Bangladesh Economy in FY2017-18

Interim Review of Macroeconomic Performance

Prepared under CPD's programme on

Independent Review of Bangladesh's Development (IRBD)

CENTRE FOR POLICY DIALOGUE

June 2018

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The views expressed in this volume are those of the CPD IRBD 2018 Team members and do not necessarily reflect the views of the CPD.

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

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Acronyms

7FYP	Seventh Five Year Plan
ADP	Annual Development Programme
ADR	Advance-Deposit Ratio
ADR	Alternative Dispute Resolution
BBS	Bangladesh Bureau of Statistics
BDT	Bangladeshi Taka
BEZA	Bangladesh Economic Zones Authority
BGMEA	Bangladesh Garment Manufacturers and Exporters Association
BKMEA	Bangladesh Knitwear Manufacturers and Exporters Association
BoP	Balance of Payment
BSCIC	Bangladesh Small and Cottage Industries Corporation
BSEC	Bangladesh Securities and Exchange Commission
BSTI	Bangladesh Standards and Testing Institution
BTMA	Bangladesh Textile Mills Association
BTRC	Bangladesh Telecommunication Regulatory Commission
CAMELS	Capital Adequacy; Assets; Management Capability; Earnings; Liquidity; Sensitivity
CBC	Customs Bond Commissionerate
CPD	Centre for Policy Dialogue
CPI	Consumer Price Index
CRAR	Capital to Risk Assets Ratio
CRR	Cash-Reserve Ratio
CSE	Chittagong Stock Exchange
CSO	Civil Society Organisation
CSR	Corporate Social Responsibility
DDM	Department of Disaster management
DFI	Development Finance Institution
DSE	Dhaka Stock Exchange
DSES	Dhaka Stock Exchange Shariah
DSEX	Dhaka Stock Exchange Broad Index
DTA	Domestic Tariff Area
EBA	Everything But Arms
EPB	Export Promotion Bureau
ERD	Economic Relations Division
EU	European Union
FCB	Foreign Commercial Bank
FDI	Foreign Direct Investment
FGD	Focus Group Discussion
G2G	Government-to-Government

GBP	Great Britain Pound
GDP	Gross Domestic Product
GED	General Economics Division
GNI	Gross National Income
GoB	Government of Bangladesh
GPS	Government Primary School
GSP	Generalised System of Preference
GST	Goods and Services Tax
HPNSDP	Health, Population and Nutrition Sector Development Programme
HS	Harmonised System
IFF	Illicit Financial Flow
IMED	Implementation Monitoring and Evaluation Division
IMF	International Monetary Fund
INGO	International Non-Government Organisation
INR	Indian Rupee
IPO	Initial Public Offering
IRBD	Independent Review of Bangladesh's Development
JRP	Joint Response Plan
KII	Key Informant Interview
L/C	Letter of Credit
LDC	Least Developed Country
LFS	Labour Force Survey
LNG	Liquefied Natural Gas
LTU	Large Taxpayers Unit
MDG	Millennium Development Goal
MEIS	Merchandise Exports from India Scheme
MLT	Medium and Long-Term
MoC	Ministry of Commerce
MoF	Ministry of Finance
MoU	Memorandum of Understanding
MPS	Monetary Policy Statement
MRFP	Monthly Report on Fiscal Position
MSME	Micro Small and Medium Enterprise
MT	Metric Ton
MTRS	Medium-Term Revenue Strategy
NBR	National Board of Revenue
NGO	Non-Government Organisation
NNPS	Newly Nationalised Primary School
NPL	Non-performing Loan
NSA	National School Assessment
NSD	National Savings Directorate
NSSS	National Social Security Strategy
ODA	Official Development Assistance
PCB	Private Commercial Bank
PEDP 3	Third Primary Education Development Programme
PPP	Public-Private Partnership
PPPA	PPP Authority
QIIP	Quantum Index of Industrial Production
RADP	Revised Annual Development Programme
REER	Real Effective Exchange Rate
RMG	Readymade Garment
SCB	State-Owned Commercial Bank
SD	Supplementary Duty
SDG	Sustainable Development Goal
SEIS	Services Exports from India Scheme

SEZ	Special Economic Zone
SME	Small and Medium Enterprise
SoE	State-Owned Enterprise
SSPS	Social Security Policy Support
STR	Student-Teacher Ratio
TIB	Transparency International Bangladesh
ToR	Terms of Reference
TVET	Technical and Vocational Education and Training
UD	Utilisation Declaration
UN ECOSOC	United Nations Economic and Social Council
UNDP	United Nations Development Programme
UNESCO	United Nations Educational, Scientific and Cultural Organisation
UNFPA	United Nations Population Fund
UNHCR	United Nations High Commissioner for Human Rights
UNICEF	United Nations Children's Fund
US	United States
USA	Unites States of America
USD	United States Dollar
VAT	Value Added Tax
VNR	Voluntary National Review
WASH	Water, Sanitation and Hygiene
WDI	World Development Indicator
WHO	World Health Organization

Chapter 1

State of the Bangladesh Economy in FY2017-18 *(Third Reading)*

This report was released to the media by the Centre for Policy Dialogue (CPD) on 3 June 2018.

1.1 INTRODUCTION

As part of its regular exercise to review the performance of the economy and analyse the key emerging development trends, CPD closely monitors the economy throughout a fiscal year. The present report is the third instalment of the State of the Bangladesh Economy in FY2017-18 prepared under CPD's flagship programme titled *Independent Review of Bangladesh's Development (IRBD)*. The objective of this report is to track trends in major macroeconomic variables and present an assessment of the performance of key sectors of Bangladesh economy during FY2017-18 in the run-up to the national budget for FY2018-19. The final instalment of this year's IRBD analysis will be released immediately after the presentation of the FY2018-19 budget, with CPD's immediate reactions to the fiscal-budgetary proposals of the national budget.

This report highlights four key areas that informs macro-financial performance of the Bangladesh economy, focusing on vulnerabilities and weaknesses, and, suggests ways to deal with these issues in the short-term through budgetary measures. These broad areas are: fiscal and budgetary framework (section 1.2), monetary and banking sector performance (section 1.3), capital market (section 1.4), and external sector performance (section 1.5).

The report makes use of the most recent data from available official and credible international sources, as well as insights gleaned from key informants to review and analyse the trends of relevant macroeconomic and development correlates. The report concludes with highlighting a number of urgent measures to be pursued by policymakers and depicting the outlook for the economy in the coming days.

1.2 FORMULATING FISCAL AND BUDGETARY MEASURES FOR FY2018-19

1.2.1 Revenue Mobilisation

There were indications at a pre-budget meeting of the Budget Monitoring and Resource Committee (BMRC) that the revenue target for FY2017-18 was to be slashed by about Tk. 28,990 crore [which included Tk. 23,190 crore for National Board of Revenue (NBR)] in the revised budget. Indeed, such a revision became inevitable. Following the marginal improvement in revenue mobilisation in the first six months (with 16.0 per cent growth) compared to the corresponding period of FY2016-17, it is likely that the revenue target for FY2017-18 will not be attained. Indeed, this has been the trend for six consecutive fiscal years. It is to be noted that, both tax revenue (17.6 per cent growth as against the annual target of 44.4 per cent) and non-tax revenue (2.9 per cent growth as against the annual target of 35.8 per cent) collection have missed their respective targets during the first half of FY2017-18 by a significant margin. According to CPD (2018a), revenue shortfall in FY2017-18 is expected to be around Tk. 50,000 crore. Under such a scenario, the revenue mobilisation target for FY2018-19, which is expected to be around 30 per cent higher than the revised target for FY2017-18, would actually require a growth of around 40 per cent (after accounting for the possible shortfall in actual collection over the revised target). Attaining the significantly high target is by any account an uphill task—success of which is highly doubtful.

Revenue mobilisation is not keeping pace with the 7FYP targets

Actual revenue mobilisation has lagged behind the corresponding medium-term targets. Indeed, revenue-GDP ratio was 10.2 per cent in FY2016-17 while the Seventh Five Year Plan (7FYP) target for the same year was 13.5 per cent. This gap is dominated by a shortfall in income tax collection which could only meet two-thirds of its planned target (Table 1.1). A large shortfall was also recorded in case of VAT and Supplementary Duties (SD), while non-tax revenue collection remained well below the potential. Indeed, failure to implement planned regulatory reforms, weak institutional capacities and absence of the needed administrative efforts have resulted in lack of improvement in mobilising additional revenue.

Table 1.1
Discrepancy between Actual and 7FYP Targets of Revenue Components

Component	Actual FY17 (in crore Tk.)	7FYP targets for FY17 (in crore Tk.)	Difference (in crore Tk.)	Gap (Difference as a share of 7FYP target, %)
Customs duty	22,578	23,420	842	3.6
VAT and SD	95,259	111,247	15,988	14.4
Income tax	52,489	80,020	27,531	34.4
Others	1,172	1,952	780	40.0
Non NBR tax	6,298	7,807	1,509	19.3
Non-tax revenue	22,956	39,034	16,078	41.2
Total revenue	**200,752**	**263,480**	**62,728**	**23.8**

Source: Authors' calculations using Ministry of Finance (MoF) and Bangladesh Planning Commission (2015) data.

Analysis of component-wise revenue-GDP ratio in FY2016-17 revealed that, revenue collected from customs duties and non-NBR taxes are close to the targets of 7FYP whereas revenue from income tax, VAT and non-tax sources are off the mark. Regarding the tax-GDP ratio, the scenario is also pessimistic. In FY2016-17 the tax-GDP ratio was 9.0 per cent against the 7FYP target of 11.5 per cent. Indeed, if the 7FYP target of tax-GDP and revenue-GDP ratio could be achieved, an additional amount of Tk. 49,421 crore and Tk. 65,981 crore respectively could be mobilised. Achieving the 7FYP targets in the area of revenue mobilisation for FY2019-20 is highly unlikely. During FY2018-20, total revenue collection needs to grow at an annual rate of 32.1 per cent to meet the target of 7FYP. Similarly, income tax collection needs to grow at an annual rate of 43.5 per cent to meet its target level in FY2019-20 (Table 1.2). In this backdrop, FY2017-18 progress, as was pointed out above, is not encouraging. Meeting the targets of revenue collection in line with the 7FYP will require significant additional efforts on the part of the NBR. Considering the abovementioned scenarios, two actions are called for: it is high time to set more realistic targets; energetic actions must be taken to broaden the tax base and significantly curtail the widespread tax evasion. The key question is, other than setting a set of ambitious targets, whether the government will be willing and able to take any concrete step in the above directions in an election year.

Table 1.2
Components of Revenue Collection

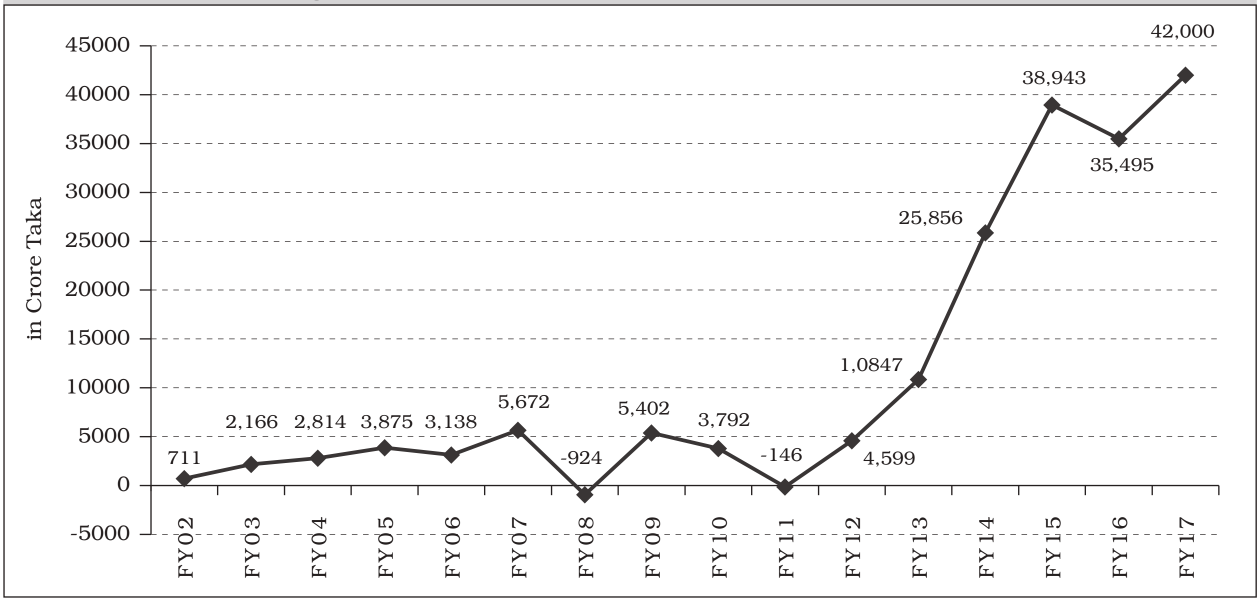
Component	Actual FY17 (% of GDP)	7FYP targets for FY17 (% of GDP)	7FYP targets for FY20 (% of GDP)	Required annual growth during FY18-FY20 (%)
Customs duty	1.1	1.2	1.3	18.3
VAT and SD	4.8	5.7	7.0	28.3
Income tax	2.7	4.1	5.4	43.5
Others	0.1	0.1	0.1	34.8
Non-NBR tax	0.3	0.4	0.4	22.2
Non-tax revenue	1.2	2.0	2.0	35.8
Total revenue	**10.2**	**13.5**	**16.1**	**32.1**

Source: Authors' calculations using Ministry of Finance (MoF) and Bangladesh Planning Commission (2015) data.

Revenue shortfall has skyrocketed in recent years

The mismatch between targeted level of revenue mobilisation and actual attainment has been a recurring phenomenon in the Bangladesh economy. As can be seen, except for two atypical years, the economy

Figure 1.1
Revenue Shortfall in Bangladesh



Source: Authors' calculations from Ministry of Finance (MoF) data.

Note: Negative numbers imply revenue surplus.

has generally suffered regular shortfalls in revenue mobilisation since FY2001-02. Although the shortfalls remained below Tk. 6,000 crore between FY2001-02 and FY2011-12, the deficit started to peak since FY2012-13 to skyrocket to the level of Tk. 42,000 crore in FY2016-17 (Figure 1.1). CPD (2018a) apprehended that revenue shortfall for FY2017-18 is likely to be about Tk. 50,000 crore. CPD had earlier estimated that tax effort in Bangladesh was far below the potential (CPD, 2016). According to UN-ESCAP (2014), actual tax collection level in Bangladesh was far below the potential level—with the gap equivalent to about 7.5 per cent of GDP. The report emphasised the need to enhance tax administration by way of streamlining procedures, widening ICT application, expanding tax base through rationalising prevailing tax exemptions and introducing new taxes. The report also stressed the need to address tax evasion and tax fraud.

Low income tax collection has been the key driver behind revenue shortfall

As can be seen from Table 1.3, the gap between actual income tax collection and the target has generally been the major component of the overall revenue shortfall over the recent years. At the same time, failure to

Table 1.3
Component-wise Share of Revenue Shortfall

(in Per cent)

Source of Revenue	FY12	FY13	FY14	FY15	FY16	FY17
Tax revenue (a+b)	12.0	86.3	95.3	68.2	85.5	77.6
a. NBR tax	5.9	82.2	93.3	66.3	84.9	75.4
Income tax	*-13.0*	*8.3*	*38.4*	*39.5*	*56.0*	*46.3*
VAT	*8.3*	*16.6*	*34.3*	*24.9*	*27.3*	*21.5*
Import duty	*13.4*	*17.9*	*6.0*	*-0.7*	*2.7*	*4.0*
Excise tax	*-4.7*	*2.3*	*1.9*	*0.6*	*-0.9*	*6.4*
Supplementary duty	*-2.6*	*33.8*	*11.3*	*0.7*	*-0.7*	*-3.4*

(Table 1.3 contd.)

(Table 1.3 contd.)

Source of Revenue	FY12	FY13	FY14	FY15	FY16	FY17
Other taxes	*4.5*	*3.4*	*1.4*	*1.3*	*0.5*	*0.6*
b. Non-NBR tax	6.1	4.1	2.0	1.9	0.6	2.3
Narcotics and liquor	*0.1*	*0.0*	*0.0*	*0.0*	*0.1*	*0.2*
Vehicles	*6.5*	*2.6*	*0.7*	*0.5*	*-0.9*	*0.7*
Land	*1.7*	*0.8*	*-0.2*	*0.2*	*0.0*	*-0.3*
Stamp	*-2.1*	*0.6*	*1.5*	*1.3*	*1.5*	*1.7*
c. Non-tax revenue	88.0	13.7	4.7	31.8	14.5	22.4
Dividend and profit	*-14.9*	*-14.9*	*0.8*	*8.7*	*5.7*	*11.2*
Post office and railway	*6.3*	*-0.3*	*0.8*	*1.4*	*0.8*	*2.0*
Interest/fees/tolls and other receipts	*96.5*	*28.8*	*3.1*	*21.7*	*7.9*	*9.2*
Total revenue (a+b+c)	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Authors' calculations from Ministry of Finance (MoF) Data.
Note: Negative numbers correspond to surplus in respective category.

collect VAT at the targeted level also resulted in considerable revenue shortfall. Deficit in non-tax revenue mobilisation, particularly relating to dividend and profit, and interest/fees/tolls and other receipts, has further accentuated the difficulty of mobilising the revenue at the envisioned level.

1.2.2 Fiscal Measures being Discussed for FY2018-19 Budget

Reduction of corporate tax rates ought to consider economy-wide impact

Reduction of corporate tax rates was at the centre of this year's pre-budget discussions on fiscal measures. Existing literature on economic impact of corporate tax rate is rather divided. A number of studies on the nexus between corporate tax and private investment, using both macro and micro-level data, found that the reduction of corporate tax rate, in general, fosters private investment (Federici and Parisi, 2015; Bruhn, 2011; Senzu and Ndebugri, 2018; Babar, Awan and Nadeem, 2017). Higher effective corporate income tax was found to have a more adverse effect on investment in the manufacturing sector than in the services (Djankov *et al.* 2010).

However, reduction in corporate tax rates has its costs. As Clark, Cebreiro, and Böhmer (2007) have found, reduction of corporate tax rate entails negative implications for the economy which include discrimination against other businesses, forgone revenue, reduction of the net present value (NPV) of capital allowances and increase of the after-cost of debt finance. More importantly, reduction of corporate tax is effective in attracting private investment only when the overall investment climate is conducive for business. The report from Committee of Experts on International Cooperation in Tax Matters at the United Nation's survey of the econometric studies suggest that tax incentives that affect investment in general and foreign direct investment (FDI) in particular, do not have nearly as much effect in developing countries as in the developed ones (United Nations, 2010). According to World Economic Forum's successive Global Competitiveness Reports, the most important reasons why companies choose to invest in a country are quality of the country's infrastructure, availability of an educated, healthy workforce, and social stability.

Indeed, corporate tax contributions providing resources for public services are vital to ensuring the revenue needed for these investments. The balance of evidence from literature suggests that, for many developing countries, fiscal incentives often do not effectively counterbalance the unattractive investment climate conditions such as poor infrastructure, macroeconomic instability, and weak governance and markets (United Nations, 2010). Deloitte's survey of corporate tax rates (Deloitte, 2018) confirms that many countries around the world apply multiple corporate tax rates across sectors. Higher tax rates are common for mining sector and for sectors where competition is regulated. India also imposes higher corporate tax rate for foreign companies (40 per cent) compared to domestic companies (30 per cent). In addition, a 7 per cent surcharge applies to domestic companies which is 2 per cent for foreign companies if corporate income exceeds Indian Rupee (INR) 10 million, and 12 percent surcharge applies to domestic companies (5 per cent for foreign companies) if income exceeds INR 100 million. Additionally, a 3 per cent cess is payable in all cases. Thus, the effective tax rate is much higher in India although the country's private investment level (along with FDI) was much higher than that of Bangladesh. Recently, India has taken an initiative to reduce corporate tax rate. 25 per cent corporate tax rate (plus surcharge and cess) is applicable for financial year 2017-18 to domestic companies with total turnover or gross receipts of up to INR 500 million in financial year 2015-16.

Corporate tax rate is an important source of revenue for Bangladesh which contributes about two-thirds of income tax collection. The fiscal measure in the area of corporate tax rate to be proposed in the budget for FY2018-19 should consider the evidence above. It is also to be noted that, in Bangladesh, corporate tax incentives are provided in a number of areas including tax holiday in general, various tax incentives (including reduced or zero tax rate) to the power sector, economic zones and exporters. Indeed, corporate tax rates should not be reduced in a hasty manner and on an ad-hoc basis. This is particularly critical considering that the next budget may not involve many new areas of revenue collection. Any revision of corporate tax rates should be done in a staggered way over the medium-term in order to absorb the adverse revenue impact. This will also provide investors predictability as they make investment decisions. Indeed, a rigorous analysis in the Bangladesh context must be done before taking any medium-term decision in this respect. Conducting such ex-ante impact analysis should be an important part of the Medium-Term Revenue Strategy (MTRS).

Erosion of disposable income justifies raising of tax-free income ceiling

Personal income tax (PIT) exemption threshold, at the general level, was increased to Tk. 2.50 lakhs in the FY2015-16 budget from the previous ceiling of Tk. 2.20 lakhs in FY2014-15—indicating a 13.6 per cent increase. This threshold has been maintained since then. The inflation adjusted value of the PIT exemption threshold becomes Tk. 2.92 lakhs as of April 2018. In fact, general CPI has experienced a 17.0 per cent increase between July 2015 and April 2018. Furthermore, the recent upward trend in inflation was primarily driven by rising food inflation. Also, data from the Labour Force Survey (LFS) 2016-17 points toward decreasing average monthly real wage of employed individuals since 2013. The aforesaid analysis depicts a picture of falling real disposable income of the individuals, particularly those belonging to the lower-middle and middle-income sections of the society. Given this backdrop, CPD reiterates its earlier recommendations (CPD, 2018a) of raising the tax-free income ceiling to Tk. 3 lakhs, and, reducing the first slab of PIT rate to 7.5 per cent from the prevailing rate of 10.0 per cent.

Effective operationalisation of transfer pricing cell is essential to curtail capital flight

Capital flight has a general tendency to increase during the election years. This situation arises as individuals respond to possible decline in political and macroeconomic stability, and the prospect of adverse future fiscal measures (Kwaramba, Mahonye, and Mandishara, 2016). Chang (2010) illustrated instances of soaring capital flight before a number of Latin American elections—mostly as a reaction to possible post-election change in government policies. Similar phenomena were also observed in the case of Ecuador (Campello, 2014) and Argentina (Gaggero, Gaggero, and Rua, 2015). Analysing data for thirty-six African countries, Frantz (2018) revealed that capital flight is relatively high during election years as opposed to other years. The author further asserted that this problem is particularly relevant for developing countries where the baseline rate of capital flight tends to be high already and channels of informal transfer also tend to be widespread. Given this backdrop, earlier apprehension of CPD (2018b) concerning trade misinvoicing and capital flight remains valid in the context of the upcoming national elections. Concerted and coordinated effort from several policy actors including the Bangladesh Bank and NBR is required to limit the scope and extent of the likely illicit financial flows (IFFs). Effective functioning of NBR's Transfer Pricing Cell through greater access to real time data, capacity building in forensic investigation, and logistical and policy support is crucial to this end.

A well thought-out list of SDs needs to be crafted

In the budget proposal for FY2017-18, SD rates at import stage were changed for a total of 1,413 items, with SD rates rising for 1,243 products and declining for 170 products (CPD, 2017a). In deciding on the SDs, this year's budget proposal ought to consider the soaring import payments and deteriorating balance of payment (BoP) situation, along with the need to provide the domestic industry strategic support. At the margin, this may also help the government compensate for the delayed reforms in revenue mobilisation.

Revenue mobilisation from niche areas should be spotlighted

In view of the recurrent shortfall in revenue mobilisation and inadequate resource generation from traditional means, the government should explore the possibilities of raising revenue from niche areas. Recovery of unpaid VAT accrued to the Large Taxpayers Unit (LTU) of the NBR, particularly those from state-owned enterprises (SoEs), should be prioritised. To this end, swift realisation of disputed revenue claims through the Alternative Dispute Resolution (ADR) mechanism must be underscored. The bottlenecks in this connection must be removed.

The next budget should not lose sight of the medium-term reforms

While the next budget may not prioritise implementation of the planned reforms, debate and discussion should continue concerning this area in order to arrive at a consensus. Hopefully this issue will gain attention during the envisaged electoral debates as well. To this end, it is important to have an implementation plan for VAT and SD Act 2012 in an informed way, taking into cognisance the prevailing concerns. Implementation of online VAT registration and filing system, digitisation of VAT process, and bringing in more businesses under the system need to continue and be pursued energetically. Emphasis should be given to finalisation of the draft Direct Tax Act and the Customs Act on an urgent basis. The next budget may consider assessing the feasibility of introducing taxation of agricultural income, a comprehensive property tax and inheritance tax in line with international practices. CPD (2018a) has earlier come up with proposals in this connection. Attention should also be given to raising efficiency through broader deployment of technology including, for example, introduction of electronic tax deduction at source (e-TDS) with issuance of tax certificates by the NBR against e-TINs linked to all TDS collection.

1.2.3 Public Expenditure

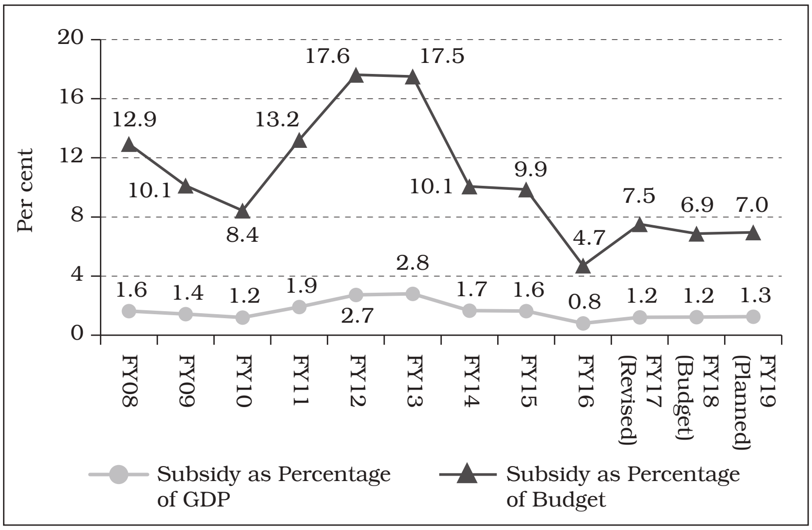
Public expenditure framework needs to be redesigned to make effective use of policy space

It has emerged as an imperative to redesign the public expenditure framework with a view to making effective use of the policy space in FY2018-19. As may be noted, growth of public expenditure in the first six months of FY2017-18 was well below the target. Expenditure on two major sources of non-development spending, i.e. 'Subsidies and Current Transfers' [with (-) 34.5 per cent growth] and 'Interest Payments' [with (-) 0.1 per cent growth] was well within the limit during July-December of FY2017-18. Overall, the non-development expenditure registered no growth against the target growth rate of 34 per cent during July-December of FY2017-18. Expenditure for Annual Development Programme (ADP) was also lower even when compared to the past trends of low rate of implementation.

Rejuvenated subsidy demand is likely to tighten fiscal space

Subsidies may need to be increased in the budget for FY2018-19 in the context of the higher demand for power and gas leading to rise in power production and import of liquefied natural gas (LNG). Subsidy allocation began to fall since FY2013-14, both as a percentage of the GDP and that of the budget, and, reached the lowest levels in FY2015-16 over the last nine years before beginning to rise again from FY2016-17. Bangladesh Petroleum Corporation (BPC) had moved on to the profit terrain in FY2014-15 and continued to earn profit till FY2016-17. It is highly likely that there will again be no allocation for BPC in the next budget. However, the government may need to keep a close watch over the movement of international petroleum prices. The allocation for subsidy in the planned budget for FY2018-19 may be increased to Tk. 32,000 crore, which is 1.3 per cent of GDP (1.2 per cent of GDP in the budget for FY2017-18) and 7.0 per cent of planned budget for FY2018-19 (6.9 per cent of budget for FY2017-18) (Figure 1.2). The first consignment of imported LNG has reached Bangladesh on April 2018 and in view of this a separate Tk. 2,500-3,000 crore may be allocated to LNG alone in FY2018-19 budget. Overall, the subsidy for power Bangladesh Power Development Board and gas (Pertobangla) is set to increase by around 22 per cent to Tk. 9,000-9,500 crore in FY2018-19. Meanwhile, due to upward trend in international energy and fertiliser prices, agriculture subsidy is likely to increase by 5.6 per cent to Tk. 9,500 crore while subsidy for export sector may register 12.5 per cent increase to Tk. 4,500 crore in FY2018-19 budget.

Figure 1.2
Subsidy as Percentage of GDP and Budget



Source: Authors' compilations from Ministry of Finance (MoF) and various newspapers.

Any adjustment as regards energy and electricity prices should be calibrated by taking into cognisance prices of all the three related items (fuel, gas and electricity), overall impact of the price-change mix for major stakeholder groups and the burden of the government's subsidy related expenditure. The government has hinted on withdrawing the 15 per cent VAT at import level to keep the LNG prices stable. Currently, there is a gap of about 1,000 million cubic feet (MMCF) of natural gas per day between domestic demand (3,781 MMCFD) and domestic supply (2,746 MMCFDS). According to the Petrobangla estimate, it will cost the government about Tk. 6,922 crore (USD 844.2 million) in a year to import 1000 mmcfd equivalent of LNG and its re-gasification. In the backdrop of the anticipated higher cost of importing LNG, the Finance Minister has hinted about increasing the prices of gas and electricity in the upcoming fiscal year. Gas suppliers are seeking a 75 per cent increase in the price of gases used for commercial purposes, from Tk. 7.39 to Tk. 12.95 per cubic metre. It should be noted that Bangladesh Energy Regulatory Commission (BERC) had last raised gas prices by a weighted average of 22.7 per cent in 2017. If the subsidy and prices of energy both increase simultaneously, it will put pressure both on the expenditure side and at the consumer level.

ADP expenditure against allocation in FY2017-18 is the lowest in recent years

Expenditure on account of the ADP is yet to mark a significant breakthrough in FY2017-18. According to the first ten months (July–April) data for the current fiscal year, actual spending under the ADP was 50.2 per cent of the originally planned allocation of Tk. 1,55,931 crore. This was lower compared to the spending (54.7 per cent) of previous fiscal year for the corresponding period. Particularly, Taka component (48.7 per cent) of the expenditure was the lowest in recent past (since FY2007-08). Among the top ten ministries and divisions that accounted for 73.3 per cent of the total ADP allocation, only three divisions and one ministry, viz. Power Division (90.5 per cent), Local Government Division (66.4 per cent), (55.4 per cent) Ministry of Science and Technology Road Transport and Highways Division (52.1 per cent), could utilise more than the overall average allocation during July–April of FY2017-18.

Due to the slow pace of implementation, when ADP was subsequently revised in March 2018, a number of major government agencies (e.g. Transport; Education and Religious Affairs; Science, Information and Communication Technology; and Oil, Gas and Natural Resources) were subjected to significant cuts in the revised ADP (RADP) for FY2017-18. ADP for FY2017-18 was slashed by Tk. 7,550 crore (or 4.8 per cent) to bring its size down to Tk. 1,48,381 crore.

Pervasive practice of including a large number of new projects and time extension in RADP

The number of unapproved ADP projects that get allocation in the RADP has been on the rise in successive fiscal years. In contrast, the reduction in total allocation has also been increasing in the RADP as compared to the ADP. This is contradictory.

- A total of 311 fresh projects were included in RADP of FY2017-18 which was the highest in the last 10 fiscal years (see Annex Table 1.1). At the same time, RADP of FY2017-18 was downsized by Tk. 7,550 crore which was also the highest since FY2008-09.
- The total allocation for these projects was Tk. 9,678 crore, of which the project aid component was only Tk. 394 crore (4.1 per cent). A few mega projects with high project cost such as Mirsarai 150 MW Duel Fuel Power Plant, Dhaka-Ashulia Elevated Expressway, Extension of Hazrat Shahjalal International Airport etc. were included in the RADP.
- Sectoral breakdown suggests that apart from Oil, Gas and Natural Resources, all 16 out of 17 ADP sectors had experienced inclusion of new projects. Highest number of new projects was included in the Transport sector (67), followed by Physical Planning, Water Supply and Housing (47) and Agriculture (30).
- 26 out of these 311 projects (8.4 per cent) are local government projects with a total allocation of Tk. 443 crore.
- In addition, 65 out of these 311 projects (20.9 per cent) received a symbolic allocation of Tk. 1 crore or less while 15 projects received allocation of only 10 lakhs or less. Majority of these symbolic projects are from Physical Planning, Water Supply and Housing (13) and Transport (11) sectors. These symbolic projects are perhaps included in the RADP due to political considerations; however, they remain unimplemented because of inadequate resource allocation. No doubt, this undermines the overall quality of ADP planning. For example, CPD conducted an exercise and found that five projects under Industry, Power, Transportation, Education and Religious Affairs and Social Welfare, Women Affairs and Youth Development sectors that received less than Tk. 1 crore in the ADP for FY2016-17 continue to receive allocation less than Tk. 1 crore in the RADP for FY2017-18.[1] All of these five projects were scheduled to be completed within or before FY2016-17, but had been carried forward more than once with only symbolic allocation due to insignificant or no cumulative progress.

[1]These projects include BSCIC Industrial Estate Kumarkhali, Kushtia (1st Revised), Establishment of E-Payment Meter at Dhaka for Electricity under the Rural Electrification Programme (Phase-1), Establishment of Ashuganj Internal Sea Port, Pagoda Based Pre-Primary Education, and Construction of 5-Storied Tribal Welfare Association (Central office and community hall) at Balashpur in Mymensingh.

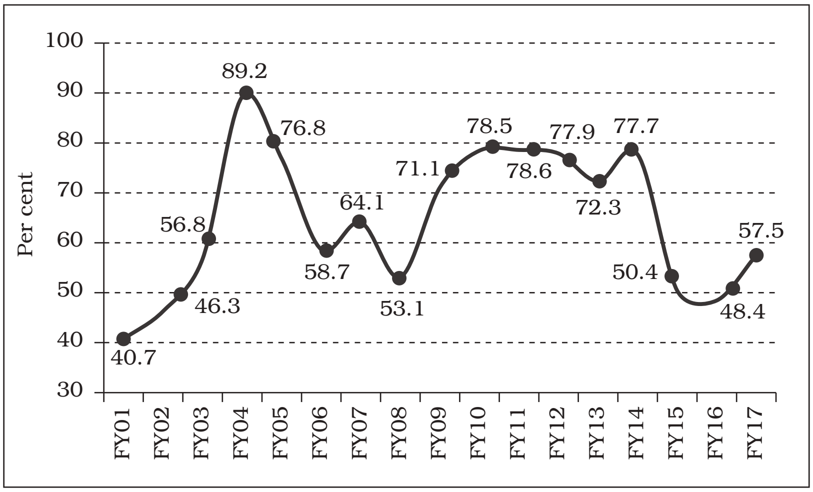
Meanwhile, a good number of projects in the top five sectors of the ADP in terms of their share in total allocation (65 per cent in FY2017-18), have seen time extension in RADP for FY2017-18. These include: Rural Development and Institutions; Power; Transport; Education and Religious Affairs; and Health, Nutrition, Population and Family Welfare. The health sector encountered the highest proportion (34.5 per cent) of extension of their projects followed by Education (31.3 per cent), Power (23.2 per cent), Rural Development (19.2 per cent), and Transport (17 per cent) (see Annex Table 1.2). In addition, five out of the top nine power sector projects, which have the potential to add about 4,000 MW to the national grid, have seen their respective project completion timelines delayed due to the slow pace of implementation.

Low physical progress has undermined quality of overall ADP implementation

It is observed that a major share of completed projects is declared as completed without those being 100 per cent completed physically. Data from Implementation Monitoring and Evaluation Division (IMED) during FY2001-FY2017 period suggests that about 65 per cent (on an average) of completed projects were stated as complete while their physical progress was not actually to the extent of 100 per cent. Indeed, completion rate here stood at only 57.5 per cent in FY2016-17 (Figure 1.3). This raises questions about the quality of project implementation in Bangladesh. Inadequate monitoring of physical progress by implementing agencies and their line ministries, negligence in submitting project completion reports and lack of initiative to respond to the identified problems by the IMED are some of the factors behind such discrepancies.

Figure 1.3

Percentage of Completed Projects that are Declared as Complete without 100 per cent Physical Progress



Source: Authors' calculations from the Implementation Monitoring and Evaluation Division (IMED) data.

The 'fast track' projects are not fast enough

The government has prioritised eight mega projects under the 'fast track' initiative. These projects include: Padma Multipurpose Bridge (PMB), Dhaka Mass Rapid Transit Development Project (DMRTDP) known as Metro Rail project, 2x1200 MW Rooppur Nuclear Power Plant (RNPP), Matarbari 2x600 MW Ultra-Super Critical Coal-Fired Power Project (MUSCCFPP), 2x660 MW Moitri Super Thermal Power Project (MSTPP), LNG terminal for importing liquid gas project, deep sea port at Sonadia in Cox's Bazar and deep sea port at Payra, Patuakhali, Padma Bridge Rail Link (PBRL) project and Construction of Single Line Dual Gauge Track from Dohazari-Ramu-Cox's Bazar and Ramu to Ghundum near Myanmar Border. Among these, the Sonadia deep sea port project has been shelved for now.

The present analysis seeks to explore the current situation as regards these priority projects based on available data as a follow up of the previous analysis. Eight out of these ten projects had initially received an allocation of Tk. 30,929 crore which is 19.8 per cent of total ADP allocation for FY2017-18. The majority of these projects are scheduled to be completed after 2019-20. The present status of these projects is:

a) The PMB project made 53.6 per cent progress in financial terms up to end April 2018. In addition, about 59 per cent of the main bridge construction was reported to be completed. This implies that only 5 per cent progress has been made in financial terms (of the total project plan) during the first ten months of FY2017-18.
b) DMRTDP project attained a cumulative financial progress of 14.9 per cent up to April 2018; of which only 5.4 per cent progress could be made during the first ten months of FY2017-18.
c) MUSCCFPP project is still in its early implementation phase and has attained 14 per cent cumulative progress till April 2018 which was only 2.8 per cent till June 2017. This implies that 11.2 per cent financial progress has been made during July–April of FY2017-18 which is a very positive sign.
d) MSTPP's (Rampal power plant) main plant fencing work has already been completed. The project received a symbolic allocation of Tk. 52 crore in the RADP for FY2017-18 for land development protection and building boundary wall for second block. Till April 2018, 15.9 per cent of the full project cost could be utilised of which 14.1 per cent financial progress was made in the first ten months of FY2017-18.
e) The first phase of the RNPP project has achieved 95.8 per cent financial progress till April 2018, while the main project with a cost of Tk. 113,093 crore has attained 8.1 per cent cumulative progress up to April 2018. It should be noted that the main project was included into the ADP of this fiscal year and received one of the highest allocations. However, the rate of utilisation (58.2 per cent) of the allocated fund during the first ten months was only marginally better than the overall ADP implementation (50.2 per cent) during the corresponding period.
f) PBRL project, which had received the second highest allocation among the fast track projects after RNPP, attained 6.3 per cent cumulative progress up to April 2018; of this only 0.4 per cent could be made during the first ten months of FY2017-18. The project was awaiting to get nod from its key financer, the China Exim Bank, with which an MoU was signed on 27 April 2018. The Executive Committee of the National Economic Council (ECNEC) has recently approved the revised project with additional cost of around 4,000 crore.
g) Based on the project cost, the cumulative progress of Dohazari Ramu Cox's Bazar and Ramu to Gundam Rail Track project (dual gauge) till February 2018 was 16.4 per cent; the earlier version of the project (meter gauge) was already well behind deadline. However, it gained some momentum in this fiscal year.
h) ECNEC initially approved an amount Tk. 1,128 crore to develop primary infrastructure associated and facilities to make Paira port operational. The feasibility study of this project has been submitted. Some limited scale infrastructures such as pontoon, crane and security building have already been developed on a 16-acre piece of land; remaining preliminary infrastructure works were scheduled to be completed by June 2018. However, the project cost shot up by nearly 197 per cent, to Tk. 3,351 crore, from the original estimate of Tk. 1,128 crore. Its timeline has now been extended up to June 2020, according to the revised proposal. Until April 2018, the project made a cumulative progress of 16.4 per cent as per the revised project cost.
i) Construction of the LNG terminal in Maheshkhali is at an early stage. In December 2016, Excelerate Energy announced that it had completed the required geotechnical and geophysical studies for the Maheshkhali LNG terminal, with a target of delivering the first LNG in early 2018. The first consignment of LNG reached Chittagong through the Excelerate Energy's floating storage and re-gasification unit (FSRU) in April 2018. The project is expected to be completed by 2020.

Based on the assessment presented above, one may conclude that the overall progress of the 'fast track' projects has been below the respective targets and not up-to-the-expectation (see Annex Table 1.3). Although five of the nine projects have made visible progress, a number of projects are behind the schedule. As a result, the distinction between 'fast track' projects and other projects remains rather unclear from the perspective of project implementation. It is expected that keeping in mind the upcoming national election, a healthy share of the development budget will be allocated to these projects in the ADP for FY2018-19 to make their progress visible.

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

In view of the low level of private investment and significant infrastructural deficit, better (in terms of quality) and timely implementation of the ADP, particularly that of growth enhancing infrastructure projects, should remain a policy priority. CPD selected a set of 20 projects under the FY2017-18 ADP which were expected to attract investment and thus stimulate growth and employment. Share of allocation for these projects in the ADP for FY2017-18 was 11.7 per cent. 13 of these 20 projects were supposed to be completed in FY2016-17 (or even earlier). Cost and completion deadlines of a number of these projects were revised; in case of a few, for more than once. All of these 13 projects were carried forward in the ADP for FY2017-18. Analysis of the progress of these 20 priority projects also suggests that majority of these will not be completed within FY2017-18 (see Annex Table 1.4).

Actual combined spending for the aforesaid 20 projects was somewhat higher (39.1 per cent during July–February of FY2017-18) than the average for all ADP projects (37.8 per cent during the same period). However, within this group, performance has tended to vary.[2] Only nine projects had more than 39.1 per cent implementation rate while one project (SASEC Road connecting Project-II: Improvement of Highway Four Lane Road of Elenga-Hatikamrul-Rangpur) had 0.1 per cent implementation during July–February of FY2017-18. Only three[3] projects are close to being completed while Bheramara Combined Cycle Plant (360 MW) Development project achieved 100 per cent financial progress by November 2018.[4] It is to be noted that, all four (could be completed) projects were already in the 'carryover' list.[5]

In case of the 10 projects which were supposed to be completed in FY2017-18 as per the timeline provided in the ADP for FY2017-18, a total allocation of Tk. 9,548 crore was needed for timely completion. However, only Tk. 3,496 crore was earmarked for these projects in RADP for FY2017-18. Considering the revised allocation that was made for FY2017-18, there are at least three projects (Dhaka–Chittagong Railway Development Project, Construction of Ghorashal 365 MW Combined Cycle Power Plant, Shahjalal Fertilizer Project) which could perhaps be completed if a 'final big push' could be given for their completion. However, it appears that the majority, if not all, of these projects will not be completed according to their timelines and will be carried forward to the ADP for FY2018-19.

Meanwhile, with regard to setting up of a number of 'model' special economic zones (SEZs) on a priority basis, progress of work till now leaves much to be desired. Only two SEZ projects (Jamalpur Economic Zone and Land Acquisition for Araihazar, Narayanganj, Mirsarai and Chittagong Economic Zones) are currently under the purview of the ADP. However, allocation made for these two projects are not adequate for their on-time completion. Even with full utilisation of the budget allocated in the RADP for FY2017-18 (Tk. 560 crore), only about 51.0 per cent of the total work may be completed by the end of the fiscal year.

Strengthen IMED with follow-up mechanisms to realise recent initiatives/policy decisions

One may recall that a number of proposals relating to expediting ADP implementation were announced last few years by the Planning Minister. These included: (i) assigning a dedicated official to each government agency for monitoring and evaluating respective projects, and (ii) delisting the longstanding 'non-operational'

[2]The standard deviation of these 21 projects is 31 which suggests large variance in execution rate of these projects.

[3]These are: Dhaka-Chittagong Railway Development Project, Ashuganj 450MW CCPP (North), Shahjalal Fertilizer Project.

[4]Considering the cumulative completion rate being more than 75 per cent.

[5]These projects were scheduled to be completed within FY2014-15 and FY2016-17 as per project timelines.

projects from the ADP[6]. Furthermore, in order to discourage the misuse of scarce public resources, ensuring transparency and accountability in development project execution, IMED has recently proposed inclusion of a number of provisions in the current Development Project Proforma (DPP) format. These include incorporation of the project design life, a compulsory feasibility study report, annual maintenance chart, analysis of stakeholders, responsibilities of project directors and executing agencies, and indicators to measure the project impact in terms of achieving the Sustainable Development Goals (SDGs). However, ensuring adequate follow up of these good initiatives remains a recurring concern. It is suggested that the upcoming budget should report on the progress made as regards the proposed actions.

As is known, the IMED provides, on a regular basis, a number of recommendations in the annual progress reports prepared on the challenges faced during the project cycle. But, these are often not adequately followed up with concrete measures. Regrettably, majority of these recommendations tend to be ignored by ministries and divisions since the IMED lacks legal authority to command compliance. For example, a total of 52 projects which were scheduled to be completed by June 2018, have requested for allocation once again in FY2018-19. Despite ensuring adequate allocation, and notification and guidance to the relevant ministries and divisions by the Planning Commission for timely completion, the concerned projects have been carried over and included again with symbolic allocation in the ADP of FY2018-19. These recommendations should be discussed and followed up in the quarterly progress meetings to monitor the progress. Energetic steps ought to be taken towards timely implementation of these proposals by the line ministries and relevant entities.

Put emphasis on higher allocation for social sectors and implement National Social Security Strategy (NSSS) targets in FY2018-19

With limited resources and higher investment demand for infrastructure development, the government faces formidable challenge in allocating adequate resource for the competing sectors. However, despite strong economic growth and the resultant higher allocative capacity of the government, the share of Government exchequer in social sectors, particularly in health and education sectors, has not experienced any major improvement. Consequently, Bangladesh is lagging behind both in terms of quality of education and health, and their outcomes despite the quantitative rise in allocation for the aforesaid sectors. The Government of Bangladesh (GoB) is confronted with the dual challenge of increasing public spending on health and education, and at the same time improving the standard of service and performance of these sectors. In view of government's commitment to attain the SDGs, particularly in areas such as education (SDG 4: Education for all by 2030) and health (SDG 3: Ensuring healthy lives and promote wellbeing for all by 2030), the urgency to address the attendant deficits has risen manifold in the current context. Ensuring adequate allocations for these two SDGs are also important since they have synergetic effect on other SDGs, such as SDG 1 on eradication of poverty, SDG 2 on attaining zero hunger and SDG 10 on reducing inequality.

Notwithstanding the marginal rise in budgetary allocations for the social sectors over the past years, Bangladesh is still one of the lowest ranked countries in the world in terms of its public expenditure for social sectors. This is not only lower compared to the globally recommended targets but also significantly low compared to the needs of the population. According to World Bank and International Monetary Fund (IMF) data, Bangladesh was ranked among the bottom group of countries with regard to education (85th out of 90 countries), health (197th out of 197 countries) and social protection expenditure (36th out of 47 countries) as percentage of GDP.

CPD (2018a) in its budget proposal noted that in view of the budgetary targets for social sectors set in the 7FYP, resource allocations for education, health and social security need to be enhanced to 2.84 per cent,

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[6]In this connection, it was planned that the concerned ministries and divisions would be served letters on 1 October every year to send the list of non-performing projects to the Planning Commission.

1.12 per cent and 1.60 per cent of GDP respectively in FY2018-19. The government also needs to take concrete steps to fully implement the NSSS. Further, the proposed universal pension scheme should receive adequate fund.

As may be observed from earlier trends, budgetary targets did not consider the proposals set out in the NSSS. For example, allowance for old age scheme was Tk. 1,440 crore in FY2015-16 while the NSSS targets are Tk. 2,010 crore (see Annex Table 1.5). Recently, after a meeting with the Finance Minister, it was decided to raise the allocation and coverage of several programmes under social safety net schemes by about Tk. 11,000 crore, from the existing Tk. 54,206 crore, in the upcoming FY2018-19 budget. This proposal is likely to raise the monthly allocation of several major safety net programmes, but will still fall short of the NSSS targets.[7]

Comparing the NSSS target allocation to the budget allocation of FY2017-18, it is seen that there was a significant gap of at least Tk. 1,640 crore for the old age allowance, Tk. 6,776 crore for child school stipends, Tk. 1,401 crore for the allowance dedicated to widowed women and Tk. 1,327 crore for disabilities schemes. Even though GoB has planned to increase the monthly allocations for the schemes, the total allocation will still be lower than the target level as stated in the NSSS document. Similarly, comparing the NSSS financing target with the proposed budget allocation for FY2018-19, it appears that there will be a financing gap.[8] Indeed, financial gap exists also for the aforesaid four schemes, between medium-term budgetary framework (MTBF) projection and NSSS target for FY2018-19.

Government efforts for social safety net programmes are not only inadequate in monetary terms but also from the perspective of coverage. For example, although the NSSS has proposed to raise the coverage of the beneficiaries under the old qge scheme to 55 lakhs by FY2017-18, according to MTBF for FY2017-18, it was expected to remain at 35 lakhs in FY2017-18 and 38.5 lakh in FY2018-19; number of beneficiaries for the old age scheme is proposed to be 40 lakhs in the upcoming fiscal year (see Annex Table 1.6). The coverage for widow's allowances is proposed to rise to 14 lakhs, though still lower than the NSSS target (32 lakhs) for FY2017-18. The increases in both these cases are not significant, though the proposed rise exceeds the MTBF projections. Similarly, the eligible beneficiaries of the disability scheme is proposed to stand at 9.3 lakhs in FY2018-19 as against the target of 10 lakhs set out in the NSSS by FY2017-18.

One of the major reasons cited for GoB's inability to earmark adequate allocations for social safety net programmes, aimed at the relatively more vulnerable and marginalised groups of the population, is resource constraint. Curiously, over the last seven years, between FY2011 and FY2017, the budget has never reached the target level. For example, in FY2016-17, the budget deficit was Tk. 37,102 crore. This is also the same for FY2017-18. While the targets set forth in the NSSS may appear to be rather ambitious, the reality is that government spending and implementation are lagging far behind the required levels.

1.2.4 Budget Deficit

Budget deficit financing needs an optimum mix

As has been the case for the last six years, budget deficit was well within the planned limit, when the first six months of FY2017-18 is considered. Although a significant revenue shortfall is envisaged, this will be offset by the lower public expenditure. The structure of financing was characterised by low net intake

[7]Old age scheme is proposed to be the same, monthly payment of Tk. 500, in FY2018-19. In comparison, the NSSS target is about Tk. 600 for the corresponding fiscal year. Other than this, monthly allowance for widows will also remain unchanged at Tk. 500, while their coverage will increase by 35,000 persons.

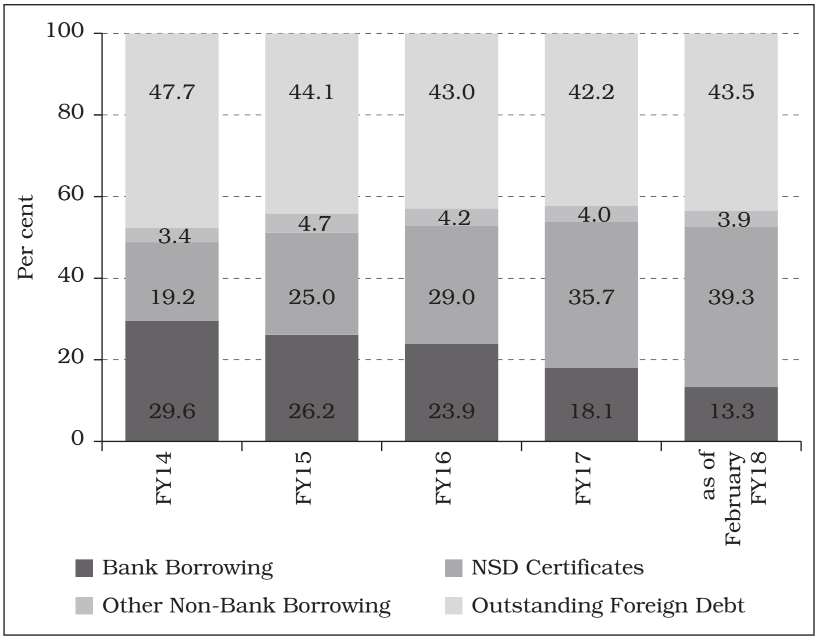
[8]The expected gap in FY2018-19 is approximately Tk. 1,560 crore for old age allowance and Tk. 1,580 crore for allowances for widowed women and Tk. 1,489 crore for disabilities schemes.

from foreign financing sources as against a heavy reliance on domestic financing sources. Within domestic financing structure, buoyant sale of high yielding national savings directorate (NSD) certificates was once again the key contributor in FY2017-18. One of the major challenges for budget FY2018-19 will be to bring back an optimum mix in the financing of the budget deficit. Since a large share of the financing has already been secured from the sale of NSD certificates, the need for bank borrowing may rather be limited. Net sales of NSD certificates stood at Tk. 33,120 crore during July–February of FY2017-18 which is already 9.9 per cent higher than the annual target set for FY2017-18. However, improvement in the utilisation of foreign resources was a positive sign and needs to be consolidated further.

Composition of outstanding public debt of Bangladesh

As regards public debt, Bangladesh's position has been, in general, comfortable. Total public debt as share of GDP is expected to increase from 31.5 per cent in FY2015-16 to 35.7 per cent in FY2019-20 (MoF, 2017). Currently, about 57 per cent of the public debt is attributable to domestic source and 43 per cent to foreign finance (Figure 1.4). Structure of debt and debt servicing will hinge on the government's ability to use more of the low-cost foreign borrowings as against high cost domestic borrowing. This, however, is not observed in recent years.

Figure 1.4
Composition of Outstanding Public Debt

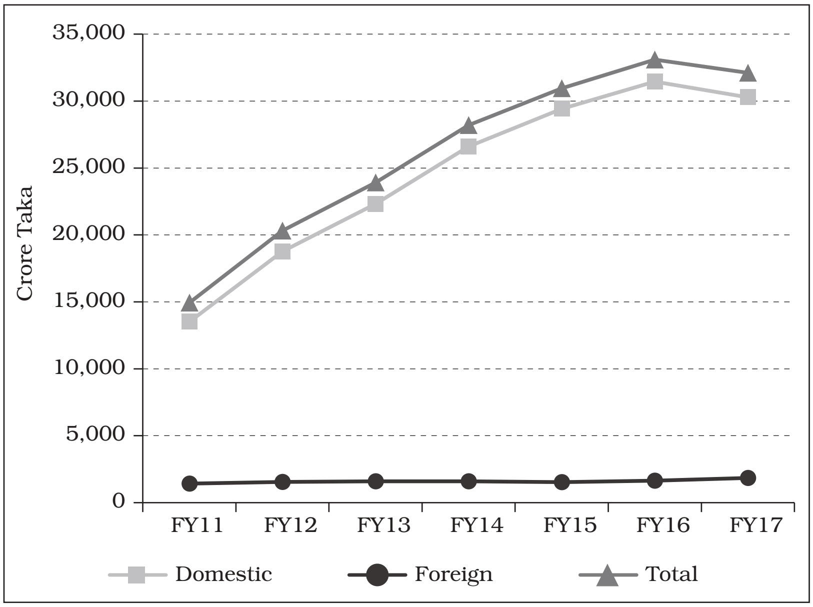


Source: Authors' estimations from the Economic Relations Division (ERD) and Bangladesh Bank data.

Within the domestic sources, debt from non-bank sources is increasing, spearheaded by the net sales of NSD; in contrast, debt from bank sources is decreasing. This has led to a gradual shift in the overall composition of the public debt. Indeed, as of February 2018, debt against sale of NSD certificate accounted for 69.5 per cent of the total outstanding domestic debt liability of the government (Tk. 224,356 crore). The corresponding figure was about 36.8 per cent (Tk. 76,398 crore) in FY2013-14. In comparison, the proportion of outstanding foreign debt in the overall debt portfolio has been rather steady.

As is known, the debt incurred from domestic sources comes with a relatively high interest rate. Interest rate on bank borrowings was 9.6 per cent while 11.7 per cent for non-bank financial institutions (NBFIs) as of end June 2017. Although, both these interest rates have reduced in recent times, still these remained higher than those on borrowings from the foreign sources. Due to high cost borrowing from the domestic

Figure 1.5
Interest Payment Expenditure



Source: Authors' calculations based on Ministry of Finance (MoF) data.

sources, the overall interest payment burden of the government has been on the rise over the past years. Total interest payment increased by a staggering 114.9 per cent from Tk. 14,943 crore in FY2010-11 to Tk. 32,114 crore in FY2016-17 (Figure 1.5). This constituted 20.9 per cent of all non-development expenditure as of December 2017.

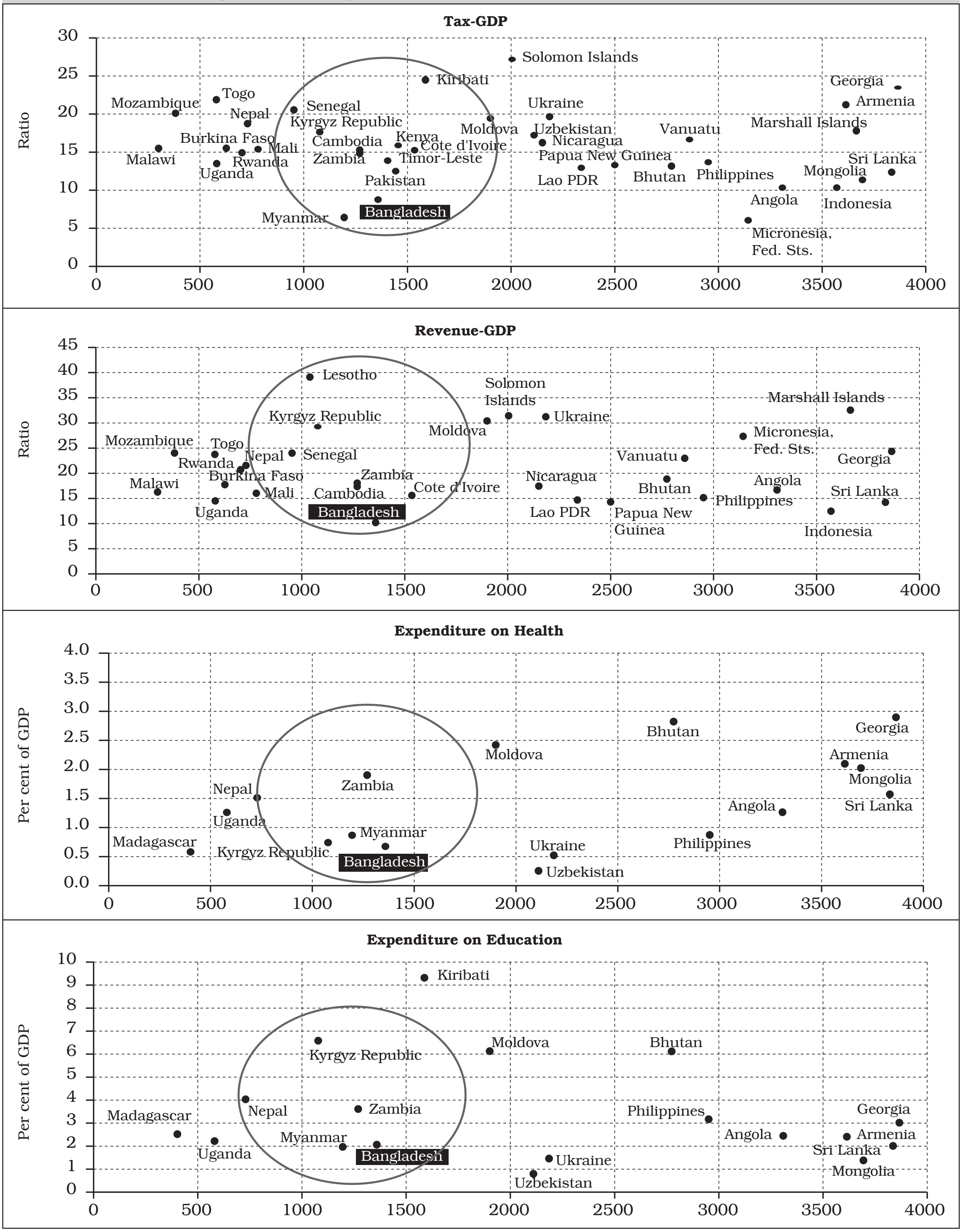
As NSD instruments entail payment of higher interest rates and, hence, higher debt servicing liability, CPD (2017b) recommended a downward revision of the NSD rates. Similar proposition was also made with respect to the maximum ceiling on purchase, particularly in view of the fall in the deposit interest rates of the commercial banks and also the medium to long-term implications of accumulating debt servicing liabilities of the government. It is encouraging to find that the government has also acknowledged the need and hinted on revising the rate downward immediately after FY2018-19 budget. Another necessary step that the government should implement relates to creating an integrated electronic database for the NSD certificate purchase so that the purchase limit clause can be enforced without harassing the small investors.

