Bangladesh Economy in FY2015-16

Interim Review of Macroeconomic Performance

Prepared under CPD's programme on

Independent Review of
IRBD
Bangladesh's Development

Centre for Policy Dialogue (CPD)

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Bangladesh Economy in FY2015-16

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Independent Review of Bangladesh's Development

iRBD

Centre for Policy Dialogue (CPD)

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The CPD IRBD 2016 Team alone remains responsible for the analyses, interpretations and conclusions presented in this publication.

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Acronyms

ACU	Asian Clearing Union
ADB	Asian Development Bank
ADP	Annual Development Programme
ADR	Advance-Deposit Ratio
AEZ	Agro-Ecological Zone
AIT	Advance Income Tax
AIMS	Aid Information Management System
ATV	Advance Trade VAT
BBS	Bangladesh Bureau of Statistics
BDT	Bangladeshi Taka
BEPZA	Bangladesh Export Processing Zone Authority
BEZA	Bangladesh Economic Zone Authority
BGMEA	Bangladesh Garment Manufacturers and Exporters Association
BIBM	Bangladesh Institute of Bank Management
BIDA	Bangladesh Investment Development Authority
BIM	Bangladesh Institute of Management
BIN	Business Identification Number
BITAC	Bangladesh Institute for Technical Assistance Center
BJMC	Bangladesh Jute Mills Corporation
BKB	Bangladesh Krishi Bank
BMET	Bureau of Manpower, Employment and Training
BMRC	Budget Monitoring and Resource Committee
BO	Beneficiary Owners
BOOT	Build-Own-Operate-Transfer
BOP	Balance of Payments
BoI	Board of Investment
BPC	Bangladesh Petroleum Corporation
BPDB	Bangladesh Power Development Board
BSCIC	Bangladesh Small and Cottage Industries Corporation
BSE	Bombay Stock Exchange (India)
BSTI	Bangladesh Standards and Testing Institution
BTC	Bangladesh Tariff Commission
CAR	Capital Adequacy Ratio
CD	Customs Duty
CDR	Credit-Deposit Ratio
CPD	Centre for Policy Dialogue
CPI	Consumer Price Index
CTG	Caretaker Government
DPP	Development Project Proposal

DAE	Department of Agricultural Extension
DAP	Di-ammonium Phosphate
DFI	Development Finance Institution
DMRTDP	Dhaka Mass Rapid Transit Development Project
DSE	Dhaka Stock Exchange
ECNEC	Executive Committee of the National Economic Council
ECR	Electronic Cash Register
EIA	Environmental Impact Assessment
EPB	Export Promotion Bureau
EPO	Export Policy Order
ERD	Economic Relations Division
ERP	Effective Rate of Protection
EU	European Union
FBCCI	Federation of Bangladesh Chambers of Commerce and Industry
FCB	Foreign Commercial Bank
FDI	Foreign Direct Investment
f.o.b	free-on-board
FSRU	Floating, Storage and Re-Gasification Unit
GCC	Gulf Cooperation Council
GDP	Gross Domestic Product
GED	General Economics Division
GFI	Global Financial Integrity
GFMD	Global Forum on Migration and Development
GNI	Gross National Income
GoB	Government of Bangladesh
HIES	Household Income and Expenditure Survey
HPNSDP	Health Population and Nutrition Sector Development Program
ICOR	Incremental Capital-Output Ratio
ICT	Information and Communication Technology
IFC	International Finance Corporation
ILO	International Labour Organization
IMED	Implementation Monitoring and Evaluation Division
IPO	Initial Public Offering
IRBD	Independent Review of Bangladesh's Development
IT	Information Technology
ITC	International Trade Centre
ITES	IT-enabled Services
JICA	Japan International Cooperation Agency
JMRIP	Joydebpur-Mymensingh Road Improvement Project
KOICA	Korean International Cooperation Agency
lb	Pound (mass)
L/C	Letter of Credit
LDC	Least Developed Country
LGFC	Local Government Finance Commission
LGI	Local Government Institution
LNG	Liquefied Natural Gas
LoC	Line of Credit
LSI	Large-scale Industry
Mcf	1,000 Cubic Feet
MDG	Millennium Development Goal
MNC	Multinational Corporation
MoA	Ministry of Agriculture
MoF	Ministry of Finance
MoP	Muriate of Potash
MoU	Memorandum of Understanding

MPS	Monetary Policy Statement
MSI	Medium-scale Industry
MSTPP	2x600 MW Maitree Super Thermal Power Project
MTBF	Medium Term Budgetary Framework
MUSCCFPP	Matarbari 2x600 MW Ultra-Super Critical Coal-Fired Power Project
MW	Megawatt
M&E	Monitoring and Evaluation
NAP	National Agriculture Policy
NBFI	Non-Bank Financial Institution
NBR	National Board of Revenue
NCB	Nationalised Commercial Bank
NGO	Non-Government Organisation
NPL	Non-Performing Loan
NPO	National Productivity Organization
NRB	Non-Resident Bangladeshi
NSD	National Savings Bond
NSDL	National Securities Depository Limited (India)
NSSS	National Social Security Strategy
NTPC	National Thermal Power Corporation (India)
NTTN	Nationwide Telecommunication Transmission Network
ODA	Official Development Assistance
OECD	Organisation for Economic Co operation and Development
PBRL	Padma Bridge Rail Link
PCB	Private Commercial Bank
PCR	Project Completion Report
PD	Project Director
PEDP-III	Primary Education Development Program-III
PERC	Public Expenditure Review Commission
P/E	Price-Earnings
PMBP	Padma Multipurpose Bridge Project
PPF	Project Preparatory Fund
PPP	Public-Private Partnership
PPP	Purchasing Power Parity
QLFS	Quarterly Labour Force Survey
RADP	Revised Annual Development Programme
RD	Regulatory Duty
REER	Real Effective Exchange Rate
RMG	Readymade Garments
RNPP	Ruppur Nuclear Power Plant
SB	Specialised Bank
SCB	State-owned Commercial Bank
SD	Supplementary Duty
SDG	Sustainable Development Goal
SDR	Special Drawing Right
SEZ	Special Economic Zone
SEQAEP	Secondary Education Quality and Access Enhancement Project
SFYP	Sixth Five Year Plan
SMA	Small Metropolitan Area
SME	Small and Medium Enterprise
SoE	State-owned Enterprise
SSI	Small-scale Industry
SSNP	Social Safety Net Programme
SWF	Sovereign Wealth Fund
TAN	Tax Deduction and Collection Account Number
TCS	Tax Collected at Source

TDS	Tax Deducted at Source
TFP	Total Factor Productivity
TIN	Taxpayer Identification Number
ToR	Terms of Reference
TPP	Technical Project Proposal
TPP	Trans-Pacific Partnership
TSP	Triple Superphosphate
UAE	United Arab Emirates
UK	United Kingdom
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
US	United States
USD	United States Dollar
USITC	United States International Trade Commission
VAT	Value Added Tax
VGF	Vulnerable Group Feeding
VND	Vietnamese Dong
WDI	World Development Indicator
WTO	World Trade Organization
7FYP	Seventh Five Year Plan

Chapter 1

State of the Bangladesh Economy in FY2015-16 *(Third Reading)*

This report was released to the media by the Centre for Policy Dialogue (CPD) on 25 May 2016.

1.1 INTRODUCTION

In the face of formidable challenges, the Bangladesh economy continued to show signs of resilience throughout the FY2015-16 period. The economy benefitted from a number of advantages from the perspective of macroeconomic management that were sustained from the previous fiscal year (FY2014-15). Macroeconomic stability was maintained, thanks to falling inflation, contained budget deficit, and large surpluses in both current and financial accounts in the balance of payments (BOP), which was reinforced by impressive export growth and rising foreign direct investment (FDI), and increasing foreign exchange reserves. Declining interest rate on lending has played an important role in the recovery of credit growth to the private sector. Provisional estimates of gross domestic product (GDP) growth rate for FY2015-16 is indicative of strong performance, although private investment (as a share of GDP) is expected to decline, and the drivers of growth to remain outside of real sectors. Moving forward, Bangladesh needs to translate this macroeconomic stability into higher investment and higher growth. Bangladesh will also need to prioritise a sustainable and inclusive growth agenda in the light of the Sustainable Development Goals (SDGs), at a time when the first year of the Seventh Five Year Plan (7FYP) comes to an end.

Despite the revealed macroeconomic stability, a number of concerns continued to plague the economy during FY2015-16. Stagnating private investment, declining agricultural growth, appreciation of the real effective exchange rate (REER), weak (particularly public) banking sector performance, and low efficiency of development spending threaten to undermine economic potential and growth prospects. Both revenue collection and public expenditure are projected to fall short of target, leaving cause for concern regarding implementation of the national budget. Initiatives in the areas of energy, special economic zones (SEZs), and rapid transit systems are yet to gain momentum, as these policy issues and necessary actions are likely to spill over into FY2016-17.

Both resource mobilisation efforts and the efficacy of resource use will need to be significantly increased in the course of the upcoming fiscal year if momentum in growth is to be sustained and further strengthened. Significant public sector funding will be needed for investment in transport and primary energy sectors. Priority tasks that the financial sector must address include strengthening financial regulation and supervision, an institutionalised loan recovery framework and energetic measures to stimulate private sector credit growth. Further reforms relating to various government regulations and auditing pertaining to commerce and industry will be needed to strengthen the competitiveness of the economy and reduce barriers to 'doing business'. Fiscal-budgetary measures in the FY2016-17 budget will need to be aligned with the objectives and targets of the 7FYP.

The present chapter is the third instalment report of CPD's flagship programme titled *Independent Review of Bangladesh's Development (IRBD)*. The report presents a detailed snapshot of the current state of the national economy and flags emerging challenges. Earlier instalments, released in January and April of 2016, provided an interim assessment of the state of the current economy and concerns regarding the upcoming budget for FY2016-17. The IRBD exercise that will be carried out in this fiscal year will also include an immediate assessment of the upcoming FY2016-17 national budget, to be released on 3 June 2016 (the day after the national budget is scheduled to be presented at the national parliament). Based on the latest national and global micro and macroeconomic data and information, this report presents CPD's assessments as regards the performance of the Bangladesh economy in FY2015-16, and the steps that are needed to be taken in view of emerging macroeconomic and sectoral scenarios.

This discussion of the state of the Bangladesh economy is segmented into the following sections: GDP growth and private investment (Section 1.2), the fiscal and budgetary framework (Section 1.3), financial sector performance (Section 1.4), and external sector dynamics (Section 1.5). Two thematic issues of current relevance are also discussed in detail, including recent crop sector dynamics and policy responses (Section

1.6), and labour market dynamics and performance (Section 1.7). The final section (Section 1.8) closes the chapter with some concluding remarks.

1.2 THE CURIOUS RELATIONSHIP BETWEEN PRIVATE INVESTMENT AND GDP GROWTH: REINVENTING THE WHEEL?

Bangladesh has been experiencing a peculiar situation whereby its modestly high 6 per cent plus GDP growth has been achieved and maintained despite sluggish growth in private investment. However, this type of situation is not uncommon in developing countries – indeed, in the early 2000s, the Philippines experienced 'rising growth with declining investment' (Bocchi, 2008). In FY2015-16, the first year of the Seventh Five Year Plan, private sector investment has failed to reach its target. If the necessary initiatives are not taken to incentivise private investment, the target for 2020 (the final year of 7FYP), set at 26.6 per cent of GDP, will be difficult to achieve. Against this backdrop, it is important to examine the in-depth reasons behind the low levels of private sector investment in FY2015-16, taking into account the performance over previous years.

1.2.1 Sources of GDP Growth: Inefficient Use of Capital Weakens Prospects for Growth

Bangladesh's economic growth over recent years has been particularly impressive when compared to that of least developed countries (LDCs) and developing countries (Table 1.1). However, it is important to identify the sources of this growth to understand its sustainability. In order to explore this, a simple econometric exercise has been carried out as part of the current study. Economic growth originates from two sources: a) factor accumulation, and b) factor productivity.[1] An attempt has been made here to capture the extent to which Bangladesh's economic growth can be explained by increased inputs of physical and human capital, and to what extent this is explained by the increased efficiency in the use of those inputs.

Table 1.1

Real GDP Growth of Economies from 2010-2014

(in Per cent)

Economies	2010	2011	2012	2013	2014	Average
World	4.1	2.8	2.2	2.3	2.5	2.7
Developing economies (excl. LDCs)	7.8	5.8	4.7	4.6	4.3	5.3
LDCs	6.0	3.9	4.1	5.5	5.1	4.9
Bangladesh	**6.1**	**6.5**	**6.5**	**6.0**	**6.2**	**6.3**

Source: Compiled from the UNCTADSTAT data.

For the purpose of this study, a growth accounting exercise has been conducted for the Bangladesh economy with the use of World Bank data.[2] The model used for this exercise is derived from a Cobb-Douglas Aggregate Production Function, assuming constant returns to scale. The technological growth rate, or the total factor productivity (TFP) growth rate, is then calculated as the residual of the growth accounting for physical and human capital. To compare the strength of this figure, the same exercise was carried out for India. The methodology of this exercise is outlined in Annex 1.1.

According to Table 1.2, over the last 24 years, Bangladesh has experienced higher growth of both physical and human capital than India. Bangladesh's average physical capital growth was 9.6 per cent compared

[1]According to neoclassical theory, the diminishing returns to capital inputs indicate that capital-driven growth is only achievable in the short-run. In the long-run, growth is achieved by the incremental efficiency of inputs that is the technological growth which is captured through the residual total factor productivity (TFP) growth (Solow, 1957).

[2]Data is taken for 24 years (1991-2014).

Table 1.2

Comparison of Sources of GDP Growth in Bangladesh and India: 1991-2014

(in Per cent)

Country	Physical Capital		Human Capital		Total Factor Productivity Growth[c]	GDP Growth
	Physical Capital Growth[a]	Contribution to GDP	Human Capital Growth[b]	Contribution to GDP		
Bangladesh	9.6	3.8	3.0	1.8	-0.3	5.3
India	9.4	3.8	2.5	1.5	1.3	6.6

Source: Nehru and Dhareshwar database of Physical Capital Stock; Barro-Lee database of mean years of schooling; World Development Indicators (WDI), World Bank.

Note: [a]Growth of physical capital is the gross capital formation as a per cent of capital stock in the respective year.

[b]Growth of human capital is the growth in the labour force (quality adjusted).

[c]TFP growth is the portion of output not explained by the amount of inputs used in production. As such, its level is determined by how efficiently and intensely the inputs are utilised in production. TFP growth is usually measured by the Solow residual.

to India's 9.4 per cent average over the corresponding years. The annual average figure for human capital growth was 3 per cent for Bangladesh compared to India's 2.5 per cent over the corresponding period. However, concerns arise in relation to Bangladesh's growth scenario when the growth of capital inputs (which include both physical and human capital) in the growth equation is accounted for. Assuming a physical capital share of 0.4[3] and constant returns to scale for both countries, the TFP growth rate for Bangladesh over the period 1991-2014 averages (-) 0.3 per cent per annum compared to India's 1.3 per cent per annum. This suggests that, although the growth rate of factor inputs in Bangladesh has been relatively high over recent years, efficiency of the factor inputs should be a matter of concern. Indeed, in the case of Bangladesh, the efficiency of input utilisation has, in fact, decreased over the examined period. Growth of capital inputs contributed 5.6 per cent on average to GDP growth, however, this has adversely affected the actual GDP growth rate, bringing it down to 5.3 per cent. In contrast, India's capital inputs accounted for only 5.3 per cent of the average annual GDP growth, while the remaining 1.3 per cent is due to increased efficiency of the capital inputs (TFP).

If Bangladesh had been able to efficiently use the physical and human capital inputs to the same degree as India, the average annual growth rate would have been approximately 7 per cent, instead of the actual 5.3 per cent over the 1991-2014 period. The total loss from the relative inefficiency has been approximately USD 607 billion (at 2014 prices) over the 1991-2014 period.

The relative difference in productivity levels in India and Bangladesh are reflected in the change in GDP per capita levels over the years. Table 1.3 shows the GDP per capita for India and Bangladesh at constant 2014 USD. In 1990, India's per capita GDP was 1.1 times that of Bangladesh. The gap between the two economies has increased over the years, and by 2014, this ratio had reached 1.46. If Bangladesh were to have had the same TFP as India over the last 24 years, the GDP per capita of Bangladesh would have been USD 1,568 in 2014, compared to the actual figure of USD 1,087 (according to the Bangladesh Bureau of Statistics (BBS) data, per capita income was USD 1,110 in FY2013-14). The GDP gap, in turn, would have also decreased and the GDP per capita would have been very similar in magnitude. This therefore calls for necessary changes to be made in national policies so as to increase FDI, improve information and communication technology (ICT) infrastructure, promote institutional improvements, and achieve greater efficiency of public expenditure, amongst others.[4]

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[3]A study conducted by Ramírez-Rondán *et al.* (2005) has estimated the share of physical capital to be 0.39. Furthermore, Collins (2007) examined the sources of growth in South Asia, and assumed the share of physical capital to be 0.35. We assume 0.4 for simplicity.

[4]Details can be found in an upcoming CPD Policy Brief: "Higher Inputs, Lower Returns: An Inquiry into the Factor Productivity Trend of Bangladesh."

Table 1.3

Comparison of per Capita GDP: Bangladesh and India (at constant 2014 USD)

Country/Ratio	1990	1995	2000	2005	2010	2014
India	515.61	598.53	733.19	934.34	1,294.88	1,581.51
Bangladesh (Actual)	470.75	525.69	600.36	706.51	894.24	1,086.81
Bangladesh (with India's level of productivity)	470.75	554.75	692.50	880.31	1,257.23	1,568.03
Ratio of India-Bangladesh (Actual)	1.10	1.14	1.22	1.32	1.45	1.46
Ratio of India-Bangladesh (with same level of productivity)	1.10	1.08	1.06	1.06	1.03	1.01

Source: Compiled from the World Development Indicators (WDI), World Bank.

1.2.2 Understanding Recent Trends in Private Investment

Sluggish private investment growth

During FY2015-16, private investment is estimated to be 21.78 per cent of GDP, and has decreased by about 0.3 percentage points since FY2014-15. Despite a favourable macroeconomic environment (e.g. moderate level of inflation, reasonable BOP and high foreign exchange reserves), private investment failed to pick up in FY2015-16. During the same period, public investment experienced a higher level of growth, which contributed to the higher total investment-GDP ratio (Figure 1.1). Unlike in the 1990s and 2000s, relatively high GDP growth against a moderate rise in investment-GDP ratio over recent years alludes to improvements in capital efficiency, as reflected in the falling incremental capital-output ratio (ICOR) (Figure 1.1).

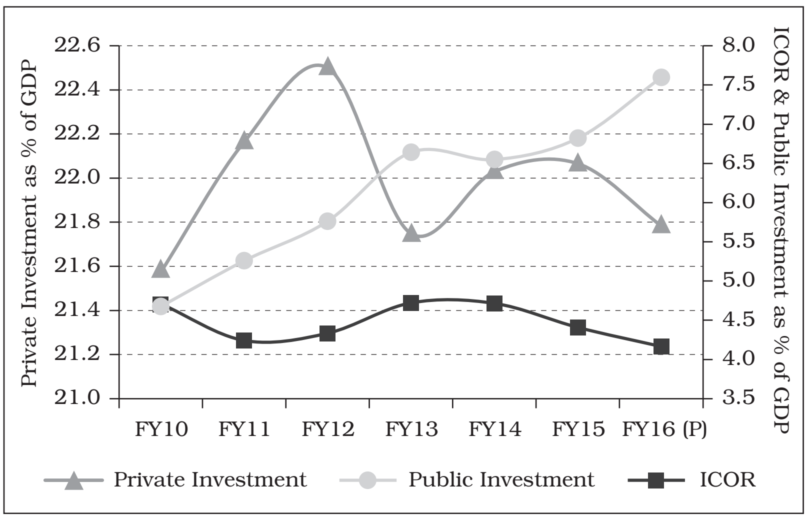


Figure 1.1

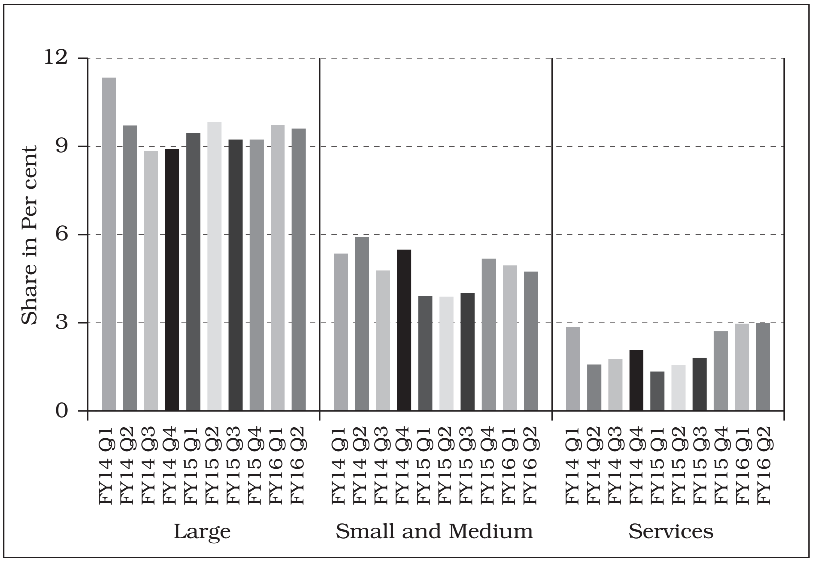
Trends in Private Investment-GDP Ratio and ICOR

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

The composition of advances is changing

In overall advances made by the commercial banks, industrial term loan has gradually lost its share to other economic activities – this share has reduced from 19.5 per cent in Q1 of FY2013-14 to 17.3 per cent in Q2 of FY2015-16 according to Bangladesh Bank data. The share of advances (outstanding) to large, medium and small industries in total advances has somewhat decelerated in FY2015-16, which is indicative of sluggish domestic private investment in manufacturing activities. Outstanding position of term loans to large industries (as a share of total advances) also declined from 11.3 per cent as of Q1 of

Figure 1.2
Outstanding Position of Term Loans as a Share of Total Advances



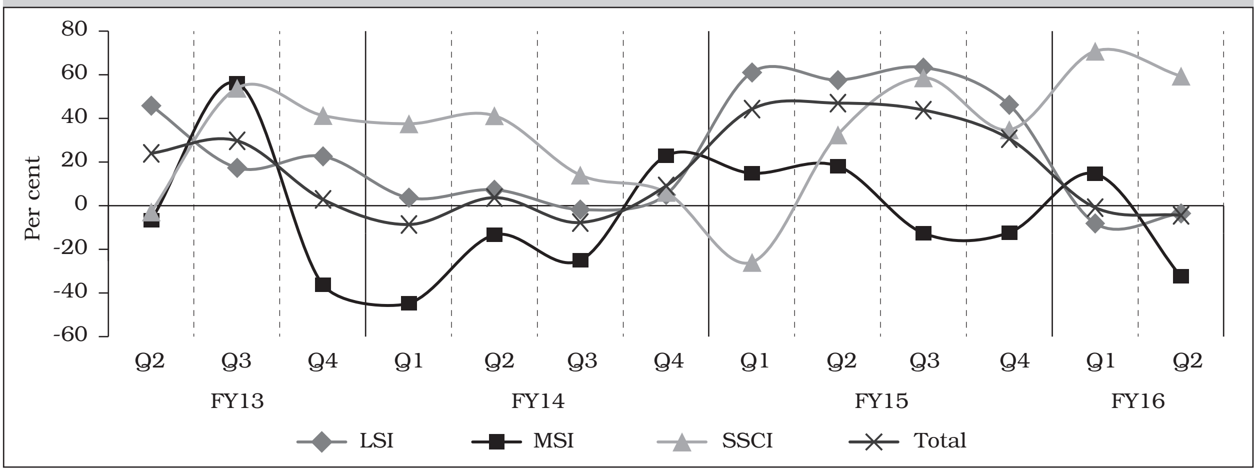
Source: Bangladesh Bank.

FY2013-14 to 9.6 per cent as of Q2 of FY2015-16 (Figure 1.2). On the other hand, the share of advances in services-related activities has continued to rise since Q1 of FY2014-15 (from 1.3 per cent to Q1 FY2014-15 to 3 per cent, Q2 FY2015-16). This is both reflective of, and likely to contribute to, rising role of services in the growth of the GDP.

Large industries determine the trend in industrial term loan growth

Large-scale industries (LSI) account for the major share of industrial term loan disbursements (75.6 per cent of total term loan). This is followed by medium scale (MSI) (14.3 per cent) and small scale (SSI) industries (10.1 per cent). This composition has changed slightly in recent years because of targeted initiatives by the central bank to disburse more loans to the small and medium enterprise (SME) sector. As a result, the gap between SSIs and MSIs in terms of share of term loans has reduced since Q1 of FY2014-15. Until 2014, growth in term loan disbursements to different industry categories had maintained a consistent trend, however, this trend has somewhat reversed since Q1 of FY2014-15 (Figure 1.3). Although there has been a rise in the disbursement of term loans for LSIs in Q2 of FY2015-16, total disbursement

Figure 1.3
Growth in Disbursement of Industrial Term Loans



Source: Bangladesh Bank.

remains lower than that of Q2 of FY2014-15. SSIs, on the other hand, have received significantly higher amounts of term loans during FY2014-15 and FY2015-16 (growth in Q1 and Q2 in FY2015-16 has been 70.8 and 59.4 per cent respectively). Loan disbursements to MSIs has not shown any consistent trend over the corresponding period.

SME loan disbursement needs better targeting

Credit to SME-related activities has increased over the last few years, thanks to targeted initiatives for the disbursement of SME credit. Targets for 2014, 2015 and 2016 were Tk. 88,753 crore, Tk. 104,587 crore and Tk. 113,503 crore respectively. Growth in the disbursement of SME loans barring Q1 of FY2015-16 has been quite significant in recent years (Figure 1.4). According to Moazzem and Basak (2016), macro-level performance as regards disbursement of SME credit resonated with what local level SMEs actually experienced. Informal arrangements under which many SMEs at the local and district levels operated, lack of customised financial products and services in response to the demand of different cluster-based industries, in addition to a variety of other reasons, have all undermined the availability and access to SME credit. It is important to monitor whether the disbursed credit is being availed by the targeted groups and whether targeted activities correspond to the demands of SME entrepreneurs.

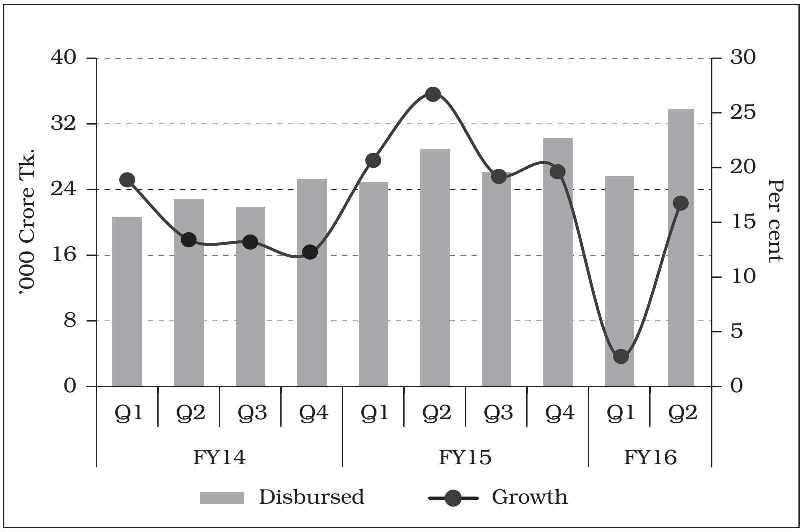


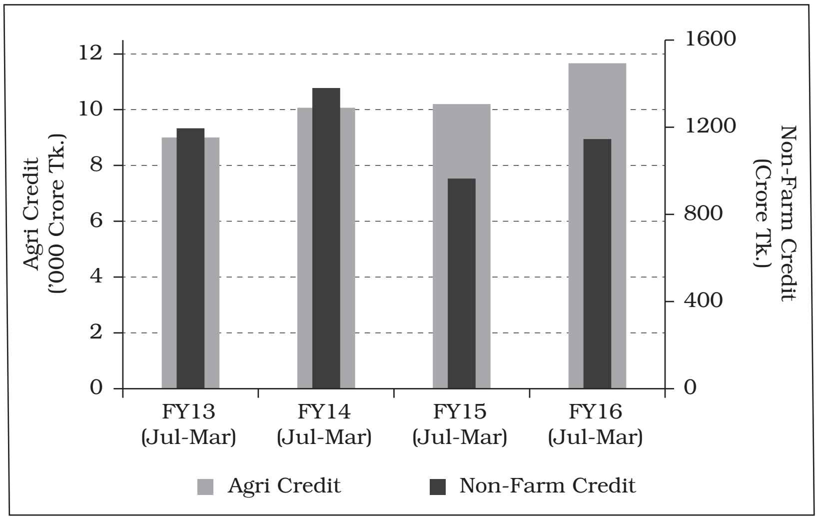
Figure 1.4
Quarter-by-Quarter Disbursement and Growth of SME Loans

Source: Bangladesh Bank.

Credit to the agricultural sector should be supplemented by targeted post-harvest support

Disbursement of credit to rural areas, particularly in agriculture and non-farm activities, has maintained a moderate level of growth over the recent years. While disbursement of agricultural credit has increased consistently during the FY2010-11 to FY2014-15 period, growth of non-farm credit failed to keep pace. During the July-March period of FY2015-16, a total of Tk. 11,667.7 crore was disbursed as agricultural credit, and Tk. 1,144.7 crore was disbursed as non-farm credit; these amounts were 14.4 per cent and 18.8 per cent (respectively) higher compared to that of the previous year (Figure 1.5). Sluggish growth in the disbursement of credit in FY2014-15 has partly contributed to this year's only moderate rise. Given the high production cost against the depressed price in the harvesting season, special efforts should be taken by the central bank to reduce commercial bank's lending interest rate for agricultural credit (the current rate is 9.68 per cent per annum). Government's various initiatives (including disbursement of credit) have facilitated pre-harvest stages of agricultural production. However, given the depressed price in the harvest season, as observed both in the recent past and today, targeted post-harvest measures are needed. This is particularly pertinent in order to ensure a fair price for farmers and the efficient marketing of agricultural

Figure 1.5
Disbursement of Agricultural and Non-Farm Credit



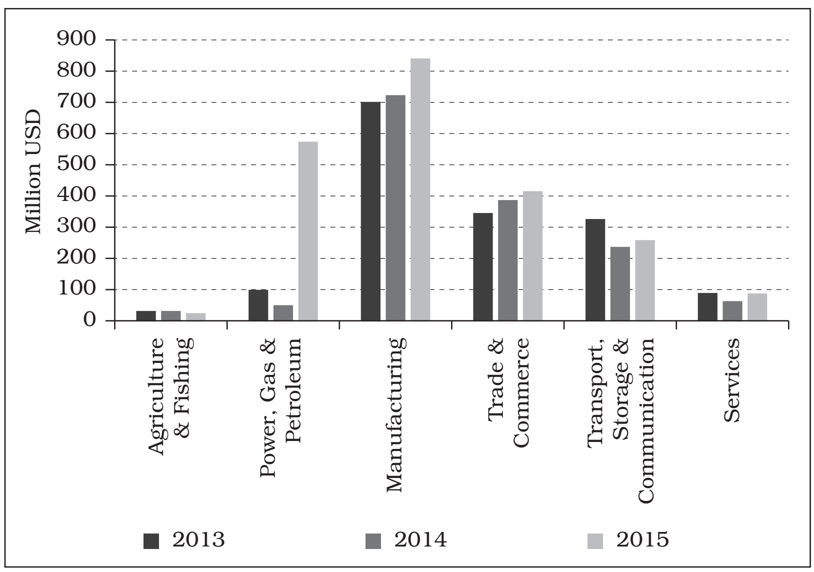
Source: Bangladesh Bank.

products both in domestic and foreign markets. In view of the emergent situation concerning agricultural price and profitability, CPD (2016a) has suggested that an Agriculture Price Commission be established to identify measures to address these concerns.

The changing composition of FDI should be supported through appropriate pre-establishment measures

Unlike domestic private investment, FDI has registered a considerable level of growth during 2015 (January-December). For the first time, inward flows of FDI surpassed the USD 2 billion mark in 2015 (USD 2,235 million), which was 44 per cent higher compared to 2014. Further, according to Bangladesh Bank data, during July-February 2016, FDI flows reached USD 1,450 million, which was 27.2 per cent higher compared to the same period of the previous year. A cross-sectoral analysis reveals that FDI flows in recent years have been directed more to manufacturing, trade and commerce-related activities (Figure 1.6). Given the labour-intensive nature of most manufacturing activities, this trend is a positive one from the point of creating more job opportunities for professionals and skilled workers. After sluggish growth in earlier years, a significant jump in FDI inflows in the power, gas and petroleum sectors in 2015 transmitted a positive signal to the gas-starved energy sector. New investment is expected to go towards exploration of

Figure 1.6
Net FDI Inflows in Selected Sectors



Source: Bangladesh Bank (various years).

new gas fields. A large share of recent FDI is actually reinvestment by existing companies, which may be taken as a positive sign since it is perhaps indicative of the growing confidence of foreign firms to continue to do business in Bangladesh. On the other hand, a deceleration in the contribution of equity capital in the total share of FDI inflows is indicative of the continuing hesitance on the part of new investors to invest in Bangladesh. In view of this, more emphasis needs to be put on addressing pre-establishment barriers that faced new foreign investors who would otherwise be willing to set up business in Bangladesh.

The registration of new investment indicates a mixed scenario. The level of registrations of new entities has slowed, both in the case of local and foreign entities, during 2015, from 1,676 in FY2012-13 to 1,429 in FY2014-15. On the other hand, over the corresponding period, the total amount of registered investment in 2015 has in fact increased from USD 8,332 million to USD 12,715 million (Table 1.4). However, during January-March 2016, both the number and amount of investment has risen compared to that in the same period of the previous year. The average size of proposed investment was larger for local investors compared to that of foreign ones.

Table 1.4

Number and Value of Local and Foreign Investment Registrations

(Million USD)

Period	Indicator	Local Investment	Joint & 100% Foreign Investment	Total
FY2013	Number of projects	1457	219	1676
	Proposed investment	5,599.0	2,733.0	8,332.0
	Proposed investment/project	3.8	12.5	16.3
FY2015	Number of projects	1309	120	1429
	Proposed investment	11,683.1	1,032.4	12,715.6
	Proposed investment/project	8.9	8.6	17.5
Jan-Mar, 2015	Number of projects	336	24	360
	Proposed investment	3,148.3	134.0	3,282.3
	Proposed investment/project	9.4	5.6	15.0
Jan-Mar, 2016	Number of projects	409	35	444
	Proposed investment	3,975.8	314.4	4,290.2
	Proposed investment/project	9.7	9.0	18.7

Source: Board of Investment (BoI).

1.2.3 The Declining Role of Private Investment in GDP Growth

An analysis of incremental contributions by different sectors towards GDP growth in FY2015-16 shows that the services sector has maintained its leading position as a contributor to GDP growth. In recent years, public administration, education and health services have been making an increasingly large contribution to GDP growth (Table 1.5). On the other hand, the contribution by wholesale and retail trade has decreased, while the contribution by financial intermediaries has remained stagnant. The contribution by industries sector has increased at a modest pace, while that of agriculture has decelerated. The rising contribution to GDP growth by the services sector has originated in those sub-sectors that are relatively less capital-intensive in nature (e.g. public administration and education). Given the role of services sector-led GDP growth (on account of mainly public sector services), yet sluggish growth in investment in the manufacturing sector, the role of private investment in GDP growth is becoming rather weak.

A major share of private investment originates from the manufacturing sector. In the manufacturing sector, apparels and textiles account for the major share of fixed assets, with a share of 48.3 per cent in total fixed

Table 1.5

Incremental Contribution to GDP Growth in the Last Five Years

(in Per cent)

Sector	FY12	FY13	FY14	FY15	FY16 (P)
Agriculture	0.52	0.41	0.70	0.53	0.40
Industries	2.47	2.59	2.27	2.74	2.95
Manufacturing	1.69	1.80	1.60	1.93	1.99
Services	3.43	2.88	2.92	3.00	3.44
Public administration and defense	0.24	0.21	0.22	0.32	0.53
Education	0.16	0.13	0.16	0.17	0.30
Health and social works	0.07	0.09	0.09	0.09	0.15
Wholesale and retail trade; repair of motor vehicles, motorcycles and personal and household goods	0.42	0.28	0.23	0.25	0.21
Financial intermediations	0.28	0.28	0.29	0.29	0.29
GDP growth	**6.52**	**6.01**	**6.06**	**6.55**	**7.05**

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

Note: P denotes provisional estimates.

assets of the manufacturing sector (BBS, 2013). The clothing and textiles sectors are therefore leading new investment in the manufacturing sector and creating new fixed assets. Lack of adequate infrastructural facilities, including the quality supply of electricity and gas (see below), the relatively high rate of interest (as mentioned in Box 1.1 in the following sub-section) and slow global recovery indicate that new investment in the apparels sector has been rather slow. Apparels enterprises in the recent times have been undertaking major restructuring initiatives where significant amount of investment is required. Given the significant resources needed and the difficulty in accessing the necessary infrastructural facilities, some entrepreneurs are yet to make good progress in this regard. According to the Bangladesh Garment Manufacturers and Exporters Association (BGMEA), a total of 618 factories have closed down in the last three years, while 250 new factories have been set up with state of the art technologies and better compliance assurance. Further, FDI inflows to the apparels and textile sector has been rather discouraging.

Although gas supply has risen in recent times, the industrial sector has not benefitted much from this. Instead, the sector has experienced a decline in the supply of gas (from 4.5 per cent in FY2013-14 to 4.1 per cent in FY2014-15) (Table 1.6). In contrast, the supply of gas to household activities has increased (from 13.2 per cent in FY2013-14 to 16.4 per cent in FY2014-15). Additionally, electricity supply has also failed to meet the growing demand. As a consequence, entrepreneurs have been discouraged to set up new enterprises.

Table 1.6

Growth in Consumption of Gas by Selected Consumer Groups

(in Per cent)

Year	Captive Power	Industry	Household	Total
FY2012	2.44	5.65	2.13	4.63
FY2013	8.02	5.80	0.57	6.37
FY2014	7.16	4.52	13.15	3.75
FY2015	4.37	4.11	16.38	5.94

Source: Petrobangla.

1.2.4 Growing Private Sector Confidence as regards Investment Prospects: CPD Rapid Assessment Survey, 2016

During February-April 2016, CPD conducted an entrepreneurs' perception survey as regards current issues of concern and interest relating to the Bangladesh economy. Attitudes about the business environment improved in 2016 compared to 2015. About 37.1 per cent of all respondents indicated positive changes in the business environment in 2016, with 33.3 per cent stating the opposite. While this was an improvement on 2015, the positive attitude was weaker than in 2014, which was the first year of the government following the elections in 2014 (Table 1.7).

Table 1.7

Perception Survey on Investment, Demand and Infrastructure (% of Total Respondents)

Question	Comment	2014	2015	2016
The investment environment in Bangladesh will	Deteriorate	35.6	61.4	33.3
	Indifferent	23.3	18.2	29.6
	Improve	41.1	20.5	37.1
How do you assess the possible changes in the demand for your firm's product during 2016?	Poor demand	20.3	32.6	11.3
	Indifferent	25.0	27.9	35.8
	High demand	54.7	39.6	52.8
What is the plan/projection as regards your firm's investment?	No investment	36.4	44.2	13.5
	Indifferent	25.8	25.6	26.9
	High investment	37.9	30.3	59.6
Do you think that initiatives for developing the land and other necessary infrastructure and utilities in the SEZs would meet the need of the investors?	Not at all	-	-	16.1
	Indifferent	-	-	16.2
	To a great extent	-	-	67.7

Source: CPD Rapid Assessment Survey, 2016.
Note: '-' denotes data not available.

The positive changes in attitudes noted above related to demand for firms' products. About 52.8 per cent of all respondents were confident about high demand for their product in 2016. This compares to 39.6 per cent in 2015 and 54.7 per cent in 2014. The majority of business executives (67.7 per cent) were very confident that the newly established SEZs will provide the necessary infrastructural support to new investment. About 59.6 per cent of entrepreneurs mentioned higher level of investment during the 2016 calendar year, compared to figures of just 37.9 and 30.3 per cent in 2014 and 2015 respectively. This is indicative of the private sector's confidence and their willingness to commit resources to investment. However, it also transpires from the survey that this confidence is contingent on the government's ability to deliver on promised services, such as setting up SEZs, and better access to gas, energy and other infrastructure.

Box 1.1

Factors Affecting Private Investment in Developing Countries: The Case of Bangladesh

A panel regression exercise covering 65 developing countries (screened on the basis of data availability) was carried out to identify the determinants of private investment. The dependent variable was investment per capita (at 2005 prices), and the regressors included real interest rate, previous year's income per capita, taxation rate, and a number of institutional variables including government effectiveness, law and order, regulatory quality, etc. It was found that only three of the variables were significant with expected signs – these included real interest rate (negative), previous year's income per capita (positive), and law and order (positive). Not only did law and order reveal a positive causation, its magnitude was also found to be somewhat significant. As such, improving law and order in Bangladesh will lead to a significant increase in per capita investment.

(Box 1.1 contd.)

(Box 1.1 contd.)

The exercise attempted to estimate what would be the outcome if law and order in Bangladesh was similar to a number of selected countries. It was found that if Bangladesh's law and order was similar to that of Sri Lanka, private investment in Bangladesh would rise by up to 33 per cent. If law and order was akin to that of India, private investment would in fact more than double. The rule of law therefore emerges as a highly significant factor in driving private investment, which in turn is crucial for ensuring high growth.

According to CPD's Rapid Assessment Survey 2016, entrepreneurs have demanded regulatory and policy changes in a number of different areas (Box Table 1.1). Approximately 28 per cent asserted the need for amendments in rules and regulations, and reforms of related institutions; 24.7 per cent stated the need for changes in fiscal policies (taxation, including value added tax (VAT)), 19 per cent highlighted the need for improvements in governance, while a further 15 per cent mentioned infrastructural improvements. The government should give high priority to transparency and accountability, reforming public services and the judicial system, reducing corruption, and improving the public procurement system, amongst others. The proper zoning of land and the establishment of SEZs across the country were both also highlighted as important.

Box Table 1.1
Areas of Concern

Areas and Issues	Responses (%)
Regulatory issues and related institutions	28.0
Fiscal policies (taxation, including VAT)	24.7
Governance	19.4
Infrastructure (land, transport, technology and energy)	15.1
Foreign exchange regulation	7.5
Financial access and service	5.4

Source: CPD Rapid Assessment Survey, 2016.

When top executives were asked about skills that are missing when they are looking for new employees, they stated that their biggest concerns related to lack of personal qualities (e.g. work ethic, confidence, leadership, being proactive, being innovative, etc.) (Box Table 1.2). Shortage of technical skills (need-based skills, information technology (IT), researchers, engineers, etc.) was the second highest concern for those surveyed. Lack of communication skills, particularly lack of English language proficiency among fresh graduates, was also highlighted as a major concern.

Box Table 1.2
Skills Lacking among Young Job-Seekers

Areas of Concern	Responses (%)
Personal qualities	34.2
Technical knowledge	24.8
Communication	19.7
Creativity and critical thinking	12.0
Experience and training	9.4

Source: CPD Rapid Assessment Survey, 2016.

1.3 FORMULATING FISCAL AND BUDGETARY MEASURES FOR FY2016-17

1.3.1 Revenue Mobilisation

Following a meeting of the Budget Monitoring and Resource Committee (BMRC), it was indicated that the revenue target for FY2015-16 was to be slashed by approximately Tk. 31,443 crore (including Tk. 26,370 crore for the National Board of Revenue (NBR)) in the revised budget (CPD, 2016b). Indeed, this drastic revision became inevitable in view of the realities on the ground. In the first six months of FY2015-16, total revenue collection posted a growth rate of 15.8 per cent against the annual target of 42.8 per cent.[5] CPD (2016b) expressed the apprehension that the year-end revenue collection in FY2015-16 was likely to be about Tk. 6,500 crore less than the recently revised target for FY2015-16, if appropriate measures were not put in place to address the emerging constraints. In view of the situation, NBR has put in an extra effort to infuse momentum in revenue collection in the last two quarters of FY2015-16. According to NBR data, revenue collection growth was 15.9 per cent during the first nine months (July-March) of FY2015-16 (compared to 14.9 per cent in FY2014-15).[6] There are indications that for FY2016-17 the revenue growth target may be set at 37.3 per cent over the revised target for FY2015-16. Therefore, the actual growth target for FY2016-17 (accounting for the possible shortfall over the revised target) may turn out to exceed the 40 per cent threshold. Reaching this target is expected to be yet another uphill task, with success being highly doubtful.

Concerns relating to the small tax base, low tax compliance and widespread tax evasion have continued to plague revenue mobilisation in Bangladesh. In this backdrop, options other than a serious revamping of the revenue mobilisation efforts and making this a policy priority are rather limited. In this regard, CPD (2016b), in its second interim report for FY2015-16, has put forward a number of proposals, including changes in the current advance income tax (AIT) collection system through progressive withholdings-at-source tax rates, introduction of the Benami Property Bill, and strengthening the Transfer Pricing Cell. The achievement of the FY2016-17 revenue target will depend largely on amendments and implementation of the VAT [value added tax] and SD [supplementary duty] Act. Regrettably, while this reform agenda is being debated, it remains the case that no clear stance has been taken by the government to date.

Amendments/implementation of the VAT and SD Act

The new VAT and SD Act 2012 is to come into force on 1 July 2016 with a uniform rate of 15 per cent for almost all goods and services.[7] However, the gap between government and other relevant stakeholders concerning implementation of this Act is yet to be bridged. In view of prior consultations with key stakeholders, the government had established a Joint Committee in October 2014 that had included both representatives from the NBR and the Federation of Bangladesh Chambers of Commerce and Industry (FBCCI). The Committee's mandate was to deliberate on views and suggestions emerging from these consultations, particularly those voiced by the business community. As is known, the business community had called for a number of amendments to the Act. The Committee agreed to some of the suggestions voiced by the stakeholders.[8] However, no follow-up steps have been taken, despite the date for presentation of the FY2016-17 budget soon approaching.

The Act envisages a number of significant changes, including abolition of the truncated rates. At present, there are at least 20 service items where VAT is applied at truncated rates (see Annex Table 1.1). Applying

[5]Revenue collections from all major sources were well below their respective targets. Income tax collection growth was particularly low during the first half of FY2015-16, being at its lowest level for 14 years.

[6]It does, however, need to be recognised that there is a large discrepancy between the data provided by the NBR and the Ministry of Finance (MoF) (CPD, 2016a) – in FY2014-15, this discrepancy was to the tune of Tk. 12,765 crore. On a positive note though, the NBR has recently initiated steps to reconcile such discrepancy.

