Independent Review of

IRBD

Bangladesh's Development

বাংলাদেশের উন্নয়নের স্বাধীন পর্যালোচনা

State of the Bangladesh Economy in FY2020-21

Third Reading

Dhaka: 31 May 2021

CENTRE FOR POLICY DIALOGUE

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- The *CPD IRBD 2021 Team* alone remains responsible for the analyses, interpretations and conclusions presented in this paper.

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Section I. Introduction

Introduction

- This report has been prepared in the context of the unprecedented impact of the ongoing COVID-19 pandemic on the economy of Bangladesh since March 2020.
- Though many had expected the wrath of the pandemic to fade away towards the first quarter of FY21, it has resurfaced in the third and fourth quarters of FY21.
- This has reiterated the need for designing the upcoming national budget for FY2022 to be presented by the Finance Minister on 3 June 2021, keeping in mind the new challenges that have emerged and are apprehended to emerge.
- The Centre for Policy Dialogue (CPD) has been emphasising right from the beginning for medium-term policy measures to address both the immediate and medium-term challenges faced by the economy due to the pandemic.
- Since March 2020, CPD has undertaken several empirical and survey-based research on the impact of the pandemic, various aspects of the government support measures to tackle the pandemic and made evidence-based sector-wise specific policy recommendations.
- CPD has also made concrete suggestions to the Finance Ministry as well as to the National Board of Revenue prior to the national budget for both FY21 and FY22.

Section II. Macroeconomic management

Public Finance

- ***Despite exhibiting signs of improvement, the annual revenue mobilisation target is unlikely to be attained***
  - There is a turnaround in tax collection - 10.5 % during the July-April FY21 as opposed to (-) 9.3 % for the corresponding period of FY20)

- Non-tax sources posted an impressive growth (29.9 %)
- Total revenue mobilisation recorded 13.4 %growth during the first ten months of FY21 against the annual target of 43.7 % - will need to grow by an astounding 122.8% in the remaining two months of FY21!

Revenue mobilisation scenario during Jul-Apr FY21

Particulars	Growth (in per cent)			
	Annual Target	Jul-Apr FY20	Jul-Apr FY21	Required May-Jun FY21
Tax revenue	56.3	-9.3	10.5	182.2
Non-tax revenue	-21.9	36.4	29.9	-127.3
Total revenue	43.7	-4.5	13.4	122.8
Foreign grants	105.1	-45.3	-69.7	120.8
Total revenue and grants	44.1	-4.6	13.3	122.8

❑ *Weak implementation of public expenditure continues*

- Up to April FY21, implementation rate of total public expenditure was 42.0% - marginally lower than last year (43.9%)
- Such low levels of budget implementation when the economy is ravaged by the adverse impacts of the pandemic, and is experiencing a second wave, is a matter of grave concern
- It reflects both weak programming of the budget as well as weak administrative capacities in the area of budget execution

Implementation status of public expenditure

Particulars	Implementation rate (in per cent)	
	Up to April FY20	Up to April FY21
Operating activity except loan	50.4	50.2
Loans and advances (Net)	-426.6	-58.5
Development activity	33.2	29.0
Net food operation	2,286.0	683.2
Total expenditure	43.9	42.0

❑ *ADP expenditure remains sluggish*

- As per IMED data, only 48.7 % of the original ADP allocation was utilised during the July-April period of FY21
  - Implementation rate of the 'Taka component' of ADP was 49.4 %, while that of 'Project Aid' amounted was 47.5 %
- Pace of implementation remains the lowest in the Health Services Division among the top ten ministries/divisions, with only a rate of 31.3 %during the July-April period
- Given the increased pressure on the public health service sector in view of the COVID-19 pandemic, the current scenario is in stark contrast to the citizen's expectations and the realities of the demands on the ground

Public Finance

- ***Budget deficit is likely to be within the programmed limit***
  - During July-April FY21, the overall deficit (including grants) 42 % lower than the corresponding figure for the July-April period of FY20
  - While the revenue collection during the July-April period of FY21 recorded a double-digit positive growth rate, the public expenditure did not increase in a corresponding manner
  - High net sales of NSD certificates had largely financed the major part of the budget deficit till April, 2021 - 69.2 % growth
  - Use of net foreign financing also improved as a source of deficit financing in FY21
  - The debt-GDP ratio of Bangladesh was 35.9 per cent at the end of FY20
  - There should be ample scope for the policymakers to pursue an expansionary fiscal policy in view of the pandemic

Industrial production

- ***Growth in industrial production was subdued, especially for small industries***
  - During the July-December FY21, the growth rate of QIIP for large and medium industries was 5.7 % - 14.3 % for the same period of FY20
  - A substantial fall was observed in the growth rate of QIIP (1.8%) for small scale industries - 10.6 % for the same period of FY20
  - This is indicative of the slow pace of recovery in manufacturing and industrial production
  - A drastic difference is discernible in the rate of recovery across the sectors
    - Production of textile and apparels, two of the largest manufacturing industries, registered negative growth rates of (-) 5.2 % and (-) 7.2 %, respectively
    - In contrast, production of leather and associated products registered an extraordinary growth rate of 32.6 %, despite the negative growth of export earnings to the tune of (-) 6.2 % during the corresponding period

Inflation

❑ *Food inflation is creeping up*

- General inflation at the national level remained somewhat stable during the first ten months of FY21
- FY21 started with a food inflation of 5.43 % at the national level, which gradually crept up to 5.73 % in April FY21
- In contrast, non-food inflation at the national level decreased to 5.22 % in April FY21 from 5.79 % in July FY21
  - Within non-food items, inflation related to medical care and health expenses increased to 8.64 % in April FY21 from 7.47 % in July FY21
- Rising trends in food inflation and that related to healthcare is worrisome, particularly in view of the ongoing COVID-19 pandemic, as these are expected to adversely impact the low-income population disproportionately

Monetary aggregates

❑ *Private sector credit did not pick up despite stimulus packages*

- Industrial term loan: (-) 30.8% lower during H1 of FY21
- Loans to SMEs: (-) 0.3 % during H1 of FY21
- Agricultural credit was on a decline throughout the fiscal year and recorded a 9.6 % growth during July-February of FY21
- Non-farm rural credit: (-) 2.2 % during July-February of FY21
- Despite average interest rate on lending being at a historical low point (7.5%), private investment did not pick up

Growth of monetary aggregates (in %)

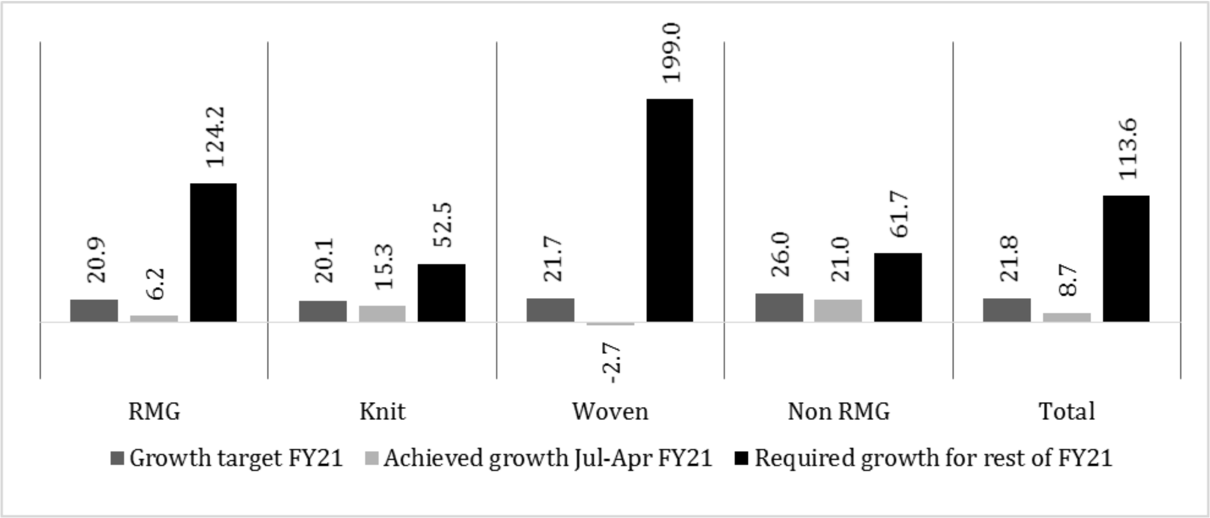
Indicators	Mar 21	Jun 21 (Jul 20 MPS target)	Jun 21 (Revised target)
1. Net foreign assets	29.7	5.8	20.1
2. Net domestic assets	8.7	18.3	13.6
2.1 Domestic credit	11.4	19.3	17.4
2.1.1 Credit to the public sector	28.3	44.4	31.7
2.1.2 Credit to the private sector	8.8	14.8	14.8
3. Broad money	13.2	15.6	15.0
4. Reserve money	11.3	13.5	13.5

External sector

❑ *A limited scale rebound is observed in export earnings*

- Total export earnings increased by 8.7 % during the July-April period of FY21 against the annual growth target of 21.8 % - likely to remain significantly below the pre-pandemic level of $40.5 billion
- Estimates carried out by the CPD indicates that the share of Knit-RMG export in total export has been on the rise, which is a positive structural change in terms of domestic value addition component

Current scenario of export (July-April FY21)



CPD (2021): State of the Bangladesh Economy in FY2020-21 (Third Reading)