1.2.5 Fiscal Framework for FY2018-19

As stated earlier, Bangladesh has one of the lowest resource mobilisation and expenditure ratios in the world considering the size of its economy. An exercise was conducted by using the World Bank and the IMF data to scatter-plot middle-income countries (MICs) with per capita GDP up to USD 4,095 and compare Bangladesh's position with low and middle-income countries (LMICs) having similar per capita GDP according to different fiscal parameters (Figure 1.6). One observes the following:

- Tax-GDP ratio ranges from 6.5 per cent to 34.2 per cent (Median: 14.9 per cent) for countries with per capita GDP between USD 1,000 to 1,500 whereas the corresponding ratio is only 8.5 per cent for Bangladesh.
- When it comes to revenue-GDP ratio, the ratio varies from 10.3 per cent to 39.1 per cent (Median: 18.1 per cent) in contrast with Bangladesh's revenue-GDP ratio of 10.3 per cent, the lowest in the cohort.
- On the contrary, countries with the aforesaid per capita GDP, on an average, spends 0.9 per cent and 3.8 per cent of the GDP respectively on health, and education. Bangladesh spends only 0.7 per cent, and 2.1 per cent of GDP respectively on the corresponding fiscal parameters.

Figure 1.6
Fiscal Parameters: Bangladesh Among the MICs



Source: Authors' calculations from World Development Indicators (WDI), World Bank and International Monetary Fund (IMF) databases.

Planned size of the budget (Tk. 460,000 crore) is envisaged to grow by about 24 per cent compared to the revised budget for FY2017-18 (RBFY2017-18) (Table 1.4). Revenue earnings will need to rise faster than public expenditure. However, budget targets take revised budget figures for FY2017-18 as the reference point. In view of this, according to CPD projections, all major parameters of fiscal framework will need to register higher growth rates to attain the targets compared to those planned in the budget FY2018-19. CPD projected that the total expenditure will need to grow by 51.8 per cent from FY2017-18 while revenue earnings will need a growth of 43.0 per cent in FY2018-19 compared to FY2017-18.[9] However, in the backdrop of the actual outcome of expenditure and income in FY2017-18, once again the fiscal framework may find the targets to be vulnerable in the face of reality, undermining the fiscal framework.

The proposed budget also envisages that the development expenditure will grow slower (16.6 per cent) than the non-ADP expenditure (29.0 per cent). The proposed budget for ADP of Tk. 173,000 crore for FY2018-19 is 37.6 per cent of the total public expenditure, which stood at 40 per cent in the RBFY2017-18. Overall, the budget deficit has been projected to be about 5.0 per cent of GDP in FY2018-19. In the budget for FY2018-19, it is expected that balance in financing the budget deficit will be restored through low foreign financing and increased non-bank borrowing. The proposed net foreign financing (including foreign grants) for FY2018-19 (Tk. 38,000 crore) is about (-) 17 per cent lower than the RBFY2017-18.[10] Government has also planned to further increase its financing from non-bank sources by about 43 per cent compared to that targeted for RBFY2017-18.

Table 1.4
Growth Rates, Budget vs. Reality

(in per cent)

Component	**Budget FY19 over Budget FY18**	**Budget FY19 over RBFY18**	**Budget FY19 over FY18 (CPD Projection)**	**FY17 over FY16 Actual**
Revenue	16.1	29.1	43.0	16.1
Tax revenue	*17.4*	*29.6*	*45.3*	*17.1*
Non-tax revenue	*5.8*	*22.7*	*30.6*	*9.0*
Total expenditure	15.0	24.0	51.9	9.3
ADP	*12.8*	*16.6*	*91.1*	*-3.5*
Non-ADP	*16.3*	*29.0*	*35.0*	*15.7*
Overall deficit (excluding grants)	12.0	12.3	77.7	8.4
Net foreign borrowing and grants	-26.8	-17.0	333.4	-49.1
National saving schemes and others	105.3	42.9	-17.5	52.6

Source: Authors' calculations from Ministry of Finance (MoF) data.

The aforementioned amount of Tk. 173,000 crore has been allocated for 1,452 projects in the ADP for FY2018-19. The amount is 16.6 per cent higher than the RADP for FY2017-18 and 10.9 per cent higher than the original ADP for FY2017-18. Of the amount, Tk. 32,555 crore (18.8 per cent of total) has been set aside for the nine mega projects, which is almost identical to the current fiscal year. This is somewhat contrary to the prevailing rhetoric of allocating more resources for these projects in view of the upcoming elections. Of these projects two including the Dhaka-Ashulia Elevated Expressway and a separate railway bridge along the Bangabandhu Bridge on the Jamuna River were introduced anew in the ADP of FY2017-18. Further, keeping in mind the national elections, all the 300 Members of the Parliaments (MPs) would receive allocations to the tune of Tk. 7,595 crore in total for the construction of five-storey buildings for six madrasas in each electoral area.

[9] CPD (2018b) projected a revenue shortfall of about Tk. 50,000 crore in FY2017-18.

[10] Regrettably, end of FY2016-17 data reveals that the government materialised little more than one-fourth (Tk. 7,900 crore of targeted Tk. 28,771 crore) of its net foreign borrowing targets set for RBFY2016-17.

An assessment of the gap between sectoral ADP expenditure and 7FYP public investment targets suggests that, allocations and expenditures of 16 ADP sectors were aligned with 10 sectors of the 7FYP for which allocation targets were provided. It was also found that:

- Between FY2015-16 and FY2017-18, 6[11] out of 10 sectors received lower amount (ranging from 1.4 per cent FY2017-18 ADP allocation for Power and Energy to 59.6 per cent FY2016-17 ADP allocation for Local Government and Rural Development) than their respective targets set out in the 7FYP. They also spent lower amount than was allocated in the respective ADP and RADP (Table 1.5).
- On a positive note, priority sectors such as infrastructure (Transport and Communication) and social sectors (Education, Health) received more allocation than the 7FYP targets.
- However, due to inability of the concerned entities to utilise the allocated funds, the gaps between 7FYP targets and respective RADP and actual expenditure figures have increased in every fiscal year for the aforementioned three sectors.

In FY2018-19, following the previous trend, infrastructure and social sectors once again received higher allocations compared to the 7FYP targets. However, according to above stated findings, these allocations are not being fully utilised, and consequently, the expected results are also not being realised.

Table 1.5
ADP Expenditure Gap as Percentage of 7FYP Targets

(in Per cent)

Sector	FY16			FY17			FY18		FY19
	ADP	RADP	Actual	ADP	RADP	Actual	ADP	RADP	ADP
Agriculture	15.4	25.3	17.5	36.8	28.0	31.1	36.7	44.3	36.4
Local Government and Rural Development	52.3	50.2	50.9	59.6	52.2	52.6	51.0	37.7	46.9
Industrial and Economic Services	7.5	-1.6	25.9	17.5	55.1	65.2	34.0	51.4	48.4
Power and Energy	0.0	10.5	10.3	-105.3	28.5	13.7	1.4	-11.4	0.7
Transport and Communication	-0.9	11.9	22.4	-2.5	0.7	22.8	-22.9	-10.6	-18.6
Housing and Community Amenities	-490.9	-486.9	-456.3	-660.9	-717.7	-690.2	-615.3	-624.7	-630.2
Education and Technology	-5.3	1.7	1.7	3.0	0.5	9.9	-34.3	-15.6	-13.2
Recreation, Culture and Religion	47.4	54.3	55.1	48.8	54.2	58.0	23.3	56.6	26.3
Health	-14.1	-4.2	16.7	-2.8	16.7	35.5	-80.4	-69.9	-23.6
General Public Services	31.4	44.3	72.1	7.1	28.5	42.7	30.1	45.7	26.6
Total	**0.0**	**6.2**	**14.0**	**8.5**	**8.5**	**16.7**	**-8.2**	**-2.9**	**-2.4**

Source: Authors' calculations using Implementation Monitoring and Evaluation Division (IMED) and Bangladesh Planning Commission (2015) data.

Based on the ADP analysis of the current fiscal year, five major conclusions can be drawn in view of the ADP for the next fiscal year.

- The quality of ADP implementation has not made any major breakthrough.
- The success of ADP implementation in FY2018-19 will largely hinge on the implementation of mega

[11]These sectors include Agriculture, Local Government and Rural Development, Industrial and Economic Services, Power and Energy, Recreation, Culture and Religion, General Public Services.

projects. Particularly, new projects or projects which are in the early stage of implementation will be required to kick-off well.

- Better utilisation of project aid in the current and upcoming fiscal years will, to a large extent, determine the overall pace of implementation. This is also important because of lowering debt-servicing liability.
- The government could not avoid taking populist projects (e.g. allocation for MPs, symbolic projects for the local government); neither could it limit the number of projects. According to policy statement the number of new projects should be limited to ensure allocation of adequate funds, for completing projects on time and to increase their development impact.
- The current implementation pace of Fast Track projects may not be adequate for their timely implementation; as a result, the expected benefits will be delayed.

More transparency in fiscal and budgetary processes should be one of the key areas of economic reforms in Bangladesh. Similar to a number of other developing countries, Bangladesh practices a budgetary process which is both complex and complicated, and at times also lacks consistency. In this connection, more focus is needed on implementing 'second generation' reforms to ensure higher levels of transparency and independence of regulatory bodies in order to raise efficiency, enhance competitiveness and guarantee distributive justice. In successive IRBD reports, CPD has strongly suggested in favour of undertaking a number of needed reform measures in order to improve macroeconomic and sectoral performance. It is worth repeating this here:

(I) Establish a Public Expenditure Review Commission (PERC)
(II) Formulate appropriate follow up mechanism for monitoring government tax incentives
(III) Disclose financial accounts of SOEs including BPC

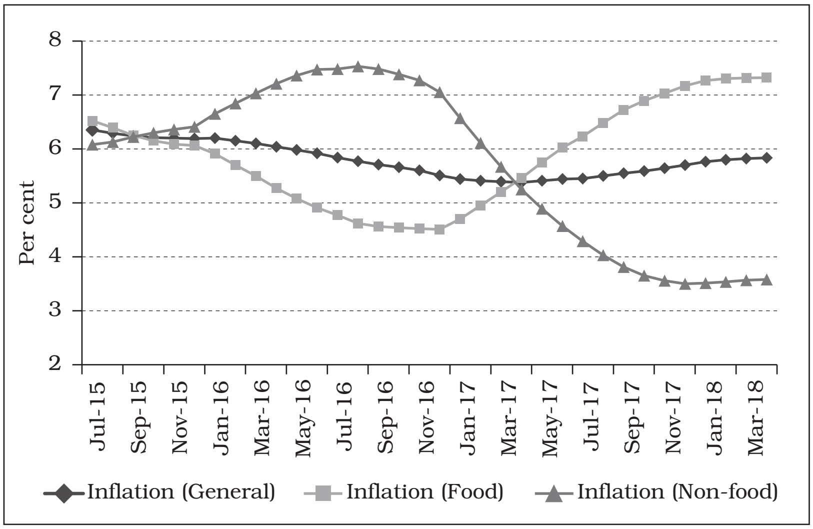
1.3 MONETARY POLICY AND BANKING SECTOR

Following the downward trend in average inflation rate, since August 2013, the inflation trajectory has started to move upward beginning from May 2017. On the other hand, the banking sector has been facing liquidity shortage in recent period. In this backdrop, key objectives of the monetary policy ought to be to ensure appropriate and timely measures to arrest growth of inflation and ensure adequate liquidity in the banking sector. As may be recalled, Bangladesh Bank in its Monetary Policy Statement (MPS) for the second half (H2) of FY 2017-18 aimed for maintaining price and macro-financial stability. It also referred to inclusivity and environmental sustainability in pursuit of employment—focused inclusive growth. A lot will depend on whether the Bangladesh Bank will be able to attain these objectives by pursuing an independent monetary policy.

1.3.1 Inflation Trends

Inflationary pace gained some strength in FY2017-18. Consecutive floods in Bangladesh during June–September 2017 left their footprints in terms of higher food prices. Indeed, food inflation started to rise from March 2017 onward and surpassed both general and non-food inflation from thereon. Food inflation overtook non-food inflation in April 2017; thereafter the divergence between the two has been on a steady rise (Figure 1.7). Thus, food inflation rose to 7.3 per cent in April 2018 from 5.5 per cent in April 2017 while non-food inflation declined to 3.6 per cent in April 2018, as opposed to 5.3 per cent in April 2017. As a result, general inflation increased to 5.8 per cent in April 2018, compared to 5.4 per cent in April 2017. Though lower than the target set out in the MPS of Bangladesh Bank for the January–June 2018 period (6 per cent), there is a need for the Bangladesh Bank to remain alert to the possibility of inflationary trend gaining momentum while crafting the monetary policy for the July–December 2018 period. As it is, annual average inflation target of 6 per cent is too high. For example, in 2018 Bangladesh had the 14th highest inflation target among 67 countries of the world (Annex Table 1.7).

Figure 1.7
National Inflation Rate (12-month average) (Base year 2005–06)



Source: Bangladesh Bureau of Statistics (BBS).

Flash floods in 2017 led to production disruption and crop losses, and consequently resulted in lower production of rice in 2016–17 (Table 1.6). Compared to 2015-16, the production of Aus rice fell by 6.8 per cent, whilst that of Boro rice fell by 4.5 per cent in 2016–17.

At the same time, the production of wheat also continued to decline in 2016–17 (Annex Figure 1.1). The cumulative impact drove food inflation high. The inverse relationship between food price and food production is quite evident in the case of Bangladesh. For example, analysis of historical data reveals that the change in the price of Aman rice is inversely related to the change in the level of its production (Figure 1.8). No doubt, the key to controlling food inflation lies in stabilising food supply.

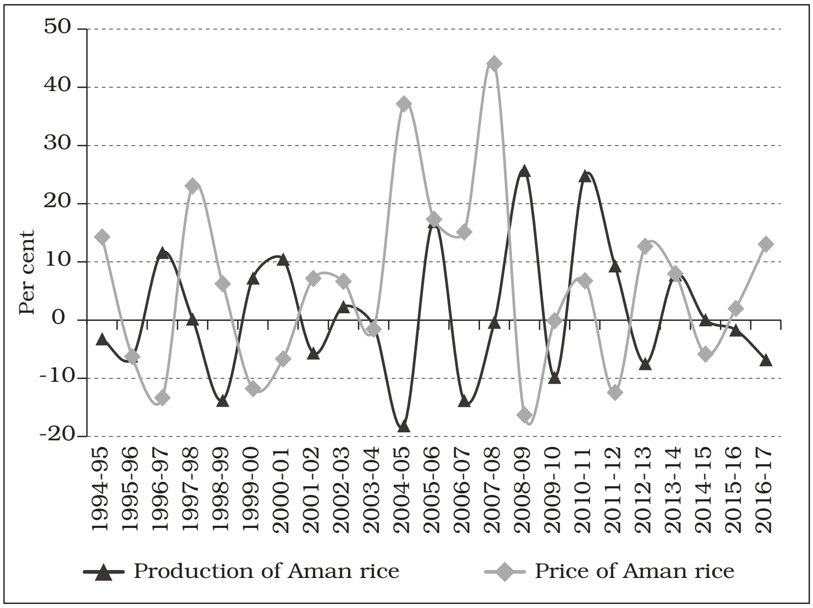
Table 1.6
Total Rice Production

(in Thousand Metric Ton)

Fiscal Year	Aus Rice	Aman Rice	Boro Rice
2000-01	1916	11249	11921
2001-02	1808	10726	11766
2002-03	1850	11115	12222
2003-04	1832	11521	12837
2004-05	1500	9820	13837
2005-06	1754	10810	13975
2006-07	1512	10841	14965
2007-08	1507	9662	17762
2008-09	1895	11613	17809
2009-10	1709	12207	18059
2010-11	2133	12792	18617
2011-12	2332	12798	18759
2012-13	2158	12897	18778
2013-14	2326	13023	19007
2014-15	2328	13190	19192
2015-16	2289	13483	18938
2016-17	2134	13656	18014

Source: Bangladesh Bureau of Statistics (BBS).

Figure 1.8
Aman Rice Production and Price

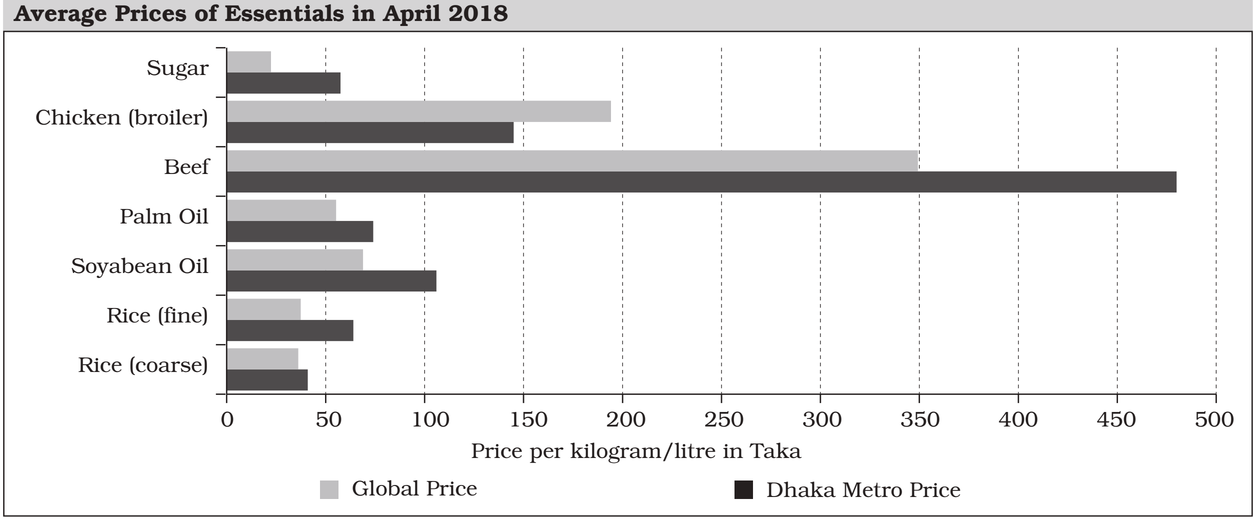


Source: Bangladesh Bureau of Statistics (BBS) data.

A comparison of Bangladesh's price levels with that of global markets indicates that the average prices of essentials in April 2018 was higher compared to international prices. For example, sugar was about 2.6 times more expensive in Dhaka metro markets in April 2018, compared to the world market. On the other hand, the price of soya bean oil was 54 per cent higher and the price of palm oil was 34 per cent higher in Dhaka in April 2018, in comparison to the world price (Figure 1.9). As is known, petrol and diesel are sold at administered prices on Bangladesh Bank. As of 28 May 2018, Bangladesh had the 65th cheapest petrol and the 39th cheapest diesel among 168 countries of the world (Global Petrol Prices, 2018).

The consumer price index (CPI) for all major non-food items, such as clothing, footwear, house rent, furniture, medical care, transport, and education increased in March 2018 compared to 2016–17 (Figure 1.10). This is particularly disquieting since it indicates an overall increase in the cost of living, a trend that has been going on for the past several years.

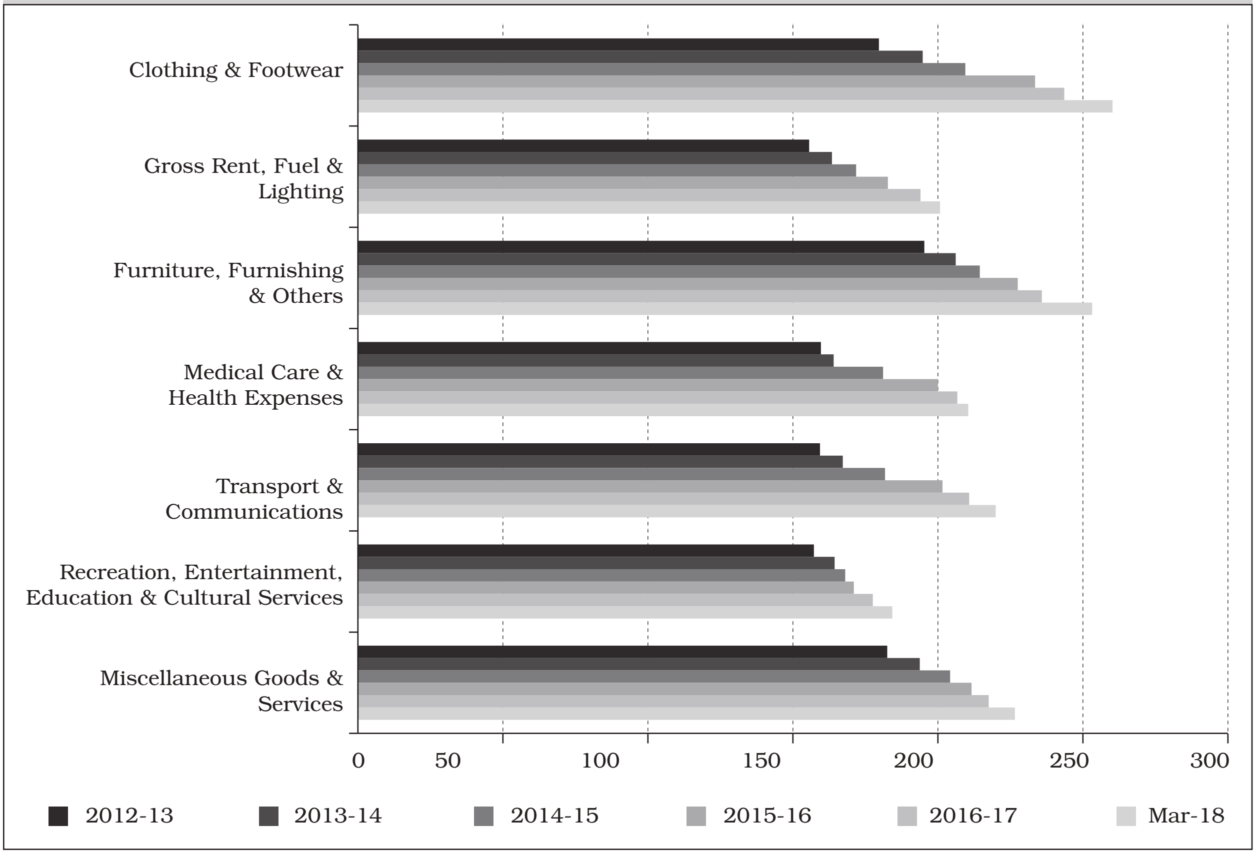
Figure 1.9
Average Prices of Essentials in April 2018



Source: Trading Corporation of Bangladesh & World Bank.

Figure 1.10

CPI of Major Non-food Items: 2012–2018 (Base year 2005–06)



Source: Bangladesh Bureau of Statistics (BBS).

Note: CPI is calculated with 2005-06 as base year.

1.3.2 Conduct and Misconduct of Monetary Policy

Monetary targets for the second half of FY 2017-18 were set to achieve a GDP growth of 7.4 per cent while maintaining the annual average inflation rate within 6 per cent (Bangladesh Bank, 2018). Overall growth of broad money supply (M2) up to April 2018 was 9.1 per cent compared to the MPS target of 13.3 per cent. This implies that further expansion of the money supply is expected in the coming months. The growth of the broad money, in recent years, has been influenced by net foreign assets and public–sector credit (CPD, 2018). The central bank has to be cautious as regards the growth of M2 since it has the potential to raise inflation.

Monetary policy is arguably the only remaining realm of the central bank's autonomy in Bangladesh. Yet in recent months, monetary policy has also succumbed to regulatory capture. There are growing concerns regarding the lack of transparency in the conduct of monetary policy. Whilst uncertainty about the conduct of monetary policy can make it easier for the central bank to deliver 'monetary surprises' and stimulate economic activity, such surprises can also lead to inflation (Cukierman and Meltzer, 1986). When key components of the money supply, such as reserve requirements, are altered, they tend to have significant effects on the general price level. Using annual data from the period 1973 to 2008, it has been shown that there exists a causal relationship between money supply growth and inflation in Bangladesh (Hossain, 2010). CPD's own analysis of annual data for the period 1996-2017 also reveal that there is a unidirectional causal relationship running from the supply of broad money to the price level (Table 1.7).

Table 1.7
Results of Granger Causality Test

Null Hypothesis	F Statistic (p value)	Chi Square Statistic (p value)	Interpretation
M2 growth does not Granger-cause CPI growth	4.06 (0.0599)	4.78 (0.0288)	Unidirectional causality running from M2 growth to CPI growth
CPI growth does not Granger-cause M2 growth	0.47 (0.5006)	0.56 (0.4554)	
Log of M2 does not Granger-cause log of CPI	8.83 (0.0082)	10.30 (0.0013)	Unidirectional causality running from log of M2 to log of CPI
Log of CPI does not Granger-cause log of M2	2.71 (0.1171)	3.16 (0.0754)	

Source: Authors' calculations from Bangladesh Bank and Bangaldesh Bureau of Statistics (BBS) data.
Note: (i) One period lag chosen; (ii) M2 growth is defined as percentage change in supply of broad money; (iii) CPI growth is defined as percentage change in consumer price index, base year 2005-06; (iv) M2 data from Bangladesh Bank and CPI data from Bangladesh Bureau of Statistics; (v) Granger causality implies predictive causality and not true causality.

Consequently, the central bank should exercise greater caution in the conduct of monetary policy, lest high inflationary pressure undermine the stability of the economy. In this regard, the central bank should be allowed the freedom to function properly without surrendering to the demands of loBangladesh Bankyists or being overshadowed by the Ministry of Finance (MoF).

1.3.3 Banking Sector

The performance of the banking sector remained off-track in FY2017-18. A number of key indicators could not meet their targets, while a number of scams and crises have remained unresolved. CPD has been closely following the banking sector and writing on its various aspects in successive IRBD reports. The section focuses on a few selected issues that are considered to be major concerns. These include non-performing loans (NPLs), BASEL III compliance, and the number of banks in the financial market.

NPLs: A South Asian phenomenon?

NPLs continued to pile up relentlessly, as NPLs hovered around the 10 per cent mark in the calendar year 2017 (Figure 1.11). Interestingly, NPLs fell below 9.5 per cent in December 2016, and again in December 2017. This is largely due to the practice of commercial banks writing off their loans at the end of the year in order to clean their balance sheets. Such off-balance sheet activities are particularly risky and may have destabilising effects on the overall banking sector. The general trend of NPL has been consistently high for the last few years. Financial frauds, lack of proper due diligence during loan sanctions, political influence on loan disbursement, and the failure to undertake strong measures against loan defaulters and wrong-doers have contributed to high NPLs in the banks. Additionally, the legal framework for dealing with NPLs, which consists of the Money Loan Court Act 2003 and Bankruptcy Act 1997, has become more or less dysfunctional. The number of judges dealing with NPL loan cases is inadequate, and as a consequence, the backlog of cases is a long one.

NPLs are classified into three categories: sub-standard loans, doubtful loans, and bad loans. Unfortunately, the amount of bad loans is much higher than the other types of NPL (Figure 1.12). Bad loans are such types of loans which are not recoverable and are considered as loss of the banks. As of December 2017, the amount of bad loans was Tk. 64,618 crore which was 87 per cent of total classified loans and 8 per cent of total loans.

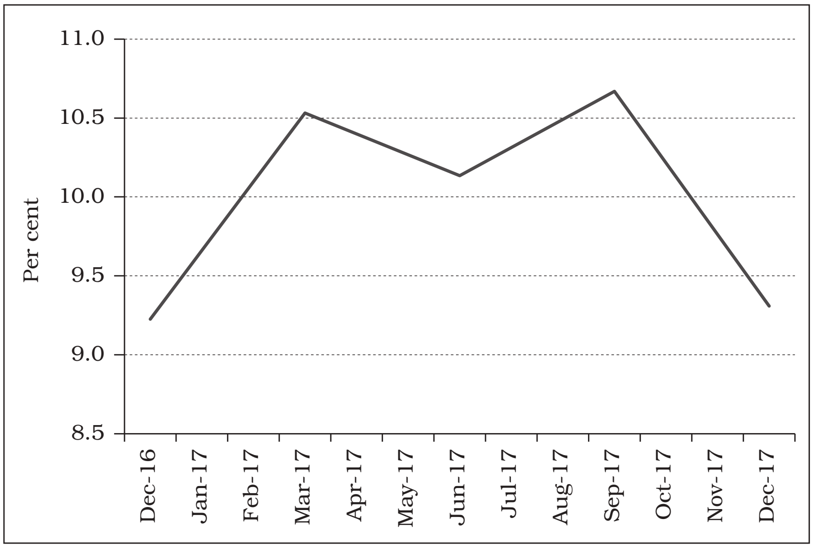


Figure 1.11
NPL as Percentage of Total Loans

Source: Bangladesh Bank.

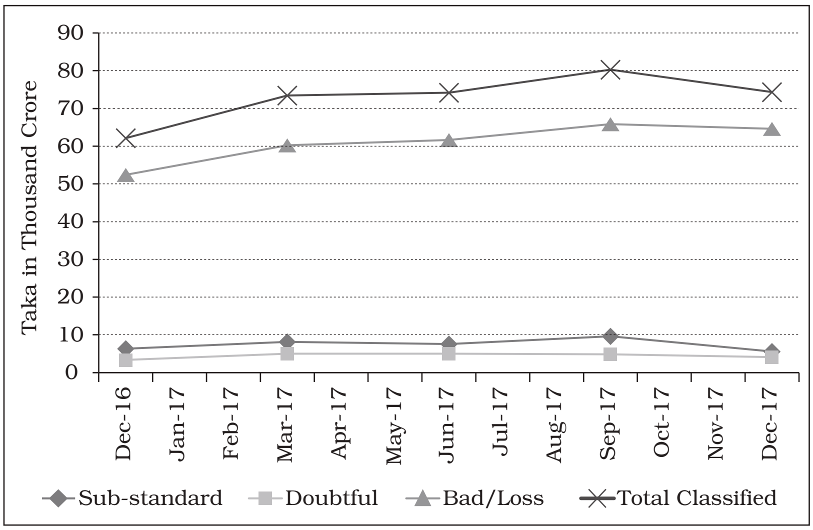


Figure 1.12
NPL and Total Loan by Types of Loan

Source: Bangladesh Bank.

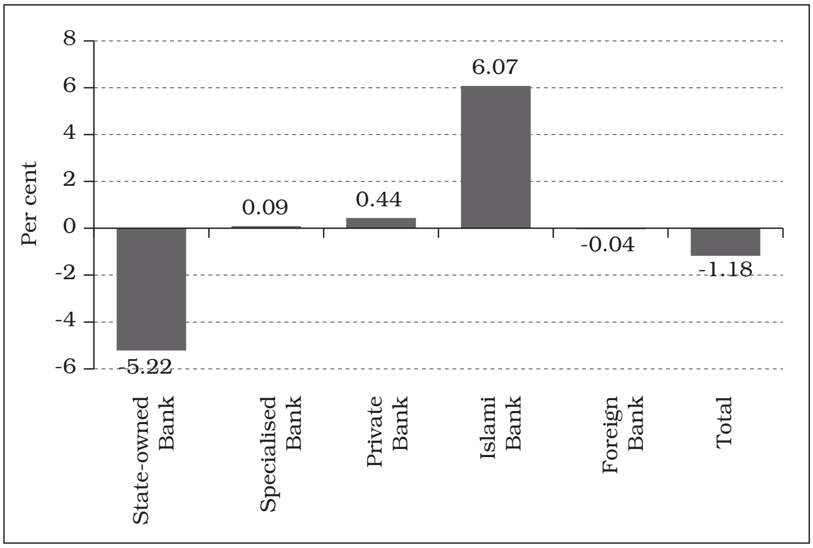
Large amount of NPLs coupled with higher dependency on NSD have contributed to recent liquidity shortage in the banking system. The liquidity position of state-owned commercial banks (SCBs) worsened between January and March 2018, as they registered a 5.22 per cent fall in total liquid assets. This led to a 1.18 per cent fall in total liquid assets in the overall banking sector from January to March 2018, even though private commercial banks (PCBs) and Islami commercial banks (ICBs) experienced improvements in the liquidity position during the same period (Figure 1.13).

The impact of reduced cash-reserve ratio (CRR) by Bangladesh Bank in April 2018 is yet to be observed. The wave of liquidity shortage was reflected in the money market. Call money rate (overnight average lending rate) was high, 4.31 per cent in April 2018 compared to 3.76 per cent in April 2017 (Figure 1.14). Average interbank lending rate was 5 per cent in March 2018.

Moreover, credit to the private sector has increased at a higher rate (18 per cent) during July 2017–March 2018 than the target rate (16.8 per cent) for FY 2017-18, though on a month-to-month basis, the growth of private sector credit came down to 13.6 per cent in April 2018, the previous months experienced higher

Figure 1.13

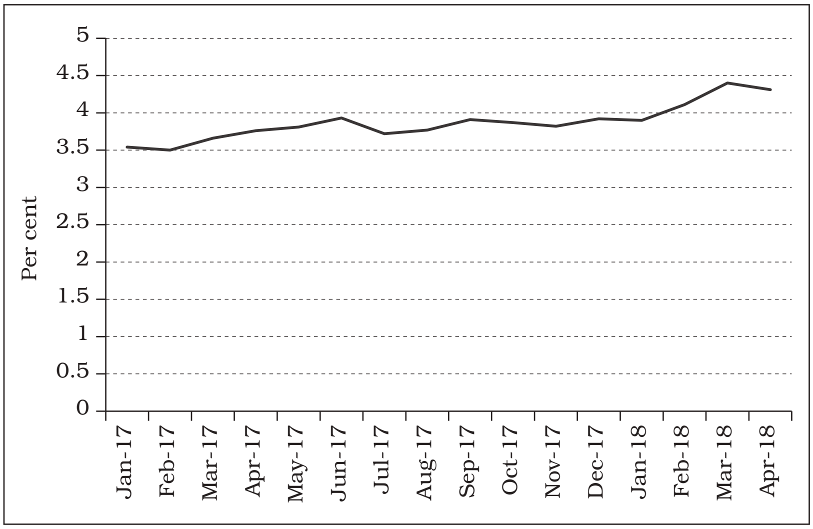
Change in Liquid Assets between January 2018 and March 2018



Source: Bangladesh Bank.

Figure 1.14

Call Money Market Average Lending Rate



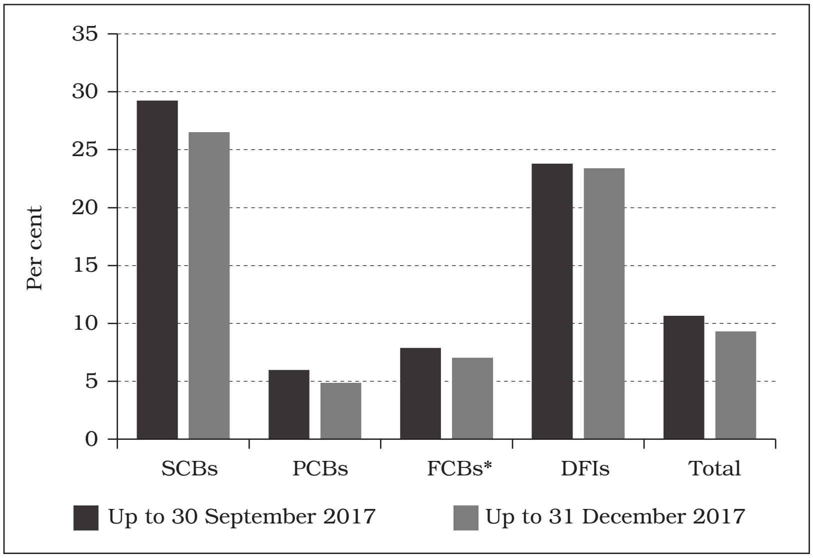
Source: Bangladesh Bank.

growth. However, what is more important is productivity of the credit and its quality. Both these remain areas of concern.

At a disaggregated level, the share of NPL in both SCBs and development finance institutions (DFIs) is very high. This reflects the inefficiency of SCBs and DFIs in loan management. Both SCBs and DFIs had more than 20 per cent NPLs in the second quarter of FY2017-18 (Figure 1.15).

In order to understand the effects of rising NPLs across countries, it is essential, at first, to get accustomed to the specific definition of an NPL. A loan that is in already in default, or close to being in default can be classified as a NPL (Bangladesh Bank, 2017). NPLs are also referred to as non-performing assets (NPAs) since loans are recorded as assets in a commercial bank's balance sheet. This is because loans create a stream of cash flows for a bank through the repayment of the principal and interest payments. According to the IMF, loans should be classified as NPLs if: i) payments of principal and interest are past due by 90 days or more, ii) interest payments equal to 90 days interest or more have been capitalised, refinanced, or rolled over, and/or iii) sufficient evidence exists to classify a loan as non-performing even in the absence of a 90

Figure 1.15
NPLs as Percentage of Total Loans by Bank Type

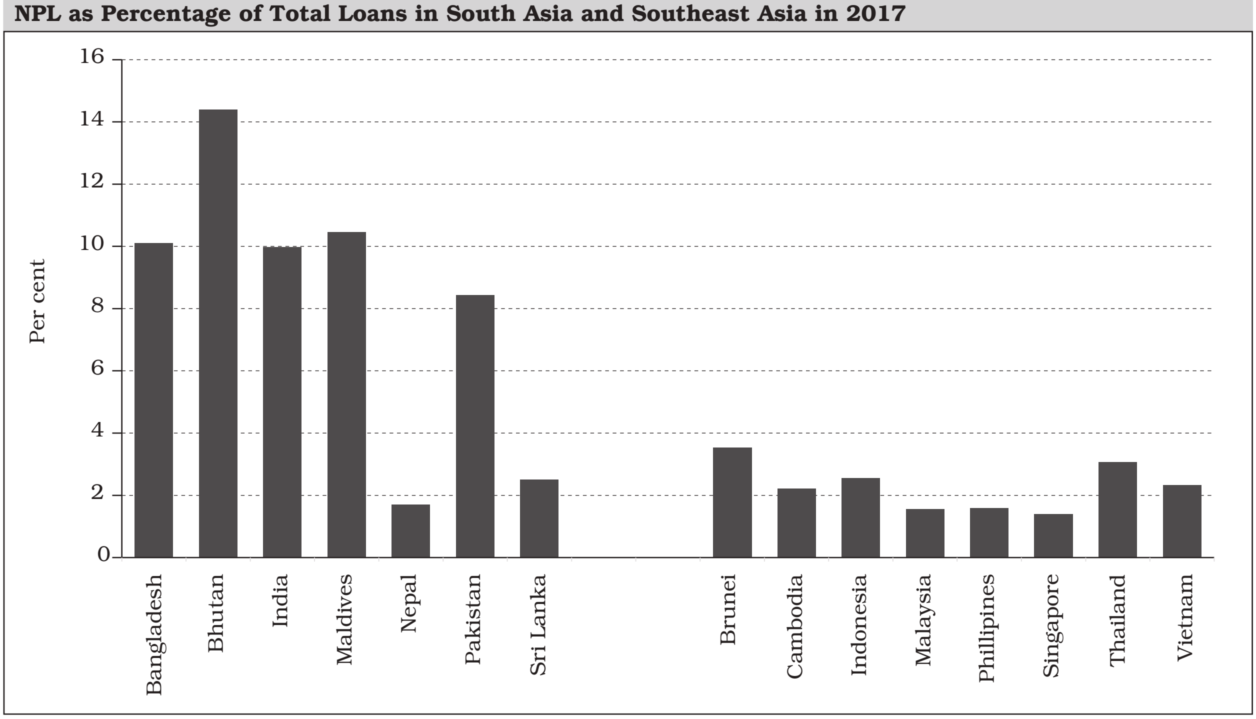


Source: Bangladesh Bank.
Note: *Foreign commercial banks (FCBs).

day past due payment, such as when the debtor files for bankruptcy. The 90-day mark is recommended as an upper threshold, and the IMF does not discourage more strict definitions of NPLs (IMF, 2006). However, there is no universal definition of an NPL, and it is acknowledged that definitions that may be appropriate in one country may not be equally appropriate in another. It is for this reason that cross-country comparability of NPLs is difficult, and adjustment of the figures may be required. However, the 90 day time period is the most widely used by countries to determine whether a loan is non-performing (Cortavarria *et al.*, 2000).

A cross-country comparison of NPLs shows that five South Asian countries, Bangladesh, Bhutan, India, Maldives, and Pakistan, had NPLs exceeding 8 per cent of total loans in 2017. On the other hand, eight

Figure 1.16
NPL as Percentage of Total Loans in South Asia and Southeast Asia in 2017



Source: Bangladesh Bank and International Monetary Fund (IMF).

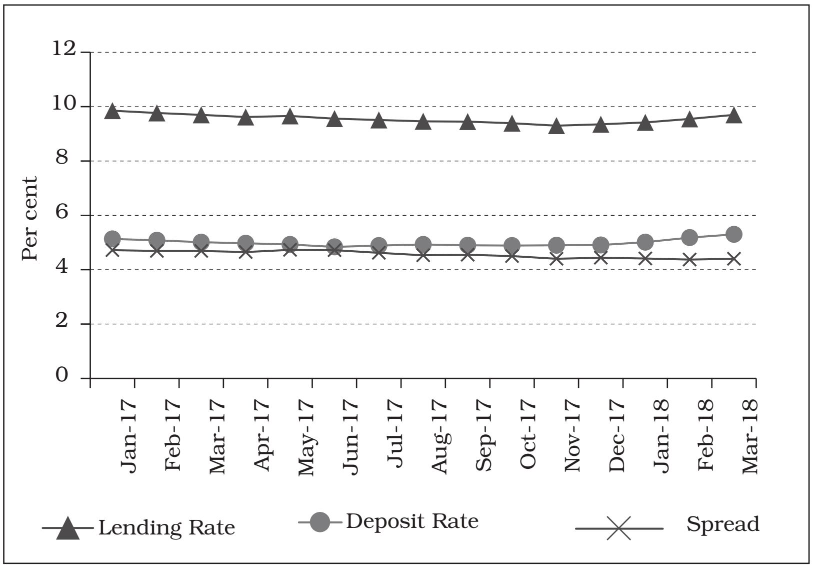
Southeast Asian countries, Brunei, Cambodia, Indonesia, Malaysia, Philippines, Singapore, Thailand, and Vietnam, all had NPLs below 4 per cent of total loans in 2017 (Figure 1.16). Hence, high NPLs appear to be a South Asian phenomenon. Understandably, South Asian countries' banking sectors are caught in a myriad of problems which is reflected through high NPLs. But what is to be noted is that, in contrast to Bangladesh, a number of these countries have initiated concrete measures to tackle the situation.

Reduction of interest rate spread to boost investment

In order to rationalise interest rate for productive sectors, the central bank has recently published a circular directing banks to reduce interest rate spread from 5 per cent to 4 per cent (Bangladesh Bank, 2018). The weighted average interest rate spread of scheduled banks was 4.4 per cent in March 2018 (Figure 1.17). Bangladesh Bank has also instructed commercial banks not to change lending rate if interest rate is stated as fixed in the credit agreement with the borrower (Bangladesh Bank, 2018). It is expected that this move of the Bangladesh Bank will result in reduced lending rates, though in the past no such initiative

Figure 1.17

Weighted Average Rate of Interest of Scheduled Banks



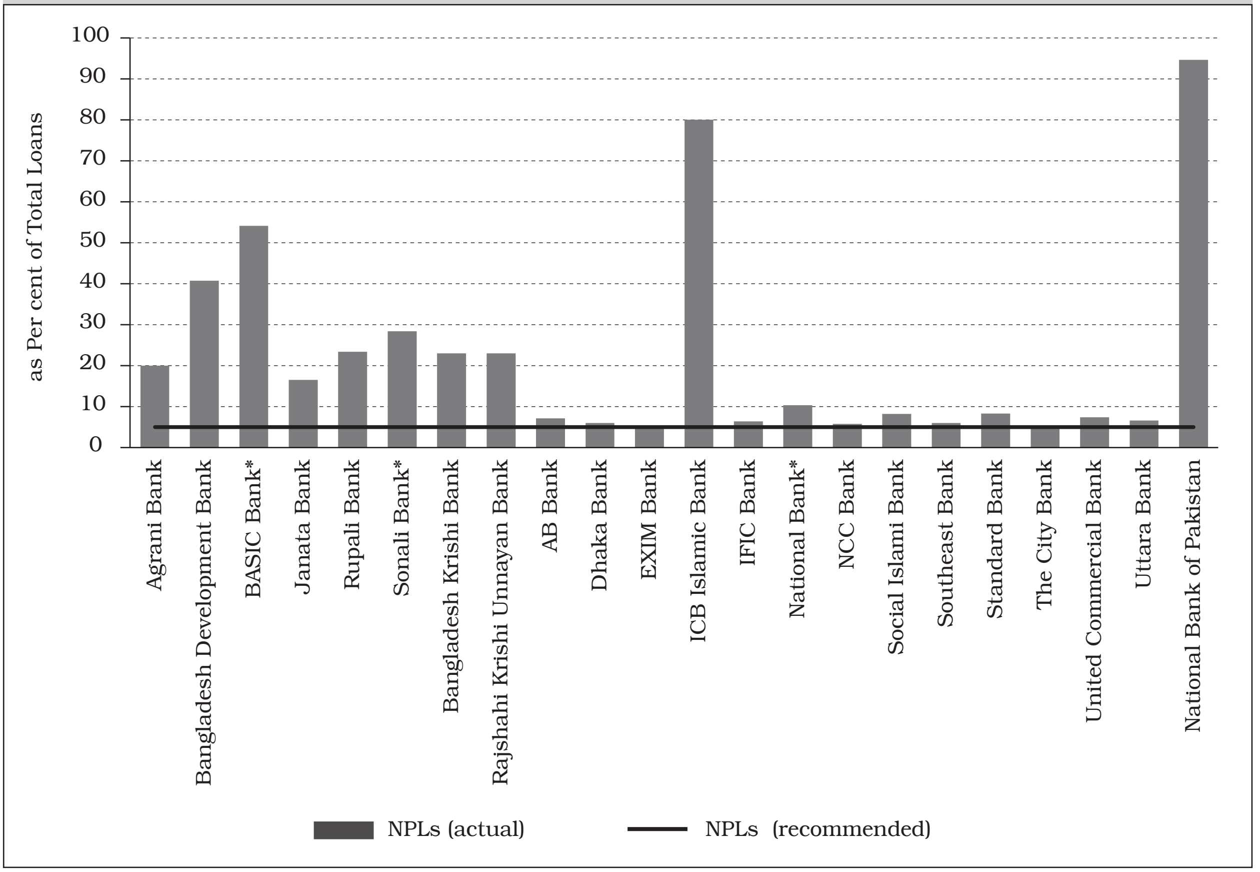
Source: Bangladesh Bank.

has been able to bring down interest rate spread to a desired level. Indeed, due to the high cost of funds, inefficiencies in the financial system and high risks of lending in Bangladesh, commercial banks tend to keep lending rates high. The desired outcome of recent directive on interest rate spread will not be realised if commercial banks attempt to reduce interest rate on deposits to make up for their profit cut due to lower lending rate. However, in order to pull depositors towards the banking system, deposit rates have to be attractive. As it is, savers are now more inclined to invest in NSD for higher return, a phenomenon which is creating high interest burden for the government. Moreover, interest rate is only one of many tools in the arsenal of monetary policy to boost investment, others being reserve requirements such as CRR and statutory liquidity ratio (SLR). Monetary policy instruments have to be combined with supportive fiscal and institutional policies and the needed infrastructure support.

BASEL III preparation of banks

BASEL III requirements stipulate that banks should maintain Common Equity Tier 1 (CET1) to Risk Weighted Assets (RWAs) ratio greater than 4.5 per cent, Liquidity Coverage Ratio (LCR) greater than 100 per cent, Net Stable Funding Ratio (NSFR) greater than 100 per cent, and Leverage Ratio greater than 3 per cent (Basel Committee on Banking Supervision, 2011, 2013, 2014, 2017). Based on the mandatory BASEL

Figure 1.18
Banks with NPL to Total Loans Ratio Greater than 5 Per cent



Source: BASEL III disclosures on risk-based capital of individual banks.
Note: *indicates data for 2016.

III disclosures of December 2017, most banks in Bangladesh were compliant with these four key BASEL III requirements (Annex Tables 1.2–1.5). However, there were notable exceptions. A number of banks such as BASIC Bank, Bangladesh Krishi Bank, Rajshahi Krishi Unnayan Bank, ICB Islamic Bank, Standard Bank, The Premier Bank, and National Bank of Pakistan are performing poorly in terms of meeting these indicators. Additionally, Sonali Bank, Al-Arafah Islamic Bank, Bangladesh Commerce Bank, National Bank, Shimanto Bank, and The Farmers Bank Limited did not disclose their BASEL III compliance status report in December 2017, as required by Bangladesh Bank regulations.

BASEL III disclosures also exposed that 22 banks had NPLs greater than 5 per cent of total loans (Figure 1.18), whilst 15 other banks did not disclose their NPL to total loan ratios. Noteworthy amongst these banks is ICB Islamic Bank. As of 31 December 2017, ICB Islamic Bank had NPL equal to 80 per cent of total loans. It may be recalled that ICB Islamic Bank was created through a central bank order, in the aftermath of the Oriental Bank crisis in 2007. Given the dismal state of the bank at present, doubts have surfaced regarding the effectiveness of the exit strategy employed by Bangladesh Bank in the case of Oriental Bank in 2007.

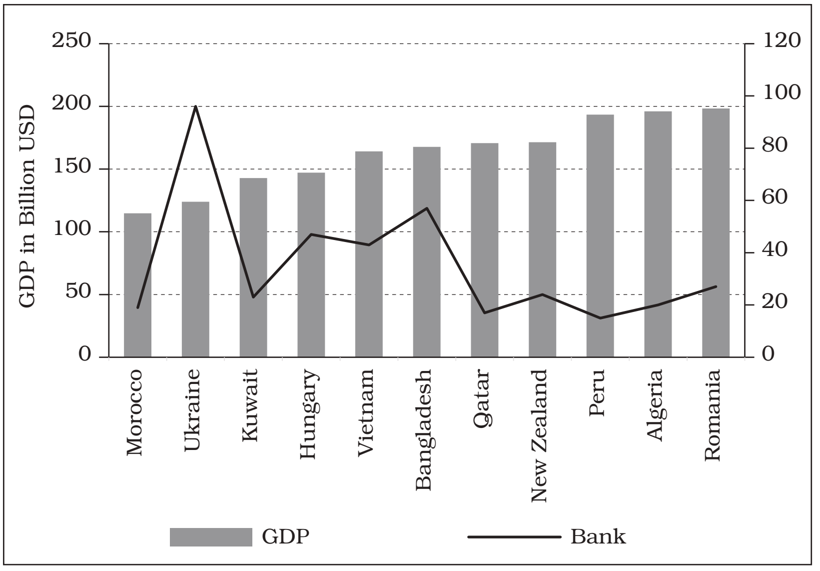
It is about time to reconsider policies towards problematic banks. In recent years, the government has often become the lender of the first resort and injected large amounts of capital into the troubled banks. However, the outcome has not been encouraging. These banks could not improve their performance despite huge re-capitalisation package offered by the government. Ironically enough, there is no moral pressure within the MoF to make sure that tax payers' money is not wasted in the name of recapitalisation of inefficient banks. Rather, MoF's sympathy has extended to the private sector banks. Directed by the MoF, the central bank reduced the minimum CRR from 6.5 per cent to 5.5 per cent bi-weekly and from 6 per cent to 5 per cent daily in April 2018. Moreover, the MoF announced that government agencies would increase their deposits of funds in PCBs from 25 per cent to 50 per cent. Both these decisions are apprehended to have negative implications. Reduced CRR may encourage banks to lend more aggressively while higher share of government funds into the private banks could result in the money going to the poor performing banks. In view of such practice of rescuing the troubled banks without any substantial outcome, taxpayers would like to have some assurance that their money is utilised in the most efficient manner.

Excessive number of banks, yet attempts to permit more

According to the Bank Company (Amendment) Act 2013, the central bank will decide to grant licenses to new commercial banks after considering the need for such banks and the overall state of the economy. Ironically, this principle is not followed in Bangladesh in case of issuing bank license. Compared to the size of the economy, the number of banks is already higher than required. More than economic justification, political pressure works for the issuance of bank licenses. And over time license for opening a new commercial bank has, in fact, become a tool for misappropriation of public money.

Figure 1.19

Number of Commercial Banks in Countries with GDP (constant, 2010 USD) between USD 114 Billion to USD 198 Billion (2016)



Source: International Monetary Fund (IMF) Financial Access Survey Data.

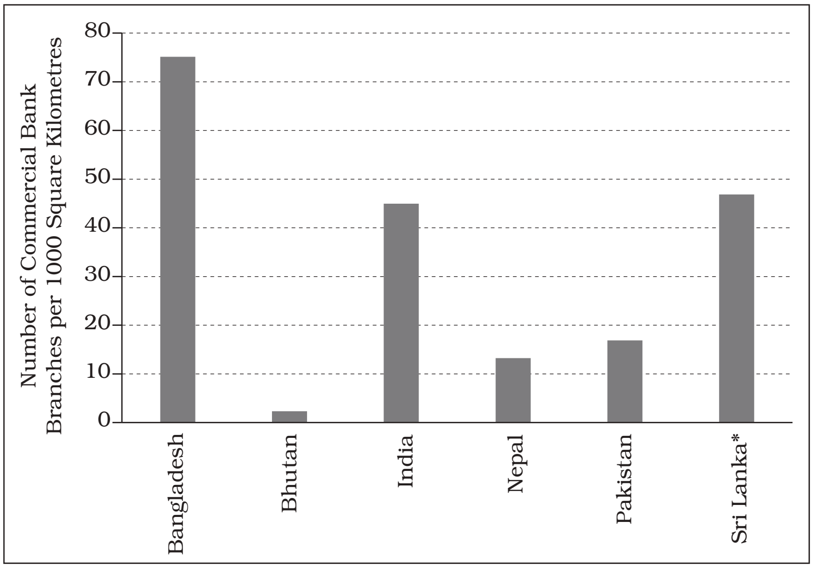
As of May 2018, Bangladesh had 57 commercial banks which constituted of 6 SCBs, 2 DFIs, 40 PCBs, and 9 FCBs. Cross-country comparison indicates that the total number of banks in Bangladesh is unusually high by global standards. For example, Mexico has only 47 commercial banks even though the GDP of Mexico in 2016 was about 7.4 times larger than that of Bangladesh in 2016 (IMF, 2018) (Annex Figure 1.2) and the total surface area of Mexico is about 13.2 times larger than that of Bangladesh (CIA, 2018). Vietnam, which had a GDP similar to that of Bangladesh in 2016, has only 43 commercial banks. In fact, amongst the cohort of countries which had a GDP between USD 114 billion to USD 198 billion in 2016, Bangladesh has the second highest number of commercial banks after Ukraine (IMF, 2018) (Figure 1.19).

Bangladesh also has a high geographic density of commercial bank branches. For example, in 2016, Bangladesh had 75 branches of commercial banks per 1000 square kilometres of land, which was the highest in the South Asia region (Figure 1.20).

Globally, if microstates that have a land area less than 1000 square kilometres are disregarded, Bangladesh has the 8th highest geographic concentration of commercial bank branches (Figure 1.21). Thus, when it

Figure 1.20

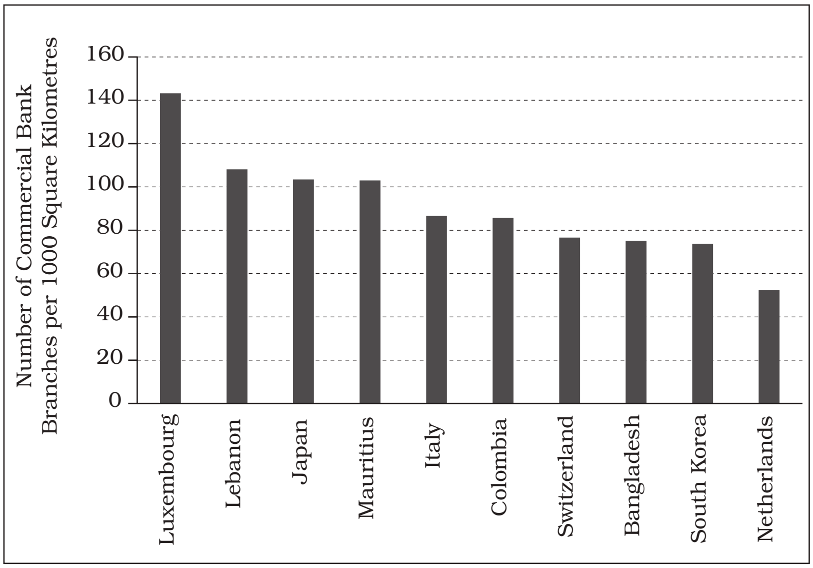
Geographic Density of Commercial Banks in South Asian Countries with GDP (constant, 2010 USD) between USD 114 Billion to USD 198 Billion (2016)



Source: International Monetary Fund (IMF) Financial Access Survey Data.
Note: * indicates data for 2015

Figure 1.21

Countries with Highest Concentration of Commercial Bank Branches (2016)



Source: International Monetary Fund (IMF) Financial Access Survey Data.

comes to the number of banks, Bangladesh falls in the same class of countries that include financial hubs such as Japan and tax havens such as Luxembourg.

Thus, the rationale of awarding new licenses to commercial banks on the premise of financial inclusion is not a justified one. The 'unbanked' population of Bangladesh comprises of two categories of people. The first category consists of poor people who live in urban slums or remote rural areas. In order to provide access to financial services to these people, mobile banking could be a superior option compared to conventional banking. In either case, these people are usually poor and uneducated, and are often not considered as potential customers by commercial banks. The second category of 'unbanked' people comprise of the population who voluntarily refrain from banking in order to conceal their financial position. Opening new commercial banks is no guarantee that this group of people will be brought within the formal financial system. Therefore, without assessment of the requirement, issuance of new licenses for more commercial banks is just another step to benefit a group of people.

1.3.4 Recommendations

Our findings reflect that inflationary pressures are building up in the economy, amidst lax control over monetary policy by the central bank. Moreover, the continued lack of discipline in the banking sector is becoming a cause for serious concern. In view of these developments, we make the following recommendations:

- The management of public food stocks requires to be revisited in order to adequately deal with agricultural supply shocks. A cost-benefit analysis may be conducted to evaluate the potential usefulness of buffer-stock schemes in stabilising food grain prices.
- A permanent Agricultural Costs and Prices Commission should be set up on an urgent basis to ensure incentive price for the producers while maintaining market stability.
- Appropriate legal and judicial reforms need to be undertaken in order to address the concerns as regards NPLs. The number of judges dealing with Money Loan Court Act 2003 and Bankruptcy Act 1997 should be increased to ensure speedy disposal of loan default cases and to reduce backlog. However, it seems that NPL in Bangladesh has become a political economy problem. So, first and foremost, political commitment from policymakers is required in order to resolve the crisis.
- Immediate action must be taken against banks that are performing poorly and are ill-prepared for BASEL III. A new exit policy for troubled banks needs to be formulated, particularly taking into cognisance the ineffectiveness of the Oriental Bank model.

New commercial banks should not be awarded licenses. Instead, mobile banking should be encouraged to promote financial inclusion.

1.4 RECENT VOLATILITY IN THE CAPITAL MARKET: TO WHAT EXTENT INSTITUTIONAL INVESTORS CONTRIBUTE TO THIS?

1.4.1 Current State of Capital Market

Despite various policies and measures undertaken over the last several years, Bangladesh's capital market has not been able to overcome the demonstrated sluggish growth. Market capitalization (as a percentage of GDP) has been on a gradual decline over the years in case of both the Dhaka Stock Exchange (DSE) and the Chittagong Stock Exchange (CSE) (Table 1.8). The number of Initial Public Offerings (IPOs) that were issued in the last several years was very few (Table 1.9). Majority of large scale local and foreign owned enterprises

Table 1.8
Market Capitalisation: DSE and CSE

Date	**Total Market Cap** ***(Billion Tk.)***	**GDP** ***(Billion Tk.)***	**Market Cap** ***Share of GDP (%)***
DSE			
30 June 2015	3247.306	15158	21.4
30 June 2016	3185.749	17328.6	18.4
29June 2017	3801	19758.2	19.2
31 May 2018	3799.5	22384.98	17.0
CSE			
30 June 2015	2593.777	15158	17.1
30 June 2016	2506.113	17328.6	14.5
29 June 2017	3123.839	19758.2	15.8
31 May 2018	3120.972	22384.98	13.9

Source: Dhaka Stock Exchange (DSE) and Chittagong Stock Exchange (CSE) Websites and Bangladesh Economic Review (2017).

have continued to remain outside the capital market. On the other hand, the high rate of over subscription (as high as 370 per cent over the size of IPOs) portrays a strong interest on the part of public shareholders.