[7]There are some exempted supplies and some zero-rated supplies. The exempted supplies and imports include the supply of the following services in relation to social welfare activities (if the services are provided by a government entity or an approved charitable institution (trust or *wakf*)): (a) healthcare and medical services; (b) education and training; and (c) childcare activities and residential care facilities for the aged, poor, infirm, or disabled persons who require permanent care. A zero-rated supply applies only to the supply of: (a) immovable property (if the land to which the immovable property relates is outside Bangladesh); (b) goods for export; and (c) zero-rated services (excluding health and education services).

[8]The Committee agreed to raise the limit of turnover tax for eligible traders, businesses and manufacturers; and provide differential treatment to small traders, businesses and some specific sectors who were to pay VAT at a reduced rate (these will not be eligible to enjoy input VAT credit).

a universal rate on these items will see a sharp rise in applicable tax, and therefore in the price of these services. The resultant price rise of some commodities and services will have spillover impacts on the economy, including on inflation. For example, consumers are currently paying VAT at the rate of 5 per cent on electricity bills. If the new Act is implemented without any amendments, consumers' electricity bills (for equivalent amount of usage) will increase by about 9.5 per cent from 1 July 2016. This is a significant rise in one year. In the same vein, at present, manufacturers are paying Tk. 825 as VAT for each ton of iron rod based on a tariff value system (specific tax), which comes to only about 2 per cent. Under the new Act, if a manufacturer cannot produce documents for VAT credit and apply the 15 per cent VAT on consumers, cost of construction, including public infrastructure, will increase.

As is known, the new Act will introduce an integrated online system for VAT registration, returns submission, refund and payment. This requires the development of necessary (soft and hard) infrastructure, human resources and skills development, training of VAT officials, and the preparation of relevant stakeholders as regards compliance. Indeed, to date, the business community, particularly small business enterprises, have very little knowledge regarding this. Further, the new automated VAT process requires testing that has not been done as yet.

Without addressing the aforementioned concerns, it will be difficult to implement the new Act from July 2016. It may also be recalled here that the Joint Committee of the NBR and the FBCCI has also proposed further amendments, a number of which are critically important. These include imposing a 4 per cent VAT on the supply value for the service sector; differential treatment of bargaining shops; and reduced VAT on a number of commodities, including iron and steel.

The proposed VAT and SD Act will also need to be reconciled on an urgent basis. To this end, the recommendations of the Joint Committee should be addressed without delay. In this regard, all preparations need to be conducted in a coordinated manner with the participation of stakeholders and tax officials, at various levels. If it demands, a 2-3 year plan may be developed to implement this Act in a realistic and staggered manner.

Reform in the advance income tax (AIT) collection system

As of now, no formal registration system exists for AIT withholding entities with the NBR. Greater transparency and higher tax mobilisation at source could be achieved through an integrated identification mechanism that links all aspects of the taxpayer's finances, to be achieved through linking of the e-TIN (taxpayer identification number) with the involved party's national ID and/or business identification number (BIN).[9] Towards this end, the experience of India could serve as a useful example for Bangladesh (see Box 1.2).

Box 1.2

AIT Collection System in India

Advance income tax in India refers to paying a part of the taxes due before the end of the fiscal year, if the concerned tax liability is more than Rs. 10,000 (Batra, 2016). Ideally, this amount should be paid in the year in which the income is received, and has to be paid on 15th day of September, December and March in instalments of 30 per cent, 30 per cent and 40 per cent respectively for self-employed persons and businessmen. Companies, however, need to pay by the 15th day of June, September, December and March. For salaried employees, AIT is not applicable as the employer deducts tax at source (TDS). The tax deducted at source by the payer is to be deposited in the income tax department account. AIT is, however, applicable to an individual when s/he has sources of income other than his/her salary.[10] Similarly, tax collection at source (TCS) arises

(Box 1.2 contd.)

[9] In addition, CPD (2016b) also called for the introduction of progressive withholdings-at-source tax rates.

[10] Examples include when an assessee earns income through capital gains on shares, capital gains on house property, interest on fixed deposits, winnings on lotteries, etc.

(Box 1.2 contd.)

for the seller of goods, with tax in this situation being collected[11] at the source of the income itself. Any individual who collects the tax has to present a certificate that specifies if the tax has been collected, the amount collected and the rate of tax applied. This information has to be presented within 10 days from the date of debit or receipt of the amount to the buyer. The taxes collected must be dispatched to the income tax department's account.

For TDS/TCS returns, an individual needs to quote a Tax Deduction and Collection Account Number (TAN)[12], which can be applied for using 'Form No. 49B' (under the Indian Income Tax Law) and submitted to any of the TIN facilitation centres that are responsible for the receipt of e-TDS returns. TAN is assigned by the Income Tax Department based on the application submitted to the TIN Facilitation Centres, which is managed by National Securities Depository Limited (NSDL). A TAN is required for all TDS/TCS returns, all TDS/TCS payment challans and certificates that are issued. TDS/TCS returns will not be accepted by banks if a TAN is not quoted. A penalty of Rs. 10,000 is applicable in the case of failure to apply for a TAN or failure to quote a TAN in the specified documents.

It is worthwhile noting that if the amount paid as advance tax is higher than the total end tax liability, there is the possibility of receiving a refund for the overspend. For instance, if the assessee has paid more than 10 per cent of the tax liability, then the assessee is entitled to receive interest at 6 per cent per annum, paid by the Income Tax department, on the excess amount.

Strengthening the Transfer Pricing Cell to reduce illicit financial flows

Global studies indicate that, between 2004 and 2013, about Tk. 44,000 crore (6.2 per cent of current GDP) was siphoned out from of Bangladesh annually, while over Tk. 76,000 crore (6.3 per cent of current GDP) was taken out from the country in 2013 alone (Kar and Spanjers, 2015).[13] Globally, international institutions, such as multinational corporations (MNCs), have been found guilty of misreporting transfer prices in order to keep their tax burdens low. This phenomena has now caught up with Bangladesh. In view of this, the Transfer Pricing Cell of NBR should be further strengthened and steps should be taken so that the Cell has access to global platforms and databases for tracing and tracking illicit flows and misinvoicing by MNCs and other business enterprises. The recent Panama Papers scandal, coupled with information provided earlier by Swiss banks, calls for an appropriate investigation to be conducted by concerned authorities in Bangladesh so as to stem illicit financial flows from the country (CPD, 2016b).

Introduction of the Benami Property Act

Recent information indicates that the underground economy (or black money economy) is quite entrenched and to a significant degree for a developing country of Bangladesh's size. Added to this, the number of taxpayers is rather small and tax avoidance is widespread. These factors of course hurt the economy particularly through lower revenue generation. A large part of the money that flows out of the country is through various forms of illicit financial flows[14], aided by high levels of corruption. As is known, in the past, legalisation of undisclosed income has, from time to time, been permitted in Bangladesh. As mentioned earlier by CPD (2016b), under Sections 19B and 19C of the Income Tax Ordinance (1984), special tax treatment was allowed for investments in real estate, as well as also in some other sectors[15] of the economy. These provisions, however, had only insignificant success. In view of this past record, there is no justification to continue with such practices. In this backdrop, CPD recommends the introduction of a Benami Property Act to bring undeclared assets within the purview of tax authorities.

[11]The tax is collected at source from the buyer, by the seller, at the point of sale.

[12]A TAN is a 10 digit alphanumeric number issued to persons who are required to deduct or collect tax on payments made by them under the Indian Income Tax Act 1961.

[13]In the case of Bangladesh, the major share of illicit flows results from trade mispricing (Kar and Spanjers, 2015).

[14]According to Global Financial Integrity (GFI) report 2015, Bangladesh ranks 26 out of 149 countries, with an average illicit financial flow of USD 5,588 million (2004-2013).

[15]Investment in government treasury bonds (10 per cent tax) or investment in productive income-generating sectors (10 per cent penalty and regular 25 per cent tax).

A similar law has been enforced in India, which Bangladesh policymakers may consider following. The Indian Benami[16] Transactions (Prohibition) Act 1988 was fist enacted on 5 September 1988.[17] However, this Act could not be implemented due to the absence of an appellate mechanism and lack of provisions for vesting of the confiscated property. The Act was further amended on 13 May 2015, with the introduction of relevant authorities for purposes of this Act. These included: (i) an Initiating Officer; (ii) an Approving Authority; (iii) an Administrator; and (iv) an Adjudicating Authority. In addition to this law, India has introduced another Act, the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act 2015, which targets the financial wealth hidden abroad by persons resident in India.

The Act seeks to particularly target the real estate sector, in which individuals hold black money in the form of benami property and generate black money in the domestic arena.[18] Movable property, such as gold and company stocks, would also come under the purview of benami transactions. It also seeks to ensure that if any individual enters into such transactions for the purpose of tax evasion or to avoid payment to creditors, the ultimate beneficiary owner, as well as individuals who assist or encourage the individual to undertake such transactions, will face penalties. The penalties imposed are quite severe – if it is proven that someone was involved in such transactions, then the person would face imprisonment (for a minimum of one year and a maximum of seven years), in addition to a fine of up to 25 per cent of the fair market value of the property. If any individual who is required to provide information under this Act knowingly furnishes false information, s/he will also face imprisonment (for a minimum of six months and a maximum of five years), along with a fine of 10 per cent of the fair market value of the property (Jain, 2015).

The Initiating Officer may initially issue a notice to any individual whom s/he considers to be a benamidar[19] as to why the property should not be considered benami. Afterwards, the property may be attached[20] for a period of 90 days from the date of notice. The Investigating Officer in charge gathers evidence and then passes an order (within 90 days from the date of issue of the notice) with preceding approval of the Approving Authority. If, for instance, an order is passed in favour of continuation of holding of the property in question, the Initiating Officer's next task would be to refer the case to the Adjudicating Authority. The Adjudicating Authority would then issue notice and pass an order as to whether or not to hold the property as benami. If an order to hold the property as benami is made, then a confiscation order is to be issued. All title and rights to such benami property shall then be vested in the Central Government, free of all encumbrances, whilst the Administrator is tasked with the management of the property. There is also scope to hear appeals against the order passed by the Adjudicating Authority through the Appellate Tribunal. The Appellate Tribunal is made up of a Chairperson and at least two other Members (both a Judicial and an Administrative Member).

One criticism of the new Act is that it makes the manager of a company (defined per the Companies Act 2013) liable for tax recovery. For any offence under this Act, all responsible individuals serving the company have to prove that the offence was committed without his/her knowledge, otherwise s/he will be held accountable and punished. Also, determination of the fair market value has proven to be challenging (Thakurta, 2015).

Although in Bangladesh there is already mentions of a prohibition of benami transactions in Chapter III of the Land Reforms Ordinance 1984 (under the title Prohibition of Benami Transaction of Immovable Property), this alone is not enough to tackle and prevent illegal activities. The upcoming budget session

[16]*Benami* is used to define a transaction in which the real beneficiary is not the one in whose name the property is purchased. As a result, the person in whose name the property is purchased is just a mask for the real beneficiary.

[17]Not applicable for the state of Jammu and Kashmir in India.

[18]In India, misuse of public trust funds is often used to create benami property. This is possible because information on such funds is not compiled in a centralised repository.

[19]The person in whose name the benami property is held or transferred.

[20]The prohibition of transfer, conversion, disposition or movement of property, by an order issued under this Act.

may like to address this issue, with the Law Ministry and the Parliament Standing Committee discussing the introduction of a suitable a Bill in this regard.

1.3.2 Public Expenditure

Redesigning the public expenditure framework

The public expenditure framework needs to be redesigned to make effective use of the policy space in FY2016-17. Growth of public expenditure in the early months of FY2015-16 was well below target. Expenditure for the two major sources of non-development spending, which are 'Subsidies and Current Transfers' and 'Interest Payments', was well within the limit during July-December of FY2015-16. Expenditure for the Annual Development Programme (ADP) was also lower than the past trends of low rate of implementation. In addition, by December 2015, the government had disbursed Tk. 1,200 crore for the purpose of recapitalising state-owned commercial banks (SCBs), with most of this money going to the "scam-hit" BASIC Bank. As may be recalled, Tk. 5,000 crore was set aside in the budget for FY2015-16 for recapitalistion.[21] Further, the government has indicated that Tk. 500 crore may be given to a few banks from the remaining allocation. However, BASIC Bank has again sought Tk. 2,600 crore afresh to meet its capital requirement under Basel II for FY2016-17.

Lower subsidy demand will provide greater fiscal space in the next fiscal year

Subsidies are set to be reduced by about 26 per cent in the revised budget for FY2015-16, thanks to the fall in fuel and fertiliser prices in the international market – this will provide some fiscal space to the government for the upcoming budget. Thanks to the drastic fall in international fuel prices, Bangladesh Petroleum Corporation (BPC) continued to make profit in FY2015-16, as it had done previously in FY2014-15. BPC will not be in need of further subsidy in FY2016-17, which releases some of the pressure on the upcoming budget.[22] Furthermore, since fuel prices fell and electricity prices at the retail level increased, the government was able to cut subsidies in these areas. The allocation for subsidies in the revised budget has been slashed to Tk. 18,940 crore, which is 1.1 per cent of GDP (1.8 per cent of GDP in FY2014-15) (Figure 1.7), and 6.4 per cent of the revised budget for FY2015-16 (10.9 per cent in the revised

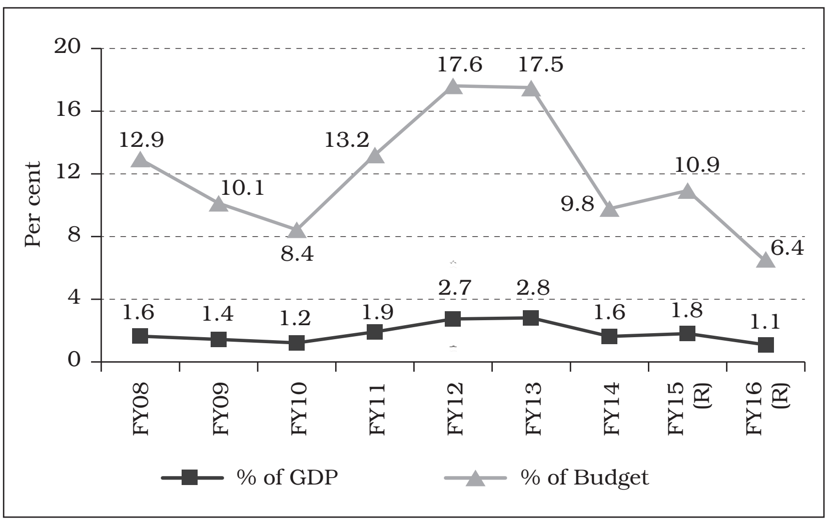


Figure 1.7
Subsidies as a Per Cent of GDP and Budget

Source: Compiled from Ministry of Finance (MoF) data and various newspapers.

[21] In FY2014-15, the government spent Tk. 1,716 crore on this account.
[22] Subsidy allocation to the tune of Tk. 800 crore was kept for BPC in the original budget for FY2015-16. This has been withdrawn in the revised budget of FY2015-16.

budget of FY2014-15). Subsidy allocation has begun to fall since FY2013-14, both as a per cent of GDP and that of budget, reaching its lowest levels in the last nine years.

Recently administered price adjustments of petroleum products

It may be recalled here that CPD's earlier analysis (2016a) revealed that a reduction in the administered prices of petroleum products will be of benefit to the economy by way of raising the GDP, creating employment opportunities and containing inflation.[23] In adjusting the fuel prices, CPD in January 2016 had called for relatively lower reductions in the prices of petrol and octane compared to diesel, furnace oil and kerosene, on the basis of equitable considerations. As may be recalled, the government has stayed away from downward adjustments of administered prices of petroleum products in the domestic market for a long time, so as to allow the BPC to repay its loans and recoup the losses it had incurred between the fiscal years of FY1999-00 and FY2014-15. In April, the government implemented cautious reductions in the prices of major petroleum products, ranging from 4.4 per cent to 10.4 per cent, approximately two years after the start of the global oil slump.[24] However, this type of price adjustment failed to generate any pass-through. For example, transport services have seen hardly any reduction (reduction of only 3 paisa/km). Further, agricultural famers were unable to benefit from this reduction in the Boro season. In addition, kerosene, used by around 10 per cent of poor households in Bangladesh as a source of fuel and lighting (BBS, 2011), has seen a reduction in price of only Tk. 3. The diesel price has reduced similar to kerosene, which will lead to higher subsidy demand for power in the upcoming budget. On the one hand, revenue will be generated from BPC, while on the other, subsidy as a per cent GDP is likely to rise. One option is to increase the price of electricity. In the upcoming budget, the government should clearly specify the future phases of fuel price reduction. To this end, the urgent disclosure and transparency of BPC finances is critical. At the same time, any adjustment as regards energy and electricity prices should be calibrated by taking into account the prices of all three related items (fuel, gas and electricity), overall impact of the price-change mix for major stakeholder groups, and the burden of government's subsidy-related expenditure.

Emphasise allocation to social sectors and implement National Social Security Strategy (NSSS) targets

Public expenditure for social sectors in Bangladesh is relatively low when compared to international standards. Indeed, Bangladesh is ranked 155th among 161 countries, and 189th among 190 countries as regards to its public spending (as a per cent of GDP) on education and health respectively.

Financial allocation toward securing the social safety net has failed to gain adequate attention in the budgetary framework in recent years (CPD, 2016a). Over the last five years, allocation for social safety net programmes (SSNPs), which also include pension-related expenditure for government employees, remained about 2 per cent of GDP – in the Sixth Five Year Plan (SFYP), the government's target was to increase the allocation to 3 per cent of GDP. As is known, the General Economic Division (GED) of the Planning Commission has recently prepared a National Social Security Strategy (NSSS).[25] In order to attain the GDP target level, the strategy document proposes to increase both allocation and coverage over the next five years (FY2015-16 to FY2019-20).

As can be observed from earlier trends, budgetary targets have failed to match the proposals set out in the NSSS. For example, allocation for the Old Age Scheme was Tk. 1,440 crore in FY2015-16, whereas

[23]Indeed, CPD estimates showed that a 10 per cent reduction in prices was likely to lead to 0.3 per cent gain in terms of GDP growth.

[24]The prices of octane and petrol have each been lowered by Tk. 10 per litre, to Tk. 89 per litre and Tk. 86 per litre respectively. The prices of diesel and kerosene have each been reduced by Tk. 3 in both cases. The government had earlier announced a reduction in the administered prices for fuel in three phases.

[25]The NSSS document has placed an emphasis on the need for a strong social security system in Bangladesh by following a 'life-cycle' approach (GED, 2015).

the equivalent NSSS target was Tk. 2,010 crore (see Annex Table 1.2). This is also reflected in the per month allocation given to the scheme's beneficiaries, as these beneficiaries receive lower than the amount proposed in the NSSS.[26] Following a meeting with the Finance Minister, it was recently agreed to increase the coverage of 18 SSNPs by raising the amount of funding allocated by over Tk. 1,000 crore for the upcoming FY2016-17.[27] This proposal is likely to raise the per month allocation of several major safety net programmes, but will still fall short of the NSSS targets.[28]

Comparing the NSSS target allocation to the budget allocation for FY2015-16, there was a significant gap of at least Tk. 570 crore for the old age allowance, Tk. 2,711 crore for child school stipends, Tk. 616 crore for the allowance dedicated to widowed women, and Tk. 720 crore for disability schemes. Even though the Government of Bangladesh (GoB) has planned to increase the per month allocation for these schemes, the total allocation will still be lower than the target level (as stated in the NSSS document). Similarly, comparing the NSSS financing target with the proposed budget allocation for FY2016-17, it appears that there will indeed be a financing gap.[29]

Government efforts for SSNPs are not only inadequate in monetary terms, but also from the perspective of coverage. For example, although the NSSS has proposed to increase the number of beneficiaries under the Old Age Scheme to 55 lakh by FY2017-18, according to the Medium Term Budgetary Framework (MTBF) for FY2015-16, it was expected to remain at 30 lakh in both FY2016-17 and FY2017-18. The number of beneficiaries for the Old Age Scheme is expected to be 31.5 lakh in the upcoming fiscal year (see Annex Table 1.3). While the coverage for widow's allowances is expected to rise to 11.7 lakh, this is still lower than the NSSS target of 32 lakh. The increase is not significant, although the proposed increase exceeds the MTBF projections. Similarly, while the number of eligible beneficiaries of the disability scheme is expected to be 7.5 lakh in FY2016-17, the target set in the NSSS is 10 lakh by FY2017-18.

Resource constraints is often given as one of the major reasons for the GoB's inability to provide adequate allocations for SSNPs that are aimed at the most vulnerable and marginalised groups. Curiously, over the last six years (between FY2010-11 and FY2015-16), the budget has never managed to reach the set target level. For example, in FY2014-15, the budget deficit was Tk. 9,893 crore lower than the target. The targets set by the NSSS may appear to be very ambitious, but the reality is that government spending and implementation fall far short of the necessary levels.

ADP expenditure against allocation in FY2015-16 is the lowest in recent years

ADP expenditure has not experienced any significant breakthrough in FY2015-16. Indeed, performance has in fact deteriorated, with growth in FY2015-16 being the lowest registered in recent years. According to the year's first ten months' data, actual ADP spending was 46.5 per cent of the originally planned allocation of Tk. 97,000 crore. This is the lowest level of expenditure since FY2008-09. Expenditure on both Taka (47.9 per cent) and project aid (43.9 per cent) was at its lowest since FY2007-08 and FY2011-12 respectively. When ADP was subsequently revised in April 2016, a number of sectors (including agriculture; water resources; oil, gas and natural resources; transport; communication; health, nutrition, population and family welfare; public administration; and science and ICT) were subjected to significant cuts due to the slow rate of implementation. ADP for FY2015-16 was slashed by Tk. 6,000 crore (or 6.6 per cent) to just Tk. 91,000 crore. Project aid was reduced by Tk. 5,340 crore (or 15.5 per cent), while the GoB allocation was reduced

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[26]The NSSS target is to distribute Tk. 500 per month to the beneficiaries under the Old Age Scheme; however, in the budget this amount is currently fixed at Tk. 400 per month.

[27]At present, this amount is Tk. 5,364 crore.

[28]It is proposed to increase the Old Age Scheme to Tk. 500 in FY2016-17, whereas the NSSS target is around Tk. 650 for the corresponding fiscal year. Other than this, the widow's monthly allowance will also see an increase to Tk. 500 from the existing level of Tk. 400, whilst the allowance dedicated to financially-insolvent disabled persons will rise to Tk. 600 from the current level of Tk. 500.

[29]For FY2016-17, the expected gap is approximately Tk. 1,640 crore for the old age allowance, Tk. 1,339 crore for allowances to widowed women, and Tk. 1,370 crore for the disability scheme.

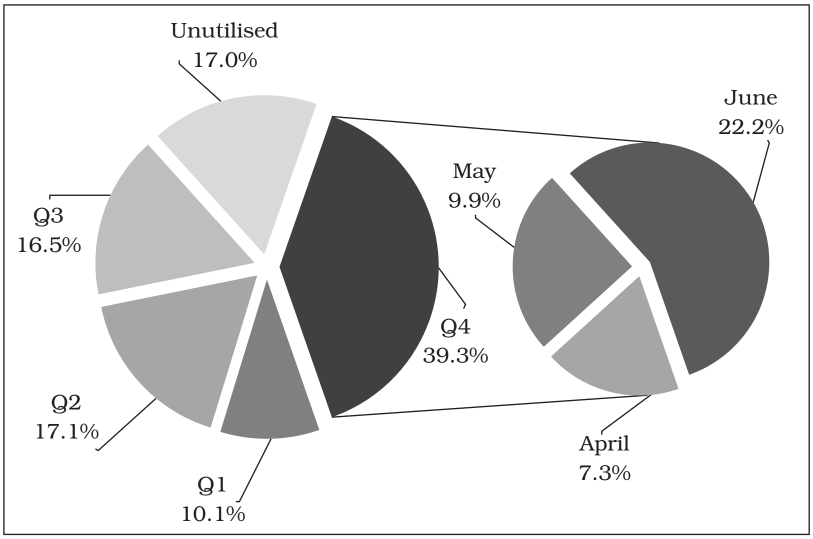
by only Tk. 660 crore (or 1.1 per cent). Given the ADP's implementation status, one would have expected a higher reduction in the ADP allocation. In addition, the number of unapproved ADP projects that receive allocation in the Revised ADP (RADP) has been rising over successive fiscal years. However, the reduction in total allocation has also been increasing in the RADP as compared to the ADP, which is contradictory. Some projects are included in the RADP due to political considerations, yet remain unimplemented due to inadequate resources – this deteriorates the overall quality of ADP planning.

The 'fourth quarter syndrome'

A chronic problem exists whereby low budget execution during the first three quarters of the financial year is followed by a large spike in expenditure in the final quarter (Q4), particularly in June. This raises questions regarding the quality of spending. Figure 1.8 shows that on average (FY2005-06 to FY2014-15) 39.3 per cent of total ADP expenditure is spent in Q4 (April-June), while only 10-17 per cent is spent in Q1-Q3. June (the final month of the fiscal year), alone contributes on average 22.2 per cent of spending, which is more than spending in any of the three previous quarters. It should also be noted that on average approximately 17 per cent of the total ADP allocation remained unutilised.

Figure 1.8

Quarterly Pattern of Actual ADP Implementation against Original Allocation (10-year average)



Source: Calculated based on Implementation, Monitoring and Evaluation Division (IMED) data.

The 'fast track' projects are not fast enough

The government has prioritised eight mega projects under the 'fast track' initiative. These include: Padma Multipurpose Bridge Project (PMBP), Dhaka Mass Rapid Transit Development Project (DMRTDP) (otherwise known as the Metro Rail project), 2x1200 MW Ruppur Nuclear Power Plant (RNPP), Matarbari 2x600 MW Ultra-Super Critical Coal-Fired Power Project (MUSCCFPP), 2x660 MW Maitree Super Thermal Power Project (MSTPP), an LNG (liquefied natural gas) gas terminal for importing liquid gas, and a Deep Sea Port in Paira, Patuakhali. A Deep Sea Port in Sonadia (Cox's Bazar) had also been planned, but that was recently scrapped. In May 2015, CPD (2015a) provided a detailed discussion on these projects.

In addition to the seven ongoing projects, two new projects were also included in the 'fast track' project list in a recent meeting of the Executive Committee of the National Economic Council (ECNEC), held in May 2016. These are the Padma Bridge Rail Link (PBRL) project and the Construction of Single Line Dual Gauge Track from Dohazari-Ramu-Cox's Bazar and Ramu to Gundum (near the border with Myanmar). The present analysis seeks to explore the current situation of these priority projects based on the available data, as a follow-up to the previous analysis.

Only four of the nine projects have received initial ADP allocation for FY2015-16. The present status of all the projects is as follows:

a. The PMBP made 34 per cent progress in financial terms up to the end of March 2015, while physical progress was 31 per cent. In addition, about 21 per cent of the main bridge construction was reported to be completed. This suggests that of the total project plan, only 5 per cent progress has been made in financial terms, and only 7 per cent progress in physical terms, during the first nine months of FY2015-16.
b. The DMRTDP achieved cumulative financial progress of 3.3 per cent up to March 2016, of which only 1.6 per cent progress could be made during the first nine months of FY2015-16.
c. The RNPP project reached 79.3 per cent cumulative progress in financial terms up to November 2015. However, 79.2 per cent of progress made occurred by June 2015, meaning that only 0.1 per cent could be added to the cumulative financial progress over the first five months of FY2015-16.
d. The MUSCCFPP is still in its early implementation phase and has attained only 0.9 per cent cumulative progress up to November 2015, having reached 0.8 per cent by June 2015.[30]
e. Based on the initial cost, the cumulative progress of the Dohazari-Ramu-Cox's Bazar and Ramu to Gundum Rail Track project (meter gauge) up to November 2015 was 16.9 per cent, meaning that the project is already well behind schedule.
f. The MSTPP's (Rampal power plant) main plant fencing work has already been completed. The project received allocation in the RADP for FY2015-16 for land development, protection and construction of boundary walls.
g. Construction of the LNG terminal in Maheshkhali is at a very early stage. Excelerate Energy Bangladesh Ltd, the joint venture company, is currently carrying out geophysical works.
h. ECNEC has recently approved Tk. 1,128 crore to develop the primary infrastructure and facilities to operationalise Paira Port. The feasibility study report of the project has already been submitted. Some limited scale infrastructure, such as a pontoon, crane and security building, have already been developed on a 16-acre piece of land. The remaining preliminary infrastructure works are scheduled to be completed by June 2018.
i. An agreement was signed between China Railway Group Limited and Bangladesh Railway on 28 January 2015 for implementation of the PBRL project.

Based on the assessment above, it can be concluded that the overall progress of the 'fast track' projects has been below target and has not met expectations (see Annex Table 1.4). Although four of the nine projects have seen visible progress, the majority of the projects are behind schedule, and there exists some degree of uncertainty (i.e. consider the example of Sonadia Deep Sea Port). As a result, from the perspective of project implementation, the distinction between 'fast track' projects and all other projects is unclear. It is yet to be seen whether a separate detailed budget for these projects, which is expected to be presented to the parliament alongside the national budget for FY2016-17, will help to accelerate the pace of implementation.

Intensive monitoring of priority projects that are close to completion should remain a priority

In view of the low level of private investment and significant infrastructural deficit, better (in terms of quality) and timelier implementation of the ADP, particularly that of growth-enhancing infrastructure projects, should remain a policy priority. CPD (2015b) selected a set of 26 ADP projects for FY2014-15 that were expected to help boost growth and employment one of which was fully implemented at a later date. CPD's second interim review of the state of the Bangladesh economy in FY2014-15 (CPD, 2015c) advocated for closer scrutiny and tracking of the progress of these projects. Share of allocation for these projects in the ADP for FY2015-16 was 17.6 per cent. Fourteen of these 26 projects were supposed to be completed in

[30]The project's land acquisition work was completed in August 2014. Other project components, such as the survey; the master plan layout, drawing, design, etc. for residential and township development; and the boundary pillar, are in progress.

FY2014-15 (or even earlier), however, the cost and completion deadlines of a number of these projects were revised – for some projects, this occurred more than once. Of these 14 projects[31], 13 were not completed in FY2014-15 and were carried forward into the FY2015-16 ADP (CPD, 2015d). Analysis of the progress of these 25 priority projects also suggests that the majority will not be completed in FY2015-16. Indeed, 23 projects were granted a time extension in the RADP of FY2015-16 (details in Annex Table 1.5).

Actual combined spending for these 25 projects was somewhat lower than the average for all ADP projects during July-March of FY2015-16, at 39.9 per cent compared to 41.1 per cent respectively. If these 25 projects are excluded, the rate of progress for all ADP projects improves only marginally to 41.4 per cent during the first ten months of FY2015-16. Further, within this group, performance has varied.[32] Only nine projects achieved more than a 41.1 per cent implementation rate, while for one project, the Mubarakpur Oil/Gas Well Exploration Project, implementation was zero during July-March of 2015. Only four[33] projects are closer to being completed.[34] However, aside from the 'Augmentation of Gas Production under Fast Track Program' project, the remaining three projects had a below average implementation record during July-March FY2015-16. It should also be noted that three out of these four 'could be completed' projects were carried over from previous years.[35]

In the case of the 10 projects that were supposed to be completed in FY2015-16 (as per the revised timeline provided in the RADP for FY2015-16, a total allocation of Tk. 8,771 crore was needed for timely completion. However, only Tk. 3,116 crore has been earmarked for these projects in the RADP for FY2015-16. Combined progress in financial terms as regards these projects up to March FY2015-16 was 56.8 per cent. Considering the revised allocation that was made for FY2015-16, there are at least four projects (Joydebpur-Mymensingh Road Development, Shahjalal Fertilizer Project, Mubarakpur Oil/Gas Well Exploration Project, and the Augmentation of Gas Production under Fast Track Program) that could perhaps be completed if a 'final push' could be given toward their completion. However, it appears that the majority, if not all, of these projects will not be completed according to their respective schedules and will have to be carried forward to the ADP for FY2016-17.

Escalating costs and time extensions have undermined overall ADP implementation

Cost and time overrun in the implementation of the ADP projects has become more pervasive in recent years. CPD analysis based on Implementation, Monitoring and Evaluation Division (IMED) data showed that of the 233 projects completed in FY2013-14, only 14.2 per cent projects were completed within the stipulated time and planned allocation. This is the lowest level since FY2000-01. About half (48.9 per cent) of the completed projects experienced time overrun, which is the highest amount since FY2000-01. This type of time overrun led to a 51.1 per cent increase in average cost of all completed projects, which is the highest in the last eight years.

Cost escalation and time extension also characterises flagship infrastructural projects. For example, the PMBP timeline has extended by 42.9 per cent due to successive revisions, which in turn led to an increase in the cost by 183.3 per cent (Table 1.8). Dhaka-Chittagong 4-lane project also faced cost escalation (77.8 per cent) and time extension (22.2 per cent), while the Joydebpur-Mymensingh Road Improvement Project

[31]Only one project, Construction of Haripur 412 MW Combined Cycle Power Plant and Associated Substation, was completed by FY2014-15.

[32]The standard deviation of these 25 projects is 48.1, which suggests a large variance in the execution rate of these projects.

[33]These include: Joydebpur-Mymensingh Road Development, Dhaka-Chittagong Railway Development Project, Shahjalal Fertilizer Project, and the Augmentation of Gas Production under the Fast Track Program.

[34]Considering the cumulative completion rate being greater than 75 per cent.

[35]These projects were scheduled to be completed within FY2014-15 as per their respective project timelines. The 'Production of Electricity by Co-generation and Establishment of North Bengal Sugar Mill' project has posted more than 100 per cent cumulative progress rate and exceeded the project cost before the timeline. The project has received allocation once more under the ADP FY2015-16.

Table 1.8
Cost and Time Overrun of Major Projects

Project	Cost (Crore Tk.)			Timeline (Years)		
	Initial Cost	Revised Cost	Increase (%)	Planned	Revised (Completion Expected)	Increase (%)
Padma Multipurpose Bridge	10,162	28,793	183.3	7	10	42.9
Dhaka-Chittagong 4-lane project	2,147	3,817	77.8	9	11	22.2
Joydebpur-Mymensingh Road Improvement Project (JMRIP)	902	1,815	101.2	3	6	100.0

Source: Compiled from Planning Commission data.

(JMRIP) experienced a 100 per cent increase in both cost and schedule. Such increases in cost and time reduce the efficacy of public investment and the private sector, with users being deprived of timely benefits. Due to non-completion of these projects within the stipulated time and cost, the crowd-in effect as regards private investment does not take place.

Furthermore, a significant number of projects in the top five sectors of the ADP, in terms of their total allocation share (65 per cent in FY2015-16), have seen time extension. These sectors include: rural development and institutions; power; transport; education and religious affairs; and health, nutrition, population and family welfare (see Annex Table 1.6). The transport sector experienced the highest increase (42 per cent), followed by power (28.8 per cent), health (28.3 per cent), rural development (26 per cent), and education (17.1 per cent). In addition, six out of the top ten power sector projects, which have the potential to add about 4,000 MW to the national grid, have experienced time extensions due to the slow pace of implementation.

Strengthening IMED by establishing follow-up mechanisms to support realisation of recent initiatives/ policy decisions

Recently the government has undertaken a number of initiatives to accelerate ADP implementation. A policy as regards the Project Preparatory Fund (PPF) that aims to facilitate timely and successful implementation of development projects has been drafted. The main objective of the PPF is to provide funds for completion of preliminary activities before the launch of any development project.[36]

One may recall that a number of proposals relating to expediting ADP implementation were announced last year by the Planning Minister. These proposals included: (i) appointing project directors through direct interviews by line ministries and divisions[37]; (ii) assigning a dedicated official to each government agency for the purposes of monitoring and evaluating projects; and (iii) delisting longstanding 'non-operational' projects from the ADP.[38] However, these have not been adequately followed up. It is recommended that the upcoming budget provides a report on progress made as regards these proposed actions.

As is known, the IMED provides a number of recommendations in annual progress reports, which are based on the challenges faced during the project cycle. However, these are often inadequately followed up with concrete measures. Regrettably, majority of these recommendations tend to be ignored by the relevant

[36]Preliminary activities include land acquisition, a feasibility study and an environmental impact assessment (EIA).
[37]Developing guidelines to this end was also planned.
[38]In this regard, it had been planned that the relevant ministries and divisions would be served letters on 1 October each year to send the list of non-performing projects to the Planning Commission.

ministries and divisions, as the IMED lacks legal authority to command compliance. These recommendations should be discussed and followed up in quarterly progress meetings so as to monitor the ADP progress. These proposals need to be implemented by the line ministries and other concerned entities.

1.3.3 Budget Deficit

Budget deficit financing needs an 'optimum mix'

As has been the case for the last four years, the budget deficit was well within the planned limit when one considers the first six months of FY2015-16. Although a significant revenue shortfall can be expected, this will be offset by lower levels of public expenditure. The structure of financing was characterised by low net intake from foreign financing sources against a heavy reliance on domestic financing sources. Within the domestic financing structure, the buoyant sale of high benefit yielding national savings certificates was the key feature in FY2015-16. One of the major challenges for the budget FY2015-16 will be to bring back a balance in the structure of financing the budget deficit. Since a large share of the financing has already been secured from the sale of National Savings Bond (NSD) certificates, the need for bank borrowing may be rather limited. However, lack of capacity to use foreign resources remains an issue of serious concern.

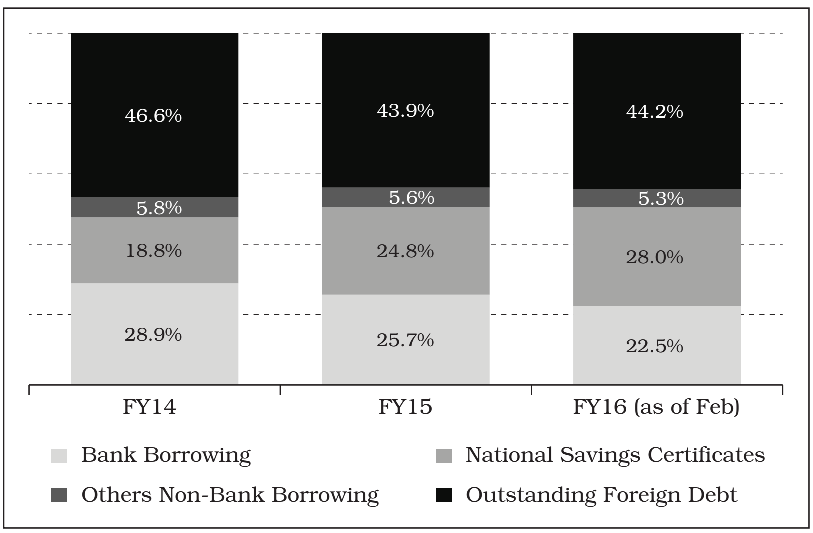
Composition of outstanding public debt of Bangladesh

As regards public debt, Bangladesh's position is generally comfortable. Total public debt is expected to decline from 35.8 per cent in FY2013-14 to 34.9 per cent in FY2017-18 (MoF, 2015). Currently, approximately 56 per cent of public debt is attributable to domestic sources and 44 per cent to foreign finance. Therefore, much will depend on the government's ability to use low-cost borrowings, which to date has not been observed.

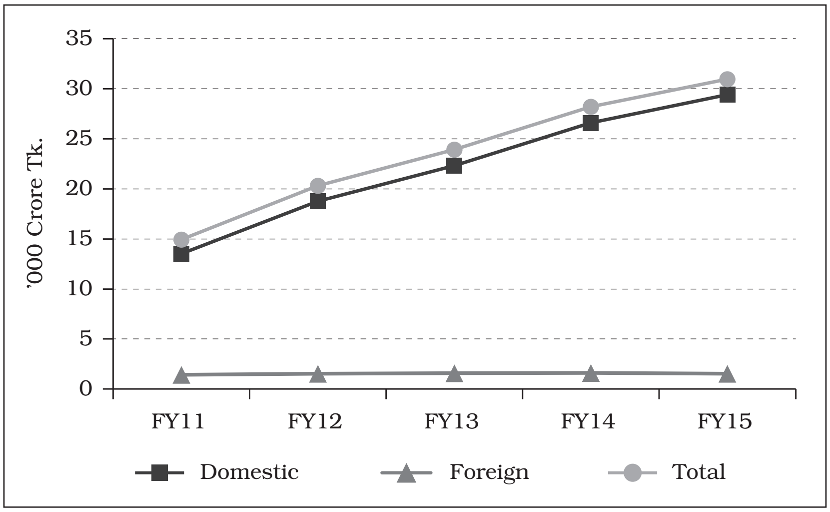
Within domestic sources, debt from non-bank sources is increasing (led by net sales of NSD), while debt from bank sources is decreasing. This has led to a gradual shift in the overall composition of public debt. Indeed, as of February 2016, debt against sales of NSD certificates accounted for 51.3 per cent of the government's total outstanding domestic debt liability (Tk. 125,021 crore) (Figure 1.9). One year ago, the corresponding figure was around 43.5 per cent (Tk. 97,581.58 crore). In comparison, the proportion of outstanding foreign debt in the overall debt portfolio has been rather steady.

Figure 1.9

Composition of Outstanding Public Debt



Source: Estimated from Economic Relations Division (ERD) and Bangladesh Bank data.



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

Figure 1.10
Interest Payment Expenditure

As is known, the debt incurred from domestic sources comes with relatively high interest rates. As of end-June 2015, the interest rate of banks was 11.7 per cent, while the interest rate of non-bank financial institutions (NBFIs) was 15.1 per cent. Although both of these interest rates have reduced in recent times, these still remain higher than those of foreign sources. Due to the high cost of borrowing from domestic sources, the overall interest payment burden of the government has been increasing over recent years (Figure 1.10).

More transparency in fiscal and budgetary processes should be a key area of any economic reforms. Similar to a number of other developing countries, Bangladesh's budgetary process is both complex and complicated, and sometimes inconsistent. In this regard, greater focus needs to be given to implementing 'second generation' reforms by ensuring higher levels of transparency and independence of regulatory bodies, so as to generate efficiency, competitiveness and distributive justice.

In successive IRBDs, CPD has strongly recommended the need to undertake a number of needed reform measures with a view to improving macroeconomic and sectoral performance. These recommendations included:

i. establishing a Public Expenditure Review Commission (PERC);
ii. formulating an appropriate follow-up mechanism for monitoring government tax incentives;
ii. disclosing the financial accounts of state-owned enterprises (SoEs) (including the BPC);
iv. establishing transparency in the government's asset acquisition;
v. ensuring transparency in the defense budget;
vi. increasing transparency in local government financing;
vii. formulating a renewed foreign aid policy in view of the changing dynamics of the global aid architecture and debt structure (as Bangladesh is now listed in the (lower) middle income country category); and
viii. keeping non-government organisation (NGO) financing in mind while crafting development financing.

1.4 THE FINANCIAL SECTOR: VEERING OFF TRACK?

Bangladesh's global financial market development ranking has fallen sharply over the recent past – from 66th in 2010-11 to 90th in 2015-16 (World Economic Forum, 2010; 2015). In terms of the availability and affordability of financial services, the ease of access to loans, soundness, regulatorly measures guiding the financial sector, and the state of securities and exchanges, Bangladesh has been deteriorating. Progress of

BASEL III implementation has also been slow, particularly in the case of state-owned commercial banks (SCBs). In a similar vein, NBFIs are also being confronted with challenges, in areas such as maintaining management standards, efficient operations and good governance. The capital market is yet to be seen as a reliable investment opportunity, being itself faced by various systemic challenges. In this backdrop, there is a need to take an in-depth look at the performance of Bangladesh's financial sector.

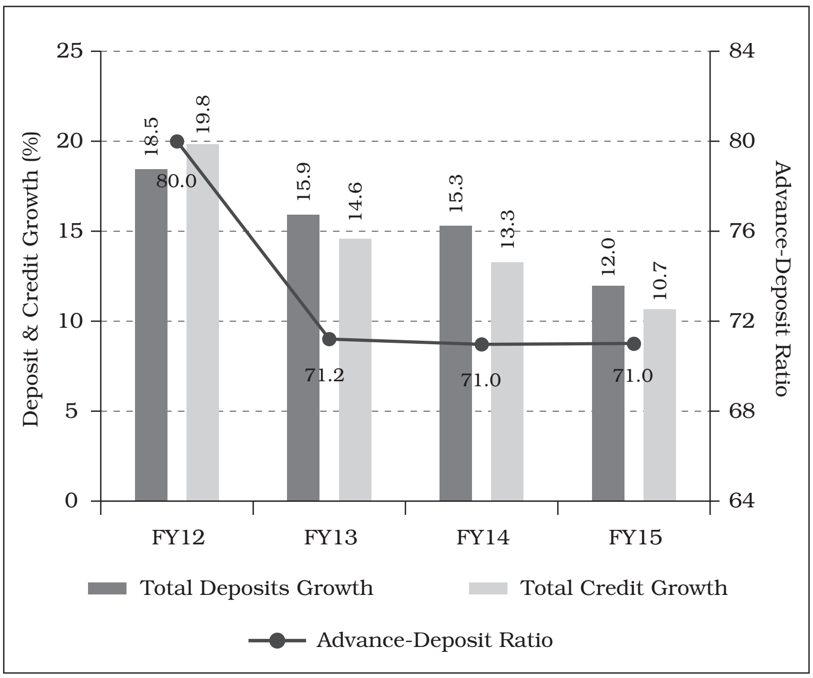
1.4.1 Performance of the Banking Sector

Disbursement of loans and advances is afflicted by demand-side constraints

The majority of commercial banks have not experienced credit expansion in recent times. The credit-deposit ratio (CDR) has been declining since 2011, falling to 69.8 per cent in September 2015. This is significantly lower than the safe CDR limits of 85 per cent set for conventional banks and 90 per cent set for Sharia-based Islamic banks. Most banks are experiencing low demand for advances (Figure 1.11). Among the reasons for this slowdown are a lack of demand in some of the major export markets, and a lack of infrastructure and related facilities, which discourages private sector investment, and increases the costs of doing business. Consequently, growth in advances and deposits has decelerated – in FY2014-15, these rates were 10.7 per cent and 12 per cent respectively. Under such a scenario, cash management by commercial banks will be an issue of growing concern. Excess liquidity in commercial banks, as a share of total assets, has doubled over the last five years, from 8.4 per cent in 2011 to 16.9 per cent in 2015 (Figure 1.12). There has also been a sharp rise in excess liquidity, particularly in SCBs and foreign commercial banks (FCBs), and to a lesser extent, in private commercial banks (PCBs) during 2013-2015. A part of this rise is influenced by the increasing amount of external borrowing by the private sector at a relatively low interest rate (Table 1.9).[39] The outstanding balance of external borrowing at the end of 2015 was USD 3.2 billion, which compares to just USD 849 million at the end of 2011.