External sector

- ***Some turnaround is noticed in the import payments scenario***
  - Growth of import payments reached 6.1% in Jul-Mar FY21 which was (-)4.8% in same period last year - primarily driven by intermediate goods
  - More than 77% of the incremental payments were made against imports of intermediate goods, thanks to crude petroleum and petroleum products which contributed almost entirely to the incremental growth of total imports
  - Given the declining food stock situation in Bangladesh, payments for food grains import increased by 20.9% during the July-March period of FY21
    - Mainly due to a whopping 3059% growth in rice import
  - However, import payments for capital machineries declined by (-) 12.8%
  - It is to be noted that, during the same period of the previous fiscal year, capital machinery declined by (-) 30.6%
  - This, once again, points towards the depressed investment scenario prevailing in the backdrop of the pandemic

External sector

- ***Surplus in overall balance and continued rise in foreign exchange reserve attributable to phenomenal inflow of remittances***
  - Current account had a surplus of USD 0.1 billion during Jul-Mar FY21
    - *thanks to extraordinary remittance inflow (35.1 % growth in 10 months)*
  - Regrettably, net FDI inflow has fallen by (-) 8.0 % during Jul-Mar FY21
  - Overall balance recorded a surplus of nearly USD 7.0 billion - only USD 0.6 billion for the corresponding period of FY20
  - Foreign exchange reserves reached USD 45.0 billion at the end of April 21
  - Exchange rate of BDT against USD remained stable throughout the July-April period of FY21 thanks to periodic interventions by the Central Bank

Policy Recommendations

- ***The trends of macroeconomic correlates in FY2021, as have been presented above, unveil a number of contrasting developments***
  - **First,** although growth in revenue mobilisation started to pick up, pace of public expenditure in FY21 failed to do so
    - This slow pace of public expenditure can be attributable to a number of attendant factors, viz. design, execution and quality
  - **Second,** in terms of growth in industrial production and manufacturing, small industries were lagging behind their large and medium counterparts
  - **Third,** food inflation was on the rise, while the opposite was true for non-food items
  - **Fourth,** although positive developments were observed in cases of export earnings, remittance inflow and foreign exchange reserves, disquieting trends were evident as regards overseas migration, import of capital machineries and FDI inflow

Policy Recommendations

- ***Underlying micro-level trends in the economy***
  - Regrettably, barring one BBS telephonic survey, no other government effort was visible to capture such dynamics
  - This lacuna in the data ecosystem was somewhat bridged by independent actors, researchers and academia
  - Major observations include:
    - While people lost their jobs due to COVID-19, the majority were able to be reemployed - many had to shift from services sectors to agricultural jobs
    - Their income and working hours did not restore to the pre-pandemic level
    - Downward adjustments in the consumption and saving pattern of people
    - Indication of a significant rise in both the poverty rate and inequality
    - Structural transformation, both in terms of employment generation and rural-urban migration, was contradictory to what was expected, defying the concept of progress towards modernisation of the economy

Policy Recommendations

❑ *Major consensus*

- Four sectors that require additional and particular attention - health, social protection, agriculture and small and medium industries
- Instead of focusing on economic growth, more emphasis should be given to saving human lives and livelihoods
- Overall use of fiscal instruments in terms of policy response was inadequate
- Design of the stimulus packages did not take cognisance of the needs of the people most distressed (e.g. small entrepreneurs)
- Policy responses by the government were mostly deployed through the traditional channels – despite having some innovative in distribution of relief packages
- Prevailing weaknesses in traditional channels and failure to comprehend local contexts oftentimes resulted in ineffective delivery of policy supports

Policy Recommendations

- ***Take cognisance of the possible impacts of the second wave of the COVID-19 pandemic***
  - Existing trends and evidence as presented by both public and independent sources need to be utilised to design the path towards recovery
  - Formulate a national budget that fully recognises the economic damage inflicted by the pandemic as well as its long- and medium-term implications
- ***Formulate a medium-term recovery plan***
  - Instead of designing a COVID-specific budget, the government largely opted for a business-as-usual one in 2020
  - Assumption was that managing the fallout from COVID-19 will be easy, and the economy will bounce back within a short period in FY21
  - Recovery from the entire fallout will take much longer than expected - susceptible to changes in the nature of COVID-19 and the availability and effectiveness of vaccines
  - Government needs to formulate a medium-term recovery plan

Policy Recommendations

❑ *Focus on equity and redistribution, not economic growth*

- The national budget for FY22 should focus more on equity, redistributive justice, protecting jobs and saving lives, and less on economic growth
- Attaining a high GDP growth should not be what the budget for FY22 should set its target on
- Rather, the budget should be one of redistribution, particularly addressing the underlying factors driving rising inequality
- Although the BBS has not yet released the final GDP growth data for FY20 and provisional estimates for FY21, it is likely to be lower than the target despite positive growth in the per capita income
- For a change, the budget should set targets as regards employment and growth in income at the household level rather than GDP growth or per capita income

Policy Recommendations

- ***Pursue an expansionary fiscal policy in FY22***
  - **First,** revenue collection should be raised in FY22 by not introducing new taxes but by curbing tax evasion, black money and illicit financial flows
    - Strategic support measures should be extended to domestic market-oriented industries with a view to diversifying the economy
  - **Second,** the sectoral prioritisation for public expenditure is critical in the budget for FY22
    - As discussed earlier, four sectors viz. health, social protection, agriculture, and small and medium businesses, should receive priority in budgetary allocation
    - In addition to these, sectors related to education and employment-generating public work programmes should also receive due attention
  - **Third,** expediting the implementation of ongoing projects under the ADP which are closer to completion should receive the highest priority
    - The high priority projects should be monitored closely on a regular basis

Policy Recommendations

❑ *Pursue an expansionary fiscal policy in FY22 (Contd.)*

- **Fourth,** time has come to make significant investment in strengthening administrative preparedness and raising institutional capacity and line Ministry capacities to implement the budget in due time, within stipulated cost and with good governance
- **Fifth,** value for money and good governance need to be ensured in order to fully realise the synergistic effects of the policy measures
  - Overpriced projects and rampant corruption in public procurement should not define expansionary fiscal policy and nepotism in implementing social safety net programmes should also be addressed
- **Sixth,** the medium-term debt scenario should enable Bangladesh to provide the much-needed policy space to pursue an expansionary fiscal policy
  - The high level of excess liquidity in the banking system will be able to provide residual financing for a higher budget deficit
  - Foreign financing should be prioritised to underwrite

Policy Recommendations

❑ ***Put supportive macroeconomic and sectoral policy measures in place***

- Redesigne the stimulus packages, taking cognisance of their weaknesses and past implementation experiences
- Continuation of the tax-exemption facilities in view of the pandemic, such as on PPE and medicines, should also continue in FY22
- Continue the two per cent incentive on Price volatility of essential commodities must be controlled
- As part of sectoral policy measures, promotion of agricultural diversity should receive continued and expanded
- As there are rising concerns as regards the food-stock situation, adequate food-stock must be maintained through imports considering the amount procured through domestic procurement

Policy Recommendations

❑ *Enhance institutional capacity and collaborative efforts*

- For attaining the inclusive development agenda, the benefits of the taken policies should reach the doorsteps of the marginalized
- For the policies to provide the expected outcomes, the institutional capacity of the institutions must be enhanced
- In the previous budget, selected non-state actors were given the responsibility of distributing the stimulus packages
- In redesigning the stimulus packages and their disbursement, other non-state actors should be made party to the process
- Involvement of non-state actors can bring in important dimensions and perspectives in case of designing the stimulus packages, their delivery and monitoring processes
- This is particularly important from the vantage point of addressing the demands of the marginalised groups

Policy Recommendations

❑ *Do not undermine medium-term reform agenda*

- Without addressing the reform agenda, the underlying weaknesses in fiscal framework and implementation of the budget will not be feasible
- CPD has been drawing attention to this in successive IRBDs. A viable completion timeline should be chalked out in the FY22 budget for reforms that are under consideration – Customs Act, Direct Tax Act and others
- At the same time, efforts towards raising the ease of doing business and improving the investment climate should be put into high gear
- The pandemic should be no excuse in this connection, rather these steps are essential for building back better

Section III. Food price volatility during COVID pandemic period: Need ‘beyond business as usual’ public policy interventions

Introduction

- In view of the ongoing covid-pandemic, food price volatility has emerged as major concern in Bangladesh
  - Global food market has experienced a complicated situation during the COVID pandemic due to the dual risks caused by health and economic risks
  - The challenges included logistic problems in marketing of agricultural products, health risks facing farm workers, adverse weather condition in some key food exporting countries, panic buying by consumers, hoarding of staple foods and export bans and restrictions put in place some of the traditional food exporting countries (ADB, 2020)
- Bangladesh's domestic market was influenced by a number of other, internal, factors
  - These include challenges in implementing government's procurement programme, and timely import of food items and food grains
- This section discusses the volatility in food prices in domestic retail market
  - Factors responsible for price volatility

Trends in prices of consumer goods during pre-covid and covid period

- An overall increase in the price of all consumer goods is discernible in international and local markets during the covid period
  - Since August, 2020 when the global economy started to bounce back following the first wave of covid pandemic, the demand for food products at global the level started to rise in tandem
- Between pre-covid and covid period, global price for rice, wheat, palm oil, soybean oil and sugar had increased by 27%, 42%, 83%, 64% and 26% respectively
  - Domestic retail prices of rice, wheat, palm oil, soybean oil and sugar have increased by 26%, 16%, 40%, 63% and 25% respectively
- In the backdrop of fall in income of the consumers during the pandemic period, the rising food prices had led to an erosion of purchasing power
  - with concerning deterioration in nutritional intake of the poor, marginalised and low-income households

