Independent Review of Bangladesh's Development

বাংলাদেশের উন্নয়নের স্বাধীন পর্যালোচনা

State of the Bangladesh Economy in FY2017-18

Second Reading

CPD's Budget Recommendations for FY2018-19

Dhaka: 17 April 2018

CENTRE FOR POLICY DIALOGUE

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Contents

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- *The CPD IRBD 2018 Team alone remains responsible for the analyses, interpretations and conclusions presented in this report.*

Section I: Introduction

1. Introduction

- National budget for FY19 is being prepared in the backdrop of the global economy transmitting mixed signals and the domestic economy experiencing emerging tensions with accentuated traditional ones
- The upcoming budget will need to address these attendant concerns through renewed efforts at raising the quality of budgetary and fiscal planning at a time of election-related uncertainties
- Consequently, a key objective of the forthcoming budget should be maintaining macroeconomic stability

Section II: The Macroeconomic Scenario

2. The Macroeconomic Scenario

Economic growth is projected by BBS to cross the 7.5% mark despite only marginal improvement in private investment

- Provisional GDP growth estimate (7.65%) was found to be higher than expectations
- Manufacturing production and construction contributed to the higher industries sector growth rate
- If the growth rates of FY2017 (7.28%) and FY2018 (7.65%) are compared, of the additional growth of 0.37 percentage points, 0.54 percentage points is expected to be contributed by the manufacturing sector
- Manufacturing industries, i.e., leather and related products (76.6%), pharmaceuticals and medicinal chemical (44.7%), textile (33%) and food products (29.3%) registered very high growth rates according to QIIP without a commensurate reflection in the export performance

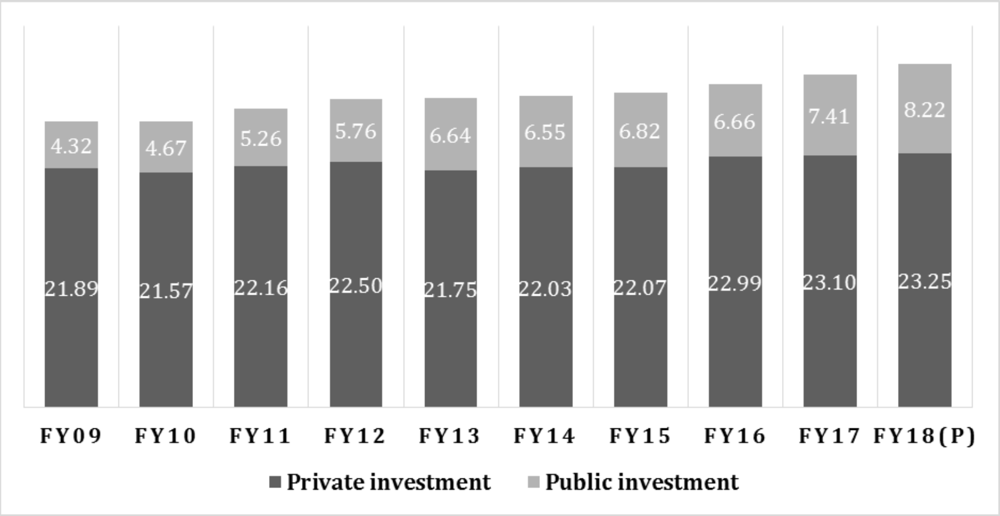
Contribution to GDP Growth Rate (%)

Sectors	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18(p)
Agriculture	0.61	1.07	0.78	0.52	0.41	0.70	0.53	0.43	0.44	0.43
Industries	1.71	1.77	2.31	2.47	2.59	2.27	2.74	3.24	3.10	3.73
Manufacturing	*1.07*	*1.08*	*1.64*	*1.69*	*1.80*	*1.60*	*1.93*	*2.26*	*2.21*	*2.75*
Construction	*0.41*	*0.45*	*0.44*	*0.54*	*0.52*	*0.53*	*0.58*	*0.59*	*0.61*	*0.71*
Services	2.66	2.89	3.25	3.43	2.88	2.92	3.00	3.21	3.41	3.21
Tax less subsidy	0.06	-0.17	0.12	0.10	0.13	0.16	0.28	0.24	0.34	0.28
GDP	**5.05**	**5.57**	**6.46**	**6.52**	**6.01**	**6.06**	**6.55**	**7.11**	**7.28**	**7.65**

Independent Review of Bangladesh's Development

- Investment as % of GDP is expected to increase by about 1 percentage points to 31.5 per cent in FY18
- The rise in public investment has considered almost 90% utilisation of the original allocations of the ADP for FY18
- Private investment is estimated to increase only marginally (by about 0.2 percentage point) to 23.3% in FY18
- Import of capital machineries recorded a 34% growth during July-February period of FY18.
  - It may be assumed that majority of these capital machineries was imported for public sector investment which has been estimated to rise by 25.6% in FY18

Investment as % of GDP



As has been observed in previous years, the year-end public expenditure is likely to be much lower than the planned figures, not to also speak about the discrepancy between figures of MoF and IMED!

Employment generation increased in FY2017 but real income had declined

- According to the latest round of the LFS, about 1.3 million additional jobs were created between 2015-16 and 2016-17
  - Net employment was almost entirely generated in the services sector (1.7 million) while only 262 thousand in industries sector
  - Net employment in agricultural sector declined by about (-) 0.7 million

Employment by broad economic sectors

Year	2010	2013	2015-16	2016-17
Sectors	Employed by broad economic sector (million)			
Total	54.1	58.1	59.5	60.8
Agriculture	25.7	26.2	25.4	24.7
Industries	9.6	12.1	12.2	12.4
Services	19.1	19.8	22.0	23.7
Sectors	Composition by broad economic sector (%)			
Total	100	100	100	100
Agriculture	47.6	45.1	42.7	40.6
Industries	17.7	23.0	20.5	20.4
Services	25.5	32.0	36.9	39.0

2. The Macroeconomic Scenario

- Within the services sector, majority of the additional jobs created in—
  - Wholesale and retail trade, except of motor vehicles (0.7 million)
  - Land transport and transport via pipeline (0.6 million)
  - Food and beverage service activities (0.1 million) and
  - Activities of households as employers (0.1 million)
- The accelerated rise in industrial value addition (in GDP) was not reflected in the employment outcome
  - Majority of the additional net jobs in the industrial sector were created in manufacturing of wearing apparel (178 thousand) and in construction of buildings (182 thousand)
  - Many important manufacturing industries, including textile and food products, continued to experience loss in terms of net jobs
- Disparities also exist among regions in terms of employment generation
  - Numbers of employment increased only in three divisions viz. Dhaka (972 thousand), Chattogram (612 thousand) and Rangpur (238 thousand)
  - In the other four divisions combined employment numbers declined by about 524 thousand

2. The Macroeconomic Scenario

- Unemployment rate has remained constant at 4.2% due to the balance of increased labour supply and increased demand
  - Definition of employment is rather loose – a person working for only one hour in a week may be considered as employed
  - However, the concept of decent work in the SDG framework goes far beyond this definition
- Unemployment rate among the relatively more educated labour force, particularly with secondary and tertiary education, had risen

Unemployment rate by education level (% of respective labour force)

Education Level	2010	2013	2015-16	2016-17
No education	2.8	3.2	2.2	1.5
Primary	3.8	2.7	2.5	2.7
Secondary	6.6	4.4	4.5	4.6
Higher secondary	13.7	7.9	13.8	14.9
Tertiary	8.3	6.7	9.0	11.2
Others				4.6
Total	4.5	4.3	4.2	4.2

2. The Macroeconomic Scenario

- ❑ Unemployment rate among the youth increased from 8.7% in FY16 to 10.6% in FY17
  - ➢ More than one-third of the total youth labour force with tertiary education (34.3%) remained unemployed in FY17

Unemployment rate by education level (% of total youth labour force)

Education Level	2010	2013	2015-16	2016-17
No education – total	15.7	12.8	6.7	4.8
No education – male	13.4	5.1	6.1	2.3
No education – female	18.8	7.7	7.4	10.0
Primary – total	21.4	17.2	8.7	5.3
Primary – male	22.2	9.0	6.4	3.7
Primary – female	20.3	8.2	13.4	9.3
Secondary – total	49.0	34.7	10.7	8.7
Secondary – male	51.4	20.2	7.8	6.7
Secondary – female	47.4	14.5	17.6	11.7
Higher secondary – total	10.4	25.6	6.0	27.0
Higher secondary – male	10.3	12.4	6.1	22.7
Higher secondary – female	10.5	13.3	5.8	35.1
Tertiary – total	2.8	9.7	12.1	34.3
Tertiary – male	2.8	5.2	10.8	30.1
Tertiary – female	2.9	4.5	15.0	42.5
Total	7.4	8.1	8.7	10.6

CPD (2018): State of the Bangladesh Economy in FY2017-18 (Second Reading)

2. The Macroeconomic Scenario

- Despite the improved number of employment, average real monthly income had suffered erosion in FY17, by (-) 2.5%

Average real monthly income from employment (in Tk., adjusted with CPI)

Year	2013	2015-16	Change (%)	2016-17	Change (%)
			National		
Male	14,309	13,844	-3.2	13,583	-1.9
Female	13,712	12,732	-7.1	12,254	-3.8
Total	14,152	13,602	-3.9	13,258	-2.5
			Urban		
Male	17,930	16,957	-5.4	17,106	0.9
Female	15,558	13,847	-11.0	13,321	-3.8
Total	17,192	16,022	-6.8	15,912	-0.7
			Rural		
Male	12,512	12,211	-2.4	11,708	-4.1
Female	12,464	11,532	-7.5	11,206	-2.8
Total	12,500	12,098	-3.2	11,608	-4.0

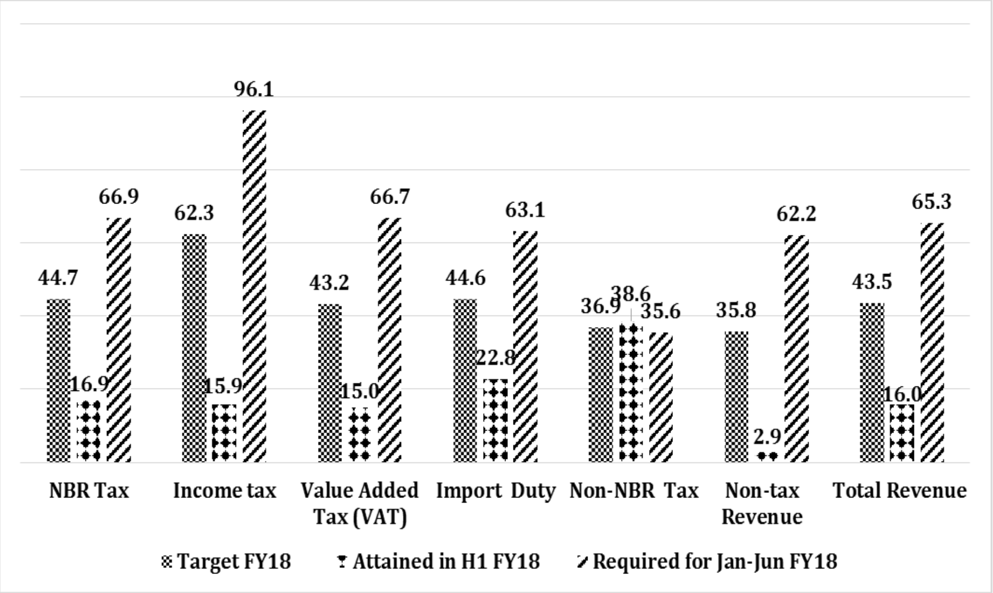
Refocus development objective from the existing 'GDP growth acceleration' centric strategy to a 'decent employment generating high economic growth' centric strategy!

