Independent Review of
iRBD
Bangladesh's Development

বাংলাদেশের উন্নয়নের স্বাধীন পর্যালোচনা

CPD's Recommendations for the National Budget FY2023-24

Weathering the Storm, Containing the Risks

Dhaka: 27 March 2023

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The CPD IRBD 2023 Team alone remains responsible for the analyses, interpretations and conclusions presented in this report.

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Section 1: Introduction

Introduction

- The national budget for FY2023-24 (FY24) will be the last budget prepared by the incumbent government prior to the upcoming national elections
- It is being prepared amidst a number of disquieting developments – both at the global and domestic fronts
- The Bangladesh development narrative, with its impressive success in terms of economic performance and commendable progress in terms of key socio-economic indicators, have come under scrutiny in view of the developments of recent times
- The challenge facing the economy is to restore macroeconomic stability, consolidate the gains of the past, and adjust to new realities keeping the growth and stability trade-off in the perspective
- The upcoming FY24 budget will need to address these attendant concerns amid election-related uncertainties
  - This will require renewed efforts towards raising the quality of macro-fiscal planning and management which, in turn, will require some hard choices on the part of the policymakers

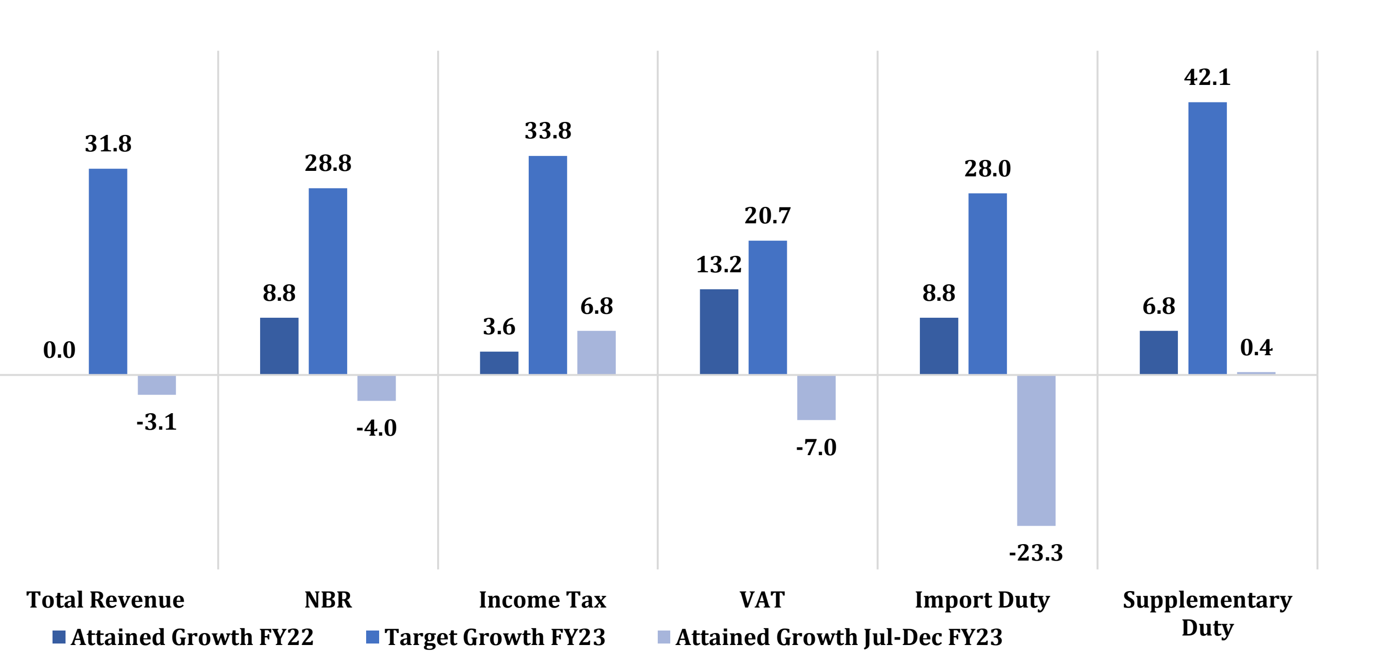
Introduction

- The present report focuses on six areas:
    a) Macroeconomic management
    b) Fiscal framework
    c) Prices of commodities
    d) Subsidies
    e) Health and education
    f) Environmental concerns
- This report highlights some of the key challenges in these areas which require immediate and heightened policy attention, particularly from the macro-fiscal management viewpoint
- Finally, this report puts forward a set of recommendations which might be considered by the policymakers while formulating the national budget for FY24. The analyses and recommendations presented by this report may also inform the electoral debates subsequent to the national budget

Section 2: Key trends in macroeconomic correlates

Shrinking fiscal space in the backdrop of a lack of momentum in revenue mobilisation

Revenue mobilisation growth by sources (%)



Source: Estimated from Monthly Report on Fiscal Position, MoF

- ❑Revenue collection was lower in FY23
- ❑VAT and import duty collection was also lower despite the rising commodity prices and substantial depreciation of BDT
- ❑ADP spending was restrained
- ❑Import restricted
- ❑More likely economic activities slowed down, and administrative efforts did not improve significantly

- ❑It is more likely that the IMF's condition to generate Tk. 3,456.5 billion in FY23 as tax revenue would remain unmet

Budget deficit financing relied highly on borrowings from the central bank

- ❑Shrinking fiscal space forced the government to go for restraining public expenditure
- ❑Budget deficit remained higher in H1 of FY23
- ❑Net foreign financing did not make any significant improvement
- ❑Net NSD certificate sales was negative (to the tune of (-) Tk. 3,065 crore)
- ❑Government's options for financing of budget deficit were limited to borrowing from the banking sector, more specifically, the central bank
- ❑Cash-strapped scheduled banks were unable to provide loans
- ❑Government borrowed about Tk. 51,266 crore from the central bank and repaid about Tk. 20,735 crore in net terms to the scheduled banks
- ❑Central bank also retracted a substantial amount of BDT as it sold USD 10.5 billion, which kept M2 and reserve money within the programmed limits
- ❑Continued borrowing from the central bank will not be advisable as it may lead to added inflationary pressure

The liquidity position of scheduled banks tightened amid deteriorating financial sector governance

- Overall liquidity in the banking system had declined sharply (by Tk. 66,581 crore)
- Islami banks as a group could not meet the total minimum liquidity requirement

Excess liquidity by bank types (crore Tk.)

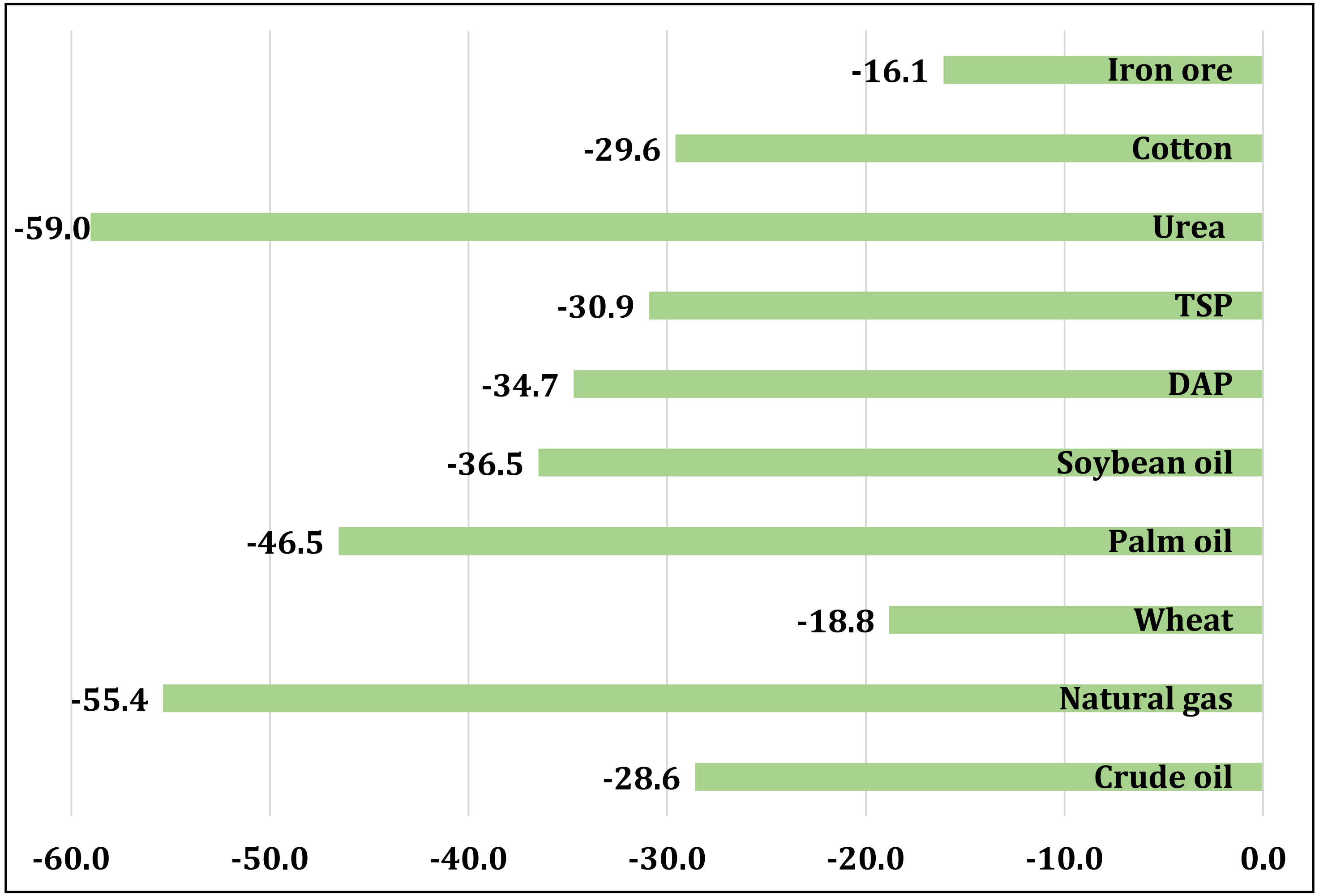
End of Month	SCB	PCB	IB	FCB	SB	All Banks
June 2022	79,430	76,376	21,792	25,743	82	203,424
October 2022	61,970	64,657	10,420	32,394	115	169,556
January 2023	51,387	55,554	(2,218)	32,051	69	136,842

Source: Bangladesh Bank.

- With declining purchasing power and lowered propensity to save, currency in circulation outside banks increased by 24.1% by the end of Jan 2023
- Good governance in the banking sector and pursuing the needed reforms is long overdue
- IMF conditionalities: (i) pilot risk-based supervision action plan to establish risk-based banking supervision by the end of June 2023; (ii) Bank Companies (Amendment) Act 2020 and the Finance Companies Act 2020 by Sep 2023, (iii) publishing banks' distressed assets in the annual financial stability report by June 2023
- CPD has been urging for setting up an independent Banking Commission

Despite some relief at the global level, there is no respite from rising commodity prices

Growth rates in selected global commodity prices between February 2023 and March 2022 (the beginning of war in Ukraine) (in %)



Source: World Bank Commodity Price Data

- Headline inflation at the global level has begun to ease
- International prices of major imported commodities recorded significant declines
- periodic formula-based price adjustment mechanism for petroleum products by the end of December 2023
- Must include an institutional efficiency audit of BPC and other entities
- Prevailing tax structure needs revision

Despite tightening imports, balance of payments remains at risk

- Sharp deterioration in BoP resulting in a drastic decline in foreign exchange reserves and significant depreciation of the BDT is one of the most distressing signals
- Deficit in overall balance reached USD 7.4 billion (Jul-Jan FY23) as there has been a conscious effort to curb imports along with significant depreciation of BDT
- Merchandise import shipment declined by (-) 5.7% (Jul-Jan FY23)
- Export growth was 9.6% (Jul-Feb FY23) - but non-RMG export declined by (-) 9.9%
- It is surprising to find that the sharp depreciation of BDT, which should have enhanced their competitive strength significantly, had failed to be realised in export terms
- Remittance inflow continued to remain in positive terrain (4.3% in Jul-Feb FY23)
- Overseas migration was far more impressive – about 27.5% (Jul-Feb FY23)
- Apprehensions about an increasing inflow of remittance through informal channels have been gaining traction
- Net foreign aid declined by (-) 12.2%; but net FDI increased by 4.1% (Jul-Jan FY23)