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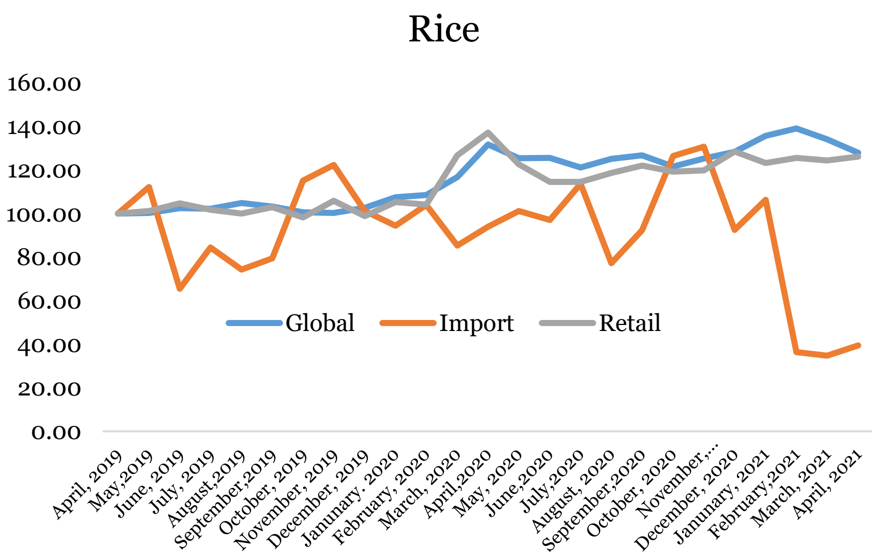
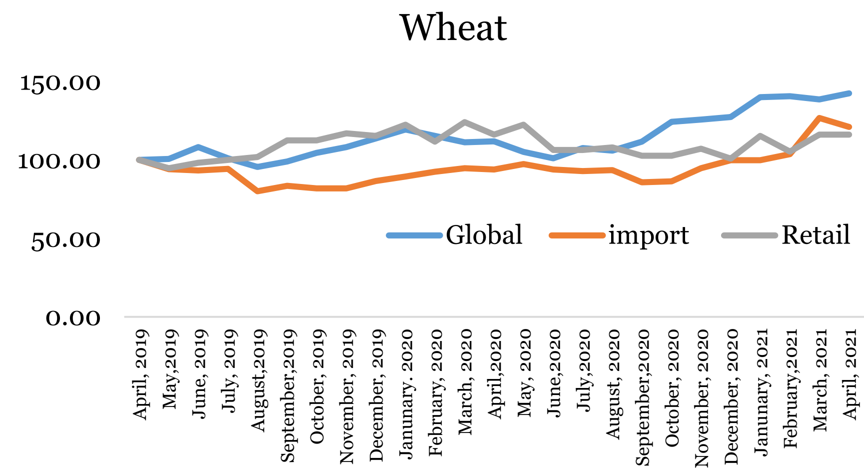
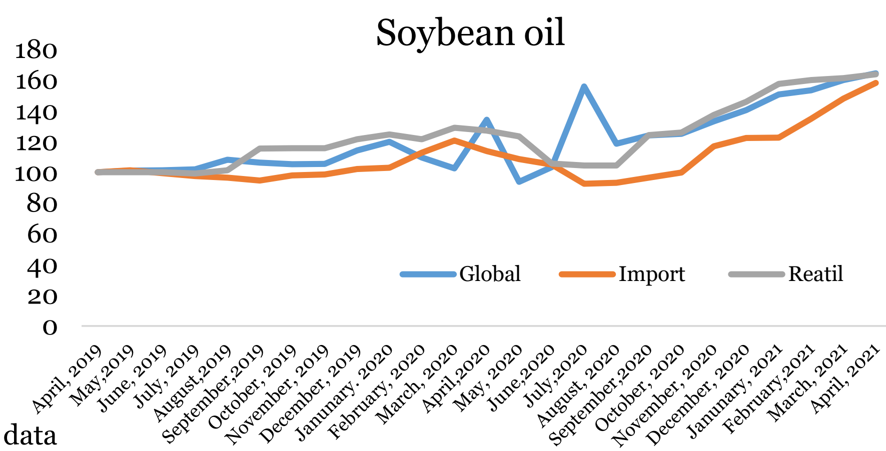
Trends in prices of consumer goods in domestic and international markets during pre-covid and covid period

Trends in food prices during pre-covid and covid periods







Source: Authors' estimation based on data collected from TCB and other sources

Price Volatility of Food Products in World and Domestic Markets

- The level of volatility in prices of different products was not the same at the domestic and international markets
    - As part of the study price volatility was measured by using the variance in monthly prices during pre-covid period (April, 2019-March, 2020) and covid period (April, 2020-March, 2021)
- Price fluctuations were rather high during the covid year compared to that of the pre-covid year concerning the selected products, both in global and local markets
    - Significant price volatility was observed in case of rice in the domestic retail market and palm oil, and soybean oil in the global market

Volatility index of market prices of selected food products

Periods	Rice		Wheat		Palm oil		Soybean		Sugar	
	Global	Retail	Global	Retail	Global	Retail	Global	Retail	Global	Retail
Pre-covid (April 2019-March 2020)	2.21	269.84	1.42	2.18	54.21	72.58	12.43	7.62	2.12	0.03
Covid (April 2020-March 2021)	2.99	849.53	5.44	5.88	185.58	113.85	153.51	98.35	0.0	0.71

Source: Estimated by authors

Price Volatility of Food Products in World and Domestic Markets

- Domestic retail prices are to a large extent impacted by the level and price of import of food concerned item
  - The study analyses the import dependency ratio of major food products of Bangladesh
- According to the estimates, none of the selected products has a level of dependence of even 1 per cent
  - The highest level of import dependence is observed in case of wheat (0.99) followed by rice (0.83 in 2020) and lentil (0.67 in 2020)
- Given the very low level of dependence on imported products, volatility in domestic retail price is likely to be explained more by internal factors as against the external factors

Import dependency ratio of selected agricultural products

	Rice	Wheat	Lentil	Soybean	Onion	Garlic
2019	0.0	0.99	0.55	0.76	0.15	0.52
2020	0.83	0.99	0.67	0.83	0.06	0.47

Source: Estimated by authors based on data collected from different sources

Price Volatility of Food Products in World and Domestic Markets

- Retail market price variation may be estimated in terms daily, weekly and monthly levels
  - It is to be noted that majority of essential food products are outside of the purview of the structure of maximum retail price (MRP)
- The inconsistent pattern of market price movements indicate that domestic market supply and market price were influenced by non-market factors
- When marketing channels of food products work smoothly across the country, variation in retail prices in different markets are expected to be within certain limits
  - The price movement within the country are not same and different retail markets behaves differently in terms of market price levels
- This variances are partly due to variance in timely availability of supply in the market, but there are also other factors at play which need to be examined.

Variance in Dhaka retail prices of rice and wheat at daily, weekly and monthly levels (July-December, 2020)

	Daily	Weekly	Monthly
Rice	1.30	0.73	3.04
Wheat	1.95	0.84	0.76

Source: Authors' calculation based on TCB data

Variance in retail prices of rice and wheat at selected markets in the country (July-December, 2020)

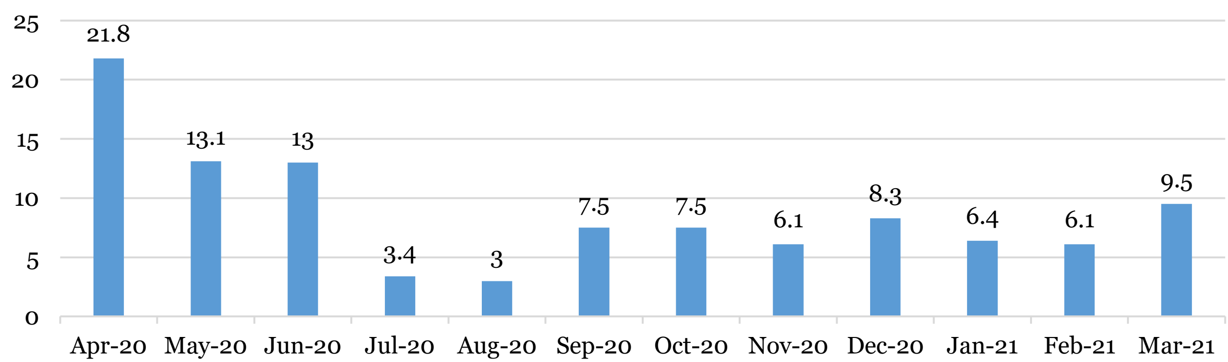
	Dhaka	Khulna	Chittagong	Rajshahi	Barisal	Rangpur	Sylhet
Rice	0.81	1.37	3.94	0.09	1.75	2.3	4.91
Wheat	9.01	0.36	0.0	0.16	6.19	9.54	0.1

Factors Driving Volatility of Retail Market Prices

Distribution of margins in the value chain

- The retail market price is influenced by the margin enjoyed by the intermediate market agents particularly at wholesale and retail levels
  - In case of rice, the rate of margin was as low as 3% during August, 2020 to as high as 21.8% in April, 2020
  - The rate of margin in wheat (atta) varied between as low as 0 per cent in August and September, 2020 to as high as 23.3% in May, 2020
  - Uncertainties in domestic supply related to production, import and stock due to the covid pandemic were to some extent responsible for the aforesaid trends