Figure 1.11

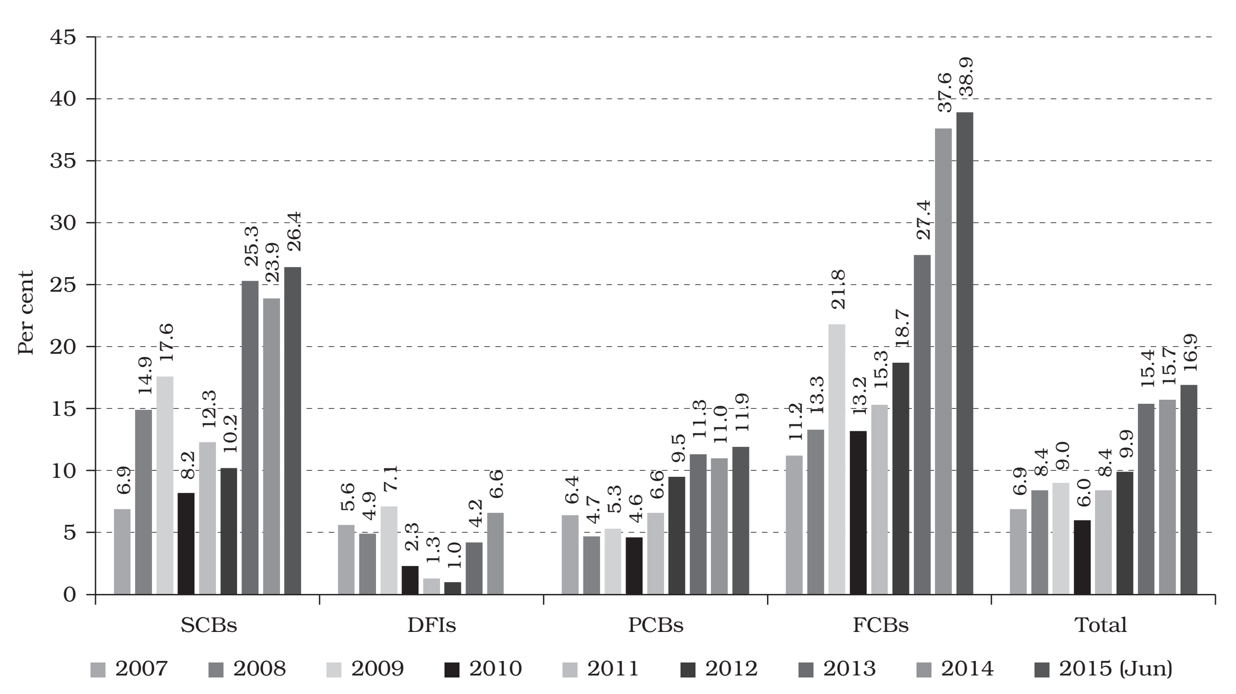
Advance-Deposit Ratio and Growth of Deposit and Credit



Source: Bangladesh Bank (2014); (2015a); (2015b).

[39]Interest rates for external borrowing tend to range between as low as less than 2 per cent (21.1 per cent of total advances) to as high as 10 per cent and above (0.07 per cent of total advances). However, a significant proportion of the loans were disbursed at a rate of 4 to 6 per cent (47 per cent).

Figure 1.12
Excess Liquidity as % of Total Assets in Commercial Banks



Source: Bangladesh Bank (2016).
Note: DFIs: Development finance institutions.

Table 1.9
Disbursement of Private Sector External Debt (Medium and Long-term)

(Million USD)

Calendar Year	Amount
2011	452.8
2012	430.3
2013	861.9
2014	1,374.1
2015	708.3

Source: Statistics Department, Bangladesh Bank.

The interest rate of commercial lending is largely influenced by commercial banks' cash management. Although average lending and deposit rates have declined in commercial banks, there is a significant difference in interest rates on deposits and advances across, and within, various categories of banks. While the difference in rates of advances and deposits is relatively low between different categories of banks, it is much higher in the case of banks belonging to a particular category (Table 1.10). Bangladesh Bank should focus more on the operations of individual banks to assess their performance with respect to deposit collection and advances. While the informal understanding that interest rate spread would be kept below 5 per cent has, on average, been followed, many banks have still failed to adhere to this requirement. There are two extreme cases as regards interest rate spread – while specialised banks (SBs) have maintained spread much lower than the 5 per cent level, FCBs have experienced significantly higher spread. The central bank should examine how banks set their respective interest rates, and the extent to which rate-setting processes follow market-based mechanisms.

Table 1.10
Interest Rate Spread by Type of Bank in March 2016

(in Per cent)

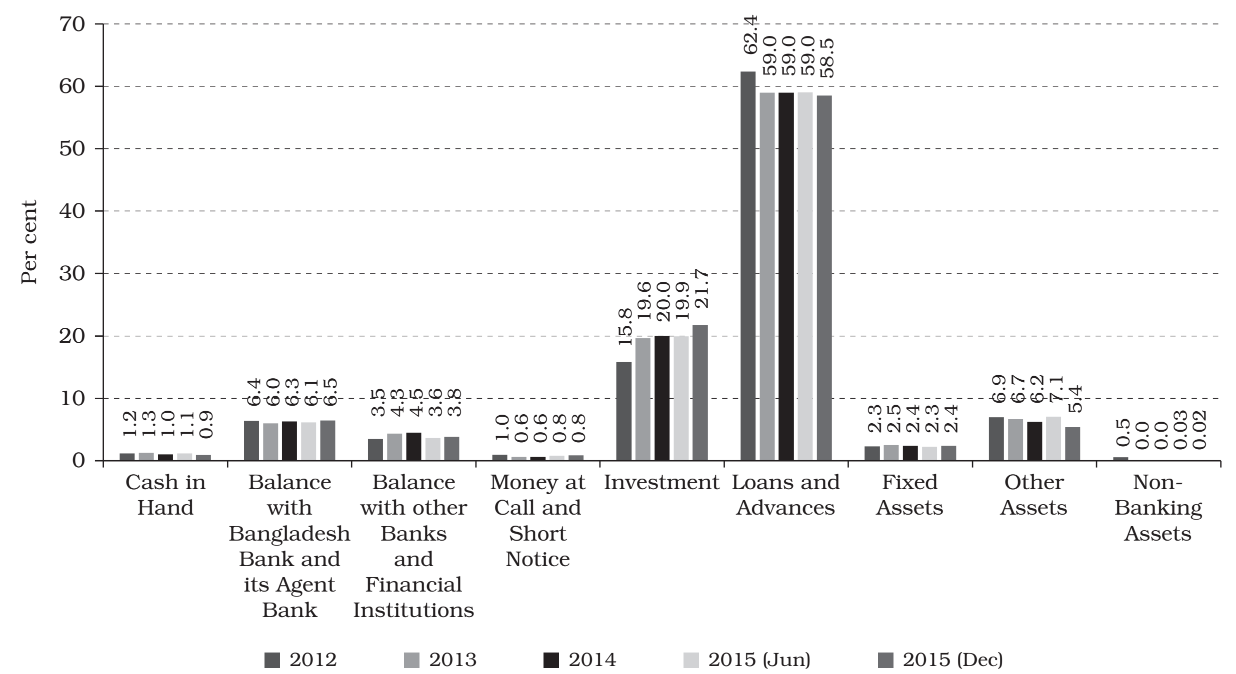
Type of Bank	Advances		Deposits		Spread	
	Weighted Average Rate	Differences between Highest and Lowest Rates	Weighted Average Rate	Differences between Highest and Lowest Rates	Weighted Average Rate	Differences between Highest and Lowest Rates
SCBs	9.93	4.28	6.07	1.64	3.86	4.49
SBs	9.48	0.10	7.46	0.92	2.02	1.02
FCBs	9.53	7.93	2.19	6.31	7.34	11.97
PCBs	11.14	7.58	6.05	6.55	5.09	6.55
All banks	10.78	10.42	5.92	9.32	4.86	12.05

Source: Calculated from Bangladesh Bank data.

Sluggish growth of loans and advances has changed the composition of bank assets

Asset growth in the banking sector was sluggish in 2015, at 12.2 per cent, which is the lowest since 2012. The slow growth of loans and advances mainly contributed to this trend. Consequently, the composition of banking assets has changed (Figure 1.13). Loans and advances, which are the predominant components in banks' assets, have seen a decline in share, while the share of banks' investment has experienced a rise. In the context of a lack of demand for banking sector credit, the rise in bank's investment calls for greater clarity, particularly with respect to the kind of investment that has been made, the time period, and the rate of return from this investment. It is likely that a significant part of this investment was made in 'unencumbered approved securities' of Bangladesh Bank, with low returns – this comprised about 70

Figure 1.13
Changes in the Composition of Banking Assets



Source: Calculated based on Bangladesh Bank (2015a); (2015b).

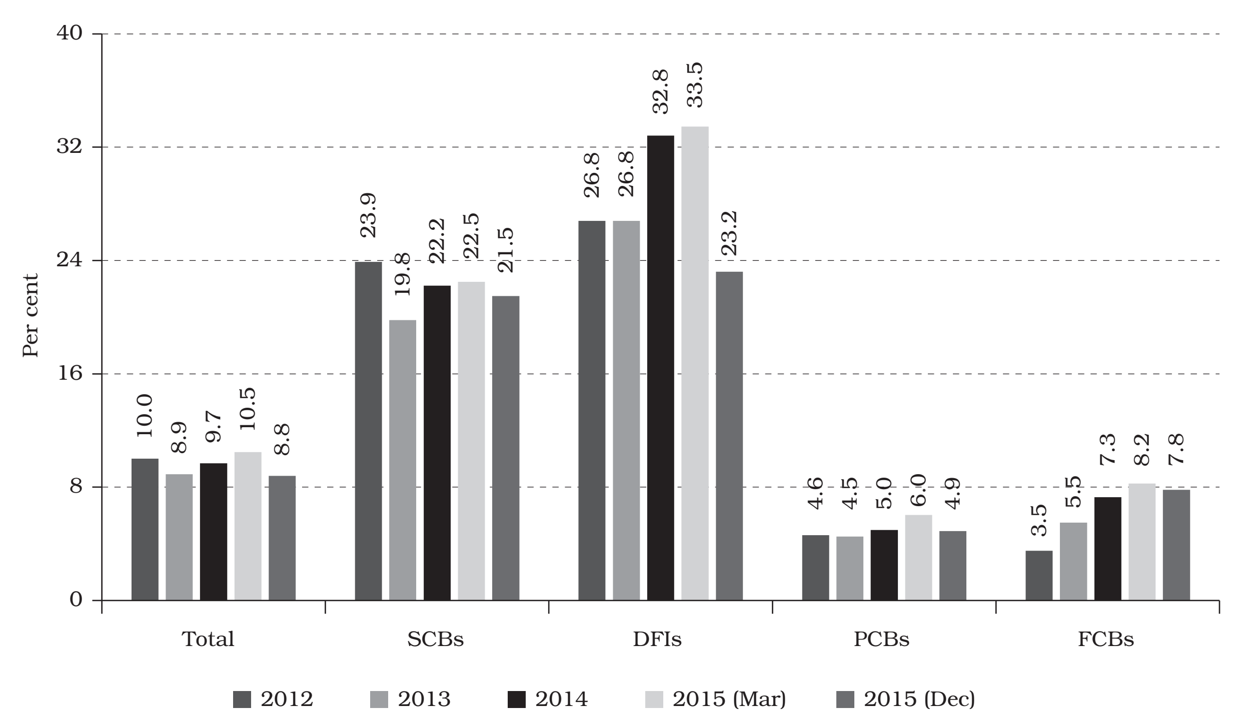
per cent of the banking sector's total liquid assets. If this is the case, it may have a detrimental impact on banks' profitability.

Asset quality is a concern

The high level of non-performing loans (NPLs) has emerged as a major concern, bringing into question the quality of banks' assets. By March 2016, NPLs totalled about Tk. 59,411 crore, which was 9.9 per cent of total loans. The per cent of NPLs therefore exceeded the recent peak of 9.69 per cent in December 2014, since when the level of NPLs had declined, thanks to the rescheduling of large corporate loans (Figure 1.14). A number of measures were undertaken to improve banks' NPL levels, including the appointment of observers in 14 commercial banks, as well as to improve the quality of management and raise operational efficacy.[40] These measures, however, have had little impact on the performance of these banks, as evident from the recent NPL situation. Indeed, during January-March 2016, the amount of NPLs of six SCBs had risen to Tk. 27,289 crore (from Tk. 23,744 crore); and for 39 PCBs, NPLs had increased to Tk. 25,331 crore (from Tk. 20,760 crore). For FCBs, loan default decreased to Tk. 1,822 crore (from Tk. 1,897 crore).

Figure 1.14

NPLs as a % of Total Loans



Source: Bangladesh Bank.

As a matter of fact, the level of NPLs in most South Asian countries has increased in recent years (Table 1.11). However, except for Pakistan, no South Asian country has experienced a situation similar to Bangladesh. The level of NPLs in Bangladesh is above the average level in South Asia and is more than double to that of India and Sri Lanka. The need to take corrective steps is therefore urgent and obvious.

[40] Bangladesh Bank appointed observers at the following banks: Sonali, Janata, Agrani, Rupali, BASIC, ICB Islami Bank, Islami Bank, Mercantile Bank, National Bank, Farmers Bank, Bangladesh Krishi Bank (BKB). Bangladesh Bank also appointed observers at NBFIs.

Table 1.11
NPLs of Banking Sector to Total Gross Loans

(in Per cent)

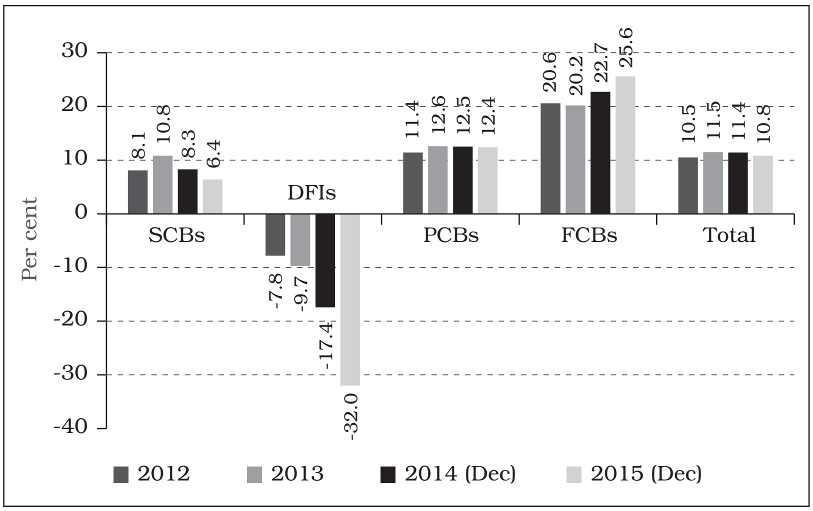
Country	2012	2013	2014	2015
Bangladesh	9.73	8.64	9.37	8.79
India	3.37	4.03	4.35	4.23
Pakistan	14.47	12.99	12.27	12.45
Sri Lanka	3.63	5.58	4.23	4.33
South Asia	4.96	5.58	7.78	8.39

Source: World Development Indicators (WDI).

The capital adequacy of many banks is behind BASEL III requirements

As per BASEL III, the capital adequacy ratio (CAR) of banks is to be raised from 10 per cent in 2015 to 12.5 per cent in 2019. The average CAR level at present is just above the minimum threshold level, at 10.8 per cent in December 2015. However, this has in fact declined from 11.4 per cent in December 2014. Once again though, the performance of different categories of banks, as well as of banks within particular categories, diverges somewhat. The performance of SCBs has deteriorated significantly in recent years – as of December 2015, the CAR of SCBs had decreased to just 6.4 per cent. Curiously, the CAR for DFIs has been negative for several years, and has deteriorated further in recent years, to (-) 32 per cent in 2015. Both FCBs and PCBs have maintained the required level, particularly FCBs, the CARs of which have risen significantly to 25.6 per cent as of December 2015) (Figure 1.15).

Figure 1.15
Capital to Risk Weighted Asset



Source: Bangladesh Bank.

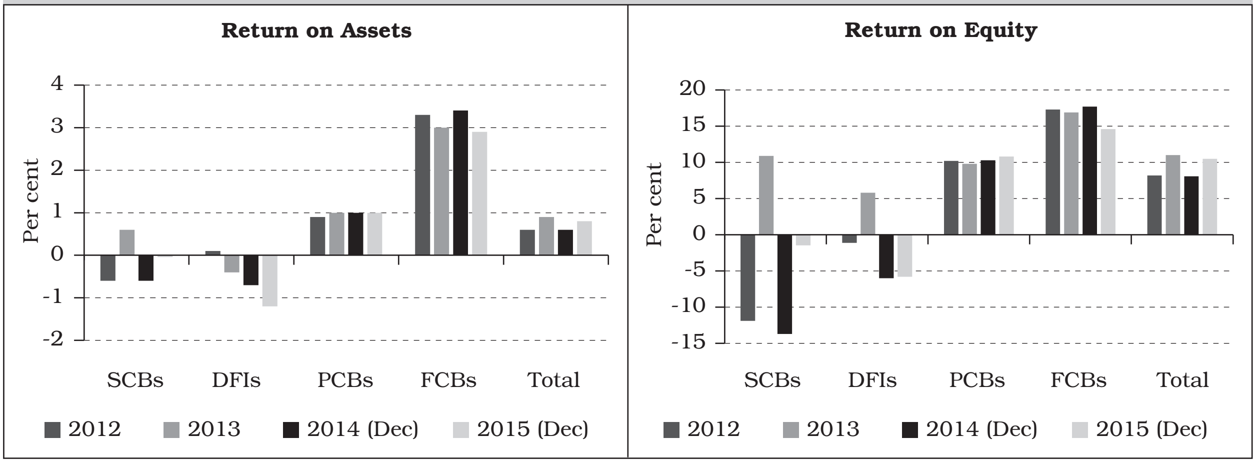
Both SCBs and DFIs need to undertake significant efforts to increase their CAR in the coming years. During the last three years, the government has spent approximately Tk. 14,477 crore on the recapitalisation of SCBs in order to meet their capital shortfall. This injection of capital has evidently had no tangible impact in improving CAR and the operational efficiency of the concerned banks. In other words, attempts to recapitalise SCBs without addressing major structural, operational and political concerns, raises questions about the justification of the government's initiatives (CPD, 2012). Stress test analysis carried out by the Bangladesh Bank (Bangladesh Bank, 2015b) indicates that eight banks have failed to meet the minimum requirement of 10 per cent, including all four SCBs and two DFIs. According to this report, the possibility of the three biggest borrowers defaulting is likely to bring 21 banks into non-compliance as regards minimum CAR.

Mixed performance in terms of profitability

Despite the aforementioned challenges, the banking sector has demonstrated resilience as regards addressing various market risk shocks, including interest rate risks, exchange rate risks and equity price risks. The profitability of banks, measured in terms of return on assets and return on equity, has shown a divergent pattern. Both return on assets and return on equity have been negative in recent years, both for SCBs and DFIs (Figure 1.16). For PCBs, both of these returns have changed little, although intra-PCB differences remain significant. FCBs have fared better in terms of ensuring higher levels of both assets and equity returns. It is important, however, to also assess the performance of individual banks as regards return on assets and equity, as this will help to inform the appropriate measures to be taken to improve performance.

Figure 1.16

Return on Assets and Equity



Source: Bangladesh Bank.

Underperformance of newly-established banks

A total of nine new banks started operations in 2013, of which one bank is conducting Sharia-based banking, and the remainder practice conventional banking – of the latter group, three are sponsored by non-resident Bangladeshis (NRBs). Within two years, these banks have expanded their branches four-fold, however, they are yet to break-even (Table 1.12). According to the latest available data, profitability of most new banks in 2014 was much lower compared to that of established banks. Net interest income to total

Table 1.12

Performance Indicators of New Banks and the Overall Banking Sector

(in Per cent)

Indicator	Year	New Bank	Banking Industry
Return on assets	2014	0.3	0.7
Return on equity	2014	1.3	8.7
Net interest income to total assets	2014	2.1	1.5
Non-interest income to total assets	2014	1.5	2.8
Capital adequacy ratio	2013 (Dec)	79.4	11.5
	2014 (Dec)	29.9	11.4
Advance-deposit ratio	2014	64.5	70.9

Source: Bangladesh Bank.

assets in 2014 was higher than established banks due mainly to new banks not facing problems with NPLs. The CAR is very high for new banks compared to that of other banks, owing to the need to comply with the minimum required capital for initiating operations. All new banks maintain higher lending and deposit rates compared to established PCBs, with interest rate spread not necessarily below the 5 per cent level for all new banks.

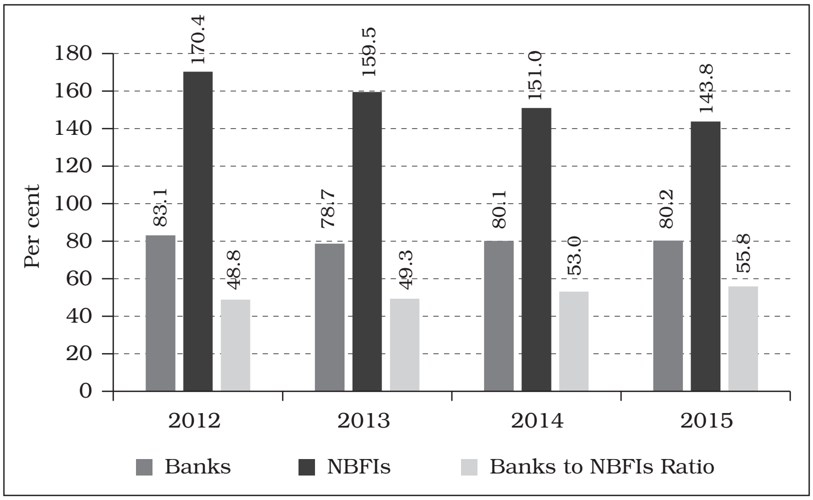
1.4.2 Performance of Non-Bank Financial Institutions (NBFIs)

Access to NBFI credit

Performance of NBFIs vis-à-vis banks is rather mixed. The advance-deposit ratio (ADR) appears rather high when compared to that of the banks (Figure 1.17), although the ADR has slowly declined over recent years. The growth in NBFI loans and leases has been volatile, with NBFIs outperforming banks, particularly in 2013 and 2015 – growth of NBFI loans was 21.7 per cent during December 2015, as against 11.3 per cent for banks in the same period (Figure 1.18). Major sectors to which NBFI loans have been disbursed include housing (17.5 per cent), trade and commerce (16.4 per cent), power and gas (10.5 per cent), and textiles (4.7 per cent). In addition, a sizable amount of the loan profile has been directed to merchant banking and as

Figure 1.17

Comparison of Total Advance/ Loan-Total Deposit Ratio between Banks and NBFIs

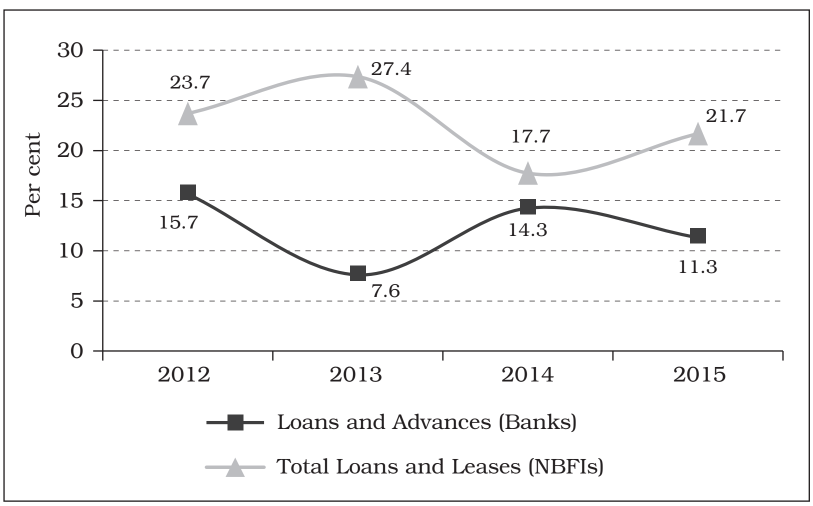


Source: Calculated based on Bangladesh Bank (2015a) and data from Bangladesh Bank website.

Note: For banks, total advance and for NBFIs, total loan were considered.

Figure 1.18

Growth of Total Loans of Banks and NBFIs



Source: Calculated based on Bangladesh Bank (2015a); (2015b).

margin loans.[41] Such a loan profile reveals different levels of risk involved in invested assets. NBFIs will need to manage these risks effectively, as otherwise their level of NPLs could rise, which would then adversely affect their return on assets.

Rise in NPLs is a growing concern for NBFIs

The rise in the level of NPLs is proving to be a major concern for the NBFIs – indeed, this is increasing at a higher pace for NBFIs compared to banks. In December 2015, NPLs in NBFIs had increased by about 103 per cent compared to December of the previous year (Figure 1.19). The rate of NPLs was 8.9 per cent for NBFIs while it was 8.8 per cent for banks. More importantly, if the NPLs of SCBs is excluded, the performance of private banks (FCBs and PCBs) was far more impressive than that of NBFIs, with NPLs at 4.9 and 7.8 per cent respectively in December 2015. A significant amount of loans and leases were disbursed in relatively risky ventures, for instance, loans to the crisis-prone housing sector, advances made through margin loans to the volatile capital market, and advances made to merchant banks. All of these may cause the number of NBFI NPLs to rise. Given that concerns as regards the housing sector and the capital market have persisted over a number of years, there is a need for a more in-depth investigation of the recent jump in the level of NPLs of these NBFIs.

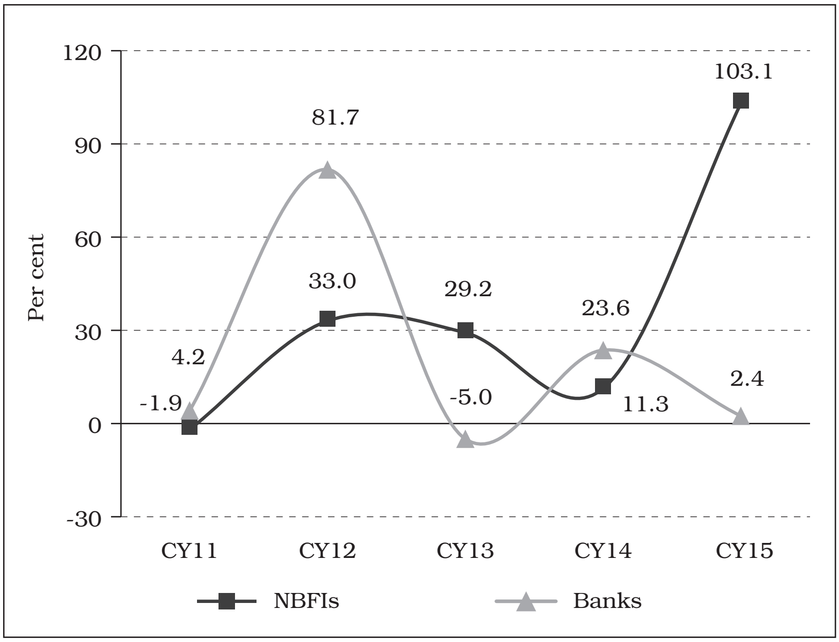


Figure 1.19
Growth of NPLs of Banks and NBFIs

Source: Calculated based on Bangladesh Bank (2015a); (2015b).

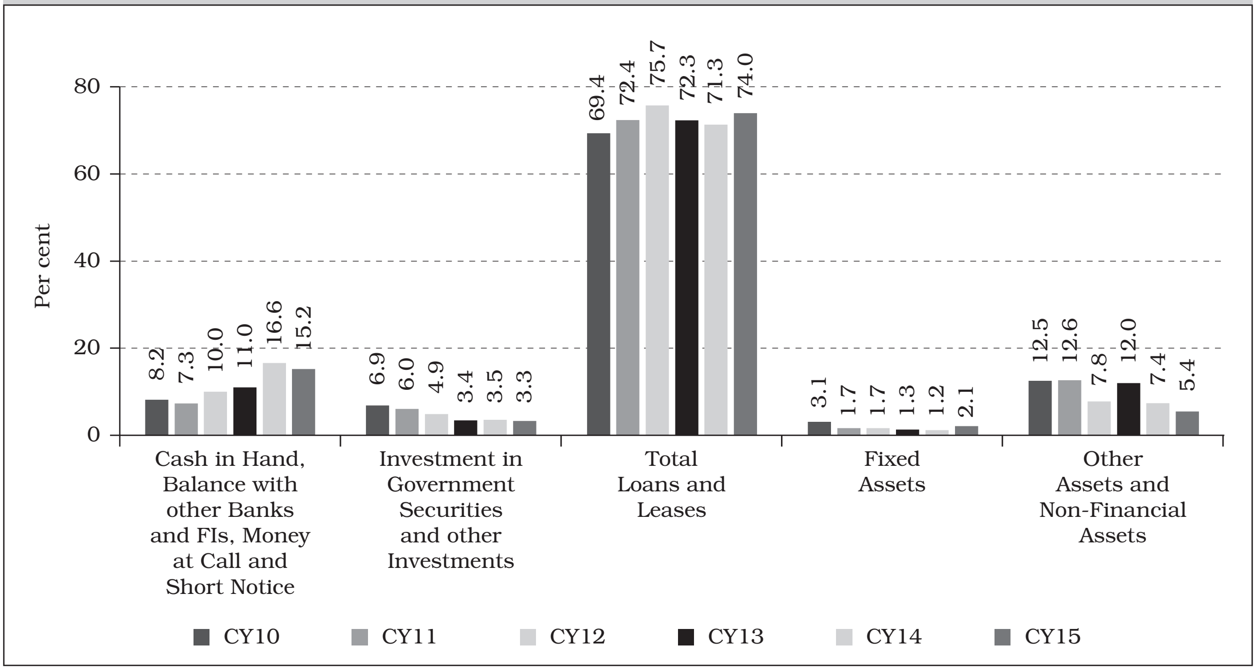
The asset structure of NBFIs raises questions

There is little surprise when one looks at the asset structure of NBFIs. Its composition is dominated by loans and leases, followed by cash-in-hand and balance with other banks and financial institutions (Figure 1.20). However, a high rate of NPLs and significant levels of cash-in-hand raise questions as regards the quality of assets. Unless the various assets ensure an adequate return, the high-cost deposit collected by NBFIs (as shown in Figure 1.21) could turn out to be a burden from the perspective of maintaining the expected level of return on assets.

[41]Based on 2014 data available from Bangladesh Bank (2015a).

Figure 1.20

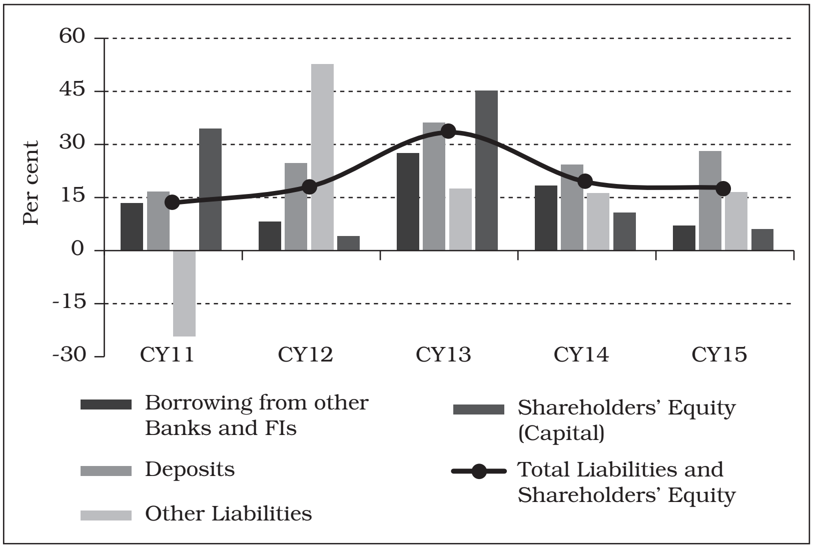
NBFI Asset Structure (as % of Total Asset)



Source: Calculated based on Bangladesh Bank (2015a); (2015b).

Figure 1.21

Growth of Liabilities and Capital of NBFIs



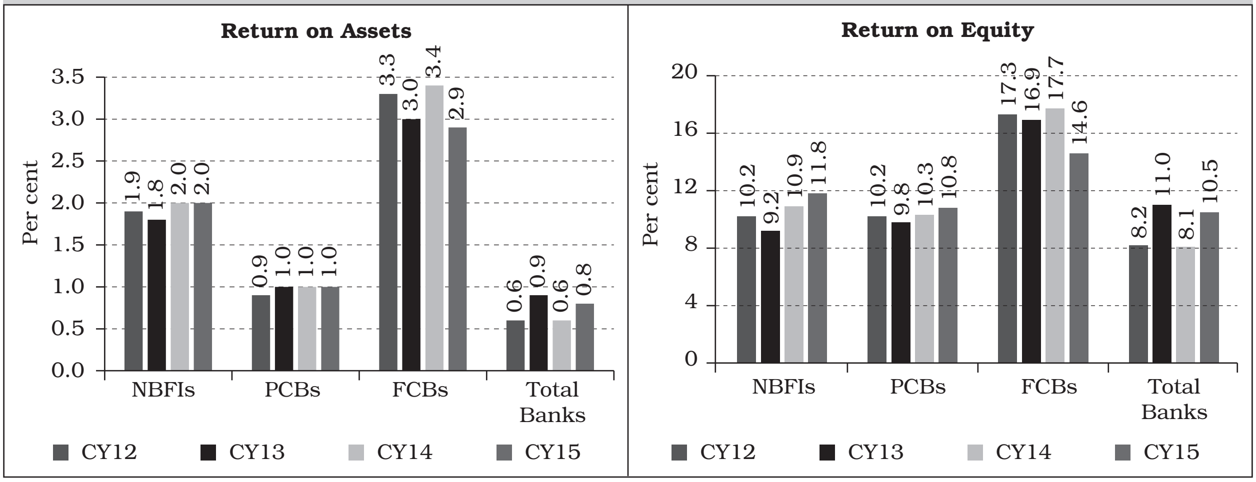
Source: Calculated based on Bangladesh Bank (2015a); (2015b).

Profitability is surprisingly high

Profitability of the NBFIs' assets has been found to be higher than that of banks. However, the situation changes if profitability of NBFIs is compared with private banks (PCBs and FCBs) only. Compared to banks, while NBFIs' return on assets is higher, return on equity is mixed (Figure 1.22). While NBFIs are better positioned both in terms of return on assets and equity compared to PCBs, they do not compare favourably with FCBs in both respects. Given the recent rise in NBFI NPLs, it is unclear whether NBFIs will continue to enjoy profitability in the future.

Figure 1.22

Comparison of Asset Profitability of NBFIs and Banks



Source: Calculated based on Bangladesh Bank (2015a); (2015b).

Risk management

NBFIs are in a better position in terms of risk management than banks. NBFIs' CAR has been maintained at a higher level than the BASEL III requirement, and has been near double that of banks for the last five years (Figure 1.23). In December 2015, capital to risk weighted assets for NBFIs was 18.7 per cent, while for banks this was 10.8 per cent on average. However, NBFIs are still far behind FCBs in this regard, as capital to risk weighted assets for the latter was 25.6 per cent in December 2015.

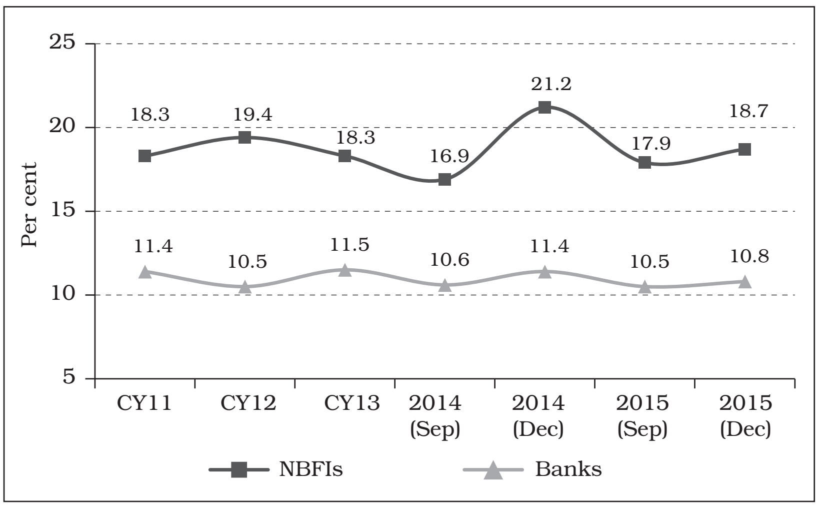


Figure 1.23

Comparison of Capital to Risk Weighted Assets between NBFIs and Banks

Source: Calculated based on Bangladesh Bank (2015a); (2015b).

1.4.3 Capital Market

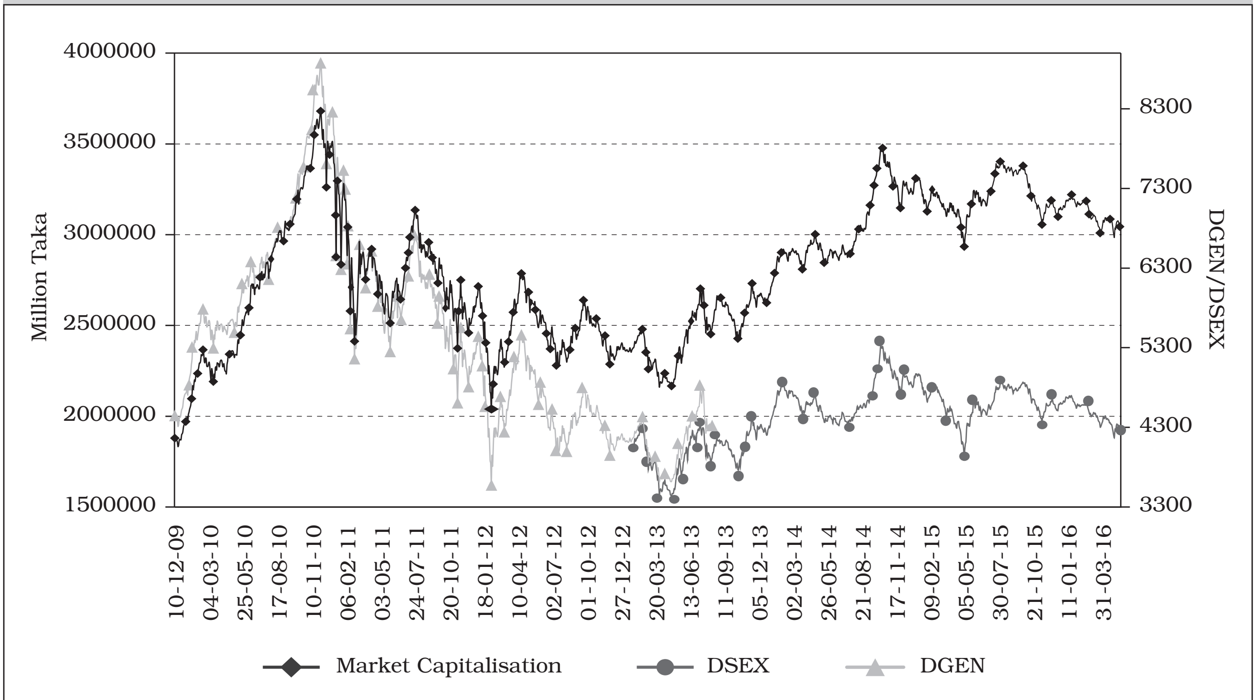
Despite the various initiatives undertaken following the 'boom and bust' of December 2010, the capital market has yet to regain its lost momentum. Major indicators related to primary and secondary markets reveal a rather depressed scenario. The Dhaka Stock Exchange (DSE) index (DSEX and DGEN) has been hovering around 4,000-5,000 over the last two years, with a decelerating trend being observed in the associated indices since early June 2015. Declining confidence among investors has adversely impacted the daily market turnover. In July-May FY2015-16, daily turnover came down to less than Tk. 3,000 million on a number of occasions, with there also being a declining trend in monthly turnover (Tk. 86.4 billion, Tk. 79.9 billion and Tk. 75.1 billion for February, March and April 2016 respectively). This poor picture can be explained in part by sluggish growth in private investment in real sectors, particularly on the part of large-scale enterprises (discussed in Section 1.2). Besides, the volatility seen in the secondary market is difficult to explain through market-based approach. Questions have also been raised as regards the efficacy of the various initiatives and approaches undertaken by the SEC to stabilise the market.

Market indices and market capitalisation remain mostly unchanged

Since the beginning of FY2015-16, the DSEX index fell by 283.94 points, with it currently standing at 4,288.65 (as of 15 May 2016) (Figure 1.24). In October 2014, the DSEX reached a peak of 5334.04, but continued to fall afterwards, with the index falling below 4000 points by June 2015. Market capitalisation has also suffered during this period, having experienced a decelerating trend since October 2014. As of 15 May, market capitalisation stood at Tk. 3,048.5 billion, approximately 17.6 per cent of the estimated GDP of the country for FY2015-16 (at market price). The number of Beneficiary Owners (BO) accounts operating in the capital market fell significantly after the market collapse, from 3.4 million in March 2011 to 2.79 million in December 2013, although since 2015 it has experienced a gradual rise – at present the number of BO accounts is 3.22 million. However, a significant number of BO accounts are either almost non-functional or conduct only limited transactions owing to the significant amount of past unpaid debt incurred against these accounts.[42]

Figure 1.24

Trends in Market Capitalisation and the DGEN/DSEX Indices



Source: Dhaka Stock Exchange (DSE).

[42]Anecdotal information indicates that the number of BO accounts that became non-functional each year was about 0.1-0.2 million.

Changes in the sectoral composition of market capitalisation

The capital market has experienced some compositional changes in terms of market capitalisation since the collapse of December 2010. The banking sector, which contributed significantly to market capitalisation in June 2010 (41 per cent), has lost ground as a result of the rising share of other sectors, such as pharmaceuticals and telecommunications. The high concentration in market share that were seen before the market crash are gradually changing with other sectors now rising up (Table 1.13). As a matter of fact, a large part of this adjustment has happened on account of market corrections.

Table 1.13

Share of Market Capitalisation in the DSE

(in Per cent)

Sector	2010 (Nov)	2016 (Apr)	Change
Banks	30.53	14.48	▼
NBFIs	13.06	5.35	▼
Fuel and Power	10.61	14.16	▲
Telecommunications	10.49	14.32	▲
Pharmaceuticals	7.41	16.49	▲
Insurance	6.23	2.89	▼
Textiles	4.16	3.24	▼
Engineering	4.11	5.81	▲
Cement	2.56	5.06	▲
Food	2.16	9.62	▲
Ceramics	1.94	0.99	▼
Mutual funds	1.21	1.09	▼
Services and real estate	1.16	0.72	▼
Tannery	0.62	0.89	▲
Travel	0.48	0.73	▲
IT	0.14	0.38	▲
Jute	0.04	0.03	▼
Paper	0.04	0.06	▲
Miscellaneous	2.92	3.46	▲

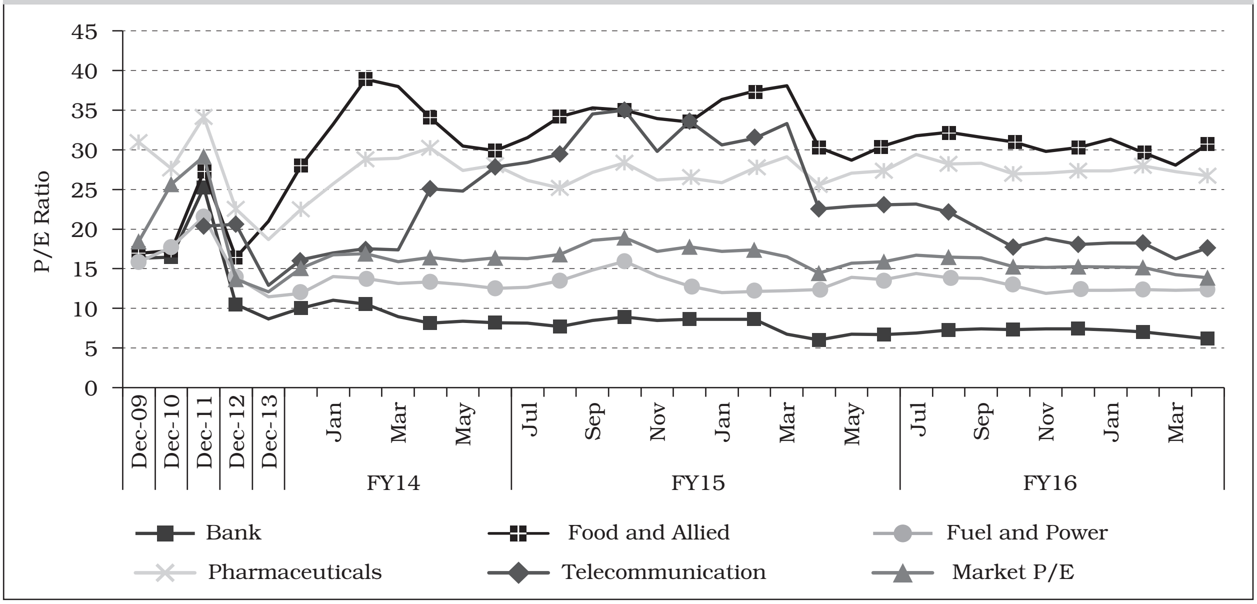
Source: Based on Dhaka Stock Exchange (DSE) website data.

Investment decisions in the secondary market are barely influenced by the price-earnings ratio of shares

The gradual fall in the average market price-earnings (P/E) ratio indicates that investing in the capital market is becoming increasingly favourable. The average P/E ratio reached a peak of 18.91 in October 2015, but has since come down to 13.86 (as of April 2016) (Figure 1.25). In the case of sectoral P/E ratios, a mixed trend can be observed for the corresponding period. The consistently low P/E ratio of shares in the banking sector has discouraged potential investors in investing in these shares. The P/E ratio is high, but consistent for the power and fuel sector, and the pharmaceuticals sector. Previously, the food and allied, and telecommunication sectors experienced high volatility in terms of their P/E ratio, however, ratios have been consistent since early 2015.

Figure 1.25

Trends in the P/E Ratio for Major Selected Sectors



Source: Dhaka Stock Exchange (DSE).

Offloading of initial public offerings (IPOs)

At present, 291 companies are listed in the capital market. Since the collapse in December 2010, 73 new companies have been listed. During the 2016 calendar year, a total of 6 IPOs have offloaded their shares, including companies in the manufacturing, insurance, IT, and fuel and power sectors, amongst others (Table 1.14). The size of the IPO in recent years indicate that medium size companies have a greater interest in being listed on the market, which is a positive sign since entry of relatively smaller sized companies is welcomed. On the other hand, this is also indicative of bigger, more established groups showing less interest in being listed. Listing of SoEs has been a longstanding issue – despite various efforts, limited progress has been made in this regard.

