the country in view of the growing demand for skilled migrant workers in the global market.

[18] Average per capita remittance sent by Bangladeshi workers in 2010 was about USD 1,600; to compare for Philippines the figure was about USD 2,300 (Rahman and Hossain 2011).

[19] This share in 2009 and 2010 was 53.7 per cent and 71.6 per cent respectively.

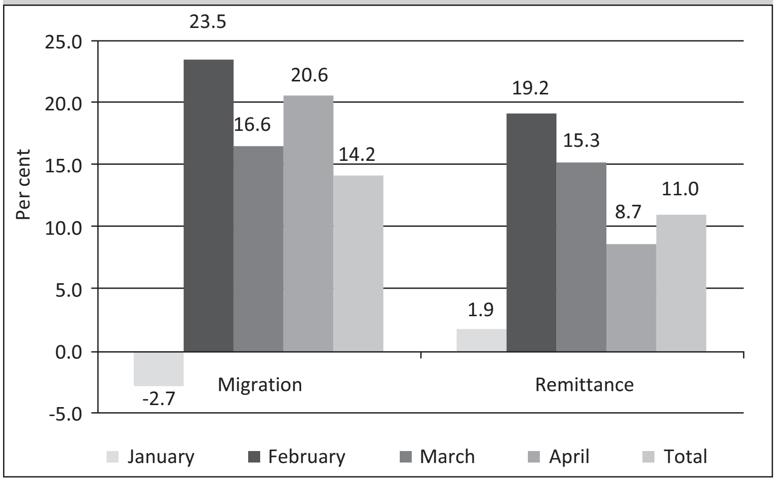
5.4.5 Crisis in the MENA Countries: How Much to Worry About?

There had been some serious concerns regarding possible negative impacts on both manpower export and remittance earnings if there was a widespread dislocation and disturbance in major host countries in the MENA region. It is a matter of some relief for Bangladesh that the available data suggests that the impact so far has not been very significant.

As Figure 5.6 depicts, both overseas migration and remittance inflow have been able to maintain reasonable growth during the January-April period of 2011 vis-à-vis the comparable period of 2010, a period which coincided with the unrest in the MENA countries. During the February-April 2011 period, when the crisis was at its peak, Bangladesh earned nearly USD 3.1 billion in remittances. This was about 14.2 per cent higher than the comparable period of 2010. Besides, the share of Libya in total remittance inflow has traditionally been very low and the scenario has barely changed in recent months.[20] It may be noted here that remittance earnings from Libya in April 2011 was USD 2.9 million, the highest ever from the country to Bangladesh in a single month. Similarly, the total inflow from Libya at the end of FY2010-11 stood at USD 5.2 million which was the highest remittance from the country in any fiscal year. This appears to be due to one-time transfer of savings by Bangladeshi migrant workers in anticipation of uncertainty over job security and earnings in future. With more than half of the stock of Bangladeshi workers returning home from Libya, remittance from the country in the coming months is expected to come down further from the low level as it is.

Figure 5.6

Month-on-Month Growth in Migration and Remittance in FY2010-11 over FY2009-10: January-April



Source: Based on the Bureau of Manpower, Employment and Training (BMET) and the Bangladesh Bank data.

As was noted, crisis in MENA countries did not have serious adverse impact on Bangladesh. However, if there is a contagion effect, or if in future such crises engulf countries such as Saudi Arab, UAE, Qatar, Oman, Kuwait and Bahrain, the impact is likely to be quite serious. Hence there is need for a Contingency Plan.

5.4.6 Possible Impact of Saudisation[21]

The recently proposed move by Saudi Arab to put a six-year cap on the residency of foreign nationals has raised serious concerns for labour-exporting countries such as Bangladesh since implementation of this decision will result in significant fall in

[20] Libya's share in total remittance inflow to Bangladesh for the months of January, February and March of 2011 was 0.0 per cent, 0.1 per cent and 0.3 per cent respectively.

[21] The *Saudisation* policy was approved by Saudi policymakers in 2006 to tackle the growing unemployment among Saudi nationals (currently, unemployment rate in Saudi Arab is 10.5 per cent). The decision to discontinue renewal of work permits for foreign workers spending six years in that country is part of a 10-point programme to intensify *Saudisation* of jobs in the private sector to reduce unemployment. The policy requires private sector companies operating in Saudi Arab to allocate 10 per cent of their total workforce for Saudi nationals. Those having less than that, will not be issued new work permits (*akama*). The Saudi government has given a five months grace period to the country's private companies to comply with the requirement.

remittance earnings.[22] It may be noted here that Saudi Arab currently accounts for about 28 per cent of the total remittance flow to Bangladesh from overseas. Considering the current total stock of Bangladeshi migrants in the country to be 2.5 million (more than 34 per cent of the global stock of migrant workers from Bangladesh), there are only about 0.5 million Bangladeshis in the country with less than six years of residency. As high as about two million Bangladeshi nationals may have to leave Saudi Arab in near future if the proposed measure is implemented within the span of one year. The number of overseas Filipino workers which is expected to be affected by the decision is estimated to be 0.35 million.[23] Besides, the Egyptian government is also concerned about the future of more than 70 per cent of its 2.5 million migrant workers in Saudi Arab as they have crossed the six years residency threshold.[24] Hence, as with Egypt and many other countries including our South Asian neighbours, there is widespread apprehension that in addition to falling remittances, the *Saudisation*-induced return migration could lead to exceptionally difficult situation for countries such as Bangladesh. It is important that Bangladesh remains vigilant in this connection, and appropriate diplomatic initiatives are taken to avert any such possibility.

5.5

IMMEDIATE TO MID-TERM DOABLES

Reducing Cost of Migration

Immediate measures need to be taken to reduce the cost of migration for Bangladeshi workers. In this context, it is of utmost importance that the consultation process between the government and BAIRA is concluded immediately and in a fruitful manner. Besides, all needed measures have to be taken to ensure effective functioning of the PKB. Recruitment of required permanent manpower for the bank should be done on an urgent basis. The government should also play a proactive role to carry out negotiations with major labour-importing countries to expedite the process of setting up branches of the PKB in those countries. This can play a major role in reducing the cost of sending remittances back home by the Bangladeshi migrant workers.

Designing a Contingency Plan

Recent developments in the MENA countries have highlighted the urgency to devise a Contingency Plan to address the needs of overseas Bangladeshi migrant workers, particularly in times of crises. Since the crisis broke out in Libya, more than 36,600 Bangladeshis have returned home aided by International Organization for Migration (IOM), GoB, and in some instances, by their employers.[25] IOM alone facilitated repatriation of about 31,051 Bangladeshis from Libya till mid-2011 (IOM 2011).[26]

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[22] http://gulfnews.com/news/gulf/saudi-arabia/saudi-arabia-plans-six-year-cap-on-expat-visas-1.814794

[23] http://www.mb.com.ph/articles/320681/350000-ofws-may-lose-jobs

[24] https://www.arcamax.com/politics/politicalnews/s-894783

[25] Discussion with BMET officials.

[26] The World Bank has given a loan of USD 40 million to Bangladesh under the *Repatriation and Livelihood Restoration for Migrant Workers Project* to service the attendant costs. Bangladesh paid IOM about USD 14 million against its support for repatriation. Besides, each of the returnees from Libya were to receive a one-time cash grant of Tk. 50,000 to meet immediate expenses including family maintenance. The disbursement began on 23 July 2011, and as of 3 November 2011, a total of 35,915 returnees from Libya received the cash grant.

Box 5.2: Contingency Plan for Emergency Situations

The government should consider designing a Contingency Plan, on an urgent basis, which could include the provision for setting up a Contingency Fund. A certain part of the Wage Earners' Welfare Fund, which currently amounts to about Tk. 300 crore, could be earmarked for this Fund. The Fund could be used towards meeting the expenses for providing emergency food, clothes and shelter to Bangladeshi migrant workers in host countries as well as facilitating their safe repatriation. Besides, addressing the needs of the returnee migrant workers is another important aspect, which as is envisaged, could be taken care of by the PKB. The Contingency Plan should be able to address the following concerns in times of crises:

- Ensuring safety and security of the Bangladeshi migrant workers in the host countries
- Immediate relief in the form of food, shelter, medicine, etc.
- Emergency evacuation
- Safe repatriation
- Rehabilitation upon return to Bangladesh
- Reintegrating returnees into domestic labour market
- Facilitating re-migration of the returnees on a priority basis

Taking Advantage of New Market Opportunities

The importance of the Saudi proposal for hosting workers of certain categories can hardly be overemphasised in the context of the continuing deceleration of manpower export to the country from Bangladesh over the recent past. Besides, such GCC countries as Saudi Arab and Qatar are likely to be in high demand for workers in the construction sector in the coming year.[27] The G2G initiative with Malaysia is another important window of opportunity to revive the growth in overseas migration. While the demand of these countries are for less and semi-skilled workers, opportunities for skilled and professional migrants are expected to be quite high in the OECD countries. Besides, opportunities have also emerged for enhancing worker migration to Maldives and Mauritius. Hence, time-bound and strategic policy initiatives will need to be taken to garner maximum benefits from these emerging market opportunities. In view of the potential impact of *Saudisation*, the need for market diversification has become even more urgent.