Percentage margin the price of rice (between retail and wholesale) in Dhaka

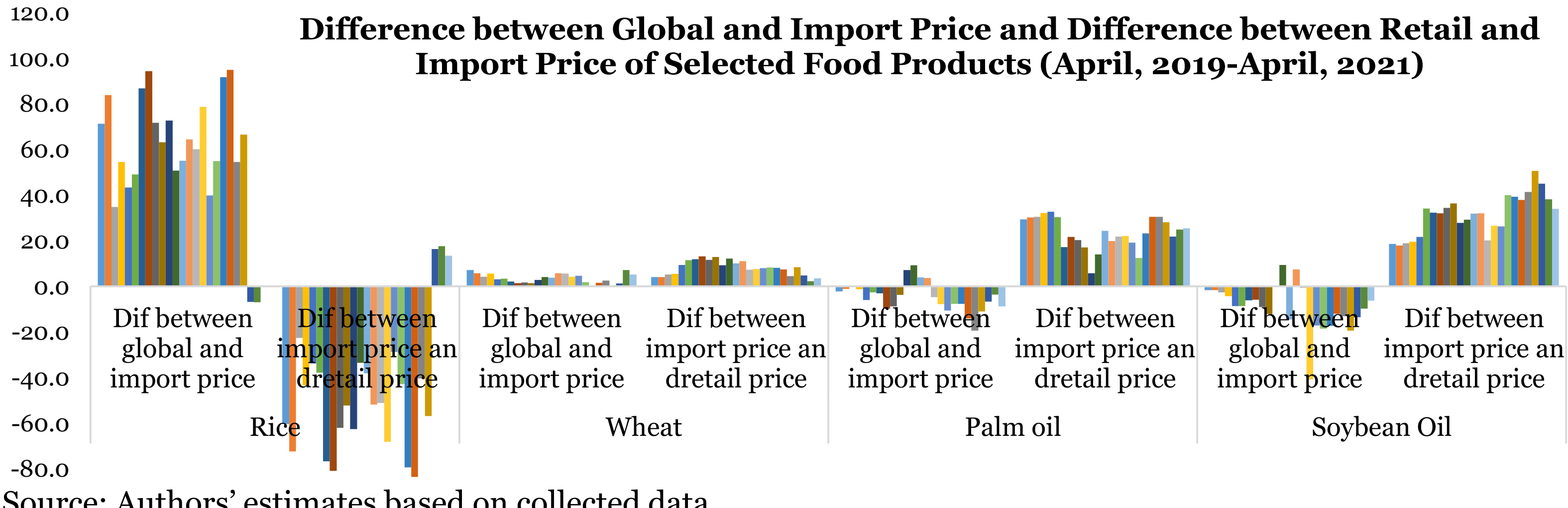


Source: FPMU, 2021

Factors Driving Volatility of Retail Market Prices

Influence of Variation of Import Prices

- Import of different food products as per requirement, and delivery on time, are highly important for ensuring stable market price
- Figure 3 shows that the gap between global market price and import price is found to be very high
  - It appears that the differences between import price and retail price is inexplicably high in case of palm oil and soybean oil (Figure)
- Import prices of rice (Tk. per kg), both during pre-covid and covid periods, shows extremely high figures (Tk.99.9 and Tk.94.9 respectively)
  - A part of high import cost is likely to be over invoiced by the importers. The particular case of rice needs to be investigated



Source: Authors' estimates based on collected data

Factors Driving Volatility of Retail Market Prices

- The price gap both at the import end as well as retail end of the value chain cannot be explained by general economic logic
- In other words, domestic retail market is likely to be influenced by non-market practices by importers, wholesalers and retailers; this has also been painted out

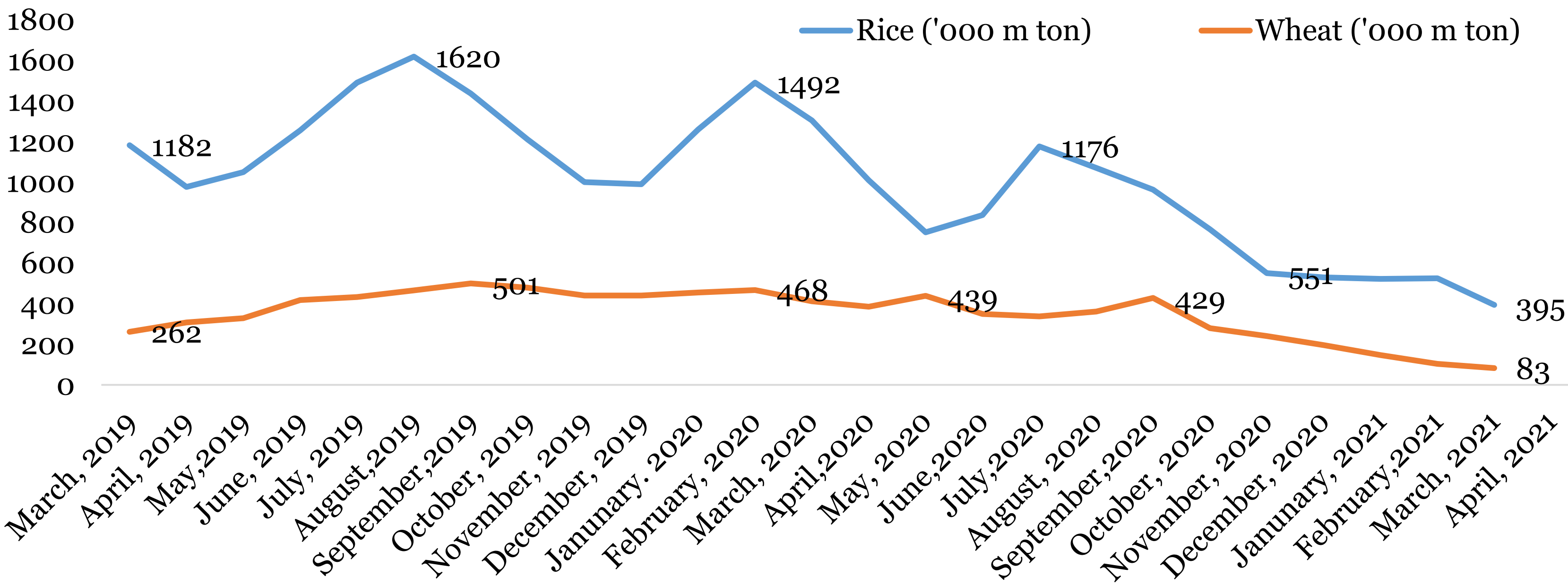
Changes in Domestic Production and Import of Selected Food Items and Food Stock of Rice and Wheat

- Domestic supply of food grains in a particular year is largely influenced by changes in domestic production and net import
  - Major food products have experienced a rise in production, except that of wheat, in FY2021
  - Import of rice, soybean and onion through the Chittagong port has declined during covid period
- In case of import and level of procurement of rice, the impacts were not notable
- In the backdrop of high price of soybean oil, reduction of import in the covid period has further led to the increase of the prices of soybean oil at the retail market

Factors Driving Volatility of Retail Market Prices

- Domestic retail prices of rice and wheat are partly influenced by the availability of public food stock of rice and wheat
- Stocks of both rice and wheat were at their lowest level at the end of April, 2021
  - This is because of the failure to attain the targeted amount of procurement of rice and wheat against the increased targets set for procurement and public food distribution under the various social support programmes

Trends in Public Food Stock during Pre-Covid and Covid Period



Source: FPMU, 2021

3.4 Factors Driving Volatility of Retail Market Prices

- The procurement of boro and aman rice during 2021 was not achieved
  - Against the target of 1.3 million m ton of rice and 0.10 mmt of wheat for FY2021, only 0.66 mmt of rice could be procured up to March, 2021
- Although procurement price of boro was increased, because of higher market price the collection till now has not been satisfactory
- Import of rice had only a modest effect on the market and the retail price of rice
  - Market tends to be highly influenced by the harvest of boro rice
- Due to low level of procurement, government has revised downward the target for distribution of rice and wheat under social support programmes
  - This will adversely affect the low-income people in terms of ensuring minimum level of food security during the ongoing pandemic period

Factors Driving Volatility of Retail Market Prices

Impact of Different Factors in Determining Retail Price: A Regression Analysis

- The analysis has been carried out for rice, wheat, palm oil, soybean oil and sugar for the period of April, 2019 – April, 2021 (Table in the following slide)
- *Rice:* the domestic retail rice price is found to be cointegrated with global and imported price of rice and public rice stock. However, imported price and public stock of rice will have a positive impact and global rice price will have a negative impact on domestic retail price in the long run
- *Wheat, soybean and palm oil:* there is significantly high cointegrating relationship between domestic wheat, soybean and palm oil prices and global and imported prices. Similar to rice, imported price and public stock of wheat have a positive impact and global wheat price have a negative impact on domestic retail price, in the long run
- *Sugar:* both in the long run and short run, domestic retail sugar price is significantly cointegrated with the global sugar price

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Factors Driving Volatility of Retail Market Prices

Cointegrating coefficients of variables with p values for selected commodities

Commodities	beta	Coefficient	P Values
Rice	Retail Price	1	.
	Global Price	0.163	0.000
	Imported Price	-1.167	0.000
	Public Stock	-0.217	0.000
	_cons	4.100	.
Wheat	Retail Price	1	.
	Imported Price	-2.841	0
	Global Price	1.426	0
	Public Stock	-0.584	0
	_cons	12.785	.
Soybean	Retail Price	1	.
	Global Price	-5.574	0
	Imported Price	5.608	0
	_cons	-3.979	.
Palm Oil	Retail Price	1	.
	Global Price	-2.869	0
	Imported Price	2.315	0
	_cons	-2.084	.
Sugar (ARDL)	LONG RUN EQUATION		
	Global Price	0.324	0
	Imported Price	0.137	0.658
	SHORT RUN EQUATION (Log of global sugar price)		
	First difference	-0.132	0.052
	Lagged difference	-0.155	0.016
	_cons	3.367	0.002