2. The Macroeconomic Scenario

Revenue mobilisation is likely to fall short of target for the sixth consecutive year in FY2018

- ❑ Due to unrealistic programming of the fiscal framework targets, a large shortfall in revenue has become a certainty
  - ➢ Revenue collection growth during H1 of FY18 was 16%
  - ➢ Revenue would need to increase at a rate of 65.3% for the remainder of the fiscal year
- ❑ NBR is also likely to miss the target
- ❑ There are signs of greater reliance on import-related revenue sources

Revenue Collection Growth



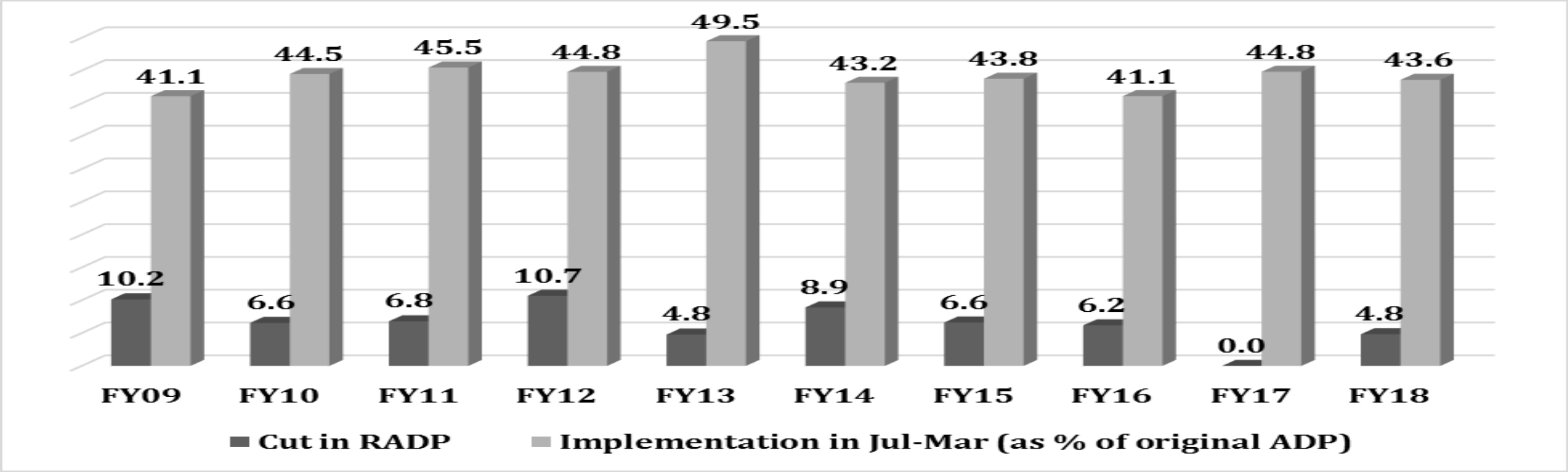
CPD's overall projection is that, revenue shortfall in the current fiscal year is likely to be about Tk. 50,000 crore

2. The Macroeconomic Scenario

ADP implementation remains business as usual despite high project aid utilization

- 43.6% of original ADP was spent during Jul-Mar of FY18
    - It was lower than the spending of FY17 (44.8) for the corresponding period
- Higher utilisation (48.2%) of foreign aid (highest since FY06) is a positive sign in the context of budget implementation trends in FY18, thanks almost solely to the Power Division

Revised ADP, the Cuts and ADP implementation scenario



2. The Macroeconomic Scenario

- Among the top 10 ministries/division having a share of 73.3% in total ADP allocation for FY18, only three (**Power Division - 79.9%, Local Govt. Division - 57.2%, Ministry of Science and Technology - 51.8%**) had been able to spend more than the average amount of allocation during July-March of FY18
- ADP was slashed by Tk. 7,550 crore (or 4.8%) to Tk. 148,381 crore from Tk. 155,931 crore
- Given the implementation status of ADP, a more substantive rationalisation of ADP allocation was perhaps called for

2. The Macroeconomic Scenario

High cost of borrowing for financing budget deficit continues

- The budget was in surplus of Tk. 201 crore during Jul-Dec of FY18
- The impact of large revenue shortfall was likely to be offset by the inability to spend budgetary allocations
- Sale of NSD certificates during Jul-Feb of FY18 was Tk. 33,120 crore – already 9.9% higher than the annual target (Tk. 30,150 crore)
- On a positive note, Net foreign borrowing and grant registered a growth of 442%, to Tk. 2,459 crore, during Jul-Dec of FY18

Inability to fully implement budgetary allocation will likely lead to further escalation of ADP project costs over the upcoming fiscal years!

2. The Macroeconomic Scenario

Inflation, driven by rising food inflation, is slowly creeping up

- Headline inflation reached 5.8% in March of FY18 (Target: 6.0%)
    - Food inflation, driven by higher rice price, is increasing
    - Non-food inflation is also rising since January 2018
- Rising global commodity prices, possibility of further depreciation of BDT, and relaxed monetary policy might increase inflationary pressure in the near future
    - The government needs to be vigilant to avoid any additional speculative pressure during Ramadan season

2. The Macroeconomic Scenario

Growth of broad money supply remained well below the target

- Public sector credit growth was negative (-) 14.2% as of Feb 2018 (Target 8.3%)
  - Thanks to limited bank borrowing by the govt for deficit financing
- Net foreign assets, posted a growth of 3.9% as of Feb 2018 (Target 0.1%)
  - However, with increasing BoP pressure, the central bank may need to release more forex from the reserve which in turn is likely to further restrain such growth
- As of Feb 2018, broad money recorded a 9.8% growth (Target 13.3%)
- Private sector credit growth was 18.5% as of Feb 2018 (Target 16.8%)

2. The Macroeconomic Scenario

Interest rates for both deposits and advances showed upward trend

- During Jul-Nov of FY18, interest rate for advances was showing a declining trend while the interest rate for deposits hovered around the 4.9% mark
  - However, both rates started to exhibit upward trend since December 2017
- The rise in deposit rate could be attributable to the government's recent move to reduce advance-deposit ratio (from 85.0% to 83.5%) and subsequent drives to collect more deposits by non-compliant banks
- Prevailing weaknesses in the banking sector including NPL and CAMELS indicators deter the banks from reducing the spread to any significant extent
  - As a result, lending rates had also risen in tandem

2. The Macroeconomic Scenario

Initiatives to boost liquidity supply contradicts government's earlier conservative monetary stance

- BB cut the cash-reserve ratio by 1 percentage point to 5.5% on bi-weekly average basis with a provision of at least 5.0% on daily basis, effective from 15 Apr, 2018
- Also, BB decreased its repo rate from 6.75% to 6.00% while keeping the Reverse Repo rate unchanged at 4.75%
- These initiatives result in increased money supply and contradicts reduction of ADR
    - The process which was followed in executing these changes must be questioned

RMG-led export earnings exhibit resilient growth but slowdown in non-RMG export growth is worrisome

- Total export earnings growth: 6.3% during Jul-Mar of FY18 (annual target 8.2%)
  - Driven by robust performance in RMG export: 9.1% growth up to Mar FY18 (Target 7.1%)
  - Export growth of both knit and woven surpassed their targets
- Non-RMG exports growth during Jul-Mar of FY18: (-) 5.5% (annual target 12.8%)
  - Mainly due to depressed export performances of leather and leather products, raw jute and engineering products
- Persistent poor performance of non-RMG exports in the non-traditional markets is a grave concern from the perspective of both product and market diversification
- Export growth in the US has been at a very low level in FY18 so far
  - Both RMG and non-RMG items exhibited subdued export growth
- Export growth in the EU: 11.7% during Jul-Mar of FY18. Both knit and woven fared well
  - Growth of non-RMG exports to the EU is displaying a gradually declining trend

Import payments driven by foodgrains and capital goods

- Import payments registered a 26.2% growth during Jul-Feb of FY18
  - Foodgrains and capital goods recorded 186.7% and 28.2% growth respectively
  - Within capital goods, capital machineries, and others grew by 42.3% and 20.7%
- Concerns remain regarding overstocking, trade misinvoicing, and capital flight following the import trends of certain commodities such as raw cotton, yarn, fabrics, edible oil, sugar, 'other import items' etc.

Upturn in outward migration is reflected partially in increased remittance inflow

- Outward migration experienced a 5.2% rise during Jul-Mar of FY18
  - Average monthly migration during this period was 76,915 - highest since FY12 for the considered timeframe
- Remittance inflow increased by 17.3% during Jul-Mar of FY18
  - This ought to be seen in the backdrop of the dismal scenario prevailing in FY17
- Average monthly remittance inflow during Jul-Feb of FY18 was USD 1,196 mln, which is USD 33 mln lower than average monthly inflow for the corresponding period of FY16

2. The Macroeconomic Scenario

Balance of payment (BoP) situation is not favourable

- Up to Feb of FY18, trade balance stood at negative USD (-) 11.7 bln, which was almost twice than that of the corresponding period of FY17
- Current account balance reached USD (-) 6.3 bln during Jul-Feb of FY18, which was about USD (-) 1.0 bln during the corresponding period of FY17
- Financial account balance rose to USD 5.7 bln
  - Net FDI inflows recorded an insignificant 0.8% growth but this was bolstered by a strong 86.3% growth in medium and long-term (MLT) loans
- Bangladesh's overall BoP stood close to negative USD (-) 1.0 bln as of Feb FY18
  - This was a surplus to the tune of USD 2.4 bln during the same period of FY17
- In the backdrop of growing imports, Bangladesh's overall balance for the entire fiscal year is likely to be in the negative terrain for the first time since FY11

BoP pressure is translated into depreciation of BDT against major currencies and slowdown in forex reserve accumulation

- Over the Jul-Mar timeframe of FY18, exchange rate of BDT against Indian Rupee has remained fairly stable. Apart from this, BDT has shown a generally depreciating trend against other major currencies such as USD, Euro, UK Pound Sterling and Chinese Yuan
- The import settlement rate, or BC selling rate, of USD was BDT 83.5 as of April 10, 2018, exhibiting a 3.2% increase from a year ago
- As a consequence of the overall deficit, foreign exchange reserves came down to about USD 33.0 bln as of April 11, 2018 from the earlier USD 33.5 bln as of June 30, 2017

Section III: From Excess Liquidity to Liquidity Crunch: The Curious Case of the Banking Sector

