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Centre for Policy Dialogue (CPD)

Independent Review of Bangladesh's Development

Promoting informed policy choices

THE PROGRAMME

The Independent Review of Bangladesh's Development (IRBD), Centre for Policy Dialogue's flagship programme, is a comprehensive assessment of the country's economic development agenda prepared by a group of Bangladeshi experts. Launched in 1995, it is Bangladesh's first civil society initiative to analyse the trends in the economy linking economic policies to development efforts. IRBD attempts to provide voice to marginalised stakeholders.

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State of the Bangladesh Economy in FY2023-24

First Reading

Key findings

1. In fiscal year (FY) 2024, revenue collection is unlikely to meet the target, Annual Development Programme (ADP) implementation is at a five-year low, and budget financing relies heavily on non-bank borrowing.
2. Inflation is primarily a domestic problem with relentlessly rising prices caused by market distortion by cartels and collusion, hidden behind deceptively low official inflation rates.
3. The cost of 24 major irregularities in the banking sector from 2008 to 2023 was equal to 2 per cent of the gross domestic product (GDP) of FY2023 or 12 per cent of the national budget of FY2024.
4. Imports, foreign direct investment, and remittance have decreased, while discrepancies in export earnings data have been uncovered.
5. Labour rights-related issues, such as violence against workers, arrests and detentions, dismissals, anti-union discrimination, threats, and prosecutions, remain unresolved.

Key Recommendations

1. Digitalise tax collection, limit public spending, and improve the fiscal data ecosystem.
2. Strengthen the Competition Commission, increase minimum wages in all sectors and industries, and enhance social protection.
3. Reform the central and commercial banks, create a conducive legal environment, release disaggregated banking data, and establish a Citizen's Commission on Banking.
4. Diversify export products and markets, allow the exchange rate to be market-determined, and maintain strong partnerships with global brands.
5. Penalise workplace discrimination and barriers to forming trade unions and undertake more projects that employ minorities.

Introduction

The economy of Bangladesh faces both domestic and international challenges. The Russia-Ukraine war slowed COVID-19 recovery. The economy faces severe external pressures High commodity prices, supply chain disruptions, and tightening of monetary policy around the world affect the economy. Exogenous factors, structural problems, weak policies, slack policy implementation, and inability to undertake reforms are straining Bangladesh's economy. The slow revenue mobilisation, high commodity prices, scheduled banks' tightened liquidity, large volume of non-performing loans (NPL), deteriorating external sector balance, and the rapidly running out of foreign exchange reserves highlighted the pressure points. Global partners have also focused on ready-made garment workers' (RMG) minimum wage strikes. Even if solutions have been identified, implementing them is complex, and many reforms have been postponed owing to elections. This policy brief highlights five major areas of emphasis: public finance, inflation, the external sector, banking, and labour rights. It emphasises the principal risks and obstacles in the aforementioned areas and offers policy recommendations.

Public Finance

The lack of timely data from the Ministry of Finance (MoF) has hindered the assessment of Bangladesh's public finance situation in FY2024. While alternative data sources, such as the National Board of Revenue (NBR), Implementation Monitoring and Evaluation Division (IMED), and Bangladesh Bank, are prompt, they often lack accuracy and congruency (Bhattacharya, Khan, Kamal, & Khan, 2022). The NBR reported a 14.4 per cent increase in their tax collection during the July–October period of FY2024. The collection of indirect taxes increased slightly at the local level. However, the collection of indirect taxes at the import level was underwhelming owing to regulation-induced import compression, even when the Bangladeshi Taka (BDT) depreciated considerably. The implementation rate of ADP during July-November FY2024 was 17.2 per cent, the lowest it had been in the last five years. The crucial question remains whether this resulted from the government's cost-cutting efforts or the inability to carry out projects due to the foreign exchange crisis. Additionally, the budget deficit financing relied heavily on non-bank borrowing in July–October FY2024, even though the net sale of national savings certificates (NCS) remained negative.

Given the ongoing dynamics, the revenue collection target for FY2024 is unlikely to be met. Moreover, restraining public expenditure to control the budget deficit will be imperative. The net NSC sales are expected to remain negative, so non-bank borrowing will be well below the target. This would result in banks being under pressure to service the budget deficit. Ultimately, the fiscal space for the government will be limited considering the liquidity pressure on the commercial banks and the government's commitment not to borrow from the central bank.