Source: Authors' estimates

Different Policy Measures to Stable the Market Supply and Market Price

Policy Measures Undertaken at the National Level

- *Rice:* In case of rice, initiatives are mainly targeted at enhancing the supply of rice in the market
  - Encouraging the private sector to import more rice by reducing the import duties and by putting emphasis on procurement of rice directly from growers in order to replenish the public food stock
  - These initiatives had limited positive impact because of the overwhelming dominance of rice millers in the domestic market and large-scale importers at the import stage
  - The influence of dominant market players in the rice value chain needs to be properly investigated and to be addressed under the jurisdiction of the Competition Commission
  - Domestic procurement policy needs major revisions where procurement from growers need to be expedited through new measures and setting procurement price of paddy and rice at a competitive level
- *Onion:* Due to inadequate amount of import, domestic supply and price experienced only a limited positive effect
  - In this backdrop, the government has decided to enhance domestic production further in order to reduce dependence on imported onion particularly from India

Different Policy Measures to Stable the Market Supply and Market Price

- At the same time, the government has decided to reinstate the earlier import duties on onion in order to discourage import and to protect domestic onion growers
- *Edible Oil:* It is alleged that a handful of importers dominate the market and influence of their 'dominant market position' as mentioned in a report of the MoC
  - Government took initiatives to make the fixed price functional by introducing MRP at the retail level
  - This had only a limited success – sales in the retail market took place at a higher price than the stipulated price
- A host of measures have been undertaken by countries to address the issue of the price volatility
  - Price Stabilization Fund (PSF) and minimum support price have been put in place in India
  - Market price support policy is being implemented in Vietnam
  - Pakistan has intensified crackdown on profiteers and hoarders across different provinces

Conclusion

- The study reveals that volatility of market food prices at the domestic level is influenced principally by domestic and internal factors, and only partly by global factors
  - The retail prices of major food products cannot be fully explained by the margin enjoyed at the wholesale and retail levels, wholesale and importers level and wholesale and growers/miller level
- Public policy undertaken to address the issue of price volatility though, taken with right intention, are often found to be ineffective in addressing the price volatility
  - A major weakness is the role of 'dominant market players' played by major importers and by the millers and big suppliers
  - Over invoicing practices at import stage also plays a role
- Against these practices, both public monitoring and public enforcement of 'competitive practices' have little impact
  - Markets of each of the agricultural products, at each stage, need to be made competitive. Transparency, accountability & institutional effectiveness are the key here
  - The Competition Commission should investigate whether major importers and millers use their dominant market player and thereby influence the market for their interest

Conclusion

- ❑ Bangladesh needs to establish formal integrated network of value chain for each of the agricultural products
- ❑ All market players involved in those value chain should be registered
  - ➢ A transparent and accountable reporting system needs to be established across the value chains
  - ➢ All types of transactions in the value chains should be based on banking system except transactions at the lowest retail levels
- ❑ Each market agents should be legally bound to share basic market information on a regular basis (e.g. monthly basis) to the public authorities which include production, procurement
  - ➢ Stock, sales, purchase and sales price, opening of LCs, price of imported products, amount of import, amount of sales to whole sellers' and retailers' level etc
- ❑ Government should form a monitoring unit which will cover all essential food and non-food products
  - ➢ The unit would work under the PMO and operational activities would be in the nature of Food Policy Monitoring Unit (FPMU) which deal with rice and wheat related issues

Conclusion

- Based on the regular assessment, the monitoring unit will extend necessary guidance for the concerned public offices and private sector associations to undertake prompt action
- The government may think of setting up a permanent Agricultural Price Commission as in India, given the highlighted importance of the concerned issues
  - Indeed, such a proposal was floated by the CPD some years back
- This proposal merits urgent consideration by the government

Section IV.
Banking sector:
Unclear present—uncertain future

Banking sector: Unclear present—uncertain future

- Since about **80%** of the government's COVID-19 response funds are in the form of **liquidity support**, banks are anticipated to play a central role in view of recovery of the pandemic-affected economy.
- CPD had previously pointed out that the nature and design of Bangladesh's COVID-19 relief funds left ample room for financial malpractices
- Despite issuing more than 100 circulars related to the liquidity support packages over the past year, the central bank has not been able to address the **regulatory gaps**.
  - This has made some of the government's liquidity support packages available also for **banks that are weak and poorly governed**; these supports were also made accessible to **loan defaulters**.
- Citing the second wave of COVID-19, the central bank has extended its moratorium on loan classification by three more months, up to 30 June 2021.
  - It is not clear what the real situation of NPLs in the banking sector is at present, and it is uncertain as to how large NPLs may actually turn out to be in the future when the moratorium is lifted.
- Since the highest share of COVID-19 related liquidity support has been offered to large industries, crony capitalists may take advantage of their strong political foothold to use the banks to obtain more than their fair share of funds.
- Commercial banks must exercise their own judgement to decide which potential loan seekers have been **"affected"** by COVID-19, since no clear, objective and quantitative criteria for defining the term "affected" has been stipulated by the central bank.

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Government's COVID-19 response

- The Government of Bangladesh had responded to health and economic emergencies caused by COVID-19 by announcing a number of liquidity support and fiscal stimulus packages targeting various sectors and people.
- The liquidity support was channeled through the banking sector which has proven to be the weakest link in the economy of Bangladesh for the past decade.
- Bangladesh's **fiscal** stimulus package is a meagre 20.41% of its total COVID-19 relief funds or only **0.91%** of its GDP, and falls far short of the 11% of GDP that is estimated to be required to mitigate the socioeconomic impacts of COVID-19.

Table: Summary of COVID-19 response funding by the government

	Allocation			
	In million USD	In crore BDT	As share of total COVID funding	As share of GDP[ii]
Total liquidity support	11,839	99,450	79.59	3.54
Total fiscal stimulus	3,037	25,503	20.41	0.91
Total COVID-19 funding	14,876	1,24,953	100.00	4.45

Note: i) Assuming an exchange rate of USD 1 equal to BDT 84, as per national budget documents of FY2021; ii) Assuming that GDP is equal to USD 334,000 million, as per the GDP for FY2020 in the national budget documents of FY2021.

"k" shaped economic recovery

- Moreover, the **varying speed of implementation** of the various liquidity support packages has created an unequal turnaround as bigger firms have rebounded more strongly, owing to quick access to liquidity packages, while **smaller firms have been largely left behind**.
- From the outset of the announcement of the COVID-19 liquidity support packages by the government, **banks have been more willing to lend to large borrowers**, but were hesitant to lend to small borrowers.
- In a "k" shaped economic recovery curve, the COVID-19 recovery path splits in two directions: large firms and public-sector institutions with direct access to government and central bank stimulus packages will make some areas of the economy recover fast but leave behind small and medium-sized enterprises (SMEs), blue-collar workers, and the under-pressure middle class.
- **The design of the stimulus packages and their distribution services a mostly "k" shaped economic recovery path in Bangladesh.**

Transparency and accountability

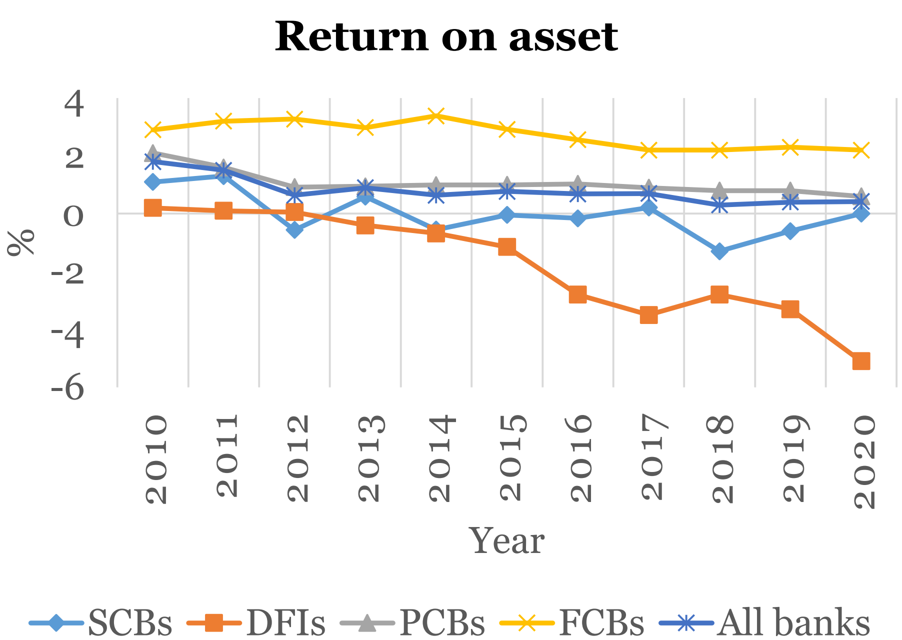
- The **transparency** and **accountability** of Bangladesh's COVID-19 stimulus plan will be key to its successful operationalisation and implementation.
- Hence, it is critical to make sure that the beneficiaries are selected based on **clear, objective, and quantitative criteria** and vested interests are not allowed to intervene.
- Without connections with the local powerful people, it has been proved to be difficult to get included in the list of beneficiaries.
- Widespread **corruption** has taken place in the distribution of government's relief items.
- Such **malpractices** have been reported in the media at a time when the economy was reeling from the worst effects of the COVID-19 crisis.
- Since the vast majority of Bangladesh's COVID-19 relief funds will be distributed through banks, there is an **opportunity for unscrupulous individuals** to profit from humanitarian aid without coming into the limelight.