Independent Review of Bangladesh's Development

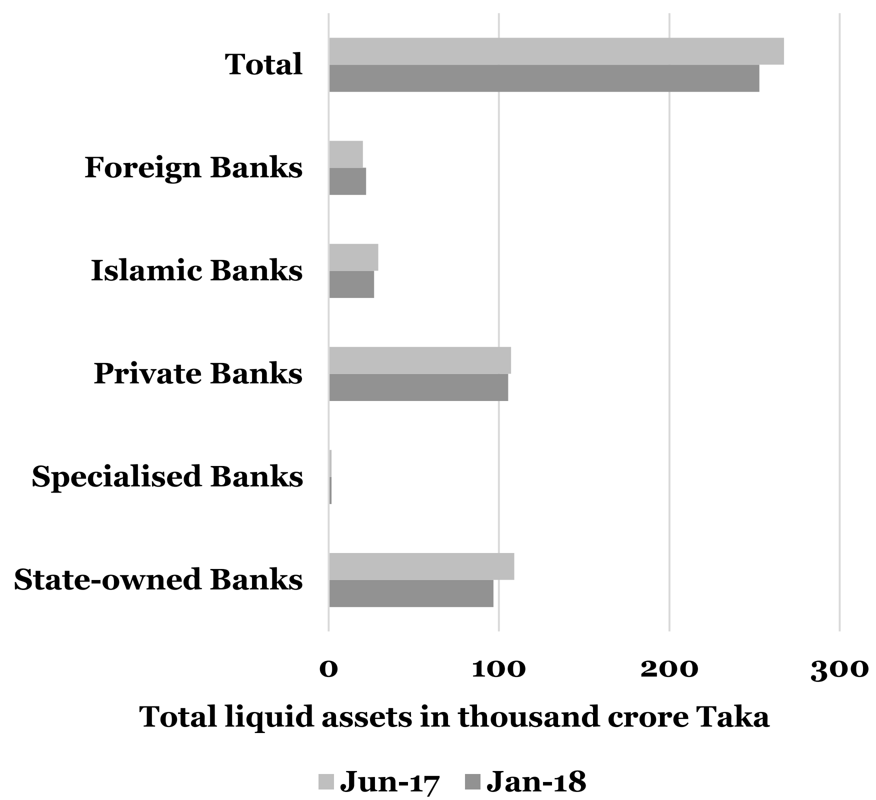
3. From excess liquidity to liquidity crunch: the curious case of the banking sector

- The banking sector of Bangladesh continues to be in a state of disarray as the fiscal year 2017-2018 draws to a close.
  - In 2017, state owned commercial banks and development finance institutions failed to meet the BASEL III requirement of maintaining capital to risk weighted asset ratio of 10%.
  - At the same time, state owned commercial banks and development finance institutions also had more than 20% non-performing loans (NPLs) in 2017.
  - Development finance institutions had an expenditure-income ratio greater than 100 for the third year in a row with consequent continuation of losses suffered.
  - Foreign commercial banks made the highest profit, but their interest rate spread was always above 6% in 2017.
  - The overall non-performing loan ratio in the banking sector also posted some rise, from 10.1% in June 2017 to 10.7% in September 2017.

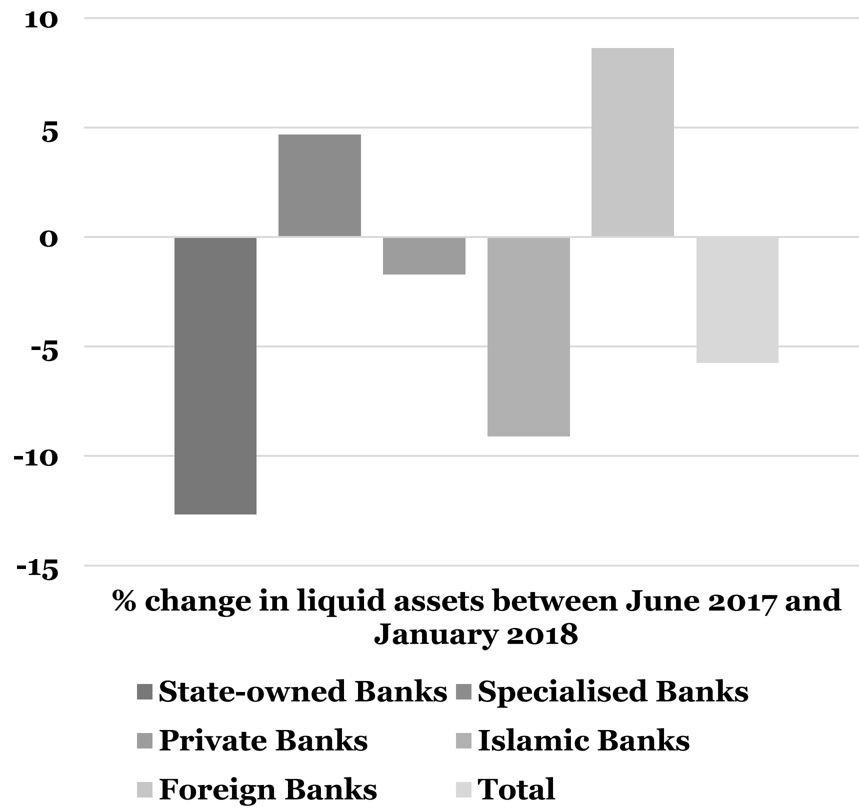
3. From excess liquidity to liquidity crunch: the curious case of the banking sector

- In the early months of 2017, a build-up of excess liquidity in the banking sector was creating concern regarding the condition of the general investment climate of the economy.
- However, liquidity position of majority of banks started to deteriorate thereon and by January 2018, there was widespread liquidity shortage in the banking sector.

Total Liquid Assets



Change in Liquid Assets



3. From excess liquidity to liquidity crunch: the curious case of the banking sector

- The central bank issued a circular on 3rd April 2018 that the minimum cash reserve requirement (CRR) would be reduced from 6.5% to 5.5% bi-weekly, and from 6% to 5% daily, starting from 15th April 2018.
- Additionally, it was decided that government agencies would increase their deposit of funds in private commercial banks from 25% to 50%.
  - These steps, taken irrespective of performance record of the private commercial banks was not justified under any pretext.
    - Indeed, this was likely to encourage poorly performing banks to continue with their business-as-usual practices.
  - The decision to reduce the CRR is contradictory to the contractionary monetary policy declared by Bangladesh Bank for January-June 2018.
  - The CRR change will likely affect the interest rates in the banking sector. The apprehension is that the deposit rate may fall faster and to a larger extent than the lending rates.
  - The reduction in the CRR may encourage banks to lend more aggressively, and indiscriminately. This will raise the risk of increase in NPLs.

3. From excess liquidity to liquidity crunch: the curious case of the banking sector

- The attempt on the part of the Ministry of Finance to rescue the private commercial banks through CRR reduction was in fact similar to government's recapitalization support for the state-owned commercial banks.
  - From FY2009 to FY2017, the government had allocated BDT 15,705 crore for the recapitalization of state owned banks.
  - This support, however, has not been translated into improvement in the performance of these banks; rather the amount of NPLs has piled up on a continuing basis over the past years.
- The recent decision to allow higher share of government funds in banks could result in the money going to poor performing ones.
  - For example, in December 2017, Farmers Bank failed to pay BDT 229 crore to Bangladesh Climate Change Trust Fund on maturity of its fixed term deposits.
  - There should have been certain conditionalities attached to this newly introduced enhanced threshold of receiving government fund.

3. From excess liquidity to liquidity crunch: the curious case of the banking sector

Recommendations for National Budget FY2018-19

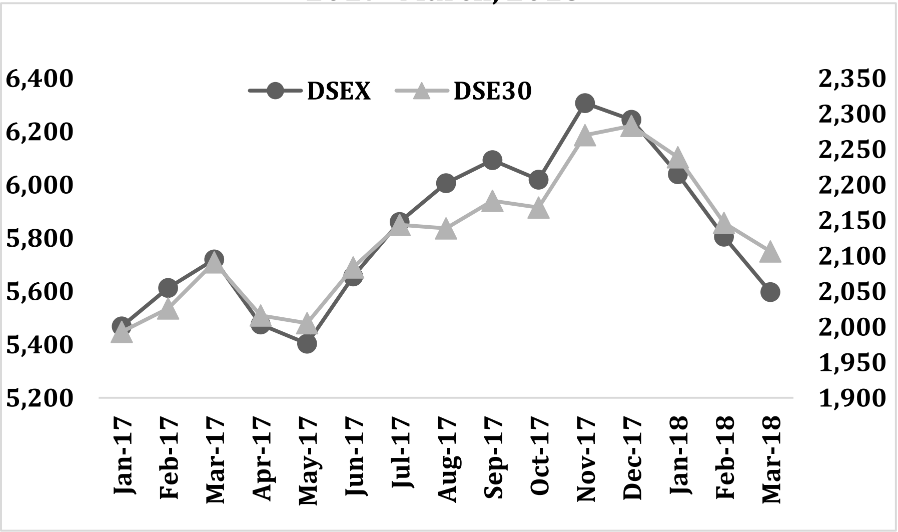
- Recapitalization of state owned commercial banks year after year should be stopped. The practice of bailing out the losing banks with public money is economically unjustified and morally incorrect.
  - There has to be a transparent exercise to find out what has actually been achieved through such funds, and when and how this type of recapitalization of banks will be brought to an end.
- Access to additional government funds as deposits should be contingent on performance of the particular private bank.
  - Only banks with less than 5% NPLs should be eligible for the additional available funds from government entities.
- The budget should allocate adequate funds for setting up an independent commission. The commission will critically assess the problems and weaknesses of the banking industry, and will suggest concrete recommendations for prudential banking.

Section IV: Bullish and Bearish Trends in the Capital Market: Role of Institutional Investors and Regulators

4. Bullish and Bearish Trends in the Capital Market: Role of Institutional Investors and Regulators

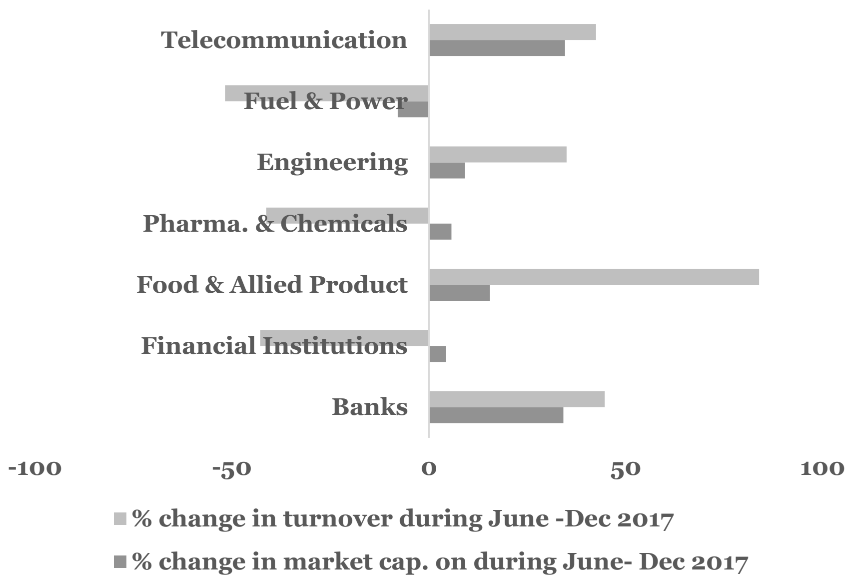
- ❑ Despite some hiccups, the capital market has maintained bullish trends in the course of calendar year 2017
  - ❑ Key indices of the DSE have registered a rise of 10-12% although total turnover declined by 70%
  - ❑ Major companies have experienced a significant rise in Jun-Dec,17
- ❑ Institutional investors, particularly by banks and NBFIs have contributed to this bullish trend

Trends of indices of DSEX and DSE30 during January, 2017- March, 2018



Source: DSE

Changes in Market Capitalisation and Turnover during June-December, 2017



4. Bullish and Bearish Trends in the Capital Market: Role of Institutional Investors and Regulators

- Permission for converting loans into paid up capital of bank subsidiaries, excess liquidity and credit growth beyond target level - had provided the opportunity to banks to make large investments in the stock market
  - 21 banks have allegedly invested beyond their exposure limit
  - Some of the banks misused the weekly reporting system
- The bullish trend had given way to a bearish outlook since Dec, 2017
  - Announcement of tightening money supply
  - Need to investigate how much of Banks' sales of shares was related to complying with new directives and whether some of the banks played due role to stabilise the market or not
- DSE has initiated the process of completing its demutualization process
  - Finalizing the proposal from the Consortium of Shanghai Stock Exchange and Shenzhen Stock Exchange
  - SEC advised to drop request to be member of different committees

4. Bullish and Bearish Trends in the Capital Market: Role of Institutional Investors and Regulators

- **Central Bank needs to increase its vigilance in monitoring activities of Banks in the Capital Market**
  - Quick responses in identifying market irregularities, and taking actions on an urgent basis
  - Need to investigate whether banks are playing their assigned role as institutional investors
- **SEC and Central Bank should collaborate to prepare a Code of Conduct for institutional investors**
  - This type of code is available in Malaysia and India
- **Regular review and monitoring of the activities of institutional partner of DSE will be required**
  - Rules and practices followed by DSE is likely to be different from those of the institutional partner
  - Review and monitoring of activities of the institutional partner would help streamline their activities and support smooth operation of DSE
  - Ensure timely implementation of various commitments made by the institutional partner
  - New technologies are required for setting up derivatives market, bond market, market maker and central clearing company etc.