Table 1.14

Number of IPOs and Total Size

Year	Number	IPO Size (Million Tk.)	IPO Size per Unit (Million Tk.)
2009	11	6,358.0	578.0
2010	5	4,116.0	823.2
2011	9	13,774.0	1,530.4
2012	10	7,743.0	774.3
2013	17	12,584.0	740.2
2014	17	9,893.0	581.9
2015	14	10,768.0	769.1
2016*	6	2,277.0	379.5

Source: Dhaka Stock Exchange (DSE).

Note: *Information as of May 2016.

Table 1.15
Number of Newly-Enlisted Companies in the BSE

Year	New Listings	Delisted Companies	Total Companies
FY2010	77	32	4975
FY2011	128	36	5067
FY2012	97	31	5133
FY2013	101	23	5211
FY2014	147	19	5336
FY2015	311	23	5624
FY2016	229	18	5835

Source: Bombay Stock Exchange, India. Retrieved from: http://www.bseindia.com/markets/keystatics/Keystat_Companies.aspx?expandable=1 (accessed on 15 May 2016).

The depth of the capital market in Bangladesh is still shallow compared to that of neighboring countries, such as India. The number of companies listed on the Bombay Stock Exchange (BSE) is 5,835, with 229 new companies being listed in 2015-16 alone (Table 1.15). Since 2011, the total number of new companies listed on the BSE has been 885 compared to 73 on the DSE. It is important to note that a significant number of companies have been delisted from the BSE over recent years, for various reasons. This is, however, quite rare in the case of Bangladeshi bourses – despite various allegations against a number of companies, no companies have been delisted since the market collapsed in 2010.

Overall, Bangladesh's capital market has remained relatively subdued for two years. Lack of strong monitoring and supervision, a poor record of enlisting new companies, a significant amount of loans having been invested in 'bad' shares, and weak performance of institutional investors who have a large amount of 'bad' shares, have all contributed toward creating a 'vicious cycle' that can only be broken with radical steps on the part of regulators as well as all concerned stakeholders.

1.4.4 Challenges Facing the Banking Sector: Beyond Traditional Issues in the Digital Era

In the recent past, Bangladesh's banking sector has experienced new risks associated with cyber security. These include ATM scams concerning four commercial banks during January 2016, followed by Bangladesh Bank's reserve heist in March 2016, and very recently, ATM scams involving a number of other commercial banks. These incidents are indicative of the vulnerability of Bangladesh's banking and financial institutions in this digital age when threats to cyber security have emerged as a growing risk. According to various recent reports, cyber security in the banking sector has been facing multiple challenges, in areas ranging from the suitability of infrastructure, safety of operation, regularity of maintenance and adequacy of the required human resources. According to Kaspersky, of all the computers used in Bangladesh, 60.5 per cent are affected by 20 different types of malwares. Knowledge and expertise about cyber security is acutely needed. A survey conducted by the Bangladesh Institute of Bank Management (BIBM) in 2016, covering 25 banks, found that local banks are facing at least 300 malware attacks every day, of which 60 per cent are carried out by local hackers (Khan, 2016). The study found that about 8 per cent of senior managers in banks were not interested in investing in IT, and 24 per cent are awaiting directives from the central bank. Further, about 70 per cent of banks actually have no dedicated IT security and risk management department. Bank's spending for development in IT is mostly concentrated in purchasing hardware and software. Despite the huge annual spending by commercial banks, only an insignificant share is spent on IT-related activities – only 4 per cent of the total IT budget is spent on cyber security management, of which 2 per cent is spent on training.

The recent heist of USD 101 million from Bangladesh Bank's reserves has exposed the weaknesses in cyber security and cyber governance as regards the central bank's operations. As is known, only USD 20 million of the funds have been retrieved (from Sri Lanka), with the fate of the remaining USD 81 million, which has found its way into casinos in the Philippines, is unknown. A number of investigations are currently ongoing to retrieve the stolen funds, to identify those responsible, and to apportion responsibility to the different parties involved, both in Bangladesh and abroad. The investigative committee submitted its interim report, with the Committee's Chairman stating that whilst the SWIFT system was mainly to blame, Bangladesh Bank and the Federal Reserve Bank of New York could not avoid responsibility.

1.4.5 Suggestive Remarks

The financial banking sector in Bangladesh stands at a crossroads. While public sector institutions are afflicted with many major problems, private sector institutions, while affected to a lesser degree, are not immune to difficulties and challenges. The vulnerabilities of the central bank have also been exposed through recent cyber-attacks. Be it the banking sector or the capital market, the weak state of governance is having a severely adverse impact on performance and efficiency. A major overhaul is therefore needed. The burden of high NPLs is resulting in sustained high interest rates and is weakening the soundness of banks. The capital market has also failed to attract equity through the listing of good companies. To address these problems and identify remedial actions, the CPD has, for quite some time, argued for the establishment of an independent Financial Sector Reform Commission. The proposed Banking Commission may like to suggest ways to restructure SCBs, including rationalisation of branches, offloading of shares, and the handing over of SCBs under private management. Concerted efforts are needed if the financial sector's health is to be restored. Good governance, transparency and accountability should be key to the corrective measures undertaken.

1.5 THE EXTERNAL SECTOR: PERFORMANCE AND POTENTIALS

With growing reserves, an upturn in export growth performance, and a positive current account balance, Bangladesh's external sector has transmitted satisfying signals in FY2015-16. However, depressed performance in the import sector, along with negative growth in remittance flows, continued to remain disquieting features of FY2015-16. Bangladesh Bank continued with its policy of active intervention in the foreign exchange market to keep the Taka from appreciating, in the process accumulating an ever larger amount of foreign exchange reserves.

1.5.1 Export

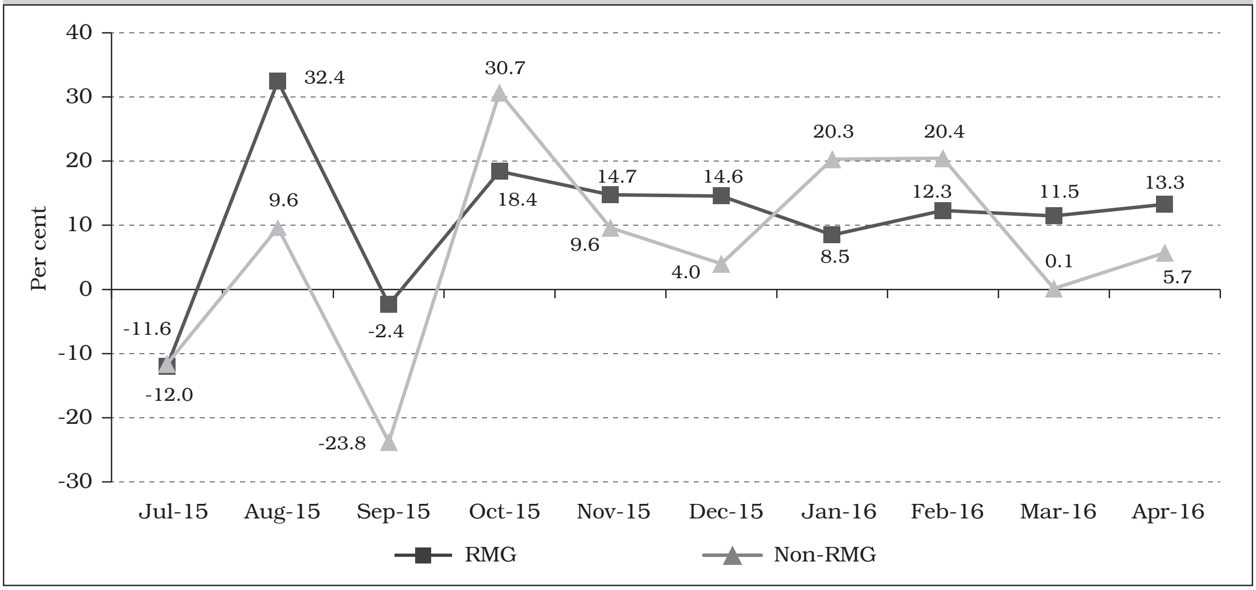
Export earnings during the first ten months of FY2015-16 were robust and recorded a growth rate of 9.2 per cent, exceeding the annual target of 7.3 per cent set for FY2015-16. It is, however, pertinent to mention that the 7FYP has set an export target of USD 54.1 billion by FY2019-20 – this calls for exports to grow by 12 per cent per annum over the plan period. From this perspective, accelerating the pace of export growth continues to remain a challenge for the upcoming years.

A sustained 10.1 per cent growth in readymade garments (RMG) exports during July-April FY2015-16 suggests further product concentration in the backdrop of slower growth of non-RMG exports (5.5 per cent growth against an annual target of 7.2 per cent growth) over the same period (Figure 1.26). Intra-RMG growth decomposition indicates further ascendancy of woven-apparels, which recorded a 12.7 per cent growth rate.

Market analysis reveals that, after registering high growth in the first quarter, export growth in the United Stats (US) market has continued to fall, now into single digits, to 9.2 per cent over the July-April

Figure 1.26

Month-on-Month Growth of RMG and Non-RMG Products in FY2015-16



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

FY2015-16 period. Indeed, in the month of April, export growth to the US was negative at (-) 1.4 per cent. During the July-April period, RMG and non-RMG exports to the US recorded growth of 8.2 per cent and 20 per cent respectively. On a positive note, according to United States International Trade Commission (USITC) data (available for the period July 2015-February 2016), this RMG growth was mainly volume-driven (Table 1.16). RMG exports of Vietnam, one of the closest competitors of Bangladesh in the US market, have also experienced strong volume-induced growth over the same period.

In the European Union (EU) market, export growth during July-April FY2015-16 was 8.5 per cent, this being largely due to 17.3 per cent growth in woven exports. This was helped by some depreciation of the Bangladeshi Taka (BDT) against the Euro. However, contrary to the US market, the growth in both knit and woven exports to the EU market was price-driven (Table 1.16). It is also worthwhile noting that non-RMG export growth to the EU market was negative over the corresponding period.[43]

Table 1.16

Price Impact of Bangladesh and Vietnam's Export Growth: July 2015-February 2016

(in Per cent)

Country	Knit (61)			Woven (62)		
	Value	Quantity	Price	Value	Quantity	Price
US Market						
Bangladesh	22.5	27.4	-3.8	26.7	16.9	8.4
Vietnam	11.4	15.0	-3.1	24.8	9.5	13.9
EU Market						
Bangladesh	16.5	5.2	10.8	19.2	2.2	16.6
Vietnam	27.6	2.1	25.0	16.4	0.8	15.4

Source: Computed from United States International Trade Commission (USITC) and EuroStat data.

[43]Non-RMG constitutes only 8 per cent of total exports from Bangladesh to the EU.

Data on the direction of exports indicates a gradual shift from traditional markets[44] (8.7 per cent growth) to non-traditional markets (11 per cent growth). The non-traditional markets currently account for about 24.3 per cent of total exports from Bangladesh. Of the major non-traditional destinations, exports to Australia (18.6 per cent), Japan (18.3 per cent) and India (27.5 per cent) posted notable growth during July-April FY2015-16. Exports to other major destinations, such as China and Turkey, posted negative growth.

In non-traditional markets, non-RMG products experienced 12 per cent growth[45], while RMG products registered about 10 per cent growth during July-April FY2015-16. However, it should be noted that the leading destinations of Bangladesh's promising non-RMG products were often oriented to the same traditional markets. For example, the major destination of shrimp is the EU, while home textile products are mainly exported to the US, Germany and the United Kingdom (UK). However, there are significant opportunities here for market diversification (see Annex Table 1.7 for details).

Export diversification has been identified as a key challenge in the 7FYP.[46] To address this issue, the government has identified 12 priority sectors in the Export Policy Order (EPO) 2015-18. These priority sectors are: apparel and garment accessories; software and ICT; pharmaceutical; ship-building; leather and footwear products; jute goods; plastic products; agro and agro-processed products; furniture; home textiles; home furnishings; and luggage. These industries have great promise and high export potential, yet face formidable challenges that need to be addressed. For example, the leather industry is currently going through a transitional phase due to the relocation of tanneries from Hajaribag to Savar.[47] Relocation has been delayed, however, due to a reluctance on the part of many entrepreneurs, inadequate infrastructure, and limited facilities for industrial set-up, all of which have affected production at the new industrial estate. It is hoped that this highly promising sector will soon be able to take advantage of this relocation. Also, in the case of jute products, their prices have fallen in the international market following political unrest in the Middle East, as well as economic recession in the Eurozone. Further, the government banned the export of raw jute to ensure an adequate supply of jute for local jute mills; this ban was lifted in April 2016.

To support exporters, and help them maintain their competitiveness in the global market, the government has continued with a variety of fiscal measures. These measures have notably included: export subsidies (cash incentives), additional incentives, bonded warehouse facilities (allowed selectively), soft and concessional short-term commercial loans, support from the export development fund, export retention quotas, import duty exemptions on raw materials, tax rebates, special income tax rates and reduced tax rates, among others. The government has separate budgetary allocations to support cash incentives given to exporters and backward linkage industries. In FY2015-16, the government allocated Tk. 3,500 crore on account of export subsidy.[48] At present, 14 sectors[49], with over 150 product categories, are making use of many of these facilities. The structure of the support has been questioned, however, with some arguing that this particularly favours RMG industries over others – over 50 per cent of the incentives have been availed by these industries. Further, appropriate targeting and the use of support provisions remain as key issues. For promoting efficient use of resources, and for stimulating effective product diversification and exploration of new markets, reassessment, and more specifically, rationalisation of these incentives and support measures is needed. It is appreciated that the government is at present revisiting the fiscal

[44]The traditional market includes the US, the EU and Canada.

[45]It may be noted that share of non-RMG products in these markets is about 48 per cent.

[46]Of the 25 background papers prepared to formulate the 7FYP, one was dedicated to identifying priorities and setting strategies for export diversification.

[47]The government has allocated Tk. 250 crore to tannery-owners as compensation for the shift, while Bangladesh Bank announced concessional loans at a 5 per cent rate for tanneries that are to be established in the Savar leather industrial estate.

[48]As reported by anecdotal sources, the government is going to increase export subsidies by another Tk. 1,000 crore, from the existing 3,500 crore, of which Tk. 500 crore will be reserved only for jute products.

[49]These sectors are: RMG industries, handmade eco-friendly products, agro and agro-processing industries, bone powder, light engineering products, meat products, shrimp, leather, ship-building, potato starch, plastic and jute.

incentives provided to exporters. This exercise should ensure efficiency in allocations and implementation. Incentive and support measures should also target the services industry in a strategic way, so as to enable Bangladesh to take full advantage of the services waiver facility accorded to LDCs in the World Trade Organization (WTO).

1.5.2 Import Payments

Import payments reached some degree of stability towards the end of the third quarter, after having been in the negative terrain in the first quarter, and experiencing significant spikes in the second quarter. Import payments increased by 6.5 per cent in July-March 2016, compared to the corresponding period in the previous fiscal year.[50] Nine out of the 23 products recorded growth higher than 6.5 per cent.[51] Intermediate goods contributed the most (53.9 per cent) to incremental growth in import payments, propelled by payments on petroleum products (23.2 per cent) and textiles (20.1 per cent). Curiously, the price of crude oil and edible oil have fallen, on average, by (-) 44.9 per cent and (-) 9.7 per cent respectively during the same period.[52] This suggests that the growth in imports of the aforementioned products was predominantly quantity-driven. Growth of investment-inducing imports showed signs of improvement during the third quarter of FY2015-16 (Table 1.17). The substantial fall in rice imports[53] was the main reason for the decline in foodgrain imports over the course of the fiscal year.

Table 1.17
Growth in Selected Imports in FY2015-16

(in Per cent)

Product	Jul-Dec FY16	Jul-Mar FY16
Capital machinery	-14.8	-5.6
Raw cotton	-9.9	-2.5
Yarn	2.1	5.5
Textile and articles thereof	8.6	9.3
Dyeing and tanning materials	-10.1	-4.4

Source: Calculated based on Bangladesh Bank data.

A cross-country comparison was carried out to analyse whether Bangladesh's import performance was in tandem with competing or similar economies for the reporting period. India, Pakistan and Sri Lanka experienced negative import growth in July-March FY2015-16 when compared to the corresponding period of the previous fiscal year (Figure 1.27). In the case of India, the large negative import growth figure has been mainly attributed to the decline in oil import bills.[54] In contrast, Cambodia and Vietnam showed positive growth, although this growth level was still lower than the high benchmarks achieved in July-January FY2014-15.

Opening of letter of credit (L/C) for July-March FY2015-16 declined by (-) 2.3 per cent compared to the corresponding period in FY2014-15.[55] L/C opening for petroleum products experienced negative growth, at (-) 40.2 per cent. Growth in L/C opening for industrial raw materials was positive, at 2.9 per cent, with

[50]During July-March of FY2014-15, the import payment growth was (-) 0.1 per cent.

[51]The top five imported products with the highest growth rates were pharmaceutical products (64.1 per cent), edible oil (57.4 per cent), oilseeds (37.1 per cent), petroleum products (34.9 per cent), and crude petroleum (15.6 per cent).

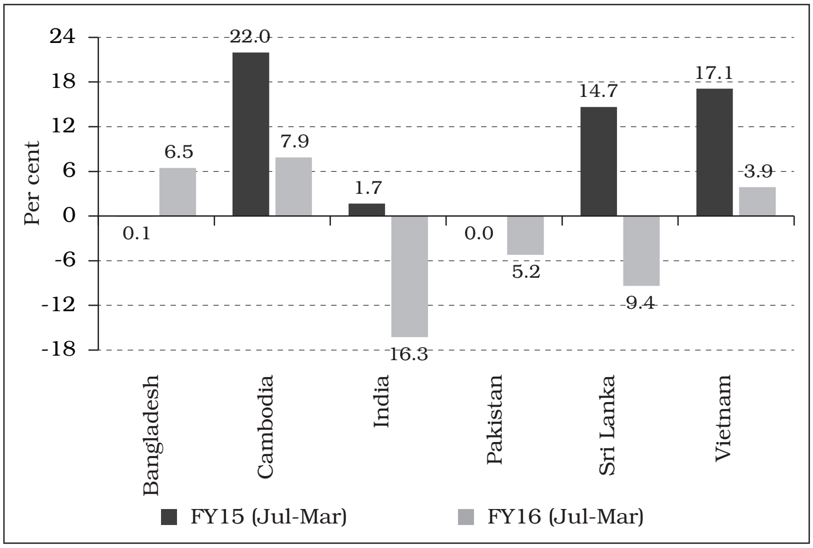
[52]The cotton price remained stable in the global market.

[53]The imposition of import duty and regulatory duty (RD) on rice (10 per cent each) could be responsible for the low level of imports.

[54]India has witnessed a falling rally in import payments for the last 7 months as a consequence of the lagged impact of falling oil prices – oil import bills have been negative for the last 16 months. This has also been as a result of lower prices of non-oil import commodities, such as gold and steel.

[55]The growth of L/C opening for July-March FY2014-15 was 9 per cent higher than that of the corresponding period in FY2013-14.

Figure 1.27
Cross-Country Comparison of Import Growth



Source: Compiled based on various sources: Bangladesh Bank, National Bank of Cambodia, Reserve Bank of India, State Bank of Pakistan, Central Bank of Sri Lanka, and Vietnam Customs (Customs Trade Statistics).

Note: Import data for Cambodia, Sri Lanka and Vietnam are available till January 2016.

growth of back to back L/C opening being consistent with the previous year for the corresponding period, at 9.5 per cent.[56] Opening of L/C in favour of capital machineries rose by 13.9 per cent during the first three quarters of FY2015-16. However, it is yet to be seen whether this is indicative of any resurgence in private sector investment.

1.5.3 Exchange Rate

Nominal exchange rate of BDT against the United States Dollar (USD) has remained stable, between Tk. 77.8 and Tk. 78.4 throughout FY2015-16. This is largely due to open market operations of the Bangladesh Bank in the form of large scale foreign exchange purchases of USD, a policy being pursued consistently in recent years in order to strategically halt appreciation of the BDT. This policy of exchange rate interventions through foreign currency purchases, enacted towards the end of FY2011-12, has helped Bangladesh to maintain export competitiveness in the global market. This is reflected in the high growth in exports (22.3 per cent) over the past four years. The trade deficit is projected to decrease to USD 4,642 million by the end of the current fiscal year, which is similar to FY2014-15 end-year figures, thanks to recent recovery in exports of knitwear and woven garments to the US and the EU, as well as soft global commodity prices (World Bank, 2016a).

While Bangladesh's ongoing exchange rate policy has helped maintain export competitiveness, concerns have been voiced as regards its sustainability. The value of the USD against other major currencies has shown significant volatility over the past ten months, with the Euro appreciating during the first half of the fiscal year. Euro has steadily weakened since then. This has largely helped to maintain export competitiveness in the EU market. However, the exchange rate policies of Bangladesh's trading competitors and recent geo-trade partnerships threaten to weaken Bangladesh's export competitiveness in the short-term. Competitors, such as Vietnam, are maintaining stable exchange rate policies, for example, under which the Dong is pegged to a composite currency basket – this has allowed the Dong to move organically with Vietnam's major trading partners' currencies.[57]

[56] Back to back L/C opening growth in July-March FY2014-15 was 9.9 per cent compared to the corresponding period in FY2013-14.

[57] This could potentially hurt Bangladesh in the long-term – as the Trans-Pacific Partnership (TPP) comes into play, Vietnam will not only enjoy free-moving currency, but also gain preferential access to major markets in the US, Canada, Japan and Australia, all of which account for nearly 20 per cent of Bangladesh's exports.

Potential concerns regarding the current exchange rate regime

Some consideration should be given to the potential pitfalls of the policy to aggressively purchase USD to maintain exchange rate stability of the BDT. Regular foreign exchange intervention entails high opportunity costs as it involves forsaking resources, as these have to be diverted from more productive purposes. Foreign exchange reserves have grown by 43.6 per cent over the last 24 months, achieved in part through Dollar purchases by Bangladesh Bank from the local market. In turn, this has caused a substantial increase of over 25 per cent in broad money supply over the same period. In targeting foreign exchange replenishment through purchase of the Dollar, consideration needs to be given to its implications for inflation. Annual average inflation started to decline from January 2014, reaching 6.04 per cent in April 2016, which was less than the target for June 2016 (6.07 per cent). However, a rising trend can be observed in the case of non-food inflation, which was 7.21 per cent in April 2016. Besides, 13.5 per cent growth in broad money supply (as of March 2016) was below the monetary policy statement (MPS) target of 15 per cent. In view of the above, while inflationary pressure is not a concern at present, it would be advisable to keep a close eye on these monetary indicators so as to ensure that the current policy of buying Dollars to maintain nominal exchange rate does not lead to inflationary pressure. While the underlying policy eliminates exchange rate volatility, it only provides advantages to Bangladesh exporters who have pursued USD-based contracts with major trading partners. Returns from exports to the EU market fell sharply in FY2014-15, due to the relative weakening of the Euro, as roughly 20 per cent of all income was made via contracted payment in Euros. Careful consideration should therefore inform currency-specific contracts in order to limit potential losses.

Should Bangladesh pursue alternatives to monetary aggregate targeting exchange rate policies?

A more appropriate currency metric that is implicitly tied to export and import performance is the REER, which should be considered alongside the nominal exchange rate for trade policy purposes. While the nominal exchange rate of BDT has remained fairly steady in recent times, the REER has gradually appreciated in value over the last three years, peaking during the last quarter. The gap between the two rates displays the relative weakening of the Taka against major trading partners, which is particularly important given Bangladesh's efforts to increase its foothold in the EU market.

The impact of REER appreciation on export competitiveness, however, remains unclear (World Bank, 2016a), with it being significantly dependent on the current (and previous period) inflation rate, money supply, and relative price-elasticities of exports and imports (Branson, 1981).[58] A number of studies (Arize, 1994), which use co-integration methodologies, have found positive and significant long-run relationships between trade balance and REER in Asia over the 1980s and 1990s. In recent years, other studies (e.g. Perara, 2009) have found this relationship to be insignificant for Sri Lanka, while Dhasmana (2012) observed a positive association for India.[59] In the context of Bangladesh, Younus and Chowdhury (2014) have shown that, from 2003 to 2014, the REER has had no significant effect on trade balance or exports and imports when other major macroeconomic indicators are taken into account.[60] Hossain and Ahmed (2009) show that lower REER volatility in the 2000s was associated with a positive impact on exports, and argue for policies centered on the stabilisation of the REER in order to boost export competitiveness. The study also argued for a larger currency basket for REER estimation.

[58]Halting REER appreciation requires reducing the inflation rate, which is already experiencing a consistent decline over the current fiscal year.

[59]As of 2011, Sri Lanka has employed a similar monetary aggregate targeting exchange rate policy involving USD purchases, while India maintains a floating currency regime.

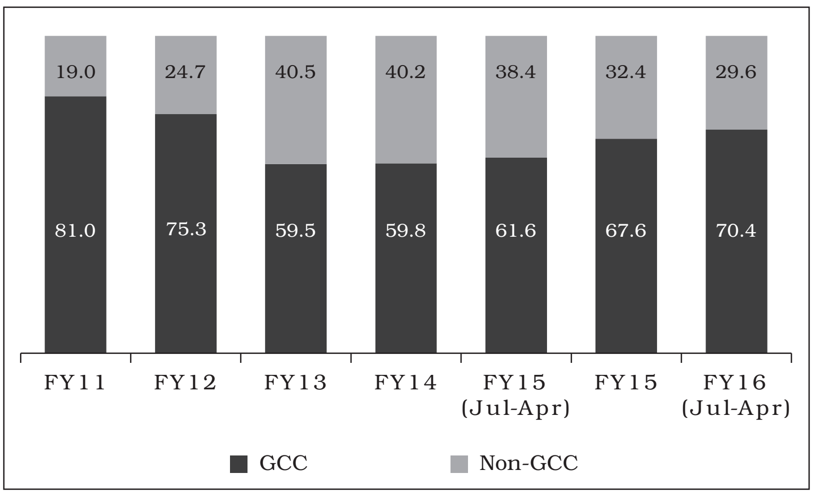
[60]This result, however, was contingent on using an 8 currency basket for REER calculations.

A time series analysis carried out for this study, which uses a combination of monthly REER estimates (138 currency basket, Bruegel Center)[61] and macroeconomic data for the past 25 years, provides some useful insights. The second column of Annex Table 1.8 shows that the absolute sum of import and export price elasticities have no statistical effect on the REER after controlling for inflation. This implies that global-level, rather than country-level, prices play a determining role in Bangladesh's trade movement. The third column of the same Table (results from an auto-regression model of trade balance determinants) shows that a large part of Bangladesh's trade balance movement can be explained by fluctuations in the REER. This suggests that the REER could be considered as an alternative basis for Bangladesh's trade policy. Consequently, using a basket of trading partners' currencies as a benchmark for intervention, rather than implicitly pegging the BDT against the USD, could help Bangladesh in pursuing a more preferred exchange rate regime, as this would help maintain export competitiveness in markets other than the US. In combination with structural reforms to address cyclical, as well as structural, factors concerning the external and internal fronts, such a policy could help sustain Bangladesh's export competitiveness from a broader perspective. In this regard, CPD recommends that Bangladesh Bank expand its currency basket for REER estimation so as to better factor in Bangladesh's current and future trade directions, and the emerging trading environment.

1.5.4 Migration and Remittances

Over the last two years, the number of international migrant workers has risen, from 222 million in 2010 to 244 million in 2015 (UNDESA, 2016). Bangladesh has also benefitted from this trend. Indeed, Bangladesh has experienced a phenomenal rise in international migration in FY2015-16 – the number of migrants going abroad during the first 10 months of FY2015-16 reached approximately 5.6 lakh, which is 51.2 per cent higher than the corresponding period of FY2014-15. Since October 2015, every month, on average, more than 50 thousand migrants travelled abroad for jobs. About 70.4 per cent of migrants went to Gulf Cooperation Council (GCC) countries in this period (Figure 1.28). Among these destinations, Saudi Arabia accounted for the highest incremental share (39.9 per cent) in this phenomenal growth. However, a significant number of people went to Oman (1.4 lakh), Qatar (1.2 lakh) and Malaysia (50.2 thousand). Migration to Singapore has been steady, at around 5 thousand workers per month. During the same

Figure 1.28
Composition of Outward Migration (% of Total)



Source: Calculated from Bureau of Manpower, Employment and Training (BMET) data.

61 Bangladesh Bank's REER estimates stem from a 10 country currency basket, which accounts for over 80 per cent of Bangladesh's total trade. In comparison, the countries that were used for the Bruegel Center's currency basket constitute over 99 per cent of Bangladesh's total trade. Nevertheless, both estimates show near identical movements over time, indicating that the countries that were not considered by the Bangladesh Bank estimate, but were used by the Bruegel Center, have not played a significant role in Bangladesh's overall trade movements.

period, female migration continued to surge. According to Bureau of Manpower, Employment and Trainging (BMET) data, the number of female migrants has now passed the 1 lakh mark (during July-April FY2015-16) for the first time in a single fiscal year since FY1991-92. 78 per cent of female migrants were destined for GCC countries, specifically for Saudi Arabia (with a share to the tune of more than 50 per cent).

However, growth of inward remittances has not matched this current trend of outward migration. During July-April FY2015-16, remittance inflows to Bangladesh declined by (-) 2.4 per cent over the corresponding period of FY2014-15. Indeed, globally, remittance inflows in 2015 registered a mere 0.4 per cent increase compared to 2014 – the slowest level of growth since the global economic crisis of 2008-09 (World Bank, 2016b). As can be seen from Table 1.18, other regional partners have also recently experienced subdued or negative growth in remittances.

Table 1.18

Comparative Analysis of Remittance Growth in FY2015-16

(in Per cent)

Country	Jul-Sep	Jul-Dec	Jul-Jan	Jul-Feb
Bangladesh	-1.9	0.0	-1.1	-1.5
Pakistan	4.0	6.3	6.0	6.1
Philippines	2.2	0.3	0.7	1.6
Sri Lanka	1.1	-3.0	-1.7	-0.6
Nepal	18.5	12.8	11.2	10.4

Source: Bangladesh Bank (www.bb.org.bd); Nepal Rastra Bank (www.nrb.org.np); the State Bank of Pakistan (www.sbp.org.pk); the Central Bank of Sri Lanka (www.cbsl.gov.lk); and the Bangko Sentral ng Pilipinas (www.bsp.gov.ph) (accessed on 19 May 2016).

Remittance inflows to Bangladesh from GCC countries declined by (-) 4.6 per cent in three quarters of FY2015-16.[62] However, global reports reveal that, following the recent fall in oil prices, remittance outflows from GCC countries (Saudi Arabia and Qatar[63]) increased by 7 per cent during July-September 2015.[64] GCC countries have used their substantial reserves to maintain spending levels and their currencies have remained stable.

There is a need for greater gender-sensitive policies in view of the rising number of female migrants from Bangladesh in recent times. This is needed both from the perspective of the home country (Bangladesh) and host countries (GCC countries). Rules, laws, institutions and programmes should be designed with gender in mind. Targets as regards ensuring safe, orderly and regular migration; limiting exploitation and abuse of migrants of all statuses; reducing the costs of recruitment and remittances; and improving data have all also been included in the SDGs.[65] In view of the SDGs, Bangladesh will need to make significant steps forward in this respect. Indeed, Bangladesh has no data on the number of returnee migrants so as to promote policies towards existing overseas migrants. Anecdotal information indicates that many Bangladeshi migrant workers have had to return home due to tightening labour markets and stricter visa regimes in major destinations (including Saudi Arabia, the United Arab Emirates (UAE), Kuwait and Malaysia). However, the actual number of returnees remains unavailable. Presently, Bangladesh is enjoying the benefits of the relatively cheap cost of sending remittances. However, a large number of migrants have remained outside the formal financial system and the tools available in host countries. As this year's chair of the Global Forum on Migration and Development (GFMD), Bangladesh has a real opportunity to contribute to good governance in global migration.

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[62] Indeed, remittances from other non-GCC countries recorded positive growth of 2.4 per cent after three quarters of FY2015-16.

[63] These two countries comprised around 50 per cent of total outward remittances from the GCC.

[64] See http://m.gulf-times.com/Story/494006

[65] These are included in the targets of SDG 8.8, SDG 10.7, SDG 10.c and SDG 17.18.

1.5.5 Foreign Exchange Reserves

Following Asian Clearing Union's (ACU) payment of USD 880 million, Bangladesh's foreign exchange reserves stood at USD 28.5 billion, as of 18 May 2016. Bangladesh Bank's continued intervention strategy of purchasing USD[66] from commercial banks with the aim of stabilising the foreign exchange market has resulted in growing reserve accumulation. This accelerated reserve accumulation is of course important from the perspective of providing safeguards and cushioning with respect to external shocks and uncertainties. Out of the official reserve assets, 87.3 per cent was kept in the form of convertible foreign currencies, of which 38.1 per cent was invested in securities and 49.2 per cent was kept in foreign national central banks.[67] Bangladesh Bank has been consistent in maintaining this particular composition of foreign exchange reserves, keeping the major proportion in safe but low-yielding foreign government securities with high liquidity. In comparison, India has 93.4 per cent of its foreign exchange reserves as foreign currency assets and 5.5 per cent as gold.

The current reserve is equivalent to more than 7 months' worth of imports. According to World Development Indicator (WDI) data, Bangladesh's foreign exchange reserves in 2014 were capable of ensuring 5.4 times the full coverage of short-term debt, which is the same as Bangladesh's RMG sector competitor, Cambodia.[68] This ratio was 1.1 for Sri Lanka, 2.6 for Vietnam, 3.8 for India and 4.9 for the Philippines. From an import dependency perspective, Bangladesh's imports were equivalent to 27.5 per cent of GDP in 2014. Other countries with a similar level of import dependency[69] tend to maintain the same reserves to GDP ratio as Bangladesh. From this perspective, Bangladesh's reserve level does not appear to be significantly high, although it is still capable of providing a cushion in case of any surge in import or other payments.

1.6 AN ASSESSMENT OF RECENT DYNAMICS IN THE CROP SECTOR AND POLICY RESPONSES

Bangladesh's crop sector has always played a critically important role from the perspective of meeting food security and job creation. As is known, the sector is dominated by rice cultivation. Thanks to a considerable rise in crop intensity and significant technological progress, Bangladesh has achieved near self-sufficiency in rice production. From a crop intensity of 177 per cent in FY2004-05, this increased to 190 per cent in FY2012-13. During this period, rice production rose by about 40 per cent, while other crops also experienced a rise in production. In recent years, there has been a widespread claim that increasing irrigation costs, higher costs of agricultural labour, and higher returns from cultivation of alternative crops, are discouraging farmers to remain engaged in rice cultivation. This has also been corroborated by research (Lagos and Hossain, 2016; IAPP, 2013). These apprehensions are also supported by a growing concern that sustaining rising productivity in rice cultivation will become more challenging in the future than it has been in the past. Boro rice cultivation, which has been the main driver of crop productivity in Bangladesh, is nearing the limits of existing technological potential. Land expansion is no longer a feasible option in Bangladesh, rather land available for cultivation is expected to decline with increasing urbanisation. Expansion of irrigation has also reached a certain limit. According to the World Bank (2016c), the most significant challenge facing agriculture is the overuse, degradation and change in quality of critical natural resources, including land and water. These challenges have been recognised in the 7FYP of Bangladesh, and a number of policies have been put forward to address these issues. In view of the above, this section revisits the recent trends in acreage of rice cultivation, as well as other major crops, to identify any major

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[66]Bangladesh Bank purchased USD 3.76 billion in FY2014-15, USD 5.15 billion in FY2013-14, and USD 4.54 billion in FY2012-13. During the ongoing FY2015-16, Bangladesh Bank has to date purchased USD 2.16 billion (as reported on 5 January 2016).

[67]Special Drawing Rights (SDRs), gold, and export development funds are the other major elements that account for 4.3, 1.9 and 6.4 per cent of the reserve respectively.

[68]This is one of the most widely-used standards of adequacy: Greenspan-Guidotti rule of 100 per cent coverage of short-term debt or "reserve to short term external debt ratio" greater than 1.

[69]This includes Indonesia (22.7 per cent), India (27 per cent) and Sri Lanka (29.4 per cent). Reserve to GDP ratio of these countries is 0.13, 0.16 and 0.1 respectively, which is approximate to Bangladesh's 0.13 ratio.

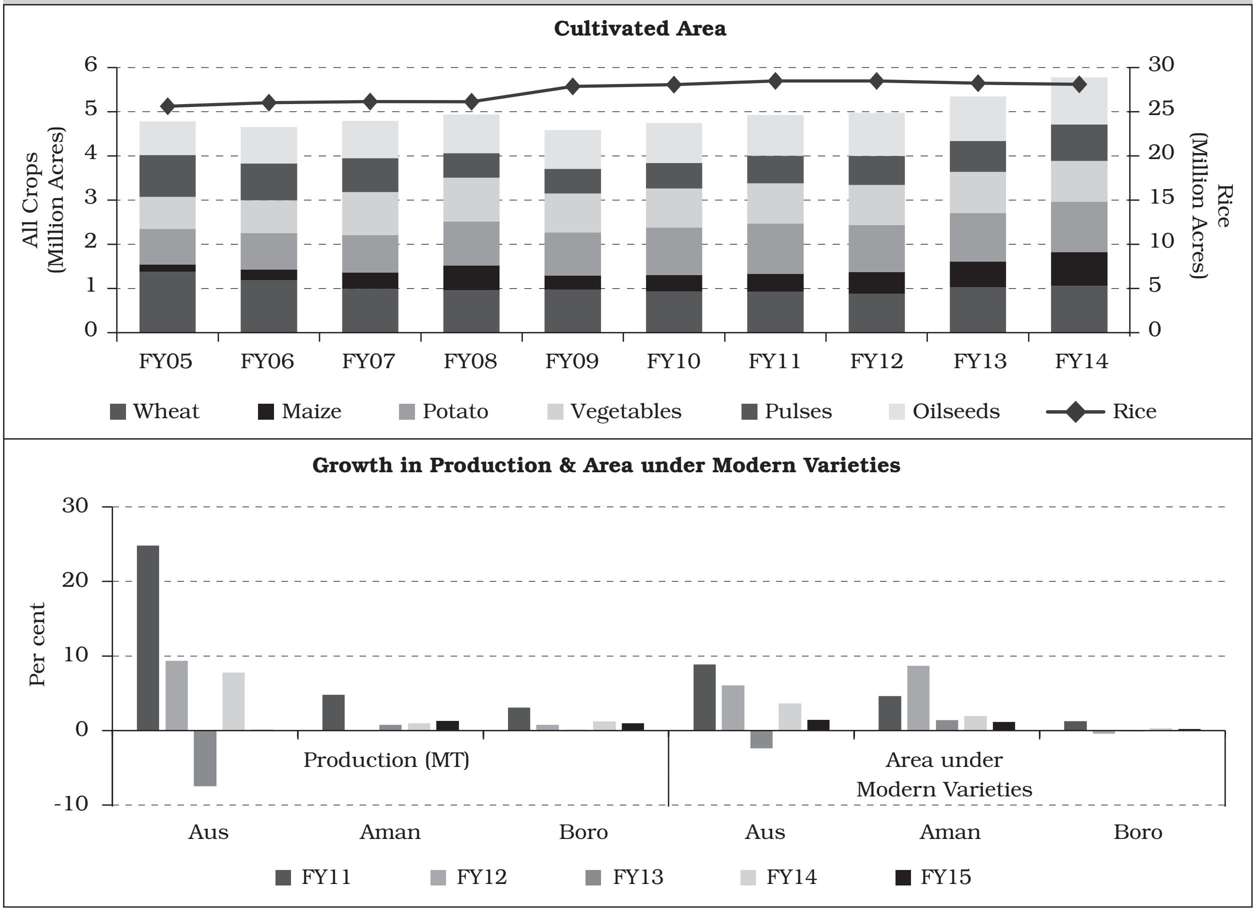
shifts in cultivation patterns. Existing government policies relating to the crop sector will also be discussed in this regard. This section also examines current fiscal-budgetary policies in the crop sector and assesses their implications.

1.6.1 Recent Trends in the Crop Sector

As is known, rice cultivation plays the most important role in Bangladesh's crop sector. However, other crops that are increasing in importance include root crops, jute, maize, and (to some extent) wheat and vegetables. Curiously, land use for rice cultivation[70] has declined since FY2012-13. In FY2011-12, the total land used for rice cultivation was approximately 28,487 thousand acres. However, this decreased to 27,907 thousand acres in FY2015-16, a decline of around (-) 2 per cent (Figure 1.29). Further, the area under rice cultivation experienced a drop of (-) 1.1 per cent (303 thousand acres) in FY2015-16 compared to FY2014-15. This was largely attributed to a (-) 3.2 per cent decline in the land area under Boro cultivation (383 thousand acres).[71] On a welcome note, however, combined production of Aus and Aman in FY2015-16 rose by 1.6 per cent. Anecdotal information also suggests that Boro production in FY2015-16 will be consistent

Figure 1.29

Recent Dynamics in the Crop Sector



Source: Estimated from Bangladesh Bureau of Statistics (BBS) and Department of Agricultural Extension (DAE) data.

Note: Modern variety includes both high-yielding varieties (HYVs) and hybrid varieties together.

[70]This includes Aus, Aman and Boro.

[71]Cultivated area under Aman increased by 148 thousand acres, while that for Aus decreased by (-) 67 thousand acres.

with production in the previous year. Overall therefore, despite a decline in total land area under rice cultivation, total production in FY2015-16 may be similar to that of the preceding year (FY2014-15).

More precisely in the case of rice crops, over the last five years, production growth rates of Aus and Aman were comparatively higher than that of Boro, although higher volatility is also present. This trend perhaps indicates the following: i) that Bangladesh has nearly reached the existing technological frontier for Boro[72] cultivation (World Bank, 2016c); ii) that there is a greater adoption of modern varieties during the Aus and Aman season; iii) and that volatility of climatic variables (e.g. maximum temperature)[73] has significantly increased over the last decade (since 2002) relative to the previous decade. In contrast, average annual rainfall[74] has decreased over the same period, showing a higher degree of volatility in the monsoon months (April-October). Assuming no immediate advancement in technology, any scope for further increase in rice cultivation may only be possible through expansion of modern varieties during the Aman and Aus season, while maintaining the existing level of Boro production. Recent incentive policies pursued by the government also indicate support for Aus and Aman.[75] As it is, climate variability has added to uncertainties faced by farmers in cultivating rice during the Aus and Aman season. In addition, excessive use of water for irrigation is causing the groundwater table to fall even further making irrigation even more costly (Alauddin and Sharma, 2013; Alauddin *et al.*, 2014).

Against this backdrop, ensuring incentivised prices for rice farmers has become a major challenge for policymakers. Recent reports from various sources suggest that farmers are unable even to recover the cost of production, let alone make profits. According to Lagos and Hossain (2016), on average, Boro farmers had to incur a loss of around 18 per cent in Boro production in FY2014-15. In view of this emergent scenario, farmers may be induced to switch to more profitable crops, particularly maize and wheat. The government will need to therefore calibrate its strategies and policies in a way that maintains a balance between rice security and crop diversification, keeping in mind the imperative of ensuring food security and nutrition.

1.6.2 Analysis of Planning and Policy Documents

Government policy actions and initiatives targeted towards dealing with the aforementioned challenges will be guided by existing medium term plans and strategies. A review of plan and policy documents, including the 7FYP, the SFYP, the National Agriculture Policy (NAP) 2013, and the MTBF of the Ministry of Agriculture (MoA), indicate four broad policy stances. Brief discussion of each of these is presented below.

Crop-zoning and climate change adaptations

In the 7FYP, the government has placed greater emphasis on expanding the cultivation of agri-crops in adverse agro-ecological zones (AEZ[76]), including in the hill tracts. To encourage crop-zoning and climate change adaptation, the planning document also recommends the promotion of modern farming practices in drought, submergence and salinity-prone areas; support to green growth agriculture by intensifying organic farming; increasing the coverage of cultivable land under high-yielding and hybrid varieties; and diversification of crop cultivation in line with nutritional demand.

[72]According to BBS estimates, in 2014-15, cultivatable land for modern varieties of Boro, Aman and Aus was 99 per cent, 78 per cent and 73 per cent respectively.
[73]Average annual maximum temperature during 1989-2001 and 2002-2013 was 33.54ºC and 33.97ºC respectively.
[74]Average annual rainfall during 1989-2001 and 2002-2013 was 2485 mm and 2416 mm respectively.
[75]This can be observed from various Ministry of Agriculture (MoA) circulars.
[76]Bangladesh has identified 30 AEZs to promote crop-zoning, considering soil quality and river hydrology.

Input support

Taking inspiration from policies and strategies set out in the SFYP and the NAP, the 7FYP has continued to emphasise efficient and balanced utilisation of land, water and fertiliser. The importance of using more surface water for irrigation has been reiterated. In addition, the use of deep tube-wells for irrigation purposes has been discouraged, while the use of force-mode pumps was encouraged instead of suction-mode pumps in water-scarce regions. Installation of solar panels for small-scale irrigation in rural areas has also been given priority.

Price support

Besides continuation of price support to farmers through existing procurement policies, other measures that have been given priority in the 7FYP and NAP include ensuring agricultural machinery availability at affordable prices for farmers through tax rebates and other measures, granting soft loans for the cultivation of selected crops, and incentivising farmers through easy and better access to credit. Although crop insurance for farmers was mentioned in the 7FYP, to date no significant progress has been made in this regard.

Research and institutions

The 7FYP pledged to increase budgetary allocation for agriculture-related research. Scientific research to improve and discover genetic modification technology at the farm-level, research for the promotion of AEZ-specific crops, and efficient and balanced use of water for irrigation, have all received heightened attention compared to previous plan documents. In addition, the establishment of a detailed collective database by agricultural research institutes was also planned in the NAP.

Indeed, in the 7FYP, crop diversification was given special attention as part of the nutrition strategy. Utilising the AEZs, the government has continued to support crop-zoning to promote market-based agriculture. The use of surface water for irrigation was given priority, while balanced use of fertiliser has been reiterated once again. Easy and better access to credit for farmers has also been mentioned. In addition, in an attempt to stimulate higher-valued crop production, research and development (R&D) has received increased allocation in the agriculture budget. However, it should be noted though that, rather than a rise, a gradual decrease in budgetary allocation for the agricultural sector is in fact clearly discernible.