Facilitating Overseas Migration from Poverty-prone Regions

The more the number of migrant workers from disadvantaged areas, the greater the effect on poverty alleviation. According to BMET, at least 4 per cent of the migrant workers going abroad through recruiting agencies should come from *monga*-prone areas. As a matter of fact, this is hardly the case. It is, however, encouraging that the Sixth Five-Year Plan (SFYP) mentions about giving special attention to export of manpower on a large scale from *monga* and other underprivileged areas. Appropriate measures will need to be put in place to ensure proper implementation and effective monitoring of these provisions. In its loan disbursement, the PKB should give priority to aspirant migrant workers from poverty-prone and backward regions.

Taking *SFYP-Plus* Measures for the Overseas Migration Sector

The SFYP deals with this sector in a somewhat disjointed manner. However, given the importance of the sector in Bangladesh economy, issues related to overseas migration and remittances deserved to be treated in a more substantial and holistic way. Initiatives such

[27] Saudi Arab has recently approved a project to build the mile-high 'Kingdom Tower'; and Qatar will be building nine fully air-conditioned stadiums for hosting the 2022 FIFA World Cup (http://www.emirates247.com/property/real-estate/kingdom-tower-gets-green-light-2011-04-13-1.380638).

as finalisation of the *Comprehensive Migration Policy* or enactment of an *Overseas Employment Act* should have been included in the agenda of actions in the SFYP. Besides, specific guidelines and workplans to strengthen the capacity of Bangladesh missions abroad to facilitate manpower export demand should be dealt within the Plan document on a priority basis. A number of other issues which did not find due attention in the final SFYP document include strengthening human resource capacity in both the Ministry of Expatriates' Welfare and Overseas Employment (MEWOE) and BMET, as well as enhancing budgetary allocations for these institutions. It is, however, expected that given the importance of the sector in the economy, as well as taking cognisance of the current growth in overseas migration and remittances, the government will come up with *SFYP-Plus* measures to ensure sustainability of the sector to effectively realise the opportunities in traditional and non-traditional labour markets.

Finalising a Comprehensive Migration Policy

Recent reports suggest that GoB is in the process of devising a *Comprehensive Migration Policy*. In this context, the *Emigration Ordinance of 1982* and the *Overseas Employment Policy of 2006* are currently being revisited. One would expect that the final outcome document, whether in the form of a *Comprehensive Migration Policy* or as an *Overseas Employment Act*, will help to address the issue of streamlining cost of migration. Appropriate operational modalities for ensuring full compliance with the law by the recruiting agencies will need to be clearly spelt out in the document.

Strengthening Bilateral, Regional and Multilateral Collaboration

The recently concluded 4th Ministerial Meeting of the Colombo Process has reinforced the need for strengthened collaboration not only with the labour-exporting countries, but also with the recipient countries.[28] Besides, GoB has ratified the *UN Convention on the Protection of the Rights of Migrant Workers and Members of their Families* in April 2011.[29] Efforts should now be strengthened, in collaboration with the 10 other partner countries of the Colombo Process, to pursue labour-importing countries to ratify the relevant UN and ILO Conventions to safeguard the interests of Bangladesh's migrant workers. Technical and strategic support from these organisations could also be sought to facilitate such negotiations. Bangladesh must also play a proactive role in the General Agreement on Trade in Services (GATS) negotiations of the World Trade Organization (WTO) with a view to ensuring a least developed country (LDC)-friendly outcome to augment services export to the global market, particularly under GATS Mode-4.

WTO-GATS and Bangladesh's Opportunity

As is known, as part of the Doha Development Round (DDR) negotiations, WTO Member countries are discussing various modalities to accord preferential market access to LDCs in the services sector. Member countries have, in principle, agreed to a waiver to the LDCs in the context of GATS.

The 'waiver' could potentially open up preferential market access for LDCs such as Bangladesh, which has a keen interest in GATS Mode-4 (Movement of Natural Persons), in the labour market of developed countries. It is of high importance that Bangladesh takes

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[28] The *Dhaka Declaration* of the Colombo Process shows much promise in identifying areas of meaningful collaboration among the Member countries. Critics, however, argue that the existing and growing competition among the labour-exporting countries might work as a deterring factor in the context of meaningful implementation of the commitments articulated in the Declaration.

[29] The Convention was initially signed by Bangladesh in October 1998. At present, Bangladesh is the third Asian country, after Sri Lanka and the Philippines, to have ratified the Convention.

an active interest in the ongoing negotiations and takes necessary steps to realise the expected potential opportunities. A special Taskforce may be constituted in view of this.

5.6

CONCLUDING REMARKS

In view of the current deceleration in overseas migration and remittance inflow, Bangladesh is now faced with a number of challenges to sustain future growth of the sector. Realising the emerging opportunities offered in Saudi Arab, Malaysia, Maldives, Mauritius and OECD countries have become even more urgent and necessary. Bangladesh will also need to prepare herself to tackle the possible adverse effects of *Saudisation* on overseas migration and remittance inflow. A number of areas will require attention and initiatives on the part of the policymakers in this context.

Reducing cost of migration should receive highest priority. A number of steps will need to be taken towards this. These include discussion with host countries to underwrite cost of migration, enforcement of government decision with regard to maximum country-specific migration cost, removal of middlemen through more field-level DEMOs and awareness raising programmes, and taking advantage of the newly-established PKB in providing loans to aspiring migrants. Special programmes will need to be initiated for women and those coming from economically disadvantaged areas. PKB can play a facilitating role in this context.

Government must also take immediate measures to finalise the proposed *Comprehensive Migration Policy* and the *Overseas Employment Act 2011*, and ensure strict compliance with the provisions on the part of the recruiting agencies. A Contingency Plan, with the required funding, should be designed and gradually put in place in view of, and taking lessons from, recent experiences with the MENA countries. Bearing in mind the fluctuating purchasing power of remittance earning, the need for reducing cost of migration and going for higher-income earning sources, backed by the needed skill endowments, has emerged as an urgent task for Bangladesh. Bangladesh should design a comprehensive plan in view of the demographic dynamics and changing labour market scenario in the developed countries. In view of the current negotiations in the WTO-GATS, and particularly in view of the proposed waiver for LDCs, Bangladesh should take a proactive stance in the ongoing negotiations, and should be ready to realise the potential opportunities that could emanate from a successful conclusion of the GATS negotiations.

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ANNEX

Dialogue Report on

State of Bangladesh Economy and Analysis of the National Budget FY2011-12

This Dialogue Report is prepared by *Mr Mashfique Ibne Akbar*, Research Associate of the Centre for Policy Dialogue (CPD).

THE DIALOGUE

The dialogue titled *State of Bangladesh Economy and Analysis of the National Budget FY2011-12* was organised by the Centre for Policy Dialogue (CPD) on 18 June 2011 at the Ruposhi Bangla Hotel, Dhaka. The dialogue focused on an in-depth analysis of the various proposals and the fiscal stances taken by the government in the national budget for FY2011-12. Participants of the dialogue included high-level policymakers, members of the national parliament, leaders of political parties, representatives from the private sector, non-government organisations (NGOs), civil society, academics and other stakeholders.

Chairman, Parliamentary Standing Committee on Public Accounts and Former State Minister for Planning, *Dr Muhiuddin Khan Alamgir*, *MP* was present at the dialogue as the Chief Guest; Special Guest of the event was *Mr Amir Khosru Mahmud Chowdhury*, Former Minister for Commerce and Chairman of Sarina Group. The keynote paper was presented by *Professor Mustafizur Rahman*, Executive Director, CPD, which contained a critical appreciation of the FY2011-12 Budget and CPD's views on various budgetary proposals. The keynote paper was followed by comments from the panel of discussants which included *Dr Mustafa K Mujeri*, Director General, Bangladesh Institute of Development Studie (BIDS); *Dr S R Osmani*, Professor, University of Ulster, UK and Visiting Professor, Department of Development Studies, BRAC University; *Major General (Retd) Amjad Khan Chowdhury*, President, Metropolitan Chamber of Commerce and Industry (MCCI) and Chief Executive Officer, Pran Group; and *Dr A B Mirza Azizul Islam*, Former Advisor to the Caretaker Government, Ministries of Finance and Planning. The dialogue was chaired by *Mr M Syeduzzaman*, Member, CPD Board of Trustees and Former Finance Minister. A full list of dialogue participants is attached at the end of this Annex.