Section V: Incentives for Export-Oriented Sectors: Recommendations for FY2019 Budget

5. Incentives for Export-Oriented Sectors: Recommendations for FY2019 Budget

Why revisiting the export incentives

- Exports will need to grow at about 17% annually over the next 3 years to attain USD 60 bln target
- Prioritise the needs of promising sectors and potential export-oriented industries
- Review of incentive instruments to raise efficiency

Challenges

- Domestic economy challenges
  - Cost of production
    - Upward revision in administrative prices of energy
    - Revision of the minimum wages
- External economy challenges
  - Bangladesh's LDC graduation
  - Brexit
  - Trade war between USA and China
  - Export incentive packages by major competitors

5. Incentives for Export-Oriented Sectors: Recommendations for FY2019 Budget

Current Status of Export Incentives

- Export incentives

Cash incentives	Export Development Fund (EDF)
Bonded warehouse	Export Promotion Fund (EPF)
Duty drawback	Export retention quota
Tax rebate	Special income tax rate
Concessional commercial loans	Reduced tax rate

5. Incentives for Export-Oriented Sectors: Recommendations for FY2019 Budget

Special bonded warehouse facilities (SBW)

- Availed of by 100% export-oriented industries
- Larger part of fiscal incentives goto the RMG sector
- Other sectors are facing challenges in availing the facility
  - Government should formulate a medium-term plan for the thrust sectors
- UD certificates are issued by BGMEA/BKMEA
  - Customs Bond Commissionerate (CBC) has limited capacity
  - CBC needs to be connected with ASYCUDA to check fabrication of UD certificates
  - introduce e-UD and e-EXP in a priority basis with adequate support
- Misuse of bond facilities should be addressed by strengthening both monitoring and enforcement and by bringing the abusers to justice
  - Coordination among BGMEA/BKMEA, customs stations, Bond Commissionerate and the Bangladesh Bank
- Regularly update the HS code list to encourage product diversification

5. Incentives for Export-Oriented Sectors: Recommendations for FY2019 Budget

Cash incentives

- RMG exporters to the EU market are currently receiving 2% additional cash incentive (initiated in FY17)
  - Was introduced in view of sharp depreciation of Euro and GBP following the Brexit referendum
  - In February 2018, Euro and GBP have appreciated by 21.3% and 17.1% respectively compared to February 2017
  - This scheme may be revisited in view of the recent developments
- Government is planning to continue 15% cash subsidy for leather exports over the next 5 years to reach its export target of USD 5 bln by FY21
  - Welcome initiative in terms of policy consistency and business predictability
  - Capacity of BSTI should be developed
- A number of investigated cases found evidence of misuse:
  - Closer cooperation among involved stakeholders (e.g. Bangladesh Bank, NBR) is required
  - Budgetary allocations should be increased to enhance data access, human resource development and effective vigilance to the concerned government agencies

5. Incentives for Export-Oriented Sectors: Recommendations for FY2019 Budget

- Bangladesh's graduation from the LDC group by 2024
  - Many preferential treatments and market access facilities will be discontinued

- The restructured incentive package could include:
  - allocation for targeted skills development
  - contribution to employee's contribution fund
  - redefining non-traditional exports
  - strengthening of institutions
  - calibrating incentives in view of market dynamics
  - enhancing efficacy of the bond system
  - ensuring more predictability in the incentive regime

Section VI: Economic Zones: Priorities to Set up ‘Model’ SEZs

Independent Review of IRBD Bangladesh's Development

6. Special Economic Zones: Priorities to Set up 'Model' SEZs

- SEZs have been receiving increased attention from the policymakers
  - Urgency of addressing the 'infrastructure deficit'
  - Diverse range of business models and financing arrangements
  - Scope for providing 'one stop service' to potential investors
- Progress in setting up SEZs has been behind the targeted timeline
  - 76 SEZs have been identified with specific locations
  - 22 SEZs have been approved by the authority
  - Developmental work in the approved SEZs has been uneven
- A target was set by BEZA to develop 20 SEZs by 2018
  - Only 10 SEZs have actually been earmarked for completion but without any specific timelines
- Development works for only 2 SEZ projects (Jamalpur and Mirersarai) are currently under the purview of the ADP, in FY18
  - Allocations made for these two projects are not adequate
  - Only 4 SEZs have completed 75% of their total developmental work

6. Special Economic Zones: Priorities to Set up 'Model' SEZs

- **Giving priority to establish few 'model' SEZs**
  - This will give investors confidence about the new architecture
  - BEZA would be able to remodel its policies and practices according to its experiences with the Model SEZs
- **Ensuring access on an equal footing**
  - BEZA should encourage non-traditional and emerging industries
  - Prudent measures must be taken so that incentive packages are not abused and misused (tax holiday incentives, land speculation)
- **Provision of adequate ADP allocation**
  - Prioritise allocation for the establishment of Model SEZs
  - Adequate allocation in the upcoming national budget for SEZs in line with the SEZ Master Plan
- **Single authority for investment promotion**
  - Activities of BEPA, BEZA and PPP Office have significant overlaps
  - Some could be centralised while others could be mandated to the dedicated wing of the centralised authority

Independent Review of Bangladesh's Development

Section VII: Budget for Social Sector: Is it Good Enough for Inclusive Growth?

7. Budget for Social Sector: Is it Good Enough for Inclusive Growth?

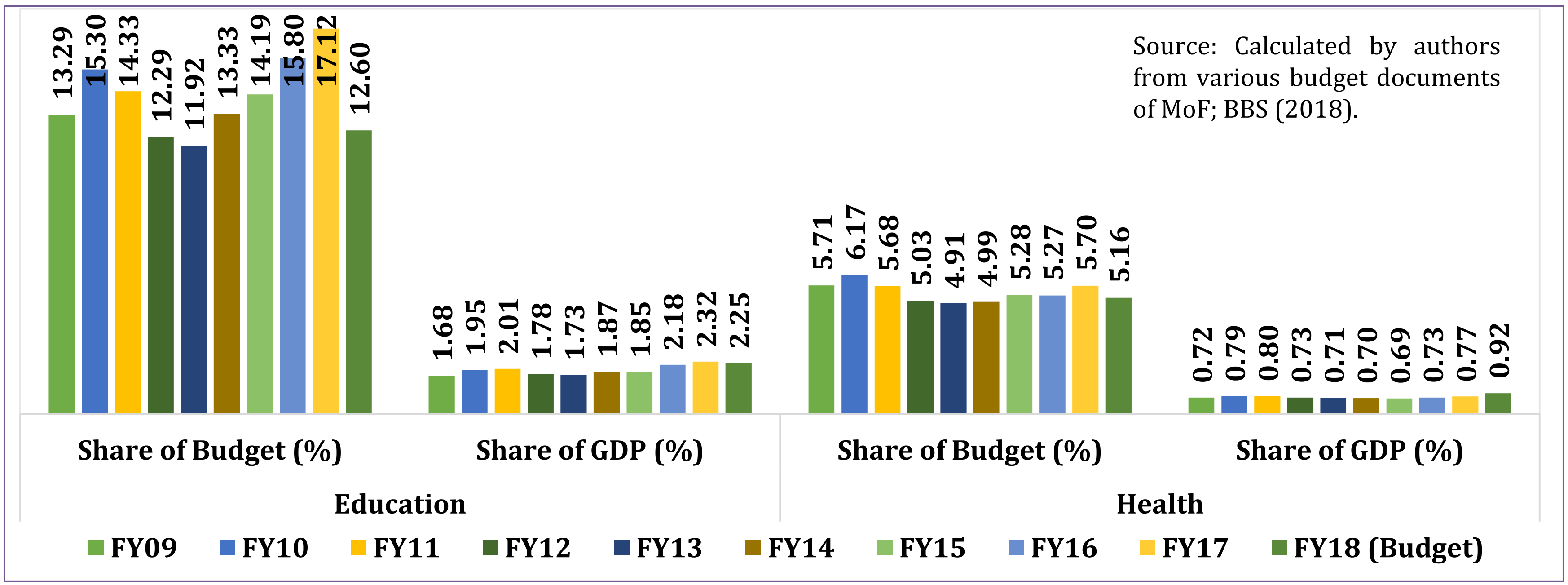
- Despite increased GDP over the years, the share of public expenditure in the social sector has not improved significantly.
- The quality of education and health service continues to remain a major concern.
- In view of government's commitment to attain the SDGs, particularly in areas such as education and health, the urgency to address the attendant deficits has risen manifold.
- National and International Targets
  - Expenditure on education to be **3% of GDP (7FYP)**
  - The Education 2030 Framework for Action set two benchmarks on domestic financing for education:
    - **4 -6% of GDP**
    - **15 -20% of public expenditure.**
  - Expenditure on health to be **1.2% of GDP (7FYP)**
  - World Health Organization (WHO) considers a benchmark of **5% of GDP or GNI** of the country.

7. Budget for Social Sector: Is it Good Enough for Inclusive Growth?

Allocations for Health and Education

Education	Health
▪ 2.25% of GDP in FY2018 while actual expenditure was 2.32% in FY2017. ▪ 12.6% of total budget in FY2018, while actual expenditure was 17.1% in FY2017.	▪ 0.92% of GDP in FY2018 while the actual expenditure was 0.77% in FY2017. ▪ 5.16% of budget in FY2018 while the actual expenditure was 5.7% in FY2018.