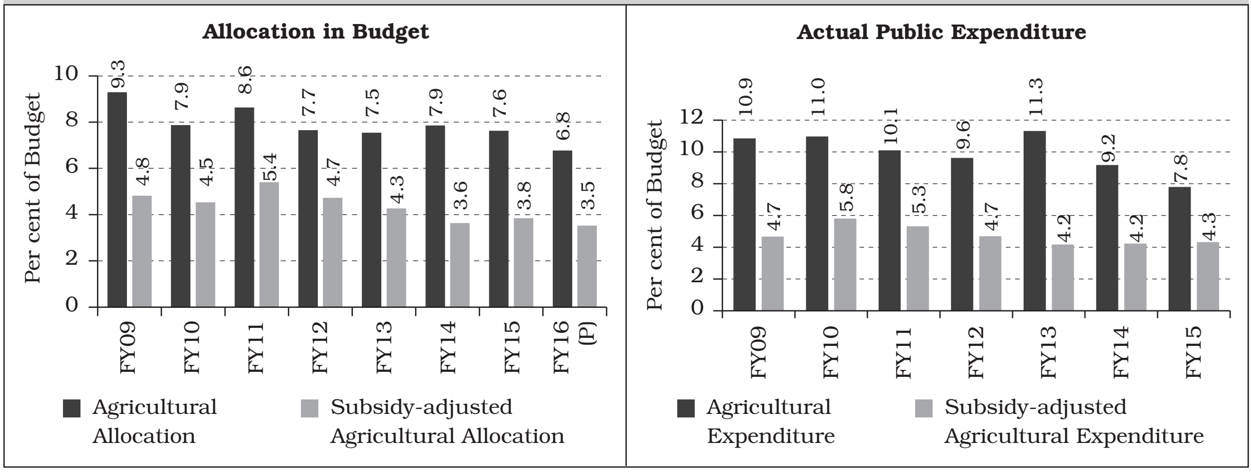
1.6.3 Budgetary Allocation and Market Interventions in Agriculture

Since FY2008-09, budgetary allocation and actual expenditure in agriculture as a share of total budget has been, on the whole, in decline (Figure 1.30). Subsidies for fertiliser and irrigation form a major share of the total agricultural allocation. The share of the allocation to such subsidies has, understandably, been in relative decline, as international prices of fertiliser have been at lower levels. While the government did not reduce fertiliser prices in response to these lower international prices, the fiscal space gained was not redirected to other heads of the agricultural sector. Adjusted for subsidy, the allocation for agriculture still experienced a decline, from 5.4 per cent of the FY2010-11 budget to 3.5 per cent of the FY2015-16 budget. It is worthwhile noting, however, that in terms of actual expenditure, the agricultural sector share has been relatively high for most years, given that other sectors have systematically failed to spend their respective allocation over the corresponding period.

Since FY2008-09, budgetary allocation for agriculture as a share of GDP, both with and without subsidy, remained more or less unchanged, at approximately 1.2 per cent and 0.6 per cent respectively (Figure 1.31). With the exception of the last two fiscal years (FY2013-14 and FY2014-15), total public expenditure on agriculture as a share of GDP was higher than its respective allocation. This trend has been largely influenced by higher demand for subsidies. As international prices of commodities fell, including

Figure 1.30

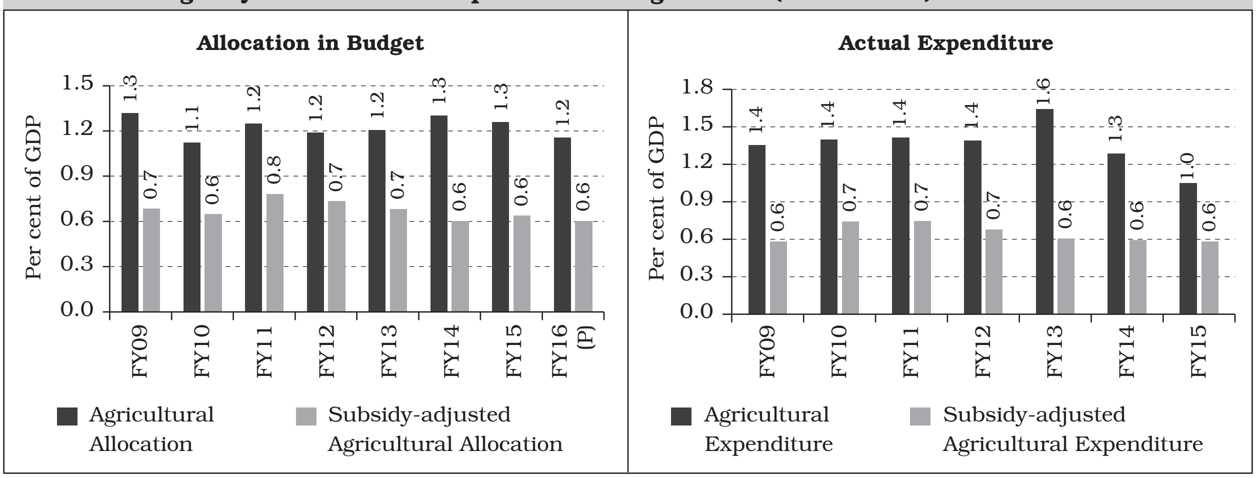
Trends in Budgetary Allocation and Expenditure for Agriculture (as % of Total Budget and Expenditure respectively)



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

Figure 1.31

Trends in Budgetary Allocation and Expenditure for Agriculture (as % of GDP)



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

those for agriculture, demand for agricultural subsidies was lower than what had been earmarked for FY2013-14 and FY2014-15 – this trend is likely to also continue into FY2015-16.

A window of fiscal space

Given that Bangladesh meets most of its fertiliser demands by importing from the international market, in order to safeguard the interests of farmers, the government typically allocates a significant share of the agricultural subsidy to fertiliser. In recent times though, lower global prices have provided the government with increased fiscal space. From FY2013-14 to FY2015-16, international prices for urea, triple superphosphate (TSP), di-ammonium phosphate (DAP) and muriate of potash (MoP) have experienced an average annual decrease of around 13.4 per cent, 6.2 per cent, 6.1 per cent and 8.5 per cent respectively. For each year from FY2013-14 to FY2015-16, the government's subsidy allocation for the agricultural sector was approximately Tk. 9,000 crore. However, actual expenditure on agricultural subsidies was Tk. 7,095 crore in FY2014-15, which is around Tk. 2,000 crore less than the original allocation. The actual figure for FY2015-16 is likely to be similar to that of FY2014-15. Early indications suggest that in the FY2016-17 budget, Tk. 9,000 crore will once again be earmarked for subsidies in the agricultural sector. However, according to CPD estimates, the requirement for agricultural subsidies in FY2016-17 is not expected to exceed Tk. 7,000-7,300 crore. The government could therefore end the year with fiscal space equivalent to approximately Tk. 1,700-2,000 crore. This provides an opportunity for enhancing budgetary allocation to other heads under the agricultural sector, however, it is not certain whether this opportunity will be taken advantage of by the government. Maximising this opportunity will require appropriate planning and enhancement of the MoA's utilisation capacity.

Implementation of selected ADP crop sector projects

There is a need to prioritise and align the implementation of agricultural projects with medium to long-term strategies set out for the agricultural sector. In this backdrop, an analysis of a selected number of agricultural sector projects from the FY2015-16 RADP has been undertaken. In the course of this analysis, of 149 agricultural projects, 56 concerning the crop sector and irrigation were selected. The costs involved in these projects was equal to or greater than Tk. 12 crore. Among these projects, 30 are related to input management, while 16 concern crop-zoning and climate change adaptation. Among other projects, nine were related to research and institutions, and one to price mechanisms. Based on their implementation status and possible completion date, the selected 56 projects were further disaggregated into five categories: a) carryover and to be completed later than FY2015-16; b) carryover and to be completed by FY2015-16; c) to be completed in FY2015-16; d) continuing beyond FY2015-16; and e) newly adopted in FY2015-16.

Among the 56 projects, eight were initially planned to be completed by (or before) FY2015-16, however, these have all already received time extensions beyond FY2015-16. The 13 projects (six carryover projects and seven completing projects) that are supposed to be completed within FY2015-16 (according to the FY2015-16 RADP) are still far from completion. Only one project, which is related to surface water-based irrigation system development, received adequate allocation to enable completion within the stipulated time (by FY2015-16). However, only 70 per cent of the allocated project costs had been spent as of November 2015. It is therefore highly unlikely that even this project will be completed within FY2015-16. Indeed, time overrun is quite common for agricultural projects. The 15 projects that received time extensions (either once or more than once) had an average project life of around 42 months. These projects, on average, have already received an additional 35 months extension (83.6 per cent). Similarly, average project cost overrun was estimated to be around 21 per cent. Indeed, among the selected 56 projects (of which 16 projects are newly adopted), 14 projects were subject to one revision, while 11 projects required two revisions to be carried out. Project take-off has also been found to be delayed. Of the 16 new projects adopted in the FY2015-16 ADP, in nine projects not a single taka was spent during the first five months of FY2015-16. Project implementation performance was relatively better for projects related to input support, followed by research and institutions, and then crop-zoning and climate change adaptation.

In summary, while the government has made plans and initiated projects in line with medium to long-term strategies, as a result of institutional and administrative weaknesses, particularly at the implementation stage, the projects are not being completed on time. Consequently, farmers and the sector as a whole are being deprived of the envisaged benefits.

Delayed government interventions

Over the last year or so, the government has undertaken a number of market interventions to protect the interests of farmers. On 11 May 2015 (during the third week of Boro harvest (according to the BBS' crop calendar)), the government imposed a 10 per cent regulatory duty (RD) on rice imports in view of high imports of rice and lower prices in the domestic market. However, the initiative had an insignificant impact. Boro farmers were not able to cover cultivation costs. On 7 December 2015 (in the first week of the Aman harvest), a second round of an additional 10 per cent of RD was imposed on imports of rice.

As is known, diesel is one of the main inputs in the irrigation process. In the backdrop of low global prices, the government recently (on 24 April 2016, the first week of the Boro harvest) adjusted fuel prices. However, while the price of diesel was decreased by just over 4 per cent, the prices of octane and petrol were reduced by about 10 per cent. Indeed, farmers failed this year to reap any benefit of this reduction given that the irrigation period of Boro cultivation was already complete. One day later, on 25 April 2016, the government announced its plan to procure 7 lakh tonnes of paddy at Tk. 23/kg and 6 lakh tonnes of rice at Tk. 32/kg during the current Boro season. The procurement timeline has been set from 5 May 2016 to 31 August 2016 – during the first month (May 5 to June 5), only paddy will be collected. The target and price for Boro paddy procurement was increased to ensure fair prices for farmers.[77] The government has prioritised the collection of Boro paddy from the farmers themselves rather than from middlemen – this is indeed a welcome initiative. However, according to field-level information, the government was unable to start the procurement process on time. This absence of the government in the paddy market has resulted in low paddy prices for producers in the harvesting season. Consequently, farmers, particularly those who are having to opt for 'distress selling', will likely once again incur considerable losses from Boro cultivation. There is therefore a need to urgently expedite the government's procurement process.

1.6.4 Policy Perspectives

Although the total land area under rice cultivation has decreased in FY2015-16, this may not significantly affect total rice production this year. However, given concerns that rice production in Bangladesh has already reached a 'technological frontier', concerted efforts will be needed to target higher productivity and more productive technology. It is true that there is some scope to adopt modern varieties, especially in the case of Aus and Aman cultivation, however, opportunities as regards Boro, the dominant crop, are rather limited. The increase in the land area for cultivation of potatoes, maize, wheat and vegetables is being dictated by farmers' commercial interests. There is therefore limited option but to ensure further rises in yield. In the backdrop of the adverse impacts of climate change, a fall in the ground water table, and increasing crop cultivation costs, the government will be required to design appropriate policy incentives and provide support to safeguard Bangladesh's food security. The government should make the best use of the fiscal space provided by reduced subsidy demand for fertilisers.

Additionally, a further reduction in the administered price of diesel may be considered. The government has already decided to allow exports of rice, which may induce some higher price adjustment. Adequate stocks, however, should be maintained for emergency support and market interventions when needed. The procurement process needs to be expedited to ensure that farmers reap the benefits of government-provided price support. The emerging fiscal space may be utilised to incentivise Aus and Aman cultivation, as well as to encourage greater agricultural diversification initiatives. The balanced use of fertilisers should be encouraged through the calibration of subsidies to different types of fertiliser. Higher subsidies could also be given to granular urea compared to its powdered form.

1.7 RECENT TRENDS IN THE LABOUR MARKET: SLOW UPTAKE IN EMPLOYMENT DESPITE IMPRESSIVE GDP PERFORMANCE

According to projections made by the Bangladesh Bureau of Statistics (BBS), GDP growth in Bangladesh could, for the first time in recent history, exceed 7 per cent. However, the services and pay-hike-driven nature of this growth has already given rise to concerns about its implications for job creation. In a country

[77] In the previous Boro season, the government procured 1 lakh ton of paddy at Tk. 22/kg and 10 lakh tonnes of rice at Tk. 32/kg.

Table 1.19

Employment to GDP Elasticity (% Change in Employment for a Corresponding 1 per cent Increase in GDP)

Component	2010	2013	2015 (Jul-Sep)
Elasticity	0.5776	0.3307	0.0796

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

like Bangladesh, which is going through a period of potential demographic dividend, labour market dynamics and employment are issues of particular importance. Employment elasticity to GDP, which is a measure of how employment varies with the growth of economic output, appears to have fallen sharply over the last five years, from 0.58 in 2010 to 0.08 in 2015 (Table 1.19).[78] High GDP growth has not been reflected in new job creation, raising questions about the nature of growth and the need to understand key bottlenecks that impede higher employment generation in the economy. As the share of the working age population in Bangladesh increases, there is a clear and growing need to secure employment for these people. Skill upgrades and productivity enhancement are becoming increasingly important issues to tackle if Bangladesh is to make its transition from a factor-driven to efficiency-driven economy, ready to take full advantage of its recently earned middle-income status.

In this backdrop, the present section seeks to give an overview of current labour market dynamics, based on information generated by the inaugural Quarterly Labour Force Survey (QLFS)[79], carried out by the BBS. A comparison has also been made to previous rounds of annual LFS so as to identify some of the key areas that call for further discussion and necessary policy initiatives. Addressing labour market issues is emerging as a major policy concern. In order to identify potential areas for labour-centric growth, a number of concerns emerging from the latest QLFS demand particular attention from a policy perspective.[80]

While labour force and employment experienced slow growth, the labour force participation rate continued to stall

Generally impressive economic performance since the early 2000s was, up until 2013, accompanied by strong growth in the Bangladesh labour force, particularly in the case of females. This trend, however, is currently showing signs of stagnation. As data shows, the labour force has only grown by 0.7 million over the last two years.[81] The urban labour force, which experienced significant growth due to a surge in internal migration between 2006 and 2013, suggests signs of recent stabilisation due to a combination of increased male and reduced female urban labour force participation (Table 1.20). From 2002 to 2013, the number of jobs rose at an impressive rate of 1.36 million per year, however, this rate has fallen to only 0.3 million since 2013 (Table 1.21).[82] The labour force participation rate has remained fairly stable over time, although its peak rate of 59.3 per cent has not been achieved since 2010 (Table 1.22). This is largely driven by a decrease in the female labour force participation rate, from 36 per cent in 2010 to 33.9 per cent in September 2015, with only 0.1 million new females entering the workforce each year.

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[78] At a time when growth is primarily dominated by low-skill industries, over-reliance on low-skill workers could potentially result in undercompetitiveness of human capital-intensive exports when competing with high-skilled labour from developed trade competitors.

[79] A major advantage of the QLFS over prior surveys is that the sample is a quasi-panel, which provides scope for dynamic analysis of employment trends.

[80] It is perhaps important to note that interpretation of quarterly results needs to consider seasonal variations in employment trends. As the QLFS only covers the months of July to September, a comprehensive overview of labour market situation in FY2015-16 may not be fully reflected in the data.

[81] BBS has reported that the large shift of unpaid family workers to paid employment between 2013 and 2015 explains why overall employment figures remained stagnant.

[82] However, the reference period for the QLFS was during a period of low rural farm-based employment opportunities, possibly indicating seasonal variance in employment.

Table 1.20
Size of the Labour Force

(Million)

Criteria	2002-03	2005-06	2010	2013	2015 (Jul-Sep)
Male	36.0	37.3	39.5	42.5	43.1
Female	10.3	12.1	17.2	18.2	18.3
Urban	11.3	11.7	13.3	17.1	17.2
Rural	35.0	37.8	43.4	43.5	44.2
Total	**46.3**	**49.5**	**56.7**	**60.7**	**61.4**

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

Table 1.21
Size of the Employed Population

(Million)

Criteria	2002-03	2005-06	2010	2013	2015 (Jul-Sep)
Male	34.5	36.1	37.9	41.2	41.8
Female	9.8	11.3	16.2	16.8	17.0
Urban	10.7	11.3	12.4	16.2	16.4
Rural	33.6	36.1	41.7	41.9	42.4
Total	**44.3**	**47.4**	**54.1**	**58.1**	**58.7**

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

Table 1.22
Labour Force Participation Rate

(in Per cent)

Criteria	2002-03	2005-06	2010	2013	2015 (Jul-Sep)
Male	87.4	86.8	82.5	81.7	82.5
Female	26.1	29.2	36.0	33.5	33.9
Urban	56.8	55.7	57.3	56.7	55.8
Rural	57.5	59.4	60.0	57.3	58.7
Total	**57.3**	**58.5**	**59.3**	**57.1**	**57.9**

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

Although unemployment has remained steady, gender disparities continue to prevail

As the data indicates, the national unemployment rate increased between 2002 and 2010, peaking at 4.5 per cent. It has since remained steady over the last two years at 4.3 per cent (Table 1.23). Rural-urban

Table 1.23
Unemployment Rate (% of respective Labour Force)

Criteria	2002-03	2005-06	2010	2013	2015 (Jul-Sep)
Male	4.2	3.2	4.1	3.0	3.1
Female	4.8	7.4	5.8	7.2	7.0
Urban	5.3	4.3	6.8	5.8	4.7
Rural	4.0	4.2	3.9	3.7	4.1
Total	**4.3**	**4.2**	**4.6**	**4.3**	**4.3**

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

variations are also becoming more pronounced, with a reduction in the urban unemployment rate being met with a corresponding rise in the rural unemployment rate (which is currently at a ten year high), possibly as a result of increased rural-to-urban migration in recent years. The female unemployment rate has recently fallen, although only marginally, remaining more than twice the rate of male unemployment.

Composition of employment – a shift favouring the tertiary sector

Between 2013 and 2015, the number of unpaid family workers declined by 31 per cent (Table 1.24). Possible reasons for this include a general reduction in agricultural farm-based employment, which is often family-operated.

Table 1.24
Employment Status

(Million)

Component	2002-03	2005-06	2010	2013	2015 (Jul-Sep)
Self-employed/own account workers	19.8	19.9	22.0	23.6	26.7
Employer	0.2	0.1	0.1	0.5	1.7
Employee (including day labourer)	15.0	15.2	18.4	22.5	22.8
Unpaid family helpers	8.1	10.3	11.8	10.6	7.3
Others	1.2	1.9	1.4	0.9	0.2
Total	**44.3**	**47.4**	**54.1**	**58.1**	**58.7**

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

Employment by industry has displayed some diverse patterns. Decline in agricultural and industrial employment has been compensated for by a surge in services sector jobs. The share of female employment in agriculture has recently increased, balanced by a drop in male agricultural employment – possible reasons for this could stem from increased domestic and international migration, which has until now been mainly male-dominated, as well as improved non-farm opportunities in rural areas.

Within the secondary sector, the manufacturing industry has experienced a strong decline in jobs from 2013 to 2015, in a reversal to the sharp growth experienced in earlier years. The data indicates that job losses in manufacturing almost entirely affected female workers (Annex Table 1.9). A combination of 600 factory closures in the last three years and a projected closure of 319 more by the end of FY2015-16[83] is likely to exacerbate this situation.[84]

Almost all service sectors experienced a decent rate of job growth. Growth in construction, transportation and other urban area centric services accounted for the share of labour that has moved out of the primary sector (Annex Table 1.9). Evidence also suggests that the labour force has slowly been moving out of the secondary sector (Table 1.25). Whether this is because new jobs are not being created in the manufacturing sector in large enough numbers, or whether such jobs are becoming relatively more capital-intensive, needs to be further examined.[85] In view of this, a more in-depth analysis of labour, capital and total factor productivity in the manufacturing sector is needed. There is also a need to improve survey indicators pertaining to inter-

[83]See http://www.thefinancialexpress-bd.com/2016/05/14/30184/BGEMA-seeks-reduction-of-tax,-VAT--for-RMG-sector

[84]This could be in part because of the slowdown in female employment opportunities in the export-oriented RMG sector following the Rana Plaza disaster in April 2013.

[85]The 2013 World Bank Enterprise Survey reveals that private sector firms experienced negative annual labour productivity growth of (-) 4.7 per cent from 2010 to 2013. In the light of near-zero global annual labour productivity growth in recent years, continuation of this trend would provide some evidence of the growing importance of capital in the secondary sector.

Table 1.25
Employment by Broad Economic Sectors

Sector	2010	2013	2015 (Jul-Sep)	2010	2013	2015 (Jul-Sep)
	Employed by Broad Economic Sector (Million)			Composition of Broad Economic Sector (%)		
Agriculture	25.7	26.2	25.8	47.6	45.1	43.9
Industry	9.6	12.1	11.5	17.7	20.8	19.6
Services	19.1	19.8	21.5	25.5	26.4	28.6
Total	**54.1**	**58.1**	**58.7**	**100.0**	**100.0**	**100.0**

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

sectoral labour mobility so as to better capture emerging job opportunities and occupational shifts. This in turn will help to better understand the push-pull factors as regards internal labour migration.

Employment remains largely informal in nature

Recent GDP growth has been primarily dominated by industries that require low-skilled labour. The relatively large size of the informal economy (Table 1.26) indicates that a reversal of this trend in the short-term is unlikely. A large part of the rural male labour force, particularly youth, have moved into formal employment over the last two years. The opposite trend, however, was observed amongst the urban female labour force, which has experienced strong growth in informal employment. As the female urban labour force constitutes over a quarter of the total female labour force, this is a potential cause for concern, as increased informality means a larger number of female workers opting for jobs with lower real wages and poorer working conditions.

Table 1.26
Share of Informal Employment (% of respective Labour Force)

Criteria	2010	2013	2015 (Jul-Sep)
Male	32.4	35.6	34.0
Female	14.9	15.2	15.7
Urban	9.3	12.1	12.7
Rural	38.0	38.6	37.1
Total	**47.4**	**50.8**	**49.8**

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

However, there are also some evidences indicating some level of increased formalisation of the job market. Informal employment has decreased amongst higher educated labourers, as the share of informal workers with higher secondary and tertiary education has decreased significantly, by 18 per cent and 21 per cent respectively, indicating that the demand for skilled lwabour is on the rise. The economy has also experienced an overall decline in informality across the agricultural and industry sectors since 2013. While the services sector has experienced a small rise in the number of informal jobs[86], a significantly larger increase in formal services sector employment indicates a general shift towards formality. As the share of labour moves out of the primary sector, and the economy experiences strong growth in the tertiary sector, the scope for the provision of 'decent work' will grow in the medium-term. Labour Force Surveys would benefit from better

[86]This was largely driven by the increase in informal urban employment, as observed through increased employment in construction, transportation and other similarly low-skilled work.

identifying jobs that may be characterised as 'decent jobs'[87], so that policymakers are able to understand to what extent 'decent jobs' are being created in the economy, and address the associated challenges.

Regressive trends in employment by skill level

The adult literacy rate in Bangladesh improved from 47.5 per cent in 2002 to 61.5 per cent in 2015. This has been driven primarily by a significant rise in female education in recent years. The need for skill upgrades has now become more urgent, particularly in the secondary and tertiary sectors. Table 1.27 shows that unemployment amongst labour force participants with secondary, higher secondary and tertiary education has risen over the last two years, while the opposite is the case for uneducated workers. Policy measures are therefore needed to create job opportunities that correspond to the skill and educational levels of the labour force. In this context, there is a need to enhance the number of workers through increased resource mobilisation for Technical and Vocational Education and Training (TVET). Proper incentives should be created for this, plus measures are needed to ensure that appropriate jobs are available for them when they enter the job market.

Table 1.27

Unemployment Rate by Education Level (% of respective Labour Force)

Criteria	2010	2013	2015 (Jul-Sep)
No education	2.8	3.2	2.1
Primary	3.8	2.7	2.9
Secondary	6.6	4.4	5.2
Higher secondary	13.7	7.9	11.8
Tertiary	8.3	6.7	5.7
Total	**4.5**	**4.3**	**4.3**

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

Rising concerns regarding youth unemployment

There is growing evidence of underutilisation of youth (aged 15-29) in the Bangladesh labour force. Indeed, the youth unemployment rate has risen steadily between 2010 and 2015, more so for female youth (aged 15-24). As of September 2015, nearly one in ten young people were unemployed (Table 1.28), which is more than twice the overall national unemployment rate. The share of youth unemployment amongst those with secondary and higher secondary education is almost three-times higher than that of young people with only primary-level education (Table 1.29). Some decline in the youth employment rate (as a share of the respective population group) may be due to greater access to education, which has meant more young people have remained in school – this is also reflected in the rising literacy rate. Female youth unemployment has increased sharply for those with primary, secondary and higher secondary education, which is indeed a worrying trend.

As youth constitute over a quarter of Bangladesh's population, and youth employment is emerging as a growing concern, heightened attention will need to be given to training and to incentivising the private sector to create more jobs that correspond to the skills of young people. Particular attention should be given to job creation for female youth.

[87]The International Labour Organization (ILO) classifies "decent work" as opportunities for work that are productive and deliver a fair income, security in the workplace, freedom for people to express their concerns, and equality of opportunity and treatment for all men and women.

Table 1.28

Youth Unemployment Rate by Age Group (% of respective Labour Force)

Criteria	2010	2013	2015 (Jul-Sep)
15-19 (Total)	10.6	10.2	13.9
15-19 (Male)	10.2	10.4	11.5
15-19 (Female)	11.4	9.8	19.5
20-24 (Total)	7.1	9.0	10.9
20-24 (Male)	6.8	9.0	9.2
20-24 (Female)	7.7	9.1	14.0
25-29 (Total)	5.4	6.3	6.0
25-29 (Male)	4.3	4.1	4.5
25-29 (Female)	7.3	10.4	9.0
Total	**7.4**	**8.1**	**9.5**

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

Table 1.29

Distribution of Youth Unemployment by Education Level (% of Total Unemployed Youth)

Criteria	2010	2013	2015 (Jul-Sep)
No education (Total)	15.7	12.8	7.5
No education (Male)	13.4	5.1	6.2
No education (Female)	18.8	7.7	9.1
Primary (Total)	21.4	17.2	15.1
Primary (Male)	22.2	9.0	14.3
Primary (Female)	20.3	8.2	15.9
Secondary (Total)	49.0	34.7	40.0
Secondary (Male)	51.4	20.2	38.8
Secondary (Female)	47.4	14.5	41.5
Higher secondary (Total)	10.4	25.6	33.3
Higher secondary (Male)	10.3	12.4	36.1
Higher secondary (Female)	10.5	13.3	30.0
Tertiary (Total)	2.8	9.7	4.0
Tertiary (Male)	2.8	5.2	4.4
Tertiary (Female)	2.9	4.5	3.5

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

Falling real wages increase poverty levels for low-income workers

Data shows that nominal monthly wages have increased marginally between 2013 and 2015, both for men and women (Table 1.30). However, after adjusting wages for Purchasing Power Parity (PPP) using Consumer Price Indices (CPI), it can be seen that wages in real terms have in fact fallen by 15 per cent over this period. This change is more prominent for the urban labour market, which suggests a growing supply of low-skilled labour in urban areas. Falling real wages have a greater marginal impact on the lower end of the income distribution, which in turn could increase inequality through a rise in relative poverty. As is known, in October 2015, the World Bank officially updated the international poverty line to USD 1.90 (Tk. 148) per day; in other words the average worker must earn at least Tk. 4,400 (per dependant) a month to survive. Salaries have therefore not risen sufficiently in real terms to cover the rising cost of living for many

Table 1.30
Average Nominal Monthly Income from Employment

(Taka)

Criteria	2013	2015 (Jul-Sep)	Change (%)
Male	11,621	11,918	2.6
Female	11,136	11,228	0.8
Urban	13,605	13,706	0.7
Rural	10,294	10,545	2.4
Total	**11,493**	**11,774**	**2.4**

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

Table 1.31
Average Monthly Income from Employment in Real Terms

(in Taka, adjusted for 2015 Purchasing Power)

Criteria	2013	2015 (Jul-Sep)	Change (%)
National			
Male	14,007	11,918	-14.9
Female	13,423	11,228	-16.4
Total	13,853	11,774	-15.0
Urban			
Male	17,103	14,406	-15.8
Female	14,840	11,968	-19.4
Total	16,399	13,706	-16.4
Rural			
Male	12,420	10,576	-14.8
Female	12,372	10,379	-16.1
Total	12,408	10,545	-15.0

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

workers. This is a particular concern for female urban workers, whose wages have in real terms fallen by 19.4 per cent since 2013 (Table 1.31).

Given that the dependency ratio in Bangladesh is greater than 2, wages, particularly in lower-skilled industries, must rise so that families are able to live decently, above the poverty line. Low wages largely stem from lower productivity jobs of an informal nature, absence of contractual arrangements, and employees' low bargaining power. A push for an increase in wages in low to semi-skilled industries has the potential to increase female labour force participation, particularly those from low-income households with little or no education, by lowering the opportunity costs associated with entering the workforce. A governmental push for increased formalisation of the workforce is therefore needed. Formalisation of jobs will also call for formalisation of enterprises. This is also essential to enforce various policies, including the newly proposed VAT law. Increased formalisation would also provide the basis for increased protection of workers' rights and improved working conditions.

Recommendations for improving labour market outcomes

In order to further accelerate Bangladesh's economic progress, labour-centric drivers of growth must be prioritised, building on Bangladesh's impressive track record in the area of education. This will call for more concerted efforts to develop human capabilities, incentivise job creation in the private sector, upgrade skills, raise labour and capital productivity, and strengthen the underlying infrastructure (Rahman *et al.*, 2014). Creating decent jobs with higher real wages and enforcing labour rights could have a positive impact on productivity, which will help raise Bangladesh's competitiveness in both domestic and global markets.

In the light of the above discussion, it is important for the government to place greater emphasis on improved labour force participation and better employment outcomes, with medium to long-term economic growth in mind. The government must focus on increasing both the number of jobs created and the quality of employment. New policies need to take into consideration the reality that more jobs are now being created in the services and tertiary sector. Emerging opportunities in the global market should also inform policy initiatives. Incentives should be established to promote self-employment and entrepreneurship that contributes to job creation. In all aspects, the particular needs and opportunities as regards female labour force participation should receive special attention.

Undertaking of the aforementioned tasks and initiatives will require greater resource allocation. Funds should be adequate in size and appropriately targeted. Institutions and incentives will need to be designed in view of emerging opportunities and challenges, some of which can be discerned from the latest survey. Transforming Bangladesh's labour force into a skilled labour force that is capable of meeting the demands of the domestic and global labour markets is a major challenge for the country's policymakers. The NSSS is a positive and timely government initiative in this regard. However, adequate budgetary allocation and targeted initiatives will be needed to implement this strategy so as to seize the opportunities of realising the demographic dividends over the next three decades.

1.8 CONCLUDING REMARKS

As the Bangladesh economy moves toward the end of FY2015-16, one may wonder how this fiscal year will be remembered from the perspective of macroeconomic management. Will this be remembered as the year when the Bangladesh economy surpassed the threshold of "seven per cent"? While, admittedly, there has been debate, if not criticism, of the provisional GDP growth figure estimated for FY2015-16, this debate does not assess the technical and factual aspects of this year's GDP growth rate estimation. Rather, it focuses on the quality of GDP growth in FY2015-16, which has remained a contentious issue, and attempts to relate this achievement to the dynamic movements of relevant macroeconomic variables. As is observed, the expected rise in GDP growth is not corroborated in the movements of other relevant macroeconomic correlates, such as private investment, term loan off-take, import of capital machineries, tax collection from domestic sources, or growth in consumption.

The analysis in this report reveals that due to low TFP levels, Bangladesh is not able to extract the potential benefits from the observed GDP growth. Besides, private investment failed to make any headway in FY2015-16 despite enhanced inflows of FDI and some recovery in private sector credit. Nevertheless, large entrepreneurs in Bangladesh have increasing confidence in regards to large-scale private investment. To seize this opportunity, delivering the necessary infrastructural facilities according to planned timelines will be of critical importance.

It is also a matter of concern that the higher level of GDP growth achieved (as per official estimates) did not create adequate employment opportunities in the economy. Indeed, the pace of job creation has slowed considerably during 2013-2015 period. It is rather surprising to find that despite attaining a double digit value addition growth rate in the manufacturing sector in the last two years, (in net terms) more than 12 lakh jobs were lost in this sector. Indeed, a GDP growth with very weak employment generating capacity will not be able to serve the development ambitions of Bangladesh.

On a welcome note, there were a number of positives to take from the macroeconomic performance of FY2015-16. Headline inflation continued to decline from last year. Export earnings rose at a faster rate compared to import payments. This has helped to secure positive BOP for yet another year, leading to augmented foreign exchange reserves. Lower international prices released the pressure on subsidy requirements. The budget deficit has also been restrained. Overall, the fiscal year will close with macroeconomic stability retained.

There were also, however, variables where performance was rather mixed. For example, the nominal exchange rate of BDT against USD remained stable, but it made gains against the currencies of Bangladesh's major competitors in the export sector. As a result, there is a concern that the export competitiveness of the country will be eroded. Again, rising non-food inflation has led to some discomfort. Output of rice may decline only marginally, but low returns from rice cultivation has emerged as a concern. In addition, delayed delivery of policy support in this regard did not help. To everyone's surprise, the overdue rationalisation of administered petroleum prices was carried out in a way that favoured the richer sections of the society.

As is known, during this fiscal year, the country's central bank's cyber security was compromised. FY2015-16 may also therefore be remembered by many as the year of the 'Central Bank heist'. However, this may not be seen as a macroeconomic management issue.

Regrettably, there were several areas which have served to put the current fiscal year in a negative light. In FY2015-16, implementation of the national budget was one of the weakest areas from the perspective of macroeconomic management. Weaknesses became visible in a number of areas, including revenue mobilisation, implementation of the ADP and maintenance of balance in financing the deficit. Income tax collection rose at its slowest pace in recent history. Overall, ADP implementation was weak, whilst the special ADP projects – the fast track projects – did not progress at the expected pace. Implementation of foreign aided projects was as usual below par.

Persistent weakness in establishing good governance in the financial sector has continued to hurt the economy. Repeated recapitalisation of state-owned banks, funded by taxpayers' money, is difficult to justify when the state could not provide adequate support to the poorest and marginalised sections of the country due to scarcity of resources. At the same time, bringing those responsible for banking scams to justice has not been possible to date. NPL continued to rise while commercial banks remained flooded with excess liquidity. Fall in average interest rate on lending is welcome as it should reduce the cost of capital and attract private investment. Regrettably, this is attained in the backdrop of a declining interest rate on deposits with unchanged interest rate spread. These weaknesses will continue to create challenges for budget implementation and macroeconomic management in FY2016-17.

The confusion and uncertainty regarding implementation modality and the timeline of the VAT and SD Act 2012 is not helpful from the perspective of stimulating private sector investment. Indeed, diverse approaches that continue to inform the discourse will need to be reconciled without delay, with a staggered implementation plan being developed if this should be deemed necessary. Administered prices of diesel and kerosene need to be readjusted to share the benefit with entrepreneurs and the poorest sections of the population. A restructured public expenditure position needs to be formulated that favours the social sector and develops programmes to support the marginalised people. The fiscal space created from lower subsidy requirements should be best utilised through reallocation of resources to important sectors, for example, agriculture, education, health and social protection, which have received scant attention in recent years. To deliver the public investment on time and at an affordable cost, administrative capacities of government agencies need to be enhanced. Alongside the 'mega projects' of the future, important ongoing ADP projects, which are close to completion, should receive greater attention from policymakers.

Slow progress as regards the reform agenda is creating obstacles in addressing and overcoming the aforementioned challenges. The government will need to energetically pursue a number of institutional and policy reforms, including in revenue mobilisation, public expenditure management, budgetary transparency and the financial sector.

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ANNEXES

Annex 1.1 Methodology of Growth Accounting Exercise

For estimating the sources of economic growth for Bangladesh, the following aggregate production function was assumed:

$$Y_t = A_t^{\gamma} K_t^{\alpha} H_t^{1-\alpha} \quad \dots \dots \dots \dots \dots (1)$$

Where:

Y_t : Output level at time t

A_t : Level of technology

K_t : Physical Capital stock at time t (data: Nehru and Dhareshwar 1993 database)

H_t : Human Capital stock at time t

[$H_t = L_t e^{R \times MYS_t}$, where L = labour force, R is the return to schooling and MYS is the mean years of schooling (Data: Labour force is taken from the World Development Indicators (WDI), World Bank. R = 5%. MYS is taken from Barro-Lee Database on Years of Schooling)]

γ: Returns to scale. It is assumed to be equal to 1 (Constant returns to scale)

α: Share of physical capital to output

(1-α): Share of human capital to output

Equation (1) can be written as

$$\frac{\Delta Y_t}{Y_t} = \alpha \frac{\Delta K_t}{K_t} + (1-\alpha) \frac{\Delta H_t}{H_t} + \gamma \frac{\Delta A_t}{A_t}$$

Where,

$\alpha \frac{\Delta K_t}{K_t}$: Contribution of physical capital growth to real GDP growth

$(1-\alpha) \frac{\Delta H_t}{H_t}$: Contribution of human capital growth to real GDP growth

$\gamma \frac{\Delta A_t}{A_t}$: Contribution of (TFP to real GDP growth. TFP is the portion of output not explained by the amount of inputs (in this case, physical and human capital) used in production. As such, its level is determined by how efficiently and intensely the inputs are utilised in production.

Estimation of TFP Growth: Assuming α=0.4, $\frac{\Delta A_t}{A_t}$ is calculated as the residual after plugging in the other values in the equation. This residual is the TFP growth.

Annex Table 1.1

Truncated VAT Rates as of September 2015

Sl. No.	Service	Truncated VAT Rate (%)
1.	Non-AC restaurant	7.5
2.	Motor garage and workshop	7.5
3.	Dockyard	7.5
4.	Construction firm	5.5
5.	Land developer	3.0
6.	Real estate business (flat seller)	1-1,100 sq. ft.: 1.5 1,101-1,600 sq. ft.: 2.5 1,600 sq. ft or above.: 4.5
7.	Furniture	in factory: 6.0 in showroom: 4.0
8.	Goldsmith	5.0
9.	Procurement provider	5.0
10.	Transport contractor	for petroleum products: 2.25 for other goods: 7.5
11.	Electricity supplier	5.0
12.	Purchaser of auctioned goods	4.0
13.	Immigration adviser	7.5
14.	English medium school	7.5
15.	Private university	7.5
16.	Private medical and engineering college	7.5
17.	Lessee of floor, space, establishment, etc.	9.0
18.	Branded RMG seller	5.0
19.	IT-enabled services (ITES)	4.5
20.	Sponsorship services	7.5

Source: http://vatbd.com/?page_id=53

Note: VAT on private universities, and private medical and engineering colleges, was later withdrawn.

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Annex Table 1.2

Allocation for Social Safety Net Programmes

(Crore Tk.)

Programme	Budget			NSSS Target	Projection vs Target		
	FY14	FY15	FY16	FY16	FY17 (P)	NSSS FY17	NSSS FY18
Old age allowance	980	1,307	1,440	2,010	1,890	3,530	3,740
Child school (primary and secondary) stipend	1,000	971	1,159	3,870	N/A	6,830	7,240
Allowances for the widowed, deserted and destitute women	364	486	534	1,150	701	2,040	2,160
Programmes for people with disabilities	132	240	360	1,080	540	1,910	2,020

Source: Calculated from GED (2015).

Annex Table 1.3
Coverage of Beneficiaries

(Lakh)

Programme	Budget			Proposal	Projection (MTBF vs NSSS)		
	FY14	FY15	FY16	FY17	MTBF FY17	MTBF FY18	NSSS FY18
Old age allowance	27.0	27.0	30.0	31.5	30.0	30.0	55.0
Child school (primary and secondary) stipend	78.0	78.0	88.0	N/A	78.0	78.0	179.0
Allowances for the widowed, deserted and destitute women	10.0	10.0	11.0	11.7	11.0	11.0	32.0
Programmes for people with disabilities	3.2	4.0	6.0	7.5	6.0	6.0	10.0

Source: Calculated from GED (2015) and Medium Term Budgetary Framework (MTBF).

Annex Table 1.4
Implementation Status of 'Fast Track' Projects

Project	Cost (Crore Tk.) (Financial Progress[a])	Allocation in FY16 ADP (Crore Tk.)	Start and End Dates	Source of Funds	Comments
Projects in Implementation Phase					
Padma Multipurpose Bridge Project (PMBP)	28,793.00 (34.0%)	7,400.00	Jan 2009-Dec 2018	GoB	Project cost has been revised twice.
Dhaka Mass Rapid Transit Development Project (DMRTDP)**	21,985.00 (3.3%)	385.00	Jul 2012-Jun 2024	GoB, JICA	Japan International Cooperation Agency (JICA) will provide 75 per cent of the total cost. Currently at the execution phase, following completion of all planning-related activities.
2x1200 MW Ruppur Nuclear Power Plant (RNPP) – Phase-I	5,087.00 (79.3%)	1,029.00	Mar 2013-Jun 2017	GoB, Russia	Total cost of the (full) RNPP project is estimated to be Tk. 101,200 crore (USD 12.65 billion). It is expected to be completed by 2022.
Matarbari 2x600 MW Ultra-Super Critical Coal-Fired Power Project (MUSCCFPP)	35,984.00 (0.9%)	234.00	Jul 2014-Jun 2023	GoB, JICA	JICA will provide 43 per cent of the total project cost. This is one of the most expensive power projects of its size in the world that will come with its own deep sea port to facilitate the import of coal.
Construction of Single Line Dual Gauge Track from Dohazari-Ramu-Cox's Bazar and Ramu to Gundum (near the border with Myanmar)	18,034.00 (0.1%)	605.63	Jul 2010-Dec 2022	GoB, ADB, China	Included as a 'fast track' project through upgrading it to dual gauge from meter gauge. Due to this, the project cost jumped to Tk. 18,034.48 crore (the previous estimate had been Tk. 1,852.35 crore). The Asian Development Bank (ADB) will bear 73 per cent of the total project cost.

(Annex Table 1.4 contd.)

(Annex Table 1.4 contd.)

Project	Cost (Crore Tk.) (Financial Progress[a])	Allocation in FY16 ADP (Crore Tk.)	Start and End Dates	Source of Funds	Comments
Projects in Pre-Approval or Pre-Execution Phase					
2 660 MW Maitree Super Thermal Power Project (MSTPP) in Rampal	14,510.00	-	Deal signed in January 2012; will begin operation in 2019	GoB, India	70 per cent by National Thermal Power Corporation (NTPC) India, to be generated through commercial borrowing. After initiating the project in 2010, the project suffered a delay of two years. The project is expected to begin operation in 2019.
LNG terminal	Build-own-operate-transfer (BOOT)	-	Deal signed in January 2015; expected to be completed by 2016	GoB, International Finance Corporation (IFC)	In January 2015, Petrobangla signed a contract with Excelerate Energy-Astra Consortium for the purposes of building the terminal. Excelerate will build the floating, storage and re-gasification unit (FSRU) under the BOOT basis, and charge USD 0.5 per Mcf (1,000 cubic feet) against its service. The additional USD 0.1 per Mcf cost, which includes the costs of fuel, tag boat operation, port facility, etc. will be covered by Petrobangla. The project was initially set for completion in 2013. The government will spend USD 1.5 billion per year to import 500 million cubic feet of LNG per day from Qatar from 2017.
Deep Sea Port at Paira	1,128.00	-	July 2015; expected to be in operation by 2023	GoB	Initial activity began in 2013. The Paira Port Authority was established in August 2013.
Padma Bridge Rail Link	34,989.00	-	Deal signed in January 2015; to be completed by June 2022	GoB, China	About 29 per cent of the total project cost will come from the state exchequer, while 71 per cent will come as project assistance from the Chinese government.
Deep Sea Port in Sonadia	55,000.00	-	NA	NA	Recently, following an ECNEC meeting, it was announced that there will no longer be a deep sea port in Sonadia.

Source: ADP for FY2015-16, daily newspapers, and websites of the relevant government agencies.

Note: [a]Progress was reported up to December 2015 for PMBP and up to March 2016 for DMRTDP. For the other three projects, i.e. RNPP, MUSCCFPP, and Construction of Single Line Dual Gauge Track from Dohazari-Ramu-Cox's Bazar and Ramu to Gundum (near to the border with Myanmar), progress was reported up to November 2015.

[b] '-' refers to 'no allocation', while 'NA' indicates 'not applicable'.

Annex Table 1.5

Implementation Status of 25 Priority Projects under ADP for FY2015-16

Sl. No.	Project	Project Cost (Crore Tk.)	Implementation Rate FY16 (Jul-Mar)	Cumulative Progress up to March 2016	Maximum Possible Completion by FY16	End Date
	Transportation					
1.	Padma Multipurpose Bridge Project	28,793.0	22.6	34.4	41.1	31 December 2018
2.	Dhaka-Chittagong 4-Lane	3,817.0	48.9	71.2	80.9	31 December 2016
3.	Joydebpur-Mymensingh Road Development	1,815.0	39.2	90.8	97.6	30 June 2016
4.	Construction of Third Karnaphuli Bridge (Revised)	683.0	17.6	69.7	70.7	31 December 2018
5.	Support to Dhaka Elevated Expressway PPP Project	3,217.0	18.1	14.2	59.9	31 December 2016
6.	Dhaka-Chittagong Railway Development Project	2,601.0	21.8	84.7	89.6	30 June 2016
7.	Construction of Bypass Road in Satkhira town connecting Bhomra Land Port	142.0	15.0	62.7	62.7	30 December 2017
	Power					
8.	Ashuganj 450 MW Combined Cycle Power Plant	3,400.0	90.4	38.1	41.4	30 June 2017
9.	Construction of Bibiana 3,400 MW Combined Cycle Power Plant	3,358.0	27.6	4.8	12.8	30 June 2016
10.	Construction of Ghorashal 365 MW Combined Cycle Power Plant	2,512.0	12.3	16.7	34.3	31 December 2016
11.	Siddhirganj 335 MW Power Plant	4,144.0	16.8	57.1	58.0	30 June 2017
12.	Shahjibazar 330 MW Combined Cycle Power Plant	2,844.0	152.2	56.3	53.1	31 December 2016
13.	Shikalbaha Dual Fuel 225 MW Combined Cycle Power Plant	2,022.0	27.9	17.9	55.2	30 June 2016
14.	Bhola 225 MW Combined Cycle Power Plant	2,001.0	50.2	39.1	49.8	30 June 2016
15.	Chapainawabganj 100 MW HFO-based Power Plant	1,113.0	31.4	16.2	33.9	30 June 2017
16.	Veramara Combined Cycle Plant (360 MW) Development	4,140.0	212.0	42.7	47.8	31 December 2017
17.	Providing Electricity Connection to 18 lakh Clients through Rural Electricity extension	6,426.0	74.7	70.0	79.7	30 June 2018
	Industry					
18.	Shahjalal Fertilizer Project	4,874.0	27.9	95.1	99.7	30 June 2016
19.	Production of Electricity by Co-generation and Establishment of the North Bengal Sugar Mill	371.0	2.3	23.4	25.4	31 December 2018
20.	Tannery Industrial Estate, Dhaka (Second Revised)	1,079.0	8.9	33.0	72.5	30 June 2016

(Annex Table 1.5 contd.)