THE KEYNOTE PAPER*

Professor Mustafizur Rahman made the keynote presentation on behalf of the CPD Team of IRBD (Independent Review of Bangladesh's Development). He started his presentation by referring to the tagline put forth by the Finance Minister in the budget speech for FY2011-12 – *Towards building a happy, prosperous and caring Bangladesh*. He emphasised on the twin aspects of implementation of the budgetary proposals and also the Annual Development Programme (ADP) from the perspective of attaining this goal. *Professor Rahman* recalled the benchmarks prevailing at the outset of the outgoing fiscal year 2010-11 as a reference against the budgetary targets. He appreciated the commendable record with regard to collection of revenue by the National Board of Revenue (NBR), and drew attention to the then comfortable state of the balance of payments (BOP), an impressive export growth, and the excess liquidity of Tk. 35,000 crore in the financial system. On the other hand, he stated that inflation was gaining momentum, energy sector was facing setbacks with rising subsidy burden, and that investment was not picking up.

Professor Rahman underscored the major trade-offs faced by the proposed national budget for FY2011-12. Discomforting early signals for FY2011-12 noted by *Professor Rahman* related to the fact of rising inflation, mounting subsidy requirements and the under pressure BOP situation. Energy sector faced formidable implementational bottlenecks in spite of some improvement with regard to generation; liquidity situation of the economy was also coming under some pressure. He also sounded some cautionary note with regard to the foreign reserve situation, remittance flow, and uncertainties related to foreign aid and food security in FY2011-12. In this connection, the speaker drew attention to the commitments in the earlier budget for FY2010-11 that were not fulfilled.

Professor Rahman mentioned that there would be four major trade-offs in the implementation of this proposed budget. The first being the trade-off between growth and macroeconomic stability. Here, maintenance of a low inflation rate would be the key factor. The target was set at 7 per cent in the budget. Payments on account of subsidies and the opportunity cost involved concerned the second trade-off; the third would be the need for higher government borrowing with consequent adverse impact on availability of funds for the private sector. The fourth trade-off related to managing the exchange rate in a manner that took care of the apparently conflicting interests of the export and remittance sectors and the import sector. He also highlighted the missing links in the various targets set out in the Medium Term Macroeconomic Framework (MTMF) and expressed doubt with regard to attaining some of the targets. In relation to MTMF, he raised the question of whether a growth rate of 7 per cent of the gross domestic product (GDP) could be attained in the backdrop of credit growth target having been reduced from 27 per cent to 20 per cent, growth of broad money (M2) coming down to 16

*A detailed CPD analysis of the national budget for FY2011-12 is presented in the Chapter 2 of this volume.

per cent from 20 per cent, and export target being reduced from over 40 per cent to 14.5 per cent. High dependence on borrowing from the banking system to finance the deficit could crowd out private investment, he apprehended. He also expressed his expectation for more clarity and transparency with respect to the subsidy being given by the government to various sectors, particularly to the power sector. He cautioned that, this could lead to serious macroeconomic management problems.

Professor Rahman dwelt on the issue of budget deficit which would be financed for the most part through domestic borrowing, which was likely to account for 60 per cent of the overall borrowing. In view of the crowding out effect on the private sector, he suggested more dependence on foreign aid, particularly in the form of grants, to ease the credit situation in the economy.

The budget for FY2011-12 proposed that 27.9 per cent of the additional taxes will need to be generated from non-NBR sources. This would be a challenging task. The speaker noted that out of Tk. 6,465 crore of additional revenue, Tk. 5,000 crore would be generated through non-tax revenue. In view of this, it was important to identify the prospective sources and state in a clear manner as to how these significant additional resources will be generated in FY2011-12.

Professor Rahman indicated that a large part of the revenue is increasingly going towards interest payments since domestic debt burden was rising. As a consequence, reliance on domestic resources is creating an added pressure on the economy. Another cause of concern was that the revenue income and revenue expenditure were of the same magnitude, resulting in absence of any surplus in the revenue budget. Hence, the development budget of Tk. 46,000 crore will need to be financed through foreign and domestic loans. He pointed out that the majority of the projects under the ADP belonged to the category of carryover projects (from previous year); only a small number of projects were actually 'new.' *Professor Rahman* expressed his concern regarding the cost-escalation effect of such carryover projects. Potential beneficiaries were deprived of the benefits owing to the delayed implementation.

A detailed overview of fiscal measures was presented by *Professor Rahman*. In the backdrop of increasing income inequality and higher levels of inflation, he appreciated the proposed increase of income tax threshold, payment of surcharge tax on wealth valued above Tk. 2 crore, and withdrawal of tax exemption for parliamentarians and government officials.

Professor Rahman commented that allocation for the agriculture sector appeared to be low: 4.23 per cent lower than in FY2010-11. He also took note of the lower allocation for agricultural subsidy in the budget. He criticised proposals relating to the industry sector, particularly with respect to tax holiday which conflicted with the stance taken in the Industrial Policy 2010. He also emphasised on the need for more support to the information and communication technology (ICT) sector. He supported the proposal to raise tax rate for brokerage houses. *Professor Rahman* stressed on the role played by the energy sector in the economy. In this regard, he observed that only 75 per cent of the rental projects went into operation in due time. Thus, generation was lower than what was projected in the medium-term energy plan. He emphasised on the need for more allocation for the education sector. With regard to safety nets, *Professor Rahman* noted that number of beneficiaries has indeed seen some fall in the budget; allocation for this sector has also seen some reduction in the proposed FY2011-12 Budget.

In conclusion, *Professor Rahman* identified four defining factors which would be critically important from the perspective of effective implementation of the budget for FY2011-12. These were: a) maintaining the balance between the financing options considered by the government; b) ensuring prudent macroeconomic management; c) strengthening institutions that deal with development expenditure; and d) a conducive political environment.

PANEL DISCUSSION

Dr Mustafa K Mujeri, Director General, BIDS

Initiating the discussion, *Dr Mustafa K Mujeri* thanked Professor Mustafizur Rahman and the CPD Team for preparing a sound analysis of the national budget. *Dr Mujeri* referred to the Sixth Five-Year Plan (SFYP) and projected that changes will be brought about in the MTMF as the year proceeded. He felt that the major target of all budgetary proposals should be poverty alleviation. *Dr Mujeri* was concerned about the sectoral composition of allocations for agriculture, industry and services sectors in the proposed budget in view of what has been set out in the SFYP. He thought that the industry sector should serve as an important and dynamic driver of growth. However, on the other hand, agriculture sector will continue to have important implications from the perspective of poverty reduction. Given the better record over the past years, he proposed to revise the poverty alleviation target set out in the SFYP to much lower than 30 per cent.

A major concern from *Dr Mujeri* related to the decline of investment-GDP ratio by one percentage point in the proposed budget. More specifically, he was worried about public investment since shortfall in public investment could also affect private investment, which was likely to have adverse impact on attainment of the growth target set out in the FY2011-12 Budget.

Dr S R Osmani, Professor, University of Ulster, UK and Visiting Professor, Department of Development Studies, BRAC University

Dr Osmani thanked CPD for a detailed and wide-ranging analysis of the proposed budget for FY2011-12. He commented that the fate of an economy depends on the policies and actions of cumulative years, and not on the fiscal policy and budget of a single year; and thus, he based his presentation on an analysis of the past budgets and compared this with the proposed FY2011-12 Budget.

Dr Osmani concentrated on fiscal policies of the government and put his focus on the major challenges that Bangladesh will face next year from the point of view of macroeconomic management. He pointed out that the relationship between fiscal policy and the overall growth of the economy was important. He thought that fiscal policy could stimulate aggregate demand as also the entire economy; fiscal policy could also influence the supply side of an economy by raising production capacity through new investment. He noted that the fiscal policy of Bangladesh has been mildly expansionary in the recent past, and he appreciated such expansion in a developing country such as Bangladesh. The main concern for *Dr Osmani* was the financing of the budget deficit and future investment. He observed that, currently budget deficit financing is dependent on domestic resources. While traditionally, other countries have borrowed from the central banks, Bangladesh had seen a tendency to borrow from the commercial banks. Borrowing from the central bank increases money supply and in return induces inflationary pressure on the economy. While Bangladesh, thus far, was able to avoid inflationary pressure, the country is having to assume the liability of increased debt repayment in the future. *Dr Osmani* stressed this point by mentioning that the government could fall into a classical debt trap. Over the last 20 years, interest payment on domestic debt has increased as a percentage of GDP. As a result, the additional government revenue is increasingly utilised for debt repayment, and the government is having to borrow further to keep up with these payments, and limiting resources for other purposes. The speaker observed that internal revenue was often not adequate to finance development expenditure; this exerts pressure on the domestic market as the government has to finance budget deficits through domestic borrowing. Also, the private sector would be affected by the crowding out effect as the public sector struggles to meet its own borrowing demands.

