



State of the Bangladesh Economy in FY2015-16

Second Reading

CPD's Budget Recommendations

Dhaka: 17 April 2016



CENTRE FOR POLICY DIALOGUE (CPD)
B A N G L A D E S H
a civil society think tank

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- The CPD IRBD 2016 Team would like to register its sincere gratitude to *Professor Rehman Sobhan*, Chairman, CPD for his advice and guidance in preparing this report.
- The Team gratefully acknowledges the valuable support provided by *Ms Anisatul Fatema Yousuf*, Director, Dialogue and Communication Division, CPD and her colleagues at the Division in preparing this report. Support of *Ms Nazmatun Noor*, Deputy Director, Dialogue and Outreach is particularly acknowledged in this connection. Contribution of the CPD Administration and Finance Division is also highly appreciated. Assistance of *Mr Hamidul Hoque Mondal*, Senior Administrative Associate is particularly appreciated.
- Concerned officials belonging to a number of institutions have extended valuable support to the CPD IRBD Team members. In this connection, the Team would like to register its sincere thanks to *Bangladesh Bank, Bangladesh Bureau of Statistics (BBS), Bangladesh Energy Regulatory Commission (BERC), Bangladesh Export Processing Zones Authority (BEPZA), Bangladesh Garment Manufactures & Exporters Association (BGMEA), Bangladesh Power Development Board (BPDB), Board of Investment (BoI), Bureau of Manpower, Employment and Training (BMET), Chittagong Stock Exchange (CSE), Department of Agricultural Extension (DAE), Dhaka Stock Exchange (DSE), Diamond Money Exchange Service Ltd., Export Promotion Bureau (EPB), Ministry of Finance (MoF), National Board of Revenue (NBR), and Planning Commission.*
- *The CPD IRBD 2016 Team alone remains responsible for the analyses, interpretations and conclusions presented in this report.*

- National budget for FY17 is being prepared in the backdrop of an inhospitable global economic environment as traditional and new tensions emerge in the national economy
- Macroeconomic conditions have remained stable due to low inflation, steady exchange rate regime and resilient export sector performance
 - GDP growth rate for FY16, projected at 7.05%, is the highest since 2007
- Old tensions persist through public expenditure leakages, low revenue growth, lack of tax compliance, weak governance, inertia in implementation of reform, and low private and public investment
- Emerging issues e.g. financial and capital market weaknesses, feeble supervision of the central bank, global economic slowdown and recent financial security concerns also pose a threat to the national economy

- Upcoming budget must address the aforementioned issues by raising the quality of budgetary and fiscal planning through reforms as needed.
 - Subsequent economic developments should cater towards implementation of the 7FYP and the SDGs through sound fiscal policy.
- Report will have two components:
 - In depth analysis of existing fiscal framework, and
 - CPD's budget recommendations regarding fiscal framework, revenue mobilization, public expenditure, budget deficit financing, fiscal measures and economic reforms.
- Four processes to receive inputs from stakeholders –
 - Telephone interviews on fiscal measures
 - A pre-budget dialogue organised by the CPD in Bogra
 - A consultation meeting with young entrepreneurs and professionals
 - An online opinion survey through Facebook and e-mail platforms to get feedbacks from citizens on expectations

Macroeconomic Backdrop in the Run-up to the National Budget for FY2017

The government expects economic growth to exceed the 7% threshold but low level of private investment may continue to remain a concern

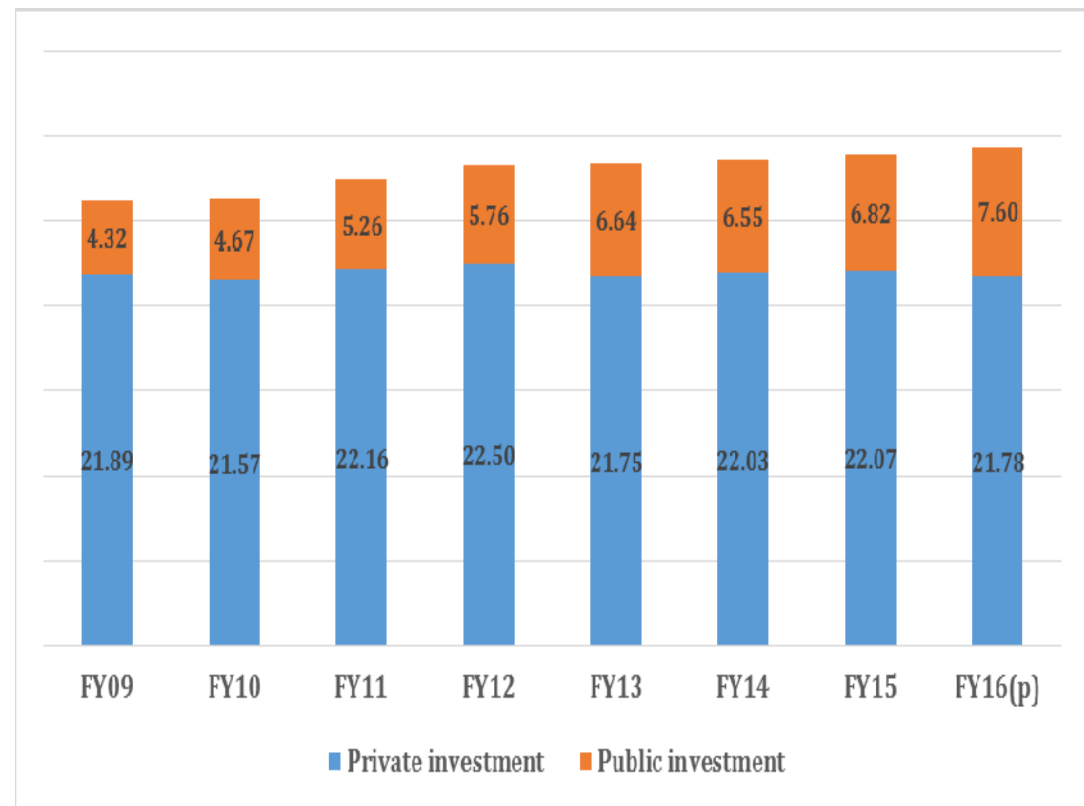
- Provisional GDP growth estimate (7.05%) was found to be higher than expectations
- Public administration and defense, education, and, health and social works contributed to the higher service sector growth rate
- If the growth rates of FY15 (6.55%) and FY16 (7.05%) are compared, of the extra growth of 0.5 percentage points, 0.4 percentage points is expected to be contributed by the national pay scale revision