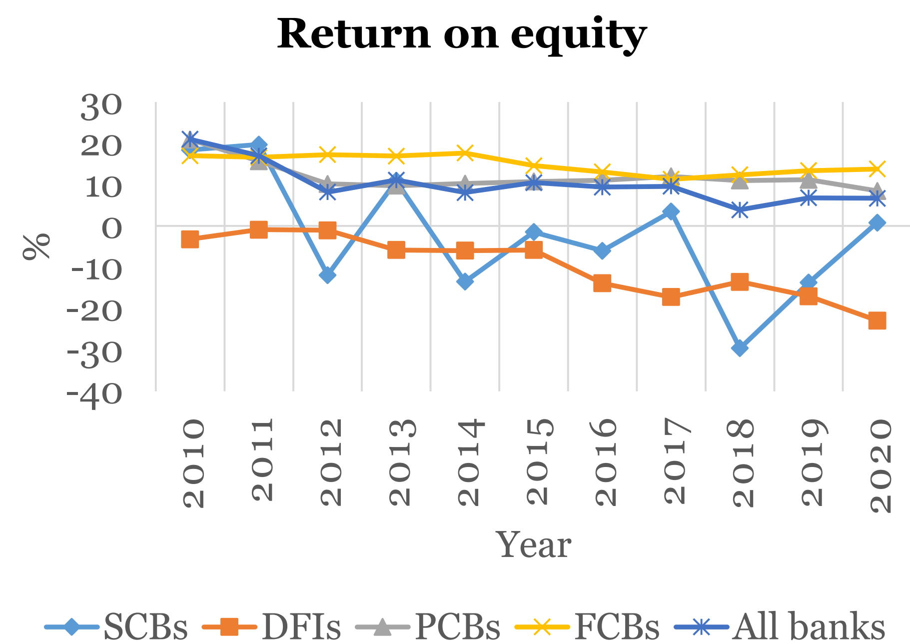
Can loans lend a helping hand?

- **Liquidity support cannot be treated as philanthropy and so banks cannot provide loans to anyone on humanitarian grounds.**
- Any bank must follow its due diligence whilst providing loans, meaning that banks are generally more inclined to provide loans to their old borrowers who are familiar to them rather than new borrowers who are unfamiliar with them.
- As a result, new borrowers with no credit history and limited records of business-related bank transactions found it difficult to obtain loans from any bank under any liquidity support package regardless of how badly affected they were due to the pandemic.
- **Liquidity support through bank loans is not the best way to cater to the needs of small borrowers and new borrowers, as well as those who are the poorest and most vulnerable.**
- There is a lack of awareness among women, and the general public at large, regarding the government's liquidity support.
- **A large portion of people, who are actually poor and in dire need, did not receive any form of support from the government—whether in the form of relief items, liquidity support or fiscal stimulus**

Profitability of banks during the pandemic

- PCBs experienced a **decline in profitability**, as their return on asset fell from 0.80% in 2019 to 0.60% in 2020, and their return on equity fell from 11.2% in 2019 to 8.5% in 2020.
- DFIs dug themselves into a deeper hole after the pandemic, as their return on asset and return on equity plummeted in 2020.
- However, FCBs were largely unaffected by the pandemic, whereas SCBs actually managed to improve their profitability in 2020.

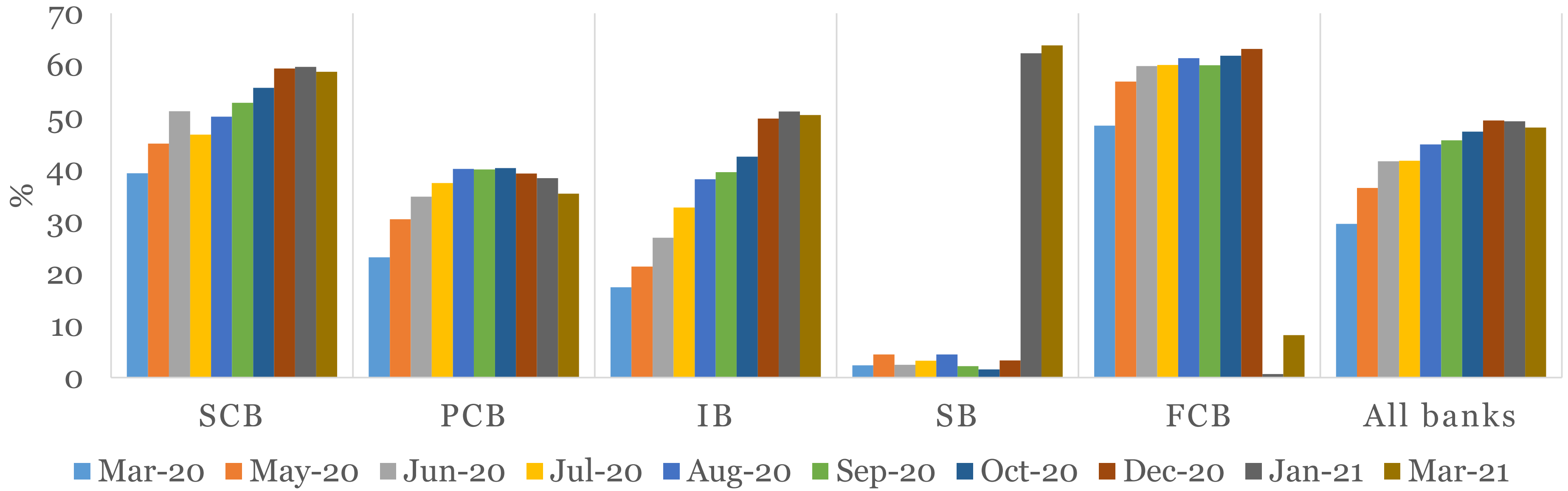




Excess liquidity

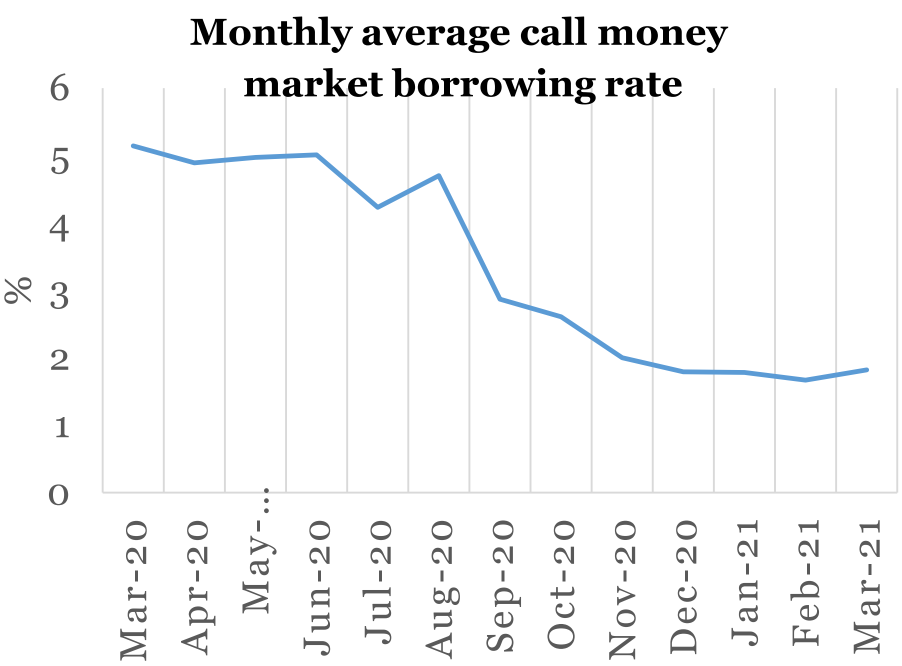
- **Data from Bangladesh Bank shows that excess liquidity in the banking sector has nearly doubled from BDT 103 thousand crore in January 2020 to BDT 205 thousand crore in December 2020.**
- During the same period, excess liquidity has more than doubled in SCBs and more than tripled in IBs.
- Excess liquid assets comprised of 48% of the total liquid assets of the banking sector in March 2021.

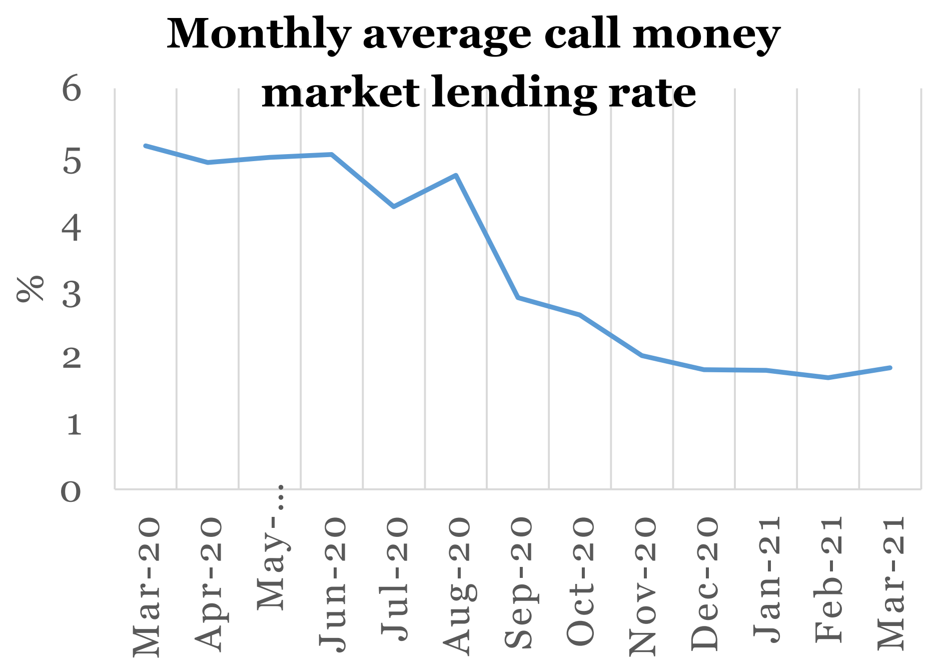
Excess liquid assets as a percentage of total liquid assets