Major General (Retd) Amjad Khan Chowdhury, President, MCCI and Chief Executive Officer, Pran Group

Major General (Retd) Chowdhury began by congratulating CPD and Professor Mustafizur Rahman in particular, for the intricate analysis of the national budget for FY2011-12. He felt that the budget proposed by the Finance Minister would be rather difficult to implement on a complete scale. He felt that poverty alleviation and employment generation could be solutions to high inflation. He noted the low foreign direct investment (FDI), exchange rate volatility, instability in law and order situation, and below-par resource generation are the major challenges facing the government for FY2011-12. The fact of double taxation at the corporate level as well as on dividends, was thought of as irrational by the speaker; he expected a more prudent approach towards fiscal governance. He stated that price hike was a major problem in Bangladesh. Bangladesh should exploit particular sectors where the economy had comparative advantage. The MCCI President concluded his comments by noting that the economy required to generate economies of scale to ensure sustainable development and that investment should be directed towards priority sectors which included both processing as well as production sectors.

Dr A B Mirza Azizul Islam, Former Advisor to the Caretaker Government, Ministries of Finance and Planning

Dr Islam was supportive of Dr Osmani's observations regarding the financing of budget deficit, and further noted that domestic borrowing essentially imposes a fiscal burden on the economy. However, domestic borrowing does not impose a macro burden as the repayment of domestic debt goes back to the citizens. Concern was expressed by the speaker regarding revenue generation which was raised in a distortionary manner, and hence, was not optimal. He observed that in the last decade or so, there was neither any distortion in the flow of credit to the private sector, nor was there any interest rate fluctuation in Bangladesh. But in recent times, due to higher levels of domestic borrowing by the government, there appears to be a liquidity crunch in the economy. The speaker criticised the target amounting to 2 per cent of GDP from external sources to finance the budget deficit and expressed serious doubts as to whether these resources could be mobilised. *Dr Islam* complimented the Finance Minister for recognising some of the challenges in the economy such as fall in remittance inflow. He also agreed with the proposal to cover this decline by exploring new labour markets. Noting that the economy was experiencing high levels of inflation and that ideally the economy would require lower non-essential expenditure, *Dr Islam* mentioned that the budget for FY2011-12 proposed no such reduction. The speaker also noted that the enhancement of government revenue was primarily required for the management of the budget deficit; however, there were no clarification of how the higher government revenue target would be achieved. He also stressed that reduction in money supply and credit supply to the private sector would not only decrease aggregate demand, but may also create problems for the supply side. The speaker indicated concern about the hefty losses that the state-owned enterprises (SoEs) were incurring as there has not been any significant development in this sector.

Dr Islam concluded that fiscal policy measures often matter less to the potential investors compared to political stability, law and order situation, adequate supply of infrastructure, discipline in the labour force, and the supply of skilled labour. He stressed that import duty structure should be reformed. Because of the existing irregularities, there are opportunities for unofficial negotiation between tax collecting officials and importers. Reforms of the import regime which took place in the 1990s were preceded by an in-depth trade policy study in the 1980s. The speaker concluded his remarks by proposing that a similar approach for the reform of the current import regime should be considered by the policymakers.

FLOOR DISCUSSION

Growth Targets

The 7 per cent growth rate proposed in the budget of FY2011-12 would require a private sector investment to the tune of about 28 per cent of GDP which was more than USD 30 billion. Keeping in mind the two prime sources of capital supply – the capital market and the banking system – the 7 per cent growth target was felt to be unachievable by *Professor Abu Ahmed*, Department of Economics, University of Dhaka and Former Chairman of Bangladesh Shilpa Bank, on the ground that the crowding out effect on the private sector from higher government borrowing and the troubled capital market was likely to have a negative growth impact. On a different note, *Mr A K M Abdus Sabur*, Research Director, Bangladesh Institute of International and Strategic Studies (BIISS) pointed out that a 7 per cent GDP growth does not necessarily mean that it would automatically translate into prosperity of the masses if inequality is also not addressed in tandem. *Mr Md Shafiul Islam*, President, Bangladesh Garment Manufacturers and Exporters Association (BGMEA) also pointed out that real growth would be adversely affected because of the increase in prices of fuel and raw materials leading to further price hike, which may also result in a rise in wage level undermining the competitive strength of the enterprises.

Budget Deficit and Financing

Noting that the economy could head towards fiscal-financial indiscipline, *Professor Abu Ahmed* attributed the reason to the fact that deficit was being financed by commercial banks and this created a crowding out effect for the private sector. *Mr Hasanul Haq Inu*, *MP* and Chairman, Parliamentary Standing Committee on Ministry of Posts and Telecommunication and President, Jatiya Samajtantrik Dal, further added to the discussion by saying that if public investment is financed by borrowing from the commercial banks, then the private investment climate could undergo significant deterioration in near future. Since lending rate was low and Bangladesh was accorded a higher credit rating in recent years, *Mr Md Shafiul Islam* suggested that the government should borrow from the international market to ease the pressure on domestic borrowing.

Overall Investment

Mr M Fazlul Azim, *MP* and Chairman, Azim Group said that investment has not been up to the mark, particularly in the power sector. In his view, the reasons for overall low level of investment included inadequate power supply, financing inefficiencies, poor law and order situation, and lack of political stability. On the other hand, *Mr Md Jashim Uddin*, First Vice President, Federation of Bangladesh Chambers of Commerce and Industry (FBCCI) and Vice Chairman, Bengal Group of Industries expressed concern about the absence of allocation in the budget for providing electricity, fuel and infrastructure to the newly introduced economic zones. This could undermine investment, he thought.

Mr Md Jashim Uddin shared his concern about the increase in advance tax payment of necessary goods from 3 per cent to 5 per cent as this measure would discourage investment. He also added that the enhanced tax on exports from 0.4 per cent to 1.5 per cent on the invoice or free on board (FOB) price was actually an imposition of 30 to 35 per cent on profit which would further push back investment. *Mr Azim* stated that the observed growth of 40 per cent in the export sector was not the real growth as this was achieved in the backdrop of a significant increase in price of raw materials. He expressed discomfort about the decision to increase export duty. To him, investment and export would further be affected because of the economic instability that was emerging in the developed world.

Subsidies

Mr M A Mannan, *MP* and Member of Parliamentary Standing Committee on Ministry of Finance strongly suggested that the agricultural subsidy should not be reduced from the present level, and if possible be increased, as higher agricultural subsidy induces higher level of net output, higher productivity and better food security. The speaker also emphasised on the need to distribute the subsidy in an appropriate manner so that it reaches the poorest farmers and not the relatively richer ones. He further suggested that the subsidy in the energy and the fuel sectors be revised and further rationalised. *Ambassador Salma Khan*, President, Women for Women noted that the 16 per cent increase in fuel subsidy proposed in the budget will mainly serve the private sector, and may not be justified from the perspective of equity and justice.

Mr Asif Ibrahim, President, Dhaka Chamber of Commerce & Industry (DCCI) and Vice-Chairman, New Age Group and Industries referred to the taxing system of India and China. India was allowing significant subsidies in the textile sector and China allowed tax exemption for the textile sector. He suggested that tax structure in the manufacturing and the poultry sectors should be compared with those in the neighbouring countries and relevant policies should be designed in the same line.

Although subsidy in the education sector has increased in FY2011-12, *Ambassador Salma Khan* believes that this should have been higher keeping in line with the neighbouring countries which allocated 4 per cent of GDP as education subsidy. She also added that subsidy for the health sector was not adequate for a low-income country such as Bangladesh.

Creating Employment Opportunity

Mr Hafiz Ahmed Majumder, *MP*, Chairman of Pubali Bank Ltd. and Chairman, Brindabon Tea Estate stressed the need for creating employment opportunities if the economy was to prosper. *Mr M A Mannan*, *MP* in this regard emphasised on the importance of the 80-day work programme, Food for Work (FFW) programme, Work for Money programme and other supplementary employment programmes, and recommended that these programmes should be further strengthened. *Mr M S Shekil Chowdhury*, Senior Vice President, DCCI and Chairperson, Centre for Non Resident Bangladeshis expressed his concern regarding tax on the brokerage houses being raised from 0.05 per cent to 0.10 per cent. He felt that this could impact negatively on self-employment.

The Issue of Black Money

Untaxed income in the economy should only be allowed to be converted into white money if these are channelled into investment-oriented sectors, stated *Mr Hafiz Ahmed Majumder*, *MP*. *Mr Shahidullah Chowdhury*, President, Bangladesh Trade Union Kendra and Presidium Member, Communist Party of Bangladesh supported the argument of Mr Majumder, stressing the reality of depressed investment situation in the economy.

Price Stability

Professor Abu Ahmed was of the opinion that many of the indicators in the economy could prove to be growth-reducing. He particularly noted the depreciating exchange rate of Taka vis-à-vis major currencies and the inflation rate that was more than 8 per cent. The speaker also added that the proposal to control inflation, which aimed at reduction in money and credit supply to the private sector, could negatively impact on growth and employment generation in the long-term, which in turn could lead to higher levels of inflation in the economy. *Mr Asif Ibrahim* stated that higher level of inflation could occur as a result of the enhancement of taxes in the manufacturing and poultry sectors.