Contribution to GDP Growth Rate (%)

Sectors	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
<i>Manufacturing</i>	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
<i>Public administration and defense</i>	0.25	0.19	0.21	0.25	0.27	0.24	0.21	0.22	0.32	0.53
<i>Education</i>	0.18	0.15	0.13	0.11	0.12	0.16	0.13	0.16	0.17	0.30
<i>Health and social works</i>	0.10	0.11	0.06	0.13	0.12	0.07	0.09	0.09	0.09	0.15
Tax less 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

- Investment as % of GDP is expected to increase by 0.5 percentage points to 29.38 per cent in FY16
- The rise in public investment has considered the original allocations of budget for FY16
- Private investment is estimated to decline by about 0.3 percentage point to 21.78 per cent in FY16
 - Both term loan disbursement and import of capital machineries have remained in the negative terrain

Investment as % of GDP



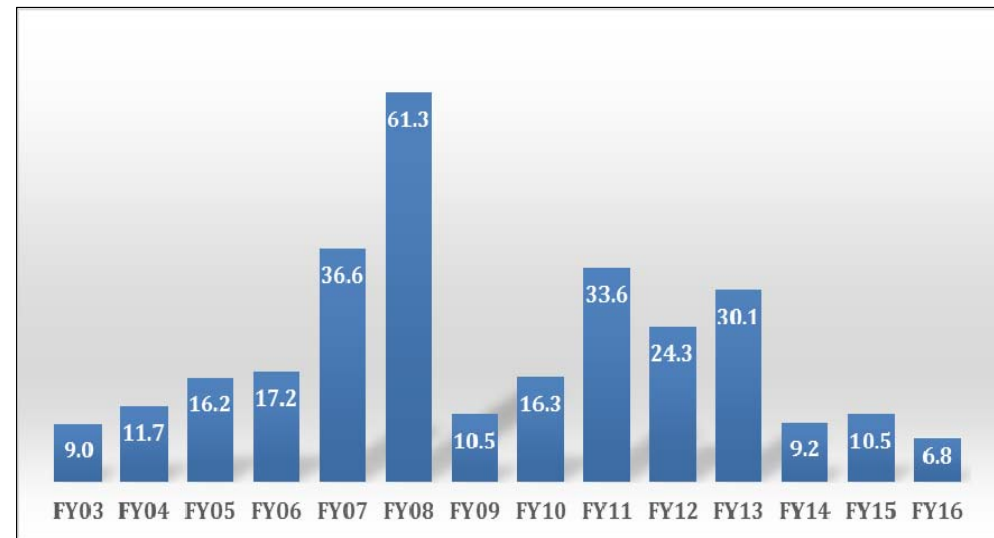
- The elevation of GDP growth in FY16 was not transmitted in other macroeconomic correlates
- Income tax collection remained much lower than estimated growth rate of nominal GDP of 14.1%
- Pace of employment generation did not take a headway followed by slowdown in private investment
 - Between 2013 and 2015 (Jul-Sept), national employment only increased by 6 lakhs (annual average being only 3 lakhs)
 - 13.8 lakhs jobs were created annually between 2003 and 2013.
- 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 as well as distributed in a just way

Macroeconomic Backdrop

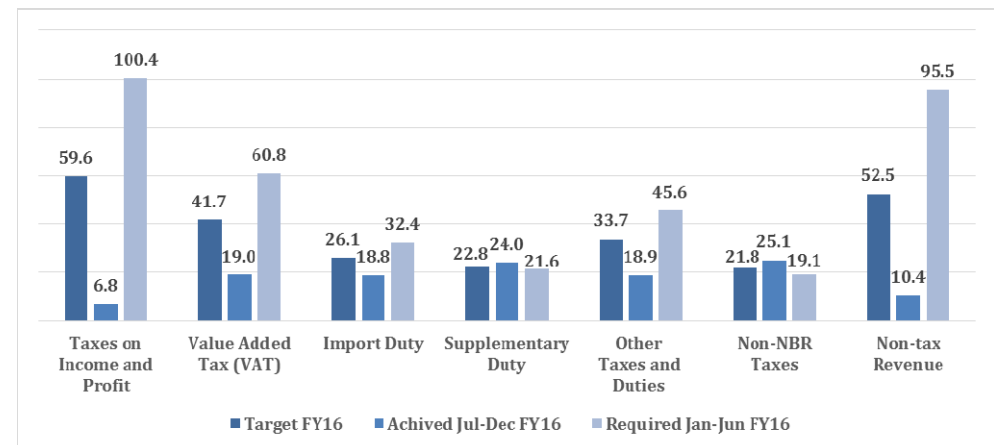
Revenue mobilisation is likely to miss the annual target by a large margin

- NBR will likely to miss the target for fourth consecutive year
 - NBR collection growth was 16.3% (Jul-Dec of FY16; target 42.3%)
 - Income tax collection growth (6.8%) was the lowest during the last 14 years
- Import duty (18.8% against 26.1% target) and supplementary duties (24.0% against 22.8%) collection were on track
- Non-tax revenue collection increased by 10%
 - Far below the target of 52.5%
- Despite a hefty profit earned by the BPC, revenue collection may fall short by Tk. 38,000 crore (Target: Tk. 208,444 cr.)

Growth of Income Tax Collection



Revenue Collection Growth



Public expenditure will be lower than planned

- 30.7% of non-development budget was spent (mere 4.7% growth) between Jul-Dec FY16
 - This figure is expected to rise as payments using new pay scale were released from January 2016
- ‘Subsidies and Current Transfers’ and ‘Interest Payments’ were well within the limit
- Tk. 1,200 crore was spent for recapitalisation of the SCBs (BFY16: Tk. 5,000 crore)
- Subsidy requirements are expected to remain at downside
 - BPC moved to the profit terrain in FY15 and continued earning profit in FY16 (drastic fall in international oil prices)
- The nature of recent acceleration of GDP growth suggests that it is largely driven by rise in public salaries