Table 1.9
IPOs in DSE

Year	No. of Companies	IPO Size in Tk. at Offer Price *(Billion Tk.)*	Post IPO Paid-up Capital *(Billion Tk.)*	Capital as per Offer Price	RANGE (%)
2016	7	5.8	7.1	121.8	51 ~ 705
2017	7	1.6	5.9	371.6	94 ~ 621
2018 (up to April)	3	0.65	2.4	375	250 ~ 667

Source: Dhaka Stock Exchange (DSE) Website.

As part of the process of demutualisation, DSE's recent initiative to take Chinese Consortium (include Shanghai Stock Exchange) as strategic partner should be seen as a positive development. Chinese Consortium is expected to develop an SME market and assist in product diversification, and jointly with the DSE, will operate the V-Next Alliance in Bangladesh. It will assist the DSE in mapping information disclosure and investor service automation framework, developing human resources, and providing technological support with a view to develop and diversify the DSE portfolio. It is hoped that this strategic partnership with international stock exchange will also help to strengthen the infrastructural facilities of the DSE and will further enhance investors' confidence in the market.

1.4.2 Recent Volatility in the Capital Market

The recent volatility in the capital market demands closer scrutiny. The fluctuations in the capital market did not reflect macroeconomic fundamentals. Despite some fluctuations, Bangladesh's capital market has evinced bullish trend (in terms of the key indicators) in the course of calendar year 2017 (Figure 1.22A). Key indices of the DSE [i.e. Dhaka Stock Exchange Broad Index (DSEX), DSE30 and Dhaka Stock Exchange Shariah (DSES)] have registered a rise of 9-14 per cent between January 2017 and mid-May 2018, although total turnover declined by 72 per cent during the same period. Major companies in the DSE such as those related to the banking and telecommunication sectors, accounting for over 38 per cent of total market share in the DSE, have experienced a significant rise both in terms of market capitalisation and turnover during the June–December 2017 period (Figure 1.22B). During 2017, a total of seven companies have offered IPOs with an oversubscription rate of 371 per cent which was lower in 2016 (oversubscription rate was 121 per cent). The bullish trend in the market had given way to a bearish outlook since December 2017 (Figure 1.22A).

It is reckoned that volatility in the capital market originates largely from the targeting and scale of investment undertaken by the institutional investors in the capital market. Institutional investors such as private commercial banks, Investment Corporation of Bangladesh (ICB), mutual funds and brokerage houses have been important market players in the Bangladesh stock market. Traditionally, such institutional investors are able to influence market trends and behaviour and help maintain stability in the capital market. Institutional investors often take investment-related decisions based on the profile and prospect of the companies listed in the market. According to Douma, George, and Kabir (2006), market performance of listed companies tend to be positively influenced by shareholding by the institutional investors. Institutional investors, particularly foreign investors, tend to be more prominent as shareholders in large companies paying low dividends and in firms having cash holdings (Dahlquist *et al.*, 2003). However, such traditional influence gets distorted when behaviour of institutional investors in the market is irrational. Deviating from usual practice, institutional investors could also decide to invest in shares with high price volatility (Singh, Vashist, and Tripathi, 2016). Sias and Stark (1997) tested the hypothesis that trading by institutional

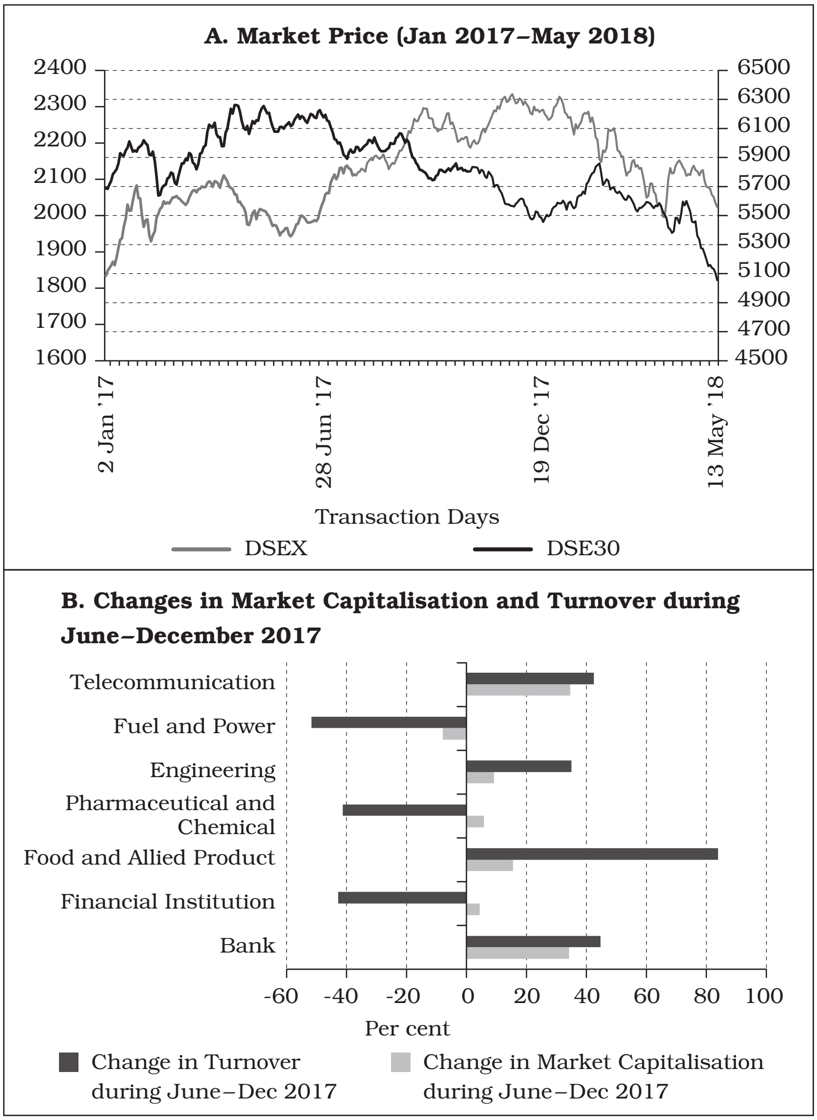


Figure 1.22
Trends in DSEX and DSE30 Indices

Source: Dhaka Stock Exchange (DSE) data.
Note: DSE30 is shown in the right vertical axis in Figure 1.22A.

investors contributes to serial correlation in daily returns. Their results show that institutional trading leads to more information disclosure and enhances the speed of price adjustment. This means when they purchase and sell in bulk, their internal decision affects the daily price of the stock. Price of shares thus influenced, leads to market volatility over the time. Bohl, Brzeszczyński, and Wilfling (2009) were of the opinion that institutions can reap benefit by misusing economies of scale in information attainment and processing. Their marginal costs of gathering and processing is relatively higher than individual traders. Institutional investors may stabilise stock prices and counter irrational behaviour on the part of individual investors' sentiments. In this backdrop, it is important to investigate to what extent institutional investors contribute to volatility in the Bangladesh stock market and what measures could be taken to address these challenges.

1.4.3 Volatility in Stock Prices at the DSE during 2016–2018

'Volatility in the capital market is a statistical measurement of the dispersion of the returns for a given security or market index'[12]. It is measured by using standard deviation from the same security: standard

[12] https://www.investopedia.com/terms/v/volatility.asp

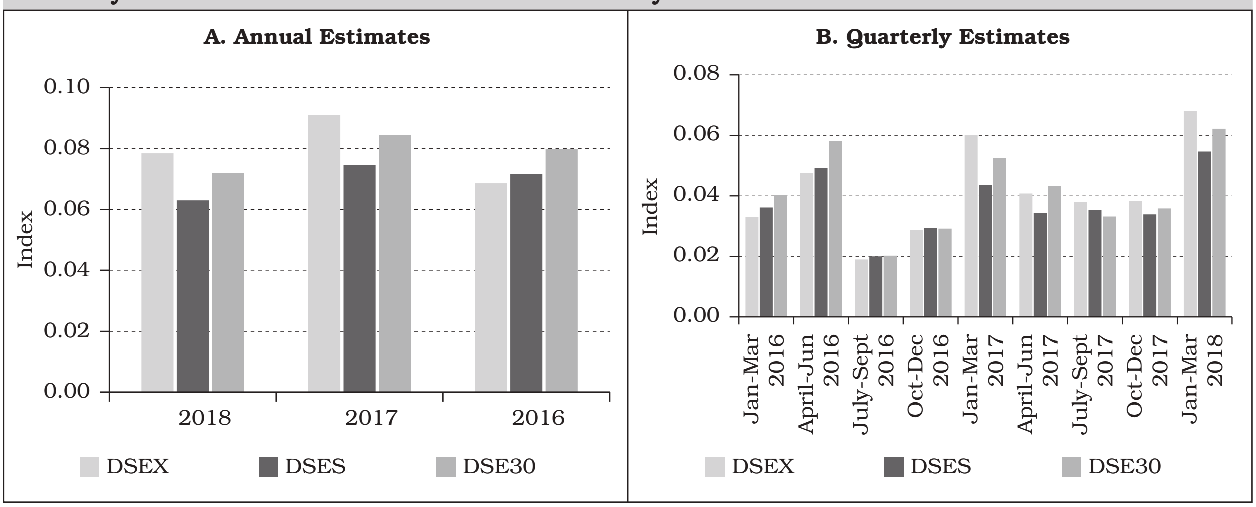
deviation of the percentage change in daily closing price multiplied by square root of trading days[13]. Generally speaking, higher volatility indicates riskier investment. The present study has made an attempt to estimate the volatility of different indices of DSE for 2016, 2017 and 2018. Figure 1.23 presents yearly and quarterly market volatilities of DSE indices. In the last three years, the stock market experienced the highest level of volatility in 2017 (volatility indices are: 0.091 for DSEX, 0.075 for DSES and 0.084 for DSE30). According to quarterly estimates, the highest level of volatility was seen in January–March 2018; prior to this the volatility reached its peak in January–March 2017. Level of volatility has fluctuated over time. Volatility for three indices did not maintain any visible pattern. However, securities under the DSEX are found to experience the highest level of volatility particularly during the periods when the market had experienced higher fluctuations during 2017 and 2018.

The volatility in the market is partly attributed to rise in investment in capital market since 2016 mainly by the institutional investors. Following the attainment of the permission granted in July 2016 to convert loans into paid-up capital of bank subsidiaries, and thereby reducing the exposure of banks' investment in the capital market within permissible limit, a number of banks had the opportunity to make additional investment in the capital market. In the backdrop of the very high amount of excess liquidity in the banking sector in 2017 (which amounted to Tk. 1.06 trillion crore at the end of June 2017), banks had made large investments in the stock market. Indeed, this had contributed, at least, in part to the bullish trend in the market.

The monetary policy for the second half of FY2017-18 had set the target of lowering the rate of credit growth (from 18.1 per cent to 16.2 per cent) with a view to tighten the money supply further. The advance-deposit ratio (ADR) was also planned to be reduced to 83.1 per cent (which was over 85 per cent) by June 2018. This compelled the banks to sell a part of their shares in order to comply with new targets set for credit growth and the ADR.[14]

Figure 1.23

Volatility Indices Based on Standard Deviation of Daily Trade

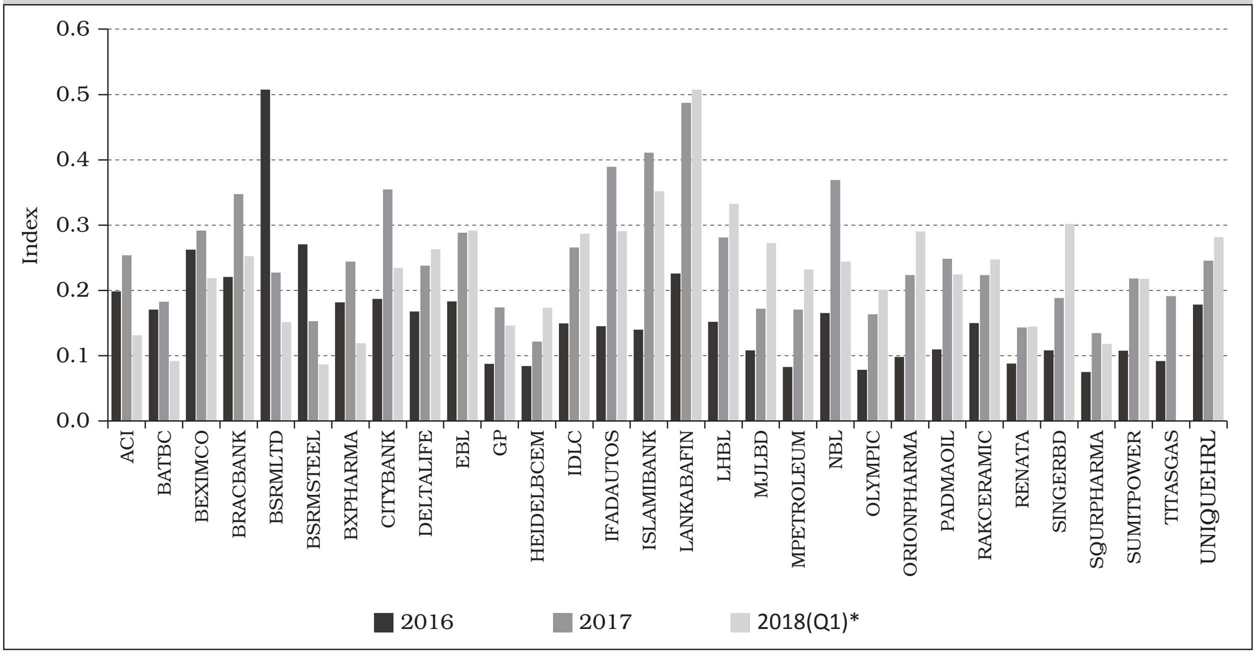


Source: Dhaka Stock Exchange (DSE) data.

[13]For details, please see, https://adamhgrimes.com/how-do-you-calculate-volatility-in-excel/

[14]Exposure limit for banks to invest in the stock market: 25 per cent of its paid-up capital, share premium, statutory reserve and retained earnings. According to reports published in national dailies, as many as 21 banks were reported to have invested in the stock market beyond their exposure limit in this period. Indeed, this was exposed in an investigation carried out by the central bank.

Figure 1.24
Volatility Indices of DSE30 (Annual)



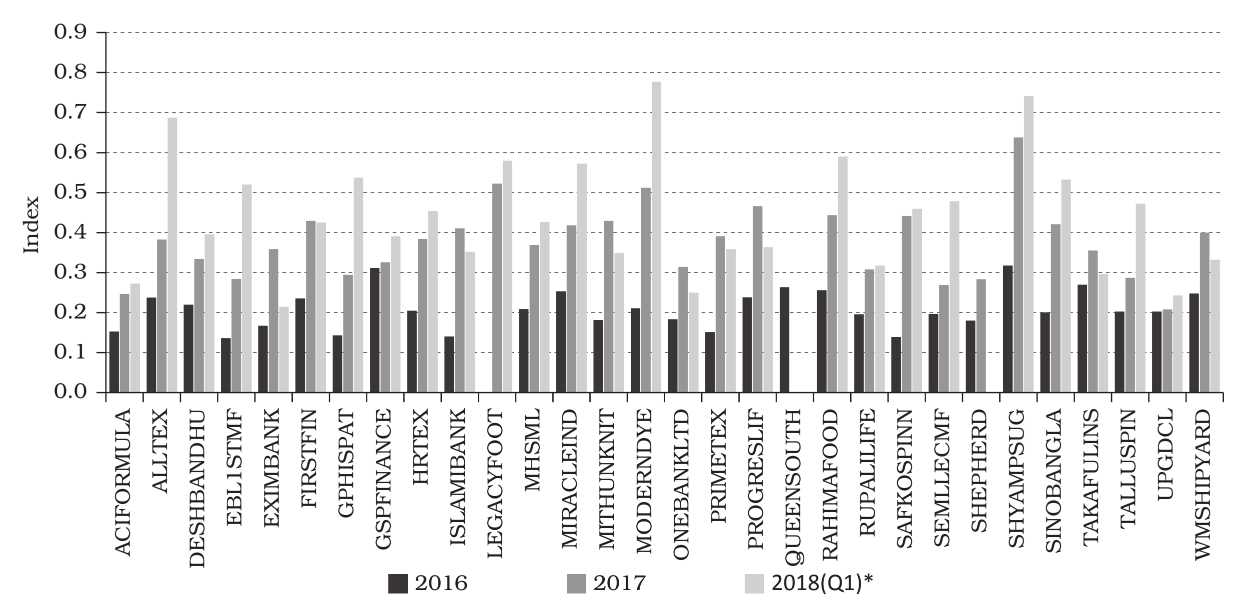
Source: Dhaka Stock Exchange (DSE) data.
Note: * First quarter (Q1).

The overall volatility (quarterly and annual) is also reflected at the company-level. A company-wise analysis of top 30 highly traded (DSE30) and low-traded 30 companies evince important insights as regards volatility. Figure 1.24 presents the volatility indices of each of the DSE30 securities during 2016, 2017 and 2018 (up to March). Among the top 30 companies, level of volatility is varied across companies for different years. However, majority of the companies have experienced higher level of volatility in 2017 while few companies had similar trends in January–March 2018. Relatively high volatility is observed for securities of stock entities such as LankaBangla Finance, Islami Bank, Ifad Autos and Lafarge Holcim Bangladesh Limited. It is important to investigate whether high volatility of some of the leading companies is related with pattern of investment undertaken by different shareholders and institutional investors.

The level of volatility in low-traded 30 companies in DSE is higher than that of DSE30 (Figure 1.25). Unlike the DSE30, the level of volatility of these low-traded companies was higher in 2016 compared to that in 2017 or 2018. Highest level of volatility was observed in securities such as Modern Dyeing, Miracle Industries and Shyampur Sugar Mills Limited, Alltex Limited and Legacy Footwear. In the backdrop of general stability in the macroeconomic situation over the corresponding period, both in the domestic and the global economy, the aforementioned volatility in the capital market has raised concern about the role played by the market players, particularly the institutional investors in Bangladesh stock market.

Figure 1.25

Volatility Indices: Low-traded 30 Companies (based on % change in share price)



Source: Dhaka Stock Exchange (DSE) data.

Note: * First quarter (Q1).

1.4.4 Institutional Investors: Role in Market Volatility

CPD has carried out an in-depth analysis of changes in shareholding by key shareholders represented by a sample set of 99 listed companies during 2016 to April 2018. The objective of this analysis is to understand how the different shareholders buy and sell their securities and to what extent this has contributed to market volatility during the 2017-18 period. CPD has collected data of 99 listed companies for five points– January 2017, June 2017, December 2017, March 2018 and April 2018. Table 1.10 presents the changes in shareholding of securities by different groups of shareholders such as sponsor directors, institutional investors and public shareholding.

During January–June 2017 period, the shareholding by major shareholders did not experience significant changes (only one company's shareholding decreased by 6 per cent). In contrast, the shareholding situation had undergone significant changes during the second half of 2017 (July–December 2017) this could have caused market volatility. This was the period, when share prices of DSE30, DSEX and DSES had experienced sharp ups and downs. The volume of shareholding has increased for shareholders in case of 26 companies; on the other hand, the shareholding had decreased in case of 25 companies. These companies include manufacturing, financial, power and energy and services. The changes in shareholding of these companies were as low as less than 1 per cent to as high as over 100 per cent. Majority of changes in shareholding was observed in case of public shareholding, both in cases of buying and selling of securities. However, both sponsor shareholders and institutional shareholders took part in selling and buying of shares during this period of volatility. Because of the sheer size of their shareholding, a limited level trading in the market was likely to cause volatility in the market. The same situation prevailed during the following quarter, i.e. January–March 2018. Shareholders of 25 companies had increased their shareholding during this period (between less than 1 per cent to more than 25 per cent). At the same time, shareholders of 36 companies had gone for selling off their shares. As before, both sponsor directors and institutional investors played a key role in this period. The situation was eased in April 2018, when changes in shareholding within these companies had slightly declined to an insignificant extent: rise in shares in 25 companies and decline in

Table 1.10

Changes in Shareholding of Securities by Different Shareholders

(no. of companies)

% Changes in Different Periods	Jan 17 and Jun 17			Jun 17 and Dec 17			Dec 17 and Mar 18			Mar 18 and Apr 18		
	Sponsor	**Inst.***	**Public**	**Sponsor**	**Inst.**	**Public**	**Sponsor**	**Inst.**	**Public**	**Sponsor**	**Inst.**	**Public**
No change	99	99	98	85	88	73	82	83	71	85	89	75
Shareholding Increased												
<1%	0	0	0	3	1	4	2	3	4	2	3	4
1-5%	0	0	0	2	1	3	2	1	5	2	1	3
5-10%	0	0	0	1	1	2	2		2	1	2	2
10-25%	0	0	0		2		1		1		1	
25-50%	0	0	0		1	2	1		1		1	2
50-100%	0	0	0									
>100%	0	0	0	1	1	1				1		
Sub-total	**0**	**0**	**0**	**7**	**7**	**12**	**8**	**4**	**13**	**6**	**8**	**11**
Shareholding Decreased												
<1%	0	0	0	2	2	5	3	1	6	3		5
1-5%	0	0	0	2	1	6	2	1	3	3	1	5
5-10%	0	0	1	2		2	3	3	2	1	1	
10-25%	0	0	0			1		1	3			2
25-50%	0	0	0	1	1	0		1		1		1
50-100%	0	0	0				1	1	1			
>100%	0	0	0					4				
Sub-total	**0**	**0**	**1**	**7**	**4**	**14**	**9**	**12**	**15**	**8**	**2**	**13**

Source: Authors' estimate.

Note: Inst. * stands for institutions.

shares in 23 companies. Overall, trading behaviour of sponsor shareholders and institutional investors during the period of uncertain situation of market volatility is partly responsible for the market behaviour. More importantly, it appears that institutional investors did not perform their expected role in stabilising the market.

Correlation of shareholding between different shareholding groups

Table 1.11 presents correlation between shareholdings of different groups for different periods. Analysis found both positive and negative correlation between shareholding groups in terms of their trading of securities in the market. A positive correlation is observed in shareholdings by sponsor shareholders and institutions as well as in case of shareholdings of sponsor shareholders and public shareholding. In contrast, there is a negative correlation between institutional investors and public shareholding for most of the period. Interestingly, the level of negative correlation rose in tandem with rise in market index (June 2017 and March 2018). The inverse relationship indicates that buying and selling behaviour of shares by institutional and public shareholders during a period of market volatility evinces that the former, despite having their role for market stability, pushed the latter in an uncertain situation. The relationship between institutional shareholding and public shareholding was found to be positive when market was less volatile (in January 2017). From this it transpires that institutional investors had contributed to volatility in the market and the sheer size of their investment in the market played a role in it.

Table 1.11
Correlation between Shareholding by Different Shareholders

Shareholding Group	January 2017	June 2017	December 2017	March 2018	April 2018
Sponsors and Institutions	0.321	0.312	0.331	0.312	0.315
Sponsors and Public Shareholding	0.458	0.467	0.460	0.467	0.460
Institutions and Public Shareholding	0.213	-0.141	-0.101	-0.141	-0.103

Source: Authors' estimate.

1.4.5 Concluding Remarks: Suggestions for Better Governance as Regards Institutional Investors

The analysis shows that market players, particularly institutional investors, did not play the expected role during the period of uncertainty in 2017 onward, which contributed, to some extent, to the volatility in the market. Moreover, their buying and selling behaviour at the time of volatility put public shareholders in an uncertain situation.

Given the importance of institutional investment in the capital market, the concept of 'responsible ownership' is gaining momentum worldwide. This concept is based on the belief that it is not enough for institutional investors to simply 'hold/sold' shares. They must also perform a proactive role to ensure good governance practices by the companies by adopting a more long-term strategy in sharing ownership. Active engagement of institutional investors is a critically important factor to strengthen overall market discipline. By bringing their voice on board and lending their reputation to gain the attention of management, they can spearhead in an ownership culture that ensures that the management gives precedence to the best interest of the company at all times.

It may be recalled in this connection that, with a view to streamline the activities of the companies listed in the capital market, the Bangladesh Securities and Exchange Commission (BSEC) issued a revised version of Corporate Governance Guidelines in 2012. The revised guidelines include many new provisions in the areas of board independence, audit committee affairs, board's declaration pertaining to corporate governance issues, certification by the Chief Executive Officer and Chief Finance Officer of the company on the truthfulness and fair presentation of the company affairs, and compliance certificate from selected professionals. However, there is very limited statement about the role of institutional investors in these guidelines, particularly with regard to transparency and safety of investment, investment policy, risk evaluation and diversification of assets etc.

Bangladesh should take lessons from other countries in order to improve the investment practices of the institutional investors in the capital market. For example, OECD has developed guidelines for 'Responsible Business Conduct for Institutional Investors' putting focus on investors' due diligence in line with the OECD Guidelines. As per these guidelines, investors will not be able to avoid their responsibilities with regard to financial and reputational risks, catering to expectations of their clients and beneficiaries as also concerning negative impact of their investment on society.

In South Africa, the guidelines for institutional investors state that managing institutions should provide information on institutional clients. Managing institutions are required to provide an updated list of all their institutional investors on a quarterly basis together with a list of: (1) all new institutional clients investing funds during the quarter; and (2) all institutional clients who terminated investment during the quarter. The lists must be provided as part of the institution's quarterly asset allocation report. Such requirements could discourage unpredictable trading practices and provide knowledge on good or bad investors and how to regulate them (South African Reserve Bank, 2018).

In Malaysia, The Institutional Investment Code (Minority Shareholder Watchdog Group, and Securities Commission Malaysia, 2014) provides guidance on effective exercise of stewardship of responsibilities towards delivery of sustainable long-term value to the institutional investors' ultimate beneficiaries or clients. The guidelines state that institutional investors should have robust policies to deal with inside information and to avoid market manipulation in their dealings. Broader ethical considerations such as policies on prevention of corruption, including anti-bribery and anti-money laundering and establishment of "Chinese wall"[15] were also to be incorporated.

Considering the global experience, BSEC should consider formulating a separate guideline for institutional investors in the capital market of Bangladesh. Such a guideline will help investors to streamline their activities in the market as well as ensure more transparency and accountability to the shareholders. The ultimate objective is to make investment behaviour of such entities more disciplined in a way that would not result in market volatility. The guideline will promote the causes of transparency, good governance and ensure safety of investors' investment. The guidelines will help institutional investors to take appropriate measures about choice of shares for investment, allocation of investment, investment policy that is approved by the shareholders every year, regular information sharing about risks, and prohibition for investment etc. Following six measures could be adopted in this connection: a) disclosure of policies regarding responsibilities; b) monitoring the performance of investee companies and periodic reporting; c) engagement with investee companies; d) implementation of policy on managing conflicts of interest; e) integrating corporate governance in investment decision-making. It is hoped that such a guideline will help instil responsible behaviour on the part of institutional investors, help reduce volatility and improve overall good governance in the capital market of Bangladesh.

1.5 EXTERNAL SECTOR BALANCES: REASONS FOR CONCERN

As FY2017-18 moved forward, the fault lines of Bangladesh's external balances exposed the vulnerabilities that has been accumulating in recent times, undermining the stability and robust performance experienced in the recent past. The emerging global economic scenario is also not reassuring. While in 2017 global economic growth (3.8 per cent) and global trade growth (4.9 per cent) were the highest since 2011, growth of key economies in 2018, and forecasts for 2019, are expected to be somewhat subdued than was originally thought. The rising fuel prices do not augur well for the world economy either.

Bangladesh's overall BoPs, for the first time since FY2010-11, continued to remain in the negative terrain throughout the third quarter of FY2017-18—result of a combination of factors, particularly in the backdrop of rising imports, and exports and remittance growth failing to catch up. Rice import has broken 32-year old record and imports related to large scale infrastructure projects have contributed to the recent surge in imports. Trade balance has come under considerable pressure with the deficit peaking at the new record high of USD 13.2 billion. This was almost twice the level of deficit in the corresponding period of FY2016-17. The rebounded export and remittances growth helped the trade deficit not to deteriorate further and the record high foreign aid disbursement provided some cushion to the overall balance. To ease the pressure on the BDT, Bangladesh Bank allowed some depreciation of the BDT against the major currencies and opted for selling more than USD 2.1 billion from the foreign exchange reserves.

1.5.1 Export Earnings

Targets and current attainments

According to the data for the first ten months (July–April) of FY2017-18, export earnings have continued to show resilience with a 6.4 per cent growth; to contrast, achieved annual growth rate for FY2016-17 was a

[15]The Chinese wall is a term describing an ethical barrier within an organisation which prevents communication that creates conflicts of interest. Source: (https://www.investopedia.com/terms/c/chinesewall.asp).

mere 1.7 per cent. However, the growth in FY2017-18, till now, remained below the strategic annual target of 8.2 per cent (Table 1.12). Indeed, to meet the annual target, export will need to post a growth of 16.7 per cent per month for the remaining two months of FY2017-18 (as compared to May and June of FY2016-17). The achieved growth has been driven by the robust performance of the readymade garment (RMG) exports which achieved a 9.4 per cent growth up to April of FY2017-18, higher than the annual target of 7.1 per cent set out for the sector.

Table 1.12
Export Target Growth and Actual Performance

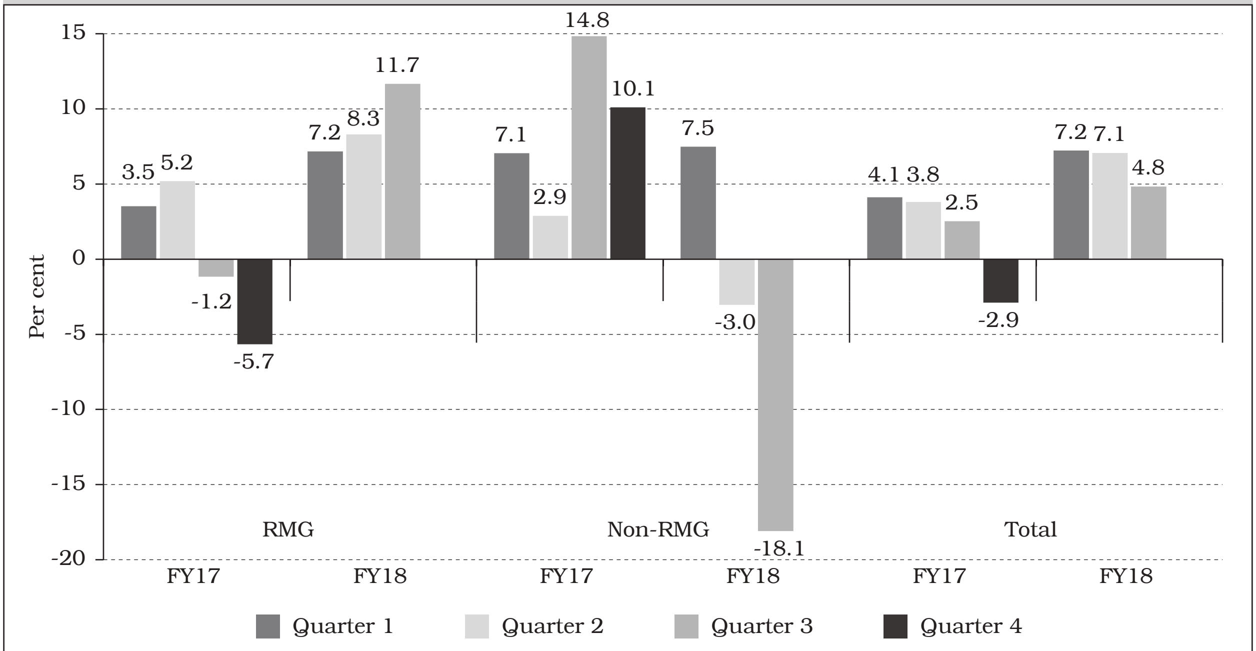
(in Per cent)

Product	Growth Target FY18	Achieved Growth Jul–Apr FY17	Achieved Growth Jul–Apr FY18	Required growth for rest of the months
RMG	7.1	2.2	9.4	-3.2
Knit	9.8	4.8	11.4	2.3
Woven	4.6	-0.1	7.4	-8.6
Non RMG	12.8	8.7	-6.2	109.6
Raw Jute	4.3	25.2	-13.8	205.1
Leather	3.2	-6.3	-27.1	349.3
Home Textiles	10.1	6.6	13.1	-4.5
Frozen Food	1.6	-3.1	2.3	-1.3
Total	**8.2**	**3.4**	**6.4**	**16.7**

Source: Export Promotion Bureau (EPB) data.

As a matter of fact, it was the performance of non-RMG products which has dragged the total export growth down. Quarter-to-quarter scrutiny of export data reveals that RMG export increased gradually from first quarter to third quarter in FY2017-18, while total export growth registered a reverse trend (Figure 1.26).

Figure 1.26
Quarter-to-Quarter Export Growth



Source: Authors' calculations from Export Promotion Bureau (EPB) data.

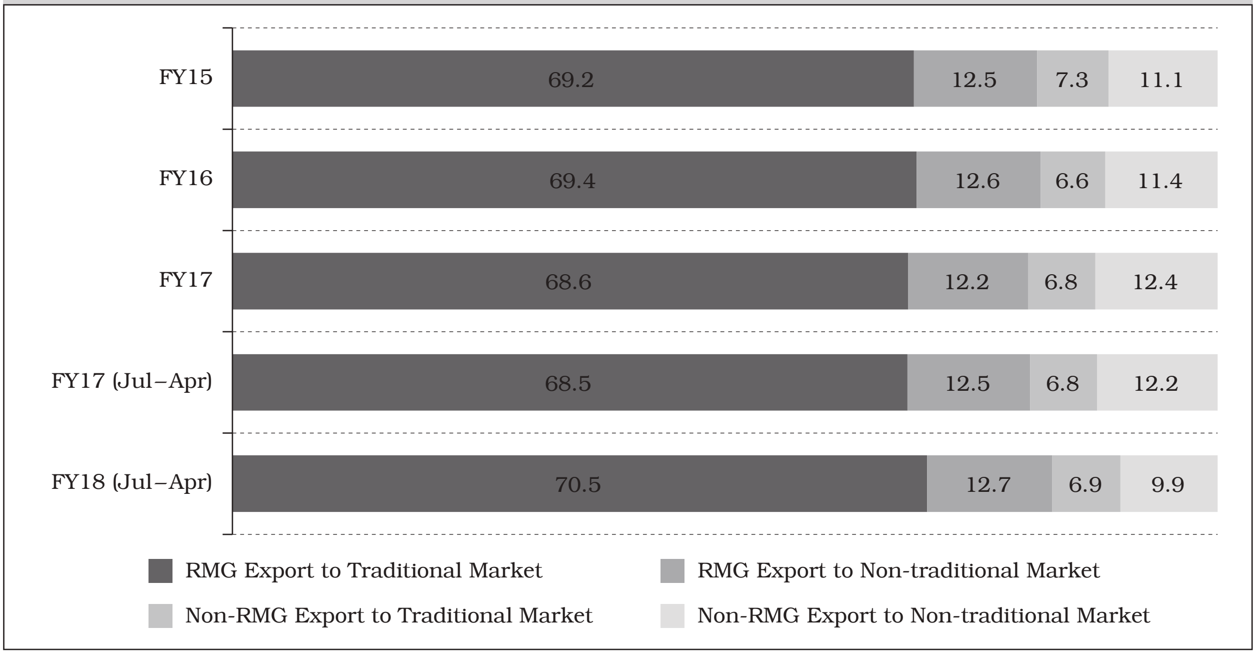
This is largely attributable to the negative growth of the non-RMG exportables during the second ((-) 3.0 per cent) and third quarters ((-) 18.1 per cent) of FY2017-18. Against the high benchmark growth in the last quarter of FY2016-17, it is unlikely that non-RMG growth will be able to recover from its performance in the last quarter of FY2017-18.

RMG-led growth with higher market concentration

In spite of the repeated initiatives towards export and market diversification, the rising concentration in recent times, on both counts, could not be arrested. Exports to the traditional markets [i.e. United States (US), European Union (EU) and Canada] have further concentrated. Consequently, growth in the traditional markets has out-performed the non-traditional market during the first ten months of FY2017-18. The share of the former has increased to 77.4 per cent (of the USD 30.4 billion of total export during July–April of FY2017-18), while the corresponding share was 76.5 per cent in FY2015 (Figure 1.27). Indeed, both RMG and non-RMG products portrayed better growth in the traditional markets when compared to non-traditional destinations. On the other hand, overall product concentration has been rising at a fast pace. RMGs comprised about 83.2 per cent of total export during July–April of FY2017-18, as against the share of 81.7 per cent in FY2014-15.

A case in point concerns the leading non-RMG export item, the leather and leather products sector. Export of this promising sector is facing a major setback. The relocation of leather industries to Savar Tannery Estate has been a prolonged process, and the consequent disruption in production and export has contributed to the emergent situation. In line with the government's mid-term policy to stimulate export of value added products, it has imposed an export ban on crust leather. Similar policy was pursued in case of jute by discouraging export of raw jute. However, policies pursued over the years have not been effective enough to stimulate a robust growth of value added products in leather and jute sectors. Lack of predictability and failure to strategically deploy the incentive mechanisms are to blame for this. Both these sectors bear the burden of the significant deficits in terms of skills and technology. Lack of adequate enforcement of

Figure 1.27
Market- and Product-Composition of Bangladesh Exports in Recent Years
(in Per cent)



Source: Authors' calculations from Export Promotion Bureau (EPB) data.

environment-friendly regulations at the production stage is an issue for the leather industry. In case of jute, its export potentials and branding as an environment friendly product have not been fully taken advantage of. Going forward, sector-specific targeted programmes and more emphasis on research and development will be needed. The recently formulated Leather Sector Export Roadmap is geared to achieve an export target of USD 5 billion by 2021. The strategic roadmap for the sector, as also for other non-RMG thrust sectors, must be implemented in all earnestness.

EU export market remained a zone of comfort

Export to the EU market maintained an 11.6 per cent growth during the first ten months of FY2017-18. Export of knit products (12.3 per cent growth) has higher growth than that of woven garments (10.7 per cent growth). Growth of non-RMG products (10.6 per cent) also matched this performance. As is expected, Bangladesh is set to graduate from the LDC status in 2024. According to current stipulation, Bangladesh will enjoy the Everything But Arms (EBA) benefits till 2027. Thereafter, it will no longer be able to reap the formidable benefits accruing from the duty free—quota free market access and the relaxed rules of origin (RoO) in place for least developed countries. Bangladesh will need to comply, and what is more important, enforce the 27 UN/ILO Conventions if it wants to apply for the Generalised System of Preferences (GSP) plus status. However, Bangladesh may have difficulty in attaining GSP plus status because of the current cap in terms of single country share in total GSP-eligible imports. Also, Brexit will call for separate negotiations with the UK.

Disquieting developments have been creeping up in the US market

According to EPB data for first ten months of FY2017-18, export growth of only 2.6 per cent was recorded for the US market. While knit garments posted a 7.8 per cent growth, the woven garments was able to record a growth of only 1.5 per cent (to recall, export of woven garments constituted the larger share in the US market). As it is, the non-RMG products experienced a negative growth over the corresponding period. Indeed, apparel imports in the US market has been experiencing a decelerating growth trend in recent years. Imposed duty on apparels and clothing accessories sector in the US was as high as 14.2 per cent (PRC, 2018a) which is the highest in 2017. Research also suggests that, Bangladesh exports faced the highest tariff of 15.2 per cent (weighted average) in the US market amongst 232 exporting countries, territories or jurisdictions, while the global average tariff of all imports to the US was only 1.4 per cent (PRC, 2018b). Bangladesh's product concentration, favouring RMGs, was also the highest compared to other major exporting countries in the US market (Table 1.13). Within RMG, concentration of the top export items from Bangladesh is also very high (as a share of total knit/woven exports). Any slowdown in the US economy makes Bangladesh's export highly susceptible in terms of growth prospects.

Table 1.13

Cross-country Comparison of Import Growth in the US Market during July–March of FY2017-18

Origin of Import	Market Size (Billion USD)	RMG	Non-RMG	Total	RMG as % Share of Total
Bangladesh	4.3	-2.0	4.4	-1.1	86.2
China	397.8	-1.6	11.9	11.1	5.4
Cambodia	2.6	9.2	50.7	19.6	68.3
India	38.1	3.4	10.1	9.5	7.2
Indonesia	15.2	-2.9	4.3	2.5	22.7
Mexico	240.8	3.7	7.9	7.8	1.1
Vietnam	35.5	8.1	9.8	9.4	25.5
Total	**1,803.0**	**1.8**	**8.4**	**8.1**	**3.5**

Source: Computed from the United States International Trade Commission (USITC) data.

Slide in Bangladesh's apparels price posed a concern

CPD, in its earlier IRBD reports has shown that, growth of export value in her major markets was primarily volume-driven. It was also observed that prices of Bangladesh's main export, RMG products, have been declining over time; these were also lower than comparator countries (CPD, 2018b). In a buyer-driven market, Bangladesh's exporters are being subjected to continuing and relentless pressure from major buying companies and retail chains. Raising product diversification and productivity are the only ways to remain competitive in the market. A country negotiating strategy to tackle the buyers' cartel needs to be crafted.

1.5.2 Import Payments

Domestic demand prompted increased import payments

Phenomenal growth is observed in terms of import payments as data for the first three quarters of FY2017-18 indicates. Indeed, import payment has risen by 24.5 per cent over the corresponding period of FY2016-17. The surge in import of rice originated from loss of crop in two successive floods and the need to replenish stocks; import of capital goods escalated to support a number of important public-sector infrastructure projects.

Import payments for the first nine months of FY2017-18, about USD 43.6 billion, almost equalled the annual import payment of FY2017. A large part of the imports, particularly for infrastructure-related projects, was underwritten by foreign aid and suppliers' credit, which eased the pressure on the reserves. Foreign exchange reserves bore the burden of paying for some of the other import payments. Bangladesh Bank allowed the BDT to depreciate to a certain extent. Depreciation of BDT reached its peak in January 2018 when it depreciated by about 5 per cent on a month-on-month basis. Indeed, US dollar gained against many of the other currencies over the corresponding period. If the BDT continues to slide against the USD, it will pose further pressure on import payments with the possibility of imported inflation.

Global commodity prices are showing upward trends

In view of US-Iran tensions, OPEC policy, demand-supply dynamics in the global market and a host of other reasons, petroleum prices have started to rise in recent times (Table 1.14). Increased global commodity prices will likely to put additional pressure on import payments in the coming months. This is particularly so because prices of many other commodities hinges on price of fuels in the international markets.

As Bangladesh's leading export items are experiencing a price fall in major destination countries and global prices of raw materials and other commodities are on the rise, Bangladesh's terms of trade deteriorated further in March 2018 compared to March 2017 (Table 1.15).

Table 1.14

Month-on-Month Growth of Global Commodity Prices in April 2018

(in Per cent)

Commodity	Change
Increase	
Crude oil (Brent)	35.2
Natural gas	31.3
Soybean oil	4.9
Rice (Thai, Vietnamese)	18.2—20.0

(Table 1.14 contd.)

(Table 1.14 contd.)

Commodity	Change
Cotton (index)	6.0
Fertilisers (DAP, TSP, Urea)	8.9—14.0
Aluminium	17.4
Decrease	
Palm oil	-2.8
Sugar	-26.9

Source: World Bank Commodity Price Data (The Pink Sheet).

Table 1.15

Changes in Terms of Trade (in view of RMG price in EU): March 2018 vs March 2017

Reference Commodity Price	Price Ratio: Knit (61)	Price Ratio: Woven (62)
Crude oil	1.38	1.41
Rice	1.25	1.28
Fertiliser (index)	1.08	1.10
Cotton (index)	1.15	1.17

Source: World Bank Commodity Price Data (The Pink Sheet) and EuroStat.

Pressure on import payments may ease in coming months as rice imports decline

An additional amount of about USD 1.6 billion payments made against import of food grains during the first three quarters of FY2017-18 may not be required in FY2018-19, releasing some of the pressure. One may recall, due to two successive floods in 2017, public food stock went record low in August 2017. The government had reduced the import duty on rice which encouraged large purchases by private dealers/ millers. As of 22 May 2018, about 38.7 lakh metric ton (MT) of rice has been imported; consequently, government rice stock has risen to 11.61 lakh MT. Since the *boro* rice production this year is expected to exceed its target production of 190 lakh MT, there may not be a reason to repeat the high import of foodgrains in FY2018-19. Indeed, the government should consider reimposing the import duty on rice in order to safeguarding farmers' interests. Whether there is any capital flight by the unscrupulous traders taking advantage of zero-duty on rice imports, should warrant close scrutiny.

Energy demand will be high in FY2018-19

To meet the growing energy demands, the government has opted to import significant amount of LNG—Bangladesh has emerged as the 41st LNG importing country in the world. The government has signed deals with Qatar's RasGas and Oman's Oman Trading International to import a total of 3.5 million MT of LNG per year. The first ship has already come to Maheshkhali with 133,000 cubic metre (cu m.) of LNG. It is to be expected that high import of LNG will raise import payments in the upcoming years.

Spending on account of mega-projects will drive imports

The government has already announced a separate budget to the tune of Tk. 30 thousand crore to be allocated for implementation of the fast-track projects under the ADP. All these projects have project aid components. It is assumed that procurement for these projects would be pre-financed from foreign aid (e.g. Bangladesh Atomic Energy Commission (BAEC) has opened import letter of credit (L/C) worth USD 11.4 billion to procure capital goods for Rooppur Nuclear Power Plant project, which will be financed from the Russian Credit). Bangladesh has already received about USD 3.4 billion worth of foreign aid to finance the aforesaid projects. However, these mega-projects also necessitate import of associated items which will have to be underwritten through general import payments, putting additional pressure on foreign currency reserves.

Repayment of foreign loans will put further pressure on reserves

As is known, Bangladesh Bank allowed private borrowers to take foreign loans from offshore commercial banks. Many of the loans will mature in this and coming years, putting pressure on foreign exchange demand.

L/C payments and openings also are indicative of the pressure on foreign exchanges

As of July–March of FY2017-18, import L/C opening stood at USD 56 billion, which was USD 35.7 billion during the matched months of FY2016-17. Till now, USD 38.1 billion worth of L/Cs have been settled. It is expected that, another USD 15-20 billion of L/Cs will be settled over the coming months. However, about USD 13 billion worth L/C remained open under 'Others' category, which do not include food, essential goods, capital goods, industrial raw materials or petroleum products. There is a need to closely examine and monitor which are these items. All this indicate a rising pressure on foreign exchange and reserves.

1.5.3 Migration and Remittances

After two consecutive years of decline, remittance flows to LMICs in 2017 has rebounded with the amount increasing by an estimated 8.5 per cent to reach USD 466 billion (World Bank, 2018). Bangladesh has also benefitted from this rising trend. Recovering from the negative growth of the last two consecutive years, remittance inflow to Bangladesh has recorded an impressive 17.7 per cent growth during July–April of FY2017-18. The Gulf Cooperation Council (GCC) countries accounted for 56.7 per cent of the USD 12.1 billion remittance inflows in July–April of FY2017-18. Saudi Arabia accounted for 17.3 per cent of the total inflows, followed by 15.9 per cent from the UAE and about 13.2 per cent from the USA. The recovery has been achieved, thanks to a number of exogenous (such as healthy economic performance in developed countries, rise in oil prices) and endogenous factors (interventions by the Bangladesh Bank coming up with stringent regulations concerning mobile banking and allowing devaluation of local currency). Indeed, as Figure 1.28 shows, all key sending countries have posted positive growth in remittances in January–March quarter of FY2017-18.

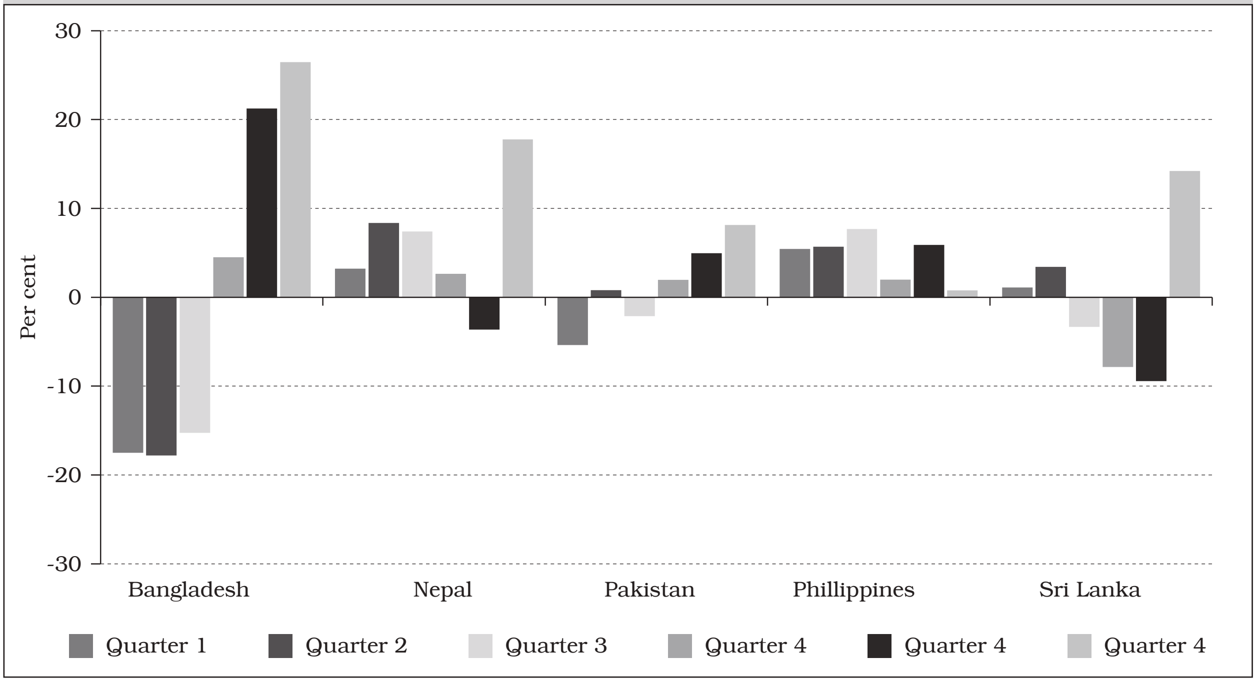
It is to be noted, that while robust remittance flows did help to narrow down the current account deficit, coming on the heels of depressed growth of the past year, the level of remittance flow in FY2017-18 will still likely to be below the peak level of USD 15.3 billion reached in FY2014-15.

In recent years, the number of migrants from Bangladesh has risen quite significantly. Between 2013 and 2017, about 23.2 lakh people have joined the migrant labour force. In the July–April 2017 period, 7.5 lakh people left Bangladesh for overseas job market; the corresponding figure for FY2017-18 was 7.6 lakh. Over the past three years 3.43 lakh female workers went, mostly to middle-east countries, as migrant workers.

The growth was significant on account of Saudi Arabia opening its market in 2015 for Bangladeshi migrants. This raised average monthly out-migration from about 35,520 in 2014 to about 84,000 in 2017. Recently, Saudi government stopped recruitment of foreign workers in 12 categories of jobs. Majority of the low-skilled Bangladeshi migrant workers fall into these categories. As a result, out-migration to Saudi Arabia has drastically fallen, by 50 per cent, during the first four months of 2018. Indeed, the number of outgoing migrants decreased in all GCC countries in first four months of 2018, while the total out-migration growth was recorded at about (-) 25.8 per cent. Malaysia is the only major country where migrant outflow remained

Figure 1.28

Quarter-over-Quarter Cross-Country Comparison of Remittances Growth



Source: Bangladesh Bank (www.bb.org.bd), Nepal Rastra Bank (www.nrb.org.np), State Bank of Pakistan (www.sbp.org.pk), The Bangko Sentral ng Pilipinas (www.bsp.gov.ph), Central Bank of Sri Lanka (www.cbsl.gov.lk). [accessed on 25 May 2018]

consistent and high. The current deceleration in the flow of migrant workers will likely have a negative impact on remittance flows, with lagged impacts.

1.5.4 Balance of Payments (BoPs)

In the face of high import payments, the negative trade balance stood at a new high of USD (-) 13.2 billion, according to the end of third quarter (Q3) data for FY2017-18 (Table 1.16). The current account balance, supported by high remittance growth, was USD (-) 7.1 billion at the end of Q3, 2018. At the same time,

Table 1.16

Trends in Bangladesh's BoPs

Item	FY11	FY15	FY16	FY17	FY18
	July–March				
Trade balance	-5,570	-4,673	-4,792	-7,039	-13,202
Export f.o.b. (including EPZ)	*16266*	*22,558*	*24,353*	*25,330*	*27,098*
Import f.o.b (including EPZ)	*21836*	*27,231*	*29,145*	*32,369*	*40,300*
Current Account Balance	***689***	***2,434***	***3,355***	***-1,372***	***-7,083***
Capital account	***342***	***344***	***364***	***252***	***229***
Financial account	***-1,298***	***808***	***761***	***3,139***	***6,055***
Foreign direct investment (net)	574	1,342	1,097	1,417	1,376
Portfolio investment (net)	-43	360	67	312	320
Errors and omissions	***-262***	***-699***	***-947***	***579***	***-609***
Overall balance	**-529**	**2,887**	**3,533**	**2,598**	**-1,408**

Source: Bangladesh Bank data.

BoP deficit stood at USD 1.4 billion, lowest since FY2010-11. This overall balance position was supported by financial and capital account surplus. Net medium and long-term (MLT) loans and net FDI respectively accounted for 61.5 per cent and 22.7 per cent of the financial account, with foreign portfolio investment remaining at very low levels.

Throughout the first three quarters of FY2017-18 foreign exchange reserves hovered around USD 33 billion, currently covering 5.2 months of imports. The days of the rapid growth in foreign reserves, rising from 7.5 billion in FY2008-09 to 33.4 billion in June FY2016-17. It is highly likely that the pressure on reserves will continue in the coming years.

Bangladesh's external sector performance has been quite robust in the recent past serving as a key pillar of its macroeconomic stability. However, as the preceding analysis indicates, it has now come under considerable pressure on several counts and the results in terms of the dynamics of the various balances bear this out. Export and remittance earnings are likely not be able to account for the expected rise in imports, with consequent impact on current account deficit. In the absence of rising flow of FDI and greater use of aid in the pipeline, the erstwhile comfortable scenario in terms of external balances are likely to be a scene of only the past. With some of the foreign currency loans incurred by the private sector, the pressure on foreign currency reserves is likely to rise further. The government is already resorting to selling dollars to keep BDT from sliding further. The likelihood of further depreciation of BDT with consequent implications in terms of imported inflation cannot be excluded. Indeed, the emerging near-term external sector scenario should be a matter of concern for the policymakers. There is a need for a serious analysis as regards how the scenario could develop and the likely implications. Energetic steps will then need to be taken to address the concern.

1.6 CONCLUDING REMARKS

As the FY2017-18 draws to its finishing line, the economy of Bangladesh leaves several marks on its performance. First, the GDP growth as estimated by the Bangladesh Bureau of Statistics (BBS), continues to be strong, setting new heights compared to other LDCs. Indeed, in recent years, high growth has contributed to higher per capita income and lower poverty rate (thought the pace of poverty reduction is slowing down). Second, growth rates of both export earnings and remittance inflow have accelerated in FY2017-18 (CPD, 2018a, 2018b). If such growth rates continue, they may contribute to restrain the building pressure on BoP to some extent. Third, though increasing, average annual inflation rate remains slightly below the target set by the MPS for the second half of FY2017-18.

This positive performance, however, has been overshadowed by a number of concerns. First, accelerated GDP growth has not been translated into desired outcome (CPD, 2018a). Indeed, employment elasticity of growth has declined significantly. Moreover, employment has not led to adequate income for decent living. Thus, benefits of high growth have not reached all citizens of the country equally. Second, the fiscal framework continues to be weak with mismatch between target and actual accomplishments. Revenue mobilisation for FY2017-18 has lagged behind the target of 7FYP, primarily due to shortfall in income tax, VAT and SD collection. At the current trend of revenue mobilisation, achievement of 7FYP target for revenue mobilisation by FY2019-20 is highly unlikely. ADP implementation also could not make any breakthrough in FY2017-18. Delays, cost overrun and institutional weakness are causing low ADP implementation. Third, the external sector has come under pressure in the face of high import payments, which had resulted in a large current account deficit. Higher growth rates of export and remittance could not account for import growth, resulting in negative BoP. Fourth, inflationary pressure has been building gradually in recent months, mainly due to higher food inflation. Inflationary pressure may continue in the coming months. This may lead to income erosion of the poor. Fifth, the banking sector and capital market have not shown any prospect of positive changes in the near future. While the banking sector is plagued with a large amount of NPL and poor compliance, the capital market has been volatile with very few new investments.

In the above context, policymakers ought to focus on two broad areas in the coming years: (i) consolidation of macroeconomic stability, and (ii) reducing inequality (consumption, income and asset) and creating decent jobs. While the importance of higher economic growth cannot be undermined, the emphasis should be more on how to distribute the benefits of growth across regions and marginalised communities. In the first and second readings of the IRBD, (chapters 3 and 2 in this publication) CPD had emphasised on the quality of the experienced higher economic growth. This has become imperative for policymakers in view of the government's commitment towards implementation of SDGs. The country is also at a crossroad in accomplishing its journey from an LDC towards a developing country. Achievements of medium to long-term development goals will critically hinge on fulfilling the short-term targets. As the country is set for a national election during FY2018-19, economic policies will have to be carefully crafted to avoid the traditional ramifications of economic management in an election year. In this context, CPD reiterates on following a restrained macroeconomic management. More specifically, CPD puts forward a few policy recommendations which deserve immediate attention of the policymakers.

- A comprehensive, detailed and realistic revenue collection plan should be designed to fulfil high revenue generation target. Such a plan should include broadening tax base, curtailment of tax evasion and tax avoidance, and checking IFFs from the country.
- A demonstrated mechanism for implementation of fast track project should be devised. Examination of the issue of over capitalisation of projects, particularly the large ones, is also necessary to save resources. Allocations for the social sectors should not be compromised while emphasising on physical infrastructure.
- Maintaining a balance between producers' and consumers' price is a tricky one. However, given the rising inequality in the rural areas and high food inflation, CPD reiterates the need for forming an Agriculture Costs and Prices Commission (ACPC) which will provide guidelines to ensure food security, recommend incentive structure for the produces and provide guidelines for price signals.
- Supporting labour-intensive, domestic market-oriented and local resource-based manufacturing and agro-based industry should be given priority by the policymakers for more decent job creation. Given the weakness in the external sector, this policy emphasis becomes more pertinent.
- Bangladesh Bank needs to remain vigilant as regards growing pressure on BoP which may result in further dents in foreign exchange reserve along with some depreciation of BDT. It will be critical for the central bank to maintain stability in the foreign exchange market to avoid any speculation and short-term volatility.
- Announcement of the much-awaited Banking Commission by the Finance Minister is a welcome move. This commission should conduct a transparency exercise of the state of the banking sector, the reasons behind weaknesses of the sector and make recommendations to overcome the crisis of the banking sector.
- BSEC should formulate a separate guideline for institutional investors in the capital market of Bangladesh. A guideline will promote the causes of transparency and ensure safety of investors' investment by taking appropriate measures about choice of shares for investment, allocation of investment, investment policy that is approved by the shareholders every year, regular information sharing about risks, and prohibition for investment that will ensure good governance and regulation.
- Given that there will be less appetite for undertaking any reform measure during the election year, the government should not lose sight of the unfinished reform agenda for various sectors. Some of these include setting up of Public Expenditure Review Commission, Local Government (Finance) Commission, Agriculture Costs and Prices Commission, Independent Financial Sector Reform Commission and Independent Statistical Commission.

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ANNEXES

Annex Tables

Annex Table 1.1
Number of New Projects vs. Reduction in RADP Allocation

Fiscal Year	ADP	RADP	Number of New Projects	Reduction
FY09	904	1,040	136	2,600
FY10	886	1,062	176	2,000
FY11	916	1,185	269	2,620
FY12	1,039	1,231	192	4,920
FY13	1,037	1,205	168	2,634
FY14	1,046	1,254	208	5,872
FY15	1,034	1,204	170	5,315
FY16	999	1,315	316	6,000
FY17	1,123	1,415	292	0
FY18	1,192	1,511	319	7,550

Source: Authors' compilation from Bangladesh Planning Commission.