Mr Hasanul Haq Inu, *MP* mentioned about the commodity price levels at the international market and stated the necessity to take action to keep the domestic prices stable. He noted that about 50 per cent of the economy is linked to the international market. He expressed concern that the government has not been able to keep the price of necessary goods stable. He further added that a combination of price stability and the expansion of the economy was essential from the proposed growth perspective. *Mr M A Mannan*, *MP* agreed with Mr Inu and stated that it was necessary to stabilise prices in the economy along with raising the level of income of the population.

Capital Market

The intervention of the government in the capital market was considered to be necessary by *Mr M A Mannan*, *MP*. He believed that this would bring stability to the market in the days to come. *Mr M S Shekil Chowdhury* stated that the recent capital market crash was affecting the non-resident Bangladeshis (NRBs) as well.

Digital Bangladesh

Mr Syed Almas Kabir, Treasurer, Bangladesh Association of Software and Information Services (BASIS) was of the view that there is hardly any reflection of the digitisation of the economy in the proposed budget. He added that *Digital Bangladesh* would mean infrastructural development and human resource development. To him, the increased import duty for optical fibre in the proposed budget contradicted the mandate and could hinder digitisation of the economy. He compared the imposition of 15 per cent value added tax (VAT) on internet against only 1.5 per cent on gold, and noted that this type of policy signal was alarming for a real *Digital Bangladesh*.

Remittance

Mr M S Shekil Chowdhury reemphasised the importance of remittance as a major contributing sector to the gross national product (GNP). He stressed on the importance of economic diplomacy in the Middle East so that more workers can go to countries in that region. He also suggested that the government should encourage public-private partnership (PPP) with NRBs to finance hospitals and schools in rural areas.

Implementation of the Proposed Budget

Mr M A Mannan, *MP* strongly argued that implementation of the proposed budget would be difficult if the inefficiency of bureaucracy persists in future. He proposed that initiatives towards decentralisation should be undertaken in order to improve the situation. *Dr Md Akram Hossain Chowdhury*, *MP* and Member of Parliamentary Standing Committee on Ministry of Food and Disaster Management agreed with him and shared concerns about the bureaucratic red-tapism and inefficiency in Bangladesh. He identified systematic corruption to be the main factor for non-implementation of the budget. *Dr Chowdhury* suggested that the budget be split to upazila level. *Mr Hasanul Haq Inu*, *MP* stated the need for closer cooperation and coordination between the Prime Minister's Office and the Cabinet Members to improve the state of implementation and efficacy of budget.

COMMENTS FROM THE SPECIAL GUEST

Mr Amir Khosru Mahmud Chowdhury thanked CPD and its Executive Director for the valuable budget analysis that was presented at the dialogue. In his address as the Special Guest, *Mr Chowdhury*, Member, Advisory Council of the Chairperson, BNP and Former Minister of Commerce discussed issues that he found to be lacking in the proposed budget for FY2011-12. He agreed with other discussants who expressed concerns regarding the prospect of implementation of the budget. He noted that the amount of agricultural subsidy has come down, and at the same time, the prices of various fertilisers have gone up. To him, this was in contradiction to the government's explicit policy of putting emphasis on the growth of the agriculture sector. He added that price of the essential components of agriculture had increased in the recent past, electricity and diesel in particular, further undermining the growth of the agriculture sector.

Mr Chowdhury noted that the imposition of 1.5 per cent tax on exports was also contradictory to the aim of Bangladesh's declared export-led growth strategy. He pointed out that the export market was a very competitive one, and in the backdrop of increasing import prices and the possible global meltdown, such measures will not be helpful.

The guest speaker stated that a sound investment environment was essential for growth and employment generation. But the investment was suffering from inadequate infrastructure and the liquidity crisis in the economy. He expressed his discomfort as regards increased interest rates and noted that the Central Bank's plan to control inflation by contracting money supply will not help the economy. He was of the opinion that the export sector will be adversely affected by this move as contractionary monetary policy and export growth cannot occur simultaneously.

Showing concern about the fragility of the capital market, *Mr Amir Khosru Mahmud Chowdhury* commented that there was no visible reforms initiative from the government to streamline the capital market. On the other hand, while he agreed that investment leads to growth, *Mr Chowdhury* was more concerned about the components that bring about positive change in the economy – purchasing power and savings in particular. He felt that Bangladesh had great potential with her low wages and low overhead costs. To him, the government should consider strengthening of investment in potential sectors, rather than sectors which had already created momentum for themselves and had already become matured in the process.

Mr Chowdhury observed that dependence on the private sector for providing utility services would only increase the benchmark costing for the industry, and ultimately lead to higher inflation. He was very critical of the delay in implementation and non-transparency with regard to new power plant projects undertaken by the government in collaboration with the private sector.

Regarding the issue of food security and procurement of foodgrains, *Mr Chowdhury* noted that producers were not getting the right price for their products; it was only a certain group that was exploiting the price fixation and ripping benefit from such manipulation. Consequently, increased import of foodgrains from the international market could lead to higher prices. *Mr Chowdhury* questioned the rationale for some of the subsidies, and was of the opinion that these subsidies could lead to a situation where the general people will have to bear a heavy burden in near future.

Mr Chowdhury felt that financing of the budget deficit was causing liquidity crisis for the private sector. He thought that the private sector could ensure high employment generation, lower wastage and greater efficiency, and hence should be given priority in terms of financing. *Mr Chowdhury* also expressed concern regarding Bangladeshi Taka (BDT) losing its value against the United States Dollar (USD) when most of the currencies in the world were appreciating against the USD.

RESPONSE FROM THE CHIEF GUEST

Greeting all the participants of the dialogue, the Chief Guest, *Dr Muhiuddin Khan Alamgir*, *MP* and Chairman, Parliamentary Standing Committee on Public Accounts and Former State Minister for Planning initiated his speech by inviting everyone to work together to resolve the weaknesses in the proposed budget that were identified in the dialogue. *Dr Alamgir* congratulated the Finance Minister and Hon'ble Prime Minister, and their colleagues for remaining vigilant against the world crisis and also for the proposed budget for FY2011-12. He added that the budget was aimed at the expansion of purchasing power of the common people and was geared towards strengthening of the development expenditure. He recommended that the government should enact an Audit Act to bring transparency of the budget, an act which was already there in India.

Emphasising on implementation of the budget, *Dr Alamgir* observed that every expenditure in the economy should comply with the Constitution and the autocratic practices with regard to expenditure decisions will need to be abolished. He called for bringing significant changes in the functioning of public institutions. He stressed that the budget itself needs to be more self-explanatory and the related ministries will need to be more transparent. Referring to the comment made by Dr Osmani, *Dr Alamgir* said that the government should only borrow when it could make proper utilisation of the funds. If non-utilisation results in only interest payments, then it would be very tough for the government to justify the loan, let alone attain the development targets.

Dr Muhiuddin Khan Alamgir felt that there was a need to support industries by integrating tax, revenues and expenditure sides. He recommended immediate establishment of an independent Revenue Commission which would be able to work closely with the government and undertake expenditure decisions. *Dr Alamgir* reviewed a number of proposals in the FY2011-12 Budget. He was critical of the tax imposed on certain necessary goods as this would hamper growth if seen from a development perspective. Regarding the power sector, he was of the opinion that initiatives must be taken to address the issue of coal extraction. He noted that progress on electricity generation had been remarkable during the tenure of the current government. *Dr Alamgir* concluded by saying that a corruption-free culture ought to be promoted if Bangladesh is to prosper in the coming days.

CLOSING REMARKS BY THE CHAIR

The Chair thanked the participants for sharing their insights, information and views on the budget of FY2011-12. He expressed his gratitude to the Chief Guest, the Special Guest, other distinguished guests and the panel of experts. *Mr M Syeduzzaman* observed that the outgoing FY2010-11 was a relatively better financial year which was characterised by increase in public revenue, a balanced growth in exports and imports, finalisation of the Padma Bridge Project proposal, progress in the energy sector, and a satisfactory GDP growth. Noting that the FY2011-12 Budget is the largest ever, he emphasised on the need for close monitoring of the budget throughout the year for the sake of proper implementation.

Mr Syeduzzaman agreed with the Bangladesh Bureau of Statistics (BBS) poverty estimates that showed a significant reduction of population below the national poverty line from 40 per cent to 31 per cent. He observed that poverty could be reduced further if ADP implementation could be realised more effectively. He noted that the volume of the budget and the ADP share in the budget had been increasing from year-to-year as per the SFYP and the *Vision 2021*. However, he was concerned that ADP implementation has continued to remain a formidable challenge in Bangladesh. He identified slowdown in the disbursement of foreign aid as a critical area of concern. *Mr Syeduzzaman* acknowledged the potential risk regarding the BOP situation; he was also worried about the exchange rate senario in the coming years.