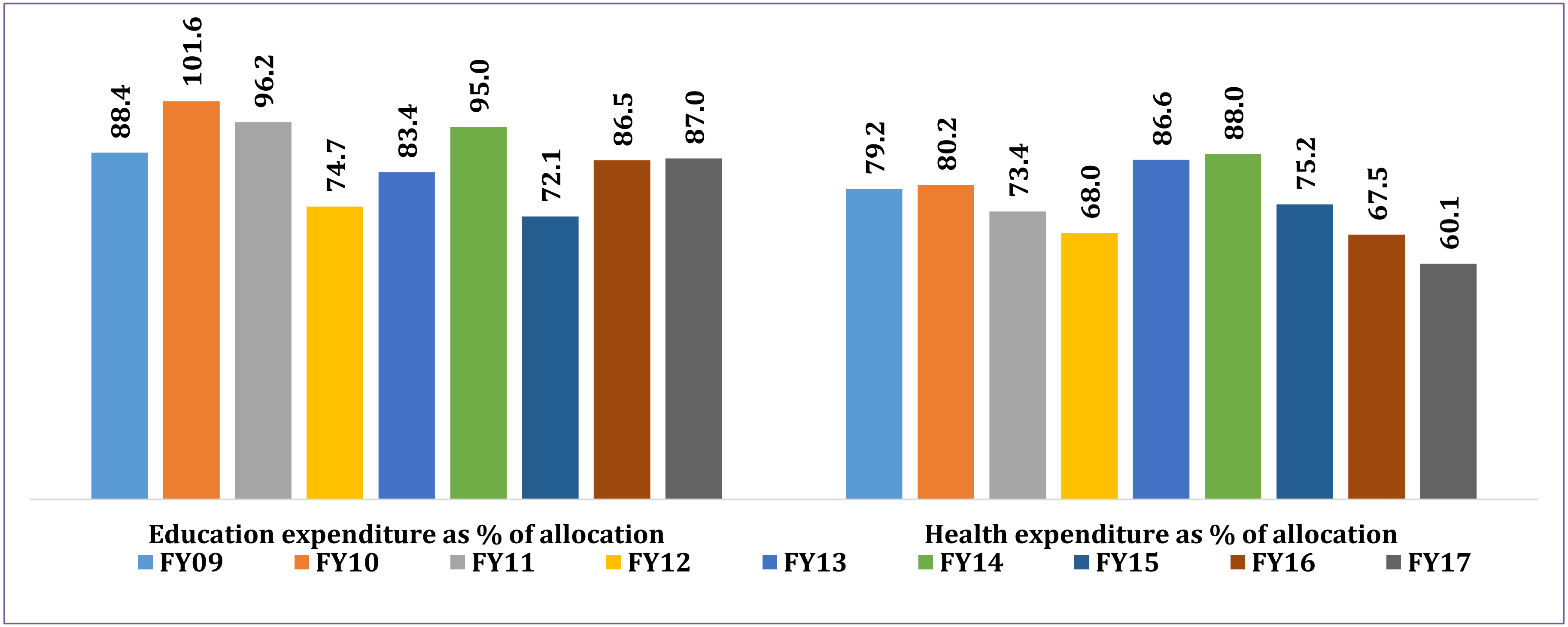
Expenditure on education and health as a percentage of GDP and total budget



7. Budget for Social Sector: Is it Good Enough for Inclusive Growth?

- Utilisation of allocated resources for the social sectors remains a problem
  - In FY2017, the government was able to spend about 87% of total allocations for education and only about 60% of total allocations for health.

Trend in utilisation of non-development budget for education and health



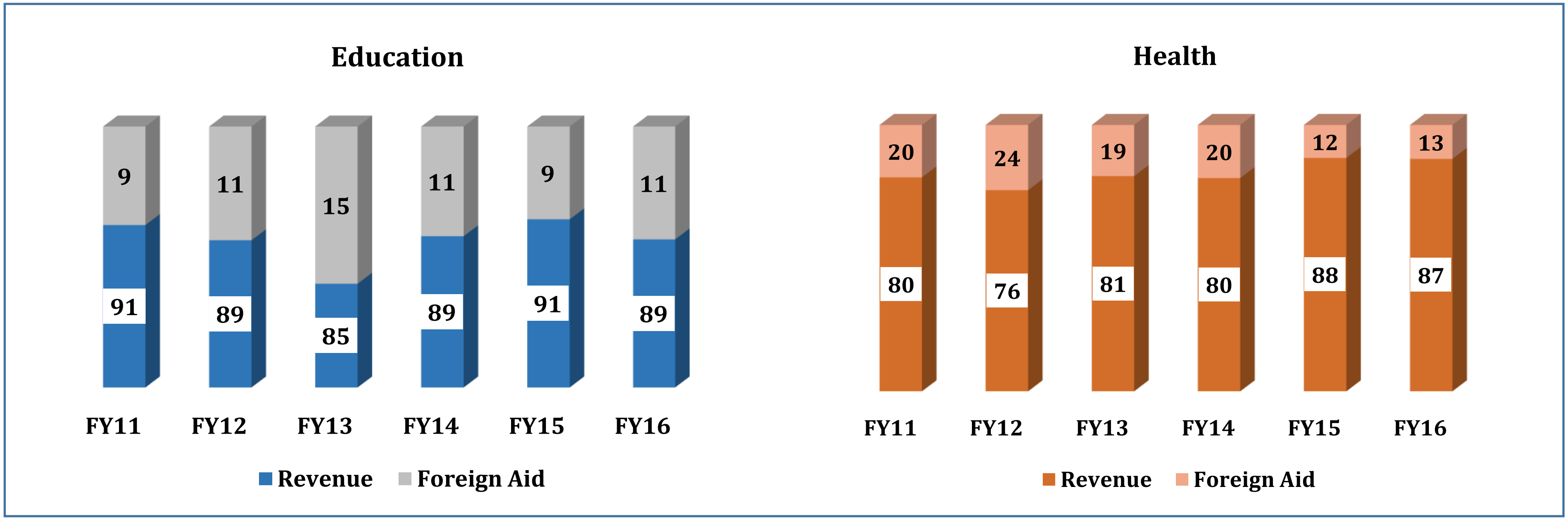
Source: Calculated by authors from Monthly Fiscal Report (various issues), Ministry of Finance (MoF).

7. Budget for Social Sector: Is it Good Enough for Inclusive Growth?

Sources of Finance

- Resources from foreign sources on account of health sector was lower in FY2016 compared to FY2012 (by 25%)
- Shares of foreign assistance in the education and health sectors have declined from the high shares of FY2014 to what these were in FY2016

Major sources of education and healthcare financing (%)



Source: Collected from ERD, MoF website.

7. Budget for Social Sector: Is it Good Enough for Inclusive Growth?

Education budget in view of emerging needs

- Bangladesh's progress in case of gross and net enrolment is satisfactory as these targets have been met
  - However, the target for dropout rates has not been achieved in FY2017.
- Quality of education is a pressing issue as learning outcomes leave much to be desired.
  - National School Assessment (NSA) 2015 shows that mean scores in 2015 for Bangla and Mathematics have fallen compared to 2013 across Grade 3 and Grade 5.

Assessment of learning as per National School Assessment

Details	2013 (Mean Scores %)	2015 (Mean Scores %)
Grade 3 Bangla	74	65
Grade 3 Math	58	41
Grade 5 Bangla	25	23
Grade 5 Math	25	10

Source: MoPME (2017a).

7. Budget for Social Sector: Is it Good Enough for Inclusive Growth?

- This can be explained by a number of factors including high student-teacher ratio (STR) and lack of qualified teachers.
  - NNPS from 33 districts and GPS from 38 districts have STR above the national target (MoPME, 2017a).
  - 27% of the Head Teacher posts and 7% of Assistant Teacher posts under Directorate of Primary Education remained vacant (MoPME, 2017b)
  - Only 58% of the primary teachers had a Bachelor/Honours or a Masters degree in 2016 (MoPME, 2017b)

Districts with the highest and lowest STR

Details	Government Primary Schools (GPS)		Newly Nationalised Primary Schools (NNPS)	
	District	STR	District	STR
Highest STR	Cox's Bazar	49	Noakhali	63
	Brahmonbaria	47	Cox's Bazar	60
	Rajbari	47	Narayangonj	57
Lowest STR	Pirojpur	24	Pirojpur	19
	Jhalokathi	24	Jhalokathi	18
	Rangamati	22	Rangamati	17

Source: MoPME (2017a).

7. Budget for Social Sector: Is it Good Enough for Inclusive Growth?

Health budget in view of emerging needs

- Over two-thirds of the total health expenditure in Bangladesh is financed by out-of-pocket spending (MoHFW, 2017)
- From the budgetary perspective, the government will need to put emphasis on indicators where targets remain unattained.

Status of selected health indicators

Indicator	Status in 2010 or 2011 or 2012	Target 2016	Progress in 2016	Remarks
Infant mortality rate (IMR)	43	31	28	Achieved
Under 5 mortality rate	53	48	35	Achieved
Maternal mortality ratio per 100000 live births.	194	<143	178	Not achieved
Neonatal mortality rate	32	21	19	Achieved
Total fertility rate (TFR)	2.3	2	2.1	Needs attention
Contraceptive prevalence rate	61.2	72	62.3	Not achieved

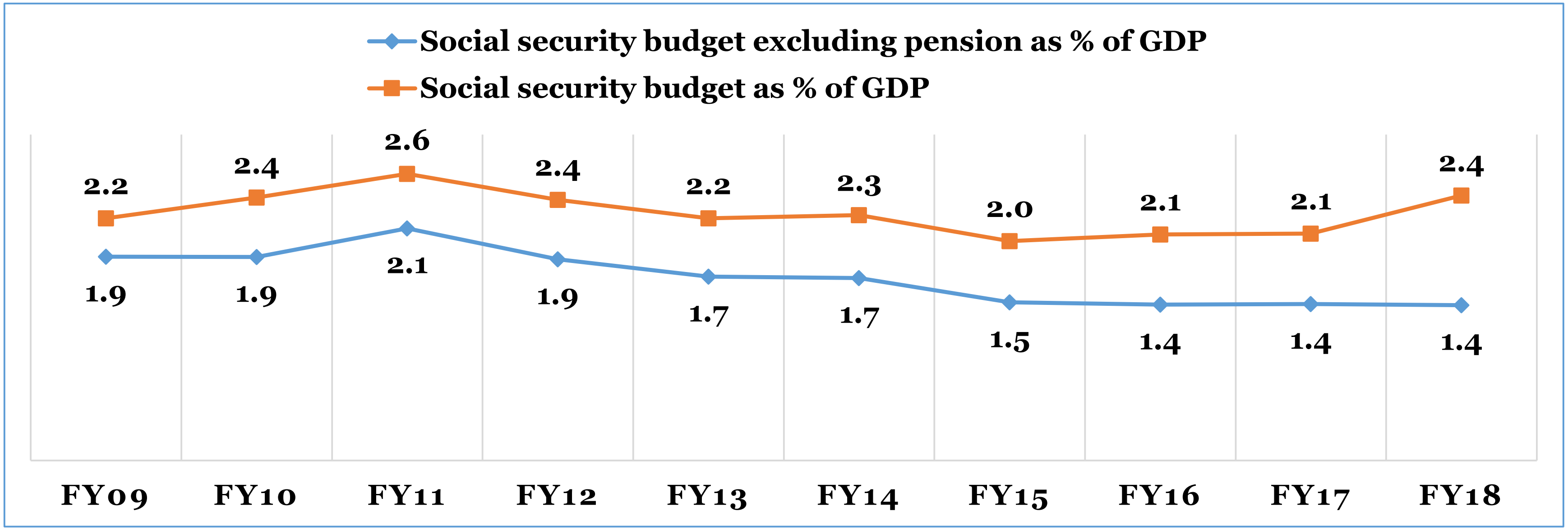
Source: MoHFW 2016 and 2012; BBS 2016.