(Annex Table 1.5 contd.)

Sl. No.	Project	Project Cost (Crore Tk.)	Implementation Rate FY16 (Jul-Mar)	Cumulative Progress up to March 2016	Maximum Possible Completion by FY16	End Date
Oil, Gas and Mineral Resources						
21.	Mubarakpur Oil/Gas Well Exploration Project	89.0	0.0	63.0	95.0	30 June 2016
22.	Augmentation of Gas Production under Fast Track Programme	1,301.0	83.5	82.1	94.8	30 June 2016
23.	Establishment of Gas Compressor Station in Asuganj and Elenga	1,494.0	8.7	65.3	65.7	31 March 2016
Rural Development & Institutions						
24.	Construction of 950m long PC Guarder Bridge over Dharla River at Phulbari Upazila of Kurigram District	207.0	60.0	33.9	41.1	30 June 2016
25.	Construction of 520m long bridge in Nagarpur-Mirzapur via Mokna over Dhaleswari River under Nagarpur Upazila of Tangail District	76.0	73.5	44.6	63.1	30 June 2017

Source: Author's calculations based on Implementation, Monitoring and Evaluation Division (IMED) data.

Note: PPP: Public-private partnership.

Annex Table 1.6

Number of Projects with Time Extension in the RADP FY2015-16

Sector	Number of Projects in ADP	Projects with Time Extension in RADP	Proportion (%) of Projects with Time Extension
Rural Development and Institutions	96	25	26.0
Power	66	19	28.8
Transport	157	66	42.0
Education and Religious Affairs	105	18	17.1
Health, Nutrition, Population and Family Welfare	46	13	28.3

Source: Author's compilation from Planning Commission.

Annex Table 1.7

Top Destinations, Market Share and Competitor Countries of Top Non-RMG Exports of Bangladesh in 2015

Product (HS Code)	Bangladesh's Export 2015 (Jan-Dec) (Million USD)	Leading Export Destinations (Bangladesh's Share as % of Total Exports)	Export Competitors (Destination's Share as % of Total Imports)
Leather (41)	300.8	Hong Kong (22.0)	Italy (17), China (14.3), India (11.4), Bangladesh (2.7; ranked 11th)
		Korea DR (19.8)	US (43.3), Italy (10.7), Brazil (8), Bangladesh (6.4; ranked 5th)
		China (16.5)	US (21.2), Brazil (10.8), Australia (9.5), Bangladesh (0.7; ranked 25th)
		Italy (16.2)	France (11), Brazil (9.5), US (6.3), Bangladesh (1.3; ranked 20th)
Leather products (42)	185.5	US (24.6)	China (63), Vietnam (8), Italy (7.3), Bangladesh (0.3; ranked 17th)
		Japan (18.4)	China (50.3), Italy (17.3), France (8.8), Bangladesh (0.6; ranked 12th)
		Germany (14.3)	China (39.7), Italy (11.4), India (10.1), Bangladesh (0.6; ranked 21st)
Leather footwear (6403)	546.6	US (20.4)	China (53.6), Vietnam (15.2), Italy (9), Bangladesh (0.8; ranked 10th)
		Germany (19.9)	China (14.1), Vietnam (13.2), Italy (12.7), Bangladesh (2.5; ranked 12th)
		Japan (17.4)	Italy (19.3), China (18), Vietnam (15.1), Bangladesh (7.3; ranked 5th)
Raw jute (5303)	90.4	India (52.5)	Bangladesh (99.8; ranked 1st)
		China (16.6)	Bangladesh (99.2; ranked 1st)
Jute yarn & twine (5307)	422.0	Turkey (46.4)	Bangladesh (99; ranked 1st)
		China (20.6)	Bangladesh (99.7; ranked 1st)
		India (14.0)	Bangladesh (99.9; ranked 1st)
Jute sacks & bags (630510)	79.0	India (64.4)	Bangladesh (71.2; ranked 1st)
Shrimps (0306)	499.0	UK (17.9)	India (19.6), Bangladesh (16.6; ranked 2nd)
		Netherlands (16.1)	India (23.5), Bangladesh (17.9; ranked 2nd)
		Germany (15.8)	Netherlands (19), Bangladesh (17.6; ranked 2nd)
Bed, kitchen toilet lines (6302)	536.9	US (14.1)	China (36), India (33), Pakistan (18), Bangladesh (1.3; ranked 6th)
		Germany (12.7)	Turkey (24.3), Pakistan (17), China (13.3), Bangladesh (4.6; ranked 7th)
		UK (9.8)	Pakistan (41.1), China (19.5), India (12.1), Bangladesh (4.5; ranked 6th)

Source: Calculated from International Trade Centre (ITC) Trade Map data.

Annex Table 1.8

Model of Real Effective Exchange Rate and Trade Balance Determinants

Variable	Ordinary Least Squares	Auto-Regression (Integrated Moving Average)
	Real Effective Exchange Rate	Trade Balance (Exports f.o.b. – Imports f.o.b.)
Exchange Rate (BDT:USD)		-7.24e+07*** (2.49e+07)
Real Effective Exchange Rate (138 country currency basket)		6.66e+07*** (1.44e+07)
GDP per capita		9442473 (7101096)
Export Volume Index (UNCTAD, 2000=100)		2367517 (6935707)
Import Volume Index (UNCTAD, 2000=100)		-2.78e+07** (1.25e+07)
Absolute sum of import and export price elasticities	0.096 (0.063)	-826445 (4996903)
Inflation (adjusted for CPI)	-0.551 (0.551)	-7.03e+07 (4.30e+07)
Foreign Direct Investment inflows (Current USD)		-0.252 (0.458)
Constant	115.95*** (3.31)	-6.48e+09*** (2.26e+09)
Observations R-squared p-value Wald Chi-squared	23 0.0706 0.0603 -	23 - 0.00 518.6
Standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.1 Years: 1991-2014		

Source: Author's estimates.

Note: f.o.b.: free-on-board; UNCTAD: United Nations Conference on Trade and Development; CPI: Consumer Price Index.

Annex Table 1.9

Employment by Major Occupation Sectors

Sector	2010	2013	2015 Jul-Sep	2010	2013	2015 Jul-Sep
	Employment by Major Industries (Million)			Employment by Major Industries (% of Labour Force)		
Agriculture, forestry and fishing	25.73	26.19	25.77	47.57	45.10	43.88
Mining and quarrying	0.11	0.23	0.07	0.20	0.40	0.12
Manufacturing – total	6.74	9.50	8.23	12.46	16.36	14.02
Manufacturing – male	4.82	5.72	5.72	8.92	9.85	9.74
Manufacturing – female	1.91	3.78	2.51	3.53	6.51	4.28
Electricity, gas, steam and air conditioning	0.10	0.12	0.12	0.18	0.20	0.20
Water supply, sewerage and waste management	0.03	0.08	0.10	0.05	0.14	0.16
Construction	2.62	2.14	2.98	4.84	3.69	5.08
Wholesale and retail trade (repair of)	7.56	7.52	7.74	13.97	12.95	13.18
Transportation and storage	3.98	3.75	4.58	7.36	6.45	7.79
Accommodation and food service activities	0.83	0.87	0.96	1.54	1.50	1.63
Information and communication	0.06	0.14	0.21	0.10	0.25	0.36
Financial and insurance activities	0.36	0.45	0.48	0.67	0.77	0.82
Real estate activities	0.04	0.07	0.10	0.06	0.13	0.18
Professional, scientific and technical	0.12	0.35	0.29	0.21	0.59	0.49
Administrative and support services	0.49	0.42	0.33	0.90	0.73	0.57
Public administration and defense	0.54	0.76	0.94	1.00	1.32	1.61
Education	1.27	1.88	2.09	2.34	3.23	3.55
Human health and social work activities	0.43	0.75	0.55	0.80	1.29	0.93
Arts, entertainment and recreation	0.07	0.05	0.07	0.12	0.09	0.13
Other service activities	2.36	1.60	2.13	4.36	2.75	3.63
Activities of households as employer	1.01	1.17	0.96	1.86	2.01	1.63
Activities of extraterritorial organisation	0.004	0.027	0.024	0.007	0.046	0.041
Total	**54.08**	**58.07**	**58.72**	**100.00**	**100.00**	**100.00**

Source: Labour Force Surveys, 2010-2015, Bangladesh Bureau of Statistics (BBS).

Chapter 2

State of the Bangladesh Economy in FY2015-16 *(Second Reading)*

CPD's Recommendations for the Upcoming Budget

This report was released to the media on 17 April 2016.

2.1 INTRODUCTION

The national budget for FY2016-17 in Bangladesh will be prepared in the context of a set of traditional, as well as emerging tensions in the national economy. The upcoming budget will be launched also in the backdrop of an inhospitable global economic environment.

Admittedly, Bangladesh economy is currently enjoying a number of advantages. The provisional gross domestic product (GDP) growth figure has been estimated to be 7.05 per cent for the current fiscal year. Macroeconomic situation in FY2015-16 has largely been rather stable. Low levels of global commodity prices ensured that the inflation rate continued to fall throughout the fiscal year, exchange rate of Bangladeshi Taka (BDT) remained stable, while the overall balance of payments (BOP) improved significantly. Export performance was resilient and public expenditure experienced expansion.

However, from the perspective of quality of macroeconomic management some conventional issues continued to remain enduring key concerns. Programmed fiscal framework for FY2015-16 evinced serious weaknesses as targets for both revenue mobilisation and public expenditure fell significantly short of their respective targets. Leakages in public expenditure emanating from lack of good governance, delayed implementation and cost escalation seriously undermined budgetary discipline. Actual revenue growth repeatedly missed the target due to lax implementation of rules, lack of tax compliance and weak governance. Many planned reforms have fallen behind the schedule due to negligence, inertia and failure to recognise the urgency of reforms. Rejuvenation of private investment has again remained elusive while public investment performance was the weakest in recent years.

Weak discipline in the financial market, lack of capital market support and weak supervision of the central bank are undermining the cause of investment, and are not helping to restore investor confidence. Continuing global economic slowdown will likely make continuation of current good performance in exports more challenging in the near term future. Financial security has emerged as a new concern in the backdrop of various scams in the commercial banks and heist from central bank reserves. The recent Panama Papers episode and rise in Swiss Bank deposits are also reasons for disquiet. All these once again reinforce the cause of taking initiatives towards good governance in the financial sector.

In view of the discussion above, the upcoming budget of FY2016-17 will need to raise the quality of budgetary and fiscal planning and put emphasis on the needed reforms. Current economic growth projections should be reviewed in view of the composition of incremental GDP, which is unlikely to lead to high job creation. This is particular important in view of subsequent developments in the economy from the perspective of implementing the ongoing Seventh Five Year Plan (7FYP). The upcoming national budget provides an opportunity for Bangladesh to reflect on the Sustainable Development Goals (SDGs) and their implementation at the national level. Fiscal policies could be an important tool for the government to make a strong start towards attainment of the global development agenda.

The present chapter is the report on the second instalment of the state of the Bangladesh economy in FY2015-16 prepared under CPD's flagship programme titled *Independent Review of Bangladesh's Development* (IRBD). The primary objective of this report is to put forward a set of recommendations in the context of the national budget for FY2016-17. This report will be followed by a comprehensive analysis of the Bangladesh economy covering FY2015-16, to be released prior to the presentation of FY2016-17 budget.[1] The final instalment of this year's IRBD will come up with CPD's reactions to the FY2016-17 budget once it is presented on June 2016.

[1]Included in the present volume as Chapter 1.

The present report has been prepared on the basis of analysis of most recent data relating to key macroeconomic, fiscal and monetary variables. The report has also drawn from the recommendations voiced at the pre-budget dialogue organised by the CPD in Bogra that focused on development of small and medium enterprises (SMEs). Yet another consultation was organised by the CPD with young entrepreneurs and professionals, and their views have also been reflected in this report. CPD had conducted an online opinion survey through Facebook and email platforms to get feedbacks from citizens on expectations from FY2016-17 budget. Such an exercise was the first time for the CPD, and views of the participants of this survey have been incorporated in this report. The report has two parts. Section 2.2 of this report presents a brief overview of the macroeconomic developments in FY2015-16 which will inform the upcoming budget. In Section 2.3, recommendations in the context of the upcoming national budget will be presented under six broad categories – fiscal framework, revenue mobilisation, public expenditure, financing of budget deficit, fiscal measures, and economic reforms and transparency in budgetary system. Section 2.4 closes the report with some concluding remarks.

2.2 MACROECONOMIC BACKDROP IN THE RUN-UP TO THE NATIONAL BUDGET FOR FY2016-17

2.2.1 Setting the Macroeconomic Benchmark for FY2015-16

In preparing the national budget of Bangladesh for FY2016-17, policymakers will need to calibrate and design the fiscal-budgetary measures and incentives by taking cognisance of the current trends concerning the key macroeconomic correlates. CPD, in its first interim review of Bangladesh's macroeconomic performance analysis in FY2015-16, released in January 2016, had pointed out that despite relative macroeconomic stability, the economy was unlikely to achieve the envisaged private investment, revenue mobilisation and public expenditure targets (CPD, 2016). This cautionary note has now been further strengthened by subsequent developments in the economy that were unforeseen at the time.

The government expects economic growth to cross past the 7 per cent threshold, but level of private investment may continue to remain a concern

According to the provisional estimates by the Bangladesh Bureau of Statistics (BBS), GDP growth in FY2015-16 is expected to be 7.05 per cent. It is only for the second time that in the course of the last two decades (since FY2006-07) the GDP growth would exceed 7 per cent. Of the 7.05 per cent overall growth in FY2015-16, agriculture sector is to contribute 0.4 per cent (0.53 per cent in FY2014-15), industries sector's contribution would be 2.95 per cent (2.74 per cent in FY2014-15), and that of the services sector to be 3.44 per cent (3 per cent in FY2014-15) (Table 2.1). As is found, services sector's growth contribution is expected to be boosted by the growth in public administration and defense, education, and health and social works – as a consequence of significant revision of government pay scale. Indeed, if the growth rates of FY2014-15 (6.55 per cent) and FY2015-16 (7.05 per cent) are compared, of the extra growth of 0.5 percentage points, 0.4 percentage points is expected to be contributed by the national pay scale revision. This then draws attention to issues of both quality and sustainability of the GDP growth.

For FY2015-16, per capita gross national income (GNI) of Bangladesh has been estimated to be about USD 1,466, which is USD 149 more than that of the preceding year (11.4 per cent growth). On the other hand, per capita GDP is also expected to increase to USD 1,384 in FY2015-16 from USD 1,236 in FY2014-15, i.e. an increase of USD 148 (12 per cent growth).

Table 2.1
Contribution to GDP Growth in Last 10 Years

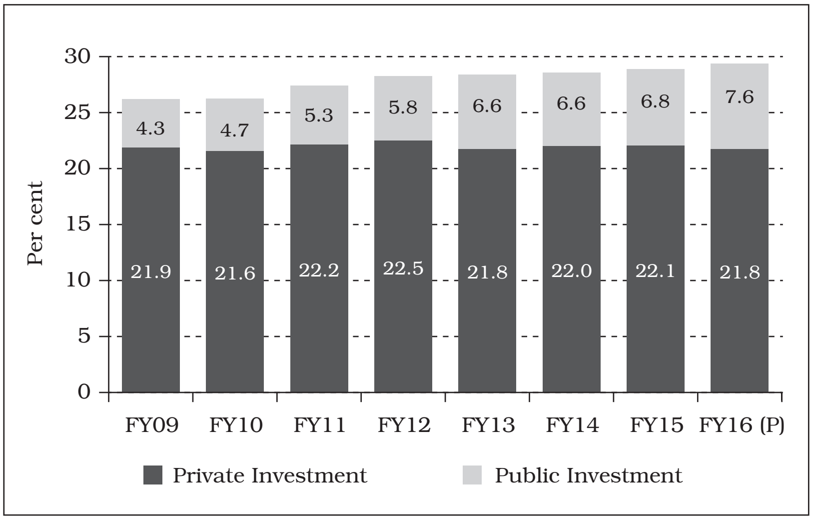
(in Per cent)

Sector	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16 (P)
Agriculture	1.21	0.81	0.61	1.07	0.78	0.52	0.41	0.70	0.53	0.40
Industries	2.18	1.73	1.71	1.77	2.31	2.47	2.59	2.27	2.74	2.95
Manufacturing	1.61	1.16	1.07	1.08	1.64	1.69	1.80	1.60	1.93	1.99
Services	3.42	3.02	2.66	2.89	3.25	3.43	2.88	2.92	3.00	3.44
Public administration and defense	0.25	0.19	0.21	0.25	0.27	0.24	0.21	0.22	0.32	0.53
Education	0.18	0.15	0.13	0.11	0.12	0.16	0.13	0.16	0.17	0.30
Health and social works	0.10	0.11	0.06	0.13	0.12	0.07	0.09	0.09	0.09	0.15
Taxless subsidy	0.26	0.46	0.06	-0.17	0.12	0.10	0.13	0.16	0.28	0.26
GDP	7.06	6.01	5.05	5.57	6.46	6.52	6.01	6.06	6.55	7.05

Source: Calculated from the Bangladesh Bureau of Statistics (BBS) data.
Note: P denotes provisional estimates.

Investment as per cent of GDP is expected to increase by 0.5 percentage points to 29.4 per cent in FY2015-16, thanks to the spurt in public investment, as reported by the BBS. Regrettably, private investment as a share of GDP is estimated to come down by about 0.3 percentage points to 21.8 per cent in FY2015-16 (Figure 2.1). This has come as a little surprise as reported growth rates of both term loan disbursement and import of capital machineries remained in the negative terrain.[2] Additionally, the rise in the public investment estimate has indeed considered the original allocations of budget for FY2015-16. As will be discussed later, the year-end public expenditure is expected to be much lower than the planned figures, hence, the public investment and GDP figures will need to be revised accordingly, when the GDP growth estimates will be finalised and the actual expenditure figures will be available.

Figure 2.1
Investment Scenario: FY2008-09 to FY2015-16



Source: Bangladesh Bureau of Statistics (BBS).
Note: P denotes provisional estimates.

[2]During the first half of FY2015-16, term loan disbursement declined by (-) 3 per cent. Import payments of capital machineries also declined during July-February period of FY2015-16 (details later in this section).

Logically speaking, the rise expected in the growth in FY2015-16 should be transmitted to, and reflected in, other macroeconomic correlates. For example, one would have expected that an enhanced GDP growth would result in higher growth in tax collection. However, income tax collection remained much lower than the estimated growth rate of nominal GDP of 14.1 per cent. Pace of new employment generation also was unlikely to gain momentum in the backdrop of slowdown in private investment. It is indicated in a recent media report that during the last two years, between 2013 and 2015 (July-September), only 6 lakh jobs were added to the Bangladesh economy (annual average being only 3 lakh). This is a drastic drop from the 13.8 lakh jobs that were created annually (on average) between 2003 and 2013.

For Bangladesh, acceleration in the GDP growth rate is a significant macroeconomic attainment. The nature of recent acceleration of GDP growth suggests that it is largely driven by rise in public salaries. It is highly likely that such boost will last for one more year when the second adjustment is made in view of the newly approved government pay scale (allowances). It is crucial that such an acceleration in economic growth is accompanied by enhanced private investment and more quality jobs for the large young labour force of the country. Along with this, it is also equally important to take into cognisance that economic growth can only serve development when it is distributed in a just way. Appropriate fiscal measures, redistributive policies and enhanced delivery of quality public service to the marginalised are the best way to serve this core objective of the budget in countries such as Bangladesh.

Revenue mobilisation in FY2015-16 is likely to miss the annual target by a large margin

The resource mobilisation target is of course to be missed once again in FY2015-16. Collection of both tax revenue and non-tax revenue continued to underperform as the ambitious targets are being chased. Data for the first six months (July-December) of FY2015-16 indicates that the National Board of Revenue (NBR) will miss its target for the fourth consecutive fiscal year.[3] Tax revenue collection by NBR registered a growth rate of 16.3 per cent during July-December of FY2015-16 as against the target of 42.3 per cent over the actual earnings in FY2014-15. Furthermore, as shown in Figure 2.2, income tax collection growth (6.8 per cent) during the first half of this fiscal year was the lowest during the last 14 years (for which data was available with CPD).

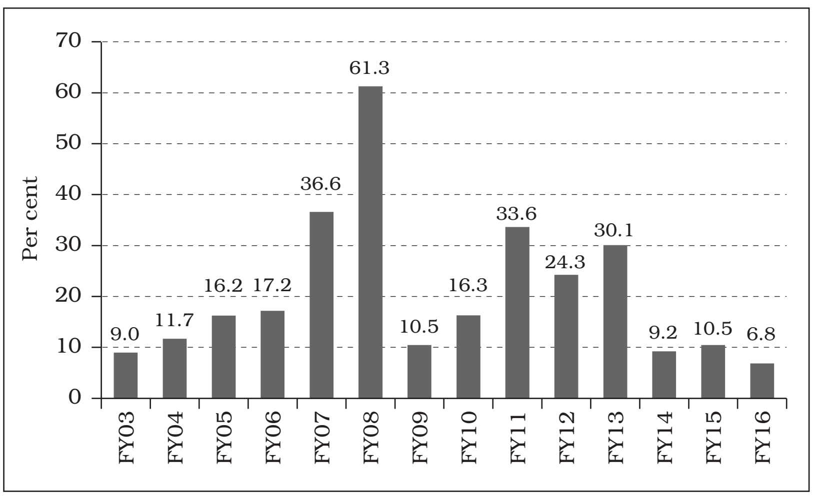


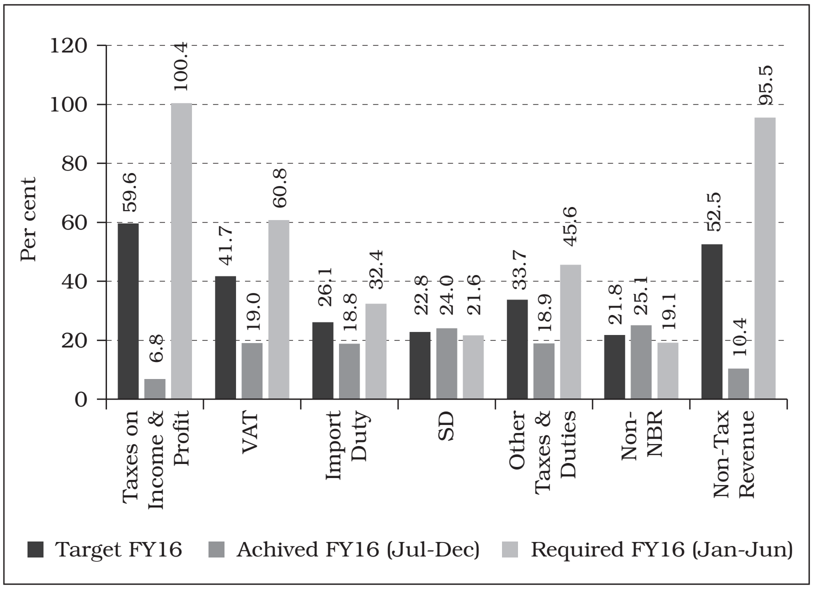
Figure 2.2

Growth Rates of Income Tax Collection

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

[3]Although NBR data shows that the revised target of revenue was achieved in FY2014-15, Ministry of Finance (MoF) data shows that there is a gap between target and actual collection. NBR data shows that the revised target of revenue was achieved in FY2014-15, Ministry of Finance (MoF) data shows that there is a gap between target and actual collection.

Figure 2.3
Growth Rates of Revenue Collection



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

Growth in the collection of supplementary duties (SDs) turned out to be the only revenue earning source that exceeded the respective annual target over the period of the first seven months (Figure 2.3). Collection of import duties was also close to the annual growth target. Indeed, target for these two heads were more realistic, when compared to those that were set in the first place for income tax and value added tax (VAT). Non-NBR tax also registered a strong growth (25.1 per cent). However, non-tax revenue collection increased by only 10.4 per cent during July-December of FY2015-16, which is far below the annual growth target (52.5 per cent). It may be recalled here that the CPD, in its earlier IRBD report released in January 2016, had apprehended that, overall revenue collection in FY2015-16 may fall short by Tk. 40,000 crore against the ambitious targets of Tk. 2,08,444 crore, if appropriate measures were not put in place to resolve the emergent constraints (CPD, 2016). Regrettably, as it appears from the more recent data, improvement in revenue generation has been rather limited. Despite a hefty profit earned by the Bangladesh Petroleum Corporation (BPC), revenue collection may fall short by about Tk. 38,000 crore in FY2015-16.

Public expenditure will be lower than planned in FY2015-16

On the expenditure side, government's non-development expenditure remained well below the targeted limit during the first half of FY2015-16. During July-December FY2015-16, 30.7 per cent of non-development budget[4] for FY2015-16 was spent, posting only a 4.7 per cent growth.[5] This figure is expected to rise in view of additional payments as per the new pay scale being released from January 2016. Expenditure for major two sources of non-development spending, i.e. 'Subsidies and Current Transfers' and 'Interest Payments' were well within the limit, with respective growth of 4.8 per cent and 9.6 per cent during July-December of FY2015-16. Expenditure for Annual Development Programme (ADP) was also lower than the past trends of low rate of implementation in the early months. In addition the government disbursed Tk. 1,200 crore for recapitalisation of the state-owned commercial banks (SCBs) till December 2015, for which a budgetary provision of Tk. 5,000 crore was set aside in FY2015-16.[6] Thanks to drastic fall in international fuel prices, BPC moved to the profit terrain in FY2014-15 and continued earning profit in FY2015-16. Hence, BPC will not be in need of further subsidy, releasing pressure in the upcoming FY2016-17 budget.

[4]The head includes non-development revenue expenditure, capital expenditure and other programmes financed from non-development budget.

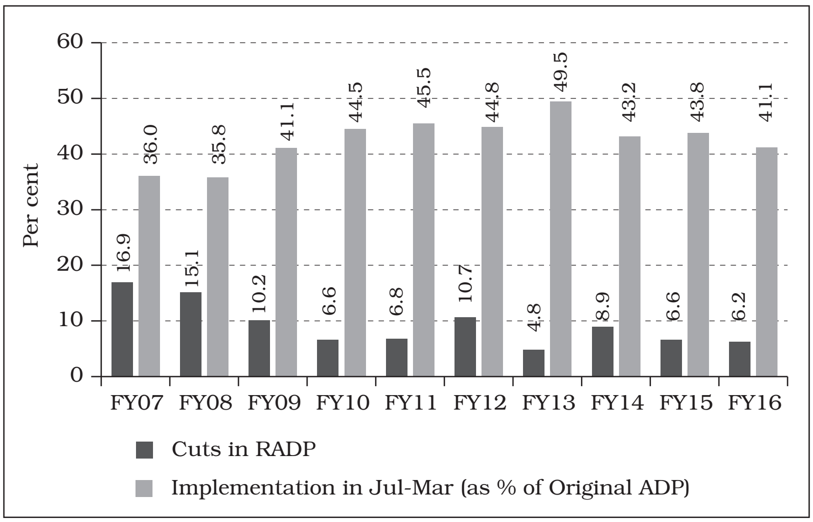
[5]In corresponding periods of FY2014-15, 41.7 per cent of the similar budget was spent and the growth target for FY2015-16 was planned at 42.3 per cent over the actual spending in FY2014-15.

[6]In FY2014-15, government spent Tk. 1,716 crore for this account.

The final public expenditure outcome will indeed largely depend on the government's decision as regards the subsidy package (i.e. decisions on adjustments of administered prices), expenditure for social safety net programmes (SSNPs) and recapitalisation of SCBs.

ADP expenditure against allocation is the lowest in recent years

Expenditure on account of the ADP is yet to mark any significant breakthrough in FY2015-16. Indeed, the performance has deteriorated and registered its lowest growth in FY2015-16 when compared to recent fiscal years. According to the first eight months' data, actual spending under ADP was 34.2 per cent of the originally planned allocation of Tk. 97,000 crore. This is the lowest level of expenditure in the last seven years (since FY2008-09). Both Taka (36.6 per cent) and project aid (30 per cent) components of the expenditure were the lowest in the recent past (since FY2008-09 and FY2011-12 respectively). When ADP was subsequently revised in April 2016, a number of sectors (e.g. Oil, Gas and Natural Resources, Communication, Physical Planning, Water Supply and Housing, and Public Administration) were subjected to substantial cuts. ADP for FY2015-16 was slashed by Tk. 6,000 crore (or 6.6 per cent) to bring the size down to Tk. 91,000 crore, as shown in Figure 2.4. Project aid component was reduced by Tk. 5,340 crore (or 18.3 per cent) while GoB (Government of Bangladesh) allocation was reduced by only Tk. 660 crore (or 1.1 per cent). Given the implementation status of the ADP, one would have expected a higher reduction in the ADP allocation. Indeed, in FY2006-07, when a similar implementation level was experienced during the first nine months, ADP was revised downward by 10.2 per cent.[7]



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

Figure 2.4

Revised ADP, the Cuts and ADP Implementation Scenario

Budget deficit remained within limit

Budget deficit was not a matter of concern in the early months of FY2015-16 and has remained within the comfort zone. The budget surplus was to the tune of Tk. 609 crore, particularly owing to sluggish public expenditure; to recall, for FY2015-16, deficit target was set at 5 per cent of GDP (excluding grants). The budget deficit was likely to rise in the second half of FY2015-16. However, it is expected to remain close to the budgetary target in the backdrop of lower levels of revenue earnings and that of public expenditure. As has been mentioned above, it is apprehended that there will be large revenue shortfall and the adverse impact on deficits was likely to be offset by unutilised budgetary allocations. Data for six months (July-December) of FY2015-16 indicated that, foreign borrowing was on the lower side while domestic borrowing

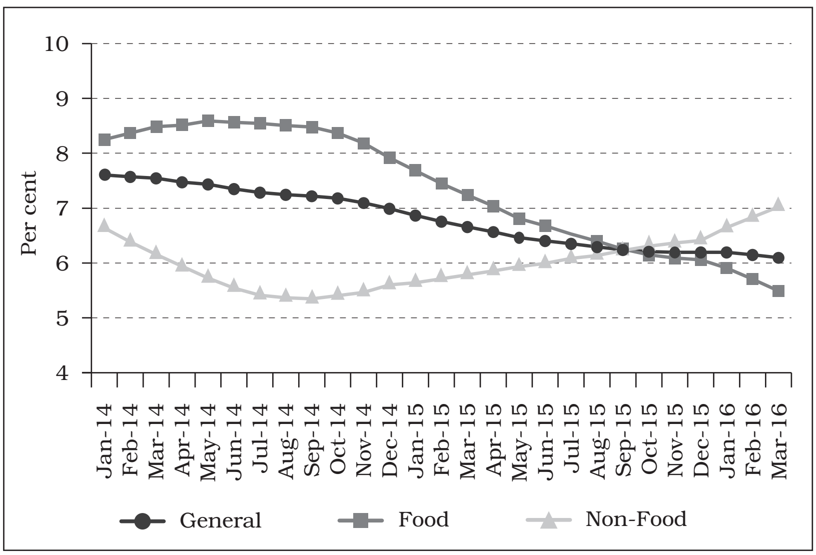
[7]However, only 82.9 per cent of the Revised ADP (RADP) was actually spent in FY2006-07.

was negative. Sale of National Savings Bond (NSD) certificates during July-December period of FY2015-16 (Tk. 13,366 crore) reached close to the annual budgetary target of Tk. 15,000 crore. However, financing from foreign sources will face formidable challenge in the second half of FY2015-16 once the development expenditure start to post rise. The government received only Tk. 224 crore (3.9 per cent) as foreign grant and Tk. 776 crore (3.2 per cent) from net foreign borrowing during July-December of FY2015-16, while the respective annual targets were Tk. 5,800 crore and Tk. 24,335 crore.

Inflation came down to reach the target level

One of the welcome trends was that, the growth in annual average inflation reached 6.10 per cent in March 2016 (Figure 2.5) against the annual target of 6.07 per cent set in the Monetary Policy Statement (MPS) of the Bangladesh Bank for January-June 2016. It is also lower than the 7FYP target of 6.2 per cent. The fall in inflation was driven by declining food inflation which was 5.5 per cent in March 2016. In contrast, non-food inflation has seen a secular rise in the fiscal year and reached 7 per cent.[8] The difference in inflation between rural and urban areas has been widening on a continuing basis since April 2015 with lower inflation in rural area. Lower global commodity prices, nearly stable exchange rate of the BDT with only marginal recent depreciation and restrained growth of broad money supply have been contributing to the falling inflation. Sustained negative growth of global commodity price index since July 2014 contributed to the falling inflation rate in Bangladesh through both direct and lagged pass-on impact. Lower broad money growth, originating from negative growth of credit to the public sector, also contributed. Negative remittance growth also played a role in restraining the inflation rate. Inflation is expected to decline further in the face of sustained lower global commodity prices and the envisaged downward adjustment of administered prices of petroleum products in the domestic market.

Figure 2.5
Annual Average Inflation Rate



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

Growth of monetary aggregates remained close to the targets

Credit to the private sector growth was 15.1 per cent as of February 2016 which marginally exceeded the monetary policy target of 14.8 per cent for end June 2016 (Table 2.2). This is the highest growth since December 2012 (16.6 per cent). The current rising trend of private sector credit growth has been underway since September 2015. Thankfully, Bangladesh Bank had revised the policy rates (repo and reverse repo) downward; this was indeed also recommended by the CPD in its previous review of the economy in January

[8]The recent pick up of non-food inflation was mainly driven by rent, fuel and lighting, and clothing and footwear.

Table 2.2
Growth of Monetary Indicators

(in Per cent)

Indicator	FY14	FY15 Target	FY15 Actual	Bangladesh Bank Target for Jun 16	Latest Actual (Feb 16)
Reserve money growth	15.5	15.9	14.3	14.3	15.5
Broad money growth	16.1	16.5	12.4	15.0	13.1
Net foreign asset	41.2	3.6	18.2	11.1	25.6 (Jan)
Net domestic assets	10.3	20.2	10.7	16.2	9.3 (Jan)
Domestic credit	11.6	17.4	10.0	15.5	11.0
Credit to the public sector	34.7	25.3	30.9	18.7	-1.9
Credit to the private sector	12.3	15.5	13.2	14.8	15.1

Source: Bangladesh Bank.

2016. Sliding real lending rate was perhaps another contributing factor.[9] However, it is difficult to explain the composition of the incremental private sector credit. It is observed that trade activities have gained momentum in recent months which was likely to generate demand for additional credit. However, as has been mentioned previously, industrial term loan disbursement has not registered any momentum. Bangladesh Bank may examine the composition to see how much of the private sector credit growth is attributed to consumer loans, and how much was actually disbursed to productive sectors.

Credit to the public sector declined by (-) 1.9 per cent as of February 2016 due to limited bank borrowing requirements by the government to underwrite the fiscal deficit incurred till now. The trend in the growth of monetary aggregates, however, was accompanied by a strong flow of net foreign assets which posted a growth rate of 25.6 per cent as of January 2016 against the target of 11.1 per cent for the end June 2016. Indeed, robust accumulation of foreign exchange reserves, to keep the exchange rate of BDT stable against United States Dollar (USD), contributed towards this strengthening. Growth rate of broad money, by the end of February 2016, fell short by 1.9 percentage points against the target of 15 per cent in June 2016.

Real interest rates declined, but limited progress made in terms of reducing spread

Real interest rates, on both lending and deposits, continued to decline in FY2015-16. In February 2016, the real average interest rate on deposits ended up in the negative terrain ((-) 0.1 per cent), a first time in past several years. This implies that the depositors will not make real gains by making deposits in commercial banks. Indeed, falling inflation is not being able to guarantee positive return on bank deposits. Lack of demand for credit has resulted in commercial banks being flushed with liquid assets and banks are discouraged to keep deposits. The fall in yields from bank deposits has pushed depositors to opt for NSD certificates. A negative real interest may discourage people from savings in the medium term, but is likely to boost consumption. Generally speaking, it will be the small savers who will be most hurt in view of this development. Indeed, this is a new challenge for the monetary policy making in Bangladesh.

For a long time, Bangladeshi entrepreneurs have been asking for lowering of the lending rates. The falling trend will be welcome by them. There was a need to reduce the interest rate spread as well, but regrettably this did not happen. Indeed, after recording some fall in FY2014-15, during the first eight months of FY2015-16, spread did not register any change and remained at 4.8 percentage points. Indeed, in November 2015, Bangladesh Bank issued a circular advising the commercial banks to keep the intermediation spread to a

[9]Average lending rate was 10.9 per cent in January 2016, which was 4.8 per cent in real terms after adjusting for the inflation rate.

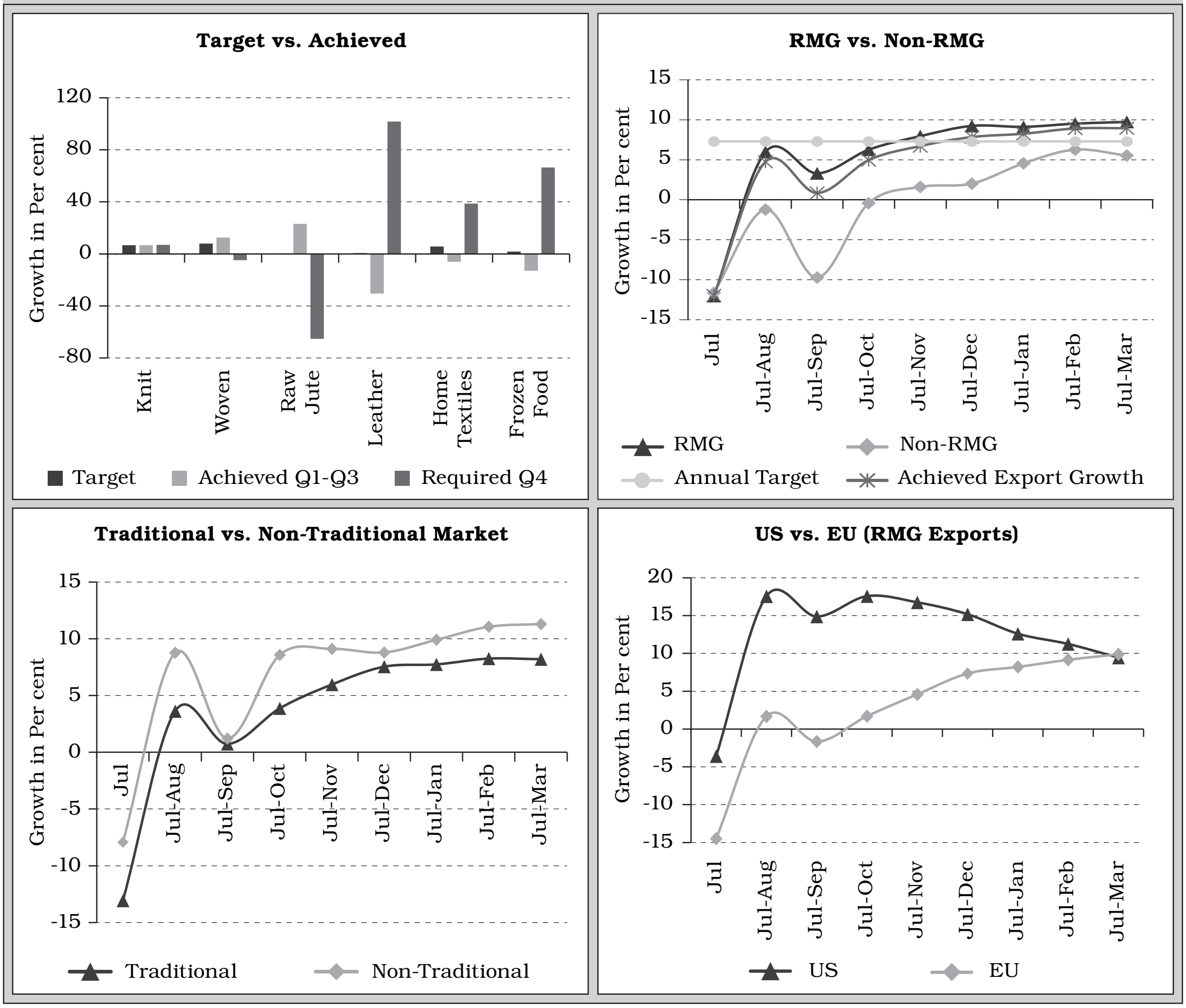
'lower single digit', i.e. less than 5 percentage points.[10] However, in February 2016, of the 39 private commercial banks (PCBs) 20, and six out of nine foreign banks, had interest rate spreads of over 5 percentage points.[11] Indeed, the miniscule decline (0.03) between December 2015 and February 2015 was entirely accounted for by the SCBs. It is important for the central bank to examine opportunities to reduce the spread.

RMG-led export earnings continued robust growth

Export earnings during the first nine months of FY2015-16 have surpassed the envisaged annual target set for FY2015-16. *First*, according to the Export Promotion Bureau (EPB) data, export receipts registered 9 per cent growth during July-March of FY2015-16 against the annual growth target of 7.3 per cent, thanks mainly to the robust growth in readymade garments (RMG) export (9.7 per cent). Woven garments posted the strongest growth (12.6 per cent) (Figure 2.6). However, non-RMG export growth was volatile and

Figure 2.6

Export Scenario after Three Quarters of FY2015-16



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

[10]In December 2015, Bangladesh Bank clarified the definition of 'lower single digit' as less than 5 percentage points. The spread here excludes the interest rates for consumer loans and credit to SMEs.

[11]In December 2015, 18 PCBs had interest rate spread higher than this threshold.

remained subdued at 5.5 per cent over the first nine months of FY2015-16. In this context, only engineering products, one of the promising sectors in terms of product diversification, has registered high growth (22.6 per cent).

Second, there was some sign of market diversification – export growth for non-traditional markets (11.3 per cent) was higher than that for the traditional markets (8.2 per cent) during the first nine months of FY2015-16. Of the major non-traditional destinations, export to Japan (16 per cent), Australia (19.2 per cent) and India (22.9 per cent) posted notable performance.[12] On the flipside, export growth to China during the reported period declined by (-) 3.6 per cent mainly due to poor performance of non-RMG exports. In contrast, export to India posted a 22.9 per cent rise.

Third, among the major traditional markets, export to the United States (US) market registered 10.4 per cent growth. Both RMG (11.3 per cent) and non-RMG (22.7 per cent) products fared good growth during July-March of FY2015-16. However, growth in this market had gradually declined since October 2015 (the growth rate was 17.3 per cent for July-October period).

Fourth, since upturn posted after the first quarter[13], export growth in the European Union (EU) market was about 7.5 per cent mainly driven by robust growth in woven (16.8 per cent). However, non-RMG products in the same market faced negative growth ((-) 12.8 per cent) during July-March of FY2015-16 compared to corresponding months of FY2014-15. Export to Germany and the United Kingdom (UK), the two major EU economies, showed positive performance (3.4 per cent and 21.4 per cent growth respectively).

Fifth, as was observed, Bangladesh's export performance held fairly well in economies where market was relatively stable and economic growth remained relatively high. Product-level analysis of RMG exports to the US market showed that, Bangladesh's export of a particular RMG product followed the global demand pattern of US for that item. In contrast, Vietnam's export of the top RMG items to the US showed a consistent resilient growth irrespective of the global demand on the part of US consumers.[14] Price analysis of RMG products reveals that, growth of knit and woven items for both Bangladesh and Vietnam in the US market were only partially driven by price (during July 2015-January 2016 period) (Table 2.3). Conversely, in the EU market, the growth was primarily price driven for both the countries.

Table 2.3

Price Impact of Bangladesh and Vietnam's Export Growth

(in Per cent)

Country	Knit (61)			Woven (62)		
	Value	Quantity	Price	Value	Quantity	Price
US market						
Bangladesh	22.33	7.74	13.54	7.93	10.00	-1.88
Vietnam	9.77	8.06	1.57	15.74	9.52	5.68
EU market						
Bangladesh	17.4	4.2	12.6	18.5	0.1	18.4
Vietnam	27.6	0.2	27.4	17.3	-0.6	17.9

Source: Computed from the United States International Trade Commission (USITC) and EuroStat data.

[12]Growth in India was an outcome of high growth in non-RMG exports.

[13]During the first quarter of FY2015-16, export growth in the EU market was (-) 4.4 per cent.

[14]It may be noted here that, Vietnam is one of the major competitors of Bangladesh's RMG export to the US market. This is particularly important in view of recently signed Trans-Pacific Partnership (TPP) deal, which may facilitate preferential access of Vietnamese RMG products to the US market which is not being enjoyed by Bangladesh.

Sixth, Bangladesh's exports may have faced challenges in terms of competitiveness on account of relative exchange rate movements when compared with Vietnam. Over this period, BDT and Vietnamese Dong (VND) against USD have depreciated by 0.8 per cent and 5.2 per cent respectively on a point-to-point basis. On the other hand, against Euro, the two aforesaid currencies appreciated by 13.3 per cent and 9.5 per cent respectively. Vietnam has indeed enjoyed some price advantages in both the US (higher depreciation) and the EU (lower appreciation) vis-à-vis Bangladesh.

There is a need for renewed efforts towards raising competitiveness of Bangladesh's exportables through both product and market diversification. Bangladesh has formulated and announced a new Export Policy Order (EPO) for 2015-18 period to support future development and raise competitiveness of the country's export sector. The policy aspires to project the Brand Bangladesh in the global market, diversify the export base, put in place special provisions, and promote incentives for the development of new products and exploration of new markets. It may be noted that the government has recently revised the existing export cash incentive structure to include a number of new exportable products (see Annex Table 2.1 for details).

Import payments rising despite lower capital machineries import

During the first eight months of FY2015-16 (July-February), import payments increased by 6.4 per cent over the corresponding months of FY2014-15; as may be recalled, the overall import growth in FY2014-15 was 11.3 per cent. After experiencing negative growth in the first quarter of the current fiscal year, imports have gained some momentum over the subsequent five months. Import growth was driven by imports of consumer goods which recorded a growth rate of 19.2 per cent.[15] Payments for importing intermediate goods increased by 6.4 per cent. In contrast, import payments for capital machinery, a key item having implications for investment, declined by (-) 7.5 per cent. Curiously, during the reported period, import of petroleum products posted a highly robust growth rate of 41.4 per cent at a time when global prices were at very low levels. Despite a positive upturn in recent months, it is likely that growth of overall import payments may remain subdued in the upcoming months of FY2015-16 due to a higher benchmark and stagnant growth of letter of credit (L/C) opening.[16]

Migration gained momentum, but yet to be reflected in remittances inflow

Over the first nine months of FY2015-16, the absolute number of migrants (5 lakh) going abroad from Bangladesh has surpassed the total annual migration (4.6 lakh) in FY2014-15, registering a phenomenal growth of 53.9 per cent over the corresponding period. Indeed, a significant boost in migration was observed (monthly average being over 45 thousand) since March 2015, followed by a further momentum gained in November 2015 (monthly average being over 60 thousand). During the reported period, migration growth to Middle East rose by 73.3 per cent. The key destinations for migrants were Oman and Qatar followed by Saudi Arabia, a destination where in a welcome development after a near-stop migration, is picking up.[17] A recent significant boost in female migration has continued in FY2015-16. About 90 thousand female workers went for overseas employment during this period. Majority of the female migrated to Saudi Arab, accounting for 44.7 per cent of total migrants.[18]

[15]Growth of import payments for edible oil was particularly high – 73.7 per cent despite the global prices being lower.