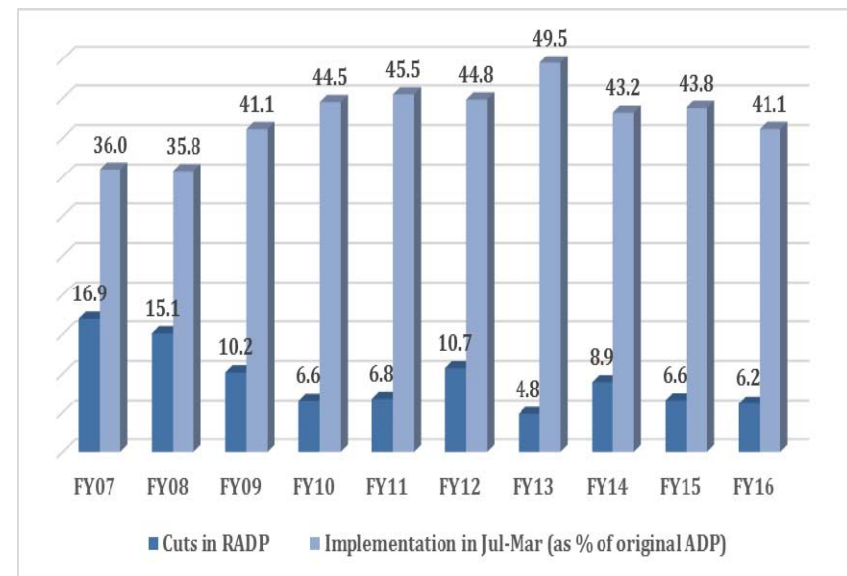
ADP expenditure against allocation is the lowest in recent years

- 41.1 % of original ADP was spent during Jul-Mar of FY15
 - This is the lowest expenditure since FY09
- ADP was slashed by Tk. 6,000 crore (or 6.6%) to Tk. 91,000 crore
- Given the implementation status of ADP, one would expect a higher reduction

Budget deficit remained within limit

- The budget was in surplus of Tk. 609 crore during Jul-Dec of FY16
- The impact of large revenue shortfall was likely to be offset by unutilised budgetary allocation
- Sale of NSD certificates during Jul-Dec of FY16 was Tk. 13,366 crore (Target: Tk. 15,000 crore)
- Financing from foreign sources will face stern challenges in the second half of FY16

Revised ADP, the Cuts and ADP implementation scenario



Inflation came down to reach the target level

- Headline inflation continued to decline in first nine months to 6.10% (Target: 6.07%)
- Food inflation (5.5%) was lower than non-food inflation (7.0%)
 - Lower global commodity prices, stable exchange rate of BDT and restrained growth of broad money supply helped contain inflation
 - Negative remittance growth also played a role in restraining inflation

Growth of monetary aggregates remained close to the targets

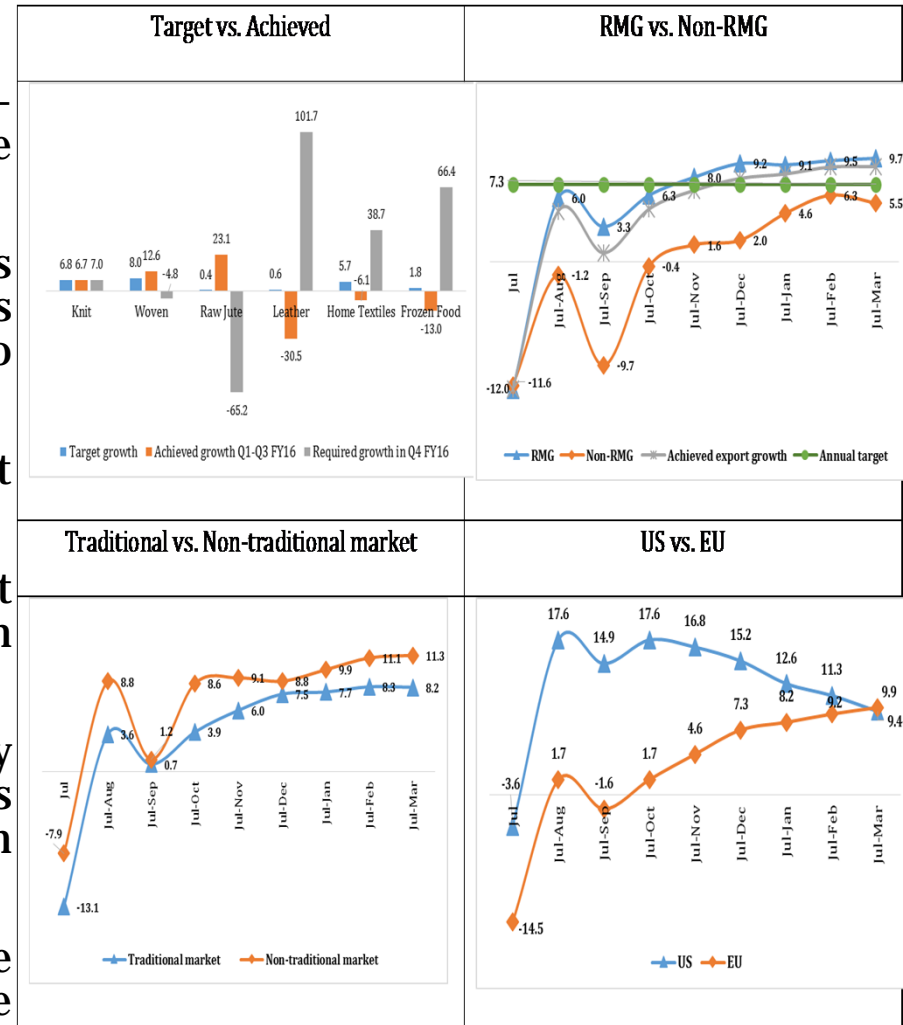
- Private sector credit growth was 15.1% as of Feb 2016 (exceeded the target of 14.8%)- highest since December 2012
 - Thanks to downward revision of repo and reverse repo rates by BB
- Public sector credit had negative growth (-1.9%) due to limited bank borrowing requirements by the government to underwrite fiscal deficit
- The trend in the growth of monetary aggregates, however, was accompanied by strong flow of net foreign assets
 - Net foreign assets posted 25.6% growth as of January 2016 (Target: 11.1%)

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 FY16
 - In February 2016, the real average interest rate on deposits ended up in the negative terrain ((-) 0.1 per cent)
 - Lack of demand for credit flooded the commercial banks with liquid assets and the banks are discouraged to keep deposits
- The fall in bank yields continued to push the 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
- Indeed, in November 2015, BB issued a circular to advise the commercial banks to keep the intermediation spread to a 'lower single digit' (i.e. less than 5 percentage points)
 - Regrettably, in February 2016, 20 among 39 PCBs and six out of nine FBs had interest rate spreads of over 5 percentage points