Despite tightening imports, balance of payments remains at risk

- Concerns remain in the area of (net) trade credit as this component of the balance of payments was found to be significantly negative ((-) 2.8 billion)
- Foreign exchange reserves declined by USD 10.5 billion (as of 22 March 2023)
- According to the IMF conditionalities, the Bangladesh Bank will need to compile and report official reserve assets as per the Balance of Payment Manual of the IMF (Sixth Edition) definition to improve transparency and reporting standards
- Since global prices have come down in recent months, it will help the government ease some of the prevailing import restrictions in the coming months, but deferred payments are still very high
- Central bank will not have much room to pump foreign exchange and may have no other option but to allow BDT to depreciate as the ongoing pressure on the balance of payments is likely to continue
- CPD has been arguing for a gradual move towards a market-determined exchange rate regime – according to IMF conditionalities, it has to be done by the end of June 2023

Take preparation towards macroeconomic management in difficult times

- The government in the past has tried to blame the war in Ukraine and the subsequent volatility in the global economy for the current situation
- However, the crises in the Bangladesh economy accumulated over the years and were rooted in weaknesses in domestic policies, lack of good governance and inability to implement the needed reforms
- Indeed, as the global economic situation is improving and global commodity prices are now coming down, there is hardly any room to blame the global volatility for the ongoing challenges confronting the Bangladesh economy
- Policymakers focus on the macroeconomic situation and policies, the implications for the general people and enterprises can and should not be ignored
- General people, particularly the fixed-income earning and low-income population groups, experienced significant erosion of purchasing power, lower levels of consumption, depleting savings and curtailing expenses for education and health
- Import restrictions have forced enterprises to operate at significantly lower capacity levels

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Take preparation towards macroeconomic management in difficult times

- If macroeconomic instability continues, attracting fresh private investment will be difficult
- Shrinking fiscal space has already forced GoB to cut back on subsidies and overall public investment.
- GoB will need to reprioritise public expenditure and opt for targeted fiscal measures
- The national budget for FY2024 will need to be cognisant of this
- It is hard to predict the extent of the impact on the economy as data for the real economy is either unavailable or unreliable – LFS data should also be made available at the earliest
- This will help the policymakers assess the economic situation better and make informed policy decisions
- Macroeconomic management in the coming months will be challenging
- Policymakers will need to make hard choices
- The fiscal, monetary and institutional policies will need to be reinforcing in nature

Take preparation towards macroeconomic management in difficult times

- Macroeconomic management should be informed by the following three objectives: **stability, discipline and consolidation**.
- **Stability** should be the anchor of the macroeconomic policy stance
- *Immediately pursue market-based interest rates and exchange rates.*
- *Stabilising the prices of the essential commodities would require economic (e.g., tax and duty relief) and institutional (e.g., market monitoring and ensuring a competitive environment and enforcement of laws and regulations) and social protection measures for the low-income and fixed-income earning population groups*
- Establish **discipline** in public expenditure (by prioritising and ensuring good value for money) and in the banking sector (by establishing good governance)
- *The government should also closely examine the debt situation – the recent exchange rate fall would require much higher foreign debt servicing payments in BDT terms*

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Take preparation towards macroeconomic management in difficult times

- **Consolidate** domestic resource mobilisation and foreign exchange inflow
- *Utmost emphasis would be required to curb tax evasion and illicit financial flows*
- *Encourage foreign exchange inflow in all forms, be it export earnings, remittances through the official channels, foreign aid (commitment and utilisation), foreign grants for NGOs, and FDI, without exception.*
- Lastly, policy formulation and implementation should be free from the capture of vested interest groups.
- The needs of the disadvantaged population groups will need to be met through adequate support programmes and speedy implementation of such declared initiatives as the 'family card'.

Section 3: Fiscal framework

Fiscal framework

- The FY23 budget failed to take cognisance of the emerging scenario and the new realities that should have informed budget design and fiscal-public expenditure proposals
  - Resulted in a fiscal framework that was rather formulaic in nature and driven by business-as-usual considerations, i.e., lofty targets were set that had a high probability of missing their marks by a considerable margin at the end of the fiscal year
- Drawing lessons from this experience, the design and fiscal targets of the upcoming FY24 should be set in a realistic manner, taking cognisance of the current macroeconomic trends – both domestic and external
- The issue of realistic target setting could take the case of revenue mobilisation as a key reference point
  - While proposing the FY23 budget, the targeted growth of revenue earnings was set at 11.3% over the revised budgetary target of FY22. However, if the actual revenue mobilisation of FY22 is considered, the growth target for FY23 actually turns out to be 31.8% - almost threefold

Fiscal framework

- According to MoF data, revenue mobilisation decreased by (-) 3.1% during Jul-Dec of FY23
  - If the annual growth target of 31.8% is to be achieved, then revenue earnings will need to increase by an unrealistic 67.4% over the remainder of FY23
- Revenue mobilised by the NBR, which accounts for about 85% of the total targeted resource envelope, decreased by (-) 4.0% during the Jul-Dec period of FY23
  - This decline can be primarily attributed to the fall in VAT and import duty collection
    - This, perhaps, is a reflection of the various import-related restrictions imposed by the government
    - On the other hand, this in all likelihood, is also indicative of a possible slowdown in economic activities
- If the current trend of revenue mobilisation persists, a large shortfall (i.e., the gap between the revenue mobilisation target and actual attainment) at the end of FY23 will become inevitable

Fiscal framework

- Taking advantage of the latest available data from both MoF and NBR, and considering the trends of other macroeconomic correlates, CPD projects that the revenue shortfall at the end of FY23 could reach approximately Tk. 75,000 crore, with total revenue collection being about Tk. 358,000 crore
  - CPD's earlier projection in Dec 22: revenue shortfall of Tk. 64,000 crore
- IMF has projected the total revenue mobilisation of FY23 and FY24 to be nearly Tk. 387,600 crore and Tk. 454,900 crore, respectively
  - If the CPD projection holds and the IMF projection for FY24 is to be achieved, then total revenue mobilisation in FY24 will need to grow by about 27% – a daunting task indeed
- As a quantitative performance criterion to avail of the IMF loan facility, the floor of tax revenue collection at the end of FY23 has been set at Tk. 345,630 crore
- The government has an uphill battle for both current and upcoming fiscal years if it wants to avail of the future instalments of the IMF loan

Fiscal framework

- The failure to utilise planned budgetary allocations has continued in FY23
- According to MoF data, total public expenditure recorded a paltry growth of 1.3% during the Jul-Dec period of FY23
  - The most alarming fact in this regard is that the ADP expenditure recorded a negative (-) 4.9% growth during this period
    - Whether it is due to limited resource availability owing to the fall in revenue mobilisation, the inability to implement the large number of projects, or is a result of the austerity measures taken by the government remains a critical question in this backdrop

Table: Growth of public expenditure components (in %)

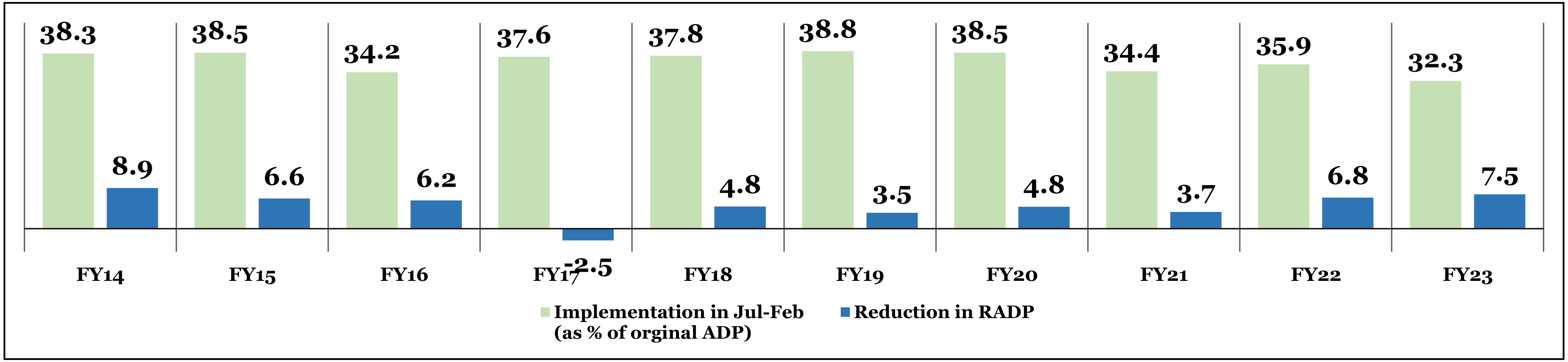
Component	Target FY22	Actual FY22	Target FY23	Jul-Dec FY22	Jul-Dec FY23	Required Jan-Jun FY23
a. Total expenditure	31.4	12.8	30.9	8.7	1.3	45.2
a.1 ADP expenditure	41.1	16.5	32.2	2.3	-4.9	41.5
a.2 Non-ADP expenditure	26.3	10.8	30.1	10.7	3.0	48.0

Source: Calculated from MoF data

Fiscal framework

- According to IMED data, ADP implementation rate was 32.3% during Jul-Feb FY23 - the lowest in the last decade
- Utilisation of project aid (PA) (35.7%) was marginally higher than the corresponding period of FY22 and was in line with the trend of last three-four years
  - It was the Power Division that primarily drove the utilisation of PA
- Utilisation of the local resource (taka) component (30.2%) was the lowest since FY14

Figure: ADP implementation scenario and reduction in RADP (in %)



Source: Calculated from IMED data

Fiscal framework

- Of the top ten ministries/divisions with a combined share of 72.5% of the total ADP allocation for FY23, four had below average utilisation rate
  - These are the Ministry of Science and Technology, Ministry of Primary and Mass Education, Health Services Division and Secondary and Higher Education Division
  - In the FY23 budget speech, ensuring timely completion of projects in education and health sectors was identified to be one of the major challenges for FY23
- The FY23 ADP was slashed by 7.5% – taking the RADP to Tk. 227,566 crore
  - A number of major government sectors (e.g., Education, Transportation and Communication, Health, and Power and Energy) were subjected to significant reduction in the RADP for FY23
- The reduction was fully on account of the PA component with the taka component remaining unchanged
  - Rather counterintuitive for two reasons: first, the rate of implementation of the PA component was better than that of the taka component, and second, in view of the ongoing foreign currency crisis, 'utilising funds available through foreign assistance', should have been given highest priority as mentioned in the budget speech

In light of the preceding discussion, the following suggestions are placed before the policymakers to take into account while formulating the national budget for FY24

- Personal income tax (PIT) structure in FY23 budget has remained mostly unchanged from the one introduced in FY21. CPD has argued that lowering of the highest tax rate (from 30% to 25%) went against the idea of tax equity. In the FY24 budget, the maximum tax rate should be restored to 30%
- Given the increased pressure of the commodity price hike, particularly those of food items, the tax-free income threshold for personal income should be increased to Tk. 3.50 lakh. As an alternative, in order to give the low-income earners some respite, the second PIT slab, which is 5% for an additional Tk 1 lakh, should be raised to Tk 3 lakh
- In the FY23 budget, the rate of investment tax rebate was fixed at 15% on the eligible amount. This means that higher taxpayers, i.e., top earners receive higher tax rebate benefits, whereas those with annual income below Tk. 15 lakh are not eligible to get any additional tax benefits. The withdrawal of this provision needs to be considered in the FY24 budget

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Fiscal framework

- The FY23 budget increased the allowable ceiling of perquisite from Tk 5.5 lakh to Tk 10 lakh. Accordingly, individuals with annual income ranging between Tk. 16.5 lakh and Tk. 30 lakh will receive additional tax benefits of up to Tk. 112,500 per year. This is another instance where the tax policies favour high-income groups. The FY24 budget may consider eliminating this clause
- All ad-hoc provisions of tax incentives should be stopped from FY24
  - NBR needs to be selective and careful in the next fiscal year as more demand for incentives will be lined up in view of current economic situation
  - Proper cost-benefit analysis must be conducted before coming up with new provisions
  - 'Sunset clauses' should be introduced in case of existing provisions
  - There should also be a medium-term plan and timeline as regards phasing out the various tax exemptions
  - An analysis of revenue forgone owing to the various tax exemptions should be provided in the next budget
    - This will draw much-needed political attention to this burning issue