7. Budget for Social Sector: Is it Good Enough for Inclusive Growth?

Budgetary allocations for social security

- ❑ Social security budget has been hovering around 2% of the GDP since FY2008-09
- ❑ In FY2018, the social security budget was 2.4% of GDP
  - ➢ In FY2018, 41.31% of the budget for social security was allocated for pension of government officials.
  - ➢ The social security budget excluding pension has been decreasing, from 2.1% of GDP in FY2011 to 1.4% of GDP in FY2018.

Social security budget as percentage of GDP

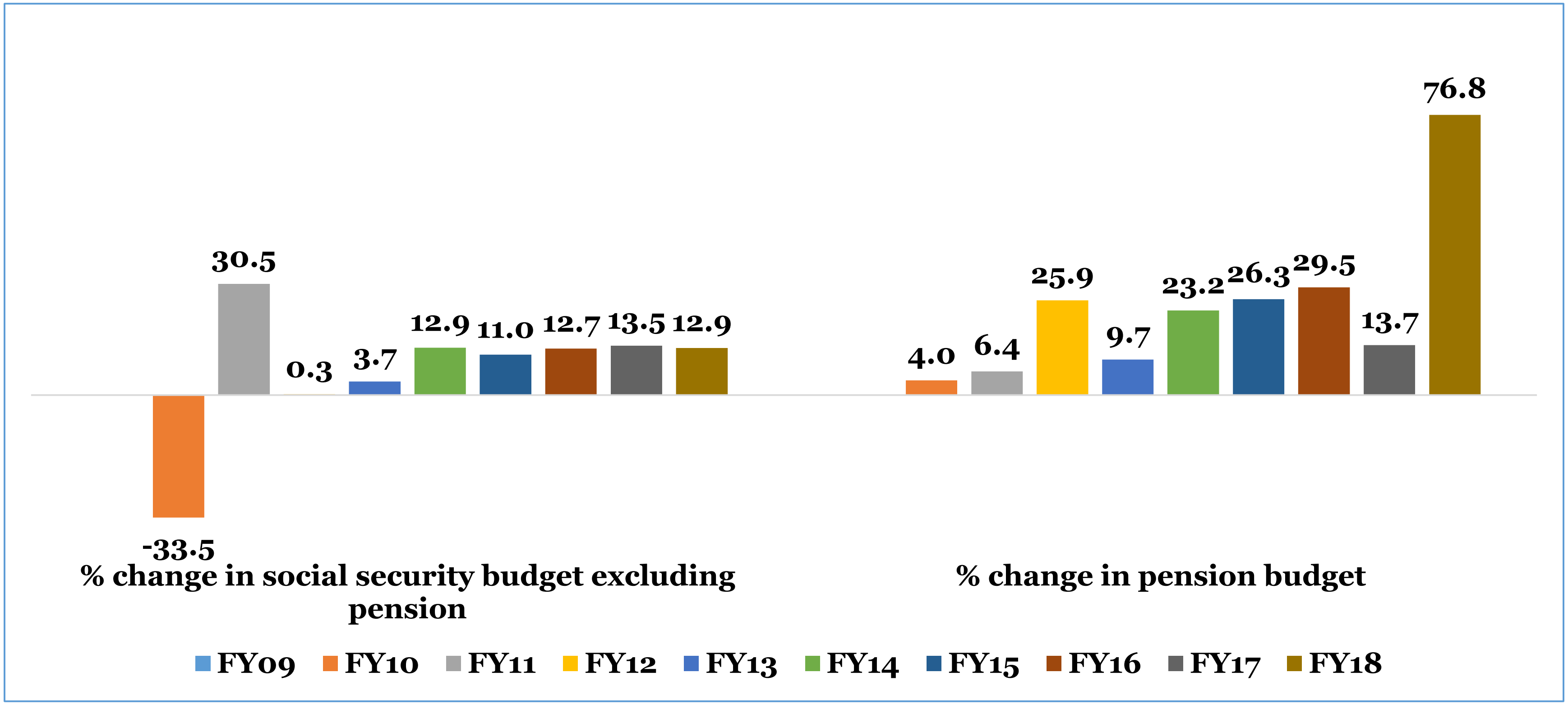


Source: Calculated from Social Security Policy Support (SSPS) Programme data.

7. Budget for Social Sector: Is it Good Enough for Inclusive Growth?

- The recent increase in social security budget was mainly due to the increase in the budget for pension.
  - For instance in FY18, the social security budget excluding pension increased by 12.9%, whereas the budget for pension increased by 76.8%.

Percentage change in social security budget and pension budget

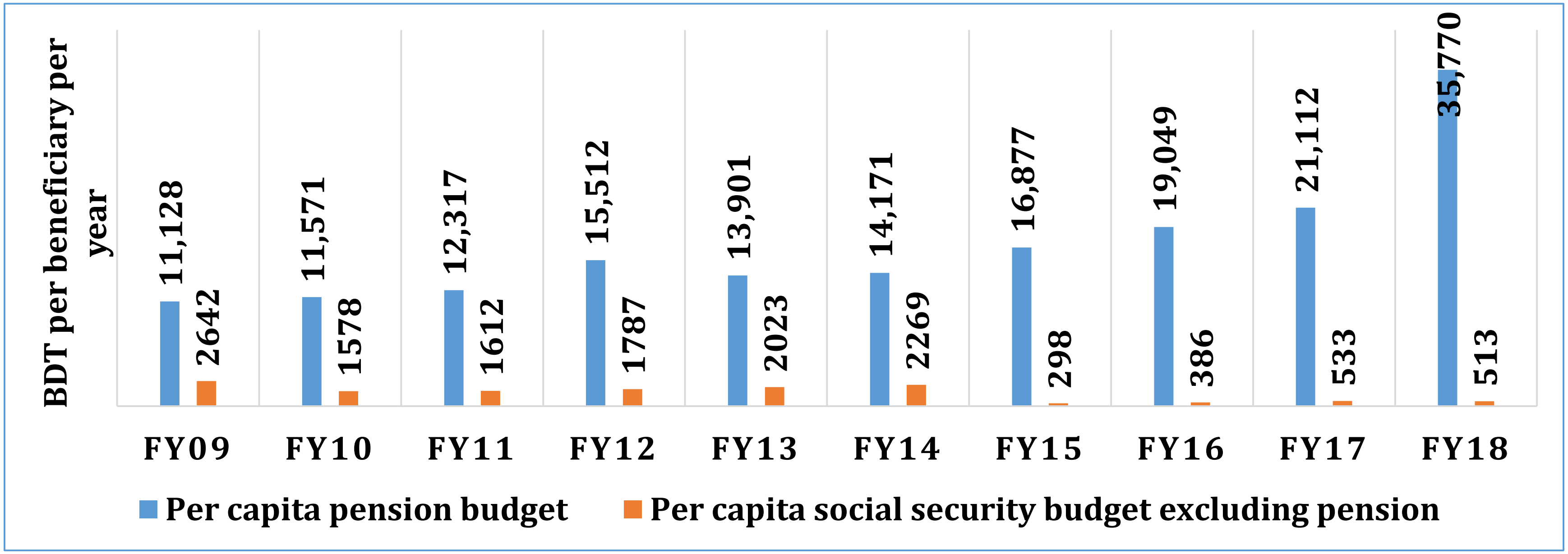


Source: Calculated from Social Security Policy Support (SSPS) Programme data.

7. Budget for Social Sector: Is it Good Enough for Inclusive Growth?

- Since FY2013, per capita budget allocation for pension has been rising, whilst at the same time the per capita budget allocation for social security excluding pension has been declining
  - In FY2018 the per capita budget allocation for pension was BDT 35,770 per beneficiary per year, compared to BDT 513 per beneficiary per year for social security programmes excluding pension
  - This means that, on average, pension beneficiaries received 69 times more money than beneficiaries of other social security programmes

Annual per capita social security and pension budget



Source: Calculated from Social Security Policy Support (SSPS) Programme data.

7. Budget for Social Sector: Is it Good Enough for Inclusive Growth?

- The government has prepared a National Social Security Strategy (NSSS) to be implemented during the 7FYP period.
  - The NSSS has broadened the scope of social security from the narrow safety net concept and included employment policies and social insurance.
  - Operationalization of such policies would be difficult since majority of the employed people is engaged in the informal sector.
  - Full implementation of the NSSS will also call for deployment of significant resources.

7. Budget for Social Sector: Is it Good Enough for Inclusive Growth?

Recommendations for National Budget FY19

- Budget for education should be at least 2.84% of GDP in FY19 (2.25% in FY18) to achieve the 7FYP targets.
- Increased budgetary allocations should focus on hiring qualified teachers and reducing the student-teacher ratio towards ensuring effective learning outcomes.
- Higher budgetary allocation should be made in order to improve skills of human resources aligned with demands of national and international job markets.
- Budget for health should be at least 1.12% of GDP in FY19 (0.92% in FY18) to meet the target laid out in 7FYP.
- Allocation should be suitably increased for putting in place adequate number of affordable and accessible public healthcare facilities, particularly with a view to reducing out-pocket-expenditure of the low income households.
- Pension for government officials should be separated from social security account.
  - Allocation for social security, excluding pension, should be raised to 1.6% of GDP in FY2019 (1.4% in FY18)
- Bring more clarity on the financing mechanism of the NSSS.
  - Allocate adequate resources in the budget in line with the NSSS and the universal pension scheme.

Section VIII: Budgetary Implications of Rohingya Crisis

8. Budgetary Implications of Rohingya Crisis

- Since August 2017, nearly 700 thousand *Rohingyas* have sought refuge in Cox's Bazar district of Bangladesh, fleeing from the massacre and violence in the Rakhine state of Myanmar. This has raised the *Rohingya* population in Bangladesh to more than 900 thousand (ISCG, March 2018).

  A Memorandum of Understanding (MoU) was signed on 23 November 2017 between Bangladesh and Myanmar for the repatriation of *Rohingyas*. Bangladesh also signed a MoU in Geneva with the UNHCR, the UN Refugee Agency on 13 April, 2018 relating to voluntary return of *Rohingya* refugees, once conditions in Myanmar are conducive.
- Five members of a family went back to Taungpyoletwei town repatriation camp in Rakhine state on 14 April 2018 but they were taken from 'No Man's Land', the area between Bangladesh and Myanmar borders.
- The GoB has been extending all possible support to the *Rohingyas* as soon as the crisis began. Various ministries of the GoB are engaged in providing humanitarian support to the *Rohingyas*. The GoB has directly spent money for the *Rohingyas*.