The Former Finance Minister expressed his opinion that the short-term assumptions of the proposed budget such as food security and macroeconomic balance would have to be realised on the ground by raising revenue collection and through increased public savings. He added that revenue generation would depend on the planned reforms of the Revenue Board.

Commenting on the need for policy coordination, he mentioned that there should be close coordination between the fiscal policy and the monetary policy. *Mr Syeduzzaman* was of the opinion that monetary policy does play a significant role in terms of managing inflation, even when the inflation was driven by exogenous shocks and factors.

The Chair expressed his discomfort about the lack of FDI inflow to the economy. In his view, with an acceptable sovereign rating and a good investment climate, along with good investment incentives, lack of FDI inflow could be explained primarily by the very poor state of infrastructure in Bangladesh.

Mr Syeduzzaman agreed with other distinguished experts and reiterated that implementation of the budget depends not only on the Finance Minister, but also on other related ministries, their respective agencies, heads of different departments and autonomous bodies. He emphasised on the need for a coordinated effort towards a better implementation of budget in FY2011-12.

The Chair concluded the dialogue by appreciating the contribution of all participants and expressed his hope that they will continue to extend support to CPD activities in future.

List of Participants

Professor Abu Ahmed
Department of Economics
University of Dhaka and
Former Chairman, Bangladesh Shilpa Bank

Dr Kazi Saleh Ahmed
Former Vice Chancellor
Jahangirnagar University and
President, FREPD

Dr Nasiruddin Ahmed
Secretary
Internal Resources Division (IRD)
Ministry of Finance and
Chairman, NBR

Mr Ziauddin Ahmed
Deputy Director, BBS

Mr Md Shamsul Alam
Director
Industry and Labour Wing, BBS

Dr Muhiuddin Khan Alamgir, MP
Chairman, Parliamentary Standing Committee on
Public Accounts and Former State Minister for Planning

Ambassador Dr Toufiq Ali
Chief Executive
Bangladesh International Arbitration Centre (BIAC) and
Former Permanent Representative of Bangladesh to the WTO

Mr M Fazlul Azim, MP
Chairman, Azim Group

Mr M A Baset
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Director, Southern Knitwear Ltd.

Dr Anwara Begum
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Advocate Masuda Rehana Begum
Bangladesh Supreme Court and
Assistant Secretary
Bangladesh Mahila Parishad

Mr Arup K Biswas
Senior Advisor, Development Affairs
Royal Norwegian Embassy

Ms Priti Chakraborty
Chairman, Xenergia Foundation and
Chairman, J & J Essential Products Ltd.

Mr Suhel Ahmed Choudhury
Former Secretary and
Former Chairman, Janata Bank

Dr Toufic Ahmad Choudhury
Director General
Bangladesh Institute of Bank Management (BIBM) and
General Secretary, Bangladesh Economic Association (BEA)

Mr Anwar-Ul-Alam Chowdhury
Former President, BGMEA and
Managing Director, Evince Group

Major General (Retd) Amjad Khan Chowdhury
President, MCCI and
Chief Executive Officer, Pran Group

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Member, Advisory Council of the Chairperson
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Former Minister for Commerce and
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Dr Md Akram Hossain Chowdhury, MP
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Mr M S Shekil Chowdhury
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Chairperson, Centre for Non Resident Bangladeshis
President and CEO, TCBL Group

Ms Rekha Chowdhury
Bangladesh Mahila Parishad

Mr Rezaul Karim Chowdhury
Convenor
Equity and Justice Working Group and
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Mr Shahidullah Chowdhury
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Former President, BKMEA and
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Managing Director, Mir Ceramics Ltd. and
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Mr Hasanul Haq Inu, MP
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Mr Syed Monjurul Islam
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Mr Syed Almas Kabir
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Mr Hossain Khaled
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Anwar Group of Industries

Engineer Rashed Maksud Khan
Managing Director, Bengal Fine Ceramics and
Advisor, Bangladesh Myanmar Business Promotion Council

Ambassador Salma Khan
President, Women for Women

Professor H I Latifi
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Mr Nooh-ul-Alam Lenin
Publicity Secretary
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Chairman, Pubali Bank Ltd. and
Chairman, Brindabon Tea Estate

Mr M A Mannan, MP
Sunamganj-3 Constituency and
Member, Parliamentary Standing Committee on
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Mr Richard Marshall
Economist, UNDP

Mr Md Abdus Salam Miah
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Former President, BGMEA and
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Mr Mahbubur Rahman
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International Chamber of Commerce - Bangladesh (ICC-B)
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First Vice President, FBCCI and
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Shokaler Khabor

Ms Sharmin Azad
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Channel i

Mr Bishawjit Dutta
Chief Reporter
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ANNEX 1

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Mr Hamid-Uz-Zaman Mamun
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The Daily Janakantha

Mr Musafir Manik
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Mr A K M Moinuddin
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United News of Bangladesh (UNB)

Mr Sadequr Rahman
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Mr Sajjadur Rahman
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The Daily Star

Mr Harunur Rashid
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The Bhorer Kagoj

Ms Sharmeen Rinvy
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Mr Mehedi Zaman
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Jai Jai Din

2 ANNEX

Report on

CPD-BEA Regional Dialogue on

An Analysis of the National Budget for FY2011-12

This Dialogue Report is prepared by *Mr Md. Zafar Sadique*, Research Associate of the Centre for Policy Dialogue (CPD).

THE DIALOGUE

The regional dialogue titled *An Analysis of the National Budget for FY2011-12*, organised by the Centre for Policy Dialogue (CPD), in collaboration with the Bangladesh Economic Association (BEA), Chittagong Chapter was held at the Chittagong Club Auditorium, Chittagong on 25 June 2011. The dialogue, which has by now become a regular CPD event under its *Independent Review of Bangladesh's Economy (IRBD)* programme, was organised with a view to exchange insights and comments on Budget FY2011-12 proposals with eminent citizens of Chittagong, the business capital of Bangladesh.

Mr Mayeenuddin Khan Badal, MP and Member, Parliamentary Standing Committee on Public Undertakings was present at the occasion as the Chief Guest. *Professor M Sekandar Khan*, the Vice Chancellor of East Delta University in Chittagong and the immediate past President of BEA, Chittagong Chapter attended the dialogue as the Special Guest. *Mr Farid Ahmed Chowdhury*, Former President of Chittagong Chamber of Commerce and Industry (CCCI) and *Professor Muinul Islam* of Department of Economics, Chittagong University shared their expert views as the Designated Discussants. CPD's Senior Research Fellow *Dr Khondaker Golam Moazzem* presented the CPD analysis of the proposed budgetary measures for FY2011-12. *Professor Jyoti Prakash Dutta*, President of BEA, Chittagong Chapter chaired the session. CPD Executive Director *Professor Mustafizur Rahman* delivered the welcome speech to initiate the proceedings of the dialogue.

The dialogue witnessed intellectual inputs from various stakeholder groups. Participants at the dialogue included politicians and government officials, business and trade leaders and industrialists, academics, university students, bankers, lawyers, representatives of non-government organisations (NGOs) and various civil society groups from Chittagong. The full list of participants is attached at the end of this Annex.

WELCOME NOTE

Professor Mustafizur Rahman, Executive Director of CPD extended his warm welcome to the designated guests and audience on behalf of the CPD. He thanked the newly elected leaders of Chittagong Chapter of BEA, for the partnership between CPD and BEA. He particularly appreciated the efforts put in by the President and the General Secretary, BEA, Chittagong Chapter towards successful holding of the dialogue.

He noted that budget provides an opportunity not only to discuss the fiscal proposals placed before the national parliament by the Finance Minister, but also creates an opportunity to brainstorm over current economic issues of concern and interests to common citizens. *Professor Rahman* felt that the policymakers would benefit from the deliberations at this regional dialogue and hoped that the views expressed by regional stakeholders will be taken cognisance of when the budget proposals would be finalised by the Jatiya Sangsad.

THE KEYNOTE PAPER*

Dr Khondaker Golam Moazzem initiated his presentation of the budget analysis by highlighting the salient features and benchmarks of the national budget for FY2011-12. He also pointed out the uncertainties and challenges facing the Bangladesh economy. *Dr Moazzem* recalled that the government could take credit for positive achievements in the areas of revenue collections, export growth, private investment and domestic demand; however, there were uncertainties with regard to such issues as foreign aid, foreign exchange reserve, food security and remittance flows. Tackling of inflation, deteriorating balance of payments (BOP) situation, access to liquidity and financing of budget deficit were identified by him as the major macroeconomic challenges those the government was likely to be confronted with during FY2011-12. Keeping broad money (M2) and private sector credit flow within their respective targets could become difficult for the government, he remarked. *Dr Moazzem* termed the projections made by the Medium Term Macroeconomic Framework (MTMF) as removed from reality and noted that there were several inconsistencies.