On a positive note, Bangladesh met several of the performance targets the International Monetary Fund (IMF) set at the end of FY2023. A large part of IMF's conditionalities on public finance focus on strategy or plan documents and policy notes but lack specific quality assurance criteria that Bangladesh must meet in forming those policy notes. Some conditionalities will require further detailing regarding their methodology (for example, price adjustment mechanism for petroleum products) and stakeholder engagement plan in the coming days. Regrettably, the IMF conditionalities do not mention anything regarding ensuring value for money for public investment as part of the programme.

A medium- and long-term revenue strategy (MLTRS) is being developed to enhance revenue collection over the next five years. The strategy should prioritise incomplete projects and reforms and analyse prevailing tax exemptions to ensure policy predictability. Moreover, it should focus on improving the data ecosystem. The strategy should also revisit agendas regarding illicit financial flows (IFF). Digitalising the entire revenue system is a high priority in the current situation (Rahman, 2023). It is essential to properly define the range of impact of MLTRS and carry out the strategy transparently. Lastly, it is important to review the public expenditure situation and formulate a strategy to safeguard the value of public money.

High Prices: The Cause Of Sorrow And Suffering

The continued increase in prices of essential goods is a notable concern for Bangladesh. The recent inflationary pressures have made it hard for low-income people to afford a living. The high inflation has reached the 10 per cent mark. The base of the consumer price index (CPI) was changed in 2021–2022, and the point-to-point inflation rates show fluctuations, with notable increases in general and food inflation (Bangladesh Bank, 2022). However, analysis shows that the new CPI may not provide the complete picture of the economy. Another grave problem is the lack of competition in the essential consumer goods market. This enables the practice of collusion and other anti-competitive behaviour, such as price manipulation, market supply dominance, or artificial scarcity creation, all for financial gain. In the last five years (1 January 2019 to 20 December 2023), the price of rice of Bangladeshi varieties has increased by as much as 23 per cent (TCB, 2023) . Moreover, prices of items such as processed flour (maida), unprocessed flour (aata), and edible oil rose before the Ukraine conflict, indicating domestic forces at work. Even common types of fish, such as Rui and Ilish (Hilsha), have experienced high prices. Prices of beef and sugar were also increasing, even though their prices were relatively stable in the world market (World Bank, 2022). The average price of sugar increased by 177 per cent between 1 January 2019 to 20 December 2023 (TCB, 2023) . Even the price of powdered milk, common condiments, and spices has risen in recent years. This persistently high inflation reflects Bangladesh's inability to utilise monetary policy effectively. In April 2020, Bangladesh Bank imposed a cap on lending and deposit rates (Bangladesh Bank, 2021). Influential businesses disapproved of the decision because of the high lending rates. However, there were no noticeable surges in private investment. Additionally, the government's borrowing from the banking system expanded the money supply in the economy (Bangladesh Bank, 2021). This fuelled inflationary pressures and reduced excess liquidity in banks. Money circulating in the underground economy through illicit methods is also responsible for aggravating the inflationary force. To tackle the grappling effects of collusion and corruption on prices and citizens, the Bangladesh Competition Commission must be strengthened. The commission should act against anti-competitive behaviour and revise its acts and clauses to be more comprehensive and robust in dealing with monopolies and oligopolies. Moreover, the minimum wage should be raised to keep up with the cost of living, and essential commodities should be made affordable. Lastly, the government should consider providing direct cash support to impoverished individuals and extending support to small businesses for survival during challenging times.