Annex Table 1.2
Number of Projects with Time Extension: RADP Compared to ADP FY2017-18

Sector	Number of Projects in ADP	Projects with Time Extension in RADP	Proportion (%) of Projects with Time Extension
Rural Development and Institutions	125	24	19.2
Power	82	19	23.2
Transport	171	29	17.0
Education and Religious Affairs	112	35	31.3
Health, Nutrition, Population and Family Welfare	55	19	34.5

Source: Authors' compilation from Bangladesh Planning Commission.

Annex Table 1.3
Implementation Status of 'Fast Track' Projects

Project Name	Project Cost in Crore Tk. (Financial progress[1], in per cent)	Allocation in FY18 ADP (Crore Tk.)	Start and End Dates	Source of Fund	Comment
Projects in Implementation Phase					
Padma Multipurpose Bridge (PMB)	28,793 (53.6)	5,524	Jan 2009-Dec 2018	GoB	Cost of the project has been revised twice.
Dhaka Mass Rapid Transit Development Project (DMRTDP)	21,985 (14.9)	3,426	Jul 2012-Jun 2024	GoB, JICA	JICA will provide 75 per cent of the total cost. Currently at the execution phase, following completion of all planning-related activities.

(Annex Table 1.3 contd.)

(Annex Table 1.3 contd.)

Project Name	Project Cost in Crore Tk. (Financial progress[1], in per cent)	Allocation in FY18 ADP (Crore Tk.)	Start and End Dates	Source of Fund	Comment
Matarbari 2x600 MW Ultra-Super Critical Coal-Fired Power Project (MUSCCFPP)	35,984 (14.0)	2,220	Jul 2014-Jun 2023	GoB, JICA	JICA will provide 43 per cent of the total project cost. This is one of the costliest power projects of its size in the world that will come with its own deep sea port to facilitate import of coal.
2×660 MW Moitree Super Thermal Power Project (MSTPP) in Rampal	16,000 (15.9)	1	Jul 2009-Jun 2020.	GoB, India	On 29 January 2012, Bangladesh Power Development Board (BPDB) signed an agreement with National Thermal Power Corporation (NTPC) to build the 1,320-megawatt Rampal plant. The PDB and the NTPC will implement the USD 1.5 billion project on a 50:50 equity basis.
2x1200 MW Rooppur Nuclear Power Plant (RNPP) -	Phase-I 5,087 (95.8)	122	Mar 2013-Jun 2018	GoB, Russia	Russia has provided Tk. 4,000 crore as project aid to complete the first phase.
	Main Project 113,093 (8.1)	10,187	Jul 2016-Dec 2025	GoB, Russia	Contract has been signed worth USD 11.38 billion with Russia in July 2016 to construct the mail power plant.
Padma Bridge Rail Link	34,989 (6.3)	7,610	Jan 2016-Jun 2022	GoB, China	PMB project. About 29 per cent of the total project cost will come from the state exchequer while 71 per cent will come as project assistance from the Chinese government.
Construction of Single Line Dual Gauge Track from Dohazari-Ramu-Cox's Bazar and Ramu to Ghundum near Myanmar Border	18,034 (16.4)	1,561	Jul 2010-Jun 2022	GoB, ADB, China	Included as a 'fast track' project when it was upgraded from meter gauge to a dual gauge. Because this project cost has jumped to Tk. 18,034.48 crore which was previously estimated to be Tk. 1,852.35 crore. Asian Development Bank (ADB) will underwrite 73 per cent of the total project cost.
Deep sea port at Payra	3,351 (20.9)	400	Jul 2015-Jun 2020.	GoB	Initial activity commenced in 2013. The Payra Port Authority was constituted in August 2013. Both time and cost escalated for this project.
LNG terminal	Build-own-operate and transfer (BOOT)	-	Deal signed in Jan 2015. Expected to be completed by 2020.	GoB, IFC	In January 2015, Petrobangla signed a contract with Excelerate Energy-Astra Consortium to build the terminal. Excelerate was assigned to build the floating, storage and regasification unit (FSRU) under build-own-operate and transfer (BOOT) basis. It was to charge USD 0.5 per MCF (1,000 cubic feet) against its service. The project was initially set for completion in 2013. In December 2016, Excelerate Energy announced it has completed the required

(Annex Table 1.3 contd.)

(Annex Table 1.3 contd.)

Project Name	Project Cost in Crore Tk. (Financial progress[1], in per cent)	Allocation in FY18 ADP (Crore Tk.)	Start and End Dates	Source of Fund	Comment
					geotechnical and geophysical studies for the Maheshkhali LNG terminal, with a target of delivering the first LNG terminal in early 2018.
Deep sea port in Sonadia	55,000	-	NA	NA	Recently it has been announced following an ECNEC meeting that there will be no deep-sea port in Sonadia.

Source: Annual Development Programme (ADP) for FY2017-18, websites of the relevant government agencies.

Note: 1/ Progress was reported up to April 2018 for all the projects.

2/ '-' refers to no allocation while 'NA' refers to not applicable.

Annex Table 1.4

Implementation Status of 20 Priority Projects under ADP for FY2017-18

Project Name	Project Cost	Implementation Rate Jul–Feb FY18	Cumulative Progress up to February 2018	Maximum Possible Completion by FY18	End Date
Transportation					
Padma Multipurpose Bridge project	28,793	18.6	52.2	65.0	31/12/18
SASEC Road Connectivity: Improvement of Joydebpur-Chandra-Tangail-Elenga Road (N-4) to 4-Lane Highway	3,365	57.5	60.4	71.8	30/03/18
SASEC Road Connecting Project-II: Improvement of Highway Four Lane Road of Alenga-Hatikamrul-Rangpur	11,899	0.1	0.0	5.0	31/08/21
Four Laning of Dhaka-Khulna Highway (N-5) from Jatrabari Intersection to Maoa (Including Ikuria-Babubazar Link Road) and Pachchar-Bhanga Portion with separate lane for slow moving vehicles	6,852	50.0	67.1	89.6	30/06/20
Greater Dhaka Sustainable Urban Transport Project (BRT Gazipur-Airport)	2,040	17.6	18.8	23.7	31/12/18
Support to Dhaka Elevated Expressway PPP Project	3,217	8.8	44.7	48.1	31/12/20
Construction of Multilane Road Tunnel under River Karnaphuli	8,447	74.9	19.9	28.4	30/06/20
Dhaka-Chittagong Railway Development Project	3,190	41.6	90.0	91.6	30/06/17
Construction of Bangabandhu Railway Bridge	9,734	57.6	1.1	1.7	31/12/23
Power					
Ashuganj 450MW CCPP (North)*	3,400	91.7	78.4	79.0	31/12/17
Construction of Bibiana-3, 400 MW Combined Cycle Power Plant	3,358	105.2	54.5	55.2	30/06/19

(Annex Table 1.4 contd.)

(Annex Table 1.4 contd.)

Project Name	Project Cost	Implementation Rate Jul–Feb FY18	Cumulative Progress up to February 2018	Maximum Possible Completion by FY18	End Date
Construction of Ghorashal 365 MW* Combined Cycle Power Plant	2,512	9.3	67.7	93.1	30/06/18
Siddhirganj 335 MW Power Plant	4,239	18.0	59.4	58.9	31/12/18
Shikalbaha Duel Fuel 225 MW Combined Cycle Power Plant	2,008	20.9	63.9	82.6	30/06/18
Bheramara Combined Cycle Plant (360 MW) Development*	4,140	50.1	116.6	87.4	31/12/17
Providing Electricity Connection to 15 lakh clients through Rural Electricity extension	6,426	76.7	47.5	53.4	31/12/18
Industry					
Shahjalal Fertilizer Project	4,874	34.7	96.7	98.3	30/06/18
Tannery Industrial Estate, Dhaka (Third Revised)	1,079	4.6	62.8	71.1	30/06/17
Oil, Gas and Mineral Resources					
Establishment of Gas Compressor Station in Ashuganj and Elenga*	1,431	11.5	68.2	82.9	30/06/18
Rural Development and Institutions					
Construction of 1490m long Pre-stressed Concrete Grider Bridge over Teesta River at Pachpir Bazar-Chilmari Upazila HQ Road of Sundargonj Upazila under Gaibandha District Project	76	6.4	2.3	4.2	30/06/19

Source: Authors' calculations from the Implementation, Monitoring and Evaluation Division (IMED) data.
Note: * Progress up to November 2017.

Annex Table 1.5
Allocation of Safety Net Programmes

(in Crore Taka)

Programme	Budget vs. NSSS target						Projection vs. Target		
	FY16	NSSS FY16	FY17	NSSS FY17	FY18	NSSS FY18	Proposed FY19	MTBF FY19	NSSS FY19
Old age allowance	1,440	2,010	1,890	3,530	2,100	3,740	2,400	2,604	3,960
Child school (primary and secondary) stipend	1,159	3,870	1,640	6,830	464	7,240	N/A	2,002	8,140
Allowances for the widowed, deserted and destitute women	534	1,150	690	2,040	759	2,160	840	941	2,420
Programmes for people with disabilities	360	1,080	540	1,910	693	2,020	781	859	2,270

Source: Authors' calculations from GED (2015) and MoF (2017).

Annex Table 1.6
Coverage of the Beneficiaries

(Persons in lakh)

Programme	Budget				Proposal	Projection
	FY16	FY17	FY18	NSSS FY18	FY19	MTBF FY19
Old age allowance	30.0	31.5	35.0	55.0	40.0	38.5
Child school (primary and Secondary) stipend	88.0	140.0	37.4	179.0	N/A	149.5
Allowances for the widowed, deserted and destitute women	11.0	11.5	12.7	32.0	14.0	13.9
Programmes for people with disabilities	6.0	7.5	8.3	10.0	9.3	9.0

Source: Authors' calculations from GED (2015) and MoF (2017).

Annex Table 1.7
Inflation Targets of Central Banks in 2018

(in Per cent)

Country	Name of Central Bank	Target in 2018	Actual in 2017
Albania	Bank of Albania	3.00 +/-1	3.00 +/-1
Argentina	Central Bank of Argentina	15.00 (8)	12-17 (8)
Armenia	Central Bank of Armenia	4.00 +/-1.5	4.00 +/-1.5
Australia	Reserve Bank of Australia	2.00 - 3.00	2.00% - 3.00
Azerbaijan	Central Bank of the Republic of Azerbaijan	6.00-8.00	monetary base
Bangladesh	Bangladesh Bank	6.00 +/-1.0	6.00 +/-1.0
Belarus	National Bank of the Republic of Belarus	max. 6.00 (2)	9% (2)
Botswana	Bank of Botswana	3.00 - 6.00	3.00 - 6.00
Brazil	Central Bank of Brazil	4.50 +/-1.50	4.50 +/-1.50
Canada	Bank of Canada	2.00 +/-1.0	2.00 +/-1.0
Chile	Central Bank of Chile	3.00 +/-1.0	3.00 +/-1.0
China	People's Bank of China	around 3.00 (9)	around 3.00 (9)
Colombia	Central Bank of Colombia	3.00 +/-1.0	3.00 +/-1.0
Costa Rica	Central Bank of Costa Rica	3.00 +/-1.0	3.00 +/-1.0
Czech Republic	Czech National Bank	2.00 +/-1.0	2.00 +/-1.0
Dominican Republic	Central Bank of the Dominican Republic	4.00 +/-1	4.00 +/-1
Egypt	Central Bank of Egypt	13.0 +/-3 (13)	13.0 +/-3 (13)
Euro Area	European Central Bank	<2.00 (11)	<2.00 (11)
Gambia	Central Bank of the Gambia	5.00	5.00
Georgia	National Bank of Georgia	5.00 (6)	5.00 (6)
Ghana	Bank of Ghana	8.00 +/-2.0	8.00 +/-2.0
Guatemala	Bank of Guatemala	4.00 +/-1.0	4.00 +/-1.0
Hungary	Central Bank of Hungary	3.00 +/-1.0	3.00 +/-1.0
Honduras	Central Bank of Honduras	4.00 +/-1.0 (15)	4.00 +/-1.0 (15)
Iceland	Central Bank of Iceland	2.50	2.50
India	Reserve Bank of India	4.00 +/-2.0	4.00 +/-2.0
Indonesia	Bank Indonesia	4.00 +/-1.0	4.00 +/-1.0
Israel	Bank of Israel	1.00 - 3.00	1.00 - 3.00

(Annex Table 1.7 contd.)

(Annex Table 1.7 contd.)

Country	Name of Central Bank	Target in 2018	2017
Jamaica	Bank of Jamaica	4.0-6.0	4.0-6.0
Japan	Bank of Japan	2.00	2.00
Kazakhstan	National Bank of Kazakhstan	5.00-7.00 (7)	6.00-8.00 (7)
Kenya	Central Bank of Kenya	5.00 +/-2.50	5.00 +/-2.50
Kyrgyzstan	National Bank of the Kyrgyz Republic	7.00	7.00
Malawi	Reserve Bank of Malawi	14.2 (3)	14.2 (3)
Mexico	Bank of Mexico	3.00 +/-1.0	3.00 +/-1.0
Moldova	National Bank of Moldova	5.00 +/-1.5	5.00 +/-1.5
Mongolia	Bank of Mongolia	<8.00 +/-2 (12)	<8.00 +/-2 (12)
Mozambique	Bank of Mozambique	5.60	5.60
Nepal	Nepal Rastra Bank	7.00	7.00
New Zealand	Reserve Bank of New Zealand	2.00 +/-1.0	2.00 +/-1.0
Nigeria	Central Bank of Nigeria	6.00 - 9.00	6.00 - 9.00
Norway	Norges Bank	2.00 (16)	2.50
Pakistan	State Bank of Pakistan	6.00 (4)	6.00 (4)
Paraguay	Central Bank of Paraguay	4.00 +/-2.0	4.00 +/-2.0
Peru	Central Reserve Bank of Peru	2.00 +/-1	2.00 +/-1
Philippines	Bangko Sentral ng Pilipinas	3.00 +/- 1.0	3.00 +/- 1.0
Poland	National Bank of Poland	2.50 +/-1.0	2.50 +/-1.0
Romania	National Bank of Romania	2.5 +/-1.0	2.5 +/-1.0
Russia	Bank of Russia	4.00	4.00
Samoa	Central Bank of Samoa	3.00	3.00
Serbia	National Bank of Serbia	3.00 +/-1.5	3.00 +/-1.5
South Africa	South African Reserve Bank	3.00 - 6.0	3.00 - 6.0
South Korea	Bank of Korea	2.00 (5)	2.00 (5)
Sri Lanka	Central Bank of Sri Lanka	3.00 - 5.0	3.00 - 5.0
Sweden	The Riksbank	2.00	2.00
Switzerland	Swiss National Bank	<2.00	<2.00
Tanzania	Bank of Tanzania	0.0-5.0 (10)	0.0-5.0 (10)
Thailand	Bank of Thailand	2.50 +/-1.5	2.50 +/-1.5
Turkey	Central Bank of Republic of Turkey	5.00 +/-2	5.00 +/-2
Uganda	Bank of Uganda	5.00 +/-2.0	5.00 +/-2.0
Ukraine	National Bank of Ukraine	5.00 +/- 1 (1)	5.00 +/- 1 (1)
United Kingdom	Bank of England	2.00	2.00
Uruguay	Central Bank of Uruguay	3.00 - 7.00	3.00 - 7.00
United States of America	Federal Reserve	2.00	2.00
Vietnam	State Bank of Vietnam	5.00	5.00
West African States	Central Bank of West African States	2.00 +/-1	2.00 +/-1
Zambia	Bank of Zambia	9.00	9.00

Source: CentralBankNews.info.

Note: (1) Slowdown path: 8.0% (+/-2%) December 2017, 6.0% (+/-2%) December 2018, 5.0% (+/-1%) December 2019; (2) 5% by end-2020; (3) Target for June 2016 implies measures to reach avg. 21% for calendar year; (4) Target for fiscal 2017/18; (5) Target for 2016-2018; (6) 4.0% target 2017, 3.0% later years; (7) 5%-7% by end-2018, 4%-6% end-2019, below but close to 4% by end-2020; (8) 10.0% for 2019, 5.0% for 2020; (9) CCP National Congress; (10) Longer-term average; (11) below, but close to, 2% over medium term; (12) target for 2017-2019; (13) target for Q4 2018, single digits thereafter; (14) target for 2017/18; (15) target for 2017/18; (16) As of 2 March 2018.

Annex Table 1.8

BASEL III Compliance Status of SCBs

(in Per cent)

Name of SCB	CET1	LCR	NSFR	LR	NPL
Agrani Bank Limited	N/A	750.40	109.89	3.11	20
Bangladesh Development Bank Limited	N/A	571.47	100.30	19.52	40.75
BASIC Bank Limited*	-17.23	236.03	88.64	-9.38	54.13
Janata Bank Limited	8.40	279.66	107.23	4.61	16.54
Rupali Bank Limited	4.99	504.73	101.31	2.60	23.40
Sonali Bank Limited*	7.45	537.90	114.03	2.81	28.38

Source: BASEL III disclosures on risk-based capital of individual banks.
Note: * indicates data for 2016.

Annex Table 1.9

BASEL III Compliance Status of DFIs

(in Per cent)

Name of DFI	CET1	LCR	NSFR	LR	NPL
Bangladesh Krishi Bank	N/A	50.76	95.66	-29.35	23
Rajshahi Krishi Unnayan Bank	-7.72	300	181	-5.25	23

Source: BASEL III disclosures on risk-based capital of individual banks.
Note: * indicates data for 2016.

Annex Table 1.10

BASEL III Compliance Status of PCBs

(in Per cent)

Name of PCB	CET1	LCR	NSFR	LR	NPL
AB Bank Limited	N/A	125.76	104.66	5.70	7.15
Al-Arafah Islami Bank Limited*	11.31	106.17	101.21	6.75	N/A
Bangladesh Commerce Bank Limited	N/A	N/A	N/A	N/A	N/A
Bank Asia Limited	8.53	109.32	105.92	5.38	4.38
BRAC Bank Limited	11.24	125.51	114.38	7.49	N/A
Dhaka Bank Limited	7.95	100.06	101.52	5.24	5.98
Dutch-Bangla Bank Limited	9.20	125.10	115.70	5.20	4.70
Eastern Bank Limited	10.24	113.35	102.82	5.59	2.50
Export Import (EXIM) Bank of Bangladesh Limited	8.65	100.15	104.70	6.70	5.32
First Security Islami Bank Limited	6.77	212.41	103.55	3.24	3.07
ICB Islamic Bank Limited	-117.15	69.48	83.27	-98.68	80.04
International Finance Investment and Commerce (IFIC) Bank Limited	9.84	102.95	100.23	7.33	6.40
Islami Bank Bangladesh Limited	8.71	127.49	108.47	4.90	N/A
Jamuna Bank Limited	7.27	136.00	115.72	5.33	4.03
Meghna Bank Limited	N/A	303.02	121.82	12.10	3.39
Mercantile Bank Limited	7.91	100.79	106.16	5.58	3.79

(Annex Table 1.10 contd.)

(Annex Table 1.10 contd.)

Name	CET1	LCR	NSFR	LR	NPL
Midland Bank Limited	19.98	249.28	128.05	13.02	N/A
Modhumoti Bank Limited	15.67	268.20	121.39	10.71	0.29
Mutual Trust Bank Limited	7.30	127.92	100.85	4.24	4.30
National Bank Limited*	11.37	178.81	110.24	10.03	10.35
National Credit and Commerce Bank Limited	10.40	123.02	101.49	7.22	5.79
NRB Bank Limited	17.34	103.85	108.59	11.85	N/A
NRB Commercial Bank Limited	N/A	109.30	112.95	9.93	N/A
NRB Global Bank Limited	N/A	300.72	105.13	6.14	1.03
One Bank Limited	7.60	104.29	121.66	5.82	N/A
Prime Bank Limited	10.01	109.58	120.08	6.61	N/A
Pubali Bank Limited	9.38	204.02	103.82	6.05	N/A
Shahjalal Islami Bank Limited	8.38	100.57	118.97	5.51	3.97
Shimanto Bank Limited	N/A	N/A	N/A	N/A	N/A
Social Islami Bank Limited	7.02	106.66	113.58	4.43	8.20
South Bangla Agriculture and Commerce Bank Limited	15.31	149.07	110.57	10.11	0.87
Southeast Bank Limited	6.80	102.81	115.55	5.16	5.99
Standard Bank Limited	9.26	87.00	104.09	6.74	8.29
The City Bank Limited	10.15	131.90	110.55	6.37	5.43
The Farmer's Bank Limited*	9.74	105.07	122.82	7.27	N/A
The Premier Bank Limited	7.85	90.18	113.72	5.06	4.69
Trust Bank Limited	7.59	102.34	102.34	4.45	3.35
Union Bank Limited	10.05	103.41	121.64	5.19	N/A
United Commercial Bank Limited	7.71	119.29	113.35	5.07	7.38
Uttara Bank Limited	11.38	908.55	108.65	6.14	6.60

Source: BASEL III disclosures on risk-based capital of individual banks.
Note: * indicates data for 2016.

Annex Table 1.11
BASEL III Compliance Status of FCBs

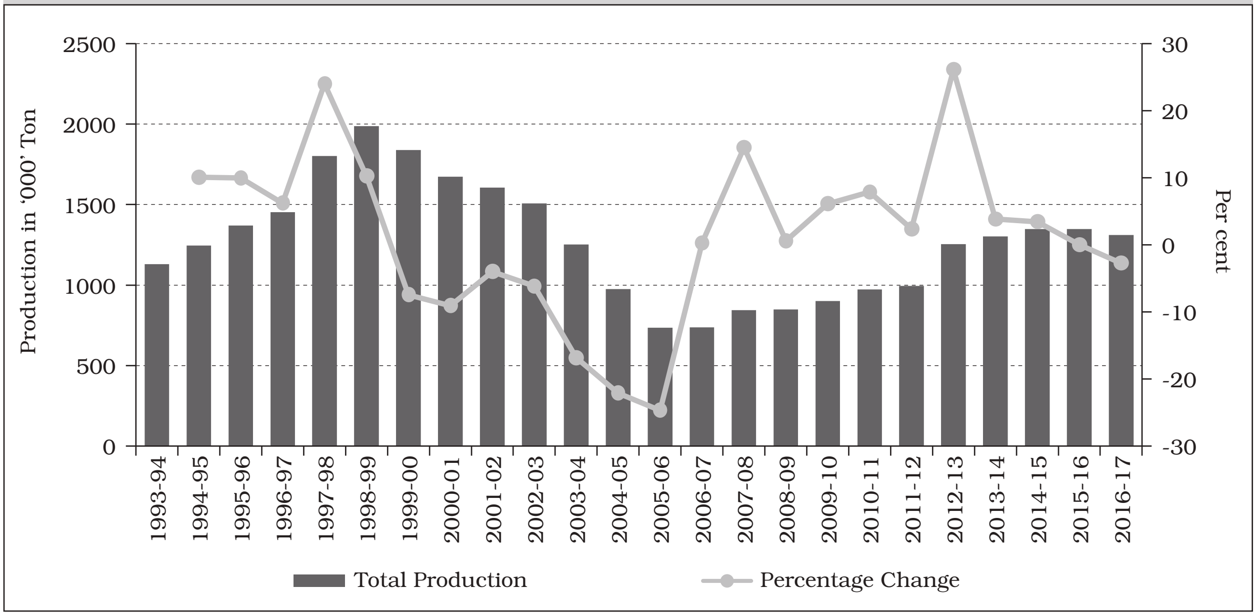
(in Per cent)

Name of FCB	CET1	LCR	NSFR	LR	NPL
Bank Al-Falah Limited	56.43	225.69	141.98	24.10	2.53
Citibank N.A	37.76	124.25	123.20	21.21	1.35
Commercial Bank of Ceylon PLC	34.49	129.45	115.59	17.89	1.39
Habib Bank Limited	N/A	120.24	102.95	35.19	8.51
National Bank of Pakistan	N/A	8.17	24.74	17.59	94.65
Standard Chartered Bank	14.24	123.11	133.03	10.06	2.95
State Bank of India	81.95	119.52	118.30	22.99	N/A
The Hongkong and Shanghai Banking Corporation (HSBC) Limited	27.91	111.13	111.96	14.51	N/A
Woori Bank	29.88	320.24	128.80	53.52	1.38

Source: BASEL III disclosures on risk-based capital of individual banks.
Note: * indicates data for 2016.

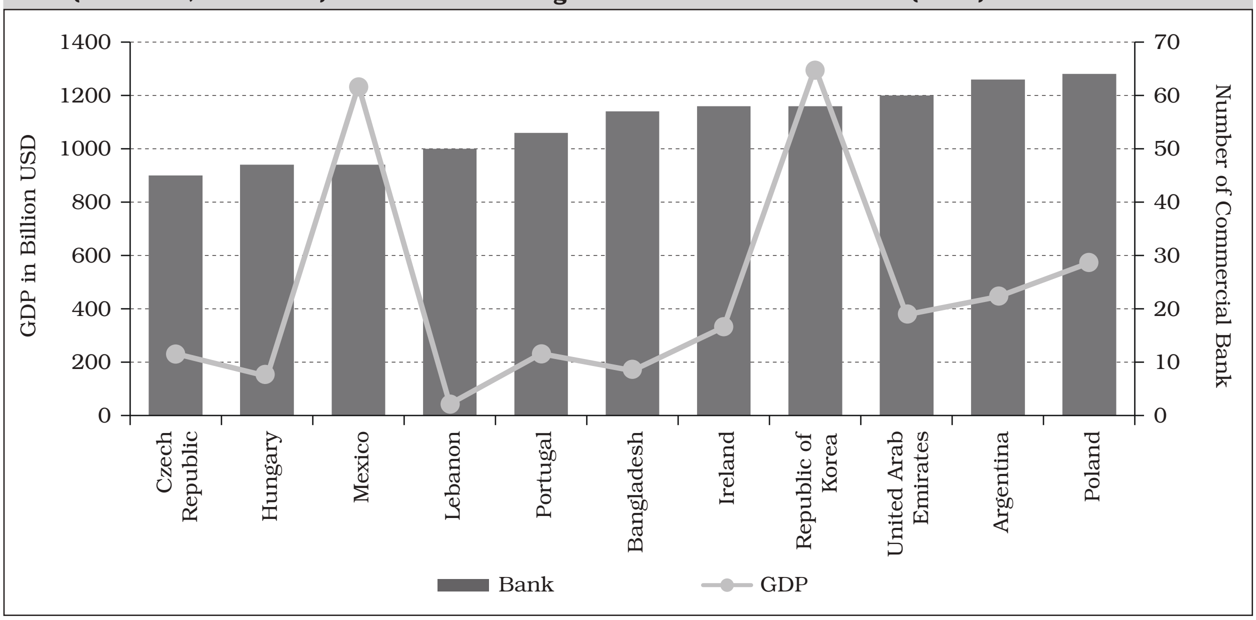
Annex Figures

Annex Figure 1.1
Wheat Production



Source: Bangladesh Bureau of Statistics (BBS).

Annex Figure 1.2
GDP (Constant, 2010 USD) of Countries having 45 to 65 Commercial Banks (2016)



Source: International Monetary Fund (IMF) Financial Access Survey Data.

Chapter 2

State of the Bangladesh Economy in FY2017-18 *(Second Reading)*

CPD's Recommendations for the Upcoming Budget

This report was released to the media by the Centre for Policy Dialogue (CPD) on 17 April 2018.

2.1 INTRODUCTION

National budget for FY2018-19, the last budget of the incumbent government before the upcoming national election, is being prepared in the backdrop of the global economy transmitting mixed signals and the domestic economy experiencing emerging tensions with accentuated traditional ones. The upcoming budget will need to address these attendant concerns through renewed efforts at raising the quality of budgetary and fiscal planning at a time of election-related uncertainties. Consequently, a key objective of the forthcoming budget should be maintaining macroeconomic stability. This report highlights some of the key challenges which call for immediate policy attention, particularly from the perspective of macroeconomic management. The report puts forward a number of recommendations which, however, may not be possible for the government to implement before the national election. Nevertheless, it is reckoned that some of these issues should find place in the electoral debates that will follow the budget.

The report focuses on eight areas: (a) macroeconomic stance towards sustainable growth acceleration and enhanced employment generation; (b) banking sector; (c) capital market; (d) incentivising export-oriented sectors; (e) catalysing private investment; (f) social security and provision of human resources development for the disadvantaged; (g) budgetary implications of *Rohingya* crisis; and (h) a Trust Fund for Sustainable Development Goals (SDGs) delivery. The report makes use of the most recent data from available official and credible international sources to review the trends of the relevant macroeconomic and development correlates and for purposes of analyses.

The present report is the second instalment of the State of the Bangladesh Economy in FY2017-18 prepared under CPD's flagship programme titled *Independent Review of Bangladesh's Development (IRBD)*. The report will be followed by a comprehensive analysis of the Bangladesh economy covering FY2018, to be released prior to the placement of the FY2018-19 budget before the Parliament expected on 7 June 2018. The final instalment of this year's IRBD analysis will be released immediately after presentation of the FY2018-19 budget with CPD's immediate reactions to the fiscal-budgetary proposals in the budget.

2.2 THE MACROECONOMIC SCENARIO

2.2.1 Setting the Macroeconomic Benchmark for FY2018-19

As the preparation of the national budget for FY2018-19 comes to its final stage, it is important that the policymakers take due cognisance of the current trends of key macroeconomic correlates while calibrating and designing the fiscal-budgetary measures and incentives. It may be recalled here that, CPD (2018) in its first interim review of Bangladesh's macroeconomic performance for the ongoing FY2017-18, released in January 2018, had drawn attention to the growing pressure on macroeconomic stability. Indeed, in the run up to the forthcoming national budget, the need for significant improvement in the quality of macroeconomic management has emerged as an urgent priority.

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

According to the provisional estimates by the Bangladesh Bureau of Statistics (BBS), gross domestic product (GDP) growth in FY2017-18 is expected to be 7.65 per cent. It is for the fourth time that in the course of the last two decades (since FY2006-07) that the GDP growth would exceed 7 per cent. Of the estimated growth rate of 7.65 per cent for FY2017-18, agriculture sector's contribution is estimated to be to the tune of 0.43 percentage points (0.44 percentage points in FY2016-17)[1], industries sector's contribution to be about 3.73 percentage points (3.10 percentage points in FY2016-17), and that of the services sector to be 3.21

[1]Agriculture sector has been estimated to grow by 9.8 per cent, highest since FY2013-14.

percentage points (3.41 percentage points in FY2016-17) (Table 2.1). Indeed, the robust estimated GDP growth number has been primarily driven by manufacturing sector, followed by the construction sector.[2] Both these sectors have posted record-breaking growth figures. Indeed, if the growth rates of FY2017 (7.28 per cent) and FY2018 (7.65 per cent) are compared, of the additional growth of 0.37 percentage points, 0.54 percentage points is expected to be contributed by the manufacturing sector.

Table 2.1

Contribution to GDP Growth over the Last Ten Years

(in percentage point)

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

Source: Authors' calculations from Bangladesh Bureau of Statistics (BBS) data.
Note: 'p' denotes provisional estimates.

Manufacturing sector's robust growth is drawn from the Quantum Index of Industrial Production (QIIP) estimates which posted 21.1 per cent growth for large and medium scale manufacturing industries during the first five months of this fiscal year. The somewhat modest recovery in export growth (6.6 per cent) during the same period was mainly dominated by readymade garments (RMG), which did not play a major part in QIIP growth.[3] Other manufacturing industries, i.e., leather and related products (76.6 per cent), pharmaceuticals and medicinal chemical (44.7 per cent), textile (33 per cent) and food products (29.3 per cent) registered very high growth rates according to QIIP without a commensurate reflection in the export performance.[4] For example, export earnings of leather and leather products, as a matter of fact, declined by (-) 3 per cent during the first five months of FY2018.

Investment as per cent of GDP is projected to increase by about one percentage point to 31.5 per cent in FY2017-18, thanks to the spurt in public investment (to 8.2 per cent). Regrettably, private investment as a share of GDP is estimated to increase only marginally (by about 0.2 percentage point) to 23.3 per cent (Figure 2.1). Meanwhile, the import of capital machineries recorded a 34 per cent growth during July-February period of FY2017-18. It may be assumed that majority of these capital machineries was imported for public sector investment which has been estimated to rise by 25.6 per cent in FY2017-18. It is reckoned that, the rise in the public investment estimate has considered almost 90 per cent utilisation of the original allocations of the Annual Development Programme (ADP) for FY2017-18. As it has been observed in previous years, the year-end public expenditure is likely to be much lower than the planned figures, not to also speak about the discrepancy between figures of Ministry of Finance (MoF) and Implementation Monitoring and Evaluation Division (IMED). CPD has been drawing attention to this last anomaly for the last several years.[5] In all likelihood, the public investment and GDP figures will need to be revised accordingly when the

[2]Growth rates of manufacturing and construction sectors are estimated to be 13.2 per cent and 10.1 per cent respectively. No other sector was able to register a double-digit growth.

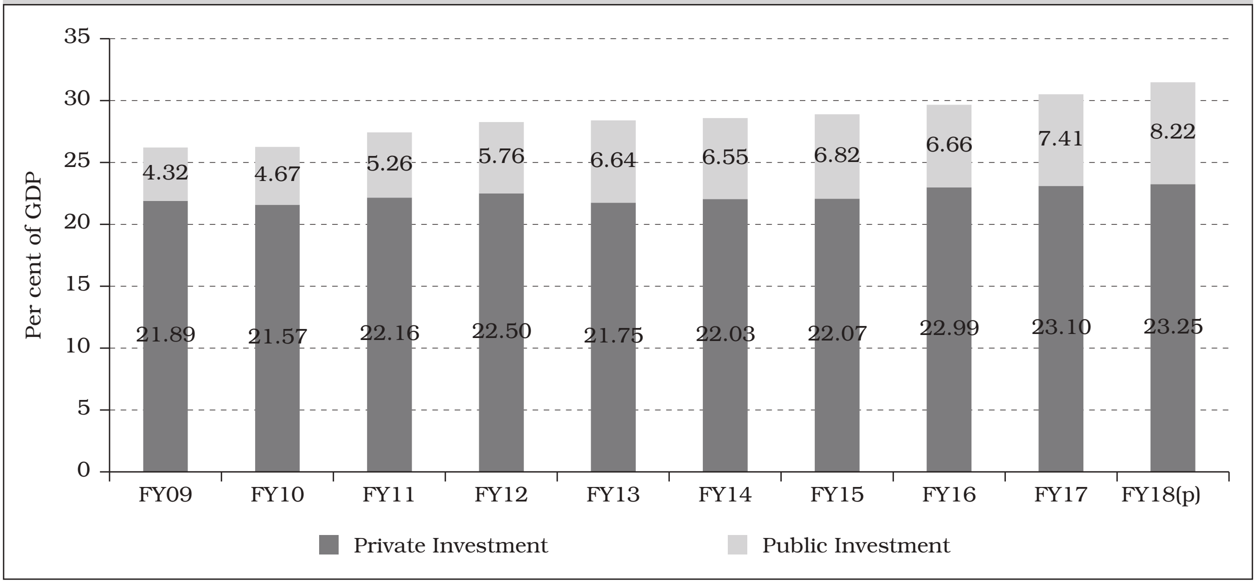
[3]The manufacturing of wearing apparel with a weight of 34.8 per cent in QIIP (large and medium), registered only 10.9 per cent growth during July–November of FY2017-18.

[4]Combined weight of these four industries was about 38 per cent of total manufacturing production.

[5]At the end of FY2016-17, the overall ADP implementation reported by IMED and MoF was 91.1 per cent and 69.8 per cent of the respective revised (as well as original) figures. The discrepancy stood at Tk. 23,574 crore.

Figure 2.1

Investment Scenario: FY2008-09 to FY2017-18



Source: Bangladesh Bureau of Statistics (BBS).

Note: 'p' denotes provisional estimates.

GDP growth estimates will be finalised after the actual expenditure figures for the full fiscal year become available.

Curiously, the growth rate of nominal GDP of 13.3 per cent was the lowest compared to the previous two fiscal years. It was indeed the relatively low GDP deflator growth (5.2 per cent) which resulted in the high real GDP growth rate. This rate was lower than the inflation rate (5.7 per cent) as of December 2017 which has been on an increasing trend since July 2017. This also raises concern as regards the quality of growth estimate.

Employment generation increased in FY2016-17 but real income had declined

As may be recalled, CPD (2018) in January 2018 had raised concerns about the slowdown in employment generation over the 2013 to 2015-16 period. On a positive development, according to the latest round of the Labour Force Survey (LFS), about 1.3 million additional jobs were created between 2015-16 and 2016-17 (BBS, 2018). Net employment was almost entirely generated in the services sector (3.7 million). In contrast, agriculture sector saw a decline of net employment by about (-) 0.7 million; while in industries sector only 262 thousand net jobs were added. As a result, share of total employment in agriculture sector reduced to 40.6 per cent in 2016-17 from 42.7 per cent in 2015-16 (Table 2.2). This share has been almost entirely seized by the services sector.

Furthermore, within the services sector, majority of the additional jobs created were in wholesale and retail trade, except of motor vehicles (0.7 million); land transport and transport via pipeline (0.6 million); food and beverage service activities (0.1 million); and activities of households as employers (0.1 million). In the industries sector, major part of the additional net jobs was created in manufacturing of wearing apparel (178 thousand) and in construction of buildings (182 thousand). It can be mentioned here that, between 2013 and 2016 period, employment in the manufacturing sector declined by about 0.9 million despite robust growth performance of the sector. Recent positive trend was not able to compensate as yet for the previous decline. It is to be noted that, many important manufacturing industries, including textile

Table 2.2
Employment by Broad Economic Sectors

Sector	2010	2013	2015-16	2016-17
	Employed by Broad Economic Sector (million)			
Total	**54.1**	**58.1**	**59.5**	**60.8**
Agriculture	25.7	26.2	25.4	24.7
Industries	9.6	12.1	12.2	12.4
Services	19.1	19.8	22.0	23.7
Composition by Broad Economic Sector (Per cent)				
Total	**100**	**100**	**100**	**100**
Agriculture	47.6	45.1	42.7	40.6
Industries	17.7	23.0	20.5	20.4
Services	25.5	32.0	36.9	39.0

Source: Authors' calculations from Bangladesh Bureau of Statistics (BBS) Data.

and food products, continued to experience loss in terms of net jobs. Hence, in FY2016-17, although, as per BBS estimates, a commendable pace of economic growth was registered, thanks to accelerated rise in industrial value addition, this was not reflected in the employment outcome.

In FY2016-17, employment numbers increased only in three divisions, viz. Dhaka (972 thousand), Chittagong (612 thousand) and Rangpur (238 thousand). In the other four divisions combined employment numbers declined by about 524 thousand.

An increased labour supply matched with increased demand helped keep unemployment rate constant at 4.2 per cent. Interestingly, this has emerged as a distinct feature of the labour market in Bangladesh. Perhaps, this is due to the fact that the definition of employment is rather loose—a person working for only one hour in a week may be considered as employed. However, the concept of decent work in the SDGs framework goes far beyond this definition, arguing in favour of rewarding employment on a long-term basis. In view of the SDGs that Bangladesh aspires to achieve, Bangladesh will need to significantly improve the context of this indicator. This is particularly evident in view of the fact that despite generating a significant number of employment in FY2016-17, unemployment rate among the relatively more educated labour force, particularly with secondary and tertiary education, had risen to 14.9 per cent and 11.2 per cent respectively (Table 2.3). In contrast, anecdotal information suggests that businesses find it difficult to find qualified job seekers for their enterprises. There is clearly a mismatch between demand and supply in the job market.

Table 2.3
Unemployment Rate by Education Level

(Per cent of respective labour force)

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

Source: Authors' calculations from Bangladesh Bureau of Statistics (BBS) Data.

Besides, it is also important to note that the unemployment rate among the youth had increased further from 8.7 per cent in FY2015-16 to 10.6 per cent in FY2016-17 (Table 2.4). This was significantly higher than the national average figure (4.2 per cent). More than one-third of the total youth labour force with tertiary education (34.3 per cent) remained unemployed in FY2016-17. The corresponding figure for female cohort was even higher (42.5 per cent). The figures have also increased over time. While reading these numbers, one needs to consider the fact that a notable share of youth in FY2016-17 was not involved in employment, education or training (29.8 per cent) (BBS, 2018). This is even higher for Bangladesh's young female population. It goes without saying that, with such high number of potential labour force remaining outside of the labour market (outside of also education and training), it will be hardly possible for Bangladesh to reap the potential benefits of the 'demographic window of opportunity'.

Table 2.4
Unemployment Rate by Education Level

(Per cent of total youth labour force)

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

Source: Authors' calculations from Bangladesh Bureau of Statistics (BBS) Data.

Despite the improved number of employment, average real monthly income had suffered erosion in FY2016-17, by (-) 2.5 per cent. The decline is higher for female labour, by (-) 3.8 per cent. It may be also important to note that between, 2013 and 2015-16, over three years, average real monthly income had also declined by (-) 3.9 per cent. Hence, not only that the declining trend in real income had continued, also the pace of deceleration has accelerated in FY2016-17. Decline in real income increased for urban male workers, although it did not reach the level of 2013 (Table 2.5). This development is being observed at a time when wages of formal labour force had been adjusted, particularly for those working in the public sector. No surprise, despite registering accelerated economic growth and generating employment, the pace of poverty reduction had slowed down. Indeed, what this indicates is that, in recent years the larger share of economic growth has been disproportionately captured by entrepreneurs and owners of land and capitals. The recent trends in the labour market dynamics thus further strengthen the need for refocusing Bangladesh's development objective from the existing 'GDP growth acceleration' centric strategy to a 'decent employment generating high economic growth' centric strategy, as was urged and advocated by CPD (2018).

Table 2.5
Average Real Monthly Income

(in Tk., adjusted with CPI)*

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

Source: Authors' estimation from Bangladesh Bureau of Statistics (BBS) Data.
Note: *Consumer Price Index (CPI).

Weak budgetary planning and implementation capacity persist

In FY2017-18, weak budgetary planning and implementation capacity continued to be a major concern. From the vantage point of the end of the first half (July–December) of FY2017-18, achievement of most of the fiscal parameters look unrealistic and highly unlikely: revenue collection, ADP, net foreign borrowing and grant will need to grow by 65.3 per cent, 136.7 per cent and 564.3 per cent respectively over the remaining six months of FY2017-18 (Table 2.6).

Table 2.6
Fiscal Framework

(growth in Per cent)

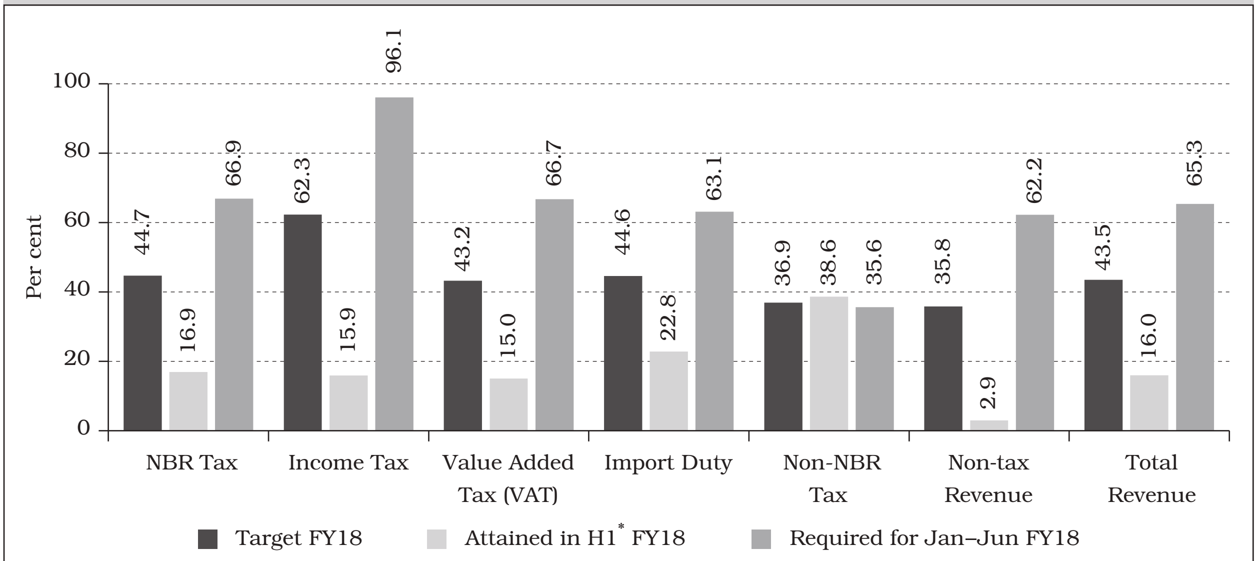
Fiscal Parameter	Target FY17	Actual FY17	Target FY18	Up to Dec FY18	Required for Jan–Jun FY18
Revenue collection	40.4	16.1	43.5	16.0	65.3
Total expenditure	42.4	9.3	53.1	7.8	79.1
ADP	*38.3*	*-3.5*	*98.4*	*4.9*	*136.7*
Non-ADP	*44.4*	*15.7*	*34.0*	*8.7*	*50.7*
Overall deficit (excl. grants)	-47.6	8.4	-84.8	103.1	-107.6
Net foreign borrowing and grant	133.8	-49.1	557.3	441.6	564.3
Foreign grants	*168.3*	*-57.4*	*529.1*	*-72.3*	*634.1*
Foreign borrowing-net	*128.5*	*-47.9*	*560.8*	*647.8*	*556.6*
Domestic borrowing	21.2	4.0	14.3	-143.5	35.0
Bank borrowing (net)	*266.9*	*-180.2*	*431.2*	*32.0*	*339,940.0*
Non-bank borrowing (net)	*-43.7*	*52.6*	*-47.6*	*-78.6*	*-37.8*
Total financing	**52.3**	**-5.5**	**84.9**	**-103.1**	**107.8**

Source: Authors' Calculations from Ministry of Finance (MoF) data.

Revenue mobilisation is likely to fall short of target for the sixth consecutive year in FY2017-18

Revenue collection showed a marginally improved performance compared to the previous fiscal year during the first half of FY2017-18 registering 16.0 per cent growth (Figure 2.2). While tax collection had somewhat improved, non-tax collection had underperformed. According to MoF data, National Board of Revenue (NBR) tax registered a growth of 16.9 per cent during first six months of FY2017-18 as against the target of 44.7 per cent.[6] However, due to unrealistic programming of the fiscal framework targets, a large shortfall in revenue has become a certainty. It may be recalled that, immediately after the national budget had been passed, CPD (2017) came up with the projection that the revenue shortfall in FY2017-18 was likely to be in the range of Tk. 43,000 crore to Tk. 55,000 crore. In order to attain the annual growth target of 43.5 per cent, total revenue would need to increase at a rate of 65.3 per cent for the remainder of the fiscal year—which is highly improbable, to say the least. Also, to be noted, there are signs of greater reliance on import-related revenue sources (22.8 per cent). Furthermore, growth of income tax collection during July-December of this fiscal year (15.9 per cent) was lower than the corresponding period of FY2016-17 (16.7 per cent). On a positive note, non-NBR tax registered a strong growth (38.6 per cent), but its share was only 4.1 per cent in the total revenue. CPD's overall projection is that, revenue shortfall in the current fiscal year is likely to be about Tk. 50,000 crore.

Figure 2.2
Growth Rates of Revenue Collection Components



Source: Authors' calculations from Ministry of Finance (MoF) data.
Note: *First half (H1).

ADP implementation remains business as usual despite high project aid utilisation

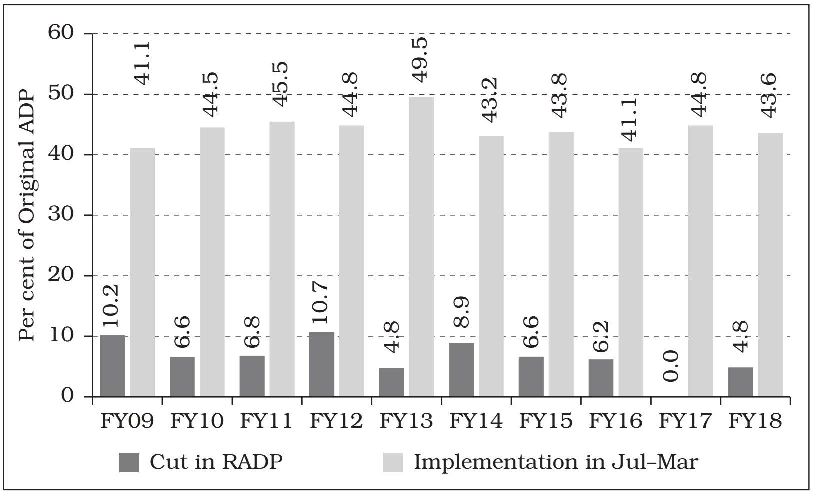
Expenditure on account of the ADP is yet to mark any significant breakthrough in FY2017-18. According to the first nine months' (July–March) data, actual spending under ADP was 43.6 per cent of the originally planned allocation of Tk. 155,931 crore which is lower than the previous fiscal year for the corresponding period. Data discrepancy among MoF and IMED is also a major concern here.[7] Higher utilisation (48.2 per cent) of foreign aid (highest since FY2005-06) is a positive sign in the context of budget implementation

[6]However, according to data reported by NBR, the NBR tax registered a growth of 17.9 per cent during July–November while it stood at 15.6 per cent during July–February of FY2017-18.

[7]According to MoF data, ADP implementation during July-December of FY2017-18 was 15.3 per cent while IMED reported the implementation rate to be 27.1 per cent (almost double) for the corresponding period.

Figure 2.3

Revised ADP (RADP), the Cuts and ADP Implementation Scenario



Source: Authors' estimation from the Implementation Monitoring and Evaluation Division (IMED) data.

trends in FY2017-18, thanks almost solely to the Power Division. Meanwhile, utilisation of local resources i.e Taka component (40.7 per cent) during July–March of FY2017-18 was the lowest since FY2007-08. Among the top 10 ministries/divisions having a share of 73.3 per cent in total ADP allocation for FY2017-18, only Power Division (79.9 per cent), Local Government Division (57.2 per cent) and Ministry of Science and Technology (51.8 per cent) had been able to spend more than the average amount of allocation during July–March of FY2017-18.

Due to slow pace of implementation, a number of major government agencies (e.g. Transport, Education and Religious Affairs, Science, Information and Communication Technology, and Oil, Gas and Natural Resources) were subjected to significant cuts in the RADP for FY2017-18. ADP for FY2017-18 was slashed by Tk. 7,550 crore (or 4.8 per cent) to bring the size down to Tk. 1,48,381 crore (Figure 2.3). Project aid component was reduced by Tk. 8,366 crore (or 13.8 per cent) while Taka component was increased by Tk. 816 crore (or 0.9 per cent) although the rate of utilisation of the latter was the slowest since FY2007-08. Given the implementation status of the ADP, a more substantive rationalisation of ADP allocation was perhaps called for.

On the other hand, delayed implementation, cost overrun and institutional weakness have undermined the effectiveness of the concerned projects. Consequently, these projects are yet to provide an impetus to private investment in Bangladesh. CPD (2018) in an earlier exercise found that in FY2015-16, of the 201 completed projects that had posted financial progress of more than 80 per cent, 93 projects had faced cost overrun with a cumulative amount of Tk. 5,640 crore.

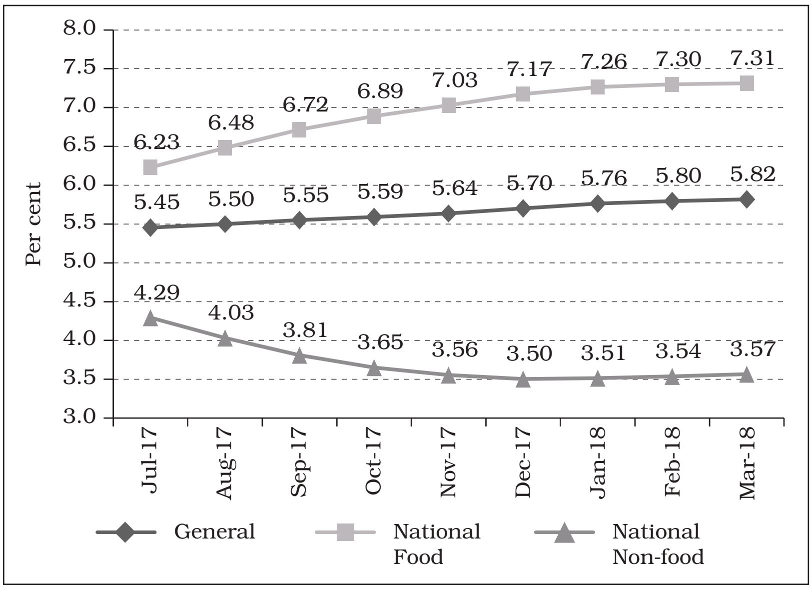
High cost of borrowing for financing budget deficit continues

The scale of budget deficit may not be a major concern since the shortfall in revenue collection is likely to be offset by the inability to spend budgetary allocations. However, high cost of borrowing from National Savings Directorate (NSD) certificates will put pressure on debt sustainability in the medium term. Net sales of NSD certificates stood at Tk. 33,120 crore during July-February of FY2017-18 which is already 9.9 per cent higher than the annual target set for FY2017-18. It appears at the moment that, the government has no plan to cut interest rates for NSD certificates for the upcoming fiscal year. On a positive note, Net foreign borrowing and grant registered a growth of 442 per cent, to Tk. 2,459 crore, during July-December of FY2017-18. Meanwhile, inability to fully implement budgetary allocation will likely lead to further escalation of ADP project costs over the upcoming fiscal years.

Inflation, although at a lower level, is slowly creeping up and is primarily driven by rising food inflation

The growth in annual average inflation reached 5.8 per cent in March of FY2017-18 (Figure 2.4) against the annual target of 6.0 per cent set in the Monetary Policy Statement (MPS) of the Bangladesh Bank for the second half of FY2017-18. However, an increasing trend can be observed since May 2017. The key reason behind this is the rising food inflation which, in turn, is mostly driven by increased rice prices. As of 9 April 2018, price of coarse, medium and fine rice exhibited 3.7 per cent, 13.0 per cent and 25.0 per cent increase on a point-to-point basis respectively.[8] Indeed, retail price of coarse rice in Bangladesh was found to be approximately 8.1 per cent higher than the average wholesale price prevailing in Kolkata as of 10 April 2018. The increase in food inflation was somewhat offset by declining non-food inflation during the July–December period of FY2017-18. However, this trend had changed with increasing non-food inflation since January of FY2017-18. During the July–March time frame of FY2017-18, urban inflation showed a declining trend while the inverse is discernible for rural inflation. As a result, the gap between urban and rural inflation narrowed during the most recent months. As was noted, inflation was mostly driven by food prices irrespective of the location i.e. rural or urban.[9] Rising global commodity prices, possibility of further depreciation of Bangladeshi Taka (BDT), and relaxed monetary policy may exacerbate inflationary pressure in the economy over the coming months. In addition to these, the government needs to be vigilant to avoid any additional speculative pressure during Ramadan season.

Figure 2.4
Annual Average Inflation Rate



Source: Bangladesh Bureau of Statistics (BBS) data.

[8] In this estimation, 10 per cent cost and freight (c & f) charge was considered and relevant exchange rate conversions were carried out. Rice price for Bangladesh and India were taken from Trading Corporation of Bangladesh (TCB) and Department of Consumer Affairs, India respectively.

[9] As per Food Planning and Monitoring Unit (FPMU) data, public stock of foodgrains at the end of March 2018 was 1,426 thousand Metric Ton (MT) – of which rice accounted for 963 thousand MT. The government has decided to distribute rice at Tk. 10 per kg to 50 lac extreme poor households. This initiative will require 750 thousand MT of rice over the months of March–April of FY2017-18 and September–November of FY2018-19. If equal amount of rice is distributed each month then additional requirement for the current fiscal year will be 300 thousand MT – creating further pressure on the public stock. Moreover, the government has decided to procure 900 thousand MT of rice at Tk. 38 per kg and 150 thousand MT of paddy at Tk. 26 per kg during the upcoming Boro harvest season (May–August 2018). The cumulative pressure of these initiatives could exert further inflationary pressure on the economy.

Growth of broad money supply remained well below the programmed level

Credit to public sector remained subdued as of February 2018 with a negative (-) 14.2 per cent growth, thanks to the limited bank borrowing required by the government to finance the fiscal deficit incurred till now (Table 2.7). Net foreign assets, as of February 2018, posted a growth of 3.9 per cent against the end-June target of 0.1 per cent. However, with increasing pressure on balance of payments (BoP), the central bank may need to release more foreign exchange from the reserve which in turn is likely to further restrain the growth of net foreign assets. At the end of February 2018, broad money recorded a 9.8 per cent growth as opposed to the target of 13.3 per cent in June 2018. Credit to the private sector growth was 18.5 per cent as of February 2018 as opposed to the monetary policy target of 16.8 per cent for end-June 2018.

Table 2.7
Growth of Monetary Indicators

(in Per cent)

Indicator	Actual			Target	
	Jun 16	Jun 17	Feb 18	Jun 18 (Jul 17 MPS)	Jun 18 (Jan 18 MPS)
Net foreign assets	22.8	11.5	3.9	5.4	0.1
Net domestic assets	14.3	10.7	11.9	16.9	17.9
Domestic credit	14.4	11.2	14.2	15.8	15.8
Credit to the Public sector	*3.3*	*-13.0*	*-14.2*	*12.0*	*8.3*
Credit to the Private sector	*16.8*	*15.7*	*18.5*	*16.3*	*16.8*
Broad money	16.3	10.9	9.8	13.9	13.3
Reserve money	30.1	16.3	10.1	12.0	12.0

Source: Bangladesh Bank data.

Interest rates for both deposits and advances showed upward trend

Interest rate for advances was showing a declining trend during the July–November period of FY2017-18 whereas the interest rate for deposits hovered around the 4.9 per cent mark. However, both rates have started to exhibit upward trend since December 2017. Overall, interest rate spread showed a generally declining trend and hovered around the 4.4 per cent mark since the beginning of 2018. The rise in deposit rate could be attributable to the government's recent move to reduce advance-deposit ratio (ADR) and subsequent drives to collect more deposits by non-compliant banks. Also, prevailing weaknesses in the banking sector including non-performing loans (NPL) and CAMELS (capital adequacy; assets; management capability; earnings; liquidity; sensitivity) indicators (discussed in details in section 2.3) deter the banks from reducing the spread to any significant extent. As a result, lending rates had also risen in tandem.

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

As was mentioned earlier, Bangladesh Bank reduced the ADR to 83.5 per cent from an earlier 85.0 per cent in January 2018 as an attempt to curb the emergent liquidity pressure arising from aggressive lending. The initial deadline to implement this was set for June 30, 2018; this was revised twice and in the end cut-off date was set at 31 March 2019. At the same time, the central bank cut the cash-reserve ratio (CRR) by 1 percentage point to 5.5 per cent on bi-weekly average basis with a provision of at least 5.0 per cent on daily basis, effective from 15 April, 2018. Also, Bangladesh Bank decreased its repo rate from 6.75 per cent to 6.00 per cent while keeping the reverse repo rate unchanged at 4.75 per cent. It is to be noted in this connection that, these changes contradict government's earlier conservative approach, with the result of increasing money supply in the market. Questions may also be raised regarding the process which was followed in executing the recent changes.

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

During the first three quarters (July–March) of FY2017-18, total export earnings have remained marginally below the strategic target but the attained export growth was significantly higher than the achieved annual growth rate of 1.7 per cent in FY2016-17. *First*, according to Export Promotion Bureau (EPB) data, total export earnings registered a 6.3 per cent growth during July–March of FY2017-18 against the envisaged annual target of 8.2 per cent. This was driven by robust performance in (RMG) export which recorded a 9.1 per cent growth up to March of FY2017-18 compared to the annual target of 7.1 per cent (Figure 2.5A). Export growth of both knit- and woven-RMG products (11.6 and 6.8 per cent respectively) during the aforesaid period surpassed their annual growth target (9.8 and 4.6 per cent respectively). Regrettably, non-RMG items were not able to replicate this record. Growth of non-RMG exports during July–March of FY2017-18 was negative (-) 5.5 per cent as opposed to the annual target growth of 12.8 per cent; this would require an astounding 68.3 per cent growth for the remainder of the fiscal year for the annual target to be attained. This slump can be mainly ascribed to depressed export performances of leather and leather products, raw jute and engineering products. CPD, in its earlier analysis, asserted that growth of export value in major markets is mostly volume-driven. It was also observed that prices of Bangladesh's main export, RMG products, were declining over time and were also lower than comparator countries (CPD, 2018). Improvement in product quality and higher productivity are key to enhancing Bangladesh's export earnings through negotiation of higher prices.

Second, throughout the course of FY2017-18, export growth in non-traditional markets was lower compared to their traditional counterparts (Figure 2.5B). Indeed, export growth in non-traditional markets entered negative terrain during July–March of FY2017-18. The key reason behind this is the persistent poor performance of non-RMG exports in the non-traditional markets. Certainly, compared to March of FY2016-17, non-RMG exports to non-traditional markets experienced a decline of (-) 53.4 per cent in March of FY2017-18. This is a serious concern from the perspective of both product and market diversification.