The public expenditure for FY2011-12 was proposed to be Tk. 163,589 crore with a projected deficit of about 5 per cent of gross domestic product (GDP). In this connection, *Dr Moazzem* shared his concerns about the proposed financing of the budget deficit. Mobilising foreign aid to the tune of USD 3.3 billion was not feasible, he thought. There will be added pressure on the banking sector to finance public expenditure. This implied that the private sector may need to compete with the government to borrow funds from the market whose supply was limited.

Dr Moazzem praised a number of fiscal measures proposed in the budget such as withdrawal of income tax exemption for parliamentarians and government officials, bringing down rate of income tax deduction for

*The keynote paper has been detailed as the Chapter 2 of the present volume.

savings instruments from 10 per cent to 5 per cent, and raising of the supplementary duty (SD) on imported fabrics and readymade garments (RMG) articles from 20 per cent to 45 per cent. He however, expressed concerns over a number of other budget proposals including withdrawal of tax holiday from six sectors (particularly jute and textile industry). He concluded his keynote presentation by highlighting the critically important factors for implementation of the budget for FY2011-12: financing, macroeconomic balance, institutional strengthening and political stability.

PANEL DISCUSSION

Mr Farid Ahmed Chowdhury, Former President, CCCI and Chairman, Frank Group of Corporation

Mr Farid Ahmed Chowdhury agreed with CPD's view that budget financing, macroeconomic stability, building up of institutional capacity and political stability were crucially important for implementation of the budget. He also recommended that sound macroeconomic management and transparent accountability of government expenditure were keys to implementation of the budget, and must be at the centre of policymakers' attention. He felt that Tk. 163,589 crore budget for FY2011-12 and the target of 7 per cent GDP growth were in line with the government's plans and *Vision 2021*, but that everything would depend on implementation.

Mr Chowdhury expressed his concern about recent debates concerning the reliability of national accounts statistics as estimated by Bangladesh Bureau of Statistics (BBS). He reckoned that the estimation of a 6.7 per cent GDP growth in FY2010-11 could prove to be somewhat overambitious. He also expressed his reservation regarding the latest population statistics of Bangladesh. He recommended that this apex official statistics agency needs to be modernised, and that its methodology should be improved and accountability should be restored. In this connection, he observed that the authenticity of the proposed budgetary targets has come under question because of lack of authentic data sources, and that this reduced both reliability and acceptability of the budgetary projections.

Stating that politics and economics were complementary, *Mr Chowdhury* pointed out that political trust and stability, and rule of law were pre-requisites not only for the successful implementation of the budgetary proposals, but also for the well-being of the citizens. However, he regretted that government often tended to deviate from budgetary stance by taking recourse to Statutory Regulatory Orders (SROs). This year, the prices of fuel, gas and fertiliser were increased before the budget which never came up in pre-budget discussions. He also emphasised the need to cut unnecessary expenditures including the ones such as unimportant foreign trips of the Members of Parliament (MPs) and government officials, and provision of tax-free car imports for the MPs. In view of accelerating the economic growth, he urged in favour of decentralisation of the governance system. In connection with this he argued for the introduction of a federal governance system instead of the prevailing centralised system.

Regarding export-oriented sectors, *Mr Chowdhury* felt that the proposed provisions of deduction of 1.5 per cent tax at source (which was previously 0.4 per cent) and the continuation of 9-15 per cent value added tax (VAT) would pose extra burden on these sectors, particularly on the RMG sector. He suggested that the budget proposals should put highest priority on trade and agriculture.

Mr Chowdhury pointed out that lack of administrative and management skills were major flaws that undermined the implementation of Annual Development Programme (ADP). Regarding the issue of economic management, he expressed his concern about the recent volatility in the country's bourse. He suggested that investors be facilitated through easy loans. In this context, he appreciated the proposition of legalising undisclosed money through investment in the capital market. However, he went on to clear his position by saying that legalisation of illegal earnings in any form must be prohibited.

Given the sluggish situation with regard to the power sector of the country and with a view to minimise dependency on costly rental power plants (RPPs), *Mr Chowdhury* urged the government for considering renewable energy sources such as wind and solar power in addition to putting more emphasis on electricity generation from gas and coal.

Mr Chowdhury welcomed the government's initiatives of broadening social safety net including old age allowances and bringing public services under the tax-umbrella. He stressed the need for dredging 127 rivers and recovering canals to facilitate navigation and mitigate water shortage during the dry seasons. He explained that this will not only create employment opportunity, but will also provide water for irrigation.

Professor Muinul Islam, Department of Economics, Chittagong University

Professor Muinul Islam felt that the proposed budget was not ambitious in view of the prevailing inflation rate in the country. He pointed out three sectors – agriculture, education and power management, as areas where the government could claim success. However, he regretted that in the budget for FY2011-12, all these sectors received lower allocation (as percentage to the total budget). He informed the audience that Bangladesh's expenditure in education as percentage of GDP has been one of the lowest in South Asia which at the end of the last government's tenure stood at only 2.07 per cent. While the current government has been able to pull it up to 2.2 per cent during its two and half year's tenure, he reminded the participants that UNESCO advocated for a gradual increase of allocation to 6 per cent of the respective country budgets.

Professor Islam mentioned that some initiatives proposed in the budget such as provision for 10 per cent surcharge for wealth over Tk. 2 crore, income taxes imposed on public services including the top of the hierarchy, and reduction of tax at source from 10 per cent to 5 per cent on savings bonds were quite commendable. In this connection, he suggested for increase of the interest rates on national savings certificates. He also welcomed the proposal of raising tax on tobacco and non-alcoholic beers which have recently gained popularity in the name of energy drinks. Reduction of taxes on spare parts of effluent treatment plants (ETPs) was also appreciable, he added. He argued in favour of subsidies for establishment of solar pumps for irrigation and called for introduction of the duty-free provision for import of intermediate inputs required for production of solar panels. He also proposed for subsidising compressed natural gas (CNG) cylinder for domestic use, so that cylinder gas can be made affordable to the poor. This will, at the same time, reduce misuse of 'pipeline-driven' domestic gas, he explained.

Arguing that the previous actions for legalisation of illegal or undisclosed money were unsuccessful, *Professor Islam* strongly opposed the provisions for investment of undisclosed money in Bangladesh Investment Facilitation Fund Company Limited (BIFFCL). He claimed that this would only encourage growth of parallel economy, which was reported to be equivalent to about 60-70 per cent of the country's formal economy in the present time.

Professor Islam urged for broadening the tax net, mentioning that only 8.5 lakh taxpayers actually paid taxes whereas the number of Tax Identification Number (TIN)-holders was well over 28 lakh. He held that bringing these TIN-holders under tax net could generate considerable amount of revenue. Citing information published by the Bangladesh Bank, he informed that 23,212 persons had over Tk. 1 crore of wealth (as of December 2010). He called for establishing a special cell in tax offices in order to assess this particular group properly. He added that while direct tax, which had the major share in total revenue collection, was critically important for the development of the country, it was also equally important to put emphasis on collection of indirect taxes. Taking note of the decline in foreign aid dependency (2 per cent of GDP), *Professor Islam* felt that Bangladesh was increasingly becoming a trade-dependent state. He compared Bangladesh's current state of development with Rostow's take-off stage and argued in favour of steps to take advantage of the global market opportunities.

FLOOR DISCUSSION

The Budget

Former Vice Chancellor of Chittagong University, *Professor Alamgir Mohammad Serajuddin* thanked CPD and BEA for creating an opportunity where stakeholders in Chittagong could discuss the proposals put forward in the national budget for FY2011-12. However, he noted with some frustration that most policy discussions were Dhaka-based. He doubted whether this type of regional discussions held in the past year were taken cognisance of and got reflected when the budgets were finalised. He felt that the government's decisions were firmed-up long before these discussions took place. He pointed out the case of price hike and inflation. These were repeatedly discussed by stakeholders, however, no concrete measure had been proposed in this year's budget. Regarding the growth projection, *Ms Shahrin Ferdousi*, student of Department of Economics, Chittagong University, felt that the rationale behind the projected GDP growth rate of 7 per cent should be more clearly spelt out by presenting the detailed methodology of estimation.

Budget Deficit

Professor Muinul Islam, the Designated Discussant raised his concern with regard to the sources of financing of the budget deficit. Despite some inconsistencies in the budget, he termed the budget, by and large, 'pragmatic.' *Dr Jamal Nazrul Islam*, Professor Emeritus of Chittagong University, expressed his anxiety over foreign financing as a way of addressing the issue of budget deficit in the form of investment or grants and loans. He also felt that such inflow contributed to rise in violence in this country.