Hope For A Sound Banking Sector Fading Away Fast

Bangladesh's banking sector has consistently demonstrated vulnerability, primarily because of a lack of good governance and a dearth of reforms. Non-performing loans (NPLs) remain unchecked, threatening the health of the country's financial system. Crony capitalists have used banks as vehicles to reach their goal of financial oligarchy. Published news reports of 24 major irregularities in the banking sector from 2008 to 2023 add up to an astronomically large amount of more than BDT 922.61 billion or more than BDT 92,261 crore , which is equivalent to 2 per cent of GDP FY2023 (BBS, 2023) and 12 per cent of the national budget FY2024 (MoF, 2023). The current state of the banking industry is precarious as fraudulent activities and irregularities plague it. The incidents indicate a notable lack of proactive measures by the authorities to address the issue and establish a sense of order within the sector. The observed escalation in defaulted loans and ongoing instances of embezzlement within the banking sector failed to demonstrate any urgency on the government's part in addressing this issue. Bangladesh Bank's sovereignty has been disrupted by the Financial Institutions Division (FID) of the MoF. State-owned commercial banks (SCBs) have failed to maintain minimum capital adequacy requirements for the past 10 years. On the other hand, the specialised banks (SBs) have remained critically under-capitalised. The total volume of NPL has increased by more than three times in the last 10 years, from BDT 427.25 billion in the fourth quarter (Q4) of FY2012 to BDT 1560.4 billion in Q4 of FY2023 (Bangladesh Bank, 2023). However, actual NPL will be much higher if distressed assets, loans in special mention accounts, loans with court injunctions, and rescheduled loans are included. The factors influencing NPLs were classified under four categories: i) institutional, ii) regulatory, iii) legal, and iv) data and informational. The rise in the required loan loss provisioning and the gap between the required loan loss provisioning and the actual provisioning are equally worrying. The recent surge in the shortfall in the loan loss provisioning in the banking sector has been driven by the loan loss provisioning shortfall in the PCBs. This fall in excess liquidity has been mainly driven by the liquidity crisis in five of 10 Islamic Shariah-based PCBs, plagued by poor governance since the ownership change of the banks. To restore good governance in the banking sector of Bangladesh, commercial banks need to be strengthened, the central bank should be empowered to act in the best interest of the depositors, a conducive legal and judicial environment should be created, and availability, access, and integrity of timely data should be ensured. A goal-specific, time-bound, inclusive, transparent, unbiased and independent Citizen's Commission on Banking should be set up to bring transparency to the prevailing situation, identify the root causes of the manifest problems, and suggest credible measures for improving the situation sustainably.

External Sector Performance: Continuing Vulnerabilities Amid Growing Uncertainty

Bangladesh's current economic vulnerabilities lie in its uncertain performance in the external sector. Indications of capital flight and a rising informal transnational fund transfer network are all important causes of concern. While the current account improved due to a decline in imports by 20.5 per cent (Bangladesh Bank, 2024) (when comparing July-October of FY2024 with July-October FY2023), this decline may negatively impact the critical macroeconomic performance indicators and GDP growth. The most concerning indication is the low Foreign Direct Investment (FDI), which declined by USD 5.2 billion in just one year. As a result, the forex reserve also decreased by USD 7.4 billion in October 2023. Moreover, Bangladesh's significant export earnings rely heavily on the RMG sector. So, the decline in RMG export growth in FY2024 caused slow growth in overall export earnings. Another factor affecting the volume of export earnings is the difference in numbers caused by free on board (FoB) and cost, insurance, and freight (CIF) values. However, the anomalies in export earnings seem to be too significant. So, there may be errors in reporting export earnings data. Additionally, since Bangladesh graduated to lower middle-income status, foreign borrowing interest rates and terms have increased. Remittance inflow to the country does not amount to what it should be. About 3.9 million people have left the country since 2019, but the remittance growth does not reflect this huge number (BMET, 2023; Bangladesh Bank, 2024). Steps have been taken to mitigate this. For example, in October 2023, an additional incentive of 2.5 per cent was given for remittance received through formal channels, and this increased the remittance flow in the formal economy for two months (Bangladesh Bank, 2024; BMET, 2023). However, unless the underground networks are dismantled and disrupted, the policies will not be sustainable. The exchange rate should be left to market forces. Even though Bangladesh Bank wants to pursue a cautious policy to control imported inflation, depreciation will incentivise remitters and make exports more competitive. The Bangladesh Bank should only intervene to a certain level and leave the currency depreciation to market forces. The plight of Bangladesh's external sector and forex reserves is a priority. The authorities should be careful with data reports and investigate sudden changes in numbers, providing a logical explanation for any significant fluctuations. Remittance flows are being encouraged through incentives, putting more financial strain on the government and raising bank expenses. The need for a market-aligned exchange rate is evident. Moreover, the RMG sector must focus on diversification in all aspects. RMG's target is to increase the quantity of exported products rather than improve the quality, so this reliance on volume for export earnings may negatively impact the industry in the long run. Bangladesh should also follow the regulations set by the import countries regarding minimum wages, the environment, and carbon dioxide (CO_2) emissions. In addition, they should maintain close partnerships with global brands to consolidate their export channels. Building a culture of dialogue among the government, experts, and professionals is necessary to form effective policies to pull the external sector out of its current state.

Labour Rights In Bangladesh: Commitments And Concerns

Bangladesh still lags in the case of maintaining labour rights. The consistent violations in the workplaces of almost all sectors remain a significant concern for the government.