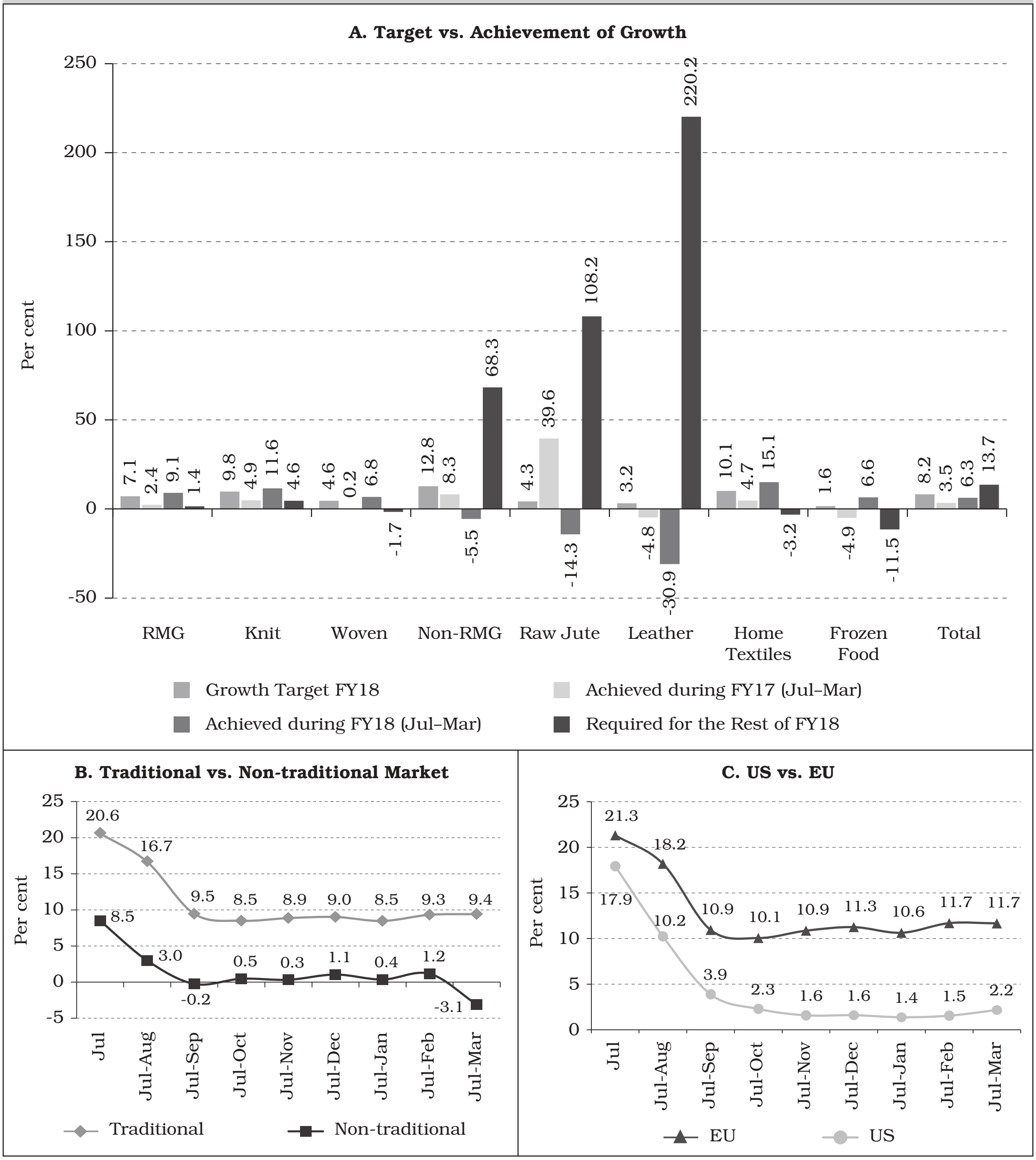
Third, amongst the traditional markets, export growth in the United States (US) has been at a very low level in FY2017-18 (Figure 2.5C). Both RMG and non-RMG items exhibited subdued export growth during July–March of FY2017-18. Amongst the RMG exports to the US, woven items – which constitute the larger share, posted an insignificant growth of 0.6 per cent during July–March of FY2017-18.

Fourth, export growth in the European Union (EU), market was 11.7 per cent during the first nine months of FY2017-18 (Figure 2.5C). This was driven by export of RMG products; export of the item to the EU market increased by 11.6 per cent. Both knit and woven items registered notable growth (12.5 per cent and 10.6 per cent respectively). Although growth of non-RMG exports to the EU has been relatively upbeat, it is displaying a gradually declining trend (from 48.2 per cent during July of FY2017-18 to 11.9 per cent during July-March of FY2017-18). In fact, the growth rate was negative (-) 4.2 per cent for March of FY2017-18 on a month-on-month basis.

Figure 2.5

Export Scenario after Three Quarters of FY2017-18

(in Per cent Growth)



Source: Authors' calculations from Export Promotion Bureau (EPB) data.

Import payments driven by food grains and capital goods

During the July–February period of FY2017-18, import payments registered a significant 26.2 per cent growth over the corresponding period of FY2016-17. This surge in import growth was primarily driven by foodgrains and capital goods which recorded 186.7 and 28.2 per cent growth respectively during the considered timeframe. Of the various foodgrains, higher import of rice continued in the backdrop of lower production, higher domestic retail prices, depleted public stock and reduced tariff. Import payments for capital machineries and other capital goods posted 42.3 per cent and 20.7 per cent growth respectively during the July–February period of FY2017-18. Intermediate goods, which account for nearly 51.0 per cent of the total import payment, exhibited a growth of 19.8 per cent. Within this category, raw cotton, yarn, and fabrics posted growth of 39.4, 18.9 and 15.2 per cent respectively. Of the consumer goods, edible oil and sugar recorded considerable import growth despite lower global prices of these commodities. Import payments for 'others import items (not specific elsewhere)' rose by 30.4 per cent during July–February of FY2017-18 when compared to the corresponding period of FY2016-17. Taking cue from these trends, earlier apprehension of CPD (2018) concerning overstocking of certain commodities, trade misinvoicing and capital flight remains valid and must receive policy attention.

Upturn in outward migration is reflected partially in increased remittance inflow

Outward migration from Bangladesh experienced a 5.2 per cent rise during July–March of FY2017-18; compared to the corresponding period of FY2016-17 the number rose to a total of 6,92,236. Nearly half of the aforesaid migrants were destined for Saudi Arabia. Average monthly migration during July–March of FY2017-18 was 76,915, which is the highest since FY2011-12 for the considered timeframe. Similarly, remittance inflow to Bangladesh registered a 17.3 per cent increase during July–March of FY2017-18. However, this impressive growth ought to be seen in the backdrop of the dismal scenario prevailed in FY2016-17. Average monthly remittance inflow during July-March of FY2017-18 was United States Dollar (USD) 1,196 million, which is USD 33 million lower than average monthly inflow for the July–March period of FY2015-16.

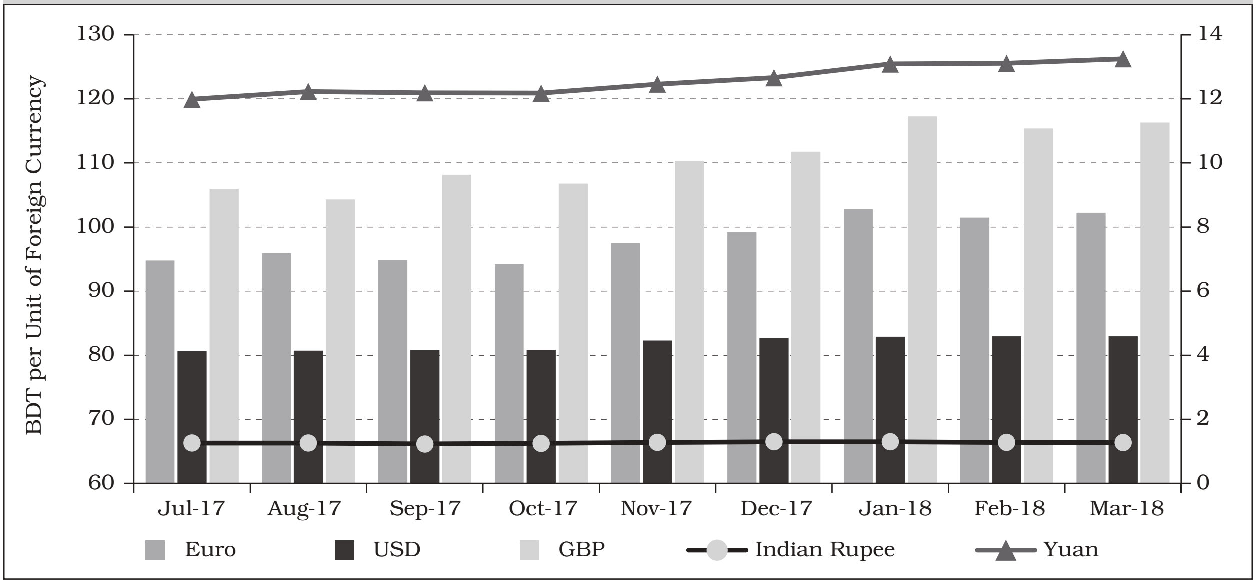
BoP situation is not favourable as both current account and overall balance have crossed into the negative zone

The adverse impact of escalated imports payment against relatively less impressive performance of export and remittances, is evident from the BoP scenario. Up to February of FY2017-18, trade balance stood at negative USD (-) 11.7 billion, which was almost twice the deficit than that of the corresponding period of FY2016-17. Current account balance, despite the aforesaid decent performance in export earnings and remittances, reached USD (-) 6.3 billion during July-February of FY2017-18. This figure was about USD (-) 1.0 billion during the corresponding period of FY2016-17. Within the financial account, net foreign direct investment (FDI) inflows recorded an insignificant 0.8 per cent growth. However, this was bolstered by a strong 86.3 per cent growth in medium and long-term (MLT) loans, and consequently, financial account balance rose to USD 5.7 billion. It must be taken into cognisance that, financial account surplus, thanks to hefty flow of MLT loans, is also partially linked with higher trade deficit. Indeed, higher imports payments was primarily required for imports related to the development projects which are often being financed through foreign inflows. Following these aforementioned trends, Bangladesh's overall BoP stood close to negative USD (-) 1.0 billion as of February FY2017-18, which was a surplus to the tune of USD 2.4 billion during the same period of FY2016-17. It appears that, in the backdrop of the growing imports, Bangladesh's overall balance for the entire fiscal year is going to be in the negative terrain for the first time since FY2010-11.

Pressure on BoP is translated into depreciation of BDT against major currencies and slowdown in foreign exchange reserve accumulation

Over the July–March timeframe of FY2017-18, exchange rate of BDT against Indian Rupee has remained fairly stable. Apart from this, BDT has shown a generally depreciating trend against other major currencies

Figure 2.6
Exchange Rate of BDT against Selected Currencies



Source: Authors' compilations from Bangladesh Bank data.
Note: Indian Rupee and Chinese Yuan are shown in the right vertical axis.

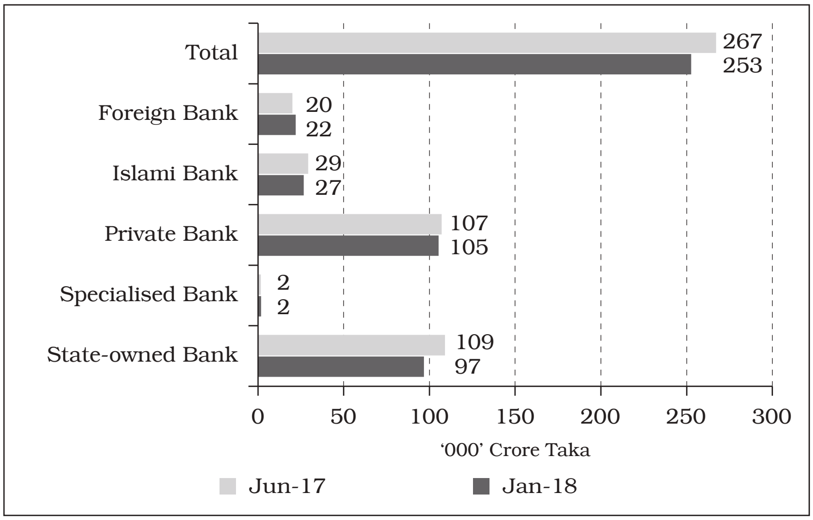
such as USD, Euro, Great Britain Pound (GBP) and Chinese Yuan (Figure 2.6). In fact, the import settlement rate, or bills for collection (BC) selling rate, of USD was BDT 83.5 as of 10 April 2018, exhibiting a 3.2 per cent increase in the exchange rate from a year ago. It may be assumed that the increased pressure on BoP has translated into depreciation of BDT. Similar trend was also found from the analysis of real effective exchange rate (CPD, 2018). As a consequence of the overall deficit, foreign exchange reserves came down to about USD 33.0 billion as of 11 April 2018 from the earlier USD 33.5 billion as of 30 June 2017.

2.3 FROM EXCESS LIQUIDITY TO LIQUIDITY CRUNCH: THE CURIOUS CASE OF THE BANKING SECTOR

The banking sector of Bangladesh continued to be in a state of disarray as the FY2017-18 draws to a close. In 2017, state-owned commercial banks (SCBs) and development finance institutions (DFIs) failed to meet the BASEL III requirement of maintaining capital to risk weighted asset ratio of 10 per cent (Bangladesh Bank, 2017). At the same time, both categories of banks had more than 20 per cent NPLs. These banks also recorded very high expenditure to income ratios in 2017, reflecting a poor state of management. Indeed, DFIs had an expenditure-income ratio greater than 100 for the third year in a row with consequent continuation of losses suffered. The foreign commercial banks, to compare, made the highest profit; however, their interest rate spread has consistently been higher than the average, and was above 6 per cent in 2017 (Bangladesh Bank, 2018). The overall NPL ratio in the banking sector also posted some rise, from 10.1 per cent in June 2017 to 10.7 per cent in September 2017.

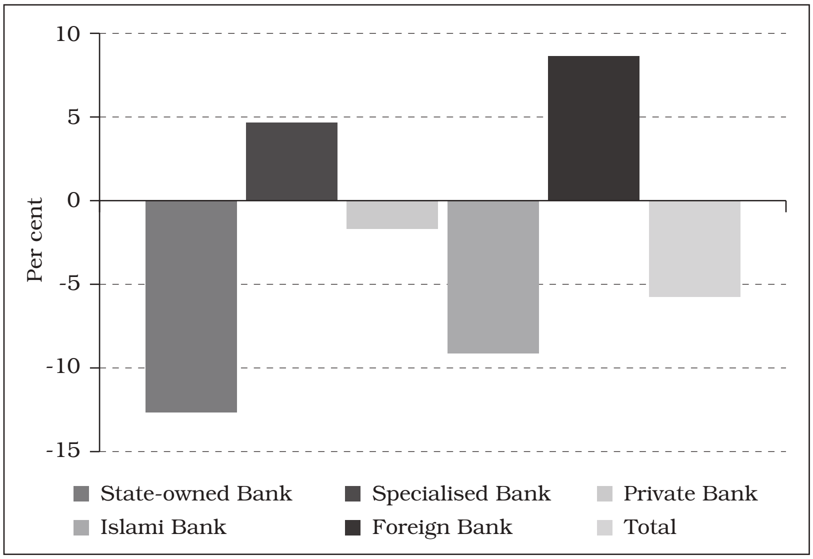
Apart from DFIs, banks in general did not face any major liquidity shortage in the early months of 2017. In fact, a build-up of excess liquidity in the banking sector led to concerns regarding the state of the general investment climate of the economy. However, liquidity position of majority of banks started to deteriorate thereon and by January 2018, there was widespread liquidity shortage in the banking sector (Figures 2.7 and 2.8).

Figure 2.7
Total Liquid Assets



Source: Major Economic Indicators, March 2018, Bangladesh Bank.

Figure 2.8
Change in Liquid Assets between June 2017 and January 2018



Source: Major Economic Indicators, March 2018, Bangladesh Bank.

The sudden shift in the scenario from an excess liquidity situation to liquidity crunch in the banking sector begs the question where the money has actually gone. Questions have been raised concerning the quality of loans paid and the apprehension about a large part of loans in the end turning out to be bad debts. The central bank should also investigate the veracity of whether the recent liquidity crunch was originated from loan defaulters who chose to repay their loans from SCBs by borrowing from private commercial banks (PCBs).

As may be recalled, the recent liquidity crisis initially started in the scam-ridden fourth generation commercial banks. This problem has become more pervasive because of the knock-on impact on other banks, either through depositor behaviour or over cautious stance by the banks in the backdrop of rising NPL. In view of this situation, and to inject more cash in the system, the central bank issued a circular on 3 April 2018 that the minimum CRR was to be reduced from 6.5 per cent to 5.5 per cent bi-weekly, and from 6 per cent to 5 per cent daily, starting from 15 April 2018. Additionally, it was decided that government agencies would increase their deposit of funds in PCBs from 25 per cent to 50 per cent. A more worrying sign is that these amendments were made primarily due to pressure from the powerful banking lobby bypassing the central bank. This has seriously undermined the independence of the central bank and has dented its credibility.

The attempt on the part of the MoF to rescue the PCBs in this way was, in fact, similar to government's recapitalisation support for the SCBs. These steps, taken irrespective of performance record of the PCBs was not justified under any pretext. Indeed, this was likely to encourage poorly performing banks to continue with their business-as-usual practices.

The decision to reduce the CRR is contradictory to the contractionary monetary policy announced by the Bangladesh Bank for January–June 2018. Reduction of the CRR will free up approximately BDT 101 billion of additional funds for banks to lend out. Such quantitative easing could lead to inflationary pressures, particularly if the loans against this money are of doubtful quality and goods and services are not produced in view of these. Particularly in an election year when there is a natural tendency for increased money supply the need for caution to be exercised should be much higher. Research has shown that in Bangladesh, a 1 per cent increase in the supply of broad money could increase the CPI by 0.80 per cent (Bahar and Rahman, 2014). The CRR change will likely affect the interest rates in the banking sector which is becoming visible in the economy. The apprehension is that the deposit rate may fall faster and to a larger extent than the lending rates. More worrying is the fact that the reduction in the CRR may encourage banks to lend more aggressively, and indiscriminately. This will raise the risk of increase in NPLs. The recent decision to allow higher share of government funds in banks could result in the money going to poor performing ones. For example, in December 2017, The Farmers Bank Ltd. failed to pay BDT 229 crore to Bangladesh Climate Change Trust Fund (BCCTF) on maturity of its fixed term deposits. There should have been certain conditionalities attached to this newly introduced enhanced threshold of receiving government fund.

As for the SCBs, the government has continued to inject money into these banks. From FY2008-09 to FY2016-17, the government had allocated BDT 15,705 crore for the recapitalisation of state-owned banks. This support, however, has not been translated into improvement in the performance of these banks; rather the amount of NPLs has piled up on a continuing basis over the past years. In all likelihood this monetary infusion will continue in the upcoming budget as well.

2.3.1 Recommendations

The core problem of the banking sector lies in the lack of good governance and the political commitment to remedy the emergent situation. While these issues are to be dealt with by keeping the medium-term strategic perspective in the purview, the government should take a number of immediate measures to overcome some of the disquieting current developments afflicting the banking sector of the country. Measures which have budgetary implications are suggested here.

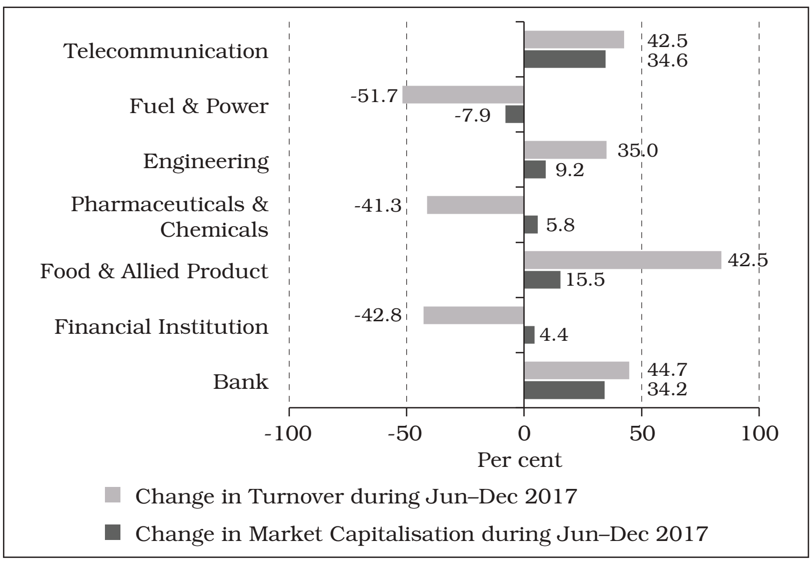
- Recapitalisation of SCBs year after year has to be stopped. Such practice of bailing out the losing banks with public money is economically unjustified and morally incorrect. There has to be a transparent exercise to find out what has actually been achieved through such funds, and when and how this type of recapitalisation of banks will be brought to an end.
- The decision to keep 50 per cent government funds with private banks goes against the spirit of central bank's monetary policy. Access to additional government funds as deposits should be contingent on performance of the particular private bank. Only banks with less than 5 per cent NPLs should be eligible for the additional available funds from government entities.
- CPD has earlier argued for setting up an independent commission for the banking sector in view of addressing emerging challenges. The broad terms of reference (ToR) of the commission will be to critically assess the problems and weaknesses of the banking industry. Such a commission will suggest concrete recommendations for prudential banking, and prepare guidelines regarding management, automation, risk management, and internal control. The budget should allocate adequate funds for setting up this commission.

2.4 BULLISH AND BEARISH TRENDS IN THE CAPITAL MARKET: ROLE OF INSTITUTIONAL INVESTORS AND REGULATORS

Despite some hiccups, the capital market has maintained bullish trends (in terms of key indicators) in the course of calendar year 2017. Key indices of the Dhaka Stock Exchange (DSE) [i.e. DSE Broad Index (DSEX), DSE30 and DSEX Shariah Index (DSES)] have registered a rise of 10–12 per cent between January 2017 and January 2018, although total turnover declined by 70 per cent during the same period. Major companies in the DSE such as those related to the banking and telecommunication sector, which comprises over 38 per cent of total market share in the DSE, have experienced a significant rise both in terms of market capitalisation and turnover during the June–December 2017 period (Figure 2.9). The bullish trend in the stock exchange is mainly attributed to the significant amount of investment made by institutional investors, particularly by bank and non-bank financial institutions prior to and during this period. After getting the permission in July 2016 for transforming loans into paid-up capital of bank subsidiaries, and thereby reducing the exposure of banks' investment in the capital market within the permissible limit, a number of banks got the opportunity to make additional investment in the capital market.[10] In the backdrop of the very high amount of excess liquidity in the banking sector in 2017 (which amounted to Tk. 1.06 trillion crore at the end of June 2017), banks had made large investments in the stock market. Indeed, this contributed, in part, to the bullish trend in the market. According to reports published in national dailies, as many as 21 banks were alleged to have invested in the stock market beyond their exposure limit in this period; this was exposed in an investigation carried out by the central bank.[11] Alongside that, some of the banks misused the weekly reporting system by making investment exceeding the exposure limit. The system was manipulated by exceeding the limit for a number of working days in order to make short-term gains. Adjustments were made just before the weekly reporting to the central bank. This type of market behaviour reflects a lack of responsibility on the part of banks as institutional investors in the capital market. According to the Bangladesh Bank, in the first half of FY2017-18 (July–December 2017) banks have disbursed about Tk. 13,100 crore as credit to the private sector, which exceeded the target set for this period; a part of this credit is likely to be invested in the capital market by banks.

Figure 2.9

Changes in Market Capitalisation and Turnover During June–December 2017



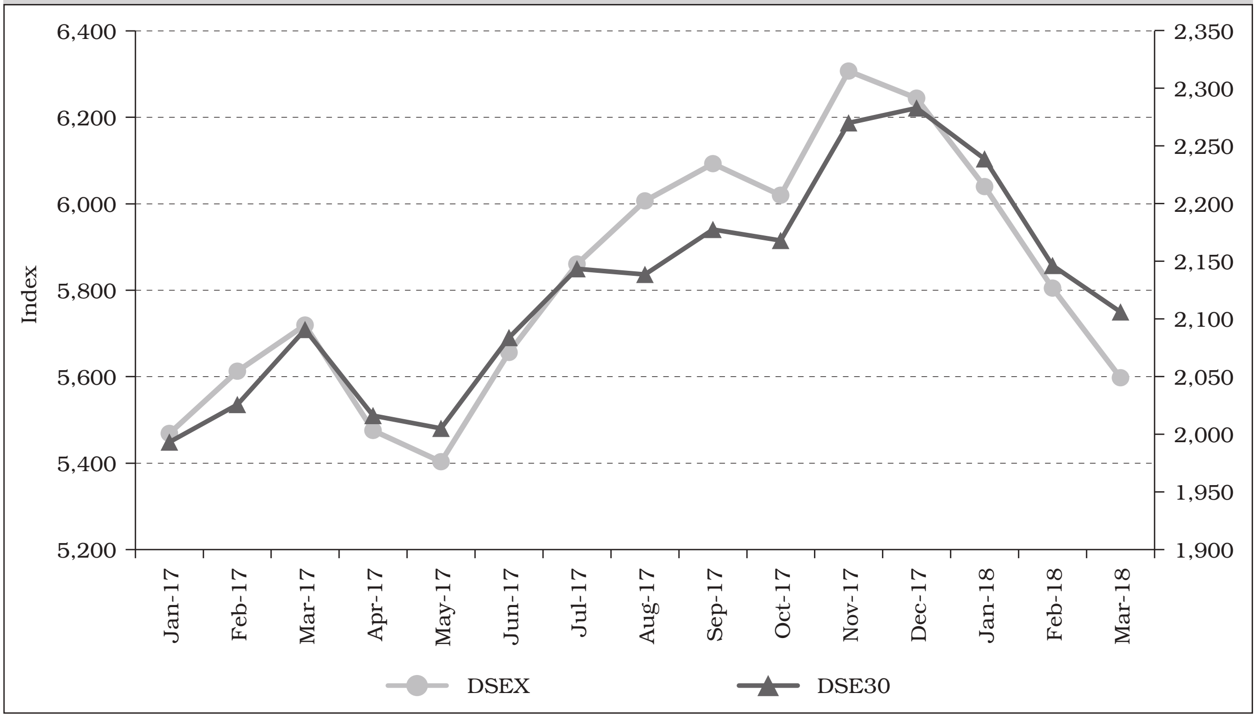
Source: Dhaka Stock Exchange (DSE) data.

[10] Loans worth Tk. 19.84 billion of 13 banks turned out to be paid-up capital of their subsidiaries (Prothom Alo, 9 October 2017). This allowed them to lower the total investment in the stock market.

[11] Exposure limit for banks to invest in the stock market: 25 per cent of its paid-up capital, share premium, statutory reserve and retained earnings.

Figure 2.10

Trends of Indices of DSEX and DSE30 During January 2017–March 2018



Source: Dhaka Stock Exchange (DSE) data.

Note: DSE30 is shown in the right vertical axis. DSEX and DSE30 data for the months of February 2018 and March 2018 were taken from the month-end figures as on 28 February 2018 and 29 March 2018, respectively.

The bullish trend in the market had given way to a bearish outlook since December 2017 (Figure 2.10). With a view to tightening the money supply further during the second half (H2) of FY2017-18, the monetary policy for H2 of FY2017-18 had set the target of lowering the rate of credit growth (from 18.1 per cent to 16.2 per cent). The ADR was also supposed to be reduced to 83.1 per cent (which was over 85 per cent) by June 2018. The announcement pushed banks to sell a part of their shares in order to comply with new targets set for credit growth and ADR. It is important to investigate which banks had sold their shares in this time and how much of that sale was related to complying with new directives of the central bank; most importantly, whether some of the banks as institutional investors played a responsible role to stabilise the market or not. During this period, the central bank, as regulator, had moved back from its own monetary policy stance of tightening money supply and credit growth—by extending the timeline for adjustment of ADR twice; first till December 2018 and the second till March 2019, and also reducing the CRR by one percentage point. These steps helped make about Tk. 10,000 crore available to the commercial banks for credit disbursement. A new directive allowed public agencies to deposit a higher share of their savings in PCBs (raised from 25 per cent of funds to 50 per cent) in order to create additional funds for credit disbursement. This type of initiative taken by the central bank raises questions about the efficacy of the monetary policy to adjust the market situation, particularly in view of the exposure of commercial banks to the capital market. It also exposed the questionable role played by commercial banks in the capital market as institutional investors.

In 2017, the long-awaited process for completion of demutualisation of the DSE had been revived. As a result, the DSE was able to select its institutional partner who would buy 25 per cent of the shares of its brokers (45 crore shares), and also will make investment for strengthening the market. The DSE has reviewed two proposals—a) Consortium of Shanghai Stock Exchange and Shenzhen Stock Exchange and b) Consortium of National Stock Exchange of India and NASDAQ. The offers made in the two proposals are quite different, particularly in terms of the offer price to purchase shares (Tk. 15 vs. Tk. 22 per share), making investment in improving technologies, requesting to get directorship on the Board, membership in various committees and getting some of the top management positions etc. Because of better offer price, specific proposal for investment in developing technologies, the DSE selected the proposal submitted by the Chinese Consortium. Following review of the Chinese proposal, the Bangladesh Securities Exchange Commission (BSEC) advised to drop its request to be member of different committees. This was important to ensure compliance with related laws of the BSEC.

2.4.1 Proposals

Central bank needs to increase its vigilance in monitoring activities of banks in the capital market

The central bank needs to be more proactive and vigilant in monitoring activities of Banks in the stock market. Introduction of daily reporting system of banks' transactions in the stock market, instead of weekly reporting system, has made the reporting system more transparent. The central bank needs to respond quickly to identify market irregularities and to take action against the irregularities on an urgent basis. On the contrary, delaying enforcement of orders, particularly those related to market irregularities, give a wrong signal about the enforcement capacity of the central bank. It is important to investigate whether banks are playing their assigned role as institutional investors, in case of buying and selling of shares, particularly at the time of bullish and bearish trends in the market during 2017 and also afterwards.

BSEC and central bank should work together to prepare a code for institutional investors

Banks, as institutional investors, have a major role to play to stabilise the stock market and also to create confidence among the minority shareholders. Banks should behave responsively in the market, particularly at the time of bullish and bearish trends, and the attendant volatility in the market. The recent behaviour of banks, both at the time of bullish and bearish situations, have raised questions about their role in the market. In this backdrop, BSEC and Bangladesh Bank may jointly prepare a code of conduct for institutional investors in the stock market. This type of code is available in other matured markets such as Malaysia and India.

Regular review and monitoring of the activities of the institutional partner of DSE will be required

Working with a reputed international stock exchange as institutional partner will be a new experience for the DSE. The rules and practices followed by DSE is likely to be different from those of the institutional partner. For example, the Shanghai Stock Exchange is governed under a controlled/centralised governance system and is not demutualised. Hence, the Shanghai Stock Exchange needs to accommodate rules, regulations and practices of the demutualised DSE. Hence, review and monitoring of the activities of the institutional partner would help streamline their activities and support smooth operation of DSE. Moreover, it is also important to ensure timely implementation of the various commitments made by the institutional partner, particularly with regard to investment in technologies and human resource development etc. Given the weak infrastructural facility and emergent needs of the market, DSE will be required to invest in new technologies for setting up the derivatives market, bond market, market maker and central clearing company etc.

2.5 INCENTIVES FOR EXPORT-ORIENTED SECTORS: RECOMMENDATIONS FOR FY2018-19 BUDGET

One of the core targets of the Seventh Five Year Plan (7FYP) is to promote industrialisation through favourable trade policy regime. Government envisaged to raise export earnings to USD 60 billion by FY2020-21. Even if the annual target of USD 37.5 billion (8.2 per cent growth) set for FY2017-18 is realised to the fullest extent, export earnings will need to grow at about 17 per cent annually over the next three years to attain the target set for FY2020-21. This will indeed be a herculean task. The challenge is exacerbated by rising uncertainties in the global market (Brexit, growing protectionism which could lead to a trade war between USA and China with consequent adverse implications for global trade), growing domestic costs of production (possibility of upward revision in administrative prices of energy and revision of the minimum wages), heightened competition (including re-emergence of India with additional policy support). In this backdrop, energetic and innovative steps will need to be taken if the pace of export growth is to be accelerated. It is from this perspective that there is a need to revise the fiscal incentives provided to the export-oriented sectors in Bangladesh to raise their efficacy to provide strategic support to export-oriented industries and activities.

2.5.1 Current State and Policy Space

A review of fiscal incentives in Bangladesh indicates that historically the larger part of fiscal incentives has gone to the RMG sector. This is not surprising. RMG accounts for, by far, the largest share in Bangladesh's exports. While its share in total export was 78.1 per cent in FY2011-12, the corresponding figure stood at 80.8 per cent at the end of FY2016-17. A number of new items (non-traditional) has emerged over the recent past; whilst the share in total export has not been significant, in terms of value and pace of growth, their performance must be taken cognisant of (Table 2.8). This reinforces the argument to recalibrate the fiscal incentive package in view of emerging demands.

Table 2.8

Growth of Major Export-Oriented Sectors in Bangladesh over Last Five Years

Product	FY12	FY17	FY17 Share	Ratio FY17/FY12	CAGR*
	in million USD				
RMG Sector	**19,090**	**28,150**	**80.8**	**1.47**	**8.1**
Knitwear	9,486	13,757	39.5	1.45	7.7
Woven garments	9,603	14,393	41.3	1.50	8.4
Non-RMG sector	**5,212**	**6,685**	**19.2**	**1.28**	**5.1**
Leather and leather product (chapters 41–43 and 6403)	664	1,234	3.5	1.86	13.2
Footwear (chapter 64) excluding 6403	102	241	0.7	2.37	18.9
Jute and jute good (chapter 53 and 6305)	967	962	2.8	0.99	-0.1
Engineering product (chapters 71–88)	375	689	2.0	1.83	12.9
Agriculture product (chapters 06–24)	403	553	1.6	1.37	6.6
Shrimp	472	446	1.3	0.95	-1.1
Headgear	53	187	0.5	3.51	28.6
Computer service	71	179	0.5	2.53	20.4
Pharmaceuticals	48	89	0.3	1.85	13.1
Plastic product (chapter 39)	89	117	0.3	1.32	5.7
Paper and paper product (chapter 48)	28	57	0.2	2.05	15.4
Ship, boat and floating structure (chapter 89)	46	66	0.2	1.43	7.4
Rubber (chapter 40)	16	28	0.1	1.75	11.9
Other non-RMG products	1,868	1,812	5.2	0.97	-0.6
Total export	**24,302**	**34,835**	**100.0**	**1.43**	**7.5**

Source: Authors' calculations based on Export Promotion Bureau (EPB) data.
Note: *Compound annual growth rate (CAGR).

The Ministry of Commerce (MoC) periodically formulates Bangladesh's Export Policy, from medium term (3-year period) perspective with a view to incentivise export-oriented activities in the economy and remove anti-export bias in the policies (or at least to mitigate/compensate for the anti-export bias). The Export Policy 2015-18 had identified a number of non-traditional exports which had significant export potentials.

These included software and IT enable services (ITES), footwear and leather products, ship and ocean-going vehicles, jute goods, agro-based products, pharmaceuticals, furniture and a number of labour-intensive products with export potentials. The Policy also identified a number of thrust sectors which were earmarked for special support in view of their potential to contribute to the export basket of the country. These included electronic products, light engineering, frozen fish, printing and packaging, rubber, silk products, handicrafts and handloom industries.

To support exporters and export-oriented entrepreneurs and help them remain competitive in the global market, successive governments in Bangladesh have put in place an array of fiscal instruments. These were in the form of export subsidy (cash incentives)[12], bonded warehouse and duty drawback facilities (through selectively issuance of bond license), tax rebate, soft and concessional short-term commercial loans, support from export development fund and export promotion fund, export retention quota, special income tax rate, reduced tax rate and a host of other support measures. Some of the incentives are export-product specific; others product-neutral. Some measures are instrumental and aimed at achieving important 7FYP objectives relating to product and market diversification and growth of exports, through allocations for skills upgradation, improvement of technology infusion, and development of trade facilitation.

The need to revisit the incentive structure and resources allocated for incentives is also called for in view of recent policy changes by some of Bangladesh's competitors in the global market. Box 2.1 presents some information about incentives for export-oriented industries provided by India in recent

Box 2.1

Export Incentives in Indian Budgets: FY2017-FY2019

FY2017 (1 April 2016–31 March 2017)

- Rs. 6,000 crore special package for the textile and apparel sector
  - Rs. 5,500 crore is for an additional 5 per cent duty drawback for garments
  - The remaining Rs. 500 crore is for additional incentives under amended Technology Upgradation Funds (TUF) scheme
- These initiatives are expected to increase exports by USD 30 billion and help attract investment worth Rs. 74,000 crore in next three years
- Government will bear the entire employer's contribution of 12 per cent under the Employers Provident Fund (EPF) scheme – additional cost of Rs. 1,170 (early provision was 8.33 per cent)

FY2018 (1 April 2017–31 March 2018)

- Rs. 6,000 crore package for employment generation and promotion of textile exports
- A set of reforms are envisaged including simplified labour laws
- Steps for technology upgradation

Mid-Term Review of Foreign Trade Policy 2015–2020 (December 2017)

- Additional fiscal incentives of around Rs. 8,500 crore under Merchandise Exports from India Scheme (MEIS) and Services Exports from India Scheme (SEIS)
- Incentive rates for the garments and made-ups have been enhanced to 4 per cent of value of exports from 2 per cent to offset the negative effect of GST since 1 July 2017 (will incur additional annual incentive of Rs. 2,743 crore)
- 2 per cent additional incentive for other micro small and medium enterprises (MSMEs) and labour-intensive industries (additional annual incentive of Rs. 4,567 crore)
- For reducing lead time, initiatives such as (i) testing of samples for drawback purpose, (ii) introduction of e-sealing facility, were undertaken

FY2019 (1 April 2018–31 March 2019)

- A comprehensive textile sector package for apparel and made-ups to the tune of Rs. 7,148 crore
- Government will continue to contribute 12 per cent of the wages of the new employees in the EPF
- Increased the funds allocated under the TUF scheme from Rs. 2,013 crore in FY2017-18 to Rs. 2,300 crore for FY2018-19
- Reduced income tax rate of 25 per cent for MSMEs (with turnover up to Rs. 250 crore in FY2016-17)

[12] It is to be noted that such cash incentives are provided only to those exporters who do not avail of the bonded warehouse facility or the duty drawback facility.

times particularly in view of offsetting some of the negative implications of introduction of the goods and services tax (GST) in 2017.

2.5.2 Review of Major Incentive Tools

Special bonded warehouse facilities

Bonded warehouse facilities, a special license scheme issued by Customs Bond Commissionerate (CBC), can be availed of by 100 per cent export-oriented industries. The bond facility allows the beneficiaries to get duty-free access when importing raw materials to be used only for exportable products. The facility has traditionally been enjoyed by the RMG exporters and, to some extent, by exporters of leather products. While in theory this facility is supposedly open for all 100 per cent export-oriented industries, real access has been quite limited. Government incurs a significant burden in the form of revenue forgone particularly when import duties on the bond products for the domestic tariff area is high. Realising the potential of the leather sector, the government has recently carried out a study to identify challenges faced by the sector in availing the bonded warehouse facilities. The study has come up with recommendations to remove the bottlenecks and facilitate access. CPD proposes that the aforesaid plan should be implemented on a priority basis in view of the significant export potential of this sector and in the context of the challenges with which the sector is confronted with. In continuation to this effort, government should formulate a medium-term plan for the thrust sectors to benefit from the special bonded warehouse facilities.

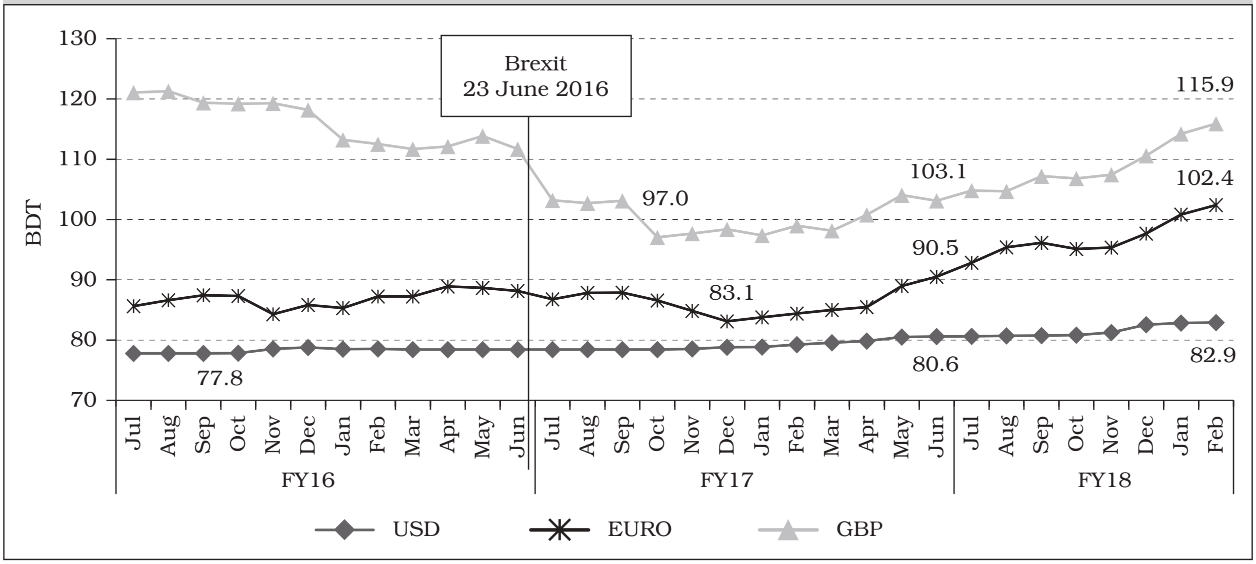
Whilst misuse of bond facilities is a concern, this should be addressed by strengthening both monitoring and enforcement and by bringing the abusers to justice; and not by limiting access to special bonded warehouse. Indeed, till now the facility has been availed of only by a few exporters outside the RMG sector. Also, a significant part of the issued licenses remained unutilised or inactive. It is felt that harassment by the bond officials and misuse of bond by the exporters—both concerns need to be addressed expeditiously. In case of RMGs, Bangladesh Garment Manufacturers and Exporters Association (BGMEA) and Bangladesh Knitwear Manufacturers and Exporters Association (BKMEA) issue the required utilisation declaration (UD) certificate on behalf of the NBR to facilitate imports of duty-free raw materials for exports under the facility. CBC has to depend on these certificates as the organisation does not have technical expertise to issue the certificate. There is widespread allegation about misuse of the facility. Whilst empowering the BGMEA with the authority to issue UD certificate was a right policy step, CBC should have the expertise and willingness to exercise due diligence. At present, the bond authority has shortage of technical expertise and human resources to carry out its responsibility. Adequate budgetary allocations should be made in FY2018-19 budget to improve the situation. The Bond Commissionerate needs to be connected with the central customs data automation process (ASYCUDA) to check fabrication of UD certificates and misuse of duty-free import facility by some unscrupulous exporters. The initiatives taken by the NBR to introduce e-UD and e-EXP are welcome steps which need to be prioritised and adequately supported. This will entail coordination among BGMEA/BKMEA, Customs stations, Bond Commissionerate and the Bangladesh Bank. Bond Commissionerate should also regularly update the harmonised system (HS) code list to facilitate import of duty-free raw materials (after proper validation) as imports by enterprises are ever changing and imports of new and differentiated raw material inputs ought to be encouraged for product diversification.

Cash incentives

Government provides significant amount of fiscal support in the form of export subsidies and cash incentives to incentivise exporters of selected sectors with promise and potential. In FY2017-18, these allocations were to the tune of Tk. 4,500 crore. In FY2016-17, about Tk. 4,395 crore was disbursed against the same amount of allocation. At present, 27 sectors receive cash incentives in the range of between 2 per cent and 20 per cent based on certain criteria. A large share of the incentives is enjoyed by major export sectors such as RMGs.

Figure 2.11

Recent Appreciation of USD, Euro and GBP against BDT



Source: Compiled from Bangladesh Bank data.

The scheme provides incentives to RMG sector and exporters associated with the sector, in various forms. A supplier of raw materials who is a member of Bangladesh Textile Mills Association (BTMA) receives 4 per cent cash incentive calculated on net free-on-board (f.o.b) of the proportionate value of the export. This incentivises the backward linkages industries and enhances domestic value addition. On the other hand, RMG exporters get additional incentives of 3 per cent for product and market diversification. There are also additional packages for textile small and medium enterprises (SMEs).

Special incentives are also introduced from time to time in view of both challenges and opportunities. RMG exporters to the EU market are currently receiving 2 per cent additional cash incentive (initiated in FY2016-17). The scheme was introduced in view of sharp depreciation of the Euro and GBP following the Brexit referendum in June 2016. However, exchange rates of Euro and GBP appreciated against BDT (Figure 2.11). In February 2018, Euro and GBP have appreciated by 21.3 per cent and 17.1 per cent, respectively against the corresponding month of 2017. This scheme may be revisited in view of the recent developments.

Among other sectors, government has put emphasis on leather sector as a potential export-oriented industry. Government is planning to continue 15 per cent cash subsidy for leather exports over the next 5 years to reach its export target of USD 5 billion by 2021. Following the recent relocation of major leather industries, the sector is facing a number of challenges which has resulted in a dip in export performance of this promising sector. A comprehensive plan needs to be designed to incentivise leather products export which could ease access to bonded warehouse facilities, support to ensure (environment and labour related) compliance and facilitate supply of skilled workforce. Capacity of Bangladesh Standards and Testing Institution (BSTI) should be developed in the area of standard certification. Predictability of incentives should be ensured.

Misuse of export subsidy facility must be addressed with proper enforcement of policies. Recently, the Bangladesh Bank has investigated a number of cases where incentives were misused. Instances included the followings: receiving incentive before getting the export bill, export bill repatriated, channelling export receipt through money exchange houses, miscalculation of value added part while using local raw materials, claiming incentives while exporting to traditional markets, and misuse of bonded warehouse facilities. CPD recommends closer cooperation among involved stakeholders including government agencies, business associations, NBR, dealing banks and Bangladesh Bank. Budgetary allocations should be increased to enhance data access, human resource development and effective vigilance to address the attendant tasks.

2.5.3 Concluding Remarks

In the light of Bangladesh's graduation from the least developed country (LDC) group by 2024, and the discontinuation of most of the preferential treatment and market access facilities including the Everything But Arms by 2027, there is an urgent need to revisit the export incentive schemes in place. This is needed by keeping in purview the LDC graduation status and also to make the incentives more targeted and effective and to check abuse.

The restructured incentive package could include allocation for targeted skills development schemes for workers in export-oriented industries, contribution to employee's contribution fund, redefining non-traditional exports, strengthening of institutions related to enforcing export incentives, calibrating incentives in view of market dynamics, raising efficacy of the bond system and more predictability in the incentive regime.

2.6 SPECIAL ECONOMIC ZONES: PRIORITIES TO SET UP 'MODEL' SEZs

In recent years, issues related to establishment of Special Economic Zones (SEZs) have been receiving increased attention from the policymakers, for several reasons. One key reason is the urgency of addressing the 'infrastructure deficit'. The diverse range of business models and financing arrangements that the SEZs could potentially accommodate is another reason. The scope for providing 'one stop service' to potential investors in the SEZs, is an added advantage. The interest of policymakers in Bangladesh at the highest level, to go for the SEZs, was reflected through the setting up of a separate implementing authority, the Bangladesh Economic Zones Authority (BEZA) in 2013. BEZA was mandated with the task of putting in place 100 SEZs by 2030. A variable geometry of combinations with participation of the Government of Bangladesh (GoB), the private sector and partner countries were to be involved in developing the SEZs. It was perceived that availability of full-packaged infrastructure facilities will incentivise potential investors to invest in the SEZs once these are ready.

Regrettably, progress in setting up SEZs has been rather slow and behind the targeted timeline. Since the inception of the BEZA, a total of 76 SEZs have been identified, with specific locations. Twenty-two SEZs have been approved by the authority till date (MoF, 2017). Progress of work in the approved SEZs has been uneven. If a continuum of tasks such as undertaking feasibility studies, land development, construction of infrastructure facilities, and allotment of plots to investors are considered, these SEZs are at different stages of development.

Whilst a target was set to develop 20 SEZs by 2018[13], the progress of work till now leaves much to be desired. Only 10 SEZs have actually been earmarked for completion but no specific timelines have been set with respect to when these could be fully in operation (MoF, 2017). According to the ADP for FY2017-18, development work for only two SEZ projects (Jamalpur and Mirsarai) are currently under the purview of the ADP. However, allocation made for these two projects are not adequate for their completion in time. Even with full utilisation of the allocated budget for FY2017-18 (Tk. 140 crore), only 24.8 per cent of the total work may be completed by the end of the fiscal year. According to SANEM (2017), only four SEZs have completed 75 per cent of their total developmental work. Indeed, the progress in setting up the private SEZs is somewhat encouraging; a number of private SEZs have completed their initial work as regards land development. Some enterprises are at different stages of being established in a few private SEZs. Evidently, the task of getting a sizeable number of SEZs ready for operation ought to be given highest priority by concerned authorities. A few suggestions are being put forward in this connection.

[13]As stated by the General Manager of BEZA, Mostaque Hassan [Habib, T. B. (2016, November 25)]

2.6.1 Giving Priority to Establish Few 'Model' SEZs

BEZA should focus on setting up a few 'model' SEZs as a beginning, on a priority basis. This will give investors confidence about the new architecture, its ability to offer the promised facilities and services, and ensure quality of the facilities as per international standards; SEZs should also assure potential investors of its institutional capacity to address the challenges faced by them in such zones. Given mixed experiences at the global level as regards success of SEZs to deliver on what they promise, Model SEZs could serve as a good branding of Bangladesh as an SEZ hub for potential investors. These would also enable the BEZA to assess its strengths and weaknesses and how to address the attendant challenges in the best way. Based on the experience, BEZA would be able to remould and remodel its policies and practices. In this regard, BEZA could draw in rather discouraging experience of Bangladesh Small and Cottage Industries Corporation (BSCIC) and important learning from BEPZA.

2.6.2 Ensuring Access on an Equal Footing

BEZA envisages to develop zones and implement the projects under six different types of ownerships and arrangements: a) Government-owned; b) Private-owned; c) Government-to-Government (G2G); d) Public-Private Partnership (PPP); e) Specialised arrangement and, f) Established by corporations. In allocating the plots under its jurisdiction, BEZA should encourage non-traditional and emerging industries (e.g. light engineering industries, accessories industries, food-processing industries, agricultural machineries industries, chemical industries, ICT-based industries and MSMEs) and provide necessary infrastructural facilities and services that cater to their specific needs. In the case of industries with proven track records (e.g. RMG, footwear, leather, Pharmaceuticals, those with high value-added products) should be encouraged. Whilst special incentive packages do provide investors in SEZs with added advantage (besides unencumbered land), prudent management and due diligence must be applied so that incentive packages are not abused and misused. Otherwise, this could create serious disincentive for investors in the domestic tariff areas (DTAs). In this context, due caution must be deployed as regard misuse of tax holiday incentives, land speculation etc.

2.6.3 Provision of Adequate ADP Allocation

Considering the slow progress of the SEZ project-related work, ADP allocation for the SEZs should commensurate with the planned work. Adequate allocation should be made in the upcoming national budget for FY2018-19 which should align with the SEZ Master Plan for development. In this regard, establishing Model SEZs with provision of full package of infrastructure facilities, services and a supportive regulatory regime should receive priority.

2.6.4 Investment Promotion Should be Carried Out by a Single Authority

Presence of multiple authorities could potentially create confusion, lead to turf wars and delay the effectiveness of the SEZs. Currently, there are several investment promotion authorities in the country which include BEZA, BEPZA, BIDA, PPP Office, BSCIC and Hi-Tech Authority etc. These authorities were established at different points in time for particular sectors and demands of the economy, in order to address specific needs. A review of the activities of these authorities reveals that activities of some of the authorities have significant overlaps e.g. BEZA, BEPZA and PPP Office. Some of the activities could be centralised and others mandated to dedicated wing of the centralised authority. Serious thought should be given towards developing an institutional architecture that best suits the needs of the investors and entrepreneurs, in the multiple types of zones currently in existence in Bangladesh.

2.7 BUDGET FOR SOCIAL SECTOR: IS IT GOOD ENOUGH FOR INCLUSIVE GROWTH?

2.7.1 Introduction

The demand for higher investment in the social sector is understandably very high in countries such as Bangladesh. However, with limited resources and competing priorities, the government faces formidable challenge in allocating adequate resource for the competing sectors. However, what is disquieting is that despite the economic growth and the resultant higher allocative capacity of the government, the share of public expenditure in social sectors, particularly in health and education sectors, has not improved significantly. Consequently, both in terms of quality of education and health and their outcomes, Bangladesh is lagging behind. Despite quantitative improvements in the education and health sectors, the quality of education and health service continues to remain a major concern. The GoB is at present faced with the dual challenge of increasing public spending on health and education, and improving the standard of service and performance of these sectors. In view of the government's commitment to attain the SDGs, particularly in areas such as education (SDG 4: Education for all by 2030) and health (SDG 3: Ensuring healthy lives and promote wellbeing for all by 2030), the urgency to address the attendant deficits has risen manifold in the current context. Other SDGs, such as SDG 1 on eradication of poverty, SDG 2 on zero hunger and SDG 10 on reducing inequality are also linked to education and health. This is also important from the perspective of inclusive growth that Bangladesh aspires to achieve. Studies have shown that public spending on health and education can reduce inequality (Hur, 2014; Maitra and Mukhopadhyay, 2012).

In view of the above, allocations for the social sector demand to be revisited in the upcoming national budget. The following sections provide a narrative on the allocation of resources for the social sector in Bangladesh during the past few years, and present a set of recommendations for the upcoming budget for FY 2018-19.

2.7.2 Allocation for Health and Education

Whilst Bangladesh has increased budgetary allocations for the social sector over the past years (Figure 2.12), these not only fall short of the globally recommended targets but are also significantly low compared to the needs of the population. As Bangladesh embarks upon its middle-income journey and steps into LDC graduation process, both expectations and needs for higher allocation, and allocative and use-efficiency of resources are emerging as important factors. Table 2.9 presents various targets for health and education sectors and Bangladesh's progress towards achieving those facrtors.

Table 2.9
Target and Reality of the Social Sector

Source	Target	Where are we	What is needed
		Education	
7FYP, GED (2015)	Expenditure on education to be 3 per cent of GDP (7FYP)	Allocations on education were: • 2.25 per cent of GDP in FY2017-18 while actual expenditure was 2.32 per cent in FY2016-17.	The estimated budget for the education sector should be at least 2.84 per cent of GDP for
Incheon Declaration, 2015[14]	The Education 2030 Framework for Action set two benchmarks on domestic financing for education:		

(Table 2.9 contd.)

[14]UNESCO together with UNICEF, the World Bank, UNFPA, UNDP, UN Women and UNHCR organised the World Education Forum 2015 in Incheon, Republic of Korea, from 19–22 May 2015, hosted by the Republic of Korea. Over 1,600 participants from 160 countries adopted the Incheon Declaration for Education 2030, which sets out a new vision for education for the next fifteen years. Available from: http://www.uis.unesco.org/Education/Documents/incheon-framework-for-action-en.pdf

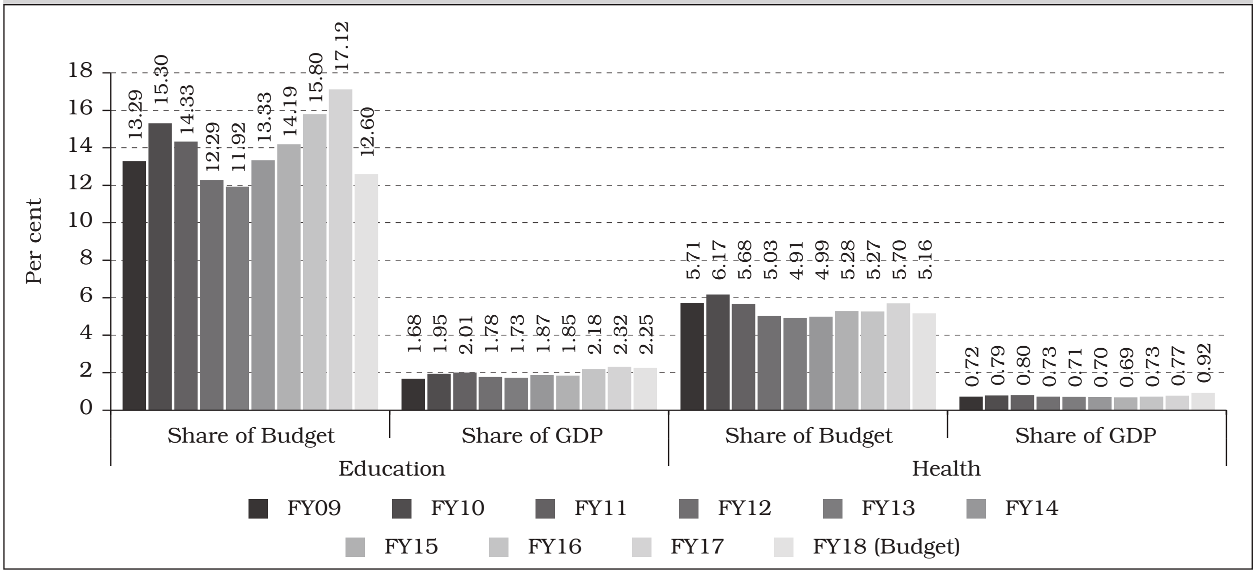
(Table 2.9 contd.)

Source	Target	Where are we	What is needed
	➢ 4–6 per cent of GDP ➢ 15–20 per cent of public expenditure.	• 12.6 per cent of total budget in FY2017-18, while actual expenditure was 17.1 per cent in FY2016-17.	FY2018-19, to achieve 3 per cent of GDP by FY2019-20 as set in 7FYP.
	Health		
7FYP, GED (2015)	Expenditure on health to be 1.2 per cent of GDP (7FYP)	Allocations on health were: • 0.92 per cent of GDP in FY2017-18 while the actual expenditure was 0.77 per cent in FY2016-17. • 5.16 per cent of budget in FY2017-18 while the actual expenditure was 5.7 per cent in FY2017-18.	Budget for the health sector should be at least 1.12 per cent of GDP in FY2018-19, to achieve the target of 1.2 per cent of GDP by FY2019-20 as set in 7FYP.
WHO observation	World Health Organization (WHO) considers a benchmark of 5 per cent of GDP or gross national income (GNI) of the country.		

Source: UNESCO *et al.* (2015); GED (2015); WHO (2003).

Figure 2.12

Expenditure on Education and Health as Percentage of GDP and Total Budget



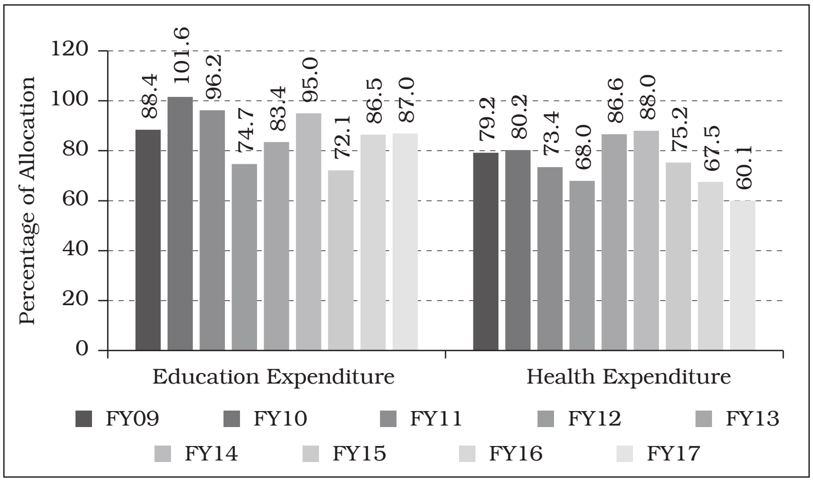
Source: Authors' calculations from various budget documents of Ministry of Finance (MoF); BBS (2018).
Note: Education budget includes figures only from Ministry of Primary and Mass Education, Secondary and Higher Education Division, and, Technical and Madrasah Education Division. For Education and Health sectors, figures up to FY17 represent actual expenditure, while for FY18, the figure is for budget allocation.

Utilisation of allocated resources for the social sector remains a problem. For example, in FY17, the government was able to spend about 87 per cent of total allocations for education and only about 60 per cent of total allocations for health (Figure 2.13). Indeed, actual expenditure for health in FY17, as share of sectoral allocations was the lowest in nine years. This clearly indicates the need for a renewed effort to enhance the capacity of concerned institutions to use the funds in an efficient manner.