Fiscal Measures

Professor Serajuddin agreed with Dr Moazzem's keynote presentation and supported the view that tax-free income limit of Tk. 180,000, which has been revised upward by 9 per cent, should have been raised to the tune of 15 per cent to adjust to the current inflation level. *Mr Jahangir Alam Chowdhury*, a tax lawyer by profession, while thanking the timely initiative by CPD and BEA, said it was his understanding that there were some discrepancies embedded in the budget with regard to some of the tax-related proposals. He mentioned that for the purpose of tax appeal, the rate has now been raised to 10 per cent against the existing 5 per cent, while for appeals in the high court the fee will now be 25 per cent. In addition to this, if the amount of tax exceeds Tk. 10 lakh, 50 per cent of this tax will need to be paid as fees. He explained that if one was supposed to legally pay Tk. 2 lakh as tax, but was taxed Tk. 1 crore, then he or she will have to pay Tk. 50 lakh as appeal fee against the potentially taxable amount of Tk. 2 lakh. He argued strongly to revisit and review this provision.

Mr Chowdhury felt that the 10 per cent surcharge on net wealth exceeding Tk. 2 crore was a welcome move, though the implication was not progressive in nature. He argued that for the sake of equity and reduction of disparity, the surcharge should be embedded with the worth of asset, rather than against the taxable amount. He did not find e-filing of tax returns to be an effective or popular tool, and felt that this was an impractical initiative in the socioeconomic context of Bangladesh.

ADP Implementation

Implementation of ADP was considered to be a success by some of the discussants in view of the 85 per cent of the budgetary allocation being actually spent. Some emphasis was given on quality of the implementation in FY2010-11 which was a welcome development. Bearing this in mind and considering the 23 per cent larger ADP proposed for FY2011-12 (of Tk. 46,000 crore), *Professor Iftekhar Uddin Chowdhury* of the Department of Sociology of Chittagong University gave prominence to the need for raising the quality of implementation rather than on the implementation rate *per se* to ensure that investments generated the expected return in terms of welfare gains.

Capital Market

Professor Serajuddin strongly opposed any provision in favour of whitening of the black money and felt that such provisions are unethical, immoral, illegal and unjust. He thought that any step that would legalise black money should be discouraged. *Mr Jahangir Alam Chowdhury* also criticised the proposed provision of allowing investment of undisclosed money in the BIFFCL fund, rather than in the capital market. He felt that the withdrawal of tax rebate cap on investment in the capital market was a speculative move at a time when the market was in disarray.

Mr Naser Uddin Ahmed Chowdhury, Former President of Chittagong Stock Exchange Ltd. recommended that government shares be offloaded in the share market to energise the country's bourse. He doubted the perception of policymakers to the effect that demutualisation of shares was responsible for what was happening in the country's capital market. He blamed lack of monitoring and weaknesses in management by the Securities and Exchange Commission (SEC) and governing bodies for the stock market disaster.

Power Sector

Ms Shahrin Ferdousi made the observation that it was important that energy and fuel security was ensured so that industrialisation could gain momentum in the country. She pointed out that though energy sector has been prioritised in the budget with 15 per cent more allocation than that of the previous year, a significant part of this amount was to be spent for payment to the RPPs. She called for a more active participation by the local organisations such as the Petrobangla and Bangladesh Petroleum Exploration & Production Company Ltd. (BAPEX) to meet the energy needs of the country. She thought that the budget should have provided appropriate signals to this.

RMG Sector

Mr Nasir Uddin Chowdhury, the First Vice President of the Bangladesh Garment Manufacturers and Exporters Association (BGMEA) informed the floor that Pakistan has declared 2011 as the Year of Textile. India has allocated Rs. 25,000 crore for skill development and welfare of labourers in the RMG sector, and China has put in place 19 different types of incentives to sustain their respective competitiveness in the RMG sector. He regretted that the Bangladesh government did not take any such measures to protect the sector. He noted that industrialists have been asking for years for setting up special industrial parks and garment villages. These would make catering to the various compliance-related requirements easier. However, this was not happening. *Mr Nasir Chowdhury* reported that costs in RMG enterprises have gone up by 83 per cent because of the revised minimum wage. In addition, expenses related to bank rate, port charges, insurance premium have also increased by about 35 per cent. Increased advance income tax (AIT) on free on board (FOB) value, as proposed in the budget, will exacerbate the situation for RMG entrepreneurs. The Former BGMEA Vice President viewed this as a hard knock delivered to the industry. He urged for adjustment of the 9 per cent VAT on rent for the small and medium enterprise (SME) sector. He recalled that a special stimulus package worth Tk. 3,280 crore was announced following the last fiscal budget, but it was not disbursed. *Mr Nasir Chowdhury* expressed his disappointment at this failure of the government and stated that such unfulfilled pronouncements have misled workers and other stakeholders in the sector. In FY2011-12, a 'New Market Penetration Stimulus Package' has been proposed, though it is not clear how this will be delivered on the ground, he added.

Education

Professor Iftekhar Uddin Chowdhury noted that the *Education Watch Report* by CAMPE in their 2009 assessment of Education for All (EFA) campaign, reported that some 16,359 villages in Bangladesh did not have a primary school. He was apprehensive that the target of attaining the Millennium Development Goal (MDG) of achieving 100 per cent literacy by 2015 may not be achieved. In the backdrop of literacy rate being only 53 per cent in Bangladesh, he urged the government to reconsider the low budgetary allocation for education.

Ms Shahrin Ferdousi felt that the imposition of import duty on foreign books proposed in the Budget FY2011-12 could prove to be rather counter-productive. She argued that, such provisions could be considered only after having established specialised translation centres to cater to domestic demand for such sources.

Chittagong Development Issues

Professor Iftekhar Uddin Chowdhury recalled that, in FY2009-10, in Chittagong alone revenue to the tune of Tk. 21,911 crore had been collected, thanks to the Chittagong Port and the ship-breaking industry. This amount was equivalent to one-fifth of the total government revenue in Bangladesh. However, no dedicated development plan for Chittagong has been put forward in the national budget. He urged for special incentives for three specialised sectors which drives Chittagong's economy – the sea port, the flourishing ship-building sector and the ship-breaking industries. These sectors should get more priority in the national development strategy and policy, he demanded. *Mr Mazharul Hoque Shah Chowdhury*, Former MP proposed that the Chittagong-Laksam-Dhaka rail route should be upgraded for speedy transportation of both goods and people. He proposed that Chittagong should be divided into two administrative districts for smoother administrative governance. This would reduce transportation pressure on Chittagong, he hoped. Development of Chittagong should be addressed from the perspective of stimulating national economy and furthering overall national interest. *Professor Alamgir Mohammad Serajuddin* urged the Chief Guest present at the dialogue Mr Mayeenuddin Khan Badal, MP to play a pioneering role for designing a comprehensive development policy for Chittagong, and ensuring its implementation.

COMMENTS FROM THE SPECIAL GUEST

Professor M Sekandar Khan, Vice Chancellor, East Delta University, Chittagong and Former President, BEA, Chittagong Chapter in his speech expressed disappointment over the increasing number of carryover projects in the ADP. He also pointed out that number of new projects was rather few in the new budget. A recently carried out CPD study had also highlighted this same issue, he noted. He remarked that although public-private partnership (PPP) was initiated with high expectations, till date progress of PPP projects has been very slow. In contrast, the recently initiated social business framework has managed to attract considerable investment including foreign direct investment (FDI). He recommended that this model should be nurtured and promoted.

RESPONSE FROM THE CHIEF GUEST

The Chief Guest, *Mr Mayeenuddin Khan Badal, MP* thanked the organisers and other distinguished participants for their important views, observations and proposals. In his speech he concentrated on four issues. *First*, he expressed his concern about political instability in the country which could undermine and hinder the economic growth in the forthcoming fiscal year and beyond. *Second*, regarding the transit issue, he suggested that the government should not provide transit facilities all over the country but delimit it to certain routes. He suggested the shorter Chittagong-Nazirhat-Ramgarh route as an appropriate one for transit traffic. If this be done, Sandwip could emerge as a major multipurpose transport hub. *Third*, he argued for a four-lane coastal highway from Patenga to Mirsharai to expand the transport connectivity between the port city and the capital. Finally, for the sake of Chittagong's development, he urged for a separate *Karnaphuli River Authority* which could serve as the institution to take care of the river and ensure development of Chittagong. He informed that a capital dredging was about to start in the Karnaphuli River shortly. This would also help operation of the *Kaptai Dam* in full-swing by addressing the problem of non-navigability. He also believed that protecting the *Karnaphuli* River ought to be seen as a key requirement to protect the Chittagong Port.

CONCLUDING REMARKS FROM THE CHAIR

Professor Jyoti Prakash Dutta in his closing remarks emphasised the need for ongoing dialogues to highlight the concerns of common citizens. He felt that to promote wider and better democracy it was important that dialogues and discussions outside of Dhaka be held more regularly. He underscored the need for putting emphasis on the quality of budget implementation. He particularly thanked the Chief Guest for his time and for sharing his valuable thoughts, and Dr Moazzem for making the keynote presentation. He also appreciated the support of the Chittagong Club Ltd. in organisation of the event. *Professor Dutta* thanked all the participants who took part in the discussion and hoped that the partnership between the CPD and BEA Chittagong Chapter would continue in future.

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