Fiscal framework

- In the FY23 budget, a new provision (Section 19F: Special Tax Treatment in respect of undisclosed offshore assets) was added to the Income Tax Ordinance 1984 to mainstream money earned and asset acquired abroad into the economy
  - Such an initiative is ethically unacceptable, will discourage honest taxpayers, and has traditionally did not generate the intended revenue
  - CPD strongly feels that this provision should be discontinued, and no such incentive finds its place in FY24 budget
  - Provisions such as Section 16H, Section 19BBBBB, and Section 19DD are still in place to legalise undisclosed income and assets. These should be discontinued from FY24
- Since the income tax exemptions for 28 IT-enabled services (ITES) are set to come to an end in FY24, a thorough examination of the incentives should be undertaken with a view to (a) selection for continuation of incentives, (b) introduction of sunset clause and (c) identify opportunities for imposition of taxes on e-commerce and digital services

Fiscal framework

- The moratorium on e-commerce taxation is set to come to an end (by 2024 or 13th WTO Ministerial Conference – MC13, whichever is earlier if no agreement is reached in the WTO in this regard). The government should take adequate preparation to (a) proactively participate in the WTO discussions and (b) identify tax measures if and when the moratorium comes to an end
- Ambiguities in current tax laws (service code 99.60) in defining e-commerce activities should be removed to enhance the scope and opportunities of revenue mobilisation
- The government plans to install additional 300,000 electronic fiscal devices (EFDs) over the next five years, which is expected to yield an additional revenue of Tk. 10,500 crore, with an initial 60,000 planned for FY2024. NBR needs to aggressively pursue this target
- NBR should launch at the earliest, a comprehensive online payment system for VAT, income tax and customs together with an interface with iBAS++ and ensure harmonisation and taxpayer data sharing across various wings of the NBR as has been envisaged in the PFM Action Plan 2018-23
  - The data-sharing issue has also been raised by the IMF

Fiscal framework

- ❑ As per data from international sources, the larger part of Bangladesh's illicit financial outflows are on account of trade mispricing
  - ➢ The Transfer Pricing Cell (TPC) of NBR, Bangladesh Financial Intelligence Unit (BFIU) and Customs Intelligence and Investigation Directorate (CIID) should work closely to deal with this issue
  - ➢ For effective implementation of the responsibility of the TPC, the FY24 budget should ensure adequate allocation for technical and human resources and forensic investigation capacities of the aforesaid entities
- ❑ The FY24 budget must focus on generating revenue from specialised sources, particularly expediting the realisation of contested revenue claims through the Alternative Dispute Resolution (ADR) mechanism. Steps should be taken to expedite the resolution of pending tax-related cases
- ❑ Priorities for public spending ought to be set out clearly in the FY24 budget. The design of the budgetary framework should take cognisance of the rising cost of essentials. In order to do this, appropriate attention should be paid to food production, SSNPs (including public works programmes), subsidies for agriculture, energy and power sectors, as well as the health and education sectors
  - ➢ Supporting the marginalised groups should be the central focus of subsidy management

Fiscal framework

- Prior government directives to reduce "unnecessary and luxury" public spending (such as the purchase of government vehicles and international travel) should be reintroduced
- The ADP for FY24 should be carefully designed with a view to containing the budget deficit. A political government may find it tempting to take on new development initiatives in the run-up to the upcoming election by adopting a populist stance
  - The budget for FY24 should refrain from any ostentatious public spending in the backdrop of the macroeconomic challenges facing the economy
- The government should prioritise implementing all foreign-funded ADP projects in light of the current foreign exchange situation. The government should give higher priority to implementing projects that are nearly finished (about 90-95% completion rate in Jun 23)
- Projects that had a 10% or lower implementation rate up till end-FY23 should be deprioritised

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Fiscal framework

- "Carryover projects" that have a maximum implementation rate of less than 30% up till end-FY23 should be re-examined to justify continuation
- The government should form an independent commission to assess the rising costs of public infrastructure projects
  - Concrete steps should be taken to ensure good governance in implementation of public infrastructure projects in particular. As a first step, the government must make all development project proformas (DPPs) available to the public for review and comments
  - To do this, the government should also think about undertaking a comprehensive assessment of public expenditures as early as possible

Section 4: The cost of living crisis in Bangladesh

The cost of living crisis

- Inflationary pressures have been building in Bangladesh even before the situation in Ukraine began.
- Recent sharp swings in energy costs have made matters worse in Bangladesh.
- The continued price growth is due in part to domestic reasons including market distortion by a small number of dominant firms and lax regulation.
- There are a number of essentials that are more expensive in Bangladesh than in other developing or industrialised countries.
- Low-income families are fighting to make ends meet as the cost of living continues to rise.
- Many families, including minimum wage earners across all sectors, are struggling to make ends meet.

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Over-dependence on indirect taxes

- Analysis reveals that at least 28 imported essential food items, currently face a high incidence of tax.
- In the backdrop of the soaring inflation, the National Board of Revenue (NBR) should reduce the duties and taxes, both at import and domestic levels, for essential commodities to provide some respite to consumers with low and limited income.
- High inflation has revealed the inherent weakness in the government's domestic resource mobilisation approach which is largely dependent on revenue collection from indirect taxes.
- Thus, fiscal policy which is highly dependent on indirect taxes propagates economic inequality in society and forces the government to trade-off revenue generation in the face of high inflation.
- It is urgently required to increase revenue collection from direct taxation and reduce dependence on indirect taxes, especially since Bangladesh is now poised to graduate from the Least Developed Countries (LDC) group.

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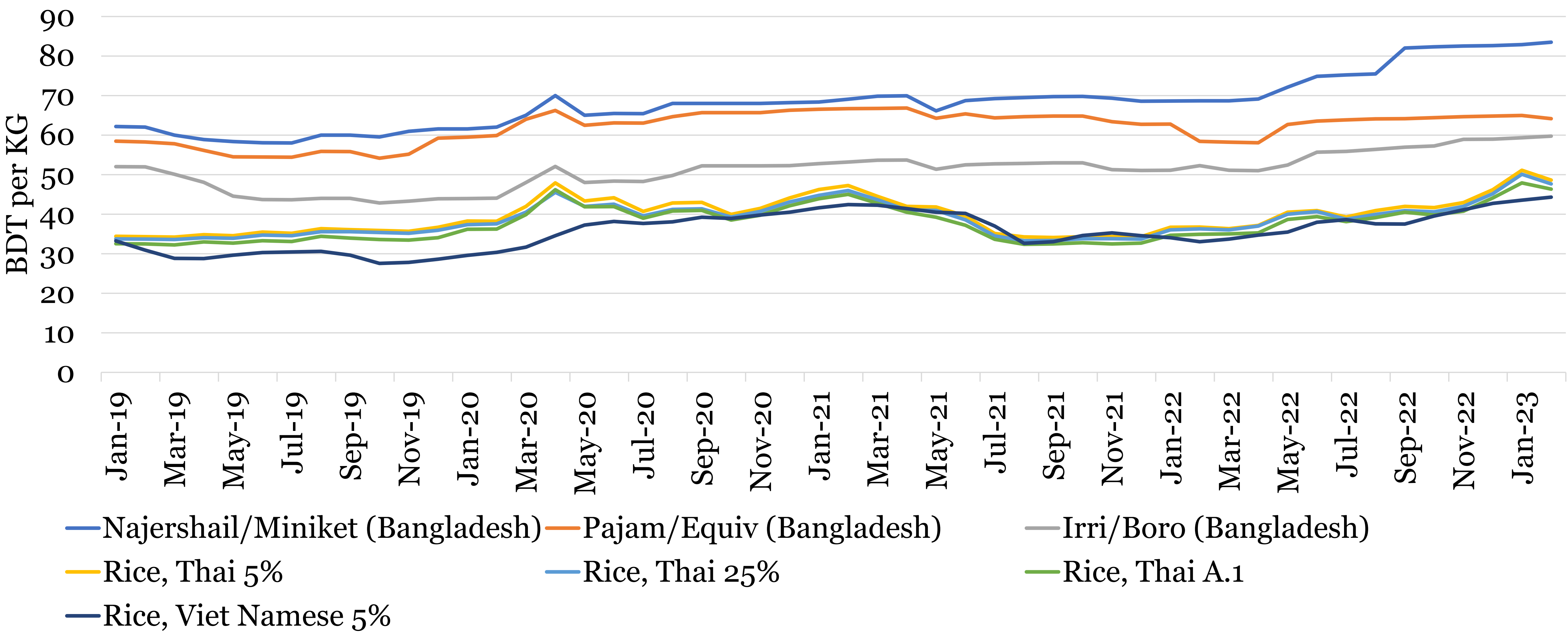
High prices only in Bangladesh?

- International comparison of prices shows that the price of essential food items do not fall in Bangladesh, even when the international prices fall.
- Additionally, the data also shows that the price of some essential food items remain consistently over the international prices.
- For brevity of exposition, we highlight the difference in domestic and international prices of four food items: rice, soyabean oil, sugar, and beef.
  - Out of these four, rice and beef are mainly produced domestically, whereas soyabean oil and sugar are mainly imported.
  - Nevertheless, we find that the price of all four items in Bangladesh is consistently higher than the international prices.

Price of rice

Figure: Price of rice in Bangladesh and international markets (in BDT per kg)



Price of soyabean oil

Figure: Price of soyabean oil in Bangladesh and international markets (in BDT per litre)

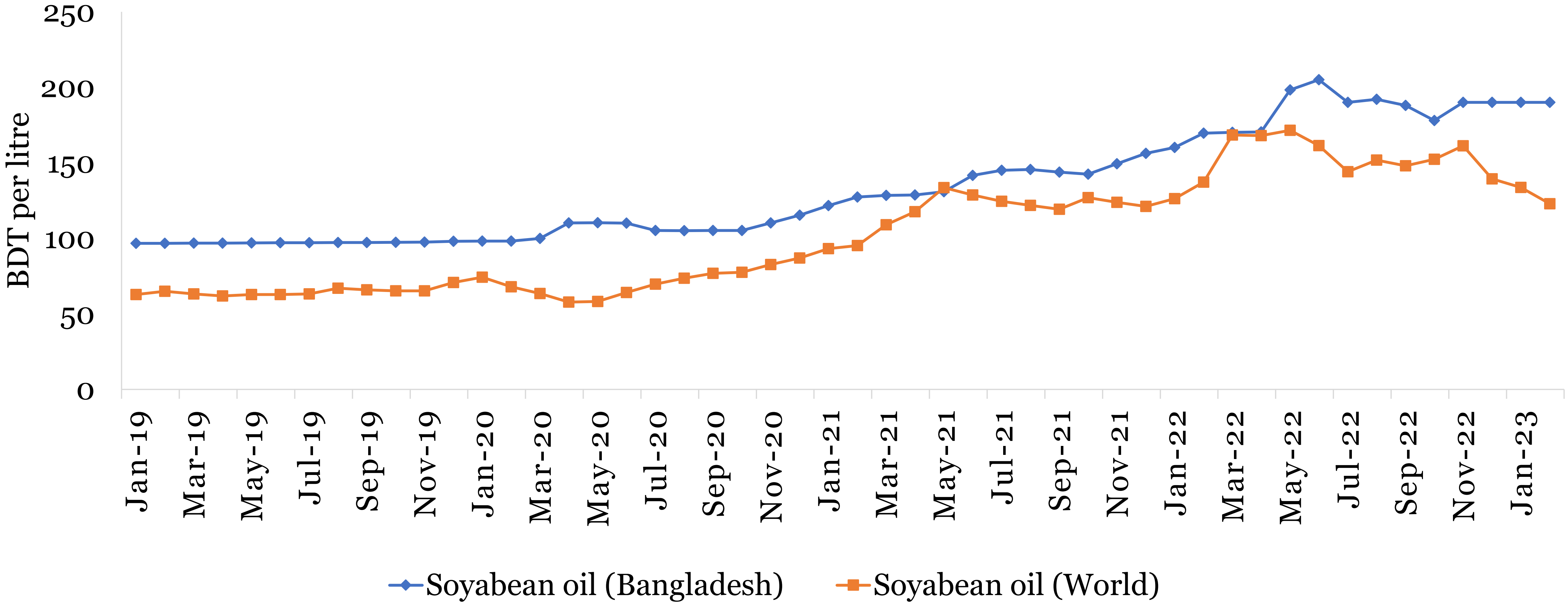
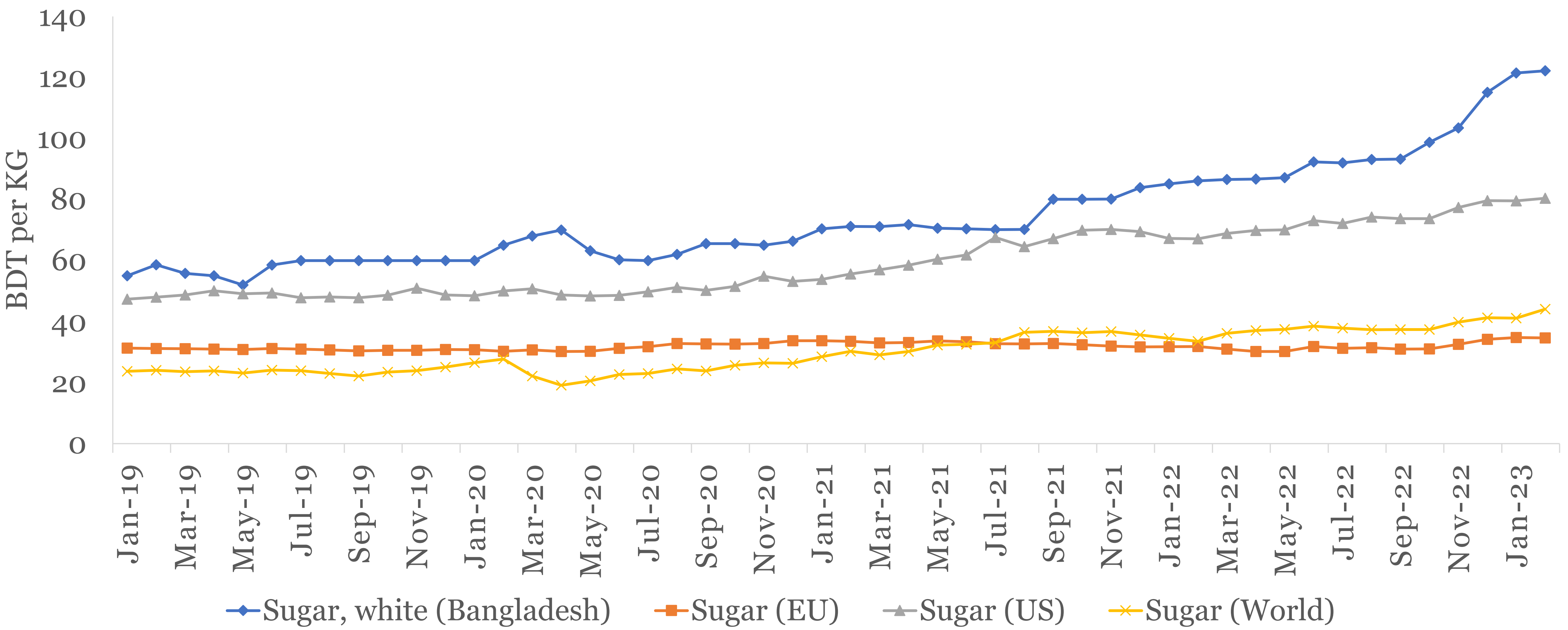