It is to be noted that financial resources from foreign sources on account of health sector was lower in FY16 compared to FY12 (by 25 per cent), putting strain on domestic resources. Additionally, both education and health sectors are receiving less resources from the donors in recent years. Figure 2.14 shows that nearly 90 per cent of the resources had been pooled from domestic sources to finance education and health sectors in FY16. As Figure 2.14 indicates, shares of foreign assistance in the education and health sectors have declined from the high shares of FY13 to what these were in FY16.

Figure 2.13

Trend in Utilisation of Non-development Budget for Education and Health

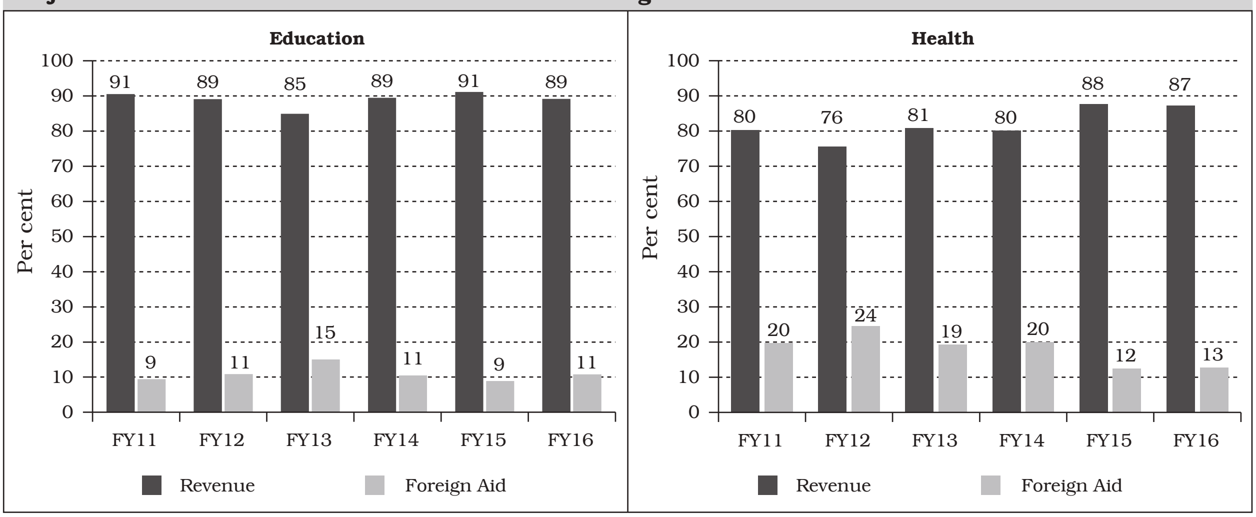


Source: Authors' calculations from Monthly Fiscal Report (various issues), Ministry of Finance (MoF).

Note: Figures represent actual expenditure as percentage of allocation.

Figure 2.14

Major Sources of Education and Healthcare Financing



Source: Authors' calculations from data on financial assistance available on Economic Relations Division (ERD), Ministry of Finance (MoF) website.

2.7.3 Challenges in the Education and Health Sectors

Several initiatives have been taken by the GoB to improve the performance of education and health sectors of Bangladesh. For example, the Health, Population and Nutrition Sector Development Programme (HPNSDP) Project (2011–17) was the largest health sector programme which was succeeded by HPNSDP 2017–22. In the education sector, the flagship programme is the Third Primary Education Development Programme (PEDP 3) which was to be implemented during 2011–16. PEDP 3 missed its original completion date by more than a year. The programme is now expected to be completed by June 2018. This programme is expected to be followed by PEDP 4 this year. The following section presents some findings as regards the abovementioned programmes on education and health sectors which will provide some indications about the budgetary initiatives needed in this connection.

Education budget in view of emerging needs

Bangladesh's progress in case of gross and net enrolment is satisfactory as these targets have been met (Annex Table 2.1). However, the target for dropout rates has not been achieved in FY2016-17. The quality of education has become a pressing issue in recent times as learning outcomes leave much to be desired. National School Assessment (NSA) 2015 shows that mean scores in 2015 for Bangla and Mathematics have fallen compared to 2013 across Grade III and Grade V (Annex Table 2.2). For example, in 2015, the mean scores achieved by Grade III and Grade V in Mathematics were 41 per cent and 10 per cent respectively, while in 2013, Grade III students had scored 58 per cent and Grade V scored 25 per cent in the two subjects (MoPME, 2017a). This can be explained by a number of factors including high student-teacher ratio (STR) and lack of qualified teachers.

The 7FYP aims for STR of 30:1 by 2018. While this has been achieved, there is significant variation within the country. For example, disaggregated data show that (Table 2.10) Cox's Bazar has the highest (49) STR in government primary schools (GPS). Among the 44 districts mentioned in the Annual Primary School Census (APSC) 2017, newly nationalised primary schools (NNPS) from 33 districts and GPS from 38 districts have STR above the national target (MoPME, 2017a).

Table 2.10

Districts with the Highest and Lowest STR

Level of STR	GPS		NNPS	
	District	STR	District	STR
Highest STR	Cox's Bazar	49	Noakhali	63
	Brahmanbaria	47	Cox's Bazar	60
	Rajbari	47	Narayangonj	57
Lowest STR	Pirojpur	24	Pirojpur	19
	Jhalokathi	24	Jhalokathi	18
	Rangamati	22	Rangamati	17

Source: MoPME (2017a).

Lack of qualified academic staffs has been a perennial problem (MoPME, 2017b). As of March 2016, 27 per cent of the Head Teacher posts and 7 per cent of Assistant Teacher posts under Directorate of Primary Education remained vacant (MoPME, 2017b). Moreover, there is a wide variation in educational qualification among the primary school teachers; in 2016, only 58 per cent of the primary teachers had a Bachelor/ Honours or a Masters degree (MoPME, 2017b).

Inadequate budget is also one of the foremost constraints facing Technical and Vocational Education and Training (TVET) stream. Almost 40 per cent of the TVET institutions reported that lack of laboratories, apparatus, and trained teachers are major challenges that limit their capacity to impart quality education (BBS, 2016).

Health budget in view of emerging needs

Budgetary allocation for the health sector has remained low. As a result, a significant amount of health expenditure is borne by the consumers of the health service themselves. Over two-thirds of the total health expenditure in Bangladesh is financed by out-of-pocket spending (MoHFW, 2017). Low public spending on health implies that the low-income households are at a disadvantageous situation because of their low disposable income. According to World Development Indicators (WDI), a staggering 4.5 per cent of the population was pushed below the $1.90 poverty line in 2010 because of out-of-pocket health care expenditure in Bangladesh.

In terms of progress of the HPNSDP, the annual implementation report of the programme revealed that only 11 targets out of the 40 had been achieved by 2014 (MoHFW, 2016). Updated information on six indicators are available from BBS (2017) and MoHFW (2017). These include infant mortality rate, under-five mortality rate, maternal mortality rate, neonatal mortality rate, total fertility rate and contraceptive prevalence rate. The status of the six indicators has been summarised in Table 2.11. As the table shows, targets of only three of the six aforementioned indicators—infant mortality rate, under-five mortality rate, and neonatal mortality rate—have been achieved in 2016. From the budgetary perspective, the government will need to put emphasis on indicators where targets remain unattained. Some of these relate to maternal mortality rate, contraceptive prevalence rate and total fertility rate.

Table 2.11

Status of Selected Indicators

Indicator	Status in 2010 or 2011 or 2012	Target 2016	Progress in 2016	Remarks
Infant mortality rate (IMR)	43	31	28	Achieved
Under-five mortality rate	53	48	35	Achieved
Maternal mortality rate per 100,000 live births.	194	<143	178	Not achieved
Neonatal mortality rate	32	21	19	Achieved
Total fertility rate (TFR)	2.3	2	2.1	Needs attention
Contraceptive prevalence rate	61.2	72	62.3	Not achieved

Source: MoHFW (2016 and 2012); BBS (2016).

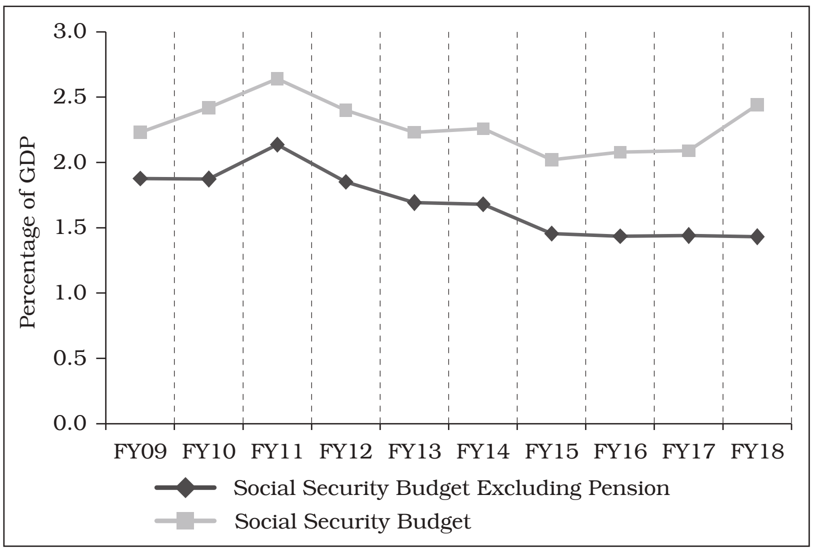
Note: Only the available updated indicators have been included.

Budgetary allocations for social security

Social security budget has been hovering around 2 per cent of the GDP since FY 2008-09, as illustrated in Figure 2.15. In FY2017-18, the social security budget was 2.4 per cent of the GDP, which exceeded the target of 2.3 per cent of GDP outlined in the 7FYP. However, a close scrutiny on the allocation for social security indicates that, in FY2017-18, 41.3 per cent of the budget for social security was allocated for

Figure 2.15

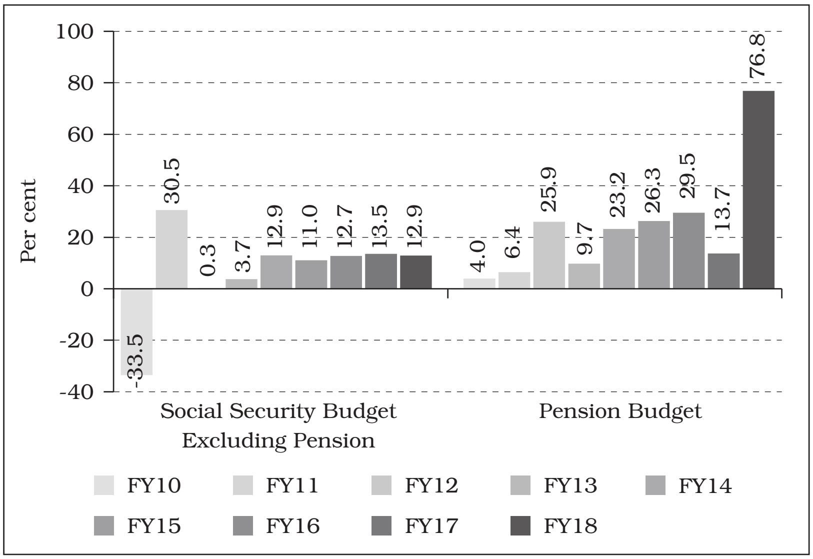
Social Security Budget as Percentage of GDP



Source: Authors' calculations from Social Security Policy Support (SSPS) Programme data.

Figure 2.16

Percentage Change in Social Security Budget and Pension Budget



Source: Authors' calculations from Social Security Policy Support (SSPS) Programme data.

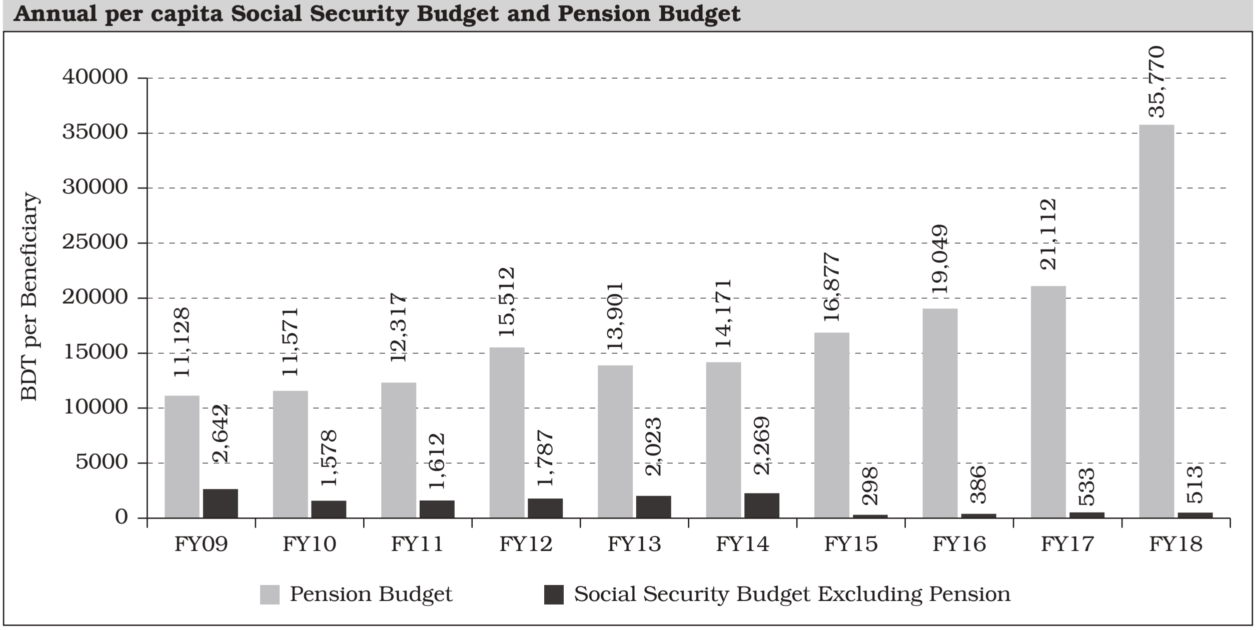
pension of government officials (GED, 2018). In fact, the social security budget excluding pension has been decreasing, from 2.1 per cent of GDP in FY2010-11 to 1.4 per cent of GDP in FY2017-18.

Thus, the recent increase in social security budget was mainly due to the increase in the budget for pension. For instance, in FY2017-18, the social security budget excluding pension increased by 12.9 per cent, whereas the budget for pension increased by 76.8 per cent (Figure 2.16).

Total and per capita budget allocations for pension dwarfs the budget allocations for all other social security programmes. In FY2017-18, pension received 41.31 per cent of the social security budget, which was equivalent to the budget allocations for the next 23 largest social security programmes combined (GED, 2018). Figure 2.17 shows that since FY2012-13, per capita budget allocation for pension has been on the

Figure 2.17

Annual per capita Social Security Budget and Pension Budget



Source: Authors' calculations from Social Security Policy Support (SSPS) Programme data.

rise, whilst at the same time per capita budget allocation for social security excluding pension has been on the decline. In FY2017-18, per capita budget allocation for pension was BDT 35,770 per beneficiary per year, compared to BDT 513 per beneficiary per year for social security programmes excluding pension. This means that, on average the amount received by pension beneficiaries is 69 times more than that of the beneficiaries of other social security programmes.

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

2.7.4 Recommendations for National Budget FY2018-19

Taking note of the prevailing situation concerning the social sector and safety net programmes, and considering their performance and budgetary allocations, CPD offers the following recommendations for the upcoming budget of FY2018-19:

- Budget for education should be at least 2.84 per cent of GDP in FY2018-19 to achieve the 7FYP targets. However, the government has to increase the education budget significantly if the relevant SDG targets are to be achieved.
- Increased budgetary allocations should focus on hiring qualified teachers and reducing the STR towards ensuring effective learning outcomes.
- Higher budgetary allocation should be made in order to improve skills of human resources aligned with demands of national and international job markets.
- In view of the low budgetary allocation for health and high out-of-pocket expenditure on this account, budgetary allocations must be significantly increased, and efficiency of resource utilisation enhanced. Budget for health should be at least 1.12 per cent of GDP in FY2018-19 to meet the target laid out in 7FYP.
- Allocation should be suitably increased for putting in place adequate number of affordable and accessible public healthcare facilities, particularly with a view to reducing out-of-pocket expenditure of the low-income households.
- Pension for government officials should be separated from social security account. Allocation for social security, excluding pension for government officials, should be raised to 1.6 per cent of GDP from the existing level of 1.4 per cent.
- Bring more clarity on the financing mechanism of the NSSS. Allocate adequate resources in the budget in line with the NSSS. Universal pension scheme should also receive adequate resource.

2.8 BUDGETARY IMPLICATIONS OF *ROHINGYA* CRISIS

Bangladesh has been dealing with the influx of estimated 200 thousand *Rohingya*s for several years now. The new influx of *Rohingya* people seeking refuge in Bangladesh since August 2017 has given rise to new challenges for the country, this time of higher magnitude. Since August 2017, nearly 700 thousand *Rohingyas* have sought refuge in Cox's Bazar district of Bangladesh, fleeing from the massacre and violence in the Rakhine state of Myanmar. This has raised the *Rohingya* population in Bangladesh to more than 900 thousand. The *Rohingya* crisis has various dimensions, which range from humanitarian to economic and strategic. As may be recalled, a Memorandum of Understanding (MoU) was signed on 23 November 2017 between Bangladesh and Myanmar for the repatriation of *Rohingyas*. The repatriation process was planned to start from 23 January 2018. However, the process is being delayed mainly due to the reluctance of Myanmarese authorities to take back the *Rohingyas.* Complexities in the verification process and uncertainty about their safe return have been delaying the process of repatriation.

A number of initiatives have been taken till now to mobilise resources in support of the *Rohingyas*. Recently, the UN agencies with International Non-Government Organisation (INGO) partners released the 2018 Joint Response Plan (JRP) in view of the *Rohingya* Humanitarian Crisis. They appealed to the international community for USD 951 million to meet the urgent needs of the nearly 1 million *Rohingyas* and more than 330 thousand local Bangladeshis in the host communities for a period of 10 months, from March 2018 to December 2018. As of 12 April 2018, an amount of only USD 73.4 million has been received which is 2.2 per cent of the total appeal mentioned above.

CPD had earlier undertaken an assessment of the resource requirement for the *Rohingyas*. In its review titled "Implications of *Rohingya* Crisis for Bangladesh", prepared as part of CPD's IRBD report in January 2018, it was mentioned that USD 882.0 million would be required for the period from September 2017 to June 2018 for meeting the needs arising from this crisis (CPD, 2018). It was also estimated that during FY2018-19 about USD 898 million would be required, assuming 300 *Rohingyas* would be repatriated every day, if population growth and inflation rate remain constant. If population and inflation are taken into consideration, the resource requirement will rise to USD 968 million for FY2018-19.

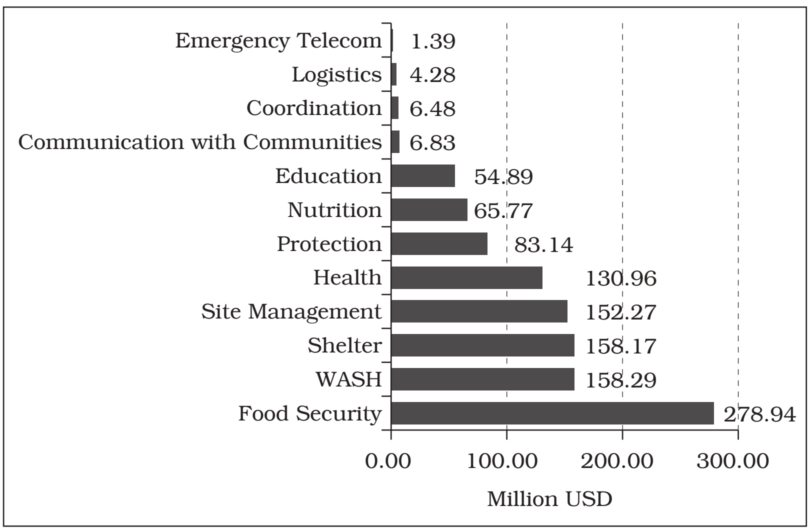
2.8.1 Costs for the *Rohingya* Crisis for FY2018-19

CPD has updated the estimation as regards the requirement for the *Rohingyas*, for FY2018-19. This is based on the appeal amount of the JRP, noted earlier. CPD's estimation makes the following assumptions: (i) 300 *Rohingyas* will be sent back to Myanmar per day from the month of July 2018; (ii) repatriation process will take place for 25 working days per month; (iii) all costs are equal for each person; and, (iv) cost of shelter construction and site management will be the same for all months. The estimates indicate an amount to the tune of USD 1,101.00 million which will be required to underwrite the costs in FY2018-19. A sector-wise needs of the *Rohingyas* shows that most of the expenditure will have to be incurred on account of food security, water sanitation and hygiene (WASH), shelter, site management and health (Figure 2.18).

According to the United Nations Office for the Coordination of the Humanitarian Affairs (UNOCHA), support from the GoB was 1 per cent of total requirement of USD 434 million during September 2017 to February 2018 (UNOCHA, 2018[15]) period. The sum was sought at the time of the first humanitarian response plan.

Figure 2.18

Sector-wise Requirements for *Rohingya* Crisis in Bangladesh (FY2018-19)



Source: Authors' calculations based on ISCG and SEG (2018); ISCG (2018).

[15]UNOCHA, 2018. Financial Tracking Service. Available from: https://fts.unocha.org/appeals/628/flows?order=directional_property&sort=asc&f%5B0%5D=sourceOrganizationIdName%3A%222981%3ABangladesh%2C%20Government%20of%22

2.8.2 Recent Initiatives of the GoB to Provide Humanitarian Support

The GoB has been extending all possible support to the *Rohingyas* as soon as the crisis began. Various ministries of the GoB are engaged in providing humanitarian support to the *Rohingyas*. The Ministry of Health and Family Welfare, Ministry of Public Administration, Ministry of Home Affairs, Ministry of Education, Ministry of Disaster Management and Relief (MoDMR), Ministry of Planning, Ministry of Social Welfare, Ministry of Defence, Bangladesh Water and Power Development Board, Ministry of Environment and Forest, and Local Government Division are actively involved in the humanitarian support process right from the beginning. According to the Refugee Cell of MoDMR, the GoB has received around BDT 1,000 crore from private donations and contributions. Of this, the GoB has directly spent around BDT 200 crore on the *Rohingya* crisis.

The GoB is planning to provide vocational training for adult *Rohingyas* to enhance their skills and carry out the jobs around the camps. Training and work opportunities in camps as barbers, tailors and cleaners could help the unskilled workforce to earn a livelihood. The children are being provided education in English and Burmese.

There is scarcity of land in Cox's Bazar and it will be difficult to relocate additional *Rohingyas* when monsoon sets in. The refugees continue to live under threats of landslides, floods and heavy storms. Around 230 thousand *Rohingyas* (10 thousand families) have been relocated from camps to safer areas around the camp in view of the approaching monsoon season. But only about 100 thousand *Rohingyas* can be relocated within the camp areas.

Considering the risk of natural disaster and security concerns and taking cognisance of tourism interests in the areas, the GoB has taken an initiative to transfer the camps from Cox's Bazar to Bhashan Char in Noakhali district. Bangladesh Navy is implementing the project costing USD 280 million to construct shelters for *Rohingyas* in the island. About 40 per cent of the construction of 1,440 houses including 120 cyclone shelters has already been completed by the Bangladesh Navy as of 19 March 2018. The National Economic Council of GoB has approved an amount equivalent to USD 280 million for the construction[16]. The relocation may begin before the upcoming rainy season depending on the progress of the construction works.

2.8.3 Recommendations

In light of the current situation of the *Rohingya* crisis, following recommendations are put forward in the context of the upcoming national budget for FY2018-19.

- Given that the requirement for the *Rohingyas* is quite significant and the repatriation process is uncertain, the GoB has to chalk out a comprehensive plan for resource mobilisation.
- Information on the flow of international fund for *Rohingyas* and the usages of these funds should be made readily available. Ministry-wise resource requirement plan for FY2018-19 would be helpful for informed resource management.
- Transparency in the allocation of budget, at the ministerial level, in view of the *Rohingya* crisis, should be ensured. This will ensure allocative efficiency and resource-use efficacy in connection with the various activities being implemented including particularly in the construction of *Rohingya* shelters at Bhashan Char, setting up of vocational training system for them and provisioning of basic facilities to help sustain livelihoods till the repatriation of the *Rohingyas*.

[16]http://www.dhakatribune.com/bangladesh/development/2017/11/28/ecnec-bhashan-char-rohingya-relocation/

2.9 A TRUST FUND FOR SDG DELIVERY

2.9.1 Background

Implementation of the aspirational agendas of the SDGs, by 2030, call for multi-stakeholder participation in achieving the 17 goals and 169 targets. Along with government and public organisations, non-state actors such as private sector, Non-Government Organisations (NGOs), Civil Society Organisations (CSOs), media, and knowledge community as also development partners are expected to play important role in implementing the diverse areas of activities associated with the SDGs. Significant amount of resources will need to be mobilised and wide-ranging activities carried out if poverty levels are to be brought down to zero, hunger eliminated, decent jobs created and triangulation of economic development, social inclusiveness and environment-friendly development are to be ensured in light of the SDGs.

Since independence, the NGOs/CSOs in Bangladesh are playing a critical role in the country's socio-economic development. Experiences reveal that, alongside the government interventions, NGOs played a crucial role in achieving the Millennium Development Goals (MDGs) in Bangladesh. For instance, non-state actors such as the Grameen Bank, BRAC, and PROSHIKA have made significant contribution to attain the MDGs through micro-credit programmes, skill development and training, and employment generation programmes (Bhuyan, 2006). There is a wide recognition that drawing on their track record and experiences in MDGs implementation, NGOs have the potential to make their mark in view of the SDGs as well. The 2030 Agenda has created an opportunity for the NGOs to get involved in the discourse as regards sustainable development at all levels. NGOs can play a key role in the process of implementing the SDGs through awareness building, mobilisation of stakeholders around the goals, and leveraging government actions. NGOs can prepare shadow reports on SDGs and feed into the Voluntary National Review (VNR) process and carry out advocacy and highlight concerns at the High Level Political Forum (HLPF) and United Nations Economic and Social Council (UN ECOSOC) meetings. Other than their own-initiated programmes, NGOs can also collaborate in projects relevant to SDGs implementation undertaken by the local governments, private sector and others. Indeed, SDG17 (promoting new partnerships) spell out the necessity of such collaboration as a key modality to attain the SDGs. NGOs are also very well-positioned to disseminate the knowledge about SDG-related progress and press for transparency and accountability in the implementation process and contribute to cost-effective and timely implementation of the attendant tasks. NGOs can also help mobilise global opinion and generate resources in support of SDGs implementation in developing countries such as Bangladesh.

A recognition by the government of the positive role NGOs could play is a sine qua non for the GO-NGO partnership to be successful. Adequate financial endowment of the NGOs is a must for the NGOs to be effective. It is in the context of the second overriding factor that the idea of setting up a SDG Trust Fund in support of the NGOs becomes a relevant proposition.

2.9.2 Rationale for an SDGs Trust Fund

As a country which has embarked upon its middle-income journey, Bangladesh is expected to face increasing challenge in attracting official development assistance (ODA) on concessional terms. Aftermath of the global financial crisis of 2008–09 and diversion of resources to address more urgent issues like migration have accentuated the challenge of mobilising aid in support of global cause such as the SDGs, however noble and worthy the cause may be.

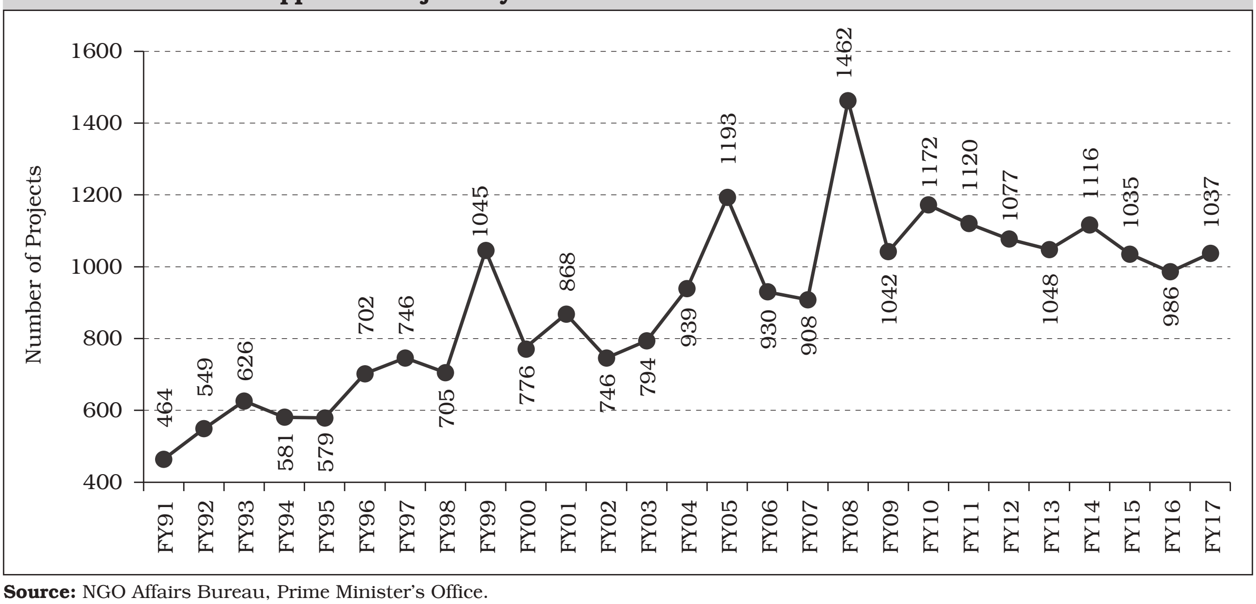
Global resource crunch and Bangladesh's achieving the status of middle-income country and LDC graduation (eligibility) are also going to affect funding of NGOs from global sources. NGOs in low-income countries and LDCs are most likely to be prioritised for global support. In 1970, government of many developed countries agreed to devote 0.7 per cent (equivalent) of their national income (GNI) as aid to developing countries of the world (Kamphof, Spitz, and Boonstoppel, 2015). This aid was to be earmarked both for governments and the NGOs. However, only a few developed countries have kept their promises. This had negative implications for fund flow and availability concerning the NGOs. All these will have important implications for the functioning of many NGOs who are dependent on foreign support. They will need alternative sources of funding to carry out their activities. As is well known, financing needs for implementing the SDGs would be significantly higher than the MDGs. A report prepared by the General Economics Division (GED, 2017) estimate that, in order to meet the additional (synchronised) financial needs of implementing the SDGs, Bangladesh will need a total of USD 928.48 billion (of which, USD 796.09 billion is estimated to come from domestic sources and USD 132.39 billion from external sources) at 2015–16 constant prices over the period of FY2017-FY2030 towards the SDGs implementation. The annual average price tag would be about USD 66.32 billion (at constant price) (GED, 2017). The GoB has rightly identified PPP as a key strategy to finance SDG implementation. The government has also identified the NGOs as a major player in implementing the SDGs and also as an important source for SDG-related financing and addressing the financing gap in implementing the SDGs. The estimated amount to be financed by the NGOs was expected to be about 5 per cent (on average) of the total additional finance requirement during the FY2017-FY2030 period (GED, 2017).

Foreign fund disbursed in favour of NGOs has been about 20.2 per cent of total ODA flow to Bangladesh in FY2016-17. Number of projects approved by the NGO Affairs Bureau was about 1037 during the FY2016-17 period (Figure 2.19). Although the flow of foreign grant fund released through the NGO Affairs Bureau shows an increasing trend, its share in the GDP has been declining (Figure 2.20).

However, the inadequacy of foreign fund earmarked for the NGOs is only one part of the argument. What is reasoned here is that the GoB should consider allocating budgetary support to the NGOs taking note of their potential role as an important contributor to SDG implementation in Bangladesh. They also need to work towards enhancing the capacity of NGOs to implement the SDGs where they have comparative advantage and proven track record. This is of particular significance in attaining the SDG aspiration of 'Leave No One Behind'. The NGOs have a natural advantage in reaching the furthest first. This is borne out by a World Bank report which shows that, about 80 per cent of the villages in Bangladesh are covered

Figure 2.19

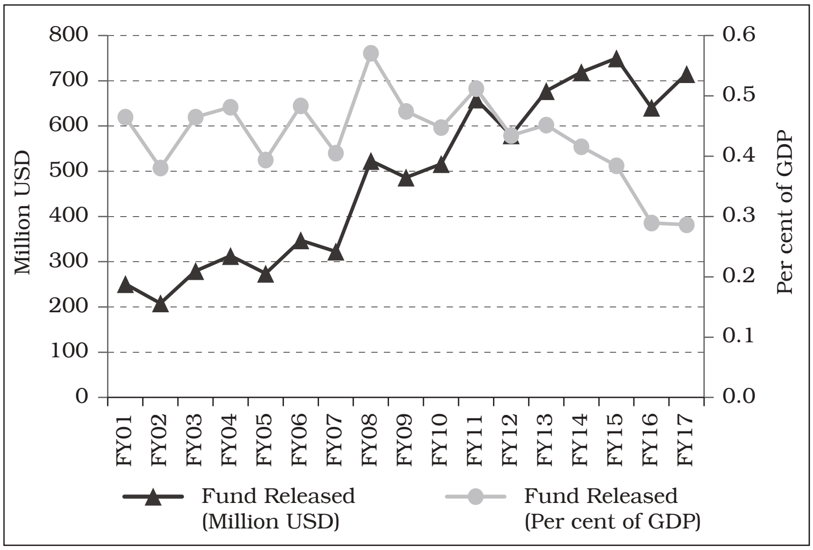
Year-wise Number of Approved Projects by NGO Affairs Bureau



Source: NGO Affairs Bureau, Prime Minister's Office.

Figure 2.20

Flow of Foreign Grant Fund Released through NGO Affairs Bureau and its Share in GDP



Source: NGO Affairs Bureau, Prime Minister's Office.

Note: Fund released as per cent of GDP is shown in the right vertical axis.

by NGO programmes or projects (World Bank, 2005 cited in Bhuyan, 2006). Also, it may ensure leveraging government activities through NGO interventions towards overall effectiveness.

It is from the above vantage point that a financing mechanism for NGOs to help them implement the SDGs is being proposed here. The idea is to set up an SDGs Trust Fund for the NGOs/CSOs.

2.9.3 Establishing an SDGs Trust Fund for the NGOs

The objective of the proposed SDGs Trust Fund is to create a financing window for NGO partnership to implement the 2030 Global Agenda in Bangladesh. NGO is used here in broader sense since all non-state actors such as NGOs, CSOs, think tanks and community organisations could be part of such an initiative. The SDGs, Fund is to be operationalised through PPP. Government may consider making budgetary allocations in the national budget to set up this fund to support NGOs/CSOs working in areas relevant to the SDGs and SDG implementation. The recipients will utilise the allocation from the Fund by maintaining transparencies and accountability in accordance with a predesigned structure and framework of operation.

The following is a proposed framework for the SDGs Trust Fund. This framework is prepared based on a review of the legal and governance structures of different Environmental Trust Funds (ETFs) established in developing countries.

Fund formation and governance

A government approved legal framework will be developed to establish the SDGs Trust Fund. There will be an MoU or other types of agreements between the national government and the Trust Fund according to the PPP law/guideline. According to the PPP law 2015, the government can contribute via financial participation in five forms: Technical Assistance Financing, Viability Gap Financing, Financing against Equity and Loan, Financing against Linked Component, and Financing against other Activities as may be planned by the PPP authority (PPPA, 2016). Procurement Guidelines for PPP Projects 2018 stimulates that in order to deliver the PPP Projects, selection of a Private Partner is to be done in four phases (PPPA, 2018). These include: Identification Phase, Development Phase, Bidding Phase, Approval and Award Phase.

A select number of "Trustees/Board Members", will be responsible for putting in place a structure, and governing a guideline for the Fund. They will also process the decisions of the Fund. Apart from this, there could be advisory committee, internal audit section, monitoring and evaluation section and other administrative sections to run the Fund, as deemed necessary. Operational plans in the areas of implementation, fundraising, resource mobilisation, communications, and evaluation etc. will need to be developed.

The Fund is expected to work independently and be tax exempted.

Size of the Fund

As was noted earlier, according to GED (2017), about 5 per cent of total additional financing requirement for SDGs in Bangladesh will need to be financed by the NGOs, on an annual basis. This implies that NGOs are envisaged to contribute to SDGs implementation to the tune of about Tk. 14,000 crore to meet the financing gap. If the total foreign fund channelled through NGOs in FY2016-17 (USD 715 million or about Tk. 6,000 crore) are considered, there may be a gap of about Tk. 8,000 crore. The idea is not to look for funds to bridge this significant gap as the government's resource constraints and limitations are well-known. The idea is to help the NGOs to draw synergies, and leverage other initiatives in areas where NGOs are best placed in terms of implementing the SDGs. Government allocation to NGOs could play a catalytic role in helping the NGOs make more effective use of resources available to them and also take up additional work. This will also help bridge the aforesaid gap as regards NGO contribution to SDGs implementation particularly taking cognisance of the fact that a significant part of the national budgetary allocation often remains underutilised on a regular basis. Since, the proposed SDGs Trust Fund is a new concept, the government may like to start with a token allocation of Tk. 500 crore. This may be further raised in phases considering demand, resource availability, and utilisation efficacy.

Sources and utilisation of the Fund

It is envisaged that the major part of the envisaged Fund will come from the national government through budgetary allocation in the ADP. Utilisation of the Fund will also have the flexibility to blend finances from multilateral and bilateral aid, NGOs, foundations, lotteries, philanthropic bodies, and innovative sources.

- Foreign and other potential donors may also be invited to contribute to this Fund.
- Private sector may also put in thier corporate social responsibility (CSR) money.

The Fund money will be allocated to eligible implementing agencies such as NGOs, CSOs, community-based organisations, and private sector entities. The implementing agencies will be selected based on the strength of respective proposals submitted against relevant calls on different SDG themes. All selection and allocation will be through a competitive process to be supervised by competent bodies to be set up by the SDGs Trust Fund Board. The Fund will also help relevant capacity building of the implementing agencies based on need assessments.

Monitoring and evaluation

A dedicated monitoring and evaluation section of the Fund will be primarily responsible for this task. It will monitor use of allocated resoures resources and examine grantee reports. Staff from the section will visit fields where implementation of activities underwritten by the Fund would be taking place, on a regular basis. It is advisable to maintain a score card for the implementing agencies which will indicate the scale of quality of implementation under different relevant indicators/criteria. Evaluation will include assessment of the project implementation outcomes according to the objectives set out in the proposal, implementing organisations' performance, and efficacy of the use of the fund disbursed. Annual progress report and other assessment tools will be used to decide on continuity of support and relevant actions to ensure best use of the grant by the recipient NGOs and CSOs.

Risk factors involved

As may be recalled here, Bangladesh has created BCCTF and Bangladesh Climate Change Resilient Fund (BCCRF) in 2010 with the purpose to help communities recover, mitigate, adjust and harness capacities, and also develop resilience in view of climate change impacts. The other objective was to make use of the fund to leverage financial assistance from development partners. However, lessons from operationalising these Funds should be appropriately drawn to run the proposed SDGs Trust Fund. A Transparency International Bangladesh (TIB) study found a number of problems that inform functioning of the two Funds including lack of transparency, political influence in selection of the NGOs, poor quality of work, and poor state of accountability in the Funds' overall operations (Haque, Rouf, and Khan, 2013). Consequently, the proposed SDGs Trust Fund should take cognisance of the possible risks and be prepared to address those accordingly.

Some of the risks that need to be considered are as follows:

- Autonomy of the implementing NGOs may be compromised due to overdependence on the Trust Fund
- Slow disbursement of funds due to poor management
- Political influence over decisions as regards grants allocation and selection of implementing NGOs
- Government agencies controlling tendency may impede the independent functioning of the Fund
- Lack of organisational/technical capacities impeding the effective implementation of the projects
- Variability and inflation of administrative costs, and/or lack of delivery, due to poor design
- Failure to coordinate with stakeholders in implementation, and monitoring and evaluation[17]
- Political instability, lack of policy continuity, change in governments could undermine effective functioning of the Fund
- Fraudulent practices by particular NGOs

Risks will need to be mitigated and addressed through appropriate up-front steps and downstream oversight. It is hoped that, new funding source will help the NGO to scale up mobilisation and collaboration.[18] The fund will also help the GoB to align its priorities in terms of implementing the SDGs and thus help synergise the activities of key stakeholder towards successful implementations of the 2030 Agenda. On the other hand, as mentioned earlier, NGOs have the advantage of working at the grass-root and with the grassroots and have the ability to reach the marginalised at low cost by leveraging their existing activities and initiatives. Thus, the proposed SDGs Trust Fund could be a win-win proposition for both the government and the NGOs.

2.10 CONCLUDING REMARKS: RECOMMENDATIONS FOR NATIONAL BUDGET FY2018-19

The overarching macroeconomic stance of the national budget for FY2018-19 should be maintaining macroeconomic stability with greater emphasis on inclusive development. Admittedly, in spite of the formidable challenges in a number of areas, the Bangladesh economy is benefitting from a number of advantages. The provisional national accounts estimates for ongoing fiscal year indicated a sustained acceleration of economic growth while employment generation figures for the previous year also showed some promise. However, as the present review suggests, in FY2016-17 average real labour income had declined; and at the same time, unemployment rates for youth and relatively more skilled labour force had increased considerably. Apparently, the jobs created during FY2016-17 were generally of low productive in nature.

[17]http://www.undp.org/content/sdfinance/en/home/solutions/environmental-trust-funds.html
[18]http://www.undp.org/content/sdfinance/en/home/solutions/environmental-trust-funds.html

Analysis of the macroeconomic correlates presented in the preceding sections reveals a number of stress points which are contributing towards the weaknesses emerging in Bangladesh's overall economic management. These include failure to mobilise resources from domestic sources at the needed level; delays, cost overrun and institutional weakness in development project implementation; financing of fiscal deficit from relatively expensive sources such as net sales of NSD certificates; gradual increase in inflation fuelled by rising food prices; disarray in the banking sector; increasing interest rate; depressed balance of payment scenario in the backdrop of spurt in import growth despite recovery in export earnings and remittance inflow along with better disbursement of foreign aid; and volatility in the exchange rate market.

In view of the emergent scenario, the need for a significant improvement in the quality of macroeconomic management cannot be overemphasised. In this backdrop, the present document puts forward the following set of recommendations in the context of the forthcoming national budget for FY2018-19. As may be recalled, CPD, over the past several years, has been repeatedly urging for initiating reforms in a number of critical areas. Evidently, in the run up to the forthcoming national election in December 2018, the government has little appetite for implementing the much-needed reform agenda. Acknowledging this reality from a political economy perspective, it is, however, critical that the reform issues inform the debate and discourse in the course of the electoral campaign so that the issues are kept alive and concrete measures toward implementation are taken by the new government after the national elections.

2.10.1 Macroeconomic Policy Stance and Fiscal Budgetary Recommendations for FY2018-19

The budget for FY2018-19 along with supportive macroeconomic policies will need to address the disquieting trends in the macroeconomic correlates. CPD, as it has recommended earlier in January 2018, in its first reading of the IRBD, continues to maintain its position in favour of a conservative macroeconomic stance and stringent macroeconomic management. The macroeconomic and fiscal-budgetary policies need to be informed by the following recommended measures.

- Bangladesh Bank must pursue a cautious monetary policy in the coming months in the backdrop of rising inflation. This will also help ease the pressure on the BoP situation. Policy consistency should be exercised in line with the MPSs. In this context, independence and authority of Bangladesh Bank must be maintained. Influence of vested interest groups needs to be restrained while formulating national economic policies. Role of the commercial banks and other institutional investors should be put under scrutiny in view of strengthening the capital market.
- Budgetary allocation for the SCBs in the form of recapitalisation, carried out repeatedly in recent years, is morally unacceptable and economically unjustifiable. Public money should be distributed to banks only in exceptional cases and only under stringent terms and conditions in order to ensure proper utilisation of taxpayers' money. At the same time, alternative avenues such as using revenue to increase capital, pursing private investors to buy bank shares, or mergers with other banks, should be explored. Under the present circumstances, these measures should particularly be applicable in case of the struggling PCBs.
- The fast-rising import payments have become a major concern due to the adverse implications for the BoPs, exchange rate stability and foreign exchange reserve accumulation. Since, a significant part of the import payments (particularly those associated with majority of the large public investment programmes) is underwritten by foreign resources, the pressure on current account is somewhat eased by the surplus in the financial account. However, the financial account surplus has not been adequate enough to arrest the deficit in the overall BoP. The demand for foreign exchange may continue in view of higher import requirement in future, and the creeping global commodity prices. The central bank should consider discouraging imports of consumer and luxurious commodities by raising Letter of Credit (L/C) margins for import and reducing the time for L/C repayment. Since the beginning of FY2017-18 there has been depreciation of BDT to the tune of about 3 per cent. Foreign exchange management should

aim at maintaining stability in the exchange rate of the BDT against USD. For the time being the foreign exchange reserves should be able to cover the pressure in the BoP. However, the central bank should remain vigilant against volatility in the domestic foreign exchange market as has been experienced in recent times.

- Historically, trade mispricing and capital flight are found to be more extensive during the election years. It may be recalled that CPD (2018) in January 2018 also raised this concern in view of recourse to overinvoicing in import payments in case of some items. Curbing such illicit financial flows will require coordinated efforts by several policy actors including the Bangladesh Bank and the NBR. The long overdue data integration process (e.g. NBR data centre) should be established to reduce trade mispricing and revenue leakages through analysis of the quality of disaggregated trade data. NBR's transfer pricing cell should be adequately endowed and vested with the required capacity to enable it to carry out its responsibilities in an effective manner.
- The forthcoming national budget must focus on raising revenue from niche areas including speedy realisation of disputed revenue claims through the Alternative Dispute Resolution. Immediate steps need to be taken in order to recover the large amount of due taxes from the state-owned enterprises.
- As was mentioned, the rate of inflation has been gradually on the rise, contributed by rising food-inflation. On the other hand, the data from the LFS 2016–17 reveal that average monthly real wage of individuals has been decreasing since 2013. These have combined to put pressure on the disposable income of lower-middle and middle-income households. The budget for FY2018-19 should consider raising the tax-free income ceiling to Tk. 3 lakhs in order to provide respite to lower middle-income households.[19] The budget may also consider reducing the personal income tax rate for the first slab to 7.5 per cent from the prevailing rate of 10.0 per cent. Resultant boost in disposable income and the consequent multiplier effect on the economy should provide opportunities for the government to make up for the forgone income through additional revenue earnings.
- The budget should take a view to assess tax incentive and exemption packages based on economic returns. The budget document should clearly mention the fiscal policy changes (in the areas of tax incentives, exemptions, rebates, surcharges etc.) which are being proposed and their impacts on different sectors/segments of the economy including revenue forgone from the point of attaining fiscal targets and ensuring transparency. More efforts will be required to expand the prevailing incentives for export-oriented sectors beyond the RMG and some of the other thrust sectors. However, institutional strengthening through enhancement of capacity of oversight agencies and enforcement of relevant laws must be ensured before taking such steps, to deter misuse of such incentives.
- The budget should refrain from reducing corporate tax rates on an ad-hoc basis, in a hasty manner and without a rigorous analysis. Adjustments of corporate tax rates, if required, should be done in a staggered way over the medium-term in order to absorb any revenue shock and provide investors predictability as regards investment decisions.
- Budgetary allocations for social sectors must be coherent with the overall development needs of the economy, particularly in view of SDG targets. According to World Bank and International Monetary Fund (IMF) data, Bangladesh was ranked among the bottom countries with regard to education (85 out of 90 countries), health (197 out of 197 countries) and social protection expenditure (36 out of 47 countries). In view of the budgetary targets for social sectors set by 7FYP, resource allocations for education, health and social security need to be enhanced to 2.84 per cent, 1.12 per cent and 1.6 per cent of GDP respectively in FY2018-19. The government also needs to take concrete steps to implement the NSSS. CPD also recommends to create an SDGs Trust Fund in the upcoming budget (with Tk. 500 crore) which can be utilised by the NGOs with a view to attain the objective 'Leave No One Behind'.
- While placing the fiscal-budgetary proposals before the parliament, budgetary implications for *Rohingya* management should be mentioned in a transparent manner. In view of the resource requirements for

[19]In the budget for FY2015-16, personal income tax (PIT) exemption threshold, at the general level, was increased to Tk. 2.5 lakhs from the previous ceiling of Tk. 2.2 lakhs in FY2014-15 (13.6 per cent increase). This threshold has been maintained ever since. At the same time, general CPI has experienced a 16.9 per cent increase between July 2015 and March 2018.

the *Rohingyas* and their repatriation process remaining uncertain, the government in this connection should have a clear plan.

- It may be tempting for a political government to consider development projects in the run up to the election by pursuing a populist approach. However, for the sake of prudent macroeconomic management, the budget for FY2018-19 should avoid all conspicuous public spending.
- Delayed implementation is a major reason that drive cost escalation of the ADP projects. Timely implementation should be prioritised, particularly for the large projects. This is particularly important to encourage crowding-in of the private investment. To this end, the implementing agencies should accelerate the pace of implementing the 'model' SEZ projects while the Finance Division will need to ensure adequate budgetary allocations. These SEZ facilities should be seen as tools for augmenting new private investment and be awarded in a competitive manner while measures should be there to check any likely misuse of tax incentives by entities in the SEZs.

2.10.2 Recommendations in the Run-Up to the Election

To sustainably improve economic management, continued efforts are needed to strengthen legal and institutional systems. Regrettably, the economic management of Bangladesh is plagued with low quality, non-performing and inadequate number of institutions. While some of the shortcomings stem from long-standing systemic issues, others might be corrected through prudent short- to medium-term policies and appropriate strategies. Independent and rigorous economy wide analyses should be conducted for all types of reforms. Indeed, the economic reform agenda should be at the forefront of the forthcoming election debates and should find place in the election manifestos of major political parties.

Both revenue-GDP and tax-GDP ratios in Bangladesh remained significantly low compared to South Asian neighbours and other emerging Asian economies. According to data from WDI, out of 105 countries (for which data was available), Bangladesh ranked 102 and 98 respectively with regard to revenue-GDP and tax-GDP ratios. The government is currently considering devising a Medium-Term Revenue Strategy (MTRS). To this end, it is critical to emphasise timely implementation of VAT and SD (Supplementary Duty) Act 2012. The implementation plan ought to be informed by the prevailing concerns. Implementation of online VAT registration and filing system and digitisation of VAT process and bringing in more businesses under the system should be given priority. Efforts should be made to finalise the draft Direct Tax Act at an early date; it should be placed in the public domain to seek opinion of relevant stakeholders and interested groups. Besides, the government needs to rationalise and modernise the Customs Act on an urgent basis. This should correspond with the current industrial and export policies (including export diversification strategies). The medium-term strategy should seek to identify innovative areas for resource mobilisation including assessing feasibility of introducing taxation of agricultural income, a comprehensive property tax and inheritance tax in line with international practices. It is also possible to gain efficiency through broader use of technology including introduction of electronic tax deduction at source (e-TDS) with issuance of tax certificates by the NBR against an e-TIN linked to each TDS collection. This will improve the state of regulating and managing the process. Indeed, the NBR should improve and utilise its tax database towards better enforcement of its policies.

Establishing a Public Expenditure Review Commission for ensuring accuracy of cost estimation of public investment projects and for raising overall effectiveness of public spending should be seen as priorities in the economic reform agenda. At the same time, it is strongly reckoned that the next government should consider establishment of a permanent Local Government (Finance) Commission towards effective devolution of power and introduction of appropriate financing modalities for local government. This initiative will help to ensure that public expenditure has greater impact at grassroots levels.

The government is currently considering introduction of a universal pension scheme and a national health insurance scheme. These will be major steps towards a more inclusive society. Both these initiatives will require legal and institutional reforms. The background technical work should be expedited so that national election debates in this context are well-informed. The budgetary implications of such steps should be captured appropriately and funding modalities need to be properly identified in preparation of implementing the schemes.

Inflation, particularly that of food items, must be checked given its negative impact on the welfare of marginalised section of the society. It is also critical that incentive prices for the producers are ensured. To this end, the government should consider setting up an Agriculture Costs and Prices Commission (ACPC). This Commission should be mandated to provide strategic guidelines to ensure food security in Bangladesh, recommend incentive structure for the producers, provide guidelines for price signals in the market and for procurement, reduce the disparity between farm-gate and retail prices of agricultural products, balance consumer-producer interests and ensure fair prices for farmers.

In the backdrop of the disarray in the banking sector, CPD reiterates its earlier proposal to establish an independent Financial Sector Reform Commission (IFSRC). This Commission will evaluate the needs of customers and the economy, identify the weaknesses, scrutinise governance structure, security system, incentives, and risk management system in the banking sector. Furthermore, the Commission will provide guidelines for NPL management and recapitalisation of banks, rescheduling of bad debt. The non-bank financial institutions could also be included within the remit of Commission's scrutiny.

Quality and timely data is central to designing plans and strategies in the area of economic policymaking. In recent times, there has been growing concern as regards quality of data and coherence and credibility of various estimations. From this perspective, the new government may consider setting up an independent Statistical Commission to examine the quality of data pertaining to key macroeconomic correlates and come up with suggestions to improve data quality and ensure autonomy of statistical organisations. This will contribute to ensuring data integrity and enhancing transparency.

The two priorities of pursuing a conservative macroeconomic policy to stabilise the economy over the short-term and designing a medium-term reform agenda, should inform macroeconomic management and preparation of fiscal-budgetary proposals in the context of the forthcoming national budget for FY2018-19.

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ANNEXES

Annex Table 2.1
PEDP III Selected Priority Indicators with Benchmarks and Targets

Indicator	2010 (baseline)	Target 2017	Status in 2017	Target 2018	Comment/other
Results Area 1: Learning Outcome					
Gross enrolment rate, primary education (boys and girls) [EFA* 5] (%)	107.7	105.0	111.7		Achieved
Net enrolment rate, primary education (boys and girls) [EFA 6] (%)	94.8	98.0	97.97		Achieved
Results Area 3.2: Effectiveness					
Dropout rate (%)	39.8	15.0	18.85		Not Achieved
Dropout rate by gender (%)					
Boys	*40.3*	*17.0*			*Needs attention*
Girls	*39.3*	*13.0*			*Needs attention*
Dropout rate by grade (%)					
Grade I	*8.5*		*1.5*		
Grade II	*3.0*		*3.0*		
Grade III	*7.7*		*3.9*		
Grade IV	*12.2*		*8.0*		
Grade V	*9.5*		*2.5*		
Coefficient of efficiency [EFA 14]					
Ideal as % of actual	*62.2*		*85.0*	*85.0*	*Needs attention*
Input years per graduate	*8.0*		*6.1*	*6.0*	*Needs attention*

Source: MoPME (2017a).
Note: *Education for All (EFA).

Annex Table 2.2
Learning Indicators as per National School Assessments

Key Performance Indicator	2011	2013	2015	Target 2018
Mean scores Grade III Bangla (%)	67	74	65	75
Mean scores Grade III Math (%)	50	58	41	60
Mean scores Grade V Bangla (%)	25	25	23	35
Mean scores Grade V Math (%)	33	25	10	40

Source: MoPME (2017a).

Chapter 3

State of the Bangladesh Economy in FY2017-18 *(First Reading)*

This report was released to the media by the Centre for Policy Dialogue (CPD) on 13 January 2018.

3.1 INTRODUCTION

The present interim review is the first reading of the State of the Bangladesh Economy in FY2017-18. The purpose of this review is to provide an assessment of the performance of the key sectors of the Bangladesh economy, and to trace the trends in crucial macroeconomic correlates during the first half of FY2017-18. Looking from the vantage point of the half-way mark of FY2017-18, the review puts under scrutiny the quality of macroeconomic management and identifies strengths and weaknesses of the economy. The report makes use of the latest available data and information from domestic and international sources. Insights from key informants are also taken into cognisance to strengthen the analyses further.

Following this introduction, Section 3.2 reassesses the major macroeconomic trends in FY2016-17 to establish the benchmarks to evaluate the performance in FY2017-18 in a comparative setting. In Section 3.3, performance of key macroeconomic variables is examined for the early months of the ongoing fiscal year. Section IV deals with a select set of contemporary issues including the *Rohingya* crisis, recent flood damage and post-flood management, and crisis in the banking sector. Finally, the report closes with some concluding remarks and anticipates possible outlook for the remainder of FY2017-18.

3.2 FY2016-17 REVISITED

As part of its regular annual assessment, CPD had earlier reviewed the performance of the Bangladesh economy in May 2017, just prior to the announcement of the national budget for FY2017-18. According to our analysis of the period under review, the macroeconomic trends transmitted a number of disquieting signals including increasing public debt burden, persisting weakness in the banking sector performance, sluggish capital market, lower growth in export earnings, and decline in remittance inflow (CPD, 2017b). The report was based on data available primarily for the first three quarters of FY2016-17. Our analysis was undertaken in the context of the budget for FY2017-18 which was programmed on the basis of the revised budget estimates for FY2016-17. As the revised and final full fiscal data for FY2016-17 for all the indicators are now available, macroeconomic correlates need another round of assessment to set the benchmark for FY2017-18.

3.2.1 Economic Growth and Investment

For the first time in the recent past, Bangladesh Bureau of Statistics (BBS) published the final estimates of the growth of gross domestic product (GDP) of the outgoing fiscal year, FY2016-17, within the first half of the subsequent fiscal year. According to the BBS final estimates, the real GDP growth in FY2016-17 increased by 0.17 percentage points to register 7.28 per cent growth. This is the highest ever growth achieved considering the new base year of 2005–06 for estimating national accounts. This is also for the second successive time that the final estimates of GDP growth by the BBS surpassed the planned target, which was set at 7.2 per cent for FY2016-17.

An analysis of contribution to GDP growth and a comparison with the previous fiscal year's performance (7.11 per cent GDP growth) shows that the incremental growth owed primarily to an increased contribution from the services sector, and in particular, from the wholesale and retail trade sector (Table 3.1). Growth contribution from financial intermediations also improved significantly in a year that was marked by deteriorating performance of the banking sector of the country. In contrast, in FY2015-16, industries (broad) sector was the lead contributor to the GDP growth of 7.11 per cent. In FY2016-17, industries sector's contribution had dropped due to lower contribution by both manufacturing and electricity sectors.[1] In case of the agriculture (broad) sector, the contribution was revised to lower than that reported in the provisional estimates as it incorporated the substantial loss of crop due to flash flood in haor areas in April 2017.

[1]On the contrary, Quantum Index of Industrial Production (QIIP) data showed that electricity production growth had significantly increased by 11.0 per cent in FY2016-17, which was only 4.8 per cent in FY2015-16.

Table 3.1
Incremental Contribution to GDP Growth in FY17

(in Per cent)

Sector	**FY16**	**FY17 (p)**	**FY17**
Agriculture	0.43	0.50	0.44
Crops and horticulture	*0.07*	*0.14*	*0.08*
Industries	3.24	3.18	3.10
Manufacturing	*2.26*	*2.21*	*2.21*
Electricity	*0.16*	*0.17*	*0.11*
Services	3.21	3.31	3.41
Public administration and defense	*0.38*	*0.34*	*0.32*
Wholesale and retail trade; repair of motor vehicles, motorcycles and, personal and household goods	*0.88*	*0.92*	*0.99*
Transport, storage and communication	*0.67*	*0.73*	*0.73*
Education	*0.26*	*0.26*	*0.26*
Health and social works	*0.13*	*0.13*	*0.13*
Financial intermediations	*0.25*	*0.25*	*0.30*
GDP growth	**7.11**	**7.24**	**7.28**

Source: Authors' calculations from BBS (2017) data.
Note: (p) stands for provisional estimates.