The US and EU, two major trade partners of Bangladesh, raised concerns about labour rights and provided areas and activities to improve the situation (The White House, 2023; European Parliament, 2023). Their concerns revolve around the right to collective bargaining, removing compulsory labour, child labour and minors in dangerous workplaces, fostering respect for workers, improving working conditions and safety, and better minimum wages that reflect the value of work.

In recent years, the government has undertaken various steps to improve the situation of labour rights in Bangladesh. However, reports show that the initiatives have not yet been sufficient. While there are some improvements, such as the reduction of child labour in hazardous places (-16.4 per cent) (ILO, 2023), the overall situation is relatively stagnant. According to the Global Rights Index produced by the International Trade Union Confederation (ITUC), Bangladesh has consistently been among the top 10 worst countries for labour rights (ITUC, 2023). In addition, the index reveals issues related to violence against workers, anti-union discrimination, and unfair detention and dismissals. Recently, new concerns have surfaced regarding government actions such as arrests and detainments against peaceful protests and the introduction of regressive laws.

While Bangladesh is trying to make progress, there are still reports of workers' unrest. Even though there was a drop in workers' unrest from 431 incidents in 2021 to 196 incidents in 2022 (BILS, 2023), it is expected to increase in 2023 due to the protests surrounding the minimum wage in the RMG industry. Workplace accidents are also a common trend in Bangladesh. In 2021 and 2022, respectively, 1,053 and 1,034 workers lost their lives because of workplace accidents, and 191 and 213 workers lost their lives because of ill-treatment (BILS, 2023).

Bangladesh's legal framework is inadequate in dealing with labour rights issues. It also fails to meet international standards. The Ministry of Commerce, Employment, and Foreign Affairs needs to take a coordinated and prompt approach to reduce the likelihood of encountering trade penalties and visa restrictions from trading partners like the US and EU. Workers should be compensated, and the minimum wage for all sectors should be revised. The legal framework for workers must be strengthened, and amendments need to be made to cover more areas and sectors. Workers should be able to voice concerns without fear of retribution. The government must gradually implement all International Labour Organization (ILO) and the United Nations Guiding Principles (UNGP) on Business and Human Rights conventions.

Conclusion

Macroeconomic instability will persist after the national elections. Policymakers must address several economic issues. The government must reduce inflation, increase tax collection, stabilise the exchange rate, and boost foreign exchange reserves. Economic inequality suggests corruption and unequal opportunities. The government predicted 7.5 per cent GDP growth in FY2024 despite significant economic headwinds following FY2023. Numerous organisations predict weaker growth, putting the government's target into doubt. Without realistic projections and solid data, policymakers cannot assess the economy and create appropriate policies. To boost economic performance, the government must address structural issues. Bangladesh's legal system is inadequate for bank defaulters and money launderers. This must be improved to establish good governance. Vested interests make change difficult, so sustainable changes and macroeconomic solutions start with good governance.

Policy Recommendations

Public finance

- The revenue collection system should be further digitalised, making it easy to pay taxes through digital systems.
- The government may need to restrain public expenditure to keep the budget deficit in check.
- The data ecosystem must be improved, and data should be made transparent.

Inflation

- The Bangladesh Competition Commission's role in the essential consumer goods market should be significantly strengthened, and the Competition Act 2012 should be revised to address monopolies.
- Given the high cost of living, the minimum wage board should consider increasing the minimum wage in all industries.
- The government should enhance social protection for low-income families to help them survive high prices.

Banking sector

- The central and commercial banks must be reformed to strengthen their governance, and the central bank should be allowed to operate autonomously.
- A conducive legal and judicial environment should be created, and the reports and data of banks and financial institutions should be published and made available to the public.
- A goal-specific, time-bound, inclusive, transparent, unbiased, and independent Citizen's Commission on Banking should be established.

External sector

- Apparel export has become very volume-driven, so there is a need for product and market diversification.
- The exchange rate should be determined by market forces and not fixed by the government.
- Bangladesh must maintain good partnerships with global brands in the RMG business.

Labour rights

- Revising the minimum wage in all overdue sectors, especially RMG, is necessary.
- The law should penalise workplace discrimination, anti-union discrimination, and barriers to forming trade unions.
- More projects that employ minorities must be undertaken, and insurance schemes, unemployment benefits, and other welfare structures targeted to them should be revisited.

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