[16]During the last four months (March-June) of FY2014-15, import payment growth was about 28.5 per cent – largely driven by high import payments for petroleum products. However, during July-February FY2015-16, L/C opening growth was (-) 1.7 per cent, and petroleum import L/C opening growth was (-) 40.5 per cent. At the same time, BPC's move to import petroleum products through open bidding may have helped.

[17]Saudi Arabian government has recently announced plans to cut spending, undertake reforms in energy subsidies and to raise revenues from taxes and privatisation, in a bid to reduce its record budget deficit due to the low oil prices (http://www.dailymirror.lk/101647/worker-remittances-inflow-likely-to-slow-down-in-2016)

[18]Indeed, 52.6 per cent of the total Bangladeshi migrants travelled to Saudi Arabia were female.

The picture as regards remittance flow has been discouraging though. Remittances inflow during July-March of FY2015-16 was USD 11.1 billion which was (-) 1.8 per cent lower than the corresponding period of the previous fiscal year. It is hoped that the rising number of migrant workers in recent times will yield higher remittances in subsequent months and years. Indeed, lower amount of remittance inflow was observed in case of eight out of the 18 major markets for Bangladesh during the period. As can be seen from Table 2.4, Sri Lanka has also received lower remittances during July-December period of 2015 compared to corresponding period of 2014. On the other hand, Pakistan (6.3 per cent) and Nepal (12.8 per cent) have posted positive growth rates. Indeed, remittance inflow to Bangladesh had continued to fall during the first two months of 2016, while other major countries recorded positive growth. There is a need to examine the underlying reasons in this connection.

Table 2.4

Comparative Analysis of Remittance Growth

(in Per cent)

Country Name	Growth in FY16		
	Jul-Dec	Jan-Feb	Jul-Feb
Bangladesh	-0.1	-6.0	-1.6
Pakistan	6.3	5.5	6.1
Sri Lanka	-3.0	8.0	-0.6
Nepal	12.8	3.1	10.4
Philippines	0.3	3.2*	0.7*

Source: Bangladesh Bank (www.bb.org.bd); Nepal Rastra Bank (www.nrb.org.np); State Bank of Pakistan (www.sbp.org.pk); Central Bank of Sri Lanka (www.cbsl.gov.lk); and The Bangko Sentral ng Pilipinas (www.bsp.gov.ph) [Accessed on 7 April 2016].
Note: *Up to January 2016.

Balance of payments situation remained favourable

Bangladesh economy experienced favourable BOP during July-February period of FY2015-16 (USD 3.1 billion) over the corresponding months of FY2014-15 (USD 2.2 billion). Trade balance was USD (-) 4.06 billion and remained almost unchanged compared to corresponding period of FY2014-15, as a consequence of high export earnings against relatively lower growth of import. Also, current account balance stood at USD 2.7 billion which was USD 511 million higher than July-February of FY2014-15 – mainly originating from higher services income. Within the financial account, net foreign direct investment (FDI) passed USD 1.4 billion to register a growth rate of 27.2 per cent over July-February of FY2014-15, whilst net trade credit was negative at USD (-) 1.2 billion.

Foreign exchange reserve continued to rise

In the backdrop of the rising BOP surplus, foreign exchange reserve has continued to rise to reach USD 28.7 billion as of 12 April 2016. During the first nine and half months of FY2015-16 foreign exchange reserve increased by USD 3.6 billion. Major share of the foreign exchange reserves was kept as convertible foreign currencies including securities, and also in the form of Special Drawing Rights, gold and export development fund, etc. According to World Development Indicator (WDI) data, foreign exchange reserve-to-GDP ratio of Bangladesh was 12.9 per cent in 2014. To compare, the figures for Indonesia (12.6 per cent) and Sri Lanka (10.4 per cent) were lower, whilst those of India (15.9 per cent), Vietnam (18.4 per cent), Philippines (28 per cent) and Nepal (31.4 per cent) were higher. Whilst there is no optimal size for forex reserves that a developing country should maintain, the fact remains that the manner in which reserves are accumulated and deployed should be a concern for policymakers. There is a strong case for Bangladesh to revisit and examine the reserve issue, from the perspective of accumulation, deployment, use[19], cost and return, as also safety and security of the foreign exchange reserves.[20]

2.3 RECOMMENDATIONS FOR THE NATIONAL BUDGET FOR FY2016-17

2.3.1 Fiscal Framework

Plug the widening fiscal projection gap

CPD, in its immediate reaction to the national budget for FY2015-16, expressed concerns regarding weaknesses in the formulation of fiscal framework in Bangladesh (CPD, 2015a). As seen from Table 2.5, between FY2008-09 and FY2014-15, the gaps between planned and actual targets have risen for almost all components of the fiscal framework. Of the key components, net foreign borrowing is the weakest, followed by ADP and revenue mobilisation. In FY2014-15, 75.6 per cent of the budget target for net foreign borrowing was not realised in the backdrop of lack of ustilisation of project aid. It is also observed that every year the government is earmarking higher allocation for ADP which cannot be spent by relevant government agencies. In last three years (FY2012-13 to FY2014-15), the gap between target for revenue mobilisation and the actual collection has also increased significantly.

Table 2.5

Fiscal Projection Gap (Budget Target *minus* Actual Outcome) as % of Budget Target

Indicator	FY09	FY10	FY11	FY12	FY13	FY14	FY15
Total expenditure	10.6	10.7	3.0	8.3	9.1	14.6	18.7
ADP	24.1	16.2	13.6	22.8	10.8	22.0	25.8
Total revenue	6.9	4.5	(-) 0.2	3.9	7.8	15.4	20.2
NBR revenue	7.9	2.6	(-) 5.4	0.3	7.9	17.7	17.2
Budget deficit	19.1	25.2	10.3	19.8	12.8	12.1	14.6
Net foreign borrowing	64.0	30.4	75.7	89.8	50.4	77.3	75.6
Net domestic borrowing	(-) 17.8	23.0	(-) 29.2	(-) 13.3	4.4	(-) 25.2	(-) 18.0

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

It is reckoned that, the government is not being able to make the needed allocation to social sectors due to resource scarcity and unattained revenue mobilisation targets. Regrettably, the public expenditure targets, particularly the development head (ADP) allocations were not fully utilised in any of the last seven years. Lower revenue mobilisation accompanied by even lower public expenditure implied failure in utilisiation of the fiscal space offered by the moderate budget deficit. Government borrowing from domestic sources, barring FY2009-10 and FY2012-13, overshot targets due to weak budget deficit financing through use of relatively cheaper foreign resources. Overall, the fiscal framework appears to be designed with built-in overprojection.

Design and implementation of national budget for FY2016-17 needs to reverse this trend. Although the revised budget is placed before the national parliament, actual budget implementation is, regrettably, not discussed adequately. The audit report is also published with a significant time lag. It is important that the Public Accounts Committee and the national parliament undertake an in-depth scrutiny of actual implementation of the national budget vis-à-vis the finalised budget.

[19]Use of foreign exchange reserves to create Sovereign Wealth Fund (SWF) is a case in point. SWF is a state-owned investment fund, derived from the country's reserve, which invests locally or internationally or both.

[20]The issue of security of reserves has become one of heightened concern following the recent heist of about USD 100 million worth of Bangladesh's reserves by hackers.

Attainment of proposed fiscal framework will once again pose challenge

Analysis of available information as regards the fiscal sector (in Section 2.2) revealed that the budget for FY2015-16 is likely to follow the prevailing trends resulting in the end with large gaps vis-à-vis fiscal projections. In this backdrop, it is important for the Ministry of Finance (MoF) to prepare the fiscal framework for FY2016-17 in a realistic manner. The first step towards this is to revise the fiscal framework for FY2015-16 in a judicious way. The Budget Monitoring and Resource Committee (BMRC) has recently indicated that both revenue and expenditure targets will be reduced by about Tk. 30-31 thousand crore (Table 2.6). It is observed that every year a highly ambitious fiscal framework is proposed which is later revised at the time of preparing the budget for the following year; actual realised figures are nowhere near the original targets.

Table 2.6

Proposed Revision of the Fiscal Framework by BMRC

Particular	Crore Tk.					Growth (%)			
	FY15 (A)	B FY16	RB FY16 (P)	B FY17 (P)	RB FY16 over B FY16 (P)	B FY16 over RB FY15	B FY16 over A FY15	RB FY16 over A FY15	B FY17 over RB FY16
Total expenditure	204,226	295,093	264,500	340,600	30,593 (10.4)	23.1	44.5	29.5	28.8
Non-ADP	143,987	198,093	173,500	227,600	24,593 (12.4)	20.3	37.6	20.5	31.2
ADP	60,238	97,000	91,000	113,000	6,000 (6.2)	29.3	61.0	51.1	24.2
Total revenue	145,950	208,443	177,000	243,000	31,443 (15.1)	27.6	42.8	21.3	37.3
NBR revenue	123,960	176,370	150,000	200,300	26,370 (15.0)	30.6	42.3	21.0	33.5
Non-NBR revenue	21,990	32,073	27,000	42,700	5,073 (15.8)	13.2	45.9	22.8	58.1
Budget deficit	58,275	86,650	87,500	97,600	-850 (-1.0)	13.6	48.7	50.1	11.5

Source: Calculated from the Ministry of Finance (MoF) data and collated information from several media reports.
Note: [a]A denotes actual; B denotes budget; RB denotes revised budget; P denotes projected.
[b]The projected revised budget and budget figures for FY2015-16 and FY2016-17 respectively might be different from the final figures to be made public on 2 June 2016 when the Finance Minister will announce the national budget for FY2016-17 before the parliament.
[c]Figures in parentheses refer to revision as percentage of original budget target.

As mentioned above, CPD estimates showed that the revenue shortfall could be even larger than expected by the BMRC. At the same time, it is also important to recall that in FY2015-16, ADP expenditure during the first nine months had been the lowest (as a share of the original allocation) in recent years. Regrettably, this unwelcome reality has not received the needed attention that it deserved during finalisation of Revised ADP (RADP) for FY2015-16. Non-ADP expenditure may also fall short of the respective revised target. Consequently, the budget deficit was likely to be lower than expected.

To be fair, the envisaged growth targets for FY2016-17 over the revised budget, e.g. revenue collection (37.3 per cent)[21], public expenditure (28.8 per cent) and budget deficit (11.5 per cent), are moderately ambitious. However, if the revised budget for FY2015-16 are not realised, which is likely to be the case, the actual growth targets for FY2016-17 (to be calculated over the lower attainments in FY2015-16) will be much higher.

[21]Revenue collection is expected to get a boost in FY2016-17 if the new VAT and SD Act can be successfully implemented.

In view of the discussion above, the fiscal framework targets for FY2016-17 including for revenue collection, public expenditure and deficit are expected to be set on the higher side. This is particularly true if the recent trend is considered. The final fiscal framework figures for FY2015-16 are likely to be lower than the proposed revised targets. Consequently, the required growth for attainment of FY2016-17 fiscal framework figures will also rise. This was also the case with the FY2015-16 budget. It is likely that if the fiscal framework targets are set in this manner (as is presented in Table 2.6), the annual growth targets will once again remain unattainable under a business-as-usual scenario.

It needs to be recognised that both revenue mobilisation (9.6 per cent of GDP in FY2014-15) and public expenditure (13.5 per cent of GDP in FY2014-15) in Bangladesh are well below the international standard. Raising the level of both public income and spending is critical for attaining the country's development targets. CPD, in its state of the economy report in January 2016, recommended that a more expansionary fiscal policy be pursued. However, such a policy will also need to be implementable.

In this context, there are two ways to correct this situation. One option for the government is to rein-in the ambition of having a fiscal framework that envisages high revenue collection and high public expenditure. Thus, the budget will need to be prepared by accepting the current reality. Alternatively, the government can set the targets at moderately ambitious level, and give due attention to the task of enhancing administrative capacity and undertake implementation of the reform agendas with due seriousness. At the same time, distribution of allocation may also need to be revisited. The quality of public expenditure should also not be compromised. These issues are discussed in more detail in the following sub-sections of the present chapter. Some of the proposed measures in this connection are discussed in latter sections. It is reckoned that, in the context of Bangladesh, the second option is more desirable.

SDGs should inform the budget for FY2016-17

It is to be expected that Bangladesh's commitment towards the SDGs will be mentioned in the budget for FY2016-17. In this context, it is important that SDGs are taken as an opportunity to bring about the needed changes in the current priorities of Bangladesh. It is hoped that these revised priorities get reflected in the upcoming national budget. As is known, resource requirement for the Millennium Development Goals (MDGs) was not estimated upfront; these were estimated only later on, individually for different goals. This also resulted in double counting. The estimates could not be appropriately used for devising MDGs implementation strategy. This needs to be corrected for implementation of the SDGs. An ongoing CPD study (Bhattacharya *et al.*, 2016) has proposed a framework to this end. Following the finalisation of the SDG indicators, there is a need for estimating resource requirement for implementing the SDGs at the country level for Bangladesh.[22] Consideration of target-based estimates is crucial in this regard. At the same time, synergy and trade-offs among the targets will need to be taken into account in order to avoid double counting. The estimated resource requirement will then need to be matched with existing flow of resources (by sources). This will eventually lead to a more accurate estimates of resource gaps, as also help identify potential sources for financing. The national budget for FY2016-17 need to take cognisance of this exercise. Priorities and the related resource envelope in view of the SDGs should be discussed in the Bangladesh parliament, and the Parliamentary Standing Committees should remain closely engaged in this process.

[22] The GoB in collaboration with the United Nations Development Programme (UNDP) has already started this process.

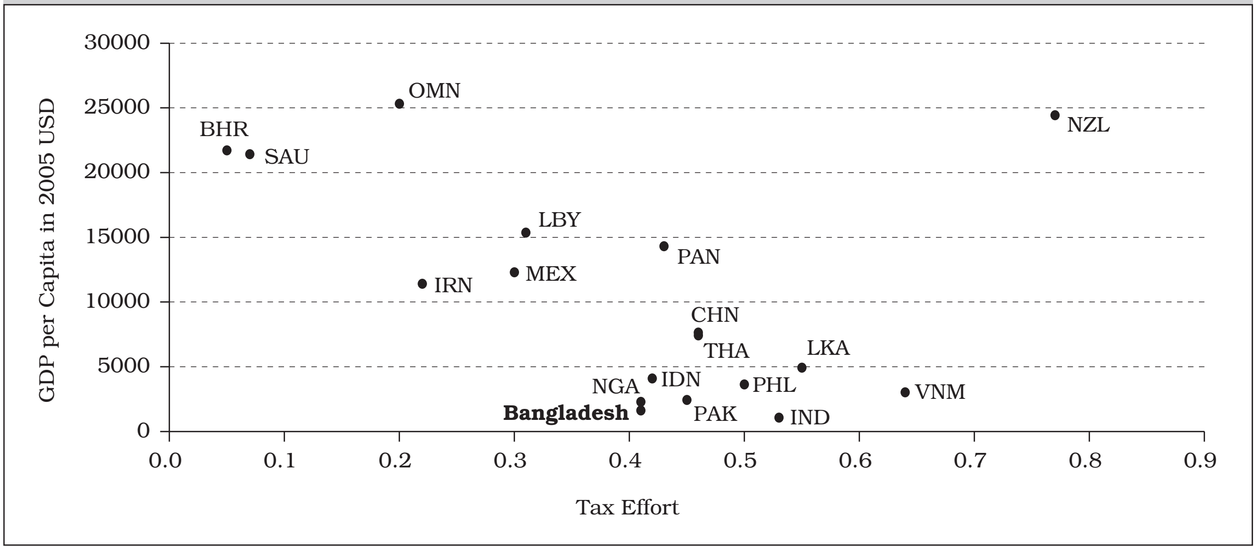
2.3.2 Revenue Mobilisation

Concerns as regards greater revenue mobilisation in the backdrop of small tax base, low tax compliance and tax evasion have plagued Bangladesh

The tax-to-GDP ratio in Bangladesh for FY2014-15 was 8.5 per cent (MoF, 2015a), which, compared to the average ratio of 15 per cent for developing countries, was one of the lowest in the world.[23] In recent years less than 1 per cent of the population has paid income tax (NBR, 2011). At 43 per cent, the national tax effort (the ratio between the share of the actual tax collection in GDP and taxable capacity) ranked Bangladesh last amongst its South Asian neighbours who (barring Pakistan) reported tax efforts of 53 to 55 per cent (Figure 2.7). The 7FYP has proposed increasing the tax-to-GDP ratio to 14.1 per cent by 2020 (GED, 2015a).[24] There will be a need for concerted efforts in areas of reforms if this ambitious target is to be achieved.

Figure 2.7

Tax Effort and GDP per Capita (113 Country Study): Is Bangladesh Lagging Behind?



Source: Fenochietto and Pessino (2013).

Widening the income tax base remains a top priority

The 7FYP has argued that an increase in the effective income tax rate[25] to 10 per cent for the top wealth decile[26] would yield a 2.5 percentage points increase in the current tax-to-GDP ratio (Tk. 43,240 crore).

Geographically equitable access to tax instruments should be extended

A CPD study on estimating potential tax efforts using Household Income and Expenditure Surveys (HIES) showed that the income taxpayer base and tax collections almost doubled and quadrupled respectively

[23] Most countries with a lower tax-to-GDP ratio are rich in natural resources such as oil, and therefore, are not reliant on tax as the primary source of revenue.

[24] The Annual Performance Agreement between the NBR and the Cabinet had set a target tax-to-GDP ratio of 10.6 per cent to be achieved by the end of the current fiscal year. However, as has been discussed above, this is unlikely to be achieved.

[25] The effective tax rate is the average rate at which an individual is taxed on earned income, or the average rate at which a corporation is taxed on pre-tax profits.

[26] Decile is a method of splitting up a set of ranked data into 10 equally large sub-sections.

Table 2.7

Tax Effort Estimates using 2005 and 2010 HIES Data

Year (by Availability of HIES Data)	Number of Potential Taxpayers (Lakh)	Number of Actual Taxpayers (Lakh)	Actual-to-Potential Income Taxpayer Ratio (%)	Amount of Potential Income Tax (Crore Tk.)	Amount of Actual Income Tax Paid (Crore Tk.)	Actual-to-Potential Income Tax Ratio (%)	Potential Income Tax-to-GDP Ratio (%)	Actual Income Tax-to-GDP Ratio (%)
2005	89.58	10.00	11.16	17,500.00	2,641.25	15.09	3.63	0.55
2010	70.26	19.19	27.31	19,700.00	9,893.24	50.21	3.05	1.53
Difference (%)	-21.57	91.93	144.72	12.57	274.57	232.74	-15.99	179.52

Source: Author's estimation.

from 2005 to 2010. However, a low compliance rates can be observed as only 27.3 per cent of all potential income taxpayers declared income tax in 2010 (Table 2.7). Hypothetically, doubling the compliance rate would increase the 2010 income tax-to-GDP ratio by an additional 1.5 percentage points (Tk. 13,700 crore). Regional variation in tax efforts was evident as, from 2005 to 2010, the share of households paying income tax rose quite dramatically in Dhaka and Chittagong urban areas and small metropolitan areas (SMAs) (Table 2.8). Potential taxpayer growth in SMAs suggests that geographically equitable access to tax instruments should be facilitated.[27]

Table 2.8

Percentage of Households, by Year and Region that Declared Income Tax

Division	Rural			Urban			Metropolitan Areas		
	2005	2010	Differences (%)	2005	2010	Differences (%)	2005	2010	Differences (%)
Barisal	<0.01	0.15	>1000	0.47	0.68	44.75	N/A	N/A	N/A
Chittagong	0.09	0.14	65.12	0.65	1.52	133.59	1.67	3.75	124.96
Dhaka	<0.01	0.14	>1000	0.81	1.89	133.17	1.04	6.29	505.38
Khulna	<0.01	0.09	>1000	0.23	1.49	554.63	0.71	N/A	N/A
Rajshahi	0.52	0.53	0.95	2.08	1.88	-9.66	1.00	0.58	-42.50
Sylhet	<0.01	<0.01	>1000	<0.01	1.00	>1000	N/A	N/A	N/A

Source: Author's estimation.

Note: Rural tax compliance were very low (below 0.01 per cent) in some surveyed regions. No households in Khulna SMA were recorded as having paid tax in the 2010 HIES, so cannot be used for comparison.

Changes to current AIT collection system through progressive withholdings-at-source tax rates would reduce scope for tax evasion by high income-earners at the stage of final settlement

The Income Tax Ordinance (1984) stipulates service-specific withholding concession. There is an opportunity to introduce progressivity to the current system by setting withholdings rates as a function of income.[28] As of now, no formal registration system exists for advance income tax (AIT) withholding entities with the NBR. Greater transparency and higher tax mobilisation at source could be achieved through an integrated identification mechanism that links all aspects of the taxpayer's finances, to be achieved through linking e-TIN (taxpayer identification number) with the involved party's national ID and/or business identification

[27] There are some evidences of underreporting of income in the HIES datasets which might affect estimates.

[28] Some industries, such as construction, display large variance in firm sizes, so a special single withholding rate for the entire industry would place differential tax burdens across firms in that sector.

number (BIN). NBR would thus have information on salaries, financial transactions and taxes for employees and business entities. NBR would also provide tax certificates to taxpayers directly through an electronic platform. Provisions for e-TIN should also be made for foreign nationals working in Bangladesh to ensure higher tax compliance from this particular group.

A major source of income tax is forgone because of largely informal arrangements in the labour market

The 2013 Bangladesh Labour Force Survey showed that roughly 50.5 million (87 per cent) of the 58.1 million employed persons aged 15 and above were informal workers.[29] To compare, while only about 10 per cent of the economy in OECD (Organisation for Economic Co-operation and Development) countries was informal, in developing countries the average was around 50 per cent. A three-fold increase in the share of formal employment to 40 per cent could lead to a near parity with the developing countries' average. This could potentially triple the income taxpayer base.[30] There is a need for a plan to raise this share. The government should therefore push for increased provision of formalisation of employment through labour law revisions where possible. In doing so the government must recognise that employment should provide gender parity and transparency of work conditions, and protect worker rights.

Greater formalisation of SMEs is necessary to improve revenue generation

A recent CPD study on SMEs showed that about 20 per cent of average firm expenditures has to be allocated towards formal registration costs, which was supposed to be provided free of charge (Rahman *et al.*, 2014).[31] These higher expenses are reported as the most common bottleneck to tax registration about 36 per cent of the surveyed firms remain unregistered due to the associated cost of compliance. Since nearly 16 per cent of all Bangladesh-based SMEs are currently not registered with the NBR, reducing compliance cost, incentivising registration and enforcing compliance will help mobilisation of SMEs' tax revenue.

Given the current corporate tax collection situation, coupled with recent rate reductions, it is advisable to keep corporate tax rates unchanged for the upcoming budget[32]

The government should address the need for transparency in the declaration of corporate taxes. Proper implementation of the recently enacted Financial Reporting Act should help in this regard. Publicly listed corporations are granted lower tax rates, and they get access to equity in the market through public trading. This provides strong incentives for companies to get publicly listed, which should be heavily encouraged by the government.

Poor land and property taxation policies can lead to underdeclaration of asset property taxes

Provisions allowing for investment of undisclosed income should be removed. Sections 19BBBBB and 19C of the Income Tax Ordinance (1984) stipulated special tax treatment provisions for investments in real estate and government Treasury bonds that persons with unexplained income sources can avail. India, in order to deal with the problem of black money, introduced a Bill (Benami Property Bill) in 1988 to target transactions carried out in other people's names. The Bangladesh government should consider similar law reforms regarding undisclosed wealth.

[29]Over 80 per cent of all non-agricultural workers were employed informally, with the distribution somewhat skewed towards female employees.

[30]However, concerns remain that this process will only bring in marginal taxpayers, where the low increase in tax revenue might not justify the cost of formalisation.

[31]Seventy per cent of all surveyed firms were not interested in obtaining tax benefits through proper tax registration, highlighting the general aversion towards tax declaration due to stringent compliance costs.

[32]The current corporate tax rate is 40 per cent, and the Tax Foundation estimated that the weighted worldwide average corporate tax rate and weighted Asian average corporate tax rate were 29.8 per cent and 26.67 per cent respectively in 2015.

Accounting for more than roughly 80 per cent of all exports, the RMG sector is a major source of tax revenue, but suffers from low tax compliance

According to NBR data, only one half of the registered garment companies submitted their income tax returns in FY2014-15.[33] Significant gains could be made from higher tax compliance of the RMG sector. Compliance had likely lowered due to the discontinuation of preferential corporate tax treatment for garments companies from 10 per cent to 35 per cent, as well as an increase in the tax-at-source rate from 0.3 per cent to 0.6 per cent. Assuming that RMG vendors operate at a 5 per cent profit margin, changing the effective tax rate has the potential to substantially raise revenue generation for the government.

Low VAT compliance performance stem from both governmental and business side bottlenecks

Briefs from the NBR showed that while VAT provides 35 per cent of total government revenue (4 per cent of current GDP), only a small share of all registered businesses pay the mandated VAT. False book-keeping and underreporting of inventory turnover are also widespread. The 2013 Bangladesh Enterprise Survey showed that 41 per cent of all firms (highest in South Asia) were expected to give 'gifts' in meetings with tax officials. Corrective actions are needed to discourage such corrupt practices. The government should reduce incentives for corruption by enforcing a strong reward and punishment system. Non-compliance amongst small businesses was primarily due to lack of access to VAT information and difficulty in filing tax returns. Measures in the form of online filing and payment of VAT, improving e-literacy amongst business-owners and switching to electronic cash registers (ECRs) could potentially facilitate increased VAT declaration and collection. Box 2.1 provides a list of VAT restructuring proposals made jointly by the NBR and the Federation of Bangladesh Chambers of Commerce and Industry (FBCCI), which proposes some revisions to truncated tax and package VAT policies in the view of new VAT law.

Box 2.1

An Update on the New VAT and SD Act 2012

The new VAT and SD Act 2012 is to come into force from 1 July 2016. The Act envisages a number of important changes: universal rate of VAT for all economic activities replacing the truncated rates; discontinuation of package VAT for small traders; no declaration as regards tariff value; significant expansion of business documentation and accounting for all registered businesses; provision of input credit only from registered enterprises. The new law will introduce an integrated online mechanism for VAT registration, return submission, refund and payment.

In view of prior consultations with key stakeholders, the government constituted a Joint Committee in October 2014 to deliberate on views and suggestions emerging from these consultations, particularly those voiced by the business community. The Committee included representatives from both the NBR and the FBCCI. The business community raised a number of issues that called for amendments to the Act; the Committee agreed to some of these. The Committee agreed to raise the limit of turnover tax for eligible traders, businesses and manufacturers, provide differential treatment to small traders, businesses and some specific sectors who were to pay VAT at a reduced rate (these will not be eligible to enjoy input VAT credit). However, difference of opinion persisted as regards collection of advance trade VAT (ATV) at import stage and provision of differential treatment for bargaining shops, amongst others.

It is to be noted that, introduction of the new VAT Act will call for development of necessary (soft and hard) infrastructure, human resource and skill development, training of VAT officials, and preparation of relevant stakeholders as regards compliance. Automation process for the new VAT regime needs test runs which has not been done as yet. The business community, particularly the SMEs, should undertake necessary preparatory works towards compliance with the new regime. All these preparations need to be done in a coordinated manner through participation of stakeholders and tax officials, at various levels.

[33] http://newagebd.net/197372/half-of-rmg-units-dont-pay-income-tax/

The NBR currently lacks adequate administrative resources in terms of human resource power and infrastructure

Dated methods and a largely paper-based work environment have constrained NBR's ability to deliver on its service and compliance improvement goals as envisaged in the NBR Modernization Plan. Greater use of information and communication technology (ICT) through electronic tax administration and declaration practices, with commensurate skills development will help tax compliance. More frequent tax fairs, raising awareness and establishment of more tax circles in high-density economic activity areas will be needed. In light of provisions being made for centralised processing of both income tax and VAT returns, there is an opportunity to go for digitising tax refunds.[34] Electronic tax compliance could also be incentivised for timely payment. NBR should consider strengthening its auditing capacity to deal with underreporting of income which undermines the cause of tax collection from large taxpayers.

Additional revenue can be generated through expedient resolution of cases by taking recourse to the Alternative Dispute Resolution (ADR) system

NBR Annual Report FY2013-14 reveals the number of ongoing tax-related cases is significant, of which high income-earning groups (above Tk. 10 lakh) constitute a major share (8,562 open cases).[35] Speedy resolution of these cases could be a potential source of revenue earnings. In view of this, energetic efforts should be made to take advantage of the ADR window and bottlenecks should be removed.

More stringent measures be implemented to reduce illicit financial outflows

Kar and Spanjers (2015) showed that around Tk. 44,000 crore (6.2 per cent of current GDP) was annually siphoned out of Bangladesh between 2004 to 2013 – over Tk. 76,000 crore (6.3 per cent of current GDP) was siphoned out of Bangladesh in 2013 alone. Globally, international institutions such as multinational corporations (MNCs) have been found guilty of misreporting transfer prices in order to keep their tax burdens low. The Transfer Pricing Cell should be further strengthened and steps should be taken so that the Cell has access to global platforms and databases for tracing and tracking illicit flows, misinvoicing by MNCs and other business enterprises. The recent Panama Papers scandal, coupled with prior information provided by Swiss banks, calls for appropriate investigation by concerned authorities in Bangladesh.

In summation, proposed changes to a progressive AIT system, increased formalisation of labour and enterprise (particularly SMEs), a digitised filing and refund/rebate system, greater transparency in corporate tax declaration, implementation of the new VAT law by taking concerns of the business community in cognisance, improved property and RMG sector tax compliance, an efficient ADR mechanism, reducing illicit financial outflows and overhaul of NBR institutional bottlenecks will significantly improve revenue mobilisation efforts.

2.3.3 Public Expenditure

Allocate resources in a prudent way

During the FY2010-11 to FY2014-15 period, the public expenditure budget could not be fully spent in any year. The government will need to utilise its resources to the fullest to put the economy on a higher growth trajectory. Reorganising and raising expenditure particularly for the social sectors, including SSNPs for the marginalised people, will help the government both in short and medium terms. And in this context, the government should not be hostage to the compulsion of keeping the budget deficit within 5 per cent of GDP.

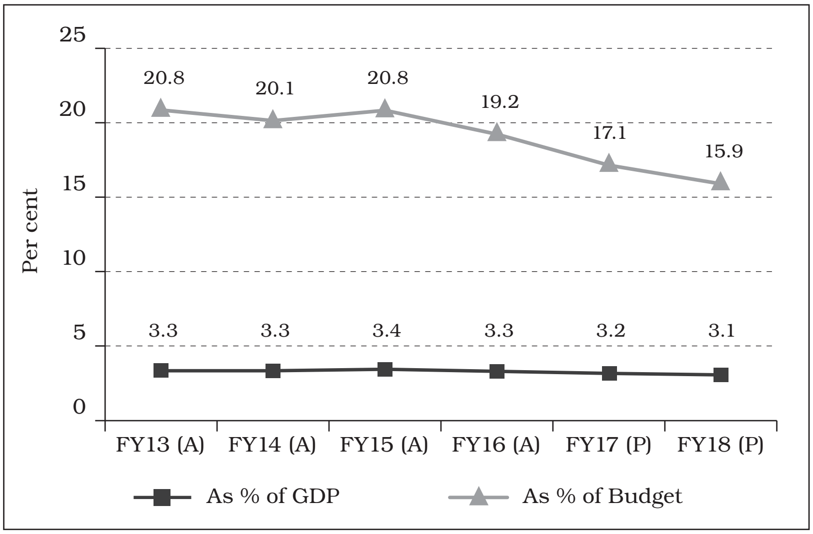
[34] The current tax code does not provide a tractable refund system.
[35] About 10.15 per cent of all unresolved cases stemmed from high-income businesses.

Emphasise allocation for social sector in budget to implement the targets of 7FYP and SDGs

Despite the government's pledge to give education, health and other social sectors the highest priority, budgetary allocation and future projections regarding social sector spending does not echo this conviction. As stated in CPD (2016), allocations for six ministries concerning social welfare and security, have gone through persistent decline both as percentage of GDP and of total budget. There was a marginal increase in FY2014-15, but the allocation decreased again in FY2015-16. According to the Medium Term Budgetary Framework (MTBF), this declining trend will continue until FY2017-18 (MoF, 2015b). This trend, as presented in Figure 2.8, is not in agreement with either the 7FYP or the SDG commitments of the GoB.

Figure 2.8

Allocation for Social Sector for Six Ministries as Percentages of GDP and Budget



Source: Calculated from Medium Term Budgetary Framework (MTBF) and Ministry of Finance (MoF).
Note: A refers to allocation and P refers to projection.

Reflect National Social Security Strategy (NSSS) targets in the national budget

Proper attention towards adequate allocation favouring SSNPs appears to be wanting in the budgetary framework in recent years (CPD, 2015a). Allocation for SSNPs (about 27 per cent of which is incurred on account of pension-related expenditure for government employees) hovered around the 2 per cent of the GDP. This allocation was targeted to be raised to 3 per cent of the GDP in the Sixth Five Year Plan (SFYP). However, this was not to be; also it is observed that the budgetary targets were not aligned with the proposals of the National Social Security Strategy (NSSS). Excluding government pension scheme, the other SSNPs' budgetary targets are much lower than envisaged in the NSSS (Table 2.9). It should also be

Table 2.9

Budgetary Allocations and Projections vs NSSS Targets of Major Safety Net Programmes

(Crore Tk.)

Programme	Budget			NSSS Target	Projection (MTBF vs. NSSS)			
	FY14	FY15	FY16	FY16	MTBF FY17	NSSS FY17	MTBF FY18	NSSS FY18
Old Age Allowance	980	1,307	1,440	2,010	1,440	3,530	1,440	3,740
Pension for Retired Government Employees and their Families	6,692	8,482	11,584	7,600	N/A	8,000	N/A	8,500

(Table 2.9 contd.)

(Table 2.9 contd.)

Programme	Budget			NSSS Target	Projection (MTBF vs. NSSS)			
	FY14	FY15	FY16	FY16	MTBF FY17	NSSS FY17	MTBF FY18	NSSS FY18
School Stipend (Primary+Secondary)	1,000	971	1,159	3,870	0	6,830	0	7,240
Allowances for the Widowed, Deserted and Destitute Women	364	486	534	1,150	534	2,040	534	2,160
Vulnerable Group Feeding (VGF)	1,327	1,419	1,453	N/A	1,575	N/A	1,719	N/A
Employment Generation Programme for Poor	1,400	1,500	1,500	N/A	1,600	N/A	1,700	N/A

Source: Calculated from Medium Term Budgetary Framework (MTBF); Ministry of Finance (MoF); and GED (2015b).

mentioned that the government's SSNPs are inadequate not only in monetary terms, but also from the coverage point of view.

Provide adequate allocation for maintenance of existing infrastructure

Infrastructure maintenance expenditures have remained stagnant in real terms over the past decade (Hussain *et al.*, 2015). Since investment expenditure has been significantly on the rise in recent years, there is a growing concern regarding the ability to ensure proper maintenance of the new capital investments. Expenditure on repair, maintenance and rehabilitation declined from about 3.9 per cent of total non-development expenditure in FY2010-11 to about 3.5 per cent in FY2014-15. This share was only 1.5 per cent for the first six months of FY2015-16. From FY2010-11 onward this share has been showing a generally declining trend (Figure 2.9). In view of the increasing expenditure on new physical infrastructure, allocation of funds for maintenance of these infrastructure should be correspondingly increased.

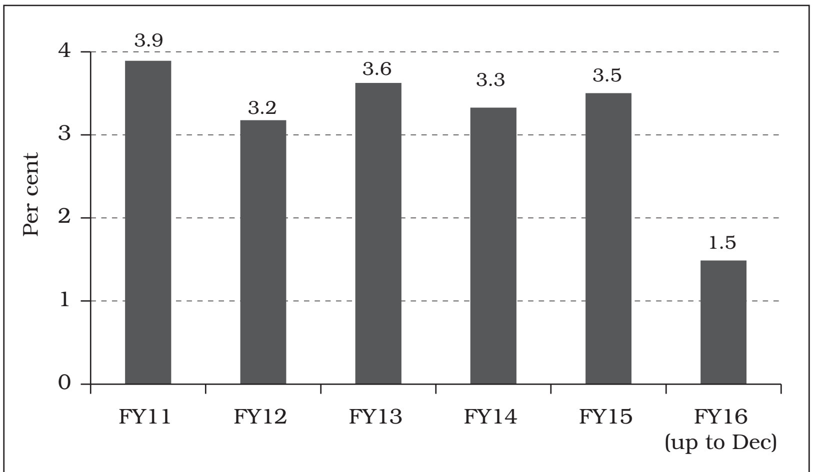


Figure 2.9

Repair, Maintenance and Rehabilitation as % of Total Non-Development Expenditure

Source: Calculated from Monthly Fiscal Reports, Ministry of Finance (MoF).

It is high time to adopt a National Subsidy Policy

In the backdrop of the low level of international petroleum prices, BPC is unlikely to seek any (subsidy) support during the FY2015-16 period. Regrettably, as of now, there is no clear reporting on the part of BPC as to the amount of profit being made and the way this profit is being distributed (e.g. repayments of past debt, dividend to government, profit accumulation, etc.). On the other hand, subsidy demand for electricity has remained persistent. The government has stayed away from downward adjustments of administered prices of petroleum products in the domestic market. It may be recalled that, earlier CPD in its state of the economy report released in January 2016, showed that a reduction in prices of petroleum product will be beneficial to the economy in terms of raising GDP, employment and containing inflation. Indeed, CPD estimates showed that a 10 per cent reduction will lead to 0.3 per cent gain in terms of GDP growth. However, apparently revenue concerns held the government back from taking a positive decision in this regard. Recently, the government has announced that it will reduce the fuel prices, but in a phased manner. At the same time, an upward adjustment of electricity and gas prices are also being contemplated. The adjustment of these administered prices should be calibrated by taking into cognisance the revisions of gas and electricity prices, overall impact of the price-change mix on major stakeholder groups, and government's subsidy-related expenditure and earnings. Besides, in the context of the required transparency in allocation, efficiency in delivery and accountability in the management of subsidies, there is an urgent need for Bangladesh to have a National Subsidy Policy. This point was forcefully articulated in a recent CPD paper (CPD, 2015b).

A comprehensive strategy for better ADP implementation

Lack of improvement in ADP implementation in FY2015-16 has once again brought into focus the need for addressing the persistent weaknesses of government's implementing agencies and the challenges faced by them. Some of the major challenges that were identified by the Ministry of Planning in the course of project implementation in FY2014-15 included land acquisition, preparation of work plan, frequent changes in schedule rates for construction, and recruitment of consultant/firm and manpower including project directors (PDs). Frequent change of PDs has also emerged as a major bottleneck. Procedural lapses which begin with delays in the approval of projects were also identified as a major reason for lax ADP implementation (CPD, 2011; 2015b). Post-approval procedural delays in land acquisition and procurement also hold back timely commencement of project work.

Further, implementation of ADP projects, in a timely manner and within initial cost estimates, continue to be problematic. In FY2013-14 only 14.2 per cent of the total 'to be completed' projects were actually completed within the stipulated time and planned allocation. About half (48.9 per cent) of the completed projects experienced time overrun. Such time overrun led to 51.1 per cent increase in the average cost of all completed projects. However, financial accounting in the form of expenditure does not necessarily mean actual implementation. Release of funds to project account is often taken as a proxy for progress of implementation. While, often financial progress of the completed projects remains high, this is not evidenced by actual progress in physical terms and as per the needed quality of work (see Annex Table 2.2).[36] Thus, the overall quality of ADP implementation is often compromised. In view of above, the following recommendations are put forward to raise the efficacy of ADP implementation in Bangladesh.

Recent government initiatives/plans should be put into effect

Recently the government has taken a number of initiatives to accelerate ADP implementation. A policy on the Project Preparatory Fund (PPF) has been drafted, with the aim to facilitate timely and successful implementation of the development projects. The main objective of the PPF is to provide funds for completion of preliminary activities before the launch of a development project.[37] This new provision and the attendant costs need to be reflected in the upcoming national budget. The government has also recently informed about its plan to appoint a foreign consultant to fast-track the ADP implementation.

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[36]An ongoing CPD study found that on an average 66.2 per cent of completed projects were declared as completed without 100 per cent physical progress during FY2000-01 to FY2014-15 period.

[37]Preliminary activities include land acquisition, feasibility study and environmental impact assessment (EIA).

One may recall that a number of proposals as regards expediting ADP implementation were announced last year by the Planning Minister. These include: (i) appointing PDs through direct interviews by the line ministries and divisions[38]; (ii) assigning a dedicated official in each government agency for monitoring and evaluating respective projects; and (iii) delisting the longstanding 'non-operational' projects from the ADP.[39] However, these are not being adequately followed up. It is recommended that the upcoming budget will report progress on these issues.

Besides, each year, Implementation Monitoring and Evaluation Division (IMED) provides some recommendations in the annual progress report based on the challenges faced during the project cycle. But, these are often not adequately followed up with concrete measures. These recommendations should be discussed and followed up in the quarterly progress meetings on ADP. The proposals need to be implemented.

Intensive monitoring of priority projects, which are close to being completed, should be a priority

In view of the low level private investment and significant infrastructure deficit, better (in terms of quality) and timely implementation of the ADP, particularly that of growth-enhancing infrastructure projects, should remain a policy priority. Earlier, CPD (2015c) selected a set of 26 projects under the ADP for FY2014-15; all these projects were supposed to help boost growth and employment. CPD's second interim review of the state of the Bangladesh economy in FY2014-15 (CPD, 2015d) urged for close scrutiny and tracking of progress of these projects. Fourteen of these 26 projects were supposed to be completed in FY2014-15 (or even earlier). Cost and completion deadline of number of these projects were revised for a few, more than once. Indeed, barring one project, the other 13 projects were not completed in FY2014-15, and were carried forward in the ADP for FY2015-16 (CPD, 2015a). One suspects that the majority of these will not be completed within FY2015-16. Further cost and time overruns for these priority projects may be a possibility unless special policy and administrative attention is given to speed up their implementation. A special task-force needs to be formed which could closely monitor the implementation of these projects. It is also important that adequate funds are allocated for these projects in the forthcoming ADP.

Landmark social sector projects should be prioritised in line with the SDGs

There are three major development programmes/projects in the social sector in the ADP – two in the education sector and one in the health sector.[40] Two out of these three projects were supposed to be completed by FY2015-16 as per respective timelines. But, CPD analysis suggests that these projects will not be completed in time; indeed, one of these two has already experienced time extension.[41] Consequently, special attention will need to be given to these important large social sector projects through adequate fund allocation in the upcoming budget for FY2016-17. Furthermore, in the next phase, project objectives will have to be redesigned and aligned with the SDG targets.

Separate strategy for foreign-aided projects needed

Foreign-aided projects are often required to follow additional procedural steps in the overall project cycle. Last year, the Planning Minister noted in a meeting that "the project directors often feel discomfort in utilising foreign aid part of the development projects although they feel much comfort in utilising local funds."[42] This, according to him, was not acceptable. He talked of undertaking an effective strategy through

[38]Developing guidelines to this end was also planned.

[39]In this connection, it was planned that the concerned ministries and divisions would be served letters on 1 October every year to send the list of non-performing projects to the Planning Commission.

[40]These are Primary Education Development Program-III (PEDP-III), Secondary Education Quality and Access Enhancement Project (SEQAEP), and Health Population and Nutrition Sector Development Program (HPNSDP).

[41]Maximum possible completion of these projects will be in the range of 59 to 76 per cent if they spend all their allocation for FY2015-16.

[42]See http://www.dhakatribune.com/business/2015/feb/16/kamal-asks-project-directors-utilise-foreign-assistance

consultation with the Economic Relations Division (ERD) of the MoF. A dedicated strategy is thus needed, with a more proactive role of the aid effectiveness unit of ERD, to simplify the overall process for fund disbursement and procedural delays concerning foreign-aided projects. Hopefully, the next budget will spell out this strategy.

Monitoring and evaluation mechanism needs to be strengthened

Project Completion Reports (PCRs) are important to assess the implementation of a particular project. As per IMED guidelines, preparation and submission of PCR to IMED should be done within three months of completion (IMED, 2012).[43] PCRs should also be made public to ensure transparency. Low quality of the submitted PCRs and also the lack of needed human resources at its disposal (as per IMED organisational structure) often do not allow proper evaluation of completed projects (see Annex Table 2.3 for recent status). An inter-ministerial committee could be constituted to maintain consistency in the quality of PCRs submitted by different ministries. The number of impact analysis of projects also needs to be increased. More independent experts should be involved in this work. Proper impact analyses could be a great help in designing future projects which will improve the overall quality of implementation and outcome.

Establish an independent Public Expenditure Review Commission

A number of countries have undertaken public expenditure reviews (at both central and state levels) with a view to achieving efficiency and ensuring accountability. These reviews are prepared taking into cognisance macroeconomic context as well as fiscal policy, public sector performance and sustainability concerns. At present, there is a need to significantly raise efficacy of public expenditure in Bangladesh, particularly in view of the increased volume and change in the composition. In this context, CPD has earlier urged for setting up an independent Public Expenditure Review Commission (PERC) which would be mandated to provide medium term policy guidelines to the government and formulate a concrete set of strategies in order to improve the current level of efficiency. The proposed Commission may be vested with broad set of responsibilities under its Terms of Reference (ToR). Some of these could be as follows:

a. Review efficacy of programmes/schemes of major departments with appropriate recommendations to be proposed for their restructuring and convergence to facilitate improvement of their development effectiveness;
b. Develop a framework for performance and outcome monitoring of the development schemes/programmes with a view to raising the efficiency of public spending;
c. Review the scope for consolidation of smaller schemes and expenditure items with common/complementary objectives into a fewer number of viable programmes;
d. Examine classification of expenditure according to the Public Moneys and Budget Management Act, 2009;
e. Suggest appropriate measures in order to address inconsistencies and inefficiency with a view to ensuring rational and effective use of public expenditure;
f. Review issues on data accountability;
g. Review processes and institutional mechanisms of programme implementation and service delivery to improve efficiency and cost effectiveness;
h. Review the framework of all subsidies, both explicit and implicit, and examine the economic rationale for their continuance; put forward recommendations for making subsidies transparent; and suggest measures for maximising their impact on the target population at minimum cost;
i. Design an effective strategy so that a reasonable proportion of expenditure on services through user charges could be ensured;

[43]As a matter of fact, about 35 per cent PCRs of total completed projects were not submitted to IMED on time in FY2011-12 which rose to 41 per cent in FY2014-15.

j. Suggest areas for adoption of new technologies for effective implementation of programmes and delivery of services;
k. Recommend a set of measures for optimising the staff strength of government departments, attached offices and institutions, for skill enhancement of existing staff, and for redeployment of programmes and delivery of services;
l. Put forward suitable recommendations as regards any other relevant issues with a view to ensuring good governance and improved management of government expenditures.