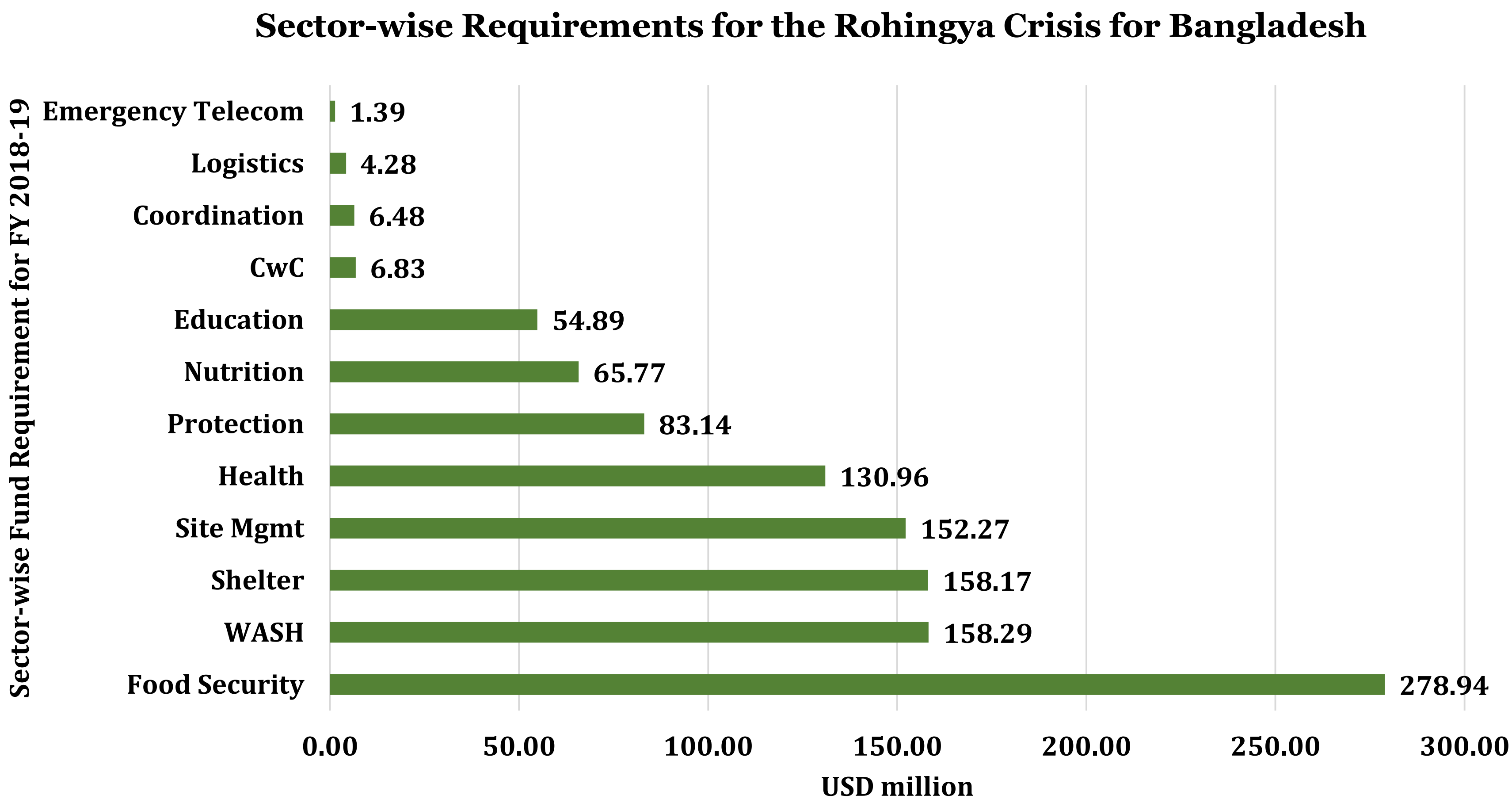
8. Budgetary Implications of Rohingya Crisis

Direct Costs of Rohingyas for the FY2019

- CPD has updated the estimation as regards the requirement for the *Rohingyas*, for FY19. This is based on the appeal amount of the Joint Response Plan (JRP) prepared by ISCG and SEG.
- According to the United Nations Office for the Coordination of the Humanitarian Affairs (UNOCHA), support from the GoB was 1 per cent of total requirement of USD 434 million during September 2017 to February 2018 (UNOCHA, 2018) period. The sum was sought at the time of the first humanitarian response plan.
- CPD's estimation makes the following assumptions: (i) 300 *Rohingyas* will be sent back to Myanmar per day from the month of July 2018; (ii) repatriation process will take place for 25 working days per month; (iii) all costs are equal for each person; and (iv) cost of shelter construction and site management will be the same for all months.
- The estimates indicate an amount to the tune of USD 1.1 billion which will be required to underwrite the costs in FY2019. A sector-wise needs of the *Rohingyas* shows that most of the expenditure will have to be incurred on account of food security, WASH, shelter, site management and health.

8. Budgetary Implications of Rohingya Crisis

Direct Costs of Rohingyas for FY2019



Source: Estimated by author based on Joint Response Plan, IOM, 2018

8. Budgetary Implications of Rohingya Crisis

Recommendations

In light of the current situation of the *Rohingya* crisis, a number of recommendations can be made for the upcoming national budget for FY19:

- Given that the requirement for the Rohingyas is quite significant and the repatriation process is uncertain, the GoB has to chalk out a comprehensive plan for resource mobilisation.
- Information on the flow of international fund for *Rohingyas* and the usages of these funds should be made readily available. Ministry-wise resource requirement plan for FY 2019 would be helpful for informed resource management.
- Transparency in the allocation of budget, at the ministerial level, in view of the Rohingya crisis, should be ensured. This will ensure allocative efficiency and resource-use efficacy in connection with the various activities being implemented including particularly in the construction of Rohingya shelters at Bhashan Char, setting up of vocational training system for them and provisioning of basic facilities to help sustain livelihoods till the repatriation of the Rohingyas.

Section IX: A Trust Fund for SDG Delivery

9. A Trust Fund for SDG Delivery

Role of NGOs in Delivering SDGs

- Since independence, the NGOs/CSOs in Bangladesh are playing a critically important role in the country's socio-economic development
- Drawing on their track record and experiences in MDGs implementation, NGOs have the potential to make their mark in view of the SDGs as well
- NGOs can play a key role in the process of implementing the SDGs through
  - Awareness building
  - Mobilisation of stakeholders around the goals
  - Leveraging Government actions
  - Preparing shadow reports on SDGs to feed into the Voluntary National Report (VNR)
  - Carrying out advocacy and highlighting concerns at the HLPF and ECOSOC meetings
  - Inducing collaboration in projects relevant to SDGs implementation undertaken by the local governments, private sector and others
  - Disseminating knowledge about SDGs and stressing for transparency and accountability in the implementation process
  - Contributing to cost-effective and timely implementation of projects
  - Mobilising global opinion and resources to support SDGs implementation
- For a successful GO-NGO Partnership and adequate financial endowment of the NGOs, the idea of setting up a **'SDG Trust Fund'** in support of the NGOs becomes a relevant proposition.

9. A Trust Fund for SDG Delivery

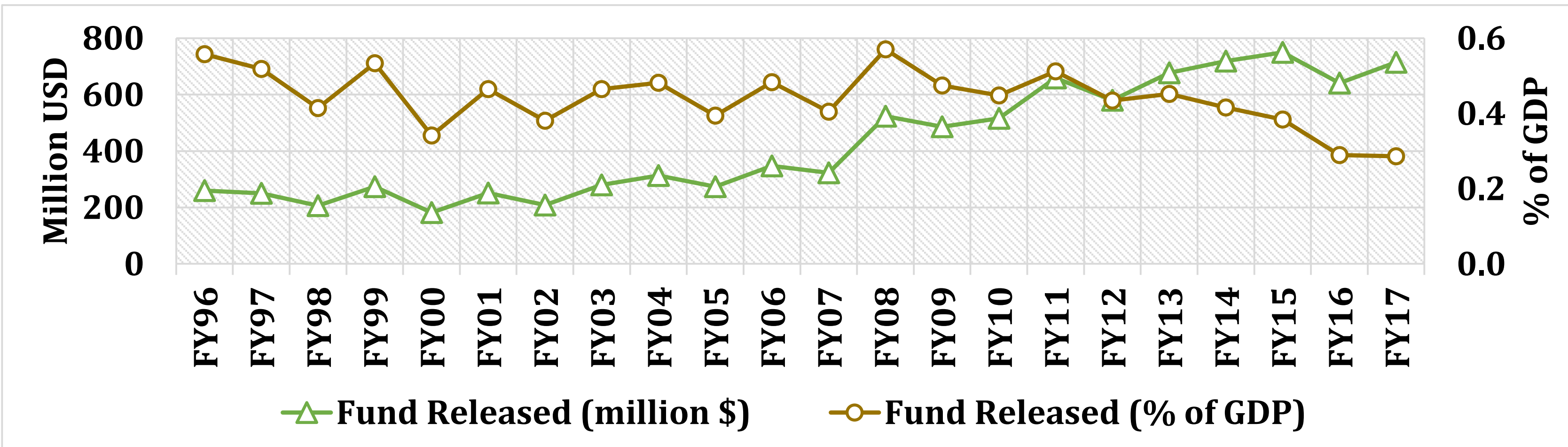
Rationale for SDG trust Fund

- Negative implications for fund flow and availability concerning the NGOs due to
  - Global resource crunch and Bangladesh's middle income and LDC graduation (eligibility)
  - Challenges in attracting ODA on concessional terms
  - Aftermath of the global financial crisis of 2008-09 and diversion of resources to address more urgent issues like migration
- These implies, NGOs will need alternative sources of funding to carry out their activities
- Financing needs for implementing the SDGs would be significantly higher than the MDGs
  - To meet the additional (synchronised) financial needs to implement the SDGs, Bangladesh will need a total of USD 928.48 billion over the period of FY 2017- FY 2030 and annual average price tag would be about USD 66.32 billion at 2015-16 constant prices.
- GoB identified
  - Public-Private Partnership (PPP) as a key strategy to finance SDGs implementation
  - NGOs' role as a major player in implementing the SDGs and also as an important source for SDG-related financing and addressing the financing gap in implementing the SDGs
- Foreign fund disbursed in favour of NGOs has been about 20.2 per cent of total ODA flow to Bangladesh in FY2017.
- Number of projects approved by the NGO affairs bureau was about 1037 during the 2016-17 period

9. A Trust Fund for SDG Delivery

- Although the flow of foreign grant fund released though the NGO affairs bureau shows an increasing trend, its share in the GDP has been declining

Flow of Foreign Grant Fund Released through NGO Affairs Bureau



Source: NGO Affairs Bureau, Prime Minister's Office

- GoB should consider allocating budgetary support to NGOs because
  - Enhanced NGO capacity to implement the SDGs where they have comparative advantage and proven track record
  - NGOs have a natural advantage in reaching the furthest first
  - It may ensure leveraging government activities through NGO interventions towards overall effectiveness.

9. A Trust Fund for SDG Delivery

Establish a SDG Trust Fund for the NGOs/CSOs

- Objective is to create a financing window for NGO partnership to implement the 2030 global agenda in Bangladesh.
- The SDG fund is to be operationalised through PPP
- The recipients will spend the money from the fund by maintaining transparencies and accountability in accordance with an identified structure and framework of operation

Proposed Framework: Prepared based on a review of the legal and governance structures of different Environmental Trust Funds (EFs) established in developing countries.

Formation and Governance: A government approved legal framework will be developed to establish the SDGs Trust Fund. There will be a Memorandum of Understanding (MoU) or other types of agreements between the national government and the Trust Fund according to the PPP law/guideline (for instance, PPP law, 2015 and Procurement Guidelines for PPP Projects 2018).

- A select number of "Trustees/Board members", will be responsible for putting in place, structuring the fund, and processing of decisions.
- There could be advisory committee, internal audit section, monitoring and evaluation section and other administrative sections to run the fund, as deemed necessary.
- Operational plans in the areas of implementation, fundraising, resource mobilisation, communications, and evaluation etc. will need to be developed.
- The fund is expected to work independently and be tax exempted.