RMG-led export earnings continued robust growth

- Export registered 9.0% growth during July-March of FY16 (Target:7.3%) – thanks to the robust growth in RMG (9.7%)
- Sign of market diversification was evident as export growth to non-traditional markets (11.3%) marked higher growth than that to the traditional markets (8.2%)
- Among the major traditional markets, export to the US market registered 10.4% growth
- Export growth in the EU market was about 7.5%-mainly driven by robust growth in woven goods (16.8%)
- Bangladesh's export performance was fairly good in economies where the market was relatively stable and economic growth remained vigilant
- Bangladesh's exports may face some preferential market erosion due to exchange rate margin when compared with Vietnam



Import payments rising despite lower capital machineries import

- Import payments increased by 6.4% during Jul-Feb of FY16
 - Driven by imports of consumer goods which recorded a growth rate of 19.2%
 - Payments for importing intermediate goods also increased by 6.4%
 - Import payments for capital machinery declined by (-) 7.5%

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

- Number of migrants (5 lakh) going abroad during Jul-Mar FY16 from Bangladesh surpassed total annual migration (4.6 lakh) in FY15 (53.9% growth)
- During this period, migration to the Middle East grew by 73.3%
 - Key destinations for migrants were Oman and Qatar followed by Saudi Arabia.
- Remittances inflow during July-March of FY16 was USD 11.1 billion which was (-) 1.8% lower than corresponding period of FY15
 - Lower amount of remittance inflow was observed in the case of eight out of the eighteen major markets for Bangladesh during the period

Balance of payment situation remained favourable

- BoP was favourable during Jul-Feb of FY16 (USD 3.1 billion) over the corresponding months of FY15 (USD 2.2 billion)
 - Trade balance was USD (-) 4.06 billion
 - Current account balance stand at USD 2.7 billion during Jul-Feb of FY16 (USD 511 million higher than FY15)– mainly originating from services income
 - Net FDI passed USD 1.4 billion (27.2% growth) during July-February of FY2015 whilst net trade credit was negative at USD (-) 1.2 billion

Foreign exchange reserve continued to rise

- Foreign exchange reserve increased to USD 28.7 billion as of 12 April 2016 (equivalent to 8 months import payment)
- Major share of the foreign exchange reserves was kept as convertible foreign currencies (including securities), and also in the form of SDRs and gold.
- According to WDI data, foreign exchange reserve-to-GDP ratio of Bangladesh was 12.9% in 2014, preceded by Indonesia (12.6%) and Sri Lanka (10.4%).
 - Compared to other Asian economies such as India (15.9%), Vietnam (18.4%), Philippines (28.0%) and Nepal (31.4%)- the reserve size of Bangladesh is not yet disproportionately or unreasonably large

Recommendations for National Budget for FY2017

Major Findings from Web-based Survey

- Budgetary process
 - Distrust for overall budget and implementation process
 - Listen to public opinions and decentralise budget
 - Work on NBR capacity building and ensure effectiveness of tax collection programmes, rather than reducing the target
 - Prepare separate give agriculture budget
 - Implement allocated ADP
 - Ensure transparency and accountability in the budgetary process
- Macroeconomic policy
 - Increase investment, reduce income inequality, create a greater job sector and reduce poverty
 - Instead of increasing taxes, widen the tax payers net
 - Allocate more resources for employment generation for the educated people
 - Reduce tax on necessary goods, education and health, and increase in luxury goods
 - Keep price of fuel, electricity, gas within reach of common people
 - Impose more tax on cigarette and alcohol

Major Findings from Web-based Survey

- **Sectoral measures**
 - Allocate more and improve quality of education and health, IT and research
 - Increase allocation for technical and technological education
 - Establish more public university and address the accommodation problem of students
 - Invest in agriculture, clean and renewable energy and SME
 - Diversify export oriented products
 - Reduce inequality in every sector
 - Improve public transport through specific guidance and more allocation.
 - Increase allocation for agriculture and ensure that the subsidy in agriculture reaches the targeted farmers
 - Explain how scam money in banking sector will be adjusted
 - Modernise railway sector and ensure proper utilisation of land of railway
- **Other institutional measures**
 - Encourage investment of black money in productive sector rather than the in real estate sector
 - Make new VAT law simple for all
 - Focus more on Human Development Index (HDI) rather than on GDP growth
 - Prevent corruption
 - Ensure people's right to information

Weakness is prevalent in the formulation of fiscal framework in Bangladesh

Fiscal projection gap (budget target minus actual outcome) as % of budget target

Indicators	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

- Between FY2009 and FY2016, the gaps between planned and actual targets have risen for almost all components of the fiscal framework.
- Necessary level of allocation to social sectors is unachievable due to resource scarcity and unattained revenue mobilisation targets
- Failure in utilisation of the fiscal space offered by the moderate budget deficit
- Overall, the fiscal framework appears to be designed with built-in over-projection
- Design and implementation of national budget for FY17 needs to reverse this trend
- Fiscal framework should be prepared in a realistic manner. The first step towards this is to revise the fiscal framework for FY2016 in a judicious way

Every year a highly ambitious fiscal framework is proposed which is later revised but the actual realised figures are nowhere near the original targets.