Call money market

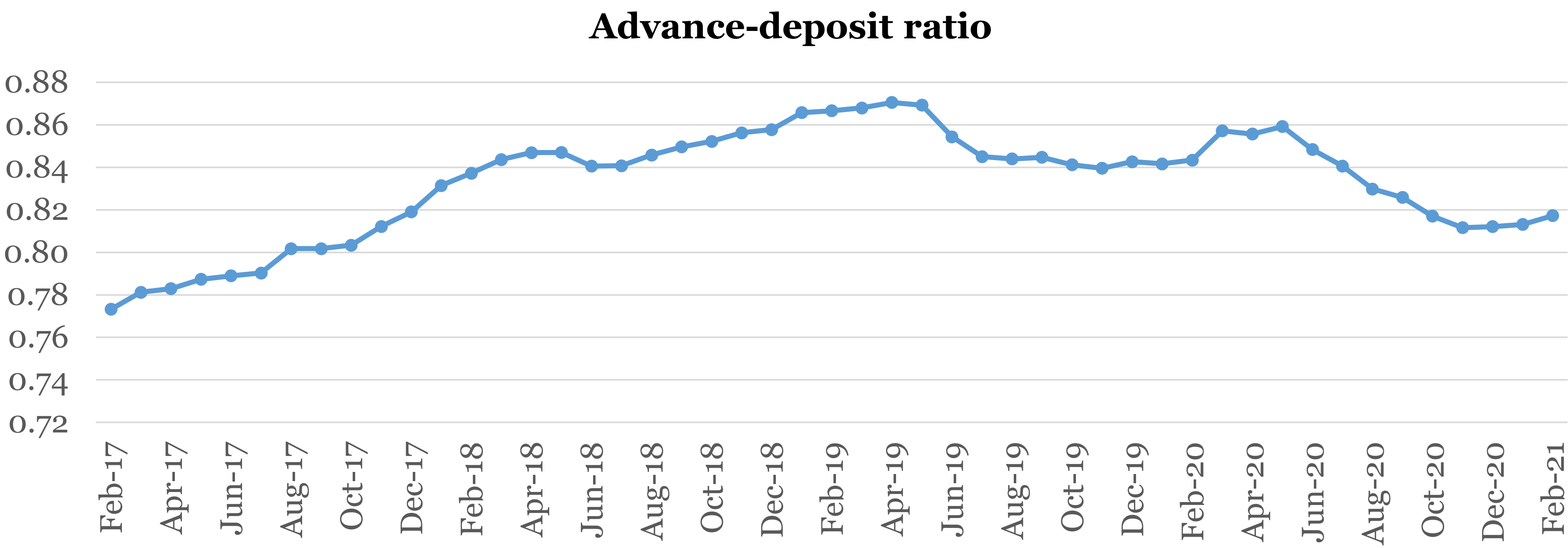
- Signs of excess liquidity were also manifested in the call money market, as the monthly average call money market borrowing and lending rates both tumbled down from June 2020 onwards.
- However, the monthly average call money market borrowing and lending rates have both somewhat increased from February 2021 to March 2021, indicating that the **situation may be changing gradually.**





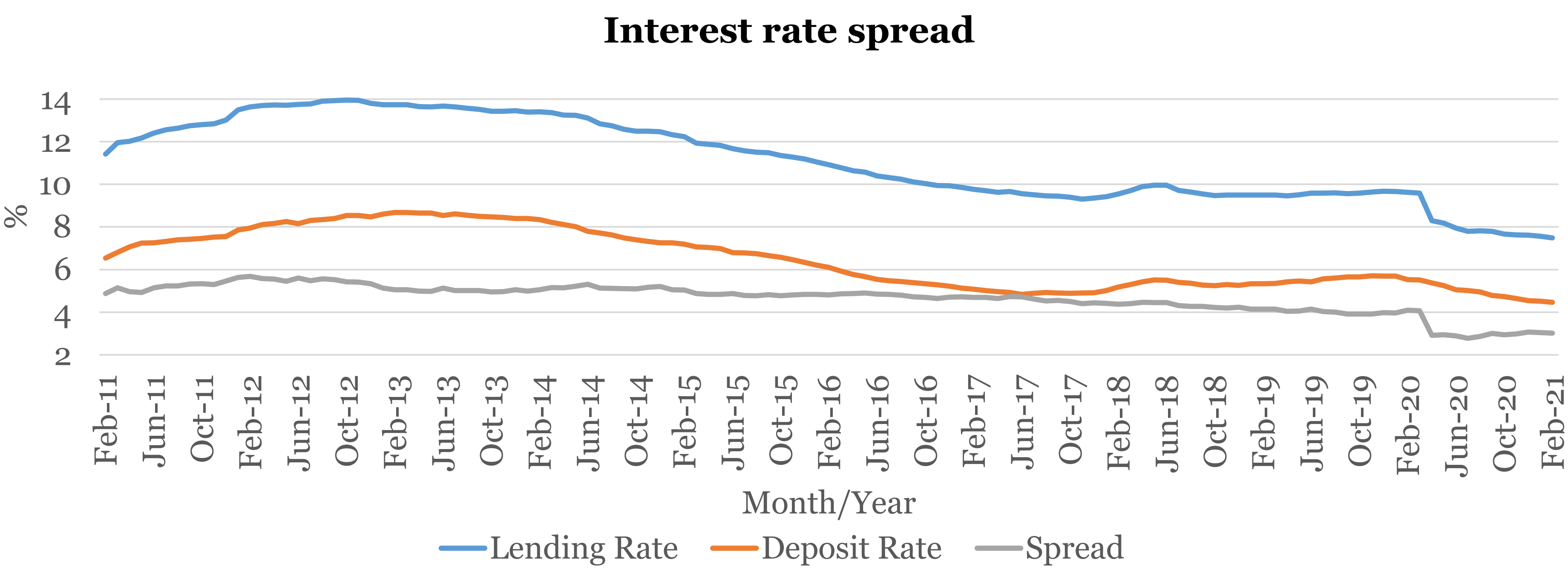
Advance-deposit ratio

- Excess liquidity is also a sign that the demand for loans is low, which is likely since the real economy is still experiencing the repercussions of the COVID-19 shock.
- The advance-deposit ratio of all banks fell to a three-year low of 0.81 in November 2020.
- However, in the early months of 2021, the advance-deposit ratio increased slightly, indicating that **economic activity may be slowly picking up**.



Interest rate spread

- Excess liquidity in the banking system has led to a fall in the interest rates, which were already quite low even prior to 2020.
- During the pandemic, the weighted average lending rate in all scheduled banks has come down sharply and the weighted average borrowing rate in all scheduled banks has also declined.
- As a result, the interest rate spread has come down, adding to the woes of the commercial banks.

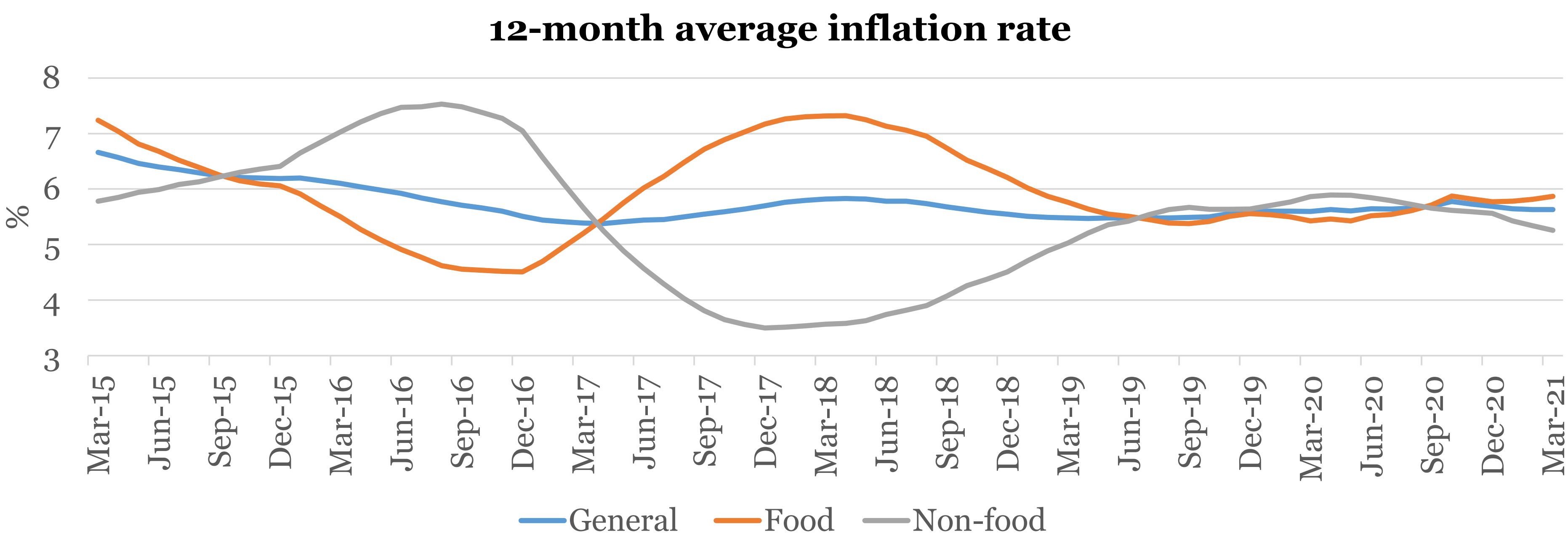


Monetary policy for a pandemic-affected economy

- Monetary policy in the upcoming fiscal year will have to tackle the challenges posed by the uncertainties caused by COVID-19, while at the same time reigning in the rising cost of living which is harming the middle class and the poor.
  - Such formidable feats must be performed in the backdrop of excess liquidity in the banking sector, which will make this effort even more arduous.
- **Excess liquidity in the banking system may induce commercial banks to behave in ways which may jeopardise the stability of the financial system and make it difficult for the central bank to achieve its monetary policy goals.**
  - For example, banks may attempt to offset their losses from holding excess liquidity by giving out risky loans which may lead to higher volume of NPLs, higher inflation, and the creation of asset bubbles.
- Excess liquidity in the banking system also weakens the interest-rate transmission mechanism of monetary policy, making monetary policy less effective in fine-tuning aggregate demand.
- Moreover, when there is excess liquidity in the banking system, commercial banks may perceive the opportunity cost of holding excess balances at the central bank to be low, and hence be slow to act to reduce excess liquidity.
  - As a result the central bank would find it more challenging to determine the ideal level of desired and excess reserves.