9. A Trust Fund for SDG Delivery

Amount

- The estimated amount to be financed by NGOs was expected to be about 5 per cent (on average) of the total additional finance requirement during the FY 2017- FY 2030 period. (GED, 2017)
- This implies that NGOs are envisaged to contribute to SDGs implementation to the tune of about Tk. 14,000 crore to meet the financing gap.
- If the total foreign fund channeled through NGOs in FY2017 (USD 715 million or about Tk. 6,000 crore) are considered, there may be a gap of about Tk. 8,000 crore
- The idea is to help the NGOs to draw synergies, and leverage other initiatives in areas where NGOs are best placed in terms of implementing the SDGs.

9. A Trust Fund for SDG Delivery

Amount

- Government allocation to NGOs,
  - Could play a catalytic role in helping the NGOs to make more effective use of funds available to them and also take up additional work
  - Could help bridge the aforesaid gap as regards NGO contribution to SDGs implementation particularly taking cognisance the fact that a significant part of the national budgetary allocation often remains underutilised on a regular basis
- Since, the proposed SDG Trust Fund is a new concept, the government may like to start with a token allocation of Tk. 500 crore.
- This may be further raised in phases considering demand, resource availability, and utilisation efficacy.

9. A Trust Fund for SDG Delivery

Sources of Fund and utilisation

- Major part of the envisaged fund will come from the national government through budgetary allocation in the ADP
- Utilisation of the fund will also have the flexibility to blend finances from multilateral and bilateral aid, NGOs, foundations, lotteries, philanthropic bodies, and innovative sources
  - Foreign and other potential donors may also be invited to contribute to this fund.
  - Private sector may also put in corporate social responsibility (CSR) money
- The fund money will be allocated to eligible implementing agencies such as NGOs, CSOs, community-based organisations, and private sector entities
- The implementing agencies will be selected based on the strength of respective proposals submitted against relevant calls on different SDG themes and all selection and allocation will be through a competitive process
- The fund will also help relevant capacity building of the implementing agencies based on need assessments

9. A Trust Fund for SDG Delivery

Monitoring and Evaluation

- Monitoring and evaluation section will monitor use of fund and examine grantee reports. Staff from the section will visit fields where implementation of activities underwritten by the Fund would be taking place, on a regular basis
- Evaluation will include assessment of the project implementation outcomes according to the objectives set out in the proposal, implementing organisations' performance, and efficacy of the use of the fund disbursed

Risk Factors

- Bangladesh has created Bangladesh Climate Change Trust Fund (BCCTF) and Bangladesh Climate Change Resilient Fund (BCCRF) in 2010
- A TIB study found a number of problems that inform functioning of the two funds including lack of transparency, political influence in selection of the NGOs, poor quality of work, and poor state of accountability in the funds' overall operations
- Lessons from operationalising these funds should be appropriately drawn to run the proposed SDG Trust Fund

9. A Trust Fund for SDG Delivery

- **Some of the risks that need to be taken cognisance of are as follows:**
  - Autonomy of the implementing NGOs may be compromised due to overdependence on trust fund
  - Slow disbursement of funds due to poor management
  - Political influence over decisions as regards grants allocation and selection of implementing NGOs
  - Government agencies controlling tendency may impede the independent functioning of the fund
  - Lack of organisational/technical capacities impeding the effective implementation of the projects
  - Variability and inflation of administrative costs, and/or lack of delivery, due to poor design
  - Failure to coordinate with stakeholders in implementation and monitoring and evaluation
  - Fraudulent practices by particular NGOs
  - Political instability, lack of policy continuity, change in governments could undermine effective functioning of the Fund

Section X: Concluding Remarks: Recommendations for National Budget FY2019

10. Concluding Remarks: Recommendations for National Budget FY2019

- The overarching macroeconomic stance of the national budget for FY19 should be maintaining macroeconomic stability with greater emphasis on inclusive development
- The provisional national accounts estimate for ongoing fiscal year indicated a sustained acceleration of economic growth while employment generation figures for the previous year also showed some promise
  - However, in FY17 average real labour income had declined and at the same time unemployment rate for youth and relatively more skilled labour force had increased considerably
- Analysis of the macroeconomic correlates presented in the preceding sections reveals a number of stress points
  - failure to mobilise resources from domestic sources at the needed level
  - delays, cost overrun and institutional weakness in development project implementation
  - financing of fiscal deficit from relatively expensive sources such as net sales of NSD certificates
  - gradual increase in inflation fuelled by rising food prices
  - disarray in the banking sector; increasing interest rate
  - depressed BoP scenario in the backdrop of spurt in import growth despite recovery in export earnings and remittance inflow along with better disbursement of foreign aid
  - volatility in the exchange rate market

10. Concluding Remarks: Recommendations for National Budget FY2019

- In view of the emergent scenario, the need for a significant improvement in the quality of macroeconomic management cannot be overemphasised
- CPD, over the past several years, has been repeatedly urging for initiating reforms in a number of critical areas
- Evidently, in the run up to the forthcoming national election in December 2018, the government has little appetite for implementing the much-needed reform agenda
- However, reform issues should inform the debate and discourse in the course of the electoral campaign so that the issues are kept alive and concrete measures toward implementation are taken by the new government after the national elections

10. Concluding Remarks: Recommendations for National Budget FY2019

Macroeconomic policy stance and fiscal budgetary recommendations for FY2019

- Bangladesh Bank must pursue a cautious monetary policy in the coming months in view of rising inflationary pressure and easing the pressure on the BoP situation
  - Influence of vested interest groups needs to be restrained while formulating national economic policies
  - Role of the commercial banks should be put under scrutiny in view of strengthening the capital market
- Budgetary allocation for the state-owned commercial banks in the form of recapitalisation, carried out repeatedly in recent years, is morally unacceptable and economically unjustifiable
  - Public money should be distributed to banks under stringent terms and conditions in order to ensure proper utilisation
  - At the same time, alternative avenues such as using revenue to increase capital, exploring private investors to buy bank shares, or mergers with other banks should be explored

10. Concluding Remarks: Recommendations for National Budget FY2019

- The fast rising import payments have become a major concern due to the adverse implications for the BoP, exchange rate stability and forex reserve accumulation
  - The central bank should consider discouraging imports of consumer and luxurious commodities by raising L/C margins for import and reducing the time for L/C repayment
  - Foreign exchange management should aim at maintaining stability in the exchange rate of the BDT against USD
  - For the time being the forex reserves should be able to cover the pressure in the BoP
  - However, central bank should remain vigilant against volatility in the domestic foreign exchange market as has been experienced in recent times
- Historically, trade mispricing and capital flight are found to be more extensive during the election year
  - Curbing such illicit financial flows will require coordinated efforts by several policy actors including the Bangladesh Bank and the NBR
  - The long overdue data integration process (e.g. NBR data centre) should be established to reduce trade mispricing and revenue leakages through analysis of the quality of disaggregated trade data
  - Transfer Pricing Cell of NBR should be vested with the required capacity to enable it to carry out its responsibilities in an effective manner

Independent Review of Bangladesh's Development

10. Concluding Remarks: Recommendations for National Budget FY2019

- The forthcoming budget must focus on raising revenue from niche areas including speedy realisation of disputed revenue claims through the Alternative Dispute Resolution (ADR)
  - Immediate steps need to be taken in order to recover the large amount of due taxes from the state-owned enterprises
- Gradual increase of inflation and declining average monthly real wage of individuals have been putting pressure on the disposable income of lower-middle and middle-income households
  - The budget for FY2019 should consider raising the tax-free income ceiling to Tk. 3 lakhs in order to provide respite to lower middle income households
  - The budget may also consider reducing the personal income tax rate for the first slab to 7.5% from the prevailing rate of 10.0%
- The budget should take a view to assess tax incentive and exemption packages based on economic returns
  - More efforts will be required to expand the prevailing incentives for export-oriented sectors beyond the RMG and some of the other thrust sectors
  - However, institutional strengthening through enhancement of capacity of oversight agencies and enforcement of relevant laws must be ensured before taking such steps

10. Concluding Remarks: Recommendations for National Budget FY2019

- The budget should refrain from reducing corporate tax rates on an ad-hoc basis, in a hasty manner and without a rigorous analysis
  - Adjustments of corporate tax rates, if required, should be done in a staggered way over the medium term in order to absorb any revenue shock and provide predictability to investors
- Budgetary allocations for social sectors must be coherent with the overall development needs of the economy, particularly in view of SDG targets
  - In view of the budgetary targets for social sectors set by 7FYP, resource allocations for education, health and social security need to be enhanced to 2.8%, 1.1% and 1.6% of GDP respectively in FY19
  - The government also needs to take concrete steps to implement the NSSS
  - CPD also recommends to create a SDG Trust Fund in the upcoming budget with Tk. 500 crore which can be utilised by the NGOs with a view to attain the objective of 'leaving no one behind'
- While placing the fiscal-budgetary proposals before the parliament, budgetary implications for *Rohingya* management should be mentioned in a transparent manner
- While it may be tempting for a political government to consider development projects in the run up to the election, FY19 budget should avoid all conspicuous public spending
- Timely implementation of ADP projects should be prioritised, particularly for the large projects
  - To this end, the implementing agencies should accelerate the pace of implementing the 'model' SEZ projects while the Finance Division will need to ensure adequate budgetary allocations

10. Concluding Remarks: Recommendations for National Budget FY2019

Recommendations in the run-up to the election

- To sustainably improve economic management, continued efforts are needed to strengthen legal and institutional system
  - Independent and rigorous economy wide analyses should be conducted for all types of reforms
- Out of 105 countries for which data was available, Bangladesh ranked 102 and 98 respectively with regard to revenue-GDP and tax-GDP ratio – Need to put emphasis on Medium Term Revenue Strategy (MTRS)
  - Emphasise timely implementation of VAT and SD Act 2012. Implementation of online VAT registration and filing system and digitisation of VAT process and bringing in more businesses under the system should be given priority
  - Efforts should be made to finalise the draft Direct Tax Act at an early date and place it in the public domain to seek opinion of relevant stakeholders and interested groups
  - GoB needs to rationalise and modernise the Customs Act on an urgent basis corresponding with the current industrial and export policies
  - NBR should improve and utilise its tax database for better enforcement
  - The medium-term revenue strategy should seek to identify innovative areas for resource mobilisation including assessing feasibility of introducing taxation of agricultural income, a comprehensive property tax and inheritance tax in line with international practices
  - Gain efficiency through broader use of technology including introduction of electronic tax deduction at source (e-TDS) with issuance of tax certificates by the NBR against an e-TIN linked to each TDS collection

10. Concluding Remarks: Recommendations for National Budget FY2019

- Establishing a Public Expenditure Review Commission for ensuring accuracy of cost estimation of public investment projects
- Consider establishment of a permanent Local Government (Finance) Commission towards effective devolution of power and introduction of appropriate financing modalities for local government
- Legal and institutional reforms will be required for the initiatives of universal pension scheme and a national health insurance
- Inflation, particularly that of food items, must be checked given its welfare impact on the marginalised section of the society
  - Government should consider setting up an Agriculture Costs and Prices Commission. It should be mandated to
    - provide strategic guidelines to ensure food security in Bangladesh
    - recommend incentive structure for the producers
    - provide guidelines for price signals in the market and for procurement
    - reduce the disparity between farm-gate and retail prices of agricultural products, and
    - balance consumer-producer interests and ensure fair prices for farmers
- Consider stablishing of an Independent Financial Sector Reform Commission (IFSRC) in the backdrop of the disarray in the banking sector
- Consider setting up an independent Statistical Commission to examine the quality of data pertaining to key macroeconomic correlates and come up with suggestions to improve data quality and ensure autonomy of statistical organisations

Independent Review of Bangladesh's Development

Thank You