Proposed revision of the fiscal framework by BMRC

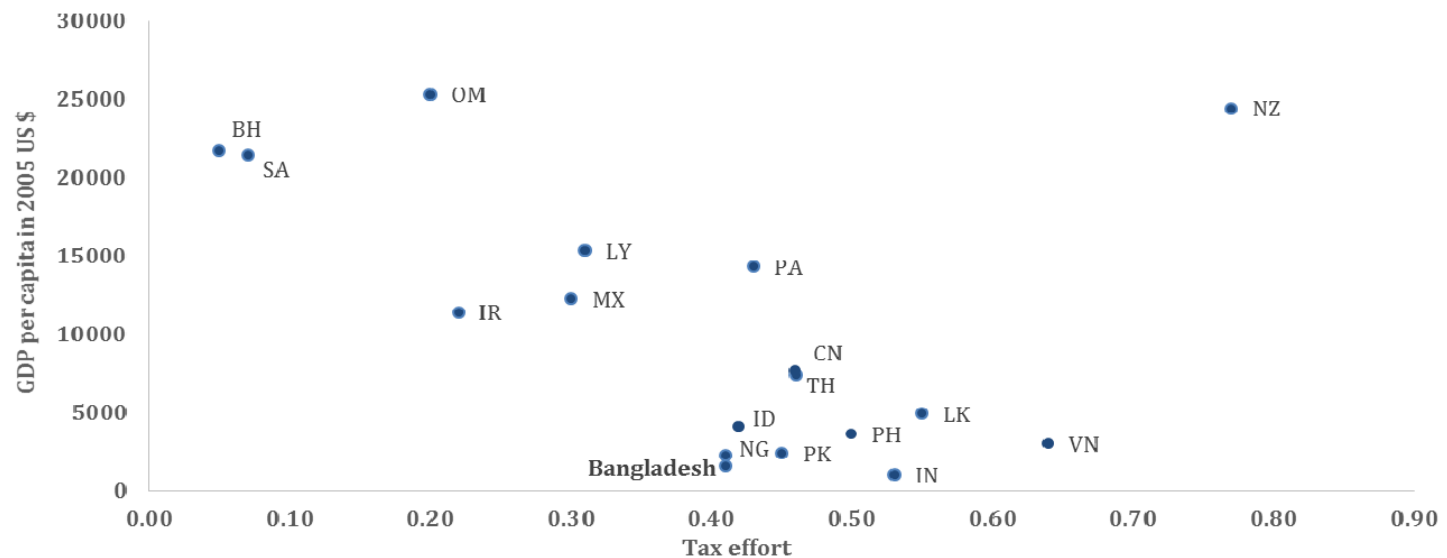
Particular	Crore Tk.					Growth (%)			
	AFY15	BFY16	RBFY16 (p)	BFY17 (p)	Revision in RBFY16 over BFY16 (p)	BFY16 over RBFY15	BFY16 over AFY15	RBFY16 over AFY15	BFY17 over RBFY16
Total expenditure	204,226	295,093	264,500	340,600	30,593 (10.4%)	23.1	44.5	29.5	28.8
Non-ADP	143,987	198,093	173,500	227,600	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

- Envisaged growth targets for FY17 over the revised budget, e.g. revenue collection (37.3%), public expenditure (28.8%) and budget deficit (11.5%), are moderately ambitious
- The final fiscal framework figures for FY16 are likely to be lower than the proposed revised targets
- If the fiscal framework targets for FY17 are set in this manner, the annual growth targets will once again remain unattainable under a business-as-usual scenario
- Two alternative ways to correct this situation. They are:
 - Preparing budget by accepting current reality
 - Setting moderately ambitious targets and put more effort in achieving it
- In the context of Bangladesh, the second option is more desirable
- SDGs should be focused intensively in the upcoming budget

Revenue mobilisation should come through reforms that widen the tax base, increase tax compliance and lower tax evasion

- Tax-GDP ratio (8.5%) is one of the lowest in the developing world (15% average)
- Bangladesh only collects 43% of potential taxable revenue, while other South Asian countries have comparatively higher tax efforts
- The 7FYP proposed increasing tax-to-GDP ratio to 14.1% by 2020

Tax effort and GDP per capita for select countries: Is Bangladesh lagging behind?



Widening the tax base is a top priority.

- The 7FYP has argued that increasing the effective income tax rate to 10% for the top wealth decile (who own 35% of national income) would yield a 2.5 percentage point increase to the current tax-to-GDP ratio
- CPD working paper (forthcoming) shows that the size income taxpayer base and income tax collections have almost doubled and quadrupled respectively between 2005 to 2010
 - Driven by revenue growth in urban and small metropolitan areas and increase in higher income taxpayers.
 - However, income tax efforts remain low as Bangladesh only collected 50 per cent (2010) of potential tax revenue, substantially below income tax effort ratios of comparable economies (e.g. 65 per cent in Uganda and Vietnam)

Government should address need for transparency in declaration of corporate taxes

- Proper implementation of recently enacted Financial Reporting Act should improve transparency and accountability in financial reporting activities
- Government should encourage more companies to be publicly listed

Formalisation of informal labour and small and medium enterprises.

- 87 per cent of the labour force, and 16 per cent of all SMEs, are informal due to lack of formal employment arrangements and high formal registration costs
- Incentives for employers to formalise non-contractual labour could potentially raise Bangladesh's formal employment rate to the developing worlds' average rate and triple the income taxpayer base
- Free business registration for SMEs would increase tax compliance, as formal registration costs account for up to one fifth of their expenditures

Changes to advance income tax (AIT) collection system should incorporate progressivity

- Progressive withholdings-at-source rate would reduce scope for tax evasion at final settlement for high income earners
- Formal registration of AIT withholding entities with the NBR would enable transparency of withholdings payment
 - Integrated identification mechanism would provide information at source regarding all aspects of the taxpayer's finances

Current asset/property taxation laws create scope for tax evasion

- Special tax exemption provisions are currently in place for investments in buildings and apartments for persons with unexplained income sources
- Abolishing special provisions for undisclosed wealth should improve tax compliance (e.g. India's Benami Act 1988)

Low VAT compliance stems from both governmental and business sector shortcomings

- Non-declaration of taxable income, false book-keeping and under-reporting of inventory turnover are widespread
- Business sector identifies high tax administration cost and low computer literacy as key bottlenecks to tax registration and return preparation.
- NBR Modernization Plan addresses reforms to provision of online VAT filing and payment, as well as introduction of ECR
- New VAT law for upcoming budget proposes changes to truncated and package VAT law aimed to improve revenue collection

Tax administration and institutional governance reforms would boost revenue growth