Figure: Price of sugar in Bangladesh and international markets (in BDT per kg)



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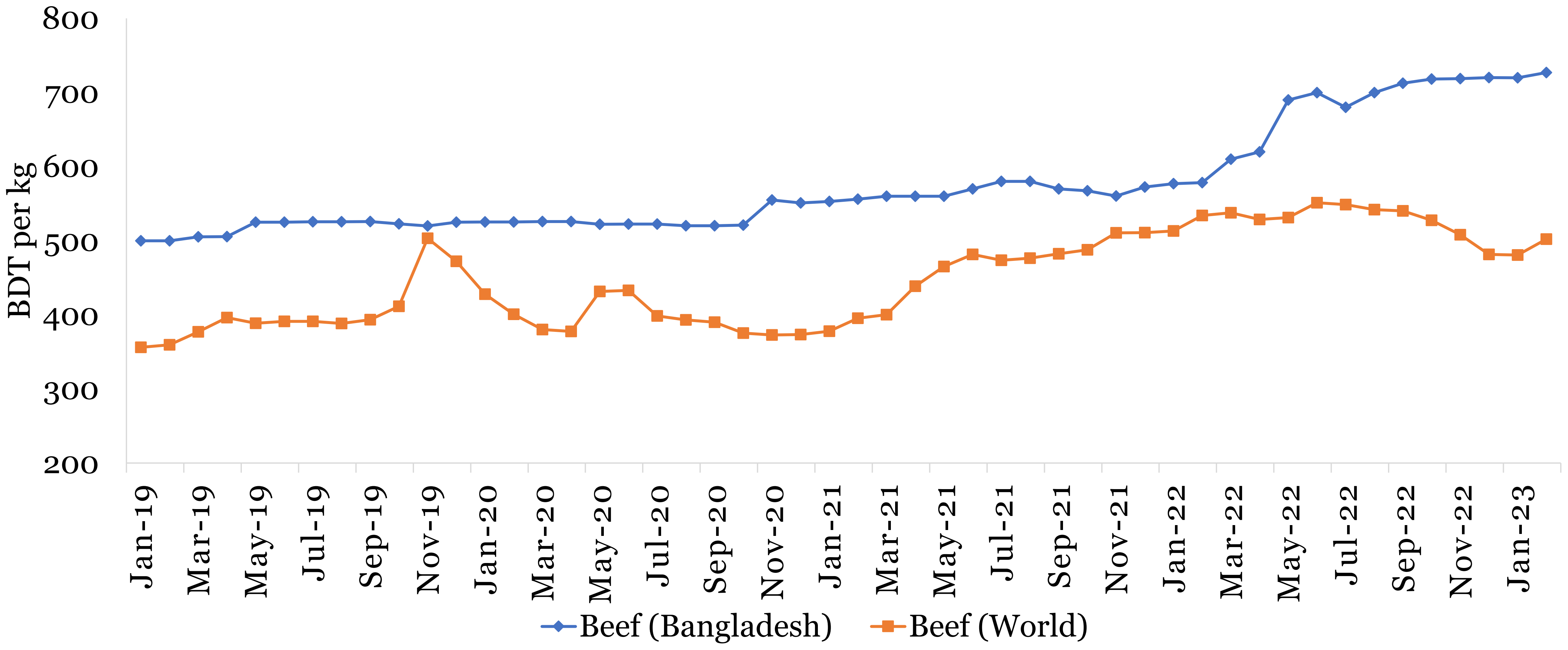
Price of beef

Figure: Price of beef in Bangladesh and international markets

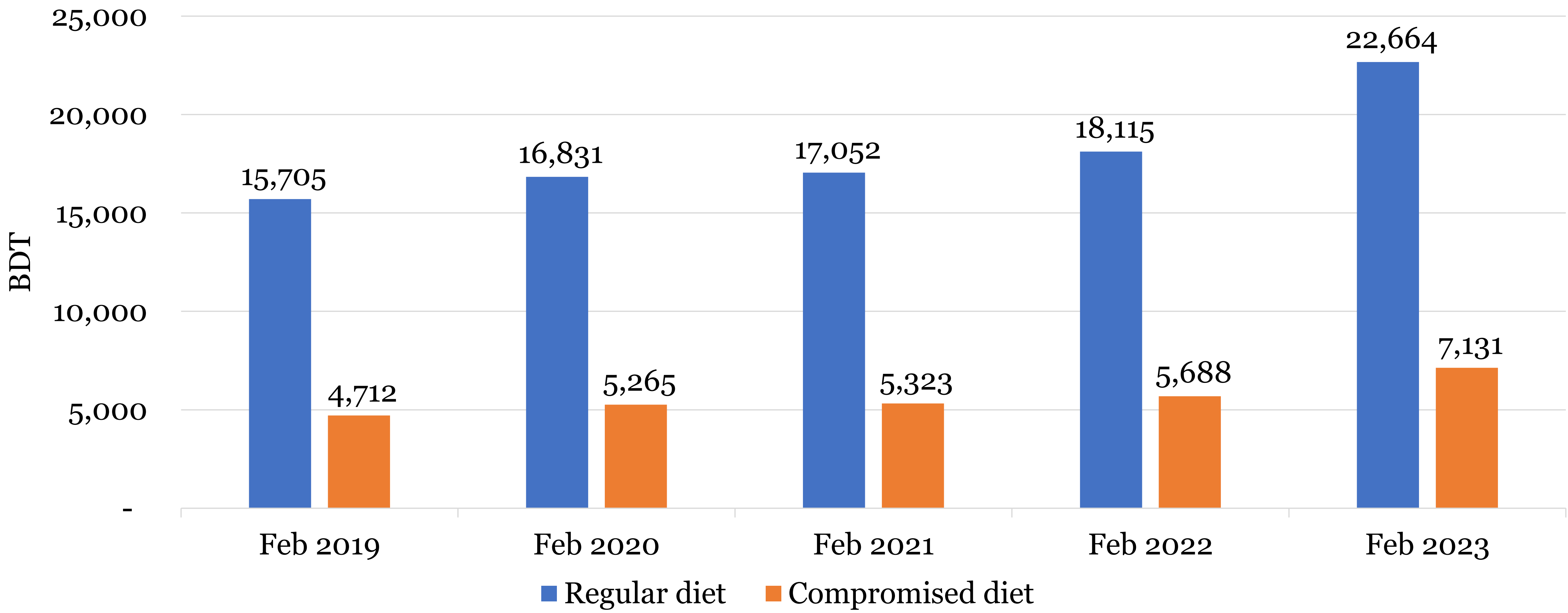


Is inflation a largely domestic phenomenon?

- These numbers indicate that the inflation prevailing in Bangladesh at present may not necessarily be imported inflation, as is commonly presumed.
- On the contrary, the inflation in Bangladesh appears to be a largely domestic phenomenon.
- As a result of these price increases, the cost of living has increased rapidly causing immense suffering to low income and fixed income households.

Average monthly food expenses

Figure: Average monthly food expenses for a household of 4 individuals in Dhaka city (in BDT)



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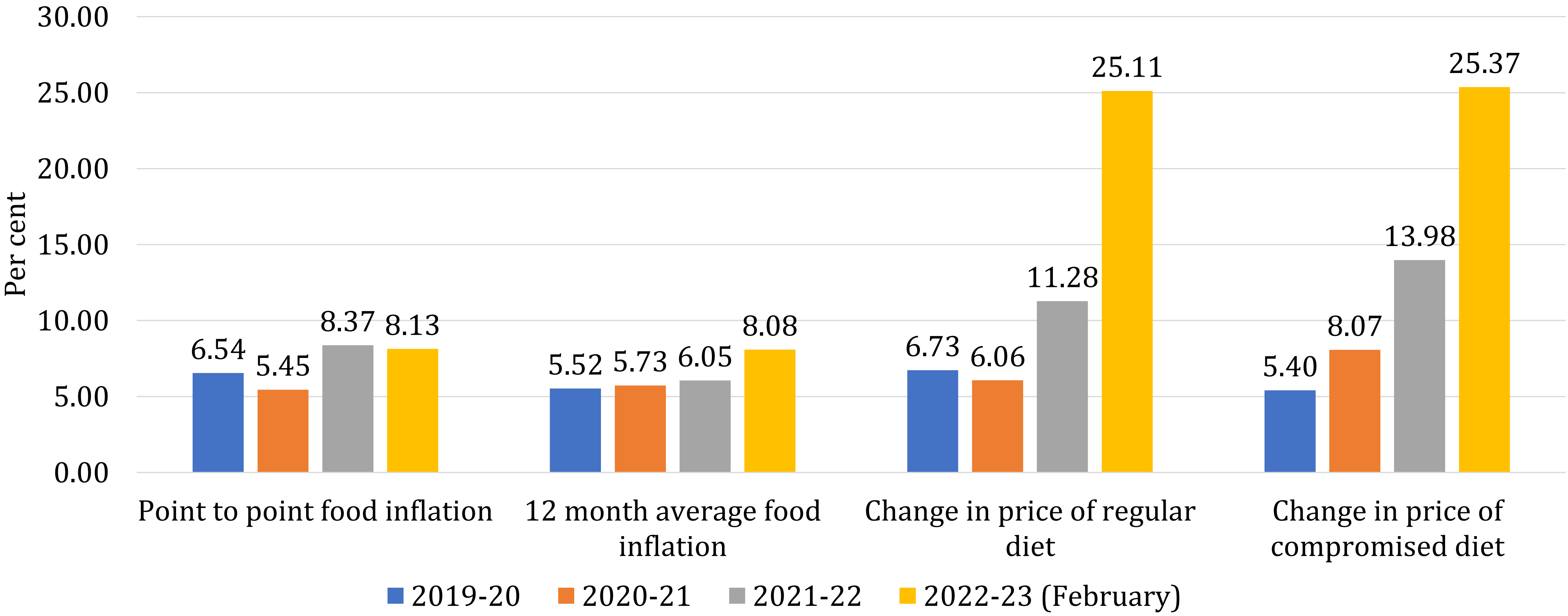
Food inflation versus change in price of essential food items

Figure: Food inflation versus change in price of essential food items



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Recommendations

- The Minimum Wage Board should consider increasing the minimum wages in all industries so that workers earning minimum wages may at least afford basic food. Private sector corporations should consider a higher salary increment in 2022, given that a 5 per cent increment of salary in the face of double-digit price hikes is compelling workers to seriously compromise their standard of living.
- Government should carefully examine the duty and tax structures of the essential commodities, both at import and domestic levels, and make downward adjustments with a view to provide some respite to low and limited income-earning consumers. The increased price level of most of the other commodities should be able to compensate for the potential revenue loss to this end.
- Tax-free income threshold for personal income should be raised to Tk. 3.50 lakh in view of the added pressure of the rising food inflation and income erosion induced by the pandemic. The next slab for personal income tax, which is 5 per cent for an additional Tk. 1 lakh, should be increased to Tk. 3 lakh to provide a cushion for the middle-income earners.