2.3.4 Budget Deficit Financing

Budget deficit financing needs an optimum mix

Over the past few years, a significant change in the sources of budget deficit financing has been observed (Figure 2.10). As was noted, net financing from foreign sources (including grants) remained low (only 0.4 per cent of GDP) in FY2014-15 due to low level of project aid utilisation in the ADP. Additionally, amongst the domestic sources, sale of NSD certificates has emerged as the single largest contributor.[44] Indeed, as of January 2016, NSD certificate sale accounted for about half of the total outstanding domestic debt liability of the government (Tk. 1,21,733 crore). A year ago, the corresponding figure was about 43 per cent (Tk. 92,136 crore).

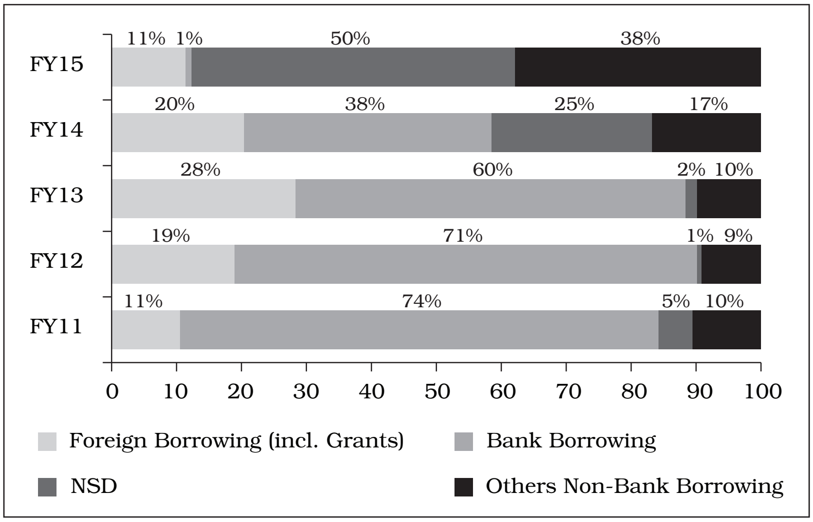

Figure 2.10
Deficit Financing Mix in Recent Years

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

As has been mentioned above, NSD net sale remained strong in FY2015-16 as rate of return from the NSD was significantly higher compared to banking sources (i.e. interest income). People are now more interested to go for savings through preferred NSD instruments. Top four NSD bonds, i.e. Family Savings Certificate (34.3 per cent), 3-month profit bearing Sanchayapatra (26.3 per cent), 5 years Bangladesh Sanchayapatra (17 per cent) and Post Office (12.8 per cent) comprised 90.3 per cent of total sale of NSD certificates in FY2014-15. Indeed, a rise in the popularity of 3-month profit bearing Sanchayapatra may be observed, as it has a relatively short maturity period (3 years, compared to 5 years for other instruments), and thus gain-wise more lucrative for small savers.

In view of the current scenario, it would be advisable that the government balances the borrowings from bank and non-banking sources. In a recent government meeting on resources for budget FY2016-17, the

[44]For example, in FY2014-15, half of the total financing originated from sale of NSD certificates. Indeed, government borrowed only Tk. 514 crore from banking sources against a hefty annual target of Tk. 31,200 crore in FY2014-15.

central bank governor proposed to cut interest rate of NSD certificates. However, it may lead to further reduction of the real interest rate on commercial bank deposits which has recently moved to negative terrain. Rather than bringing down the savings certificate rates significantly, since many small savers do take advantage of the schemes, lowering of the maximum purchase amount could be a preferred policy option. This will also reduce fiscal liability of the government. However, stringent maintenance of eligibility criteria, digitisation of the purchase process and adoption of penalty measures for violation of rules will have to be put in place to deter financially better-off investors from purchasing the relatively high-yielding NSD facilities beyond the reduced limit.

2.3.5 Fiscal Measures

Proper assessment of effective fiscal measures needed

Fiscal measures are important instruments deployed by the government in the national budget with a view to achieve specific objectives. Bangladesh's national budgets offer various fiscal measures targeting different groups – consumers, micro, small and medium entrepreneurs, corporate bodies, owners of export-oriented industries, importers and retailers, limited income-earners, asset holders, etc. While such measures attempt to target the demands of various groups, in absence of proper pre- and post-impact assessment it is difficult to appreciate whether such measures are adequate or not, how long those measures are needed to be in place, what direct and indirect benefits are enjoyed by the target groups, and what is the overall economic impact of these measures. One general observation in view of the above is that, there should be comprehensive ex-ante and ex-post analyses of the various measures (see Box 2.2). This exercise will help identify fiscal measures that are most appropriate to address the developmental challenges facing the country.

During FY2015-16, government has further extended tax holiday facility for the Information Technology Enabled Services (ITES) and Nationwide Telecommunication Transmission Network (NTTN) sector till 30

Box 2.2

Stakeholders' Perception on Selected Fiscal Measures for FY2015-16

CPD conducted a number of telephone interviews to get the perception of relevant stakeholders whose interests were impacted by various fiscal measures in the budget for current fiscal year (FY2015-16). A number of observations came up on some selected fiscal measures following the interviews.

a) Personal income tax: Some low-income earners felt that, raising the threshold limit of the personal income tax from Tk. 220,000 to Tk. 250,000 and subsequent changes in the other income slabs were good moves, but it did not go far enough.

b) Corporate income tax: The initiative to reduce corporate income tax for public listed companies from 27.5 per cent to 25 per cent, and for public listed bank, insurance and financial institutions from 42.5 per cent to 40 per cent, was in general welcomed by budgetary business entities. However, they felt that transition of such moves into investment was contingent upon many other factors.

c) Changes in duty structure at import stage: A total of 1,675 products have seen changes in customs duties (CDs)/SDs/regulatory duties (RDs) at the import stage in the FY2015-16 budget which was a major move towards reducing the effective rate of protection (ERP) enjoyed by these products. Considering that the levels of development of local industries was quite diverse, competition faced by domestic industries was uneven, owing to tax avoidance in case of imported products and incidences of dumping through import, a proper assessment is needed to analytically determine the levels of effective protection that is needed for the development of local industries, and then calibrate fiscal policies accordingly.

The general perception is that there should be more consultations with key consumer-producer groups, these should be appropriately documented and then get reflected in the budget.

June 2024 from the earlier 30 June 2019. Tax holiday has been given for automobile manufacturing and tyre manufacturing industries as well. Besides, existing area-based tax holiday facility has been continued. However, stakeholders gave mixed reaction as regards such measures as they felt that without having necessary infrastructural facilities in place it would be difficult to attract entrepreneurs to invest in those supported sectors; tax holiday facility alone was not enough.

In this backdrop, it is felt that there should be a proper institutional set-up to assess the impact and implications of various fiscal measures announced in the national budgets. As in many other countries, the Finance Ministry should publish a list of all fiscal incentives offered in the budgets and their implications in terms of effective rate of protection (ERP), foregone tax revenues, benefits expected and justification for the duration for which such incentives were to be offered. This type of analytical work and assessments could be carried out by the NBR in association with the Bangladesh Tariff Commission (BTC), and for this necessary human resources and technical support will have to be made available. Impact assessment of various fiscal measures should be made public at the end of the fiscal year when the new budget is presented.

Support needed to make small businesses tax compliant

A large number of SMEs of the country are not tax compliant – many SMEs are not registered with appropriate authorities; many do not have a TIN or have VAT registration (see Box 2.3 below). NBR should take energetic measures to encourage these informal business entities to get registered through awareness-raising programmes, dissemination of information about advantages of formalisation and enforcement of relevant laws. The majority of small entrepreneurs do not maintain proper accounting system which is an essential pre-condition to be compliant under the new VAT law. Small entrepreneurs often do not have the needed accounting knowledge and also are not in a position to hire accountants. NBR should develop a proper work plan to encourage SMEs to get registered, organise training sessions, prepare manuals, and in general to do all the needful in preparation of introduction of the new VAT law as well as to provide necessary training to make them able to undertake the required tasks to be compliant as per requirement.

Box 2.3

Pre-Budget Dialogue 2016 – Development of the SMEs of the Bogra Region: Challenges and Initiatives

CPD organised a pre-budget dialogue on 24 March 2016 in Bogra city with the objective of getting local level stakeholders' perspectives on various fiscal and budgetary measures favouring the development of SMEs.[45] Based on the presentation and views expressed by the stakeholder on the dialogue, following suggestions emerged in the context of the upcoming national budget for FY2016-17.

a) Special efforts needed to formalise SMEs: A large part of SME units in the Bogra region are not tax compliant – these enterprises operate without necessary documents such as business registration, VAT identification number, TIN and other documents. Lack of formalisation often does not allow these SMEs to enjoy fiscal incentives; on the other hand, under the proposed new VAT Act these entities were likely to face legal difficulties as well. In view of this, there was a felt need for concerted efforts towards formalisation of SMEs.

b) 'Customisation' of financial products for better access to finance: Access to finance is yet to reach the doorsteps of small entrepreneurs due to various reasons. Lack of proper documents is a major reason why they are not being able to access credit from commercial banks which have dedicated low interest windows for SMEs. Given the nature of market demand and the marketing patterns, entrepreneurs would like to have more flexibility in the repayment schedule of loans from banks (e.g. seasonal nature of demand for credit, business cycle, etc.). In this backdrop, commercial banks should identify innovative and 'customised' financial products to reach potential SME clients. A district monitoring committee should be constituted to monitor whether SME loan is being disbursed properly to the target groups.

(Box 2.3 contd.)

[45]Moazzem *et al.* (2016).

(Box 2.3 contd.)

c) Support to organise the unorganised entrepreneurs: Challenges faced by regional SMEs will be difficult to address in the absence of cluster-based association/groups, as was observed by participants of the Bogra dialogue. Such clusters would be helpful not only for lobbying with appropriate authorities in articulating budget-related demands, but also from the perspective of implementing supportive measures and deploying the fiscal-monetary incentives for SMEs. It was also felt that strong and effective local government institutions (LGIs) were needed for the above to happen. Participants at the dialogue also felt that good infrastructure was needed to facilitate both production and marketing, and in this context, they urged for construction of four-lane Bogra-Tangail highway.

d) Support for development of 'customised' infrastructure: Lack of proper transport facility leads to high production/business costs for SME clusters located in rural areas in the Bogra region. Bogra BSCIC (Bangladesh Small and Cottage Industries Corporation) industrial estates lack necessary land and other facilities to accommodate the needs of old and new SMEs. In this context, these regional SMEs need more 'customised' infrastructure for more economically viable operation of their supply chains. In this connection participants urged that a special economic zone for SMEs be set up in the Bogra region.

e) Overcoming challenges to raise competitiveness: Different clusters face different types of challenges in maintaining their competitiveness. These relate to differences in market segments they cater to, domestic or export orientation, product quality and standards, competition with substitute products (both local and imported), lack of infrastructure and linkages with retail markets. Support measures for SMEs should be calibrated according to the particular types of felt-needs that they would like to address. Many SMEs would like to target regional and global markets; they need marketing support to be able to do this. In this backdrop, they are in need for supportive measures and incentives to raise productivity, improve quality and standards, and deal with market access, marketing knowledge and risk management. Regional technical institutes such as (Bangladesh Institute for Technical Assistance Center (BITAC) at Bogra) should be adequately endowed to provide such services.

f) Developing women entrepreneurship: Despite various efforts at the national level, women entrepreneurs at regional level face formidable difficulties in setting up enterprises and in getting access to special credit facilities targeted to cater to their particular needs. Participants complained about lack of gender sensitivity among concerned officials, be it banks or government offices. On their part, banks also complained about difficulty they face in categorising women SMEs and lack of formalisation concerning women-led enterprises which make it difficult to provide credit from special and dedicated window set up to develop women entrepreneurship and women-led enterprises. It was felt that targeted programmes were needed to address the challenges and problems voiced by both sides.

2.3.6 Fiscal, Budgetary and Other Economic Reforms

Fiscal and budgetary reforms

CPD (2016) strongly suggests in favour of undertaking the needed reform measures with a view to improve macroeconomic and sectoral efficiency. In this connection, more focus is needed on implementing 'second generation' reforms by ensuring higher levels of transparency and independence of regulatory bodies to generate efficiency, competitiveness and distributive justice. Higher transparency in fiscal and budgetary processes should be one of the key areas of these reforms. As some of the other developing countries, Bangladesh practices a budgetary process which is both complex and complicated, and sometimes hidden and inconsistent. Fiscal and budgetary transparency calls for "openness towards the public at large about government structure and functions, fiscal policy intentions, public sector accounts and projections" (UN, 2000: 18). Transparency could be achieved through five key aspects: a) clarity and openness about the budget decision-making process and the underlying constitutional or statutory authority; b) public disclosure and distribution of budget information; c) detailed reporting of budget expenditure/revenue; d) a comprehensive scope, accounting for assets and liabilities, targets, projections, performance measures and structural balance; and e) budget integrity, control and accountability and budget forecasting and projections. Bangladesh lags far behind in terms of international standards for compliance as regards transparency in the budgetary processes. It may be noted here that, Bangladesh meets only 12 out of 76 standards in the process of implementing national budget. Discussion in the Parliament and Parliamentary Standing Committees and more active engagement of key stakeholders such as civil society actor, workers

Box 2.4

Opinion of Young Professionals in view of the Upcoming FY2016-17 Budget

CPD organised a discussion session with young professionals titled "Conversation with Future Leaders" on 25 February 2016 as part of a series of consultations which were organised to discuss relevant issues concerning the upcoming national budget for FY2016-17. Eleven young entrepreneurs and leaders participated in the discussion session. A number of concerns, as also recommendations in view of the upcoming budget emerged from this discussion. The participants felt the need for a more proactive involvement of youth in national policy making. The discussants urged for a platform where the views of the future generation of the country on issues of national importance could be voiced and heard. They felt that policy debates in Bangladesh are often over-politicised, and because of this, even constructive and meaningful inputs on key developmental issues are often not acted upon. They thought that there is an uncertainty as regards implementation of the needed reform initiatives. Participants put emphasis on the need to ensure that development was sustainable and that policies should be designed in such a manner that the cause of sustainability got advanced. Participants were of the opinion that the FY2016-17 budget should be formulated by taking cognisance of economic priorities and allocative efficiency. They suggested that fiscal structure, proposals and incentives should be designed in a manner that balances the interests of domestic and export-oriented industries. They urged for higher allocation for education, particularly putting emphasis on tertiary education. They recommended that more resources should be allocated for skills development, highlighting the cause of employability; they also asked for setting up a Green Fund to promote environment-friendly investments and production processes. Participants felt that sectors such as ICT, fashion and design segments in production processes and e-commerce-based activities where young people have an interest and advantage should receive incentives and budgetary support.

and business representatives will be needed to ensure transparency in this regard. Indeed, during a consultation meeting with CPD, the young professionals of Bangladesh also called for greater voice in the budgetary process (Box 2.4).

Present study highlights lack of transparency in a number of areas where reform measures are called for. These include:

- Disclosure of financial accounts of state-owned enterprises (SoEs);
- Transparency in government's asset acquisition;
- Transparency in defense budget;
- Transparency in local government financing;
- Transparency of non-government organisation (NGO) financing; and
- Transparency in South-South financial transactions, a case being the Indian Line of Credit (LoC).

Disclosure of financial accounts of SoEs

Financial accounts of the 29 SoEs need to be made public in a transparent manner in order to better understand financial health of these enterprises. There is a lack of clarity as regards major heads of their financial accounts such as income, expenditure, income, profit/loss, debt, liability and assets, etc. For example, BPC, a state-owned commercial agency, experienced a major change in its financial account and health between FY2013-14 and FY2015-16 because of the windfall gain enjoyed on account of the differences in the petroleum prices between the international (low prices) market and the domestic regulated (high administered prices) market. According to Bangladesh Economic Review 2014, BPC incurred a net loss of Tk. 2,489.86 crore till FY2013-14, it has unpaid debt service liability of Tk. 19,71,617.6 crore (as of June 2013) and total due of Tk. 14,183.64 crore (till December 2013). However, the financial position of BPC has significantly improved over the following period, thanks to the low price of petroleum in the international market. According to Bangladesh Economic Review 2015, BPC made a net profit of Tk. 3,454.7 crore till 22 April 2014; its unpaid debt service liability has reduced to Tk. 22,28,423.9 crore (as of June 2014) and total due fell to Tk. 11,152.78 crore (till 31 December 2014). Financial position of BPC has definitely improved further in FY2015-16 due to the falling fuel price in the global market, with domestic prices remaining the same. Higher transparency of the financial account of BPC would help understand how the windfall gain has changed BPC's bottom line, how this has been utilised by BPC till date (a part of this profit was perhaps used to adjust accumulated losses and repay earlier debts). Transparency in this regard will help better and more appropriate policy making in the areas of price adjustments and allocating relative benefits to be enjoyed by key stakeholders and sectors (e.g. farmers, transport users, producers, exporters and consumers).

Bangladesh Jute Mills Corporation (BJMC), another SoE, has been operating with a huge loss for last several years (net loss at the end of FY2014-15 was Tk. 640 crore) and its unpaid debt service liability was to the tune of Tk. 412,260.6 crore and the outstanding amount was around Tk. 1,219.1 crore (by FY2013-14). Recently, the GoB has decided to disburse a total of Tk. 1,000 crore to meet BJMC's dues with its workers which include Tk. 275 crore for gratuity, Tk. 300 crore for provident fund and workers' salaries for eight months' worth Tk. 48 crore, and the rest towards other activities. In business-as-usual case, expenses related to gratuity and provident fund are supposed to be adjusted in a 'built-in' manner, which either was not the case here, or the accumulated reserves were used for other purposes which should not have been the case. It is not clear whether dues with jute growers and jute traders will be adjusted from this additional budget. There is no denying that workers should not be penalised for bad policies and their dues have to be given. However, there is a need for transparency in the manner BJMC works and about its accounting and management practices. BJMC should present a detailed financial account including the assets and liabilities it has, its debts and dues and its accounting practices. This is needed for a better understanding about its work and financial position. Likewise, other SoEs should also disclose their financial accounts and management practices in a transparent manner. Taxpayers' money help run the SoEs, and they have a right to know how their money is spent and whether it is well spent.

Transparency in government's asset acquisition

Each year the government allocates a significant amount of resources for non-development, capital expenditure which includes acquisition of assets and works and investments in shares and equities. According to the budget statement of FY2015-16, this expenditure has almost doubled over the most recent two years – from Tk. 10,441 crore in FY2013-14 (actual) to Tk. 19,988 crore in FY2015-16 (budget) (Table 2.10). While the rise in such expenses is well understood in a growing economy like Bangladesh, the quality of the capital expenditure remains questionable. For example, government has spent about Tk. 14,477 crore for investment for recapitalisation of nationalised commercial banks (NCBs) over a period of three

Table 2.10

Non-Development Capital Expenditure

(Crore Tk.)

Source of Expenditure	FY14	FY15	FY15	FY16
Acquisition of assets and works	5,607	7,025	8,231	8,038
Acquisition of assets	3,857	5,763	6,456	6,683
Acquisition of lands	487	144	193	158
Construction and works	1,263	1,118	1,582	1,197
Investments in shares and equities	4,834	18,985	13,797	11,950
Share capital	57	11,160	7,472	5,025
Equity investment	300	2,800	1,300	1,900
Investment for recapitalisation	4,477	5,000	5,000	5,000
Others	-	25	25	25
Total non-development capital expenditure	**10,441**	**26,010**	**22,028**	**19,988**

Source: Ministry of Finance (MoF).

years with a view to help these banks meet respective capital shortfalls. Given the persistent weakness in the governance of the NCBs along with operational weaknesses, this type of periodic rescue will hardly address the root causes. Rather, it helps sustain the anomalies and inefficiencies. There is an urgent need to examine the underlying causes in an in-depth manner. It may be recalled in this connection that CPD has been persistently arguing for setting up a Financial Sector Commission with a view to addressing the emergent challenges.

Transparency in defense budget

The reporting mechanism concerning the defense spending in Bangladesh is highly non-transparent – it does not even provide aggregated budgetary figures as regards the allocations for defense spending (e.g. spending on arms and ammunition, soldiers' pay, etc.). Analysis of defense budget during FY2008-09 to FY2014-15 reveals that revised budget has always been higher than the budgetary allocations for the respective year (Table 2.11). Except for two fiscal years, the actual spending is also higher than the revised budget. Thus, for the last six fiscal years (FY2008-09 to FY2014-15), actual spending on defense is found to be significantly larger than the budgetary allocation of the respective year. In FY2013-14, there has been a significant increase in the actual spending as compared to the budgetary allocation, by about Tk. 4,000 crore. In the same fiscal year, the share of defense spending in total government expenditure increased from 7.1 per cent of budgetary allocation to 10.3 per cent in real terms. Rise in expenditure is mainly attributed to significant jump in non-development expenditure which outweighed the reduced development expenditure in each successive years. This pattern of defense spending indicates better capacity in utilising the budget by concerned bodies. However, questions about allocative efficiency remain a concern at a time social sectors are failing to meet the targets for lack of resources. Indeed, a number of sectors experienced same or almost similar trend in case of budget spending including public order and safety (same), recreation, culture and religious affairs (partly same) and agriculture, fisheries and livestock (partly same). In this backdrop, more transparency in the defense budget will be helpful in bringing more transparency in overall budgetary transparency and predictability. Apart from this, a number corporate activities are in operation mainly through the Army Welfare Trust and the Sena Kalyan Sangstha with a view to support the families of the armed forces. The legal entity of these corporations and other related activities need to be better clarified, and in case these entities are legally linked with the Armed forces, their financial accounts should be presented transparently in the national budgetary process. All these will help bring transparency and accountability in overall budgetary process in Bangladesh and will hopefully lead to better allocation and allocative efficiency of resources.

Table 2.11
Trends in Defense Spending in Bangladesh

(Crore Tk.)

Year	Allocation/Disbursement			Difference		
	Budget	Revised Budget	Actual	Revised-Original	Actual-Revised	Actual-Original
FY09	6,644.9	6,885.5	6,251.5	+240.6	-634.0	-393.4
FY10	7,051.4	7,875.1	8,471.6	+823.7	+596.5	+1,420.2
FY11	9,175.6	9,319.5	10,222.4	+143.9	+902.9	+1,046.8
FY12	11,246.8	12,212.7	12,218.4	+965.9	+5.7	+971.6
FY13	12,886.1	13,502.6	12,988.4	+616.5	-514.2	+102.3
FY14	14,457.1	15,180.0	18,330.8	+722.9	+3,150.8	+3,873.7
FY15	16,462.1	17,770.1	17,484.6	+1,308.0	-285.5	+1,022.5

Source: Author's calculation based on the Ministry of Finance (MoF) data.

Transparency in local government financing

Absence of detailed information as regards financing of the local government institutions (LGIs), lack of consistent pattern in central government transfers to the local government (LG), and the non-transparent way as to how resources should be allocated among the different LG departments are some of the key challenges that were identified in research works related to LG finance. In addition to poor financial management and the fiscal stress, LGs have also been criticised for weak accountability mechanism and lack of transparency (Bhattacharya *et al.*, 2013). To deal with the above mentioned challenges, three recommendations have been proposed: a) a separate LG budget to reflect the local needs and demands. For instance, India prepares separate budget for the railway; b) proper clarification as regards the fate of the much-hyped district budgets is needed as it appears to have been dropped. Introduction of the district budget was a good move and is important to address regional disparity in resource allocation and strengthen empowerment of district administration; and c) establishment of a permanent Local Government Finance Commission (LGFC) to ensure proper devolution of power, appropriate financing for LG and to make these self-sufficient.[46] Such a commission may be constituted as an autonomous body. The commission may be mandated to advise the government as regards budgetary allocation of LGs, central government transfer/ special grants to the LGIs, potential sources of revenue, appropriate tax levels to be levied by LG, resolution of disputes between LGs over financial matters and tenders, overseeing of auditing, financial management and accountability and monitoring of overall performance, citizens' participation, implementation of the Local Economic Development[47] and financing aspects for SDG implementation at the local level.

Transparency of NGO financing

The NGO sector in Bangladesh deals with significant resources. These resources are deployed in a host of activities which have developmental consequences for the country. However, these activities and the involved resources are not properly reflected in the national budget. A major share of the finances to the NGO sector is allocated from foreign aid. Since FY2008-09, proportion of aid disbursed through the non-government sector has increased significantly. The latest figures show a fall in allocation in absolute figure but a rise in share. For instance, the proportion of total official assistance going to non-government sector rose from 20.1 per cent in FY2014-15 to 26.2 per cent in FY2015-16 (July-March) (see Annex Table 2.4). On the other hand, project-level finance released through the NGOs as a proportion of GDP as well as the fiscal budget has been declining since FY2012-13. The contribution of NGOs activities in some sectors (in terms of non-government aid allocation vis-à-vis total public expenditure) is quite significant – these include labour and employment, health and nutrition and agriculture (Table 2.12). Previous budget analyses carried out by the CPD had pointed out lower budgetary allocation for women and child affairs, primary and mass education and health and family welfare, from FY2011-12 to FY2015-16. Despite this, significant achievement in a number of social sectors such as reducing under-five mortality and infant mortality, improving enrollment in primary education and reducing the proportion of population living below the national upper poverty line, etc. have indeed been possible, thanks to significant contribution made by the NGOs in respective areas (GED, 2015c). It is reckoned that, reflecting NGO allocation and activities in the budget will provide a more comprehensive picture as to the overall development plan of the country. MoF, with the support of NGO Affairs Bureau, could develop a suitable format for reporting NGOs' activities in the national budget.

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[46]This type of LGFC is found in Uganda (operational since February 1995), and recently an independent Commission on Local Government Finance has also been established in England in 2014 to examine the system of funding of the LG in England.
[47]Bangladesh is a signatory of the document promoted by the Commonwealth Local Government Forum (CLGF).

Table 2.12

Financing Contribution of NGOs in Different Sectors (Aid Allocation as % of Total Allocation)

Sector	FY11	FY12	FY13	FY14	FY15	FY16
Agriculture	0.66	1.59	1.10	4.81	8.36	1.39
Health, Nutrition, Population and Family Welfare	0.31	1.33	2.81	8.64	4.56	3.62
Industries	0.00	0.00	7.63	5.21	3.17	-
Labour and Employment	1.75	3.05	26.64	27.38	12.71	-
Power, oil, gas	0.00	0.00	0.00	0.02	0.05	0.07
Public Administration	0.11	0.12	0.12	2.56	0.33	0.22
Rural Development and Rural Institutions	0.05	0.72	0.92	5.70	2.02	0.96
Transport	0.00	0.00	0.00	0.00	0.03	0.00

Source: Based on the Economic Relations Division (ERD) data.
Note: '-' denotes data not available.

Transparency in South-South transactions: Case of Indian LoC

The importance of South-South Cooperation as a complementary source of finance is getting increasing recognition, and also gaining growing importance in many developing countries. This is more so in the backdrop of declining net official development assistance (ODA) from the 'traditional' providers of the North (Development Initiatives, 2014). In recent times, Bangladesh has signed two Memorandums of Understanding (MoUs), for two bilateral dollar credit lines with India, one in 2010 and the other in 2015.

As is known, South-South development finance often faces the challenge of lack of a guiding framework within which these transfers take place. Development organisations from the North, such as Japan International Cooperation Agency (JICA), Korean International Cooperation Agency (KOICA), World Bank and Asian Development Bank (ADB), generally operate within their clearly defined institutional and operational rules. In case of Southern financing projects such guiding principles and rules are often absent. Bilateral finance, like the one from India, is at first negotiated by the ERD under the MoF; however, implementation and project-wise allocation is made directly with the concerned ministries under which the selected projects are to be implemented. The finance, in this case, is transferred from one ministry to another without any central authority supervising it. Consequently no clearly defined central reporting takes place and the transactions are made on an ad hoc basis. For example, JICA and KOICA directly deal with the ERD to provide funds centrally. On the other hand, Indian Export-Import (EXIM) Bank will provide funds from the USD 1 billion LoC directly to the project ministries or the contractors according to the allocation decided from the development project proposal (DPP) and technical project proposal (TPP). In this context, there is a concern as regards consistency and quality assurance of the projects undertaken with the funds as there is no binding rules and regulations guiding the financial flows. Also, it is very difficult to carry out economic analysis because feasibility studies, which include analysis of the environmental impact of these projects, and also the monitoring reports, are not shared with the concerned policymakers and stakeholders. This also impedes the ability to make suggestions vis-à-vis the economic and social implications of projects under bilateral South-South credit as opposed to those under North-South finance.

In this backdrop it is suggested that the DPP and TPP of the projects financed by the LoC be made available to the policymakers and other stakeholders to enable adequate analysis of the economic impact of the LoC deals. Also the quarterly monitoring and evaluation reports should be prepared. These will help monitor implementation status of the projects, calculate the rate of return on investment, and assess the socio-economic impacts of the project. In order to maintain such reporting and information, there is a need to set up a central reporting system. Clearly defined operational rules and regulations should be formulated. These will also help address the issues of 'tied aid' and 'untying of aid' which have been a concern in the context of Indian LoC, particularly as regards local procurement to be made from the credit. These steps will enhance transparency and accountability in projects under South-South cooperation.

Economic reforms

Economic reforms in the present analysis highlights a number of areas. These include:

- Enforcement of Public Service Act 2015;
- Commission for financial sector reforms;
- Setting up of other commissions;
- Enforcement of Financial Reporting Act;
- Enactment of new/amended laws, rules and acts;
- Operational reforms; and
- Organisational reforms.

Enforcement of Public Service Act 2015

The Public Service Act has been under consideration for quite some time now. Enforcement of the Public Service Act will hopefully improve management and operation of public offices as it puts talks of undertaking a number of special focus on administrative reforms. The Act recommends separate rules for examination for promotion, performance appraisal, career training and skill development, privileges, incentives and preservation of quota for disabled persons and backward communities. It is felt that, there should be clear guidelines in a number of areas including establishment of proper mechanism for performance appraisal (designing evidence-based rules for performance appraisal) and digitalisation of public service provisions (providing good practice-based rules on digitalisation of public service provisions). There should be proposals for reorganisation and rationalisation of public offices, reorganisation of cadre services and reconstitution of Senior Service Pool, etc. It is hoped that the national parliament will carry out an in-depth review of the Public Service Act, and the Act will be verified soon.

Commission for financial sector reforms

In the recent past, a number of financial scams, particularly concerning the NCBs, have exposed major weaknesses in the banking sector. These include poor decision-making and supervisory capacity, weak risk management system, and also failure of the central bank to carry out due diligence and undertake its supervisory tasks (CPD, 2012). Rising non-performing loan (NPL), quality of outstanding loans and declining profitability are also concerns. Some of the non-NCBs are also not immune to such maladies. The way licenses for new banks are issued have also given rise to questions. The overall health of the financial sector has emerged as an area of increasing disquiet.

The recent heist of USD 101 million from the central bank from its foreign currency reserve account in US Federal Reserve through cyber-hacking, is one of the most crucial events that are of concern to the governance in the banking sector. ATM fraud has added a new dimension to financial sector governance in Bangladesh. Preceding this it was the stealing of money by cloning ATM cards from private local banks. According to a Bangladesh Institute of Bank Management (BIBM) study, average spending by Bangladesh Bank's commercial banks for cyber security is significantly lower when compared to the needed level.

In this backdrop, the CPD has proposed setting up an Independent Financial Sector Reform Commission which will undertake an in-depth review and assessment of the health and performance of the financial sector of Bangladesh. The Commission will assess the needs of customers and the economy, identify the weaknesses, review governance structure, security system, incentives and risk management system; it will provide guidelines to deal with NPL and recapitalisation of banks, rescheduling of bad debt. The non-bank financial institutions (NBFIs) could also be included within the remit of Commission's scrutiny, including insurance companies and capital market. The Commission will prepare guidelines and make recommendations as regards reforms needed, automation, risk-management, real-time scrutiny, checks and balances, in-built good governance mechanisms, internal control, role of various players in banks and other financial institutions. In view of the recent heist, the Commission may also be entasked with the responsibility of coming up with recommendations to improve cyber security, good governance, efficiency and operations of the central bank.

Setting up other commissions

A number of independent commissions need to be set up in order to ensure better transparency in economic governance. These could include an independent statistical commission to validate the macroeconomic correlates and an independent public expenditure review commission.

Enforcement of Financial Reporting Act

Financial Reporting Act could be a major vehicle towards ensuring greater transparency in financial reportings made by commercial/business entities in the country. As it stands, after the Act was passed by the Parliament no visible progress has been made as regards the follow-up activities that were needed. Steps should be taken, with proper timelines, for setting up the envisaged Financial Reporting Council. Besides, it is important to fix the financial reporting and auditing standards in order to implement the Act properly.

Enactment of new/amended laws, rules and acts

A number of investment, commerce and business-related policies need to be amended and updated in order to make them functional, modern and effective in the current and future contexts. These include Customs Act 1969, Foreign Private Investment (Promotion and Protection) Act 1980, Companies Act 1994, Trade Mark Act 1940, Mine Act, 1923, Port Act, 1908, Export and Import Control Act 1950, Patent and Design Act, 1921, Inland Shipping Act, 1976, Weight and Measurement Act, 1961, and Acquisition and Requisition of Immovable Properties Act, 1982. Besides a number of new laws/acts are required in order to make businesses more functional and efficient; some of these are Business Organization Act, Anti-Dumping and Countervailing Act, etc.

A number of rules and regulations related to various laws and acts need to be upgraded/amended/added. These include rules for Investment Act, Port rules, Patent and Design rules, Pre-shipment Inspection Order 2000 and Import, Export and Indentors' Registration Order 1979. A number of new policies need to be adopted in order to facilitate private investment in manufacturing and related service sectors; these include Coal Policy and Shipping Policy.

Operational reforms

Entrepreneurs often suffer from lack of clarity concerning the various rules and regulations. New investors, particularly the SME entrepreneurs, are not aware of the different procedural requirements in order to carry on their respective businesses. Given the differences in the business processes, authorised public domains should be put in place where necessary documents and related formalities, procedures and processes would be available on the website. Lack of clarity as regards business processes also discourages foreign investors. Anecdotal information indicates that foreign investors get better guidance from publicly available documents in India regarding investment opportunity, modalities for registration and process of approval from different public entities despite the fact that investment regime in India is more stringent compared to that in Bangladesh. Clearly spelt out public documents as regards business processes should be made easily available (preferably on dedicated website) so that investors have a sound understanding about the entire range of business processes.

There is a large gap between adopted policies/rules/regulations and their implementation at the business level. For example, a number of incentives and support measures have been announced under the Industrial Policy 2012, Export Policy 2015 and SME Policy Framework 2005, for different categories of sectors/industries that include 'booster sectors', 'thrust sectors' and 'high-priority' sectors, etc. However, procedures, eligibility and documentation to avail of those incentives have not been spelt out in a clear and transparent manner. Neither are these readily available. Since these incentives are mentioned in the policies but not in acts/laws, there is no binding requirement either to provide these services to the entrepreneurs. Unless these incentives are included in the finance bill, there is no guarantee that investors will actually get those benefits. Also, there should be greater coherence as regards policies and measures put in place by different ministries and departments. Besides, proper implementation of different rules/regulations/ policies should receive due priority from the relevant public institutions.[48]

Foreign investors often face problems both at pre- and post-establishment phases of investment. Although, in a formal sense foreign investors are welcome to invest in Bangladesh in any sector without limit (except for the few 'reserved' sectors), functionally they are confronted with a variety of 'hidden' barriers. Cases of non-cooperation from various related agencies and institutions are not unknown. This contradicts with the stated policies pursued by, and Acts enacted in, Bangladesh. Foreign investors often do not have access to industry-related information such as market size, major market players and their market shares, major risks, sources of raw materials, and information on major suppliers in the supply chain, market access conditions, etc. Easier access to, and availability of, all related information concerning the different sectors are needed to enhance the ease of doing business in Bangladesh.

Organisational reforms

Organisational reforms are urgent to raise efficacy of public institutions, particularly in view of the changing nature of demands for public services in a fast-changing world. For example, a number of organisations under various Ministries act as facilitators for private investment; these include Bangladesh Investment Development Authority (BIDA) (previously the Board of Investment (BoI)), Bangladesh Export Processing Zone Authority (BEPZA), Bangladesh Small and Cottage Industries Corporation (BSCIC), Bangladesh Economic Zone Authority (BEZA) and different local authorities. Given that the nature of work is similar, there is a need for clear division of focus and labour of these institutions; at the same time there is a need for greater coordination among those.

The Ministry of Industry needs to revisit and then refocus its overall objectives and activities. Despite the fact that the Ministry is supposed to play a key role in the context of Bangladesh's industrialisation, till date its role has only been a limited one. The Ministry should be developed as the focal point for pursuing the cause of industrialisation in Bangladesh and its activities ought to cover all types of industries (both domestic market-oriented and export-oriented). It should act as a repository of industry-related information, providing technical support and ensuring business facilitation. Strengthening of the associate institutes including National Productivity Organization (NPO), Patent, Design and Trade Mark Division, Bangladesh Institute of Management (BIM) and Bangladesh Standards and Testing Institution (BSTI) is also of critical importance if the Ministry is to play its desired role.

[48]Anecdotal information indicates that individual entrepreneurs tend to encounter difficulties at the micro-level when their business cases are dealt by designated desk officers.

Government should conduct a serious rethink about the future of the loss-making SoEs. As is known, these are managed under the Ministry of Industry and Ministry of Jute and Textiles. There is scope for further rationalisation of the operation of some of the SoEs. Independent studies should be carried out to examine the various options in this regard. Government should also design an appropriate policy to lease out land of the SoEs to the private sector for establishment of new enterprises. At present, this is often being done on an ad hoc basis, in a non-transparent manner.

There is a need for more interaction between the public and the private sector; at present this is done only on a limited scale. A Private Sector Development Policy Coordination Committee was constituted in 2013 under the office of the Prime Minister; however, scope of work of this Committee appears to be limited. In order to better facilitate the workings of the private sector, it is important to set up a commission to identify institutional bottlenecks both at macro and micro levels. The commission will come up with concrete suggestions for respective ministries and departments to undertake necessary measures in a time-bound manner. These recommendations could include both laws and regulations as also operational tools and modalities, documentation and procedures. For a continuing interface and interaction between private sector and policymakers, institutional arrangement such as the Better Business Forum set up by the Caretaker Government (CTG) in 2007 can also be considered.

2.4 CONCLUDING REMARKS

The budget framework for FY2016-17 has to be more robust in comparison to that of the earlier years, particularly by setting the targets based on more realistic revised budget figures of the elapsing year. Further, for making the budget more realistic, one has to either forgo the ambition of attaining high revenue collection and public expenditure targets, or give due attention to the task of enhancing administrative capacity and undertake implementation of the reform agendas for realisiing moderately ambitious targets.

While a country such as Bangladesh needs more public expenditure (as percentage of GDP), it is only to be expected that the country will make stronger efforts not only in financial resource mobilisation, but also in appropriate utilisation of the mobilised resources from both domestic and external sources. Reclaiming the momentum of domestic revenue collection – particularly under the income tax head – will be critical in this respect. Operationalisation of the new VAT Act would need a number of preparatory measures including those in the area of capacity development on the part of concerned institutions as well as the business. As regards external financing, enhanced utilisation of foreign aid in the pipeline would make the critical difference in ADP implementation. It goes without saying that tax evasion and leakages through illicit financial outflow have to also get priority in the ensuing budget. Taking advantage of the expended fiscal space triggered by reduction in subsidy demands, self-financed allocation may be increased in human development sectors as well as towards promoting social protection schemes. Indeed, such an expansionary move is supposed to alleviate domestic demand depression. It is quite disappointing that the government has secularly failed to make good use of the available fiscal space which has by default resulted in a below programme budget deficit.

Efforts to mobilise more financial resources to service the expenditure targets have to be underpinned by measures geared towards institutional reforms. These measures should include, among others, expansion of the tax base, introduction of a Benami Property Bill, changes in tax procedures for exporters, greater use of ICT-based tax compliance, operationalisation of Transfer Pricing Cell, and expanded use of ADR.

There should be a proper institutional set-up to assess the impact and implications of the various fiscal measures in terms of ERP, foregone tax revenues, benefits expected and justification for the duration for which such incentives were to be offered in the national budgets.

Possibility of mobilisation of more domestic revenue in FY2016-17 will be closely related to the possibility of the capacity to improve both the quantity and quality of public expenditure. In this connection, strengthening of the monitoring and evaluation (M&E) system of the IMED will be of defining importance. Indeed, one has to make a decisive move from financial disbursement-based project assessment method to results-based assessment. This new approach needs to be introduced in tandem with putting in place a prioritised monitoring mechanism for the foreign aid projects which will also be crucial for improving the performance of the ADP.

A separate but integrated budget for LGIs may also provide a strong impetus towards improving the opportunities for higher domestic resource mobilisation as well as the possibility of improved demand-driven public investments. Evidently, one is still awaiting to know why the district budget initiative was so unceremoniously discontinued in FY2015-16. It is strongly reckoned that establishment of a permanent Local Government (Finance) Commission may effectively contribute towards devolution of power and introduction of appropriate financing modalities, and help to ensure that public expenditure has greater impact at grassroots levels.

It will not be an overstatement to observe that the banking sector and the financial market are currently least prepared to provide the necessary support towards implementation of the contemplated budgetary measures as well as to boost private investment. Indeed, it is high time that we set up a high-powered Financial Reforms Committee (Commission) to provide an objective and in-depth assessment of the current health of the banking sector as well as non-banking financial markets and recommend measures to address the attendant problems and for enhancing performance of financial institutions. It will also be important to fix financial reporting and auditing standards in order to properly implement the Financial Reporting Act.

In the same vein, it has become imperative to finalise and put in action the much overdue Public Service Act. Similarly, in the backdrop of ongoing debate as regards GDP growth figures, the rational for setting up an independent National Statistics Review Committee has become all the more stronger.

It should be emphasised that substantive success of the national budget for FY2016-17 will be defined not so much through its allocative gestures, but through reform measures it will recommend (and implement) in different areas of budgetary process. One such set of reform measures will entail bringing more transparency to this process. Such measures should include the followings:

- Presentation of detailed financial accounts of the SoEs including their assets and liabilities, contingent debts and dues, and accounting practices;
- Full disclosure of the details of projects financed from external sources through foreign LoCs of different non-concessional loans;
- More sunshine on defense economy covering budgetary and off-budget allocations and spending as well utilisation of income from quasi-commercial sources;
- Linkages of NGO finances with government spending in different sectors as per the approvals provided by the NGO Affairs Bureau.

Finally, it may be pointed out that notwithstanding the immediate benefits gained from the fall in fuel price, the evolving global economic environment may not remain supportive for Bangladesh economy which is being increasingly integrated with the international supply chains. Thus, the upcoming budget should have some built-in safeguards in its implementation strategy which may be triggered in case of adverse impact emanating from the global economy.

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ANNEXES

Annex Table 2.1
Recent Changes in Export Incentives

Export Item	Old Rate (%)	New/Revised Rate (%)[a]	Previous Circular Date	New Circular Date
Revisions in cash incentives				
Leather goods	12.50	15.00	13 July 2015	4 April 2016
Jute goods	10.00	10.00	13 July 2015	7 April 2016
Textile	4.00	6.00	13 July 2015	4 April 2016
Shrimp[b]	3.79	4.98	3 June 2003	4 April 2016
Other fishes[b]	1.10	1.97	12 December 2002	4 April 2016
New cash subsidies				
Furniture		15.00		11 April 2016
Plastic products		10.00		11 April 2016
Potato starch		20.00		4 April 2016

Source: Compiled from Bangladesh Bank Circulars.
Note: [a]All new and revised rates are retrospectively effective from 1 July 2015.
[b]Ceiling for maximum free-on-board (f.o.b) value in USD per lb.

Annex Table 2.2
Projects that are not 100% Physically Completed but Declared as Completed

Year	No. of Completed Projects	No. of Projects with 100% Physical Progress	No. of Projects that are Not 100% Physically Completed but Declared as Completed	% of Total Completed Projects
FY2001	162	96	66	40.7
FY2002	162	87	75	46.3
FY2003	169	73	96	56.8
FY2004	232	25	207	89.2
FY2005	164	38	126	76.8
FY2006	225	93	132	58.7
FY2007	181	65	116	64.1
FY2008	239	112	127	53.1
FY2009	173	50	123	71.1
FY2010	195	42	153	78.5
FY2011	257	55	202	78.6
FY2012	199	44	155	77.9
FY2013	206	57	149	72.3
FY2014	233	52	181	77.7
FY2015	240	119	121	50.4

Source: Author's compilation from the Implementation Monitoring and Evaluation Division (IMED) data.

Annex Table 2.3

Status of PCR Submission and Impact Evaluation

Year	No. of Completed Projects	PCR Submitted	PCR Not Submitted	% of Total Completed Projects	Impact Evaluation
FY2012	Not available	Not available	Not available	Not available	10
FY2013	206	134	72	65.0	22
FY2014	233	141	92	60.5	14
FY2015	240	141	99	58.8	15

Source: Author's compilation from the Implementation Monitoring and Evaluation Division (IMED) data.

Annex Table 2.4

Share of ODA Disbursed through the Non-Government Sector

Component	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16
Total aid disbursement (Million USD)	38.77	108.05	149.16	238.70	629.38	4270.71	3580.76	1677.50
Total allocation to non-government sector (Million USD)	7.79	34.42	31.26	86.26	262.05	1142.06	719.69	439.65
As a % of total aid disbursement	20.09	31.86	20.96	36.14	41.64	26.74	20.10	26.21

Source: Aid Information Management System (AIMS), Economic Relations Division (ERD).

Independent Review of
IRBD
Bangladesh's Development

Under its Independent Review of Bangladesh's Development (IRBD) programme, the Centre for Policy Dialogue (CPD) has been preparing analyses of the major macroeconomic performance indicators of Bangladesh economy, on an ongoing basis, for two decades now. Following is a list of publications that have been brought out by the CPD under the CPD-IRBD programme:

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- State of the Bangladesh Economy in FY2013-14 and Outlook for FY2014-15
- Bangladesh Economy in FY2013-14: Third Interim Review of Macroeconomic Performance
- State of the Bangladesh Economy in FY2012-13 and Outlook for FY2013-14
- Bangladesh Economy in FY2012-13: Second Interim Review of Macroeconomic Performance
- State of the Bangladesh Economy in FY2011-12 and Outlook for FY2012-13
- Bangladesh Economy in FY2011-12: Third Interim Review of Macroeconomic Performance
- State of the Bangladesh Economy in FY2010-11 and Outlook for FY2011-12
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