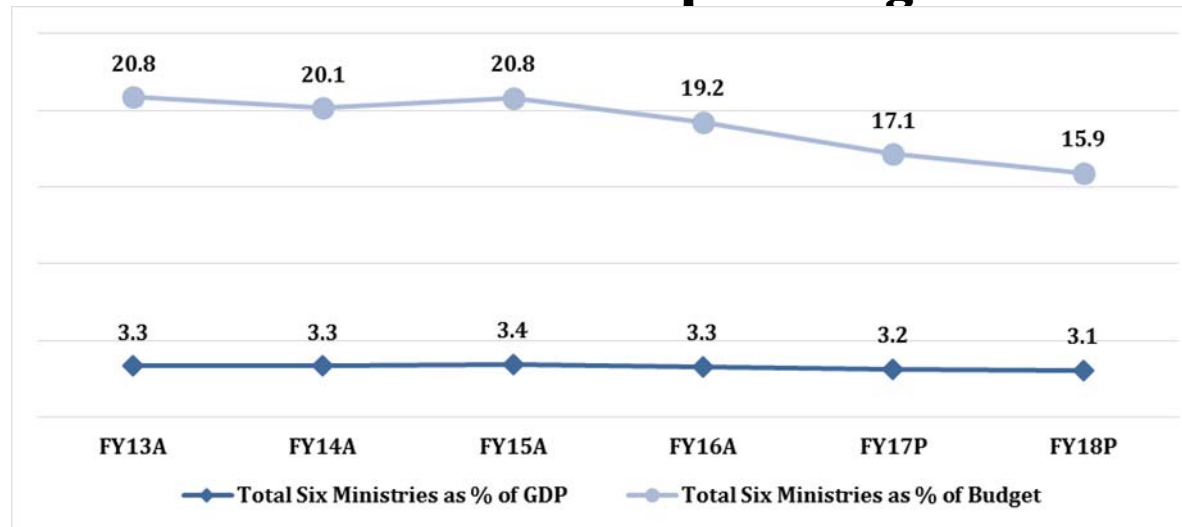
- Improvements to quantity and quality of tax officials through skill development and creation of more tax circles in high-density economic activity areas.
- Increased use of ICT for tax declaration and processing
 - Digital system that processes tax refunds/rebate for overpayment, through which tax concessions could be awarded for timely payment
- Large taxpayer units should be audited more stringently for which NBR auditing capacity has to improve
- Efficient speedy resolution of open cases under the Alternate Dispute Resolution (ADR) system, prioritizing high revenue cases
- Efforts to curb illicit financial outflows by strengthening the Transfer Pricing Cell (TPC) and through appropriate official investigation of the recent Panama Papers scandal

In order to increase revenue mobilisation, CPD recommends:

- Introduction of progressive AIT mechanism
- Increased formalisation of labour, small and medium enterprises
- Digitised tax 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
- Improve property and RMG sector tax compliance
- Efficient, speedy ADR system
- Reducing illicit financial outflows
- Overhaul of NBR institutional bottlenecks (quality of administration, monitoring and punishment of tax evasion, access to tax instruments)

- During FY2011-FY2015, the public expenditure budget was not fully spent annually. Full utilisation of resources will put the economy on a higher growth trajectory
- Budgetary allocation and future projection regarding social sector spending shows a declining trend both as percentage of GDP and of total budget. This is not in agreement with either the 7FYP or the SDG commitments of the GoB

Allocation for social sector as percentage of GDP and budget

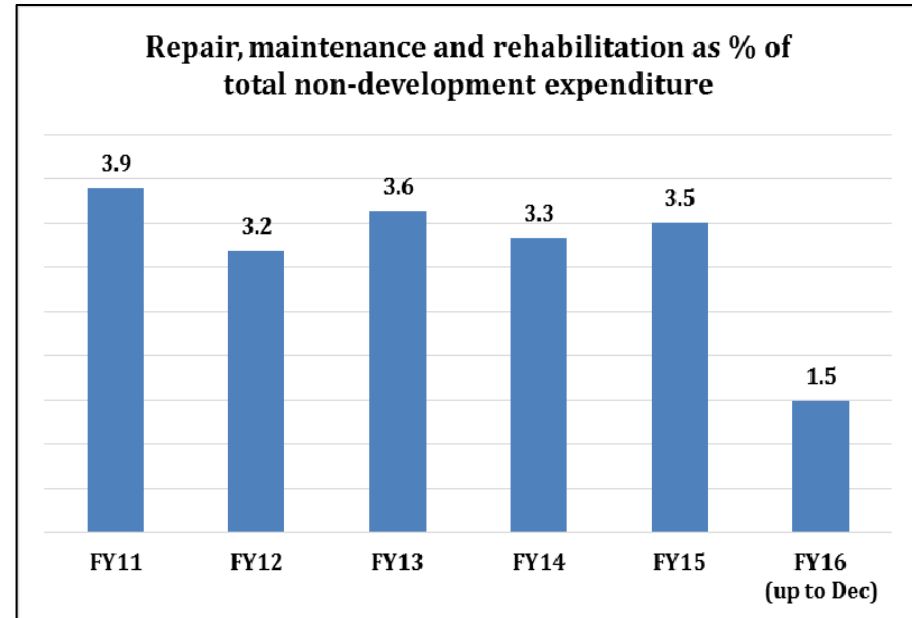


- Excluding government pension schemes, budgetary targets for SSNP spending were not aligned with the proposals of National Social Security Strategy (NSSS)
- These social safety net programmes are inadequate in monetary terms as well as from the coverage point of view

Budgetary allocations and projections vs NSSS targets of major safety net programmes (Taka in crore)

Programmes	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
Child School (Primary+Secondary) Stipend	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

- In view of the increasing expenditure on new physical infrastructure, allocation of funds for infrastructural maintenance should be correspondingly increased. From FY2011 onward, the share of repair, maintenance and rehabilitation in total non-development expenditure has showed a generally declining trend



- Reorganizing and raising expenditure particularly for the social sectors, including social safety net programmes for marginalised people, will help the government both in the short and medium term
- In this context, the government should not be feel compelled to maintain the budget deficit within 5% of GDP

- Despite the low level of international petroleum prices and consequent profits made by BPC, revenue concerns apparently held the government back from making any downward adjustment of administered petroleum prices.
- As of now, there is regrettably 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.).
- Although there is no subsidy requirement for BPC now, subsidy demand for electricity has remained persistent.
- Recently the government has announced that it will reduce petroleum prices in a phased manner. At the same time, an upward adjustment of electricity and gas prices are also being considered.
- The adjustment of petroleum prices should be calibrated by taking into account 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.
- 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.

- The key challenges in project implementation can be identified as:
 - Land acquisition
 - Preparation of work plan
 - Frequent changes in schedule rates for construction and recruitment of consultant/firm and manpower
 - Frequent change of project directors
 - Procedural lapses which begin with delays in the approval of projects
 - Post-approval procedural delays in land acquisition and procurement
- Implementation of ADP projects, in a timely manner and within initial cost estimates, continue to be problematic. In FY14 only 14.2% of the total 'to be completed projects' were actually completed within the stipulated time and planned allocation. About 48.9% of the completed projects experienced time overrun, causing a 51.1% increase in the average cost of all completed projects.
- Financial accounting in the form of expenditure does not necessarily mean actual implementation. An ongoing CPD study found that on an average 66.2% of completed projects were declared as completed without 100% physical progress during the FY2001-2015 period

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. This new provision and the attendant costs need to be reflected in the upcoming national budget. A number of proposals announced last year by the Planning Minister but not being adequately followed up
 - appointing PDs through direct interviews
 - assigning a dedicated official in each government agency for M&E
 - delisting the longstanding 'non-operational' projects
- Proposals and recommendations brought forth by the Ministry of Planning and IMED were not adequately followed up. It is recommended that the upcoming budget report progress and reflect on these issues

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

- A special task-force needs to be formed which would closely monitor implementation of growth-enhancing infrastructure projects. It is also important that adequate funds for these projects are allocated in the forthcoming ADP

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

- Special attention needs to be given to important large social sector projects through adequate fund allocation in the budget for FY2017. Furthermore, these project objectives will have to be redesigned and aligned with the SDG targets

Separate strategy for foreign-aided projects needed

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

Monitoring and evaluation mechanism needs to be strengthened

- Project Completion Reports (PCR) are important to assess implementation of a particular project. PCRs should be made public to ensure transparency. Low quality of the PCRs submitted and the lack of needed human resources (as per IMED organizational structure) often do not allow proper evaluation of completed projects. An inter-ministerial committee could be formed to address these issues.