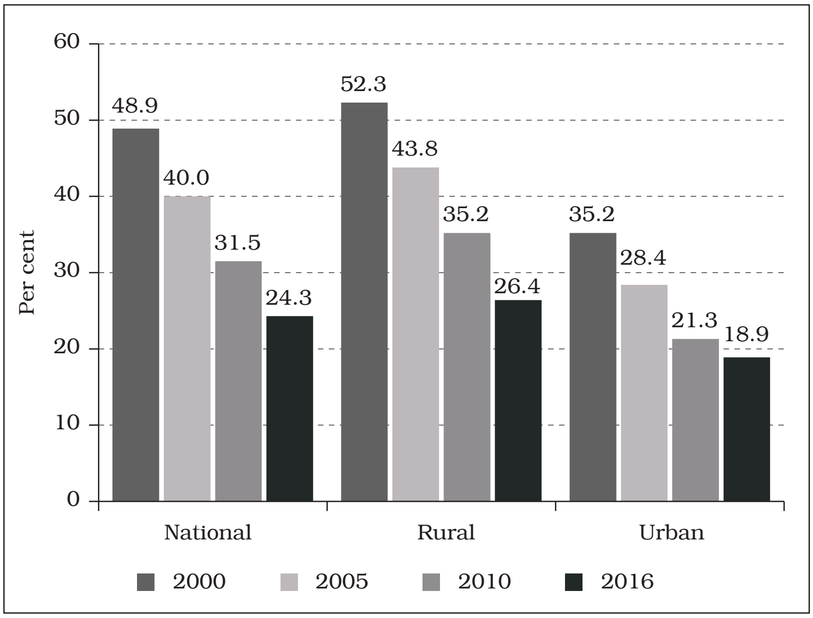
Nonetheless, as BBS data showed, industries sector has continued to grow at double digit (10.2 per cent) with significant contribution from the large and medium scale manufacturing industries (11.0 per cent growth). QIIP data suggests that a number of large scale industries posted significant growth in FY2016-17, including leather and related products (53.4 per cent growth) in spite of the production dislocation due to shifting of factories from the Hazaribagh area, textile (21.2 per cent), pharmaceuticals and medicinal chemical manufacturer (32.1 per cent) and manufacture of other non-metallic mineral products (32.3 per cent). The combined weight of these four industries was about one-third of the total industrial production. However, this high growth recorded by large scale industrial production failed to get reflected in the export figures. Indeed, export earnings eventually registered only 1.7 per cent growth in FY2016-17 and in particular, the readymade garment (RMG) exports posted only 0.2 per cent growth. It is also pertinent to note that, in FY2016-17, export earnings of leather and leather products increased by only 6.3 per cent. The export figures do corroborate the high growth of the manufacturing sub-sectors, putting under doubt the reliability of the production data.

Private investment as share of GDP, in the backdrop of some rise in the past, remained more or less at the same level, rising to 23.1 per cent from 23.0 per cent in FY2015-16. Private sector credit growth was consistent throughout the period and recorded 15.6 per cent growth against the 16.5 per cent target growth as of June 2017. On the other hand, public investment has increased by a not insignificant 0.7 percentage points to reach 7.4 per cent of GDP in FY2016-17. Gross national savings as a share of GDP has declined to 29.6 per cent which was 30.8 per cent in FY2015-16. Per capita gross national income (GNI) has increased to USD 1,610 per capita in FY2016-17 from USD 1,464 in FY2015-16, a rise of 9.9 per cent.

3.2.2 New Trends in Poverty and Inequality

The new estimates of Household Income and Expenditure Survey (HIES) 2016 (survey conducted during April 2016–March 2017) has brought forth a number of interesting trends in poverty and inequality. The poverty head count rate, calculated by using the cost of basic needs method, declined to 24.3 per cent in 2016 at the national level from 31.5 per cent in 2010 (Figure 3.1). Over the same period, rural poverty reduced to 26.4 per cent from 35.2 per cent while urban poverty went down to 18.9 per cent from 21.3 per cent over the aforesaid period. Despite the improvement, poverty reduction continues to be a major

Figure 3.1
Poverty Rates in Bangladesh Based on the Upper Poverty Line



Source: BBS (2017).

challenge with poverty being an important feature in the rural areas with its relatively higher incidence when compared to the urban counterparts. One encouraging note in this regard is that the difference between the rural and urban poverty incidence has been on gradual decline over time. In 2000, the difference was about 17 percentage points which had come down to 7.5 percentage points in 2016.

Despite this being the most important national target, the pace of poverty reduction has been exhibiting a declining trend at all levels. The Seventh Five Year Plan (7FYP) recognised accelerated poverty reduction as the key objective during the Plan (2016–20) period. During the 2010–16 period, the national poverty rate declined by 1.2 percentage points per annum; in contrast, the decline was 1.8 and 1.7 percentage points per annum respectively for the 2000–05 and 2005–10 periods. Despite rural poverty decline being above 1.5 percentage points per annum for the three aforementioned periods, urban poverty reduction has consistently been at a slower pace—this was only 0.4 percentage point per annum during 2010–16.

Poverty and employment estimates pose questions in the context of the benefits of the attained economic growth. Indeed, it is perplexing that a reduction in the poverty level decelerated at a time when Bangladesh's GDP was growing at an annual average of 6.5 per cent. One key reason behind this phenomenon could be the composition (quality) of the attained growth. In recent years, growth was mainly driven by the manufacturing and service industries. On the other hand, the contribution of agriculture to growth has been on the decline. It must be noted that agriculture still accounts for over 42 per cent of the total employment in Bangladesh. Concurrently, employment growth has been quite dismal in recent years. During 2010–16, the growth in average annual employment was 1.9 per cent, which was 2.7 per cent during 2005–10 (Table 3.2). Lower employment growth rate coupled with declining share of national income from agriculture may well have contributed to a low pace of labour income growth in comparison to the GDP growth. As a result, the income of the poor people—which typically depends on labour income—has been growing at a sluggish pace compared to that of the relatively richer ones.

The emerging scenario sends a cautionary note to the effect that poverty reduction in Bangladesh will become progressively challenging. Addressing the attendant tasks will call for improved targeted programmes favouring the more marginalised groups, creating jobs for them and expansion of the social safety net programmes. Along with this, the emergence of the urban poverty incidence inertia must also be thoroughly analysed and corrective steps should be taken.

Table 3.2

GDP Growth, Employment Growth, and Poverty Reduction Trends in Bangladesh

Average Annual	2000–05	2005–10	2010–16
GDP growth (%)	5.1	6.1	6.5
Employment growth (%)	3.3	2.7	1.9
Poverty reduction (percentage point)	1.8	1.7	1.2

Source: Authors' calculations from Bangladesh Bureau of Statistics (BBS) data.

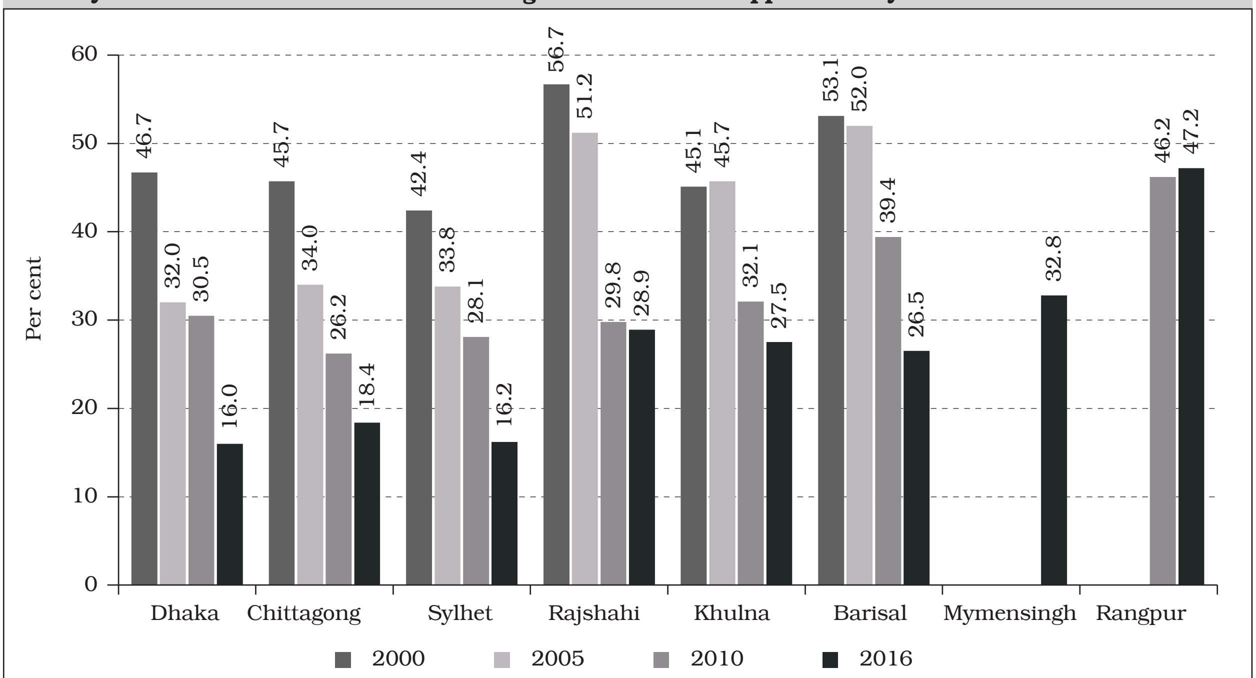
Note: Compound annual growth rate (CAGR) was deployed to calculate average annual growth of GDP and employment. For employment growth, figures from Bangladesh Labour Force Survey-1999-00; 2005-06; 2010; and 2015-16 was used.

It seems the East-West divide in the poverty scenario of Bangladesh has reappeared. Regional disparity in poverty incidence has been a longstanding feature in the economy of Bangladesh. The Eastern Divisions of Bangladesh (Chittagong, Dhaka and Sylhet) have traditionally fared well compared to their Western counterparts (Barisal, Khulna, Rajshahi) in the context of poverty incidence (Figure 3.2). The picture is about the same as regards the rate of poverty reduction in these Divisions. During the 2010–16 period, all the Eastern Divisions experienced significant decline in their respective poverty rates. At the same time, the Western regions—except Barisal—managed to ensure marginal poverty reduction. This scenario was in stark contrast to the 2005–10 period when the Western Divisions outpaced the Eastern ones with respect to poverty reduction. The newly formed Divisions, Mymensingh and Rangpur, for which long time series data is not available—also exhibit parallel dynamics.

On a positive note, standard of living indicators displayed some signs of progress over the corresponding period. In general, people's access to amenities — better housing material, drinking water source, sanitation, electricity, mobile and internet facilities — has improved over the 2010–16 period. Literacy rate has also

Figure 3.2

Poverty Rates in Different Divisions of Bangladesh Based on Upper Poverty Line



Source: BBS (2017).

Note: Mymensingh was under the Dhaka Division at the time of HIES 2010. Prior to 2010, Rangpur Division was part of Rajshahi Division. The poverty estimates of Rangpur Division for 2016 is not directly comparable with 2010 due to methodological differences.

portrayed improvement at national, rural and urban levels during 2010–16. However, the pace of progress in the urban areas was rather slow, and this holds for both male and female demographics.

Income growth has not been able to match expenditure growth. Household income has increased during 2010–16 at national, rural and urban levels. However, the pace of household expenditure growth has outpaced that of income at national and rural levels. During 2016, the expenditure for rural households has surpassed their income. To this end, it must be noted that rural households have witnessed a 47 per cent increase in expenditure between 2010 and 2016 while this figure was 27 per cent for the urban households. Income growth for both types of households was about 37 per cent.

The evidence of income concentration at the top is both disquieting and overwhelming. During the 2010–16 period, income inequality in Bangladesh was on the rise at national, rural and urban levels. Over the same period, consumption inequality was fairly constant. It was discussed earlier that income growth of the poor people was sluggish compared to that of the non-poor people. This factor is triggering an increase in income inequality. The share of income of the lowest 5 per cent of the households has dropped down to 0.23 per cent in 2016 from 0.78 per cent in 2010. In contrast, the income share of the top 5 per cent of the households has gone up to 27.89 per cent in 2016 from 24.61 per cent in 2010. This is another indication of income concentration at the top which has also contributed to increased income inequality.

The abovementioned scenario becomes even more depressing if household income distribution is investigated at the decile level. If monthly (nominal) income per household is considered, it appears that the bottom 5 per cent and 10 per cent households, at all levels, have suffered significant decline between 2010 and 2016. Meanwhile, the situation was favourable for households in other deciles – particularly in the top 5 per cent and 10 per cent levels (Table 3.3). However, the situation was more equitable between 2005 and 2010. Based on the above analysis, the unambiguous conclusion that can be inferred is that the rich are getting richer while the poor are getting poorer.

Table 3.3
Decile Distribution of Average Household Income

Household Distribution	2005			2010			2016			Growth *(%)		
	N	R	U	N	R	U	N	R	U	N	R	U
Bottom 5%	1,109	1,073	1,402	1,791	1,698	2,504	733	668	1,219	-59.1	-60.7	-51.3
Decile-1	1,441	1,371	1,883	2,296	2,152	3,262	1,610	1,415	2,618	-29.9	-34.2	-19.7
Decile-2	2,348	2,212	3,160	3,696	3,406	5,091	4,512	4,006	6,747	22.1	17.6	32.5
Decile-3	2,953	2,767	4,049	4,706	4,332	6,508	6,442	5,782	9,432	36.9	33.5	44.9
Decile-4	3,602	3,303	4,823	5,740	5,239	8,254	8,180	7,304	11,260	42.5	39.4	36.4
Decile-5	4,293	3,919	5,922	6,899	6,204	10,396	9,934	8,853	13,336	44.0	42.7	28.3
Decile-6	5,165	4,650	7,094	8,403	7,381	12,587	11,975	10,616	16,179	42.5	43.8	28.5
Decile-7	6,288	5,650	8,925	10,400	8,982	15,322	14,542	12,605	18,842	39.8	40.3	23.0
Decile-8	7,967	7,003	10,651	13,201	11,095	19,556	17,747	15,730	23,671	34.4	41.8	21.0
Decile-9	10,855	9,405	15,150	18,298	14,993	26,492	23,662	20,684	30,034	29.3	38.0	13.4
Decile-10	27,112	20,674	42,982	41,141	32,697	57,284	60,846	46,522	93,509	47.9	42.3	63.2
Top 5%	38,795	28,074	63,552	56,500	44,246	77,070	88,941	64,762	144,958	57.4	46.4	88.1

Source: Authors' calculations from BBS (2017).

Note: N, R and U imply National, Rural and Urban respectively. '*' indicates growth in 2016 over 2010.

Wealth inequality depicts an even direr picture. Bhattacharya *et al.* (2017) attempted to calculate wealth inequality for Bangladesh based on 2005 and 2010 HIES data.[2] Rich population's share in total wealth (in

[2] In this calculation, wealth was defined as the sum of value of agricultural assets, non-agricultural enterprises, owner-occupied houses, consumer durable goods, land and properties, and other assets.

terms of value) surged from 2005 to 2010 at the country, rural and urban levels while the scenario was exactly the opposite for the poor (Table 3.4). This situation is reflected on the upward movement in the Gini coefficient. Indeed, national Gini coefficient, which is 0.74, reflects a significantly high level of inequality by any standard.

Table 3.4
Percentage Share of Wealth at Household Level and Gini Coefficient

(in Per cent)

Household Distribution	National		Rural		Urban	
	2005	2010	2005	2010	2005	2010
Bottom 1%	0.00	0.00	0.00	0.00	0.00	0.00
Bottom 5%	0.06	0.04	0.01	0.08	0.02	0.02
Top 5%	47.99	51.32	35.24	35.75	51.67	53.64
Top 1%	24.00	28.87	13.63	16.22	24.32	30.09
Gini coefficient	0.72	0.74	0.63	0.62	0.78	0.79

Source: Bhattacharya *et al.* (2017).

3.2.3 Fiscal Framework

CPD, in its immediate reaction to the national budget for FY2017-18, had observed that the widening gap between planned and realised budget was becoming a common feature, and weakness, concerning the public finance framework. At the end of the FY2016-17, both from income and expenditure sides, the ambitious targets set for FY2016-17 did not materialise; rather, the gap has widened further when juxtaposed to that of FY2015-16. This is particularly true in case of resource mobilisation and public expenditure targets.

Revenue earnings

Since FY2013-14, the government had to revise the revenue targets, particularly National Board of Revenue (NBR) targets, downward, for four years in a row now. In FY2016-17, NBR's budgetary targets were slashed by Tk. 18,152 crore (7.5 per cent of the budgetary targets) from the original plan. With no exception to the previous years, NBR had put up a special effort to infuse momentum in revenue collection during the last quarter of FY2016-17; however, it has failed by a significant margin. At the end, NBR fell short even of its revised target by Tk. 13,502 crore. According to the Ministry of Finance (MoF) data, overall revenue earnings (i.e. NBR tax, non-NBR tax and non-tax) in FY2016-17 experienced a shortfall of about Tk. 42,000 crore from the original target. It may be noted here that, CPD had estimated that the total revenue earnings may fall short of the target by about Tk. 38,000 crore in FY2016-17 (CPD 2017b). Hence, revenue growth target for FY2017-18, which was already set at the higher level of 31.8 per cent based on the revised budget for FY2016-17, in effect resulted in the unrealistic growth target of 43.5 per cent. Final figures of FY2016-17 revealed that realised revenue collection growth was only 16.1 per cent (Table 3.5), with 82.7 per cent of

Table 3.5
Shifts in the Fiscal Framework: Growth Targets and Achievements in FY2016-17

Indicator	FY17B over FY16RB	FY17B over FY16A	FY17RB over FY16A	FY17A over FY16A	Attainment rate (%)	
					FY16	FY17
Revenue collection	36.8	40.4	26.3	16.1	83.0	82.7
NBR tax revenue	*35.4*	*38.9*	*26.5*	*17.3*	*82.9*	*84.4*
Non-NBR tax revenue	*34.3*	*28.4*	*28.6*	*11.6*	*96.1*	*86.9*
Non-tax revenue	*47.0*	*53.6*	*24.6*	*9.0*	*80.4*	*71.0*

(Table 3.5 contd.)

(Table 3.5 contd.)

Indicator	FY17B over FY16RB	FY17B over FY16A	FY17RB over FY16A	FY17A over FY16A	Attainment rate (%)	
					FY16	FY17
Total expenditure	28.7	42.4	32.6	9.3	81.1	76.8
ADP	*21.6*	*38.3*	*38.3*	*-3.5*	*82.5*	*69.8*
Non-ADP	*32.5*	*44.4*	*29.7*	*15.7*	*80.4*	*80.1*
Month when change reported	Jun'16	Sep'16	Mar'17	Sep'17		

Source: Authors' calculations from MoF (2017) data.

Note: FY17B refers to budgetary target growth in FY17; FY17RB refers to revised budgetary target growth in FY17; FY17A refers to actual growth in FY17.

the revenue collection target having been achieved in FY2016-17. This was quite similar to the attainment rate of 83 per cent in FY2015-16. Consistent falling of income tax's share in the revenue in recent years has emerged as a nagging concern. Share of income tax in FY2016-17 was only 29.5 per cent of total revenue income, declining from its peak of about 34.0 per cent in FY2013-14.

Expenditure

On the expenditure side, actual budgetary expenditure was rather poor when compared to the revenue earnings. Actual expenditure in FY2016-17 was only 76.8 per cent while the same was 81.1 per cent in FY2015-16. More importantly, spending on development projects was slower than the non-development expenditure in FY2016-17 and suffered from heavy spending towards the closing months, undermining the quality of work commonly known as the 'last quarter syndrome'. According to MoF data, implementation of Annual Development Plan (ADP) projects was found to be only 69.8 per cent of the original allocation. Indeed, the MoF data shows that actual spending in absolute term in FY2016-17 was also lower than that of FY2015-16.

It deserves to be noted here that, actual ADP implementation rate reported by the Implementation Monitoring and Evaluation Division (IMED) was 91.1 per cent of the original allocation; this was significantly higher than MoF data. Indeed, the difference is about Tk. 23,575 crore. Similar difference is also evident in case of revenue earning data reported by the NBR and the MoF. Thus, greater inter-ministerial coordination and consultation is called for to reconcile the final figures reported by these concerned government agencies.

Budget deficit

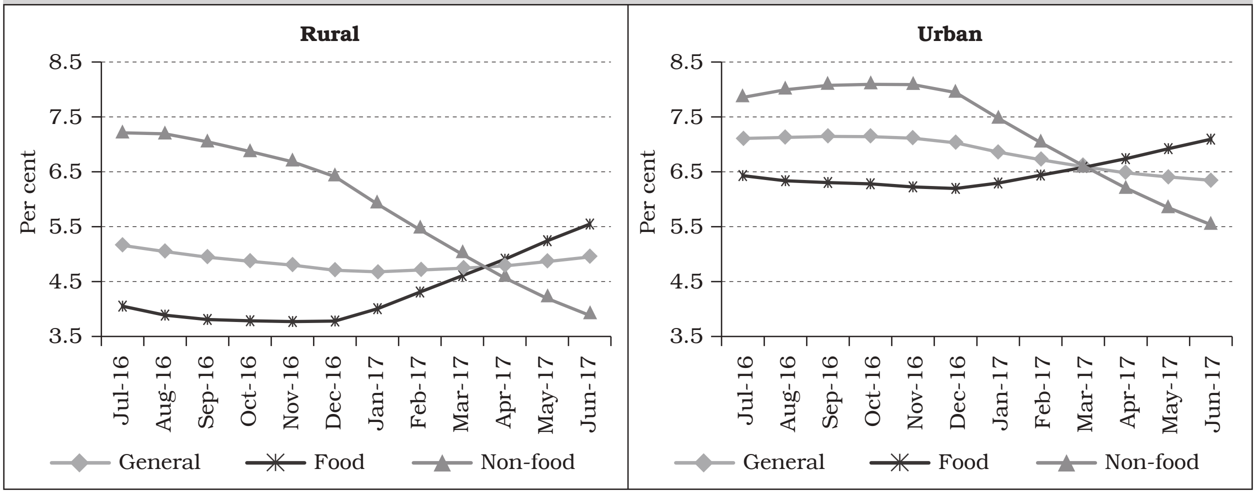
In the backdrop of persistent low levels of attainment of budgetary targets in FY2016-17, the budget deficit remained well within the target. Budget deficit turned out to be much lower at 3.1 per cent of GDP against a target of 5.0 per cent of GDP for FY2016-17. Yet again, heavy reliance was on domestic sources which accounted for about 87.0 per cent of total financing in FY2016-17. One predominant source of financing throughout the fiscal year was net sales of national savings directorate (NSD) certificates mainly because NSD's offer significantly higher interest rates than the banking system. At the end of FY2016-17, net sale of NSD certificates surpassed the original target of Tk. 19,610 crore by a significant margin with the accumulated figure turning out to be to the tune to Tk. 51,590 crore. At the end of FY2016-17, government's net borrowing from the banking system was (-) 8,515 crore indicating net repayment of earlier borrowing.

Evidently, the targets for FY2017-18 were set under the assumption that the revised targets for FY2016-17 will be attained when all accounts were closed. The year closing final figures now reveal that the revenue collection and public expenditure figures that were taken as reference numbers for preparation for the fiscal framework were on the high side and by significant margin. Taking note of the past trends, and interest rate on bank deposits being at low levels, one may apprehend that the financing plan for budget deficit in FY2017-18 will also diverge significantly in favour of high cost sources.

3.2.4 Inflation

According to BBS data, the annual average inflation in June 2017 was 5.4 per cent—well contained within the target of 5.8 per cent envisaged in the Monetary Policy Statement (MPS) of Bangladesh Bank. Indeed, inflation has steadily come down to 5.4 per cent in January 2017 and remained there until the end of FY2016-17. Non-food inflation started to drop from 7.5 per cent in September and stayed at 4.6 per cent in June 2017. On the other hand, food inflation started to move up from 4.5 per cent in December 2016 and reached 6.0 per cent in June 2017 primarily due to higher global food prices and various natural disasters. The *haor* flash flood in April caused significant loss of *boro* crops. This, coupled with the government's failure to achieve procurement targets of food grains and inability to ensure timely import of rice, resulted in high food inflation. Indeed, from April 2017 onward, food inflation started to climb above the national average, while non-food inflation went below the national average. The rural-urban dynamics of inflation was rather interesting in FY2016-17. For both food and non-food commodities, inflation was lower in rural areas throughout the FY2016-17 (Figure 3.3). However, as the Figure 3.3 depicts, rural areas tend to succumb to inflationary pressure in a more intense manner compared to urban areas.

Figure 3.3
Inflationary Trends in FY2016-17

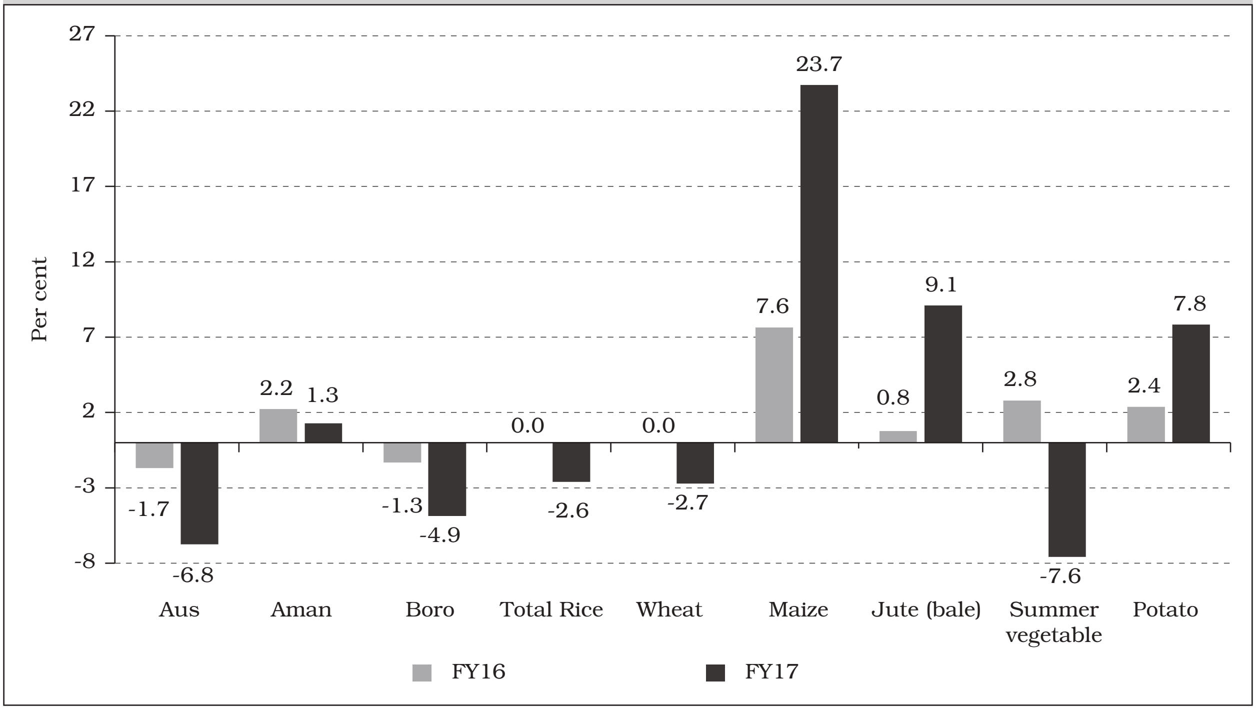


Source: Based on Bangladesh Bureau of Statistics (BBS) Data.

Production of both rice and wheat came down in FY2016-17. Indeed, food grain production was almost the same for the preceding two years (FY2016 and FY2015). In FY2016-17, food grain production declined by (-) 2.6 per cent. Actually, production of rice declined by 9.4 lakh metric tons (MT) and wheat production dropped by 0.4 lakh MT. The production shortfall of rice was mainly attributable to the loss of *boro* rice during the early flash flood in *haor* areas. According to the BBS, about 9.8 lakh MT *boro* rice was damaged during that flood. However, CPD, on the basis of analysis of the data of Department of Disaster Management (DDM), estimated that, the amount of damaged *boro* rice production was higher (15.8 lakh MT) than the official estimates. Similarly, summer vegetable crop was damaged by the early flash flood. Among the three main rice crops, only *aman* rice production posted a positive growth figure of 1.3 per cent (Figure 3.4).

In addition to production losses, weak management of public food stock exacerbated the food situation in FY2016-17. During the *boro* crop season of FY2016-17, the government managed to procure only 20 per cent of targeted amount of rice from millers and paddy from the farmers. At the same time, public food stock replenishment through import of rice was inadequate to stabilise the market price. The combined factors of significant *boro* crop loss in *haor* areas, the government's failure to procure planned amount paddy/rice,

Figure 3.4
Growth of Major Crop Production



Source: Authors' calculations from Bangladesh Bureau of Statistics (BBS) data.

delayed decision as regards duty reduction on rice import and unsuccessful attempts to import rice through public channels eventually transmitted wrong signals to the market. Consequently, the price of rice and hence, food inflation, surged significantly.

In contrast, high profitability of maize cultivation continued to incentivise the farmers to produce more maize. Production of maize rose significantly, registering a 23.7 per cent growth. Other than maize, the production growth rates of jute, potato, onion and winter vegetables were 9.1 per cent, 7.8 per cent, 7.7 per cent and 5.6 per cent respectively. Production growth rates of pulses, chilies, oilseeds were more or less business-as-usual.

3.2.5 Monetary Growth and Financial Institutions

Growth rates of different monetary aggregates in the elapsed fiscal year remained varied compared to their respective annual targets. Growth rate of broad money hovered around 13–14 per cent throughout the fiscal year and at the end of June 2017 ended up at only 10.9 per cent while the target limit was 15.5 per cent (Table 3.6). Credit expansion to the public sector was negative during the reporting period as the government made repayments to banks in the backdrop of lower demand for bank borrowings to service fiscal deficit. Growth of private sector credit was very consistent, about 16 per cent, and closed the year with 15.7 per cent growth while annual target was set at 16.5 per cent. Volatility in exchange rate during the last quarter of FY2016-17 contributed to the limiting of the excessive flow of net foreign assets, which gradually declined to 14.4 per cent as of June 2017. However, the growth was still higher than the programmed level of 10.1 per cent.

In the backdrop of consistent private investment, the classified loans in Bangladesh banking sector had come down during the first half of FY2016-17 (to 9.23 per cent of total loans outstanding) due to several

Table 3.6
Growth of Monetary Aggregates in FY2016-17

(in Per cent)

Monetary Aggregates	Actual FY16	Target FY17	Actual FY17
Net foreign assets	23.2	10.1	14.4
Net domestic assets	14.2	17.3	9.7
Domestic credit	14.2	16.4	11.2
Credit to public sector	*2.6*	*NA*	*-12.0*
Credit to private sector	*16.8*	*16.5*	*15.7*
Net other assets	*14.4*	*NA*	*19.7*
Broad money	16.3	15.5	10.9

Source: Bangladesh Bank Data.

provisioning and rescheduling measures concerning bad loans. However, at the end of June 2017, the figure once again stood at double digit level (10.1 per cent of total loans outstanding).

The banking sector experience was a major setback for the Bangladesh economy in FY2016-17. A number of new scams were exposed, which pushed the sector deeper into risky terrain in FY2016-17. The rise of non-performing loans (NPLs), lower capital adequacy and the overall lack of governance evinced the banking sector's growing weaknesses in FY2016-17. State-owned commercial banks (SCBs) faced serious capital deficit which in turn created additional fiscal pressure for the government. The government had to spend Tk. 1,585 crore for recapitalisation of the SCBs; however, the default loan situation of the SCBs failed to improve. It goes without saying that, there is hardly any justification to use public money towards compensating for the greed of bank defaulters and inefficient management of the sector. A number of private commercial banks have joined the ranks of those affected by poor banking governance. In spite of repeated calls to strengthen its supervisory-regulatory role, the central bank was not able to make any tangible dent in terms of improving the performance of the banking sector and state of financial sector governance. (Section 3.4.1 will discuss in details on governance in the banking sector.)

3.2.6 External Sector

While in FY2015-16 export earnings were able to achieve the target growth, export growth in FY2016-17 was rather disappointing. Throughout the FY2016-17, export performance was sluggish, finally registering only 1.7 per cent growth against the 8.0 per cent target growth. While the annual growth of the RMG sector was only 0.2 per cent, non-RMG products, in aggregate, were able to achieve the annual target (Table 3.7). Export growth to EU market[3] slowed-down gradually throughout FY2016-17, but managed to register 3.5 per cent growth. The other two traditional markets [United States of America (USA) and Canada] experienced negative growth (-6.0 per cent and -3.0 per cent respectively) mainly due to underperformance of the RMG sector.[4] The non-traditional market growth was 4.2 per cent.

Following a strong comeback in the second half, net foreign aid disbursement was about United States of America (USD) 2.6 billion in FY2016-17, posting a growth of 2.1 per cent. Indeed, it was during the last two months of the fiscal year when the bulk, about USD 1 billion aid, was disbursed. In the first half of FY2016-17 the net disbursement had experienced considerable volatility with (-) 12.7 per cent growth. Inflow of remittance had experienced a repeat major setback in FY2016-17 and recorded a double digit negative growth for the first time in the history, i.e. [(-) 14.5 per cent]. The gross remittance inflow of USD 12.8 billion

[3]EU market accounted for 55.5 per cent of total export earnings in FY2016-17.

[4]Indeed, non-RMG exports to USA and Canada markets registered higher growth compared to the EU markets.

Table 3.7
Comparison of Growth of Export Earnings in FY2015-16 and FY2016-17

(in Per cent)

Product	Growth Target FY16	Actual Growth FY16	Growth Target FY17	Actual Growth FY17
RMG	7.4	10.2	8.1	0.2
Knit	*6.8*	*7.5*	*6.1*	*3.0*
Woven	*8.0*	*12.8*	*10.0*	*-2.3*
Non-RMG	7.2	7.8	7.4	8.5
Raw jute	*0.4*	*55.2*	*5.1*	*-3.1*
Leather	*0.6*	*-30.1*	*0.8*	*-16.3*
Home textiles	*5.7*	*-6.4*	*2.9*	*6.1*
Frozen food	*1.8*	*-5.7*	*1.0*	*-1.7*
Total Export	**7.3**	**9.8**	**8.0**	**1.7**

Source: Authors' calculations from the Export Promotion Bureau (EPB) data.

in FY2016-17 was the lowest since FY2011-12. Curiously, during the same period, overseas employment continued to surge and registered a strong 32.3 per cent growth in FY2016-17, thanks to more than half the total migrant workers going to Saudi Arabia.

On the payment side, import growth was relatively steady and posted 9.0 per cent growth at the end of FY2016-17. A distinguishing feature of import in FY2016-17 was the import of high growth of consumer goods (i.e. edible oil, pulses and sugar). At the same time, some import substitution was also evident as raw cotton import was significantly high (12.7 per cent), while import of yarn (0.2 per cent) and textile articles [(-) 2.9 per cent] had seen a decline in growth. However, import of capital goods (with 24.4 per cent contribution) remained the major driver of the incremental growth in imports.

In the backdrop of high trade deficit [USD (-) 9,472 million in FY2016-17, which was USD (-) 6,460 million in FY2015-16], current account balance entered into the negative terrain [USD (-) 1,480 million] since FY2012. With lower trade credit (net) and commendable foreign direct investment (FDI) inflow in the financial account, Bangladesh's overall balance of payment (BoP) managed to keep a surplus of USD 3,169 million in FY2016-17 which was, indeed, USD 5,036 million in FY2015-16. To keep the balance intact, accumulated forex reserves played an important role. At the end of June 2017, forex reserves stood at USD 33.4 billion, which was USD 30.2 billion at the end of FY2015-16. However, after maintaining stability for a significant period of time, exchange rate of Bangladeshi Taka (BDT) against USD crossed the 80 BDT/USD mark in May 2017, after January 2013, to close FY2016-17 with a depreciation of 2.8 per cent.

3.3 MACROECONOMIC PERFORMANCE IN FY2017-18: EARLY SIGNALS

3.3.1 State of the Public Finance

CPD (2017b) had earlier predicted that, since the revised budget for FY2016-17 was unlikely to be realised, all major parameters of fiscal framework programmed in the budget for FY2017-18 would eventually require to register higher than planned growth rates. This apprehension has indeed turned out to be the reality following the publication of the final figures of FY2016-17. Indeed, for all indicators except for net borrowing from non-bank sources, the actual growth targets for FY2017-18 were found to be significantly higher than the targets set, taking the revised budget for FY2016-17 as reference point. For example, the total revenue growth target for FY2017-18, which was set at 31.8 per cent based on the revised budget for FY2016-17, rose to 43.5 per cent. Also, the growth target of public expenditure increased to 53.1 per cent from 26.2 per cent (Table 3.8). ADP expenditure in FY2017-18 will need to be almost twice the actual ADP expenditure in FY2016-17, the growth target for which was set at 38.5 per cent. Overall, budget deficit has been projected at 5.0 per cent of GDP (same as the revised budget for FY2016-17) while the actual deficit excluding grants for FY2016-17 was only 3.1 per cent. This has caused the deficit target to increase by 84.8 per cent in FY2017-18. Net foreign financing will need to be 5.6 times of FY2016-17 to reach the anticipated gross foreign aid flow of USD 7.6 billion. To compare, the highest corresponding figure in Bangladesh's history was USD 3.5 billion in FY2015-16.

Table 3.8

Fiscal Framework for FY2017-18: Target vs. Reality of Growth

(in Per cent)

Fiscal Parameter	Budget FY18 over Revised Budget FY17	FY18 over FY17 Actual
Revenue collection	31.8	43.5
NBR tax revenue	*34.2*	*44.7*
Non-NBR revenue	*18.8*	*36.0*
Total expenditure	26.2	53.1
ADP	*38.5*	*98.4*
Non-ADP	*19.6*	*34.0*
Overall deficit (excl. grant)	13.8	84.8
Net foreign borrowing and grant	80.5	557.3
Domestic borrowing	-13.7	14.3
Bank borrowing (Net)	*18.0*	*431.2*
Non-Bank borrowing (Net)	*-30.1*	*-47.6*

Source: Authors' calculations from Ministry of Finance (MoF) data.

Box 3.1

Data Paradox Continues

Data discrepancy continues to hinder a proper assessment of the public finance management system. Divergence between data provided by several government agencies, viz. NBR, IMED, Bangladesh Bank, and the Integrated Budget and Accounting System (iBAS) reported by the MoF, has been a case in point in recent years (Box Table 3.1, 3.2 and 3.3). CPD (2017a) has drawn attention to the divergence in the practices of different agencies—in terms of methodology; data collection tools and techniques; and accounting practices—to be key reasons behind this. It was also mentioned that, compared to the other available estimates, MoF figures are more reliable and methodical. Nonetheless, the prevailing scenario impedes budgetary monitoring and compromises the quality of fiscal and budgetary planning. Additionally, deployment of contingency measures based on contradictory data could be misleading. In this backdrop, CPD once again urges policymakers for reconciliation and consolidation of data between these estimates in order to enhance the monitoring mechanism and ensure the efficiency of public finance management.

Box Table 3.1

NBR Revenue Collection: Data Discrepancy

Fiscal Year	MRFP	NBR	Difference	% Departure from MRFP
	in Crore Tk.			
FY13	103,332	109,152	5,820	5.6
FY14	111,423	120,820	9,397	8.4
FY15	123,916	135,701	11,785	9.5
FY16	146,240	155,519	9,279	6.3
FY17	171,498	185,004	13,506	7.9
Jul-Aug FY18	28,207	27,162	-1,045	-3.7

Source: Authors' calculations from National Board of Revenue (NBR) and Ministry of Finance (MoF) data.

Note: MRFP refers to Monthly Report on Fiscal Position which is prepared by the Finance Division of the Ministry of Finance, GoB (Available from: www.mof.gov.bd/).

(Box 3.1 contd.)

(Box 3.1 contd.)

Box Table 3.2
ADP Expenditure: Data Discrepancy

Fiscal Year	MRFP	IMED	Difference	% Departure from MRFP
	in Crore Tk.			
FY13	49,474	50,035	562	1.1
FY14	55,328	56,913	1,586	2.9
FY15	60,004	68,524	8,520	14.2
FY16	80,042	83,581	3,539	4.4
FY17	77,265	100,839	23,574	30.5
Jul-Aug FY18	8,204	7,755	-449	-5.5

Source: Authors' calculations from Implementation Monitoring and Evaluation Division (IMED) and Ministry of Finance (MoF) data.

Box Table 3.3
Budget Deficit: Data Discrepancy

Fiscal Year	MRFP	Bangladesh Bank	Difference	% Departure from MRFP
	in Crore Tk.			
FY13	44,647	40,678	-3,969	-8.9
FY14	47,849	36,204	-11,645	-24.3
FY15	53,324	44,420	-8,904	-16.7
FY16	66,318	58,707	-7,611	-11.5
FY17	60,751	57,084	-3,667	-6.0
Jul-Aug FY18	1,077	15,296	14,219	1320.9

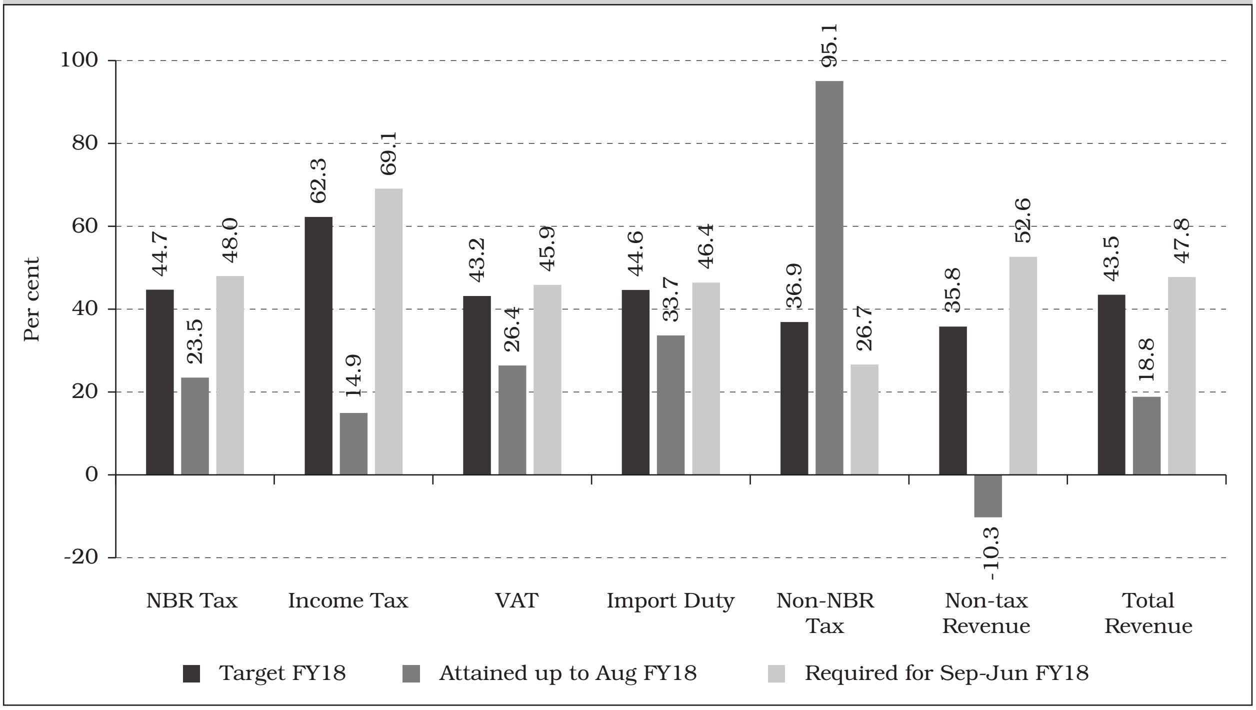
Source: Authors' calculations from Bangladesh Bank and Ministry of Finance (MoF) data.

Revenue earnings

Revenue mobilisation is anticipated to fall short of target for the sixth consecutive year in FY2017-18 in the backdrop of the very ambitious level set for attainment and failure of implementing the VAT and SD Act 2012. CPD had earlier predicted that the revenue shortfall in FY2017-18 could be between Tk. 43,000 crore and Tk. 55,000 crore (National Budget FY2017-18 Post-Approval Observations, 2017). During July-August of FY2017-18, total revenue mobilisation was 18.8 per cent higher than that of the corresponding period of the preceding fiscal year (Figure 3.5). In order to attain the annual growth target of 43.5 per cent, total revenue will have to increase at a rate of 47.8 per cent for the remainder of the fiscal year—which is highly unlikely to say the least. NBR achieved a growth of 23.5 per cent during the July-August period of FY2017-18 which was 24.1 per cent during the corresponding period of FY2016-17[5], well below the annual growth target of 44.7 per cent. The required growth of NBR collection for the rest of FY2017-18 will have to be 48 per cent. Of the NBR collected revenues, income tax rose only by 14.9 per cent during July–August of FY2017-18 against the annual growth target of 62.3 per cent—thus requiring a 69.1 per cent growth for the rest of FY2017-18. Non-tax revenue decreased by (-) 10.3 per cent while Non-NBR tax increased by 95.1 per cent during the first two months of FY2017-18. The boost in Non-NBR tax will not have a significantly large impact on the total revenue collection as it accounts for only 3.0 per cent of the total collection target. Recently, the Hon'ble Finance Minister informed the Parliament that revenue collection during the first five months of FY2017-18 increased by about 18 per cent, but also maintained that an early (and drastic) revision of the budgetary targets is not on the cards.

[5]According to data available from NBR, during July–October period of FY2017-18, revenue mobilised by NBR rose by 18.3 per cent compared to the corresponding period of FY2016-17. This was driven by modest performance in customs duty and VAT collection. Income tax collection increased by only 16.4 per cent during the aforesaid period, thus requiring a growth of about 43 per cent for the remainder of the fiscal year.

Figure 3.5
Growth Rates of Revenue Collection Components



Source: Authors' calculations from Ministry of Finance (MoF) data.

In the backdrop of anticipated shortfall, primarily emerging from the failure to implement the VAT and SD Act 2012, the government should explore alternative avenues of revenue mobilisation. To this end, the collection process of unpaid value added tax (VAT) accruing to the Large Taxpayers Unit (LTU) of the NBR should be prioritised. As has been reported in several media outlets, a number of large companies—including state owned Petrobangla—allegedly owe a large amount of dues in the form of unaccounted VAT. Appropriate use of the Alternative Dispute Resolution (ADR) system could be a useful step in this regard.

Another potential source of revenue could be the forthcoming auction of fourth generation (4G) mobile telecommunications licence by the Bangladesh Telecommunication Regulatory Commission (BTRC). The licensees will have to pay a number of fees, contribution and charges to the commission including: application/processing fee of Tk. 5 lakh; license acquisition fee of Tk. 10 crore; annual license fee of Tk. 5 crore; gross revenue sharing and social obligation fund of 5.5 per cent and 1 per cent respectively from annual audited gross revenue; and bank guarantee of Tk. 150 crore. As may be recalled, the base prices for auction of 2100 MHz, 1800 MHz and 900 MHz have been set at USD 27 million, USD 30 million and USD 30 million respectively per MHz of spectrum.

In view of the apprehended shortfall in revenue collection, a number of factors may put considerable stress in the fiscal management of FY2017-18 from the expenditure side. First, the required amount of resources to assist the persecuted *Rohingya* community could result in overstretching of the fiscal framework (discussed in details in section 3.4.3). Second, flood and subsequent damage control measures could take up a substantial amount of resources (discussed in details in section 3.4.2). And finally, public foodgrains import at higher cost from the international market in the backdrop of procurement failure could exacerbate the scenario further (discussed in details in section 3.3.2).

Non-development expenditure

During the first two months (July–August) of FY2017-18, total public expenditure (including both development and non-development expenditure) increased by 29.7 per cent compared to the corresponding period of FY2016-17. This is well below the annual growth target of 53.1 per cent. Non-development expenditure increased by 31.7 per cent during the aforementioned period. 'Pay and allowances' registered 53.4 per cent growth during July–August of FY2017-18. Over the same period, domestic interest payments increased by 26.4 per cent whereas foreign interest payments decreased by (-) 7.9 per cent. Subsidy and transfer expenditure increased by 18.7 per cent during July–August of FY2017-18 compared to the matching period of FY2016-17.

ADP expenditure

According to the IMED data, expenditure for ADP showed signs of improvement during the first five months of FY2017-18. Share of allocation spent over the first five–month period in FY2017-18 is the highest since FY2012-13, thanks to higher project aid expenditure. Data for July–November of FY2017-18 indicates that, actual spending under ADP was 20.1 per cent of the originally planned allocation of Tk. 155,931 crore (Annex Table 3.1). While only 18.5 per cent of allocated local resources (Taka component) was spent, which was the lowest in the last 10 fiscal years, project aid utilisation (22.6 per cent) is the highest since FY2010-11 (Annex Table 3.1). Analysis of the top 10 Ministries/Divisions, which account for 73.3 per cent of the total ADP allocation in FY2017-18, suggests that the expenditure in July–November was the highest (22.8 per cent) in the last five fiscal years, but was mainly driven by the Power Division (47.6 per cent) (Annex Table 3.2).[6] Power Division spent 54.8 per cent of its project aid allocation during July–November period of FY2017-18. This spending was mainly driven by the largest 15[7] out of 82 power projects for FY2017-18. Indeed, this has helped to increase both the total ADP expenditure and particularly the project aid utilisation to a large extent. Without Power Division, project aid utilisation and total ADP implementation rates would drop by 12 percentage points and 6 percentage points respectively for the July–November period of FY2017-18 (Figure 3.6).[8]

High financial progress but low physical progress concerning the completed projects is a disturbing feature of the ADP. In FY2015-16, out of 258 completed ADP projects 123 were declared 'completed' despite failing to meet physical implementation target. Out of the aforesaid projects, 33 projects (26.8 per cent) belonged to the Transportation sector and 20 to the Agriculture sector (Table 3.9).[9] Moreover, about three-fourths of these projects were enlisted as Investment projects. The average completion period of these projects was 5.3 years with the highest and the lowest durations being 18 years and less than one year accordingly.

In addition, in FY2015-16, a total of 134 ADP projects registered zero physical progress (out of 1,557 projects, i.e. 8.6 per cent), despite more than one-fourth of such projects accounting for at least some amount of financial expenditure. As far as the sectoral breakdown is concerned, 48 out of these 134 projects belong to the Transportation sector, followed by the Physical Planning, Water Supply and Housing sector (39 projects). The rest of the projects were shared by the remaining sectors. Moreover, an even more alarming fact is that 29 of these projects had zero physical progress despite more than 50 per cent of their respective allocations having been spent already. For instance, the 'Construction/Acquisition of 4 no. 108

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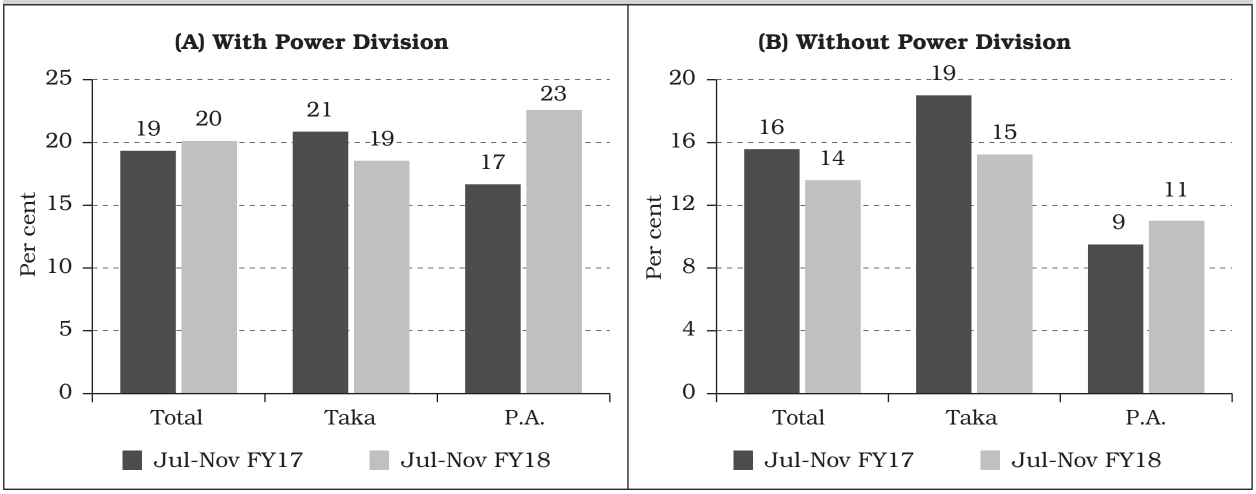
[6] The other Ministries and Divisions that have performed better than average include Road Transport and Highways Division (26.8 per cent), Local Government Division (23.8 per cent) and Ministry of Primary and Mass Education (23.7 per cent). The remaining ministries and divisions have registered below average performance during the aforementioned period.

[7] These 15 projects with a project aid allocation of 9,017 crore constitute 75.5 per cent of total project aid allocated for power division.

[8] Among 42 Ministries and Divisions that received project aid for FY2017-18, Power Division accounts for only 21.1 per cent of total project aid.

[9] 11 projects belonged to the Physical Planning, Water Supply and Housing sector and 9 to the Water Resources sector, while the rest were shared amongst other sectors.

Figure 3.6
Total ADP Implementation



Source: Authors' calculations from Implementation Monitoring and Evaluation Division (IMED) data.

TEU's Self /Propelled Cellular Container Vessel of 100 TEU's for BIWTC' project under the Ministry of Shipping, is one out of 14 such projects that already exhausted 100 per cent of their respective allocated funds but still accounted for zero physical progress during the aforementioned fiscal year.

Table 3.9
Characteristics of Projects with High Financial Progress but Low Physical Progress

<table>
<tr><td colspan="4">Projects Declared Completed without 100% Physical Progress</td></tr>
<tr><td rowspan="2">Number of projects 123</td><td>Top 5 Sectors (no. of projects)</td><td>Type of Projects</td><td>Completion Time (years)</td></tr>
<tr><td>Transportation 33
Agriculture 20
Physical planning, water supply and housing 11
Education and religion 10
Water resources 9</td><td>Investment 94
Technical Assistance 27
Self-financed 2</td><td>Average period 5.3
Highest completion period 18
Lowest completion period 0.8</td></tr>
<tr><td colspan="4">Projects with 'zero' Physical Progress</td></tr>
<tr><td></td><td>Top 2 Sectors (no. of projects)</td><td colspan="2">Number of Projects with</td></tr>
<tr><td>Number of projects 134</td><td>Transportation 48
Physical planning, Water supply and housing 39</td><td colspan="2">50% financial progress, but zero physical progress – 29
100% financial progress, but zero physical progress - 14</td></tr>
</table>

Source: Authors' calculations based on Implementation Monitoring and Evaluation Division (IMED) data.

Cost overrun of projects lead to wastage of public resource

In order to find the cost escalation of projects, CPD conducted an exercise covering all the projects which were declared completed in FY2006 and in FY2015-16, and which had a financial progress of 80 per cent or more. It was found from the analysis that in FY2015-16, out of 201 completed projects that had more than 80 per cent financial progress, 93 projects faced cost overrun with a cumulative amount of Tk. 5,640 crore (Annex Table 3.3). This additional amount is equivalent to 13.1 per cent of the costs of all the completed projects in FY2015-16 which is an increase of 36.1 per cent compared to FY2005-06. Ministry/Division-wise breakdown suggests that out of 24 Ministries and Divisions that faced cost escalation in FY2015-16, Local Government Division (Tk. 1,868 crore), Ministry of Communication (Tk. 1,073 crore), Energy and

Mineral Resources Division (Tk. 921 crore), Ministry of Food and Disaster Management (Tk. 661 crore), and Ministry of Primary and Mass Education (Tk. 356 crore) were the top five Ministries and Divisions which experienced increased cost escalation compared to FY2005-06. On a positive note, Power Division could minimise the escalated cost of its completed projects in FY2015-16 compared to FY2005-06.

Financing of budget deficit

Till August FY2017-18, budget deficit was well within the projected limit. Although a shortfall in revenue mobilisation is expected, it should be offset by lower expenditure in the public sector. Deficit financing was primarily driven by the buoyant sale of NSD certificates. NSD certificate sale up to August of FY2017-18 was Tk. 9,045 crore which is 30 per cent of the annual target of Tk. 30,150 crore[10]. On a positive note, foreign financing gained significant momentum during the first two months of FY2017-18. Higher utilisation of foreign aid in ADP implementation is also corroborating this trend. This is also reflected in the financial account of the BoPs (discussed in details in section 3.3.3).

Higher interest rates compared to bank deposits induced the savers to invest more in the NSD certificates. Table 3.10 presents a typewise distribution of incremental share of selected NSD certificate sale and associated interest rates. As can be seen, most of the sales increase occurred in instruments with higher interest rates from the 19 types available. From the fiscal management perspective this could become a pressure point in the context of debt servicing liability in the medium-term.

Table 3.10
Incremental Share of Selected NSD Certificate Sale and their Interest Rates

Name of Scheme	Incremental Share of Sales				Ongoing Interest Rate (%)
	FY14	FY15	FY16	FY17	
5-year Bangladesh savings certificate	10.99	10.70	14.92	6.64	9.35-11.28
Family savings certificate	7.05	39.30	13.30	33.44	9.50-11.52
3 monthly profit bearing savings certificate	63.15	33.71	0.68	32.18	10.00-11.04
Pensioner savings certificate	1.49	3.24	29.43	12.72	9.70-11-76
Post office savings bank - ordinary account	0.07	0.50	3.80	0.63	7.50
Post office savings bank - fixed deposit account	10.99	10.34	25.28	14.87	10.20-11.28
Wage earner development bond	1.88	1.75	12.06	-0.58	12.00

Source: Authors' calculations from Department of National Savings data.

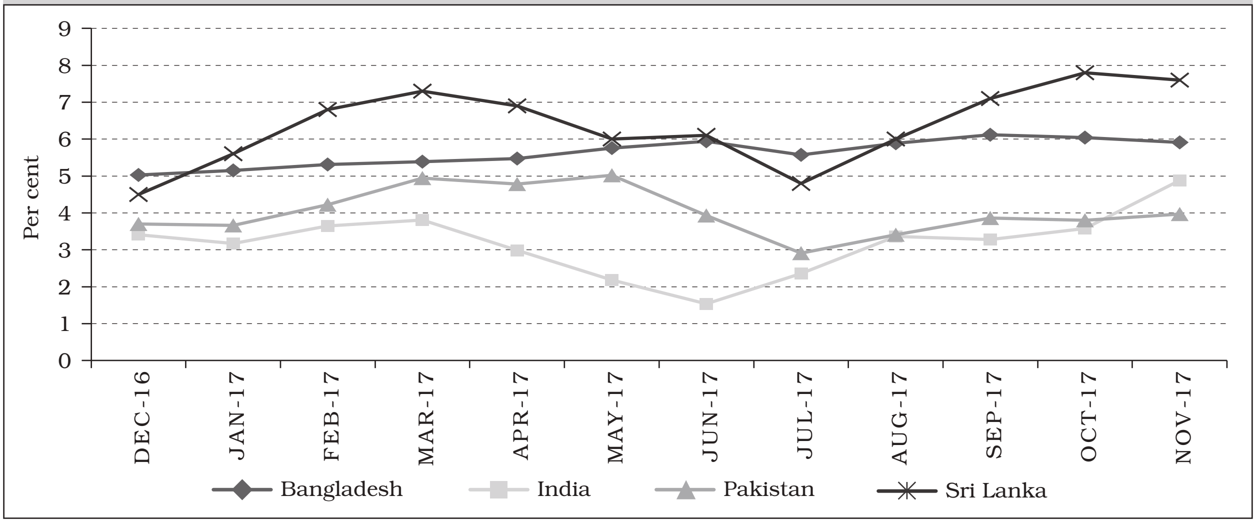
3.3.2 Inflation and Monetary Sector Scenarios

Inflation in Bangladesh and South Asian countries

Since mid-2017, Bangladesh, as is also the case with other South Asian countries, has experienced a rise in inflation (Figure 3.7). Consecutive floods in Bangladesh, and other natural disasters across the region, had adverse effects on domestic food production and food prices, and this was the main reason behind the inflationary pressure. In Bangladesh, the rate of inflation in December 2017 was 5.83 per cent. Though the overall inflation rate was within the MPS target (5.9 per cent for first half of 2018), food inflation was relatively high and rose significantly during this period (7.13 per cent in December 2017 *vis-à-vis* 5.38 per cent in December 2016). Rice, the major product in the commodity basket of the consumer price index (CPI), is currently traded at a price that is about 23.3 per cent higher than the previous year (Tk. 44–46

[10]According to Bangladesh Bank data, sale of NSD certificate till October of FY2017-18 was Tk. 17,315 crore which is 57.4 per cent of the annual target.

Figure 3.7
Inflation in South Asia



Source: World Bank (2017).

per kg for coarse rice in December 2017 against about Tk. 35−38 per kg in December 2016).[11] However, as Table 3.11 indicates, the rise in food inflation across the region during the June 2016–October 2017 period did not have a strong relationship with the global food market—domestic food price actually had negative correlation with global food prices. Nevertheless, a lagged response cannot be altogether ruled out.

Table 3.11
Correlation between Global Food Price Index and Local Food Price Index

Country	Food Price Index (Global vs Local)	Rice Price Index (Global-Rice vs Local-Food)
Bangladesh	-0.71	-0.83
India	-0.82	-0.80
Pakistan	-0.71	-0.91
Sri Lanka	-0.43	-0.26

Source: Based on data from WFP (2017).