Recommendations

- Volume of essential commodities sold through the open market system (OMS) should be increased. Government should set higher targets for foodgrains procurement and food distribution programmes. To this end, adequate resources should be allocated in the FY2023 budget. Furthermore, the distribution of these commodities must be managed efficiently and without corruption so that only the eligible can obtain the essential items at lower prices.
- Competition Commission's role should be strengthened. Required skilled professionals should be hired to this end, particularly with a view to monitoring markets for essential commodities on a regular basis. The Commission should create a database, monitor the operations of prominent market players on a regular basis, investigate market control and manipulation (if any), and take appropriate actions. An adequate budget should be earmarked for the Commission to perform these duties. To this end, the Ministry of Commerce should also work in tandem with the Commission. The Bangladesh Competition Commission should adopt a strong stance against cartels and a zero-tolerance policy towards collusive practices. Furthermore, the Competition Act 2012 should be revised to directly address monopolies and include specific anti-trust clauses, along with concrete penalties for violators.

Recommendations

- Government should provide additional support for subsidised credit programmes for the agriculture sector (both crop and non-crop) to incentivise production during the next fiscal year.
- Government should continue providing stimulus to the small and medium enterprises to help them survive the difficult times.
- Government should extend the scope of direct cash/kind assistance programmes for low-income population groups.

Section 5: Subsidy rationalisation and subsidy management in major sectors

Subsidy rationalisation and subsidy management in major sectors

- The subsidy expenditure of the government has skyrocketed within a short period of time and has become a major concern in view of limited fiscal space.
  - In the national budget FY23, total subsidy expenditure is projected to be Tk 82,745 crore, which is about 1.9% of GDP (Table 5.1)
  - The subsidy is distributed in three forms- (a) cash loan, (b) subsidy, and (c) fiscal incentives. Rise of cash loans to Bangladesh Power Development Board (PDB), subsidy to gas and cash incentives to agriculture and remittances are the main areas that caused such a rise in subsidy expenditure in recent years.
- Hence, the government has made specific commitments with regard to subsidy rationalisation and management as part of meeting the loan conditionality set by the IMF

Table 5.1: Total Subsidy (in Billion BDT and as % of government expenditure)

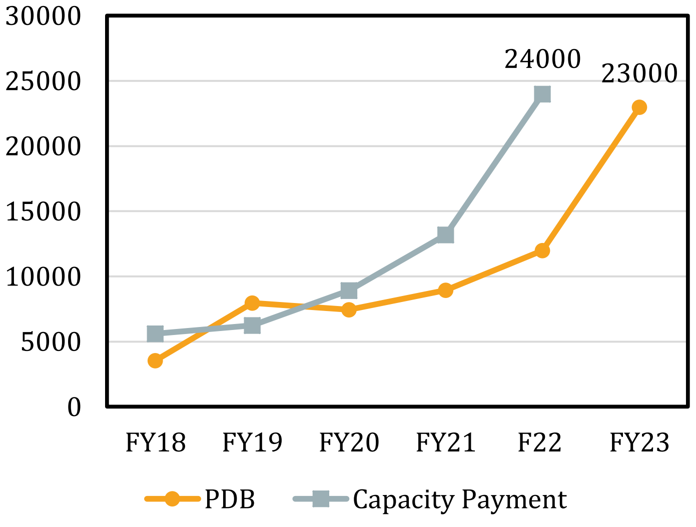
Items	Subsidy (Tk in billion)							
	FY16	**FY17**	**FY18**	**FY19**	**FY20**	**FY21**	**FY22**	**FY23**
Cash loan	29.07	51.73	35.52	113.41	128.86	110.49	133.73	
Subsidy	10.86	29.43	50.20	91.44	76.86	89.57	208.0	
Fiscal incentives	99.31	80.05	96.81	118.17	213.54	182.56	260.25	
Total subsidy	139.24	161,21	182.53	323.02	419.26	382.62	601.98	**827.45**
% of government expenditure	5.8	6.0	5.67	8.25	10.14	8.22	10.15	**12.20**
% of GDP								**1.9**

Source: Based on Ministry of Finance

5.1 Subsidy in the Power and Energy Sector

- ❑ The power and energy sector is the government's biggest subsidy expenditure shareholder (40% of the total subsidy allocation in FY23).
  - ➢ Within this sector, the power sector gets the lion's share of the distribution (79.3% of total allocation for the sector)
    - During the budget of the FY23, a subsidy of Tk 17,000 crore was proposed for the power sector which has been revised upward to Tk 23,000 in the revised budget for FY23
    - In the budget for FY23, Tk 6,000 crore was proposed for importing LNG
    - There is no subsidy allocated for imported petroleum
- ❑ BPDB claims subsidy for the power sector with the argument of rising import price of raw materials such as- HSD, HFO and LNG and their higher transmission and distribution costs to the power plants.
  - ➢ However, a large part of the subsidy burden is caused due to excess power generation capacity and resultant capacity payment to the independent power producers (IPPs) (figure 5.1.1)

Figure 5.1.1: Trend of subsidy and capacity payment (crore Tk)



Source: MTMPS 2022- 23 to 2024- 25, TBS

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Subsidy rationalisation and subsidy management in major sectors

- Bangladesh's government has resumed LNG import from the international market and intends to import even more LNG in future to meet the gas shortages will cause a higher subsidy burden
  - A part of the high expenses has been met by passing it on to the consumers at a high retail price of LNG/gas
- BPC requested a subsidy of Tk 19,358 crore at a later stage which is not accepted with the argument that it is making a profit on petroleum products (e.g., diesel) after the recent adjustment of tariff at the retail level
- The government has gradually increased the retail price of electricity, gas and fuel to align with the government's commitment to comply with IMF condition of slowly moving towards market-based tariff rates for petroleum products

Subsidy rationalisation and subsidy management in major sectors

1) **Subsidy of the power sector should be rationalised by reducing the burden of capacity payment provided to IPPs and QRRs**
   - The government should gradually step out of the vicious cycle of capacity payment to the IPPs and QRRs through signing/renewing agreements under 'no electricity, no pay' clause

2) **A market-based price-setting mechanism should be introduced in the power and energy sector under Bangladesh Petroleum Corporation (BPC)**
   - As the energy prices at global market is gradually declining, and domestic petroleum companies are now in surplus, it is the right time to introduce a periodic formula-based fuel price adjustment mechanism
   - BPC should start market-determined price-setting mechanism for petroleum prices from July 2023
     - The price can be monitored and adjusted on a monthly basis in accordance to the global energy market

Subsidy rationalisation and subsidy management in major sectors

3) Budget allocation should be provided on a priority basis for domestic gas exploration

- The national budget of the ongoing fiscal year neither has projects relating to gas exploration nor includes an allocation for intensive gas exploration and expedited work plan
- The ongoing exploration programme must be implemented earliest possible with necessary fiscal support its short-term exploration programme by drilling 22 wells

4) Promoting clean energy could ultimately help the power and energy sector out of subsidy burden

- The government needs to take measures such as reduction of customs duty and VAT on renewable energy-related technologies and types of machinery
  - Even subsiding clean energy-based projects and initiatives can create a level playing field
- The renewable energy project investors in public and private sectors get exemption from corporate income tax for 5 years
- They should be provided 10 years of tax holiday as fiscal support

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5.2 Fiscal incentives for the Export Sector

- In the national budget for FY23, significant fiscal incentives were allocated for the export sector, like those in earlier fiscal years
  - The number of items eligible for different export cash incentives increased to 43 in FY23
  - RMG products were made eligible for multiple kinds of cash incentives
- Fiscal incentives for export products and jute goods have been consistently increasing in line with the rise in the export of different export products
  - During FY22, a total of Tk 9,000 crore (including for Jute) was spent as incentive to the export sector (according to Ministry of Finance)
  - Majority of export cash incentives have been in effect without any specific time period over a long period
  - Uncertainty remains over the real effectiveness of these incentives in promoting the export of these products in traditional and non-traditional markets (such as a negative relation between cash incentives and export performance for Nepal found by Paudel et al., 2020)
  - A major overhauling in the structure of cash incentives for the export sector is needed targeting the future outlook of the country's export

Subsidy rationalisation and subsidy management in major sectors

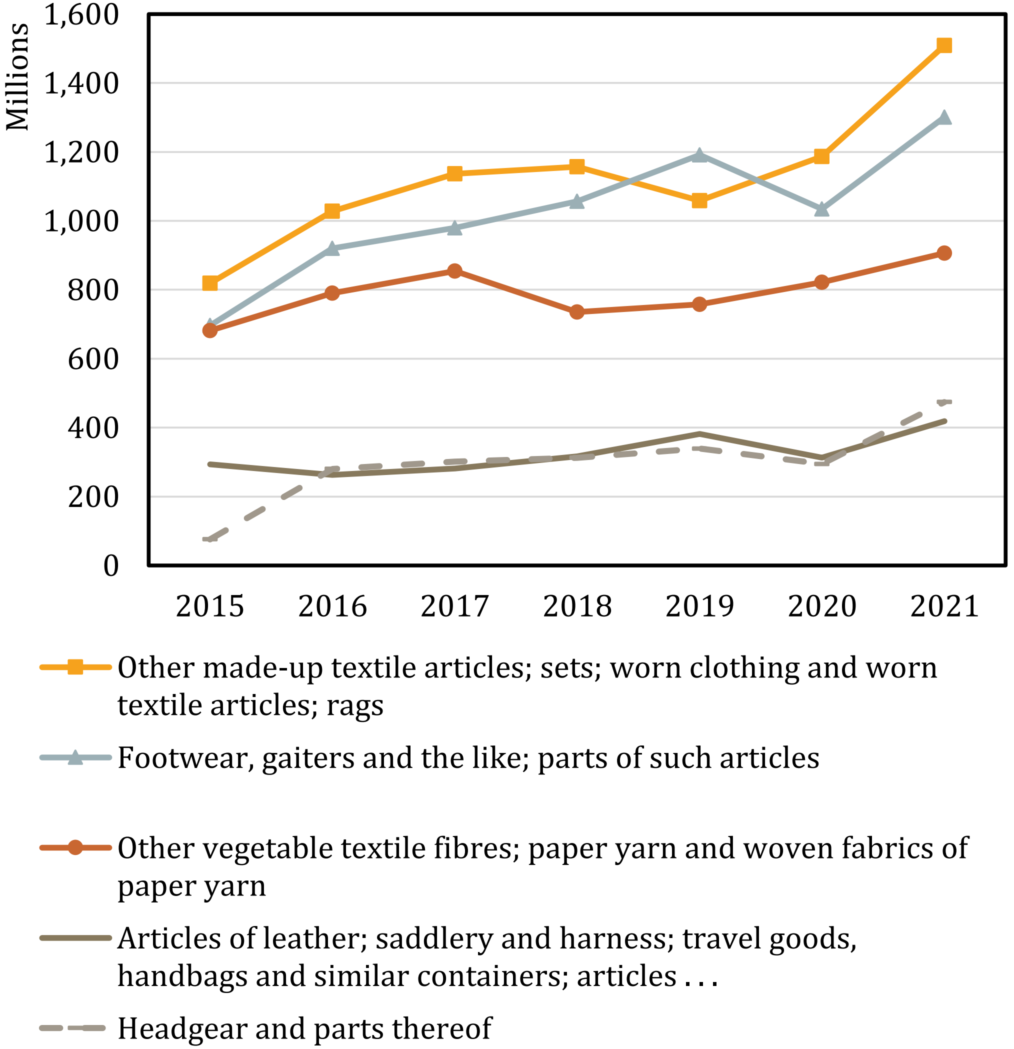
1) A detailed study on the assessment of the effectiveness of cash incentives for export needs to be undertaken:

- The Ministry of Commerce, with the support of the Bangladesh Trade and Tariff Commission, should undertake a detailed study to assess the effectiveness of cash incentives for export products
- Such a study should help assess whether the cash incentives were able to achieve the targets, identify the demand for existing cash incentives, and identify the requirement for cash incentives for new and emerging products
- It will also assist in redistributing the cash incentives for promoting intra-RMG and non-RMG diversification

2) Give more priority to non-RMG sectors for providing export cash incentives:

- Although the rate of cash incentive for RMG is lower than the many non-RMG products, given that RMG industry exports the highest amount, the sector also gets the highest amount of cash incentives
- In view of promoting export diversification, the national budget for FY24 may consider shifting a portion of RMG cash incentives to non-RMG products that have higher export potential

Figure 5.2.1: Export trend of some key non-RMG product (in million USD)



Source: ITC Trade Map (2023)

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Subsidy rationalisation and subsidy management in major sectors

3) Allocate more subsidy for non-cotton textiles:

- The increase in global demand for blended fabrics and apparel at the consumer level has led to an increase in the demand for non-cotton textiles as well
- However, Bangladeshi textile still has a limited capacity to produce non-cotton textiles (manmade fibre, synthetic fibre, polyester etc.)
- The budget of the current fiscal year (FY23) did not allocate any dedicated subsidy for non-cotton fabrics
- Providing special cash incentives for exporting non-cotton products in the national budget for FY24 would enhance export outside cotton-based products

4) Find out strategies to gradually withdraw traditional cash incentives for export:

- After Bangladesh graduates from the LDC category in 2026, it cannot provide cash incentives for export in its current form as per WTO rule
- Hence, the government needs to gradually reduce subsidies from the export sector to let it be prepared for the post-LDC scenario
- While direct export subsidy gradually needs to be reduced, at the same time, innovative incentive schemes (such as subsidy for skill and technology upgradation, active labour market programmes, social safety net programmes, health insurance and support for ease of doing business etc.) needs to prioritise for supporting the export industry

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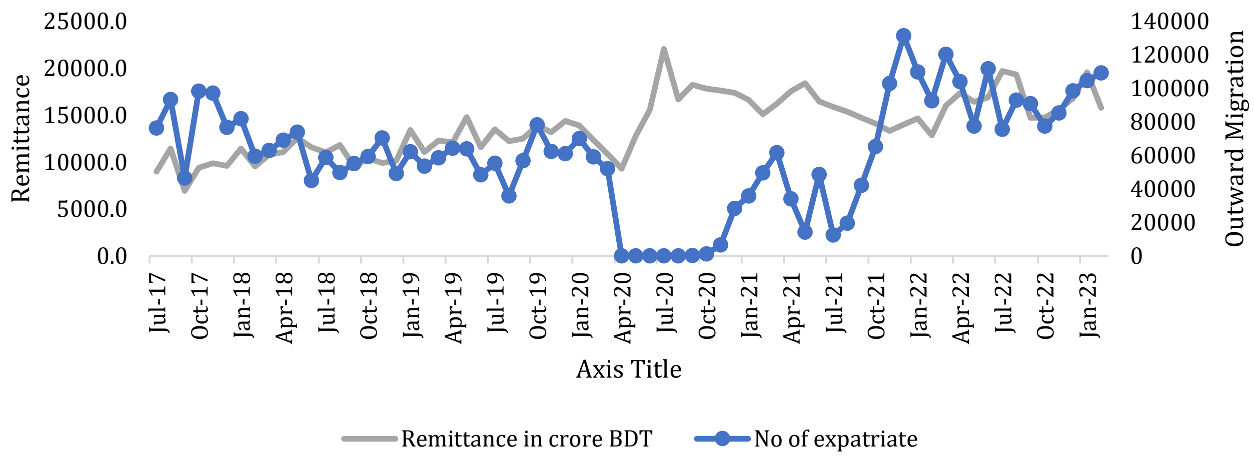
5.3 Cash incentive for Inward Remittance

- Over the years, cash incentives have been on the rise because of the rising remittance inflow– from BDT30.6 bl in FY20 to BDT50 bl in FY22 owing to the record number of workers migration in FY23 (up to February 23) (Fig 5.3.1)
  - The remittance inflow in every month has remained within a limit indicating a part of the remittance is likely to be sent to the country through the informal channel
  - Since the introduction of cash incentives on workers' remittances in FY20, the govt. has spent a total of Tk15,442 crore
  - CID has found that hundi traders laundered Tk 75,000 crore in 2021 through different MFS operators which is 35.7% of the formally remitted amount

Figure 5.3.1: Remittance earnings (in crore BDT) and outward migration



Source: Based on Bangladesh Bank (2023)

1) Introduce the market-based exchange rate to reduce the exchange rate gaps

- The government may consider introducing market-based exchange rates between USD and BDT
- At present exchange rate against USD is Tk 113 (as of 25 March 2023), while the remittance exchange rate is Tk 107 (as of 22 March 2023)
- Such a measure would reduce the demand for cash incentives for inward remittance as the exchange rate would be considerably higher – above the 2.5% cash incentives provided at present
- This would reduce the demand for using the informal channel to remit forex abroad

2) Preventing the hundi business by strengthening operations in the banking channel as well by the Police

- The central bank, commercial banks and law enforcement agencies should work hard to trace, track and identify hundi agents and hand them over to law enforcement agencies
- The Bangladesh Bank and other government organisations related to the prevention of anti-laundering must be more vigilant in tracking and prosecuting hundi operators
- The central bank has anti-money laundering guidelines to detect and prevent this activity which should be strictly implemented

3) Proactive role of embassy and consulate at migrant destination countries

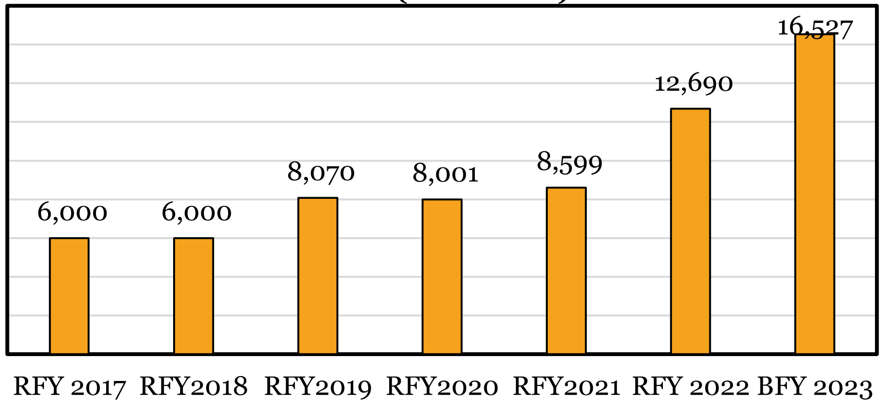
- The government has an established network in foreign countries where a number of labour attaché are available for ensuring the welfare of the migrant workers
- In this regard, labour attaché can play a proactive role in terms of encouraging migrant workers to remit money through formal channels
- Necessary allocations should be made for the Ministry of Foreign Affairs and MoEWOE to increase the number of labour attaché or to take initiatives to source services from private agencies to meet the demand of the migrant workers in the destination countries
- The services will include establish awareness against the hundi transaction and promoting formal remittance channels, and benefits for migrant workers for remitting money through formal channels

Subsidy rationalisation and subsidy management in major sectors

5.4 Subsidy in Agriculture

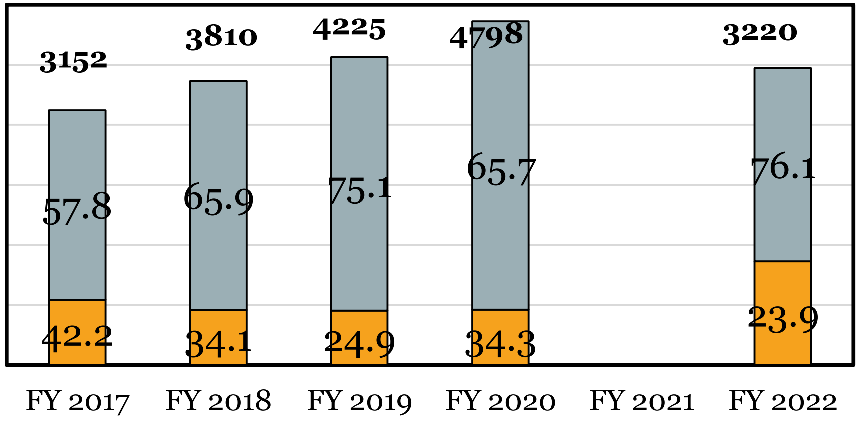
- The agriculture sector has been one of the biggest subsidy recipients in the national budget
  - For the current fiscal year (FY23), a total of Tk 16,527 crore was proposed as subsidy for the agriculture sector, the highest-ever budget allocation for agriculture subsidy (Figure 5.4.1)
- Along with the lion's share of agriculture subsidy for the fertilisers, the budget proposed to continue providing incentives for agriculture mechanisation, rehabilitation aid, rebate on the electricity bills for the electricity use in irrigation pumps (20%), subsidised interest rate credit for farmers (at 4% interest), and cash incentive for export of agriculture products (20%)
- However, continuing the same subsidy facilities for the upcoming fiscal year (FY24) could be challenging
- In view of the shortage of gas supply, the public fertiliser company (i.e., Shahjalal Fertiliser Company) has stopped their operation lately while the increase in the import cost has led to a decrease in the amount of fertiliser imported
- Hence, after a consecutive rise in recent years, the fertiliser supply fell during FY22 (Figure 5.4.2)

Figure 5.4.1: Allocation of subsidy for agriculture sector (in Tk crore)



Source: Ministry of Finance

Figure 5.4.2: Total (in '000 mt) and share of import and production of fertiliser in Bangladesh



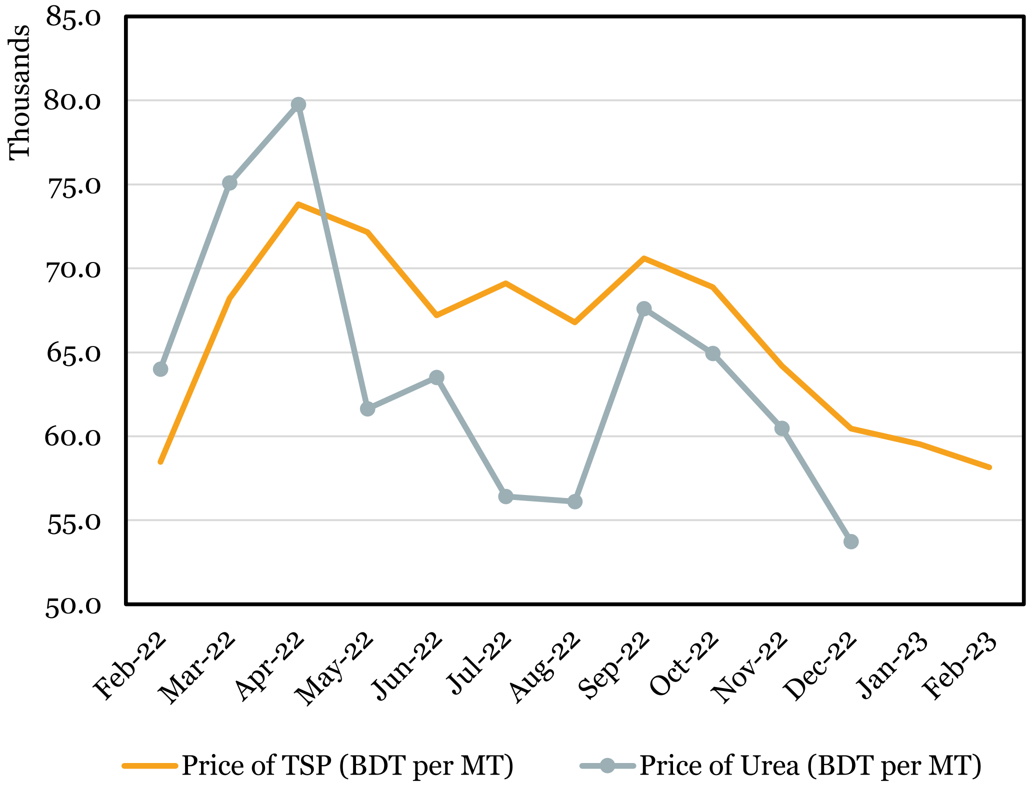
Source: Based on FPMU website data

Subsidy rationalisation and subsidy management in major sectors

1) Continue providing higher subsidy for fertiliser:

- Irrespective of the current fiscal space status and other challenges, the fertiliser subsidy must be continued in the FY24 to ensure food production gets the utmost priority in a time of uncertainty over the global food supply
- The extent of the burden for subsidising fertiliser in the upcoming fiscal year (FY24) is expected to be slightly less than the current fiscal year
- The reasons include-
    - a) the recent decreasing trend of the price of fertilisers in the international market (despite an increase in the price of the US dollar) (Figure 5.4.3);
    - b) the government has already increased the price of Urea by Tk 6 per kilogram in August 2022 (both at dealer and farmer levels); and
    - c) the decrease in requirement of subsidies in other sectors, mainly in the energy sector (as per conditions set by IMF)

Figure 5.4.3: Global monthly price of fertilisers



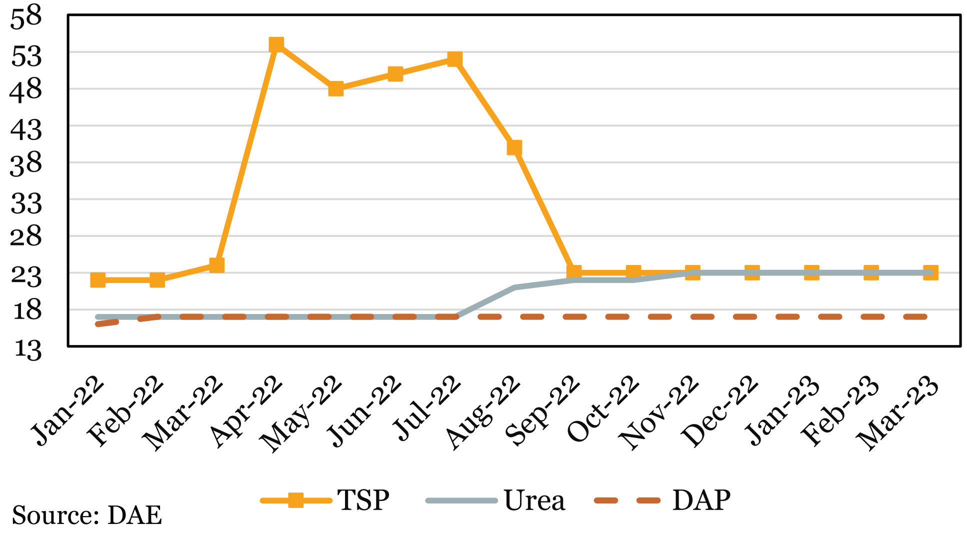
Source: Based on World Bank

Subsidy rationalisation and subsidy management in major sectors

2) Go for more effective subsidy management:

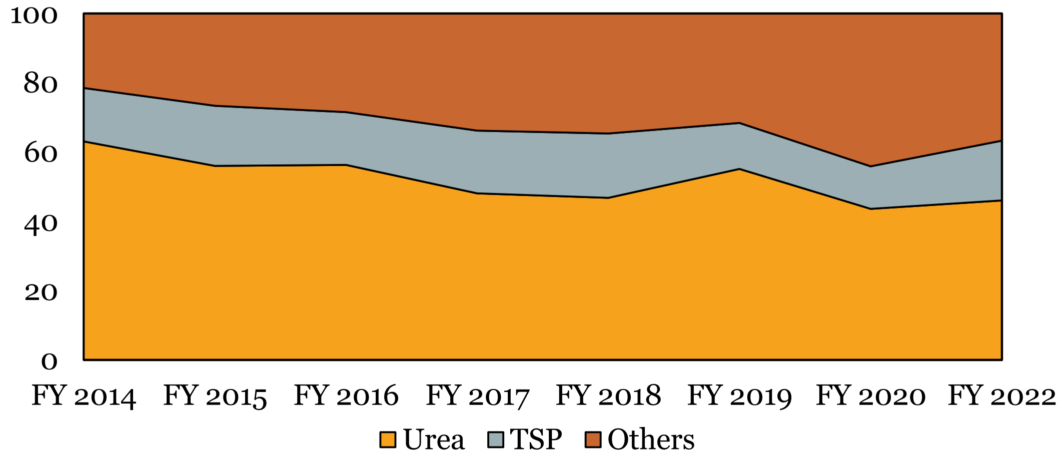
- While the subsidy needs to be there for fertiliser, proper subsidy management can ease the fiscal burden and yield more benefits. Some of the areas need particular attention:
- The strengthening of market monitoring mechanism must be ensured in view of continuous allegations that farmers in many places are being unable to buy fertilisers at a subsidised price (Also reflected partly in Figure 5.4.4)
- Higher allocation should be considered on promoting the use of balanced fertiliser so that the misuse of fertiliser gets decreased along with increases in the production (Figure 5.4.5 indicates that the share of the supply of fertiliser is still higher for urea alone)
- Continue allocating a sizable share of funds for agricultural research targeting decreasing the use of fertiliser and increasing the use of technologies to enhance production

Figure 5.4.4: National average monthly price of fertiliser (Tk per KG)



Source: DAE

Figure 5.4.5: Share of market supply of different fertilisers (domestic production + import)



Source: FPMU

Subsidy rationalisation and subsidy management in major sectors

3) Pursue scope of quick transformation to solar-based irrigation system from diesel-based irrigation system :

- Although the current fiscal year's budget enabled the facility of subsidised electricity price for irrigation, it could be difficult to carry on providing this subsidy in the coming year
- Moreover, the government needs to comply with the conditionality of the IMF of lifting subsidy from diesel price
- Hence, a distinct focus needs to be made on the quickest transformation of solar-based irrigation systems from diesel-based irrigation.
- In this regard, the target of transforming 200 diesel-based irrigation by 2023 to solar-based ones should be ensured
- More importantly, a plan needs to take to transform 1.34 million diesel-based power pumps into solar-based ones by 2030

Section 6: Fiscal policy for maximising social welfare

Independent Review of Bangladesh's Development (IRBD)

Budget allocation in health sector

- ❑Bangladesh's **budget allocation for the health sector** has been **less than 1% of GDP for more than a decade**
- ❑On the contrary, *in 2017 at least 30 Least Developed Countries (LDCs) spent more than 1% of GDP on health*
- ❑**The out-of-pocket expenditure on health in Bangladesh is the highest sixth highest in the world in 2019**
- ❑It is necessary to increase the budget allocation and budget utilisation of the health sector, and also implement a number of fiscal measures to promote improved public health and in turn maximise welfare for society

A single and specific tax on cigarettes: BDT 10 per stick

- The government should **eliminate the tiers of cigarette taxation and replace them with a single universal system**
- Additionally, **a specific excise duty, which is fixed per stick and per pack, should be implemented** instead of an ad valorem tax

Proposed tax structure for cigarettes (per pack of 10 cigarettes)

Current tax structure in FY 2021-2022						Proposed tax structure for FY2022-2023				
	Retail price		SD				Retail price		Specific excise duty	
Tier	Pack of 10 (in BDT)	Per stick (in BDT)	Per pack of 10 (in %)	Per pack of 10 (in BDT)	Per stick (in BDT)	Tier	Per pack of 10 (in BDT)	Per stick (in BDT)	Per pack of 10 (in BDT)	Per stick (in BDT)
Low	40+	4.0	57	22.80	2.28	Universal	Market based	Market based	100	10
Medium	65+	6.5	65	42.25	4.22					
High	111+	11.1	65	72.15	7.21					
Premium	142+	14.2	65	92.30	9.23					

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A single and specific tax on Bidi: BDT 3 per stick

CPD proposes a specific excise tax of BDT 3 per stick for all Bidi to be implemented in FY24

Proposed tax structure for Bidi

<table>
<tr><th colspan="6">Current tax structure in FY 2021-2022</th><th colspan="5">Proposed tax structure in FY2023-24</th></tr>
<tr><th></th><th colspan="2">Retail price</th><th colspan="3">SD</th><th></th><th colspan="2">Retail price</th><th colspan="2">Specific excise duty</th></tr>
<tr><th>Type of bidi</th><th>Per pack (in BDT)</th><th>Per stick (in BDT)</th><th>Per pack (in %)</th><th>Per pack (in BDT)</th><th>Per stick (in BDT)</th><th>Type of bidi</th><th>Per pack (in BDT)</th><th>Per stick</th><th>Per pack (in BDT)</th><th>Per stick (in BDT)</th></tr>
<tr><td>Non-filtered 25 stick handmade bidi</td><td>18</td><td>0.72</td><td>30</td><td>5.40</td><td>0.22</td><td rowspan="5">All</td><td rowspan="5">Market based</td><td rowspan="5">Market based</td><td>75</td><td rowspan="5">3</td></tr>
<tr><td>Non-filtered 12 stick handmade bidi</td><td>9</td><td>1.33</td><td>30</td><td>2.70</td><td>0.23</td><td>36</td></tr>
<tr><td>Non-filtered 8 stick handmade bidi</td><td>6</td><td>1.33</td><td>30</td><td>1.80</td><td>0.23</td><td>24</td></tr>
<tr><td>Filtered 20 stick handmade bidi</td><td>19</td><td>1.05</td><td>40</td><td>7.60</td><td>0.38</td><td>60</td></tr>
<tr><td>Filtered 10 stick handmade bidi</td><td>10</td><td>1.00</td><td>40</td><td>4.00</td><td>0.40</td><td>30</td></tr>
</table>

A single and specific tax on Jarda and Gul: BDT 6 per gram

- CPD proposes a **specific excise duty of BDT 6 on per gram of Jarda and Gul** to be implemented in FY24
- Such a specific tax on Jarda and Gul should be increased by at least BDT 1 each year, to account for annual inflation and income growth

Proposed tax structure for Jarda and Gul

<table>
<tr><th colspan="6">Current tax structure in FY2022-2023</th><th colspan="5">Proposed tax structure in FY2023-2024</th></tr>
<tr><th></th><th colspan="2">Retail price</th><th colspan="3">SD</th><th></th><th colspan="2">Retail price</th><th colspan="2">Specific excise duty</th></tr>
<tr><th>Type of product</th><th>Per 10gm (in BDT)</th><th>Per gm (in BDT)</th><th>Per 10 gm (in %)</th><th>Per 10 gm (in BDT)</th><th>Per gm (in BDT)</th><th>Type of product</th><th>Per 10gm (in BDT)</th><th>Per gm (in BDT)</th><th>Per 10gm (in BDT)</th><th>Per gm (in BDT)</th></tr>
<tr><td>10gm Jarda</td><td>40</td><td>4</td><td>55</td><td>22</td><td>2.2</td><td>10gm jarda</td><td rowspan="2">Market based</td><td rowspan="2">Market based</td><td rowspan="2">60</td><td rowspan="2">6</td></tr>
<tr><td>10gm Gul</td><td>20</td><td>2</td><td>55</td><td>11</td><td>1.1</td><td>10gm gul</td></tr>
</table>

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Health Development Surcharge and VAT on cigarettes and other tobacco products

- We propose that that the **Health Development Surcharge** on cigarettes and other tobacco products to be **increased from 1 per cent to 5 per cent**, and the **VAT** on cigarettes and other tobacco products to be **increased from 15 per cent to 20 cent** in FY24

Proposed Health Development Surcharge and VAT on cigarettes and other tobacco products

	Current Tax Structure for FY23		Proposed Tax Structure for FY24	
	Health Development Surcharge (in per cent)	VAT (in per cent)	Health Development Surcharge (in per cent)	VAT (in per cent)
Cigarettes	1	15	5	20
Biri	1	15	5	20
Jarda	1	15	5	20
Gul	1	15	5	20

Corporate tax on tobacco product manufacturing companies

- The effective tax for a publicly listed tobacco company **deceased by 1 percentage point in 2022**
- CPD proposes that the **corporate tax on all companies manufacturing tobacco products** to be **increased** from 45% in FY22 to **50% in FY24**, and the associated **surcharge** to be increased from 2.5% in FY22 to **5% in FY24**
- The National Board of Revenue (NBR) should not give highest taxpayer award or any other social recognition to any individual or company involved in the tobacco business.