In view of the increased volume and change in the composition of public expenditure, there is an urgent need to raise efficiency. In this context, CPD had earlier urged for the establishment of an independent Public Expenditure Review Commission (PERC). The core responsibilities of proposed commission will include:

- Reviewing the efficacy of programmes/schemes and proposing appropriate recommendations for improving efficiency.
- Developing a framework for performance and outcome monitoring.
- Reviewing the scope for consolidation of smaller schemes and expenditure items with common/complementary objectives.
- Suggesting measures to address inconsistencies and inefficiency in public expenditure.
- Ensuring data accountability.
- Examining economic rationale and cost-benefit analysis for proper subsidy management.
- Suggesting areas for adoption of new technologies for effective implementation of programmes and delivery of services.
- Recommending suitable measures for optimising and enhancing the staff strength of government departments.

- Over the past few years, significant change in the sources of budget deficit financing has been observed.
 - Net financing from foreign sources (including grants) remained low (only 0.4 per cent of GDP) in FY2015 due to low level of project aid utilisation in the ADP.
 - Among domestic sources, sale of NSD certificates has emerged as the single largest contributor.
- Individuals prefer to save using NSD instruments as rate of return from the NSD is significantly higher compared to banking sources (i.e. interest income).
- In view of the current scenario, it would be advisable for the government to balance the borrowings from bank and non-banking sources.
- Since many small savers take advantage of the schemes, lowering of the maximum purchase amount, rather than bringing down the savings certificate rates, could be the preferred policy option.
- 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.

a. Proper Assessment of Fiscal Measures Needed

- National budget offers various fiscal measures targeting different groups
 - Lack of proper pre and post-impact assessment makes it difficult to appreciate such measures in terms of adequacy, benefits, timeliness and economic impact
- There should be comprehensive ex-ante and ex-post analyses of the various measures
 - Such exercises will help identify fiscal measures that are most appropriate to address the developmental challenges facing the country
- Proper assessment is needed to analytically determine the levels of ERP required for the development of local industries
 - Assessments could be carried out by NBR in association with the BTC for which necessary human resources and technical support will have to be made available

b. Support Needed to Make Small Businesses Tax Compliant

- Majority of SMEs are not tax compliant - not registered with appropriate authorities; do not have TIN or have VAT registration
 - Small entrepreneurs do not maintain proper accounting system which is an essential pre-condition for compliance under the new VAT Law
- NBR should develop a proper work plan to encourage SMEs to get registered and undertake all necessary preparations in light of the new VAT law

Following suggestions emerged from a pre-budget dialogue organised by CPD in Bogra city in the context of the upcoming National Budget for FY2017:

- **Special efforts needed to formalise SMEs**
 - Lack of formalisation often does not allow these SMEs to enjoy fiscal incentives; then again, under the proposed new VAT Act these were likely to face legal difficulties
- **'Customisation' of Financial Products for better access to finance**
 - Banks should identify innovative and 'customised' (flexible) financial products to reach potential SME clients
- **Support organisation of unorganised entrepreneurs**
 - Challenges faced by regional SMEs will be difficult to address in the absence of cluster-based association/groups
- **Support for development of 'customised' infrastructure**
 - Regional SMEs need more 'customised' infrastructure for more economically viable operation of their supply chains
- **Overcoming challenges to raise competitiveness**
 - Need for supportive measures and incentives to raise productivity, quality and standard
- **Developing women entrepreneurship**
 - Women entrepreneurs at regional level face formidable difficulties in setting up enterprises and in getting access to special credit facilities

Fiscal and Budgetary Reforms

- ❑ Competitiveness and distributive justice through 'second generation reforms' higher levels of transparency and independence of regulatory bodies are needed to generate efficiency.
- ❑ Bangladesh lags far behind in terms of international standards for compliance with regards to transparency in the budgetary processes - only 12 out of 76 standards in the process of implementing national budget are being met
- ❑ Transparency could be achieved through five key aspects –
 - ❑ Clarity and openness about the budget decision-making process and the underlying constitutional or statutory authority;
 - ❑ Public disclosure and distribution of budget information;
 - ❑ Detailed reporting of budget expenditure/revenue;
 - ❑ A comprehensive scope, accounting for assets and liabilities, targets, projections, performance measures and structural balance; and
 - ❑ Budget integrity, control and accountability, and budget forecasting and projections

Disclosure of Financial Accounts of SoEs

- ❑ Lack of clarity exists in detail accounts of income, expenditure, profit/loss, debt, liability and asset etc. of the 29 SoEs
 - ❑ Financial Accounts need to be made public in a transparent manner
- ❑ **BPC:** Financial position has further improved in FY2016 due to the falling fuel price in the global market
 - ❑ Transparency is needed for better price adjustment policy along with allocation of major benefit to farmers, transport users, producers, exporters and consumers
- ❑ **BJMC:** Detailed financial account including the assets and liabilities, debts and dues, and its accounting practices need to be publicly available
- ❑ Other SOEs should also disclose their financial accounts and management practices in a transparent manner

Transparency in Government's Asset Acquisition

- GoB has spent Tk.14,477 crore for investments in recapitalisation of nationalised commercial banks over a period of three years with a view to help the NCBs meet respective capital shortfalls
- This type of periodic rescue will hardly address the root causes. In this context, CPD has been persistently arguing for setting up a Financial Sector Commission with the intention of correcting the emergent situation

Non-development Capital Expenditure (crore Tk.)