Inflation rate: A far cry from the content of living

- ❑ Over the years, the central bank has set various targets for inflation and seemingly achieved or come close to achieving them.
- ❑ **However, it appears that the inflation rate has lost its relevance to the real world as even the middle class are increasingly finding it difficult to make ends meet in the face of income erosion.**
- ❑ The data shows that the 12-month average food and non-food inflation rates have fluctuated in a cyclical pattern over the past several years.
- ❑ In the long-term, the overall general inflation rate has experienced a slight decline.



CPI consumption basket: Does it reflect consumption pattern?

Food expenditure as a share of income (in %)

	National	Rural	Urban
2000	42	48	32
2005	45	50	36
2010	53	57	45
2016	46	52	37

Food expenditure as a share of consumption expenditure (in %)

	National	Rural	Urban
2000	55	59	45
2005	54	59	45
2010	55	59	48
2016	48	50	43

Weights used for food in calculation of CPI (base year 2005)

	National	Rural	Urban
2000			
2005	56	61	47
2010	56	61	47
2016	56	61	47

- **Engel's law** states that *as income increases, people spend a smaller proportion of their total income on food*
  - In Bangladesh, *nominal* household income increased by 7.86% per year on average and *real* household income increased by 0.16% per year on average between 2010 and 2016
    - *food expenditure as a share of income* **decreased** from **53%** in **2010** to **46%** in **2016**
    - *food expenditure as a share of total consumption expenditure* **decreased** from **55%** in **2010** to **48%** in **2016**
- However, the *weights used for food in the calculation of CPI are significantly higher than share of food expenditure in either income or consumption expenditure*
- **Thus, the consumption basket used for calculating overall general inflation was created in 2005 and does not reflect the current consumption pattern of consumers or the actual prices in the market**

Source: BBS

CPI consumption basket: Does it reflect consumption pattern?

Weights used for calculating CPI vs. actual distribution of consumption expenditure

	Weights used for non-food items in calculating CPI (base year 2005)	Distribution of consumption expenditure based on crowd-sourced data
Non food	44	60
Clothing	7	3
Rent	15	17
Transport	6	21
Recreation	4	7

- Crowd-sourced data of prices of 5,621 items contributed by 449 respondents during November 2019 to November 2020 show that
  - share of **non-food** items in actual consumption expenditure was **16% higher** than the weight in CPI
  - share of **rent** in in actual consumption expenditure was **2% higher** than the weight in CPI
  - Share of **transport** in actual consumption expenditure was **15% higher** than the weight in CPI
- **Thus, the consumption basket used for calculating non-food inflation does not accurately portray the behaviour of the consumers at present or the market prices prevailing at the moment**

Source: BBS and Numbeo

Conclusions

- Stimulus packages provided through banks has created **new avenues for corruption and malpractices**.
- **Repayment of loans provided through stimulus packages** may become a cause of concern in the coming days.
- Once the moratorium on loan classification is eventually lifted, the level of **non-performing loans may also rise suddenly**
- Liquidity support and fiscal stimulus packages rolled out without prior assessment of the ground realities may not be able to address the **needs of the most vulnerable people in society**.
- In particular, **providing loans to vulnerable individuals and small businesses may not yield the expected results.**
- Hence, it is urgent for the government to reconsider liquidity support as the primary mode of economic response to COVID-19, and **increase fiscal stimulus and direct cash transfers to the poor.**

Conclusions (cont.)

- Sound macroeconomic management and prudential supervision must be rooted in established economic theory and high-quality empirical evidence.
- **Unfortunately, lack of data integrity in recent years has seriously compromised the effectiveness of the government's policies and the central bank's directives, thus jeopardising the overall economic progress of the country.**
- Calculating CPI on a base year and consumption basket which is 16 years old appears to be naïve at best and manipulative at worst.
- As even the middle-class struggle to make ends meet, it seems unlikely that long-term inflation is declining.
- **It is apprehended that actual inflation may likely be significantly higher than the reported values.**

Recommendations

- **Loan defaulters** should not be allowed to access any of the COVID-19 related liquidity support packages.
- **Weak and poorly governed banks** should be barred from participating in the COVID-19 related liquidity support packages. Banks which are not fully compliant with BASEL III or the Banking Company Act should be not be allowed to participate in the COVID-19 related liquidity support packages.
- Clear, objective, and quantitative criteria should be declared to properly identify **“affected”** businesses and individuals.
- **Transparency and accountability mechanisms** should be built into all COVID-19 related liquidity support packages, and more disaggregated data on the implementation status of all liquidity support packages should be published on a monthly basis.
- **Disbursement** of the government’s COVID-19 liquidity support for small businesses, farmers, and low-income professionals should be **expedited immediately**.

Recommendations (cont.)

- The government must **acknowledge the actual scale of the COVID-19 crisis** and then **formulate a specific and target-oriented post-COVID recovery plan** that aims to build back better. A thorough **needs assessment** should be conducted to understand the extent of damage done by COVID-19, the amount of support required, and the people who need the support the most.
- **Public awareness about the liquidity support and fiscal stimulus packages** should be raised through nation-wide campaigns so that the general population can clearly understand what kinds of support are being provided by the government, who are eligible for such support, and how to obtain the support.
- **Liquidity support is inappropriate for small borrowers and new borrowers, as well as those who are the poorest and most vulnerable.** Therefore, direct cash support should be provided by the government so that these groups can adjust to the shocks of COVID-19.

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Recommendations (cont.)

- **Corruption in the targeting and selection of beneficiaries of cash transfer programmes must be addressed immediately.**
- A **multi-stakeholder taskforce** with representatives from the various ministries, central bank, commercial banks, trade bodies, civil society, non-government organisations. and academia should be formed for monitoring the delivery of the COVID-19 liquidity support and fiscal stimulus packages and assessing their effectiveness.
- Banks with excess liquidity should be discouraged by the central bank from taking unnecessary risks.
- A goal-specific, time-bound, inclusive, transparent, unbiased and independent **Citizen's Commission on Banking** should be set up in order to bring transparency in the prevailing situation, identify the root causes of the manifest problems, and suggest credible measures for improving the situation sustainably.
- **A new consumption basket should be formulated for calculating CPI inflation**, based on rigorous research as regards consumer behaviour and expenditure patterns. All targets, projections, and plans in the monetary policy and the 8th Five Year Plan should be revised in accordance with this new consumption basket for CPI and new base year for inflation.

Section V. Concluding remarks

Concluding Remarks

- While the government did come up with a number of initiatives to mitigate the sufferings of the people and overcome the adverse effects on the economy in view of the pandemic, the much-expected turnaround is still not there
- One conclusion that can be drawn from the analysis presented in the proceeding sections is that addressing embedded institutional weaknesses and resilient recovery have become entwined
- Inherent weaknesses in the banking sector are undermining the government's efforts to trigger economic recovery through bank-dependent stimulus packages
- Attempts to trigger private sector investment through subsidies, incentives and working capital support are not being able to compensate for the inherent challenges that continue to undermine the competitiveness of the private enterprises
- Reaching those who are left behind are proving to be difficult in the absence of effective local-level institutions and access to real-time data
- Generating domestic resources to underwrite the needed resources have been weakened in the absence of the much needed fiscal reforms

Concluding Remarks

- The net outcome of the above has been that private sector investment has been below the targets set out in the plans and budget and as manifested in the negative growth of capital goods and term loan uptake and that of FDI
- Revenue generation figures remain way below the targets, and redistributive functions of fiscal policies can not be excluded because of the enforcement capacities and failure to implement long-awaited fiscal reforms
- FY21 targets for export growth remain way below targets
- Even during the pandemic, the much needed expansionary fiscal-budgetary policies could not be implemented because of continuing and endemic weaknesses of implementing agencies and line Ministries
- No tangible change could be brought in terms of the capacity to both earn and to spend

Concluding Remarks

Recommendations that cover both short-term urgent measures and medium-term macroeconomic management, institutional capacity building and reform measures in three areas:

- From the approach to the design of budget for FY22, stress has been given to pursuance of expansionary fiscal policy, focusing on redistribution rather than economic growth
  - From the public expenditure side, priority has been urged for social safety net, health, education and CSME-oriented investment-augmenting measures
- Adequately, affordability and price stability has been prioritised in the discussion as regards food items
  - Towards this, fiscal measures, timely import, and food stock management have been stressed
- In terms of reform measures setting up of Banking Commission, Agriculture Price Commission, Competition Commission and fiscal reforms have been emphasised to create the foundations of a good-governed and well functioning economy that will help to recover from the pandemic and build back better

Independent Review of Bangladesh's Development

Stay Well, Stay Safe

CPD (2021): State of the Bangladesh Economy in FY2020-21 (Third Reading)