Proposed corporate tax on tobacco product manufacturing companies

	Current tax structure in FY23		Proposed tax structure for FY24		Proposed tax structure for FY26	
Type of company	**Corporate tax (in %)**	**Surcharge (in %)**	**Corporate tax (in %)**	**Surcharge (in %)**	**Corporate tax (in %)**	**Surcharge (in %)**
All companies manufacturing tobacco products	45	2.5	50	5	55	7.5

High opportunity cost of tobacco cultivation

- **Tobacco leaf cultivation used up 99,600 acres of arable land** in Bangladesh in 2020-21
  - The quantity of **boro rice** that could be produced on this land could meet the demand of additional **12.5 Lakh** people for a **whole year**
  - The quantity of **wheat** that could be produced on this land could sustain the wheat demand of additional **1 crore 84 lakh** people for a **whole year.**
- Tobacco leaf export has more than doubled in the last fiscal year.
- **CPD believes the 25 per cent tax on export that was waived for tobacco companies operating in export processing zones (EPZs) must be reinstated in FY24**

A hard tax on soft drinks and energy drinks

- Carbonated soft drink and energy drinks contain a substantial amount of sugar which is a major cause for obesity, diabetes, and tooth decay
- Typically, **a single can of a soft drink** which is around 355 millilitres, contains **39 grams of sugar** is equivalent to roughly about **10 teaspoons of sugar**, while the World Health Organisation (WHO) recommends that adults **should not consume more than 6 teaspoons of sugar daily to lead a healthy lifestyle**
    - Currently, the beverage and carbonated industry is subjected to a 25% SD for carbonated soft drinks, 35% SD for energy drinks, and 15% VAT applicable for both

A hard tax on soft drinks and energy drinks

- For soft drinks and energy drinks, **CPD recommends that the government should put a specific excise duty of BDT 0.10 per ml or BDT 100 per litre**
- Placing a specific excise duty on soft drinks and energy drinks **will provide the government with substantial revenue** and also minimise the risks of related diseases and health expenditures of the general people
- This will also allow the economy to achieve SDG target 3.4 which aims to **reduce non-communicable diseases** by one-third by 2030

Proposed Tax Structure for Soft Drinks and Energy Drinks

Current Tax Structure for FY 2022-2023			Proposed Tax Structure for FY 2023-2024			
Beverage	**SD (%)**	**VAT (%)**	**Beverage**	**Specific excise duty (BDT per ml)**	**Specific excise duty (BDT per litre)**	**VAT (%)**
Soft drinks	25	15	Soft drinks	0.10	100	20
Energy drinks	35	15	Energy drinks	0.10	100	20

Tax on sanitary napkins: a gender tax harming women and girls

- **Menstrual hygiene is a fundamental right for women and girls which is violated when menstrual hygiene products are subjected to all kinds of tax**
- Locally produced **sanitary napkins and similar sanitary products** are subjected to **high prices** because of **high total tax incidence (TTI) on imports of raw materials** required for their manufacture
- According to Bangladesh Customs, SD on imported raw materials required for manufacturing sanitary napkins, such as air laid paper was 20%, VAT and advance income tax (AIT) on other necessary raw materials were 15% and 5%, respectively in FY22

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Tax on sanitary napkins: a gender tax harming women and girls

❑CPD proposes that:

- **TTI on imported raw materials required to produce sanitary napkins should be zero by exempting all form of VAT, CD, SD AIT, RD, AT and AIT**
- Raw materials used to produce sanitary napkins fall under 12 HS codes, including 48239094, 35052000, 35069110, 39069000, 39199020, 39201020 and 40021100
- TTI of all these raw materials **should be made zero** to ensure affordable sanitary napkins for women and girls from all levels of income
- The **TTI on imported sanitary napkins** in FY22 was **127.72%**, which is recommended to **be reduced to 31.93% in FY24** so that the product remains low-priced, but at the same time the domestic manufacturers of sanitary napkins receive some level of tariff protection

Tax on medicines in view of LDC graduation

- Under the VAT and Supplementary Duty Act 2012, the government imposed 2.4% VAT on pharmaceuticals including medicines at local trading stage and 15% VAT on import of pharmaceutical ingredients and raw materials for production
- As an LDC, Bangladesh's pharmaceutical industry is currently enjoying facilities under WTO's Trade Related Property Rights (TRIPS) pharmaceutical waiver
- The TRIPS pharmaceuticals waiver will be withdrawn starting from 2026, so Bangladesh will lose the LDC-specific support measures under this agreement.
- CPD recommends that the **VAT on medicines should be exempted starting from FY26** to ensure that medicines continue to be affordable to all even after the loss of TRIPS waiver in 2026

Budget allocation in the education sector

- Education budget as a *share of total budget* **decreased from 14% in FY10 to 11.7% in FY22**
- The revised education budget as a *share of GDP* **decreased to 1.9% in FY22 to 1.8% in the revised budget for FY21**
  - Education budget utilisation has been decreasing over the years, in particular for development expenditure
  - Therefore, it is necessary to not only **increase the budget allocation and budget utilisation of the education sector**, but also to undertake a variety of fiscal policies to encourage better education and, as a result, maximise social welfare

Removal of existing taxes on education

- While the government has exempted Bengali medium schools, and later private universities from paying VAT on tuition fees, the **VAT on English medium schools continues to be at 5%**
  - The existing VAT puts an additional burden on the parents of middle-income households
  - **Therefore, the VAT on tuition fees for English medium schools should be exempted in FY24**
- English medium schools follow international curriculum and their students are assigned to read imported foreign books. At present the **total tax incidence on imported books is 73.96%**
  - This puts further strain on families from middle-income households and impedes the efforts made in order to achieve SDG 4, which aims for inclusive and quality education for all
  - **Therefore, all taxes on imported foreign books should also be exempted in FY24**

Proposal for increased budget allocation for all education stipends

➢ **CPD proposes an increase in the allocation for all education stipends to be implemented in the budget for FY24**

	Current stipend structure in FY23			**Proposed stipend structure in FY24**	
Name of stipend	**Number of beneficiaries (in crore)**	**Total budget allocation (in crore BDT)**	**Allocation per beneficiary per year (in BDT)**	**Total budget allocation (in crore BDT)**	**Allocation per beneficiary per year (in BDT)**
Student stipend for primary education level	1.400	1,900	1,357	8,400	6,000
Stipends for secondary, higher secondary and madrasah education level students	0.529	1,980	3,524	5,225	10,000
Stipends for undergraduate and postgraduate level students	0.0136	72	6,142	195	15,000
Stipends for students of technical education institutions	0.0612	343	5,935	834	15,000
Stipends for physically challenged students	0.010	96	9,564	200	20,000
Stipend for improving the livelihood of transgender, Bede and disadvantaged community	0.003	26	9,759	54	20,000
Total for stipend programmes	2.017	4,417		14,908	

CPD (2023): CPD's Recommendations for the National Budget FY2023-24: Weathering the Storm, Containing the Risks

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Section 7: Fiscal measures to support green transition

Budget for a breath of fresh air

- The PM 2.5 concentration in Bangladesh's air was **13.2 times higher than the World Health Organization's (WHO) safe air quality guideline** as of 26 March 2023 (IQAir, 2022).
- Bangladesh is committed to reduce greenhouse gas (GHG) emissions by 6.73% in five sectors namely, power, transport, industry, waste and land use by 2030 as per its Nationally Determined Contribution (NDC) document
- According to the updated NDC of Bangladesh, USD 14.9 billion and USD 21.6 billion are required to deliver unconditional and conditional commitment respectively
- **To achieve these GHG emission reduction targets, Bangladesh needs to implement a variety of tax and regulatory measures**

Fiscal measures to reduce air pollution

- An extensive policy that considers **VAT exemption on all types of equipment in a renewable power plant**, especially solar power plants, should be considered from FY24
- An **incentive tariff can be considered for electricity generated from renewables** according to the Renewable Energy Policy 2008, which allows *electricity generated from renewable sources to be priced 10% higher than the highest purchase price of electricity generated from fossil fuel sources*
- A **1% surcharge on the goods produced by industries polluting the environment** should be implemented completely in FY24
- Bangladesh can **implement a carbon tax equivalent to 3% of the price of fossil fuels starting from FY24**, in order to gradually meet the government's target set out in the Eighth Five Year Plan (8FYP) which aims to implement a 5% carbon tax on the price of fossil fuels by 2025 and 15% carbon tax on the price of fossil fuels by 2041

Fiscal measures to reduce air pollution

- The government should **phase out fossil fuel subsidies starting from FY24;** all fossil fuels may be sold at the international market price and this price may be updated each month
- A **formal feed-in tariff policy exclusively for renewable energy needs to be implemented in FY24** so a clear incentive package reaches all types of potential renewable energy producers, regardless of their generation capacity
- In order to reduce air polluting originating from the transport sector, the government should reform the advance income tax (AIT) structure on private motor vehicles so that the **AIT on fossil fuel driven motor vehicles** is **5% to 50% higher than the AIT on hybrid and fully electric vehicles**, depending on the size the vehicle's engine and electric motor
- The government should also **consider imposing an AIT on motorcycles from FY24**, depending on the size of the motorcycle's engine

Plastic pollution getting out of hand

- There are 1,212 dump sites in Bangladesh that contribute between 24,032 and 36,047 tonnes of plastic waste annually to the country's rivers
- Alarmingly, **87% of the plastic waste generated in Bangladesh was inadequately managed**, which led to the country becoming the tenth largest contributor of mismanaged plastic waste in the world in 2010
- *Between 26 March 2020 and 25 April 2020, around 14,165 tonnes of single use plastic waste was generated in Bangladesh*, which included 455 million surgical masks, 1,216 million polyethene hand gloves, 189 million surgical hand gloves and 49 million bottles of hand sanitizer
- The **Ganges River**, which runs through Bangladesh and into the Bay of Bengal, was estimated to be the **second largest river source of plastic inputs into the ocean worldwide** in 2015

Fiscal measures to reduce plastic pollution

- With the goal of reducing plastic pollution, the government should **consider bringing single-use plastic products under taxation in FY24**
  - Such single-use plastic products may include: cutlery such as forks, knives, spoons, and chopsticks; plates; straws; beverage stirrers; sticks to be attached to and to support balloons; food containers made of expanded polystyrene; beverage containers made of expanded polystyrene; and cups for beverages made of expanded polystyrene
- The budget for FY24 should **allocate additional funding for the Joint Rivers Commission to establish a bilateral plastic waste reduction initiative with India**
  - The Government of India should also contribute to this initiative with funding, as well as technical and logistical support, in order to ensure the reduction of plastic waste in the 54 transboundary rivers shared between Bangladesh and India

Section 8: Conclusion

Conclusion

- The national budget for FY24 will be placed at a time when the country is facing formidable challenges in a number of areas
  - The adverse impacts of the rise in global commodity prices following the conflict in Ukraine started to be felt on many socio-economic correlates of Bangladesh just at a time when the economy was recuperating from the harshest effects of COVID-19
- While these factors have certainly accentuated the macroeconomic situation of the country, they should not draw the attention away from the accumulated and embedded weaknesses within the Bangladesh economy
- As far as the trends during FY23 are concerned, the major correlates exhibit signs of serious stress within the Bangladesh economy
  - This has been manifested in, inter alia, negative growth in revenue mobilisation, slow implementation of ADP, increased reliance on bank borrowing for deficit financing – particularly from the central bank, skyrocketing prices of essentials, declining liquidity situation of banks, deteriorating external sector balance and foreign exchange reserve
- Amid these disquieting developments, perhaps the silver lining is that the global economic situation is slowly improving, and global commodity prices are on a downward trajectory

Conclusion

- In the current context, policymakers' scope of manoeuvring policy measures has become rather limited given the declining fiscal space
- Given the current macroeconomic situation, pressure on policymakers to provide various tax reliefs and other incentives will be intensified. At the same time, demand for budgetary allocations towards various sectors will be increased
- In this scenario, targeted fiscal measures geared towards catering the needs of the fixed-income earning and low-income population should take the centre stage. Such measures should be accompanied by monetary measures focusing on stability (e.g., market-based interest rates and exchange rates)
- Good governance and discipline are of paramount importance for these polices to bring forth their intended results
  - The reform measures proposed by the IMF might prove to be beneficial in this regard

Conclusion

- Proper acknowledgement of the current scenario should be at the forefront while formulating the budget for the next fiscal year
- While it might be disincentivising for a political government to do so in an election year, as recent experience shows, failure in this regard will result in a macro-fiscal policy stance that does not meet the needs of the time
- The budget for FY24 should take cognisance of the emerging realities adequately, assess the available policy options diligently and formulate the measures accordingly
- Further instability originating on account of policy missteps may be unwarranted in an election year

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