	Budget 2015-16	Revised 2014-15	Budget 2014-15	Actual 2013-14
<i>Acquisition of Assets and works</i>	8,038	8,231.00	7,025	5,607
Acquisition of Assets	6,683	6,456	5,763	3,857
<i>Investments in Shares and Equities</i>	11,950	13,797	18,985	4,834
Investment for Recapitalisation	5,000	5,000	5,000	4,477
Total -Non-Development Capital Expenditure	19,988	22,028	26,010	10,441

Source: Ministry of Finance, GoB

Transparency in Defense Budget

- ❑ The reporting mechanism concerning defense spending in Bangladesh is highly non-transparent
 - ❑ During FY10-FY15, actual spending on defense was found to be significantly larger than the budgetary allocation of the respective year
- ❑ Pattern of defense spending indicates better capacity in utilizing the budget by concerned bodies
- ❑ Questions about allocative efficiency remain a concern at a time when social sectors are failing to meet the targets for lack of resources
- ❑ Transparency in the defense budget is needed to bring clarity to the overall budgetary procedure

Trend in Defense Spending in Bangladesh (in Crore Tk.)

FY	Allocation/ Disbursement		Difference	
	Budget	Actual	Revised - Original	Actual - Original
2009	6644.9	6251.5	+240.6	-393.4
2010	7051.4	8471.6	+823.7	+1420.2
2011	9175.6	10222.4	+143.9	+1046.8
2012	11246.8	12218.4	+965.9	+971.6
2013	12886.1	12988.4	+616.5	+102.3
2014	14457.1	18330.8	+722.9	+3873.7
2015	16462.1	17484.6	+1308.0	+1022.5

Source: calculated from Ministry of Finance data

Transparency in Local Government (LG) Financing

- ❑ LG financing lacks detailed information, a consistent pattern in central government transfers to LG, and a transparent way of resource allocation among the different LG departments
 - ❑ A *separate budget for LG* to reflect the local needs and demands
 - ❑ Proper clarification as regards the fate of *District budget* and
 - ❑ Establishment of a *permanent 'Local Government Finance Commission (LGFC)'* to ensure proper devolution of power, appropriate financing for LG self-sufficiency

Transparency of NGO Financing

- ❑ Development activities of the NGOs and the involved resources are not properly reflected in the national budget
 - ❑ Total official assistance going to non-government sector rose from 20% in FY15 to 26% in FY16
- ❑ 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

Transparency in South-South Transactions: Case of Indian LoC

- ❑ South–South development finance often face the challenge of lack of a guiding framework within which these transfers take place.
 - ❑ No clearly defined central reporting takes place and the transactions are made on an ad hoc basis.
 - ❑ Concern regarding consistency and quality assurance of the projects undertaken with these funds
- ❑ DPP and TPP of the projects financed by LoC should be made available to the policymakers and other stakeholders to enable adequate analysis of the economic impact of LoC deals
 - ❑ Quarterly monitoring and evaluation reports should be prepared - need to set up a central reporting system.

B. Economic Reforms

a. Commission for Financial Sector Reform

- ❑ Recent financial scams, particularly concerning the NCBs, rising NPL, quality of outstanding loans and declining profitability are some major concerns in the banking sector at present.
- ❑ Central bank cyber-heist, ATM fraud added a new dimension to financial sector governance
 - ❑ The way licenses for new banks are issued have also given cause for concern.
- ❑ CPD has proposed setting up an Independent Financial Sector Reform Commission (IFSRC). Commission may look into following issues -
 - ❑ Preparing guidelines and making 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.
 - ❑ 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.

Enforcement of Public Service Act 2015

- ❑ Clear guidelines are needed in a number of areas including establishment of proper mechanism for performance appraisal and digitalization of public service provisions.
- ❑ Design of evidence-based rules for performance appraisal, provision of good practice based rules on digitalization of public service provisions, proposals for reorganization and rationalization of public offices are necessary.

Enforcement of 'Financial Reporting Act'

- ❑ After the Act was passed by the Parliament no visible progress has been made.
- ❑ 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.

Setting up Statistical Commission

- ❑ An independent statistical commission to validate the macroeconomic correlates.

Enactment of New/Amended Laws, Rules and Acts

□ A number of investment, commerce and business related policies need to be amended and updated to make them functional, modern and effective in both current and future contexts.

□ **Act:** 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 and Inland Shipping Act, 1976, Weight and Measurement Act, 1961, Acquisition and Requisition of Immovable Properties Act, 1982.

□ **Law:** Business Organization Act, Anti-Dumping and Countervailing Act etc.

□ **Rules and regulations and Polices:** rules for Investment Act, Port rules, PSI Order 2000, Import, Export and Indentors' Registration Order 1979, Patent and Design rules, Pre-shipment Inspection Order 2000 and Import, Export and Indentors' Registration Order 1979, Coal Policy and Shipping Policy.

Operational Reforms

- ❑ Large gap between adopted policies/rules/regulations and their implementation at the business level
 - ❑ These incentives are neither in acts/laws, nor is there any binding requirement to provide these services to the entrepreneurs
- ❑ Proper implementation of different rules/regulations/policies should receive due priority from relevant public institutions
- ❑ Clear division of focus and labour between BIDA (previously BOI), BEPZA, BSCIC, BEZA and different local authorities; at the same time there is a need for greater coordination among these entities
- ❑ MoI should act as a repository of industry-related information, providing technical support and ensuring business facilitation
- ❑ Govt. should conduct a serious rethink about the future of the loss-making SoEs.
 - ❑ Independent studies should be carried out to examine the various options in this regard including land usage
- ❑ In order to better facilitate the workings of the private sector, it is important to set up a Commission to identify institutional bottlenecks at both micro and macro levels

Concluding Remarks

- Budget framework for FY2017 has to be more robust by setting the targets based on more realistic revised budget figures of the elapsing year
- Stronger efforts not only in financial resource mobilisation, but also in appropriate utilisation of the mobilised resources from both domestic and external sources
- Restructure public expenditure in favour of human development sectors and towards promoting social protection schemes
- Recommendations for resource mobilisation include 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
- 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

- Transparency in budget making process is critical –
 - Implementation of Financial Reporting Act
 - Presentation of detailed financial accounts of the SoEs
 - Disclosure of details of projects financed from non-concessional loans
 - More sunshine on defence economy
 - Linkages of NGO finances with government spending
- Reforms in a number of new areas –
 - Financial Reforms Commission
 - National Statistics Review Committee
- Emphasise implementation of existing reform agenda
- Put in place built-in safeguards for possible adverse impact emanating from the global economy



Thank You