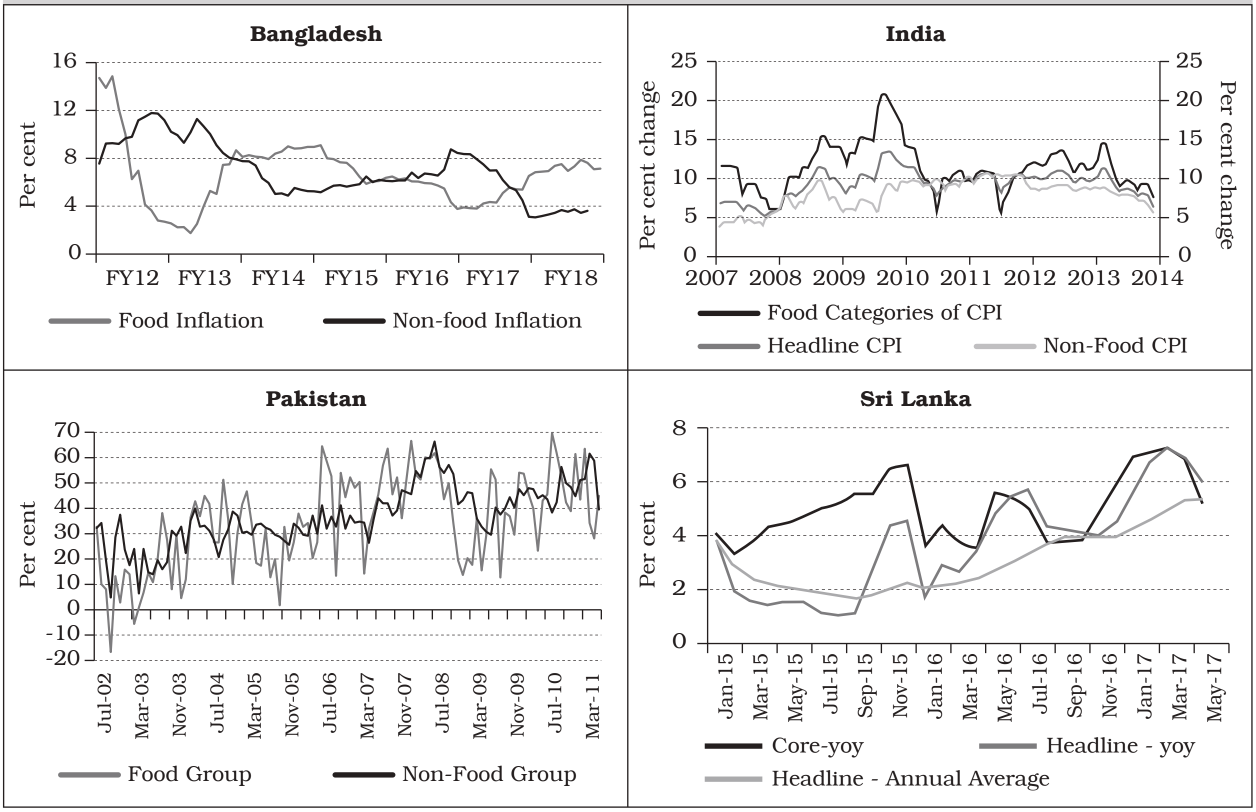
Relation between food and non-food inflation

Bangladesh's food and non-food inflation, unlike those of other South Asian countries, evince a peculiar trend. Food and non-food inflation in Bangladesh maintain a negative correlation (-0.32) which remains negative even in the lagged periods. Literature shows that this inverse relationship is not found in case of other South Asian countries and in other developing countries (Figure 3.8)[12]. Since July 2016, prices of most of the components of non-food inflation in Bangladesh have gradually reduced around the time when the food inflation had started to rise (Figure 3.9). Such trends in most of the components of non-food inflation is difficult to match with other available information. For example, the cost of living index of Dhaka (Available from: https://www.numbeo.com/cost-of-living/rankings.jsp)—particularly those of non-food indices for mid-2017—was either unchanged or had marginally increased *vis-à-vis* those of the comparable period of the previous years (Figure 3.10). Hence the official statistics of non-food inflation is not aligned with other relevant information.

[11] Prices of other variety of rice are also about 21−30 percent higher. Again, the price of wheat in December 2017 is 6.78 percent higher than the price in December 2016.

[12] In Bolivia, food and non-food inflation have a strong positive relation with lagged effect.

Figure 3.8
Food and Non-Food Inflation



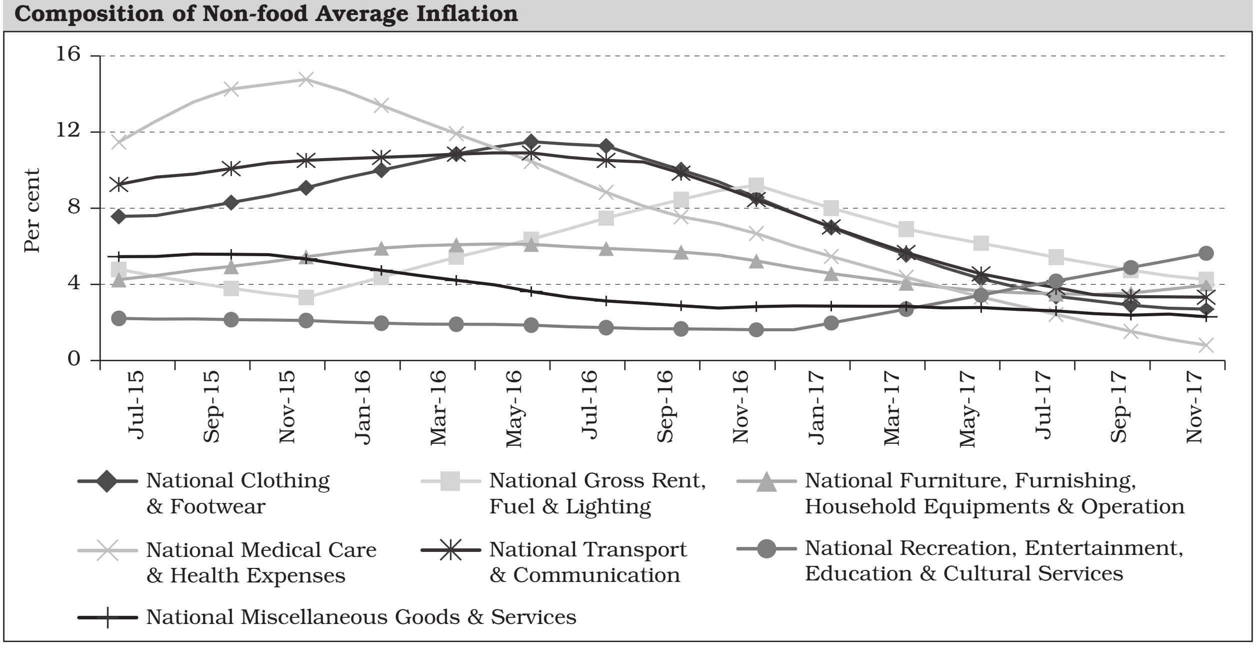
Source: For Bangladesh: Bangladesh Bank

For India: https://www.imf.org/external/pubs/ft/wp/2016/wp1602.pdf

For Pakistan: https://mpra.ub.uni-muenchen.de/45009/1/MPRA_paper_45009.pdf

For Sri Lanka: Department of Census and Statistics, Sri Lanka

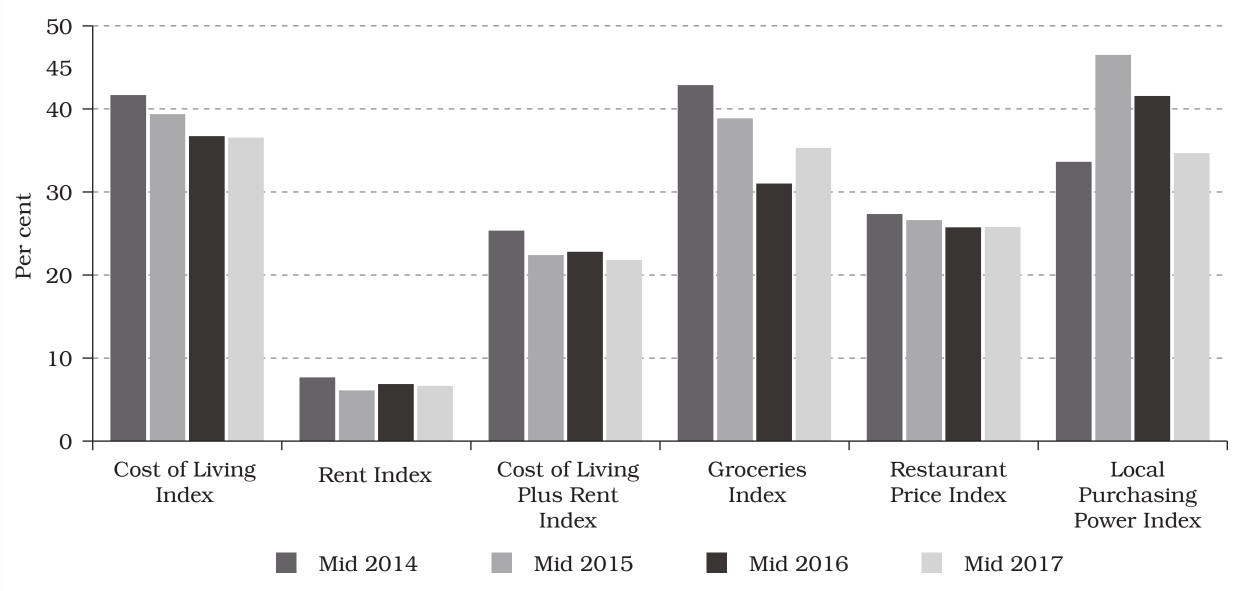
Figure 3.9
Composition of Non-food Average Inflation



Source: BBS (2017).

Figure 3.10

Cost of Living Index in Dhaka



Source: Based on the data available from: https://www.numbeo.com/cost-of- (accessed on 8 January 2018).

Impact of inflation on households and government's initiatives

The burden of the spike in inflation was difficult to accommodate by consumers—particularly those belonging to low-income households. For example, a possible means to compensate for high inflation would have been a rise in nominal wages in various sectors over that of rate of inflation. However, during October 2017 the wage indices for major economic activities experienced a rise between 6.1 per cent and 7.5 per cent over the comparable period of the previous year (Table 3.12). The slow growth in wage indices was observed in case of construction (6.1 per cent) and services (6.4 per cent) and relatively high growth was seen in case of fishery (7.2 per cent) and production (7.5 per cent). In other words, the slow rise in wages alongside the increase in inflation left workers of some sectors (such as construction and services) with just enough to meet the bare minimum requirement of household expenses.

Table 3.12

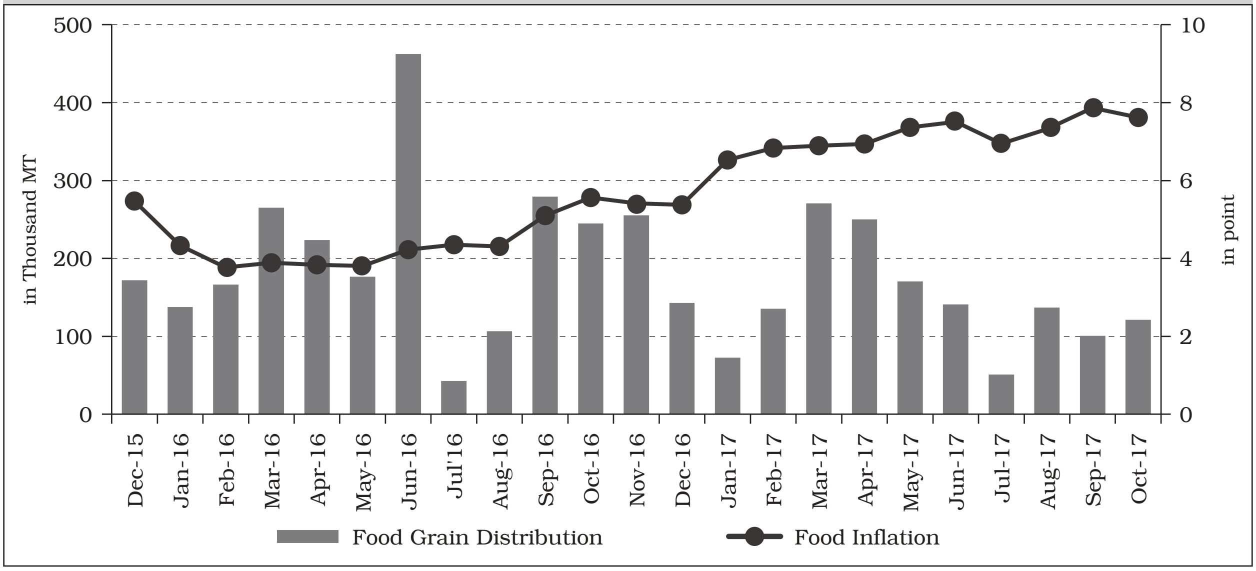
Changes in Wage Indices in Major Economic Activities

Sector	**October 2016–October 2017**
Agriculture	6.6
Agriculture	*6.6*
Fishery	*7.2*
Industries	6.7
Construction	*6.1*
Production	*7.5*
Services	6.4
General	**6.6**

Source: BBS (2017).

Figure 3.11

Trends in Food inflation and Public Food Distribution



Source: Ministry of Food; WFP (2017).

In view of this adverse situation, government's food and non-food support under the different safety net programmes was expected to provide at least some relief to the low-income households. Regrettably, government's safety net related activities, particularly distribution of food grain, was found to be inadequate. During January–November 2017 total distribution of food was 1.68 million MT, which was 28.8 per cent less (2.36 million MT) compared to the same period of the previous year. Most importantly, the food grain distribution was at the lowest level when the inflationary pressure was at its peak (Figure 3.11). Food grain distribution was inadequate in the second quarter of FY17 and the first and second quarters of FY18. This state of poor food grain distribution at a time of high food inflation is likely to have adversely impacted on the purchasing power of the low-income people with consequent implications for poverty and food insecurity.

A major reason behind the failure to ensure adequate food supply under the Public Food Distribution System (PFDS), at a time of high food inflation during FY17 and FY18, is inadequate food grain stocks. If the inverse relationship between availability of food stock and food inflation (correlation coefficient: -0.75) is considered, low food stock in FY17 and FY18 may have contributed to a further upward push in the food price. The high food inflation is likely to continue in the coming months, which will further erode consumers' purchasing capacity. The situation is exacerbated because of lower production of *aman* rice against the targeted amount which had adverse impact on public procurement. A simple exercise of requirement of food stock for distribution under PFDS for the rest of the FY2017-18 period shows that there will be a possible shortfall of food grain, ranging between 0.21 to 0.35 million MT (Table 3.13). This amount of food grain needs to be imported through public channel (without depending on purchase from the private sector, from the local market). This would require an additional food budget to the tune of about Tk.700 crore to Tk.1,152 crore. Hence, necessary provision of funds as well as appropriate initiatives for import should be undertaken in the coming months.

Table 3.13
Requirement of Food to Replenish PFDS Stock during Second Half of FY2017-18

(in Million MT)

Particular	FY18 (Target)	FY 18 (Actual as of 21 Dec, 2017)	Difference between Target and Actual	Difference between Target and Actual (assuming Aman procurement target is met)
Food distribution	2.44	0.66	1.78	1.78
Rice	*1.86*	*0.52*	*1.34*	*1.34*
Wheat	*0.58*	*0.14*	*0.43*	*0.43*
Food procurement (domestic)	1.10	0.60	0.50	0.14
Rice	*1.00*	*0.50*	*0.50*	*0.14*
Wheat	*0.10*	*0.10*	*0.00*	*0.00*
Public import		0.83		
Rice		*0.53*		
Wheat		*0.30*		
Requirement of food for distribution (4=1-2-3)			0.35	0.21
Rice			*0.31*	
Wheat			*0.04*	
Cost of import (USD)		395		83.58 million
Cost of import (BDT)		33,180	1,152 crore	702.10 crore

Source: Based on the Data of the Ministry of Food, Government of Bangladesh (GoB).
Note: Import price is considered to be USD 395 per MT; Exchange rate 1 USD is equal to BDT 84.

Growth of monetary aggregates

By and large, the monetary sector remained at subdued level during the first half of FY2017-18. Overall growth of broad money (M2) till November, 2017 was 10.8 per cent against the MPS target of 12.9 per cent for December 2017 (Table 3.14). In recent years, growth of broad money was significantly influenced by one or two components instead of the balanced growth of the involved components. During FY2015 to FY2018 (up to November, 2017), growth of major components of broad money experienced a mixed trend (Figure 3.12)—on the one hand, growth of net foreign assets decelerated (only 6.4 per cent up to October 2017) and public sector credit significantly declined [(-)14.8 per cent as of November 2017]; on the other hand, credit to the private sector experienced considerably high growth (19.1 per cent up to November 2017) which was even higher than the MPS target for the first half of FY2017-18 (16.2 per cent for December 2017). Among

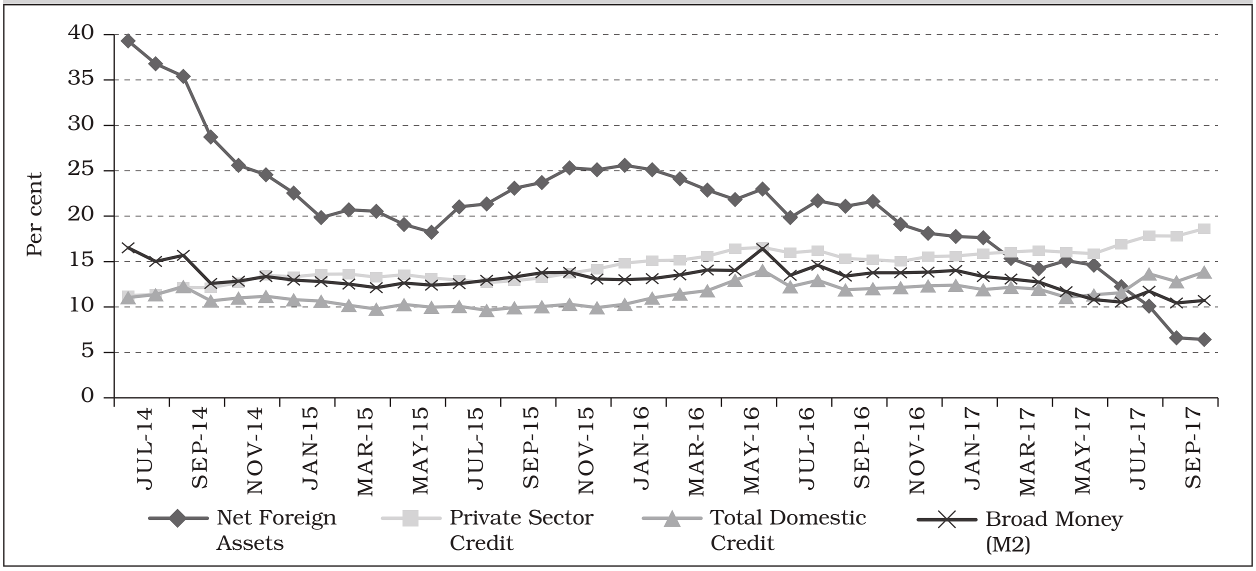
Table 3.14
Growth of Monetary Indicators (Outstanding as of November 2017)

Indicator	June 2016 (Actual)	June 2017 (Actual)	December 2017 (Target)	November 2017 (Actual)
Net foreign assets	23	14.6	4.7	6.4*
Net domestic assets	11.9	11.9	15.9	12.3*
Domestic credit	14	11.3	14.4	14.5
Credit to the public sector	*3.6*	*-14.8*	*3.8*	*-14.8*
Credit to the private sector	*16.6*	*15.9*	*16.2*	*19.1*
Broad money	16.4	10.8	12.9	10.8

Source: Bangladesh Bank (2017).
***Note:** Figures are outstanding up to October 2017.

Figure 3.12

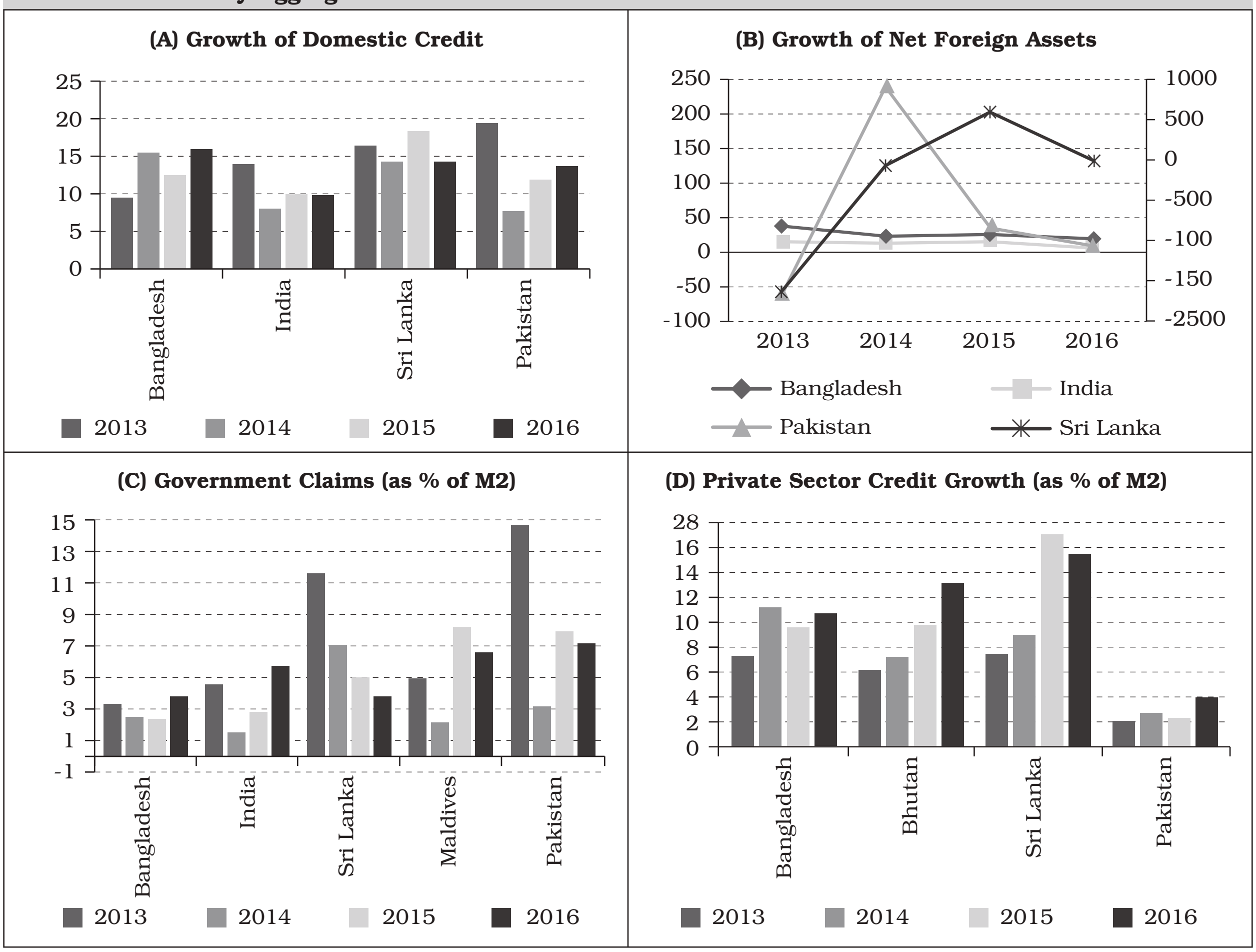
Growth of Monetary Aggregates: FY15 to FY18 (up to October)



Source: Bangladesh Bank (2017).

Figure 3.13

Growth of Monetary Aggregates in Selected South Asian Countries: 2013-2016



Source: World Bank [https://data.worldbank.org/indicator/FB.AST.NPER.ZS (accessed on 6 January 2018)].

the South Asian countries, such a mixed trend is observed in case of Sri Lanka (high growth of private sector credit and negative growth of foreign assets and slowdown of government credit) (Figure 3.13). This is happening at a time when the performance of Sri Lanka's financial sector has weakened.[13] In this backdrop, it is necessary to examine the structure, and composition of growth of key components of broad money, with a view to understand the quality of money supply growth in Bangladesh.

The quality of broad money growth can be examined through various indicators. The income velocity of money, measured by ratio of broad money and GDP, followed a declining trend over the past several years apart from FY2016-17 when there was a rise—from 1.89 in FY2015-16 to 1.94 in FY2016-17 (Table 3.15). A slowdown in income velocity may reduce the speed of transactions of real goods and services. Given the sluggish growth of M2 in FY2017-18 with a possible higher growth in GDP, velocity of money may

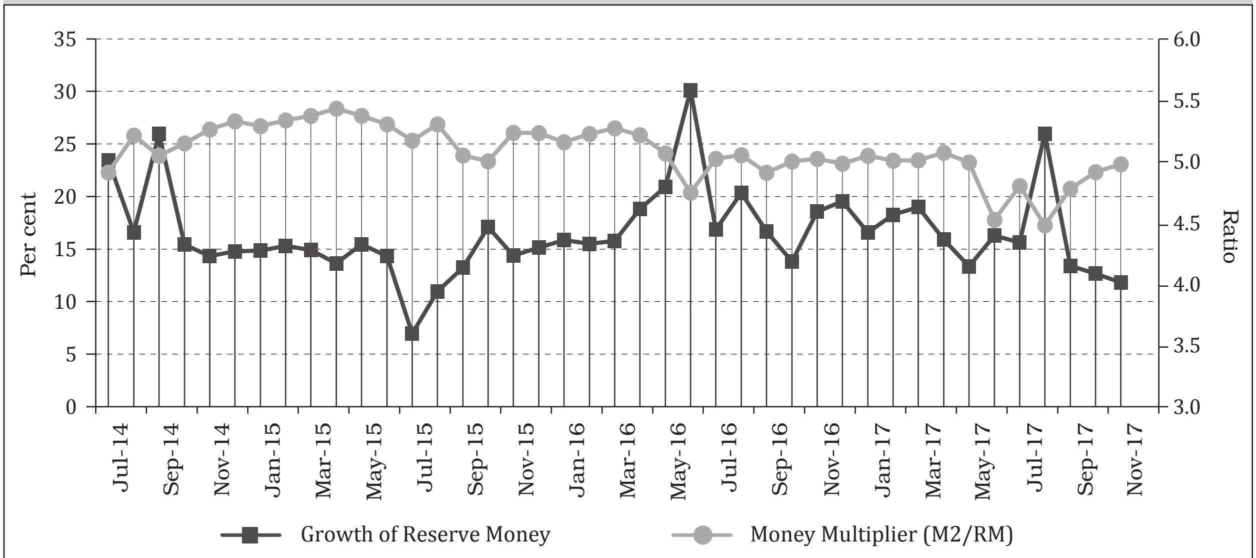
Table 3.15
Income Velocity of Money

(in Billion Taka)

Fiscal Year	GDP at Current Market Price	Broad Money (M2) (end June position)	Income Velocity of Money
FY10	7975.39	3630.31	2.20
FY11	9158.29	4405.20	2.08
FY12	10552.04	5171.10	2.04
FY13	11989.23	6035.05	1.99
FY14	13436.74	7006.24	1.92
FY15	15158.02	7876.14	1.92
FY16	17328.64	9163.78	1.89
FY17	19758.17	10160.76	1.94

Source: Bangladesh Bank (2017).

Figure 3.14
Growth of Reserve Money and Money Multiplier



Source: Bangladesh Bank (2017).

[13]Sri Lanka's ranking in financial development in case of global competitiveness index has slipped in recent years from 72 in 2015 to 96 in 2018. Similar to that, Bangladesh's ranking in the same indicator has declined from 88 in 2015 to 98 in 2018.

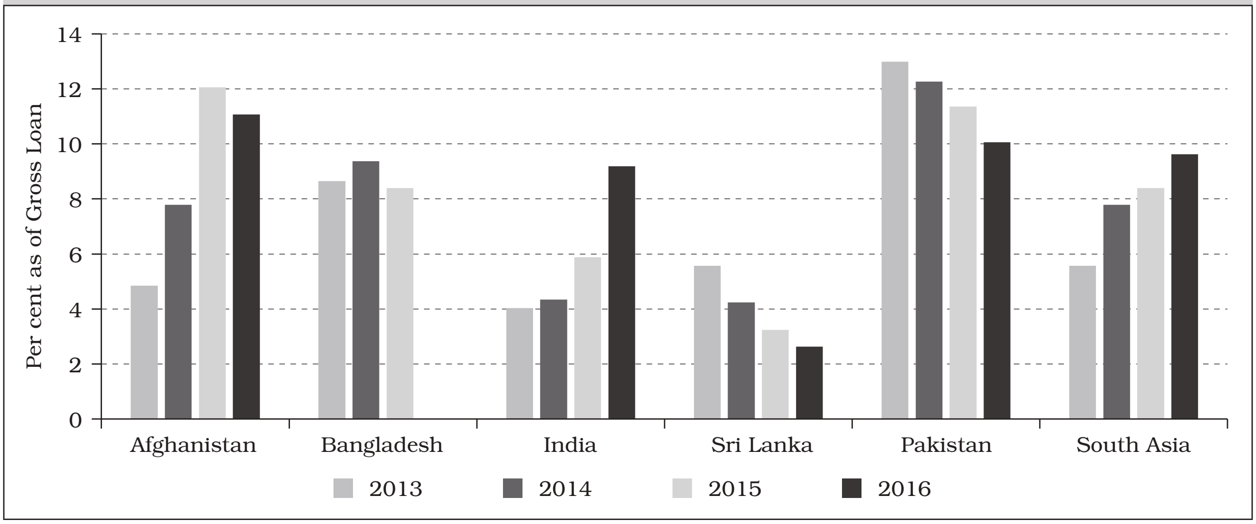
experience a further slowdown in FY2017-18 which would have further adverse effects on transactions in the real sector. Similarly, money multiplier decreased from 5.02 in November 2016 to 4.98 in November 2017 which pushed banks to maintain higher reserve money (Figure 3.14). Due to lower demand for credit, liquidity in the banking system remains high. Total liquid asset amounted to Tk. 261 thousand crore as of September 2017, while the minimum requirement was Tk. 169 thousand crore.

Private sector credit

The growth of private sector credit till November 2017 exceeded the MPS target which apparently is indicative of a buoyant growth of investment in the country. While a part of growth of private sector credit is attributed to investment in major industry and infrastructure sectors, a part of the rise in private sector credit is linked to other activities. With the rise in private sector credit, some compositional changes in advances were observed where share of advances to some traditional sectors such as trade and commerce was overtaken by the industries sector. The highest share of advances is now in the industries sector (38.9 per cent) followed by retail trade and commerce (35.6 per cent). More specifically, rise in share in advances was observed in case of term loan and working capital distributed to large, medium and small industries and construction sectors. On the other hand, decline in credit was observed in case of retail trade, export financing and import financing. Such a compositional change is likely to help in industrial growth. However, a high share of NPL in Bangladesh (which is close to the South Asian average), mostly attributed to the industries sector, has put the quality of private sector credit under scrutiny (Figure 3.15).

Figure 3.15

NPL 2013–16



Source: World Bank [https://data.worldbank.org/indicator/FB.AST.NPER.ZS (accessed on 6 January 2018)].

Excess liquidity in the banking sector contributed to pushing down both deposit and lending rates. The lending rate declined at a slower pace compared to that of the deposit rate.[14] A disaggregated sector-wise analysis showed that the decline in lending rates was not at the same level in all the sectors (Table 3.16) – despite the reduction. Relatively high lending rates prevailed in case of advances through credit cards (36 per cent), term loans to small industries (18 per cent), working capital to large and small industries (18-19 per cent) and housing loans (17.8 per cent). On the other hand, a relatively low lending rate prevailed

[14]The lending rate and deposit rate declined from 9.94 per cent and 5.29 per cent respectively in November 2016 to 9.30 per cent and 4.90 per cent respectively in November 2017. At the end of November 2017, the interest rate spread remained at 4.40 per cent, which decreased by 0.25 percentage points from the previous year.

Table 3.16
'Maximum' and 'Minimum' Lending Rates by Sectors during November 2013 – November 2017

Activity	Nov 2013		Nov 2014		Nov 2015		Nov 2016		Nov 2017	
	Max	Min	Max	Min	Max	Min	Max	Min	Max	Min
Agriculture	13	4	13	4	11	4	10	2	9	2
Term loan to large and medium scale industry	18	10	17.5	8	17	9	16.5	5	16.5	6
Term loan to small industry	23.75	12.5	23.75	10	18	11	20	8	18	8
Working capital to large and medium scale industry	18	11	18	8	18	7	18	3.5	18	5.9
Working capital to small industry	23.75	12.5	23.75	11	24	11	20	8	19	8
Export	7	7	7	7	7	7	7	6.75	7	6.75
Trade financing	19.5	11	18.5	7.5	18	10	17	9	15.75	9
Housing loan	19.5	5	19.5	9	18	10	17.75	7	17.75	8
Consumer credit	23	12.5	23	10	19	12	19	9	19	8.25
Credit card	31.5	18	30	18	35	18	34.5	18	36	14
Credit to NBFIs	20.5	10	20.5	8	18	8	17	5.25	19	4.75
Others	20.5	4	19	5	20	5	19	2.88	19	2.88

Source: Bangladesh Bank (2017).

in case of agriculture (9 per cent) and export (7 per cent). In each sector, the gap between maximum and minimum lending rates were still quite high. Hence, despite a decline in the interest rates, high rates of lending continued to prevail in key sectors, discouraging investors.

The quality of private sector credit can be examined through a number of other indicators. First, there is a growing concentration of bank lending to large and medium scale industries. Both the stress test and resilience test indicate that having a default incurred by 3, 7 and 10 largest borrowers in each bank, the number of banks which could become non-compliant [in maintaining the minimum required Capital to Risk Assets Ratio (CRAR)] was 25, 38 and 4 respectively (Bangladesh Bank, 2017). Second, rising share of NPLs may put a number of banks at high risks – the rise in NPL by 3, 9 and 15 per cent was likely to put 6, 27 and 37 banks respectively in a situation where they could become non-compliant (to maintain the minimum required CRAR) (Bangladesh Bank, 2017). Thus the quality of private sector credit needs to be monitored very closely and necessary initiatives will need to be taken both by the central bank through strict supervision, and by the commercial banks through better credit and risk management to improve the quality of private sector credit.

Public sector credit

Government's dependence on non-bank financial instruments to meet its fiscal requirement continued in FY2017-18. During the July–October period, the government's net borrowing from non-bank sources was 18,193 crore which was 9.7 per cent higher than the comparable period of the previous year. During this period (July–October 2017), the government repaid interest payment of Tk. 6,732 crore against the principal amount of Tk. 9,468 crore. The government of Bangladesh (GoB) should be cautious about the repayment burden it is creating, owing to the increasingly accumulating borrowings on account of the NSD. It may be recalled that, CPD in its earlier IRBD reports argued for putting a lower ceiling on NSD sales and a downward review of the interest rates. If the government could borrow more from the banking system, it would reduce the pressure of excess liquidity.

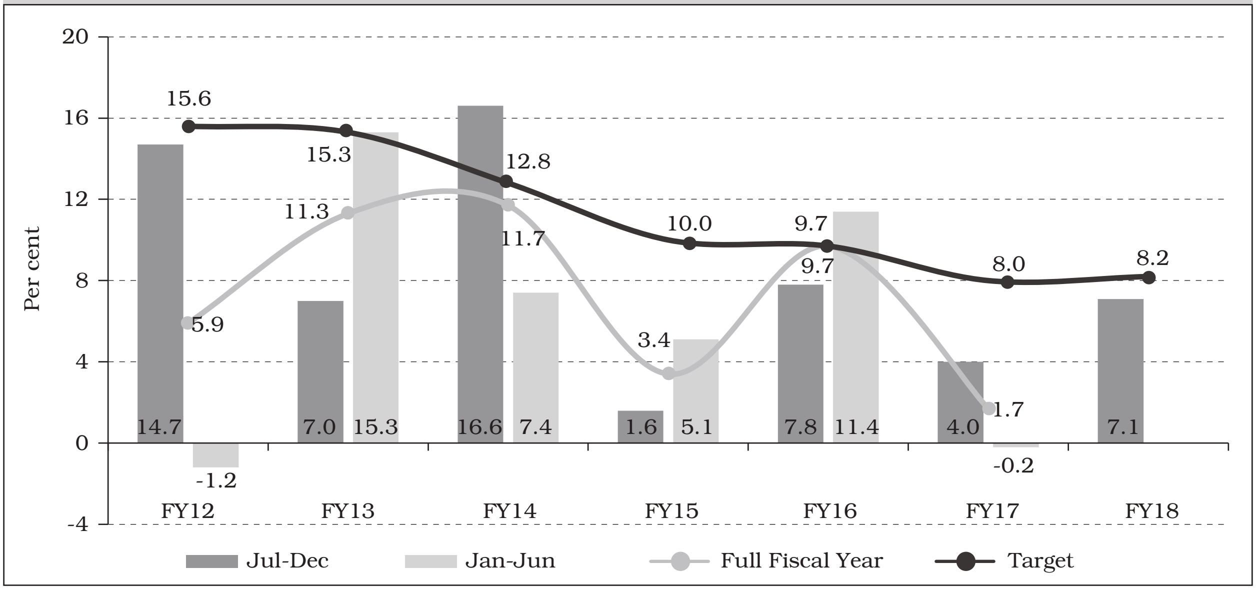
3.3.3 External Sector Performance

Export earnings

In a departure from the disquieting developments experienced in FY2016-17, the export sector of Bangladesh evinced some positive signals during the first half of FY2017-18. Exports bounced back and the growth rate was aligned with the annual target set for FY2017-18. Total export earnings during the first half of FY2017-18 was USD 17.9 billion and the recorded growth rate was 7.1 per cent for July–December of FY2017-18, against the 4 per cent growth in the corresponding period of FY2016-17.[15] Export growth fell short of the target growth for all the years post-FY2010-11 barring FY2016 (Figure 3.12). However, the export growth of earlier months suggests that it is well on track to attain the FY2017-18 target growth of 8.2 per cent for achieving the envisaged export earnings of USD 37.5 billion. A period-on-period growth of 9.2 per cent will be required in the remaining half (January–June) of FY2017-18 to reach this target (Figure 3.16).

Figure 3.16

Export Growth Targets and Achievements for Recent Fiscal Years



Source: Authors' calculations based on data from the Export Promotion Bureau (EPB).

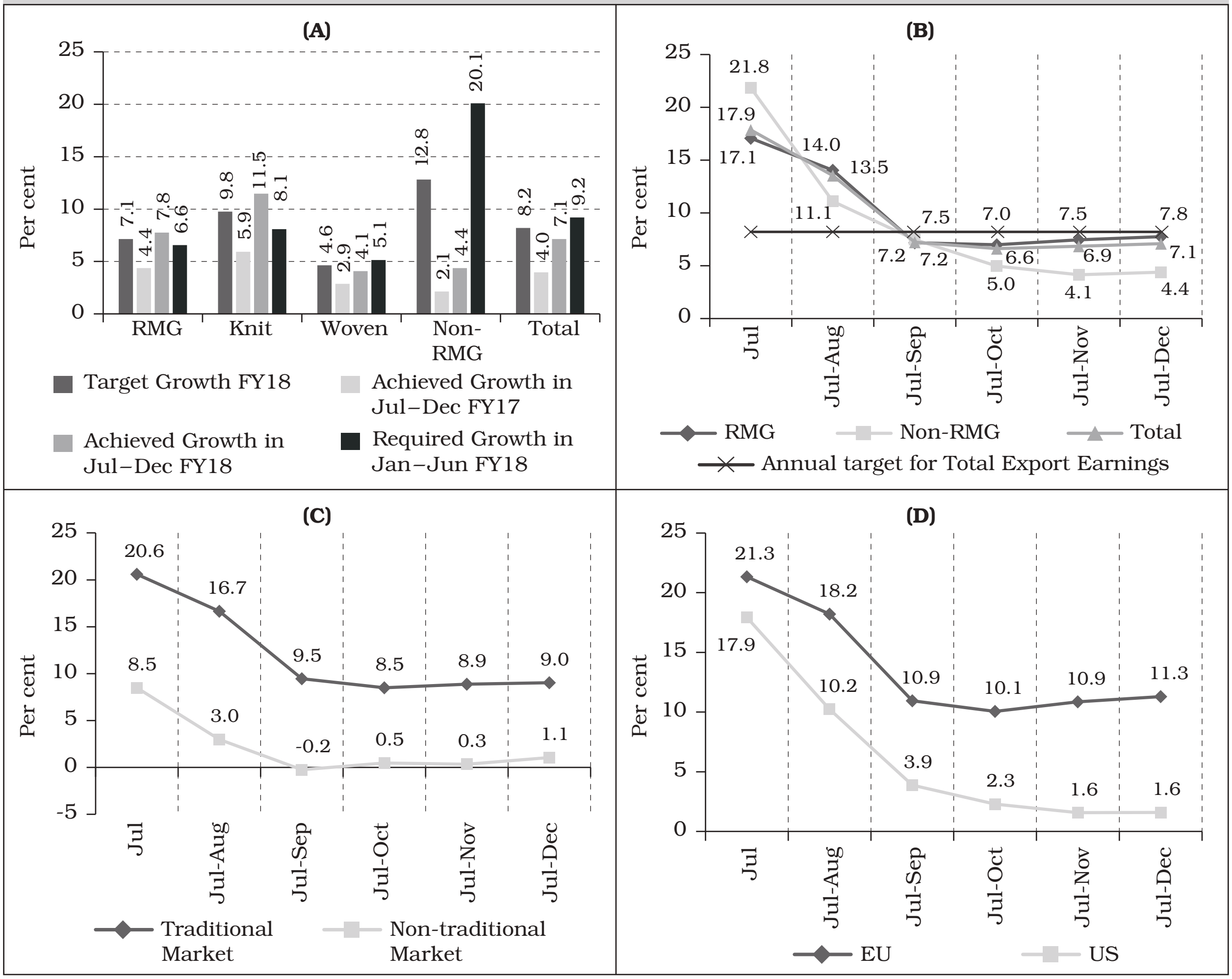
A trend growth analysis of export data for the last five years indicates a cyclical pattern of growth performance during the two halves of respective fiscal years. If the growth was robust in the first half of a fiscal year, growth in the second half tended to be low and vice versa; export growth was buoyant against low benchmark growth (growth rate of corresponding half of previous fiscal year) and depressed against high benchmark growth (Figure 3.17A).

RMG recorded a growth of 7.8 per cent during July–December period of FY2017-18 providing a Phillip to the overall export earnings (Figure 3.17B). Accelerated growth of RMG exports was particularly observed in the second quarter of FY2017-18, thanks to the growth in export of knit products (11.5 per cent). Regrettably, growth from non-RMG export earnings (4.4 per cent) was unable to keep pace, particularly

[15]FY2016-17 started off with negative growth in total export earnings [(-) 3.5% for the month of July 2016] with a fall in export earnings from a major driving component, RMG [(-) 4.4 per cent growth] constituting of knit and woven which showed negative growth of similar extent. The growth in export earnings was way below the target of 8 per cent almost all through FY2016-17, ending with 1.8 per cent fiscal year-on-fiscal year growth in June 2017.

Figure 3.17

Growth (Period on Period) for July–December FY2017-18



Source: Authors' calculations based on data from the Export Promotion Bureau (EPB).

in non-traditional markets. Growth of non-RMG exports to the traditional markets[16] was 11.7 per cent in July–Dec 2017 and (-) 0.2 in non-traditional markets.

Market analyses show that exports to the key traditional markets gained some momentum with a growth of 9.0 per cent (Figure 3.17C)[17], which was higher than the growth rate for the corresponding period in FY2016-17 (4.8 per cent) and in FY2015-16 (7.5 per cent). Export growth in the EU market picked up by 11.3 per cent after an initial fall[18] (Figure 3.17D). Phase-out of the initial shock emanating from the Brexit was one possible reason. Some upturn in the global economic outlook and the attendant demand was another reason. Future export in the key United Kingdom (UK) market will depend on how the Brexit negotiations span out in the coming years. Trade arrangements that Bangladesh is able to negotiate following graduation from the least development country (LDC) status will also have implications for the duty-free market access currently enjoyed in the European Union under the Everything But Arms (EBA) scheme. Following Bangladesh's graduation from LDC status, exports will lose the preferential margins and

[16]Traditional markets being the EU, the US and Canada.
[17]11.3 per cent growth in the EU market, 9.2 in Canada and 1.6 in the US market.
[18]Cumulative growth fell from 21.3 to 10.9 per cent in the first quarter.

consequently, its competitiveness in major markets will be undermined. Rahman and Bari (in press) in a study found that the elimination of LDC-specific tariff preferences may lead to an 8.7 per cent increase in the aggregate tariff rate for Bangladesh's export to the EU.

Analysis of the US market for RMG products reveals that imports from Bangladesh and China decreased by 5.1 and 3.8 per cent during July–October period of FY2017-18, whereas other prime competitors[19] of Bangladesh experienced significant growth.[20] In general, RMG imports by the US has been on the decline in recent years[21]. Between 2015 and 2017 (for July–October period) the share of RMG imports from Bangladesh in the US market declined by 0.2 percentage points. In contrast, Vietnam has gained an additional market share of 2.1 percentage points. Gains in market share appears to have been at the expense of China, which has lost its share by 3.2 percentage points in the US market over the mentioned period (Table 3.17). These are growing signs that it is Vietnam which is taking the advantage of China's displacement.

Table 3.17
Analysis of RMG Imports in the US Market[22]

Country	Period on Period Growth				Compositional Share			
	July–October				July–October			
	2011	2013	2015	2017	2011	2013	2015	2017
Bangladesh	8.7	17.9	11.9	-5.1	4.9	5.5	5.7	5.5
Cambodia	17.4	-48.0	2.7	5.2	3.2	3.0	2.8	2.8
China	2.9	2.9	1.5	-3.8	42.8	42.1	40.5	37.3
India	4.4	16.5	3.1	7.5	3.3	3.4	3.5	3.9
Vietnam	13.7	13.6	11.2	7.8	8.2	9.8	11.9	14.0

Source: Authors' calculations using data from United States International Trade Commission (USITC) and Eurostat.

In both the key markets (of the US and EU) the price effects and volume effects (within the export value growth) experienced pulls in opposite direction. Growth in the value of exports in these markets are mostly volume-driven. Previous analyses (CPD, 2017b) showed that prices of RMG products from Bangladesh in both the EU and the US markets have been falling since 2014. Further analysis[23] in terms of monthly changes showed that in the year 2017 average prices of knit and woven experienced a decline. Whilst the trend for Bangladesh's major competitors such as China, India and Cambodia was the same, their respective average prices were at higher levels. Vietnam, on the other hand, experienced an increase in price of woven products in the US market.

Further in-depth analysis on a more disaggregated level showed that Bangladesh's top three RMG export items in the US and the EU markets experienced a fall in price for both knit and woven categories respectively, for 2017. The extent and rate of fall of average prices in the EU was lower than that in the US, and the same was true for exports of knit products relative to exports of woven products. Comparing the average price[24] received by the top three knit and woven products (for Bangladesh) in the US and EU market, it is observed

[19]Other trade competitors considered are Cambodia, India and Vietnam.

[20]Knit exports to the US increased by 0.1 per cent and woven exports decreased by 7.2 per cent.

[21]During the period 2011–2017 the highest yearly growth in RMG imports of the US was in 2011 (7.3 per cent) and it has been lower and at times negative terrain after that.

[22]The growth rates reported here are yearly growth rates which have been reported in this table bi-annually.

[23]All the analyses mentioned here onwards has been done based on the data obtained from the USITC and Eurostat websites respectively, using the customs value and quantity of exports to the US and EU markets.

[24]Average for products (at HS-8 digit level) and for the period: July–October 2017 in the US market and July–September 2017 in the EU market. The reference period is the current fiscal year, based on the availability of data.

that Bangladesh received lower prices for the majority of her export products[25] (Annex Table 3.4). Since even for items at disaggregated level, Bangladesh's price was somewhat lower than key competitors, it is possible that there is scope for Bangladesh to negotiate better prices though an improvement in the quality and design of the same items.

The Export Policy 2015–2018 of Bangladesh will phase out this year. The developments in the key markets, strategic interventions from competing economies[26] and the shift of trade arrangements post LDC-graduation should inform the formulation of the next Export Policy to enhance Bangladesh's export competitiveness.

Import payments

Import payments recorded a significant growth to the tune of 28.7 per cent during the first four months of FY2017-18 (Table 3.18)[27]. Import payments for rice was significantly high (USD 623 million i.e. 9 times higher than that of the previous year). The import of rice is likely to continue in view of the higher domestic retail prices, lower public stock and reduced tariff. Import payments for consumer goods also registered a high growth of 29.3 per cent, primarily because of the significant growth of import payments for edible oil (39 per cent) and sugar (50.8 per cent). In view of the declining global price of sugar, posting this high growth would entail a large increase in volume. Also, the high import payments for edible oil is also likely to be volume driven, albeit the marginal rise in global prices in recent months. These trends call for appropriate monitoring of the market on the part of the Ministry of Commerce (Moc) with the purpose of checking whether businesses are making overstock of edible oil and sugar or whether there is over-invoicing.

Table 3.18
Import Payments for July–October of FY2017-18

Item	July-October				
	FY17	FY18	% Growth	Share of Import (FY18)	Incremental Growth (FY18)
	(in million USD)				
Rice	6.8	623.4	9,067.6	3.4	14.9
Edible oil	437.4	608.0	39.0	3.3	4.1
Sugar	286.1	431.4	50.8	2.3	3.5
Oil seeds	84.7	223.6	164.0	1.2	3.4
Raw cotton	613.1	1,078.3	75.9	5.8	11.3
Plastic and rubber	655.4	798.4	21.8	4.3	3.5
Capital machinery	1,195.9	1,720.7	43.9	9.3	12.7
Other capital goods	2,255.3	2,637.8	17.0	14.2	9.3
Others	8,859.4	10,405.0	17.4	56.2	37.4
Total	**14,394.1**	**18,526.6**	**28.7**	**100**	**100.0**

Source: Authors' calculations based on Bangladesh Bank data.

More than half of the import payments were on account of intermediate goods. In the period of July–October of FY2017-18, the growth of import payments for intermediate goods was about 19 per cent, significantly higher than the corresponding period of FY2016-17 (when growth was 2.6 per cent). Despite global price

[25] It should not be wrongly deduced that this is competitive price since at the most disaggregated level in the market (at the selling point) similar products (in terms of quality) of different countries would attract approximately the same price to maintain competitiveness.

[26] For example, India has recently reviewed her Foreign Trade Policy and announced new incentives for RMG and textile (Rs 1140), leather and footwear (Rs 749 crore) among others under the Merchandise Exports from India Scheme (MEIS). Several specific procedural relaxation and trade facilitation measures have been taken to assist exporters.

[27] However, letter of credit (L/C) settlement growth (of about 8.3 per cent for the period of July–November 2017) does not commensurate with the actual import payments growth.

stability of raw cotton and an upturn in the growth of RMG exports, the high growth of over 75 per cent in import payments for this item appears to be suspicious (the growth peaking since November 2016). There has not been any fall in yarn and fabrics import, neither has there been a sudden spurt in investment in spinning. With fall in prices of raw cotton, the high imports would allude to very high import in terms of volume, which reinforces the need for investigation into the matter.

Growth in import payments of other intermediate goods such as textiles (14 per cent) and yarn (13.4 per cent) and, dyeing and tanning materials (13.2 per cent) were high with potential positive impact on exports over the subsequent two quarters of FY2017-18. Import of chemicals (18 per cent), plastic and rubber (21.3 per cent), iron and steel (16.2 per cent), and clinker (12.6 per cent) showed high growth. This rise is driven by the higher demand in the backdrop of global economic upturn, decision by the Organisation of the Petroleum Exporting Countries (OPEC) and Russia to curtail oil production, Iran controversy and a fall in global inventory.

In general, the import figures, for certain items, do not tally well with global price movements, L/C settlement figures, domestic production and credit uptake and investment trends. As was mentioned earlier, import payment figures ought to be subjected to closer scrutiny by the NBR and the Bangladesh Bank to identify cases of over-invoicing and capital flight. Bangladeshi policymakers should also keep in mind that, the country may face an additional burden of import payments in the second half of the current fiscal year, as the prices of key imported commodities such as crude oil evinced signs of rise.

Import payments growth for capital machinery also increased by a high 43.9 per cent during July–October of FY2017-18 compared to the corresponding period of the last fiscal year. Imports on account of public sector led infrastructure projects were perhaps part of the story. Import payments for other capital goods registered significant growth of 17 per cent. Import payments growth of 'others import items (not specific elsewhere)' was 45 per cent for the July–October period of FY2017-18 when compared to the corresponding period of the previous fiscal year.

Terms of trade

Terms of trade for Bangladesh has worsened when prices of major importables such as crude oil, rice, cotton and fertiliser are juxtaposed with the prices of Bangladesh's major export item, the RMG. For example, in October 2016 import payments for 1 barrel of crude oil was costing the equivalent of earnings from exports of 3.7 kg of knitwear products in the US; to contrast, the corresponding figure for October 2017 was 4.3 kg, an increase of 17.3 per cent (Table 3.19). This may be interpreted as a loss of purchasing power of 1 USD

Table 3.19
Terms of Trade against RMG Exports in the US and EU Markets*

Selected Major Import product	US market						EU market					
	KG of knit (61)			KG of woven (62)			KG of knit (61)			KG of woven (62)		
	Oct-17	Oct-16	Increase (in %)	Oct-17	Oct-16	Increase (in %)	Sep-17	Sep-16	Increase (in %)	Sep-17	Sep-16	Increase (in %)
1 barrel of crude oil	4.3	3.7	17.3	3.4	2.4	42.0	3.8	3.6	5.0	3.2	2.9	7.4
1 MT of rice	30.7	27.3	12.5	24.7	18.2	36.1	28.7	30.7	-6.5	24.0	25.1	-4.3
1 kg of cotton	0.1	0.1	5.3	0.1	0.1	27.5	0.1	0.1	-7.5	0.1	0.1	-5.4
Fertilizer (index)	6.1	5.3	14.9	4.9	3.5	39.0	5.3	5.7	-6.9	4.4	4.6	-4.8

Source: Authors' calculations using data from United States Integrational Trade Commission (USITC), Eurostat and World Bank Pink Sheet.

Note: * Base refers to October 2016.

earned from export. Indeed, this holds true for many of the major imported products of Bangladesh such as rice, cotton, fertilisers, etc.

The EU market portrays a similar picture in case of oil; although the picture is welcomely different for some of the other imported items. Table 3.20 reveals the purchasing power of RMG exports in terms of some key import items.

Remittance and migration

Month-on-month remittance flow returned to the positive terrain in the first half of FY2017-18 in the backdrop of a significant decline [by (-) 17.5 per cent] for the corresponding period of FY2016-17. Indeed, during July–December period of FY2017-18, remittance was 12.5 per cent higher than that of the corresponding period of FY2016-17 but still remained (-) 7.4 per cent lower when compared to the same period of FY2014-15. Cross-country comparison of remittance growth for the July–November[28] period for the past six fiscal years (FY2013 to FY2018) indicates an upturn, albeit at slow pace[29] originating from Middle–East countries (Table 3.20). Rise in crude oil price and change in policies in some key host countries such as KSA (a rise in minimum wage, change in *akama* system) could be possible reasons. Besides, depreciation of BDT against USD (as well as other currencies) may have contributed to this. However, even if the current pace of remittance growth continues in the second half of FY2017-18, the amount in the end of FY2017-18 will be around USD 14 billion which would still be lower than the remittance flow in FY2012-13.

Table 3.20

Country-wise Growth (Cumulative Months) in Remittance Earnings

Fiscal Year	July to November			July-October*	
	Bangladesh	Pakistan	Sri Lanka	Nepal	Philippines
FY13	24.3	14.2	16.8	3.5	6.9
FY14	-9.0	7.1	11.1	25.4	7.4
FY15	11.7	17.5	6.6	2.4	8.5
FY16	-0.6	7.2	-0.7	11.7	0.6
FY17	-15.7	-2.4	0.5	4.3	3.3
FY18	10.8	2.4	-7.4	2.6	3.5

Source: Authors' calculations from respective central bank statistics.

Note: * The calculations are done based on latest data available.

More than half of the migrant workers are destined for Saudi Arabia

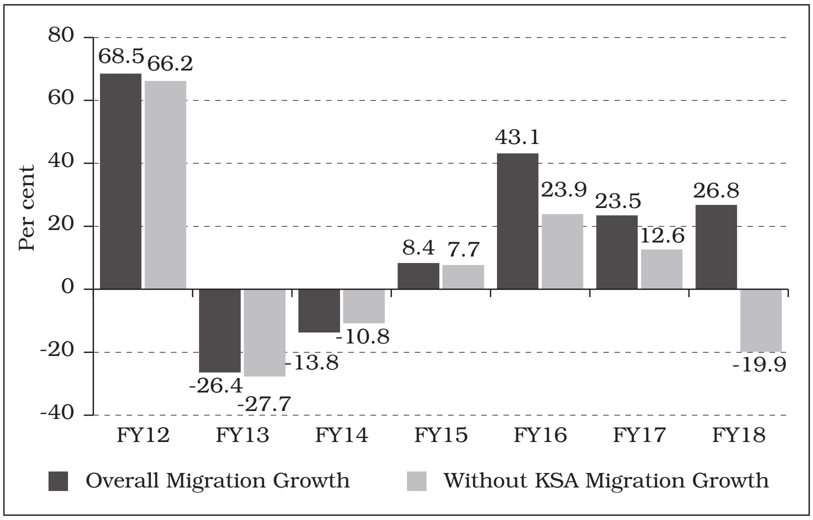
In keeping with the trends over the last two fiscal years, during the first half (July–December) of FY2017-18, migration growth has recorded a high of 26.8 per cent. But if one excludes the number of migrants going to Saudi Arabia [more than half of the migrants (51.0 per cent)] during the corresponding period, the overall migration growth showed a negative growth rate of (-) 20 per cent (Figure 3.18). In the aforementioned period, 69 per cent of the total female migrants (57,156) went to Saudi Arabia. Ensuring the safety and security of all migrants, especially of the female migrants should remain a concern for Bangladesh[30].

[28]Latest available figures for Nepal and Philippines were for July–October 2017 period.

[29]The pace of remittance growth has been particularly telling in case of Bangladesh when compared to other South Asian countries such as Pakistan and Nepal. Sri Lanka has, indeed, registered a negative growth during July–November period of FY2017-18.

[30]Majority of the countries in the Middle East did not ratify international labour rules and regulations.

Figure 3.18
Bangladesh's Migration Growth Trends with and without KSA (July–December, FY18)



Source: Authors' calculations from Bureau of Manpower, Employment and Training (BMET) data.

Remittance earnings are originating from traditional markets, concentration of migrants has increased in the Middle East

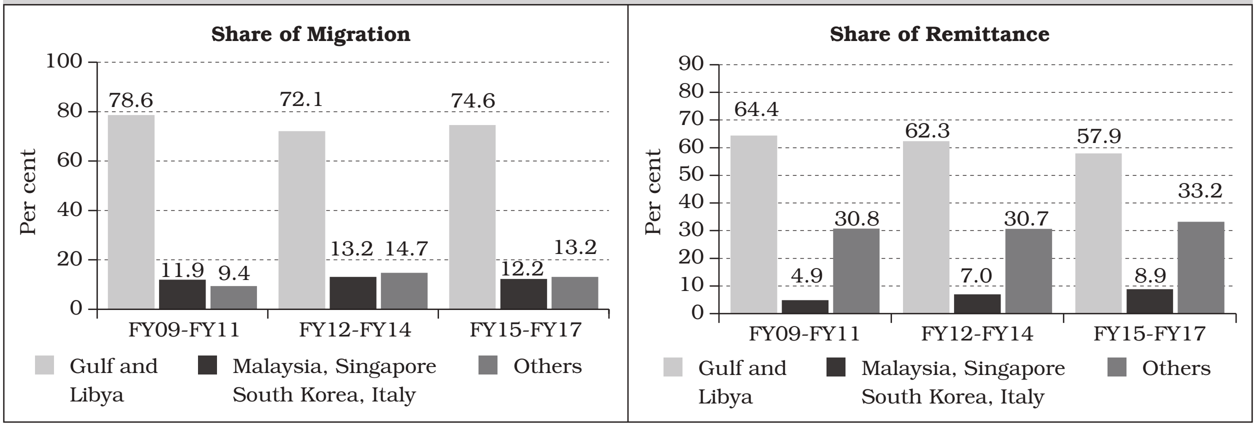
While an increase in remittance inflows from Saudi Arabia is expected to rise in the future, in the first six months of FY2017-18 the corresponding growth was only about 5 per cent. Trend analysis shows that the composition of remittance inflow has remained more or less unchanged (about 56.4 per cent of remittance earnings came from the Gulf countries in the first half of FY2017-18[31]). The concentration of migrants in the Middle East has also posted a rise. Among the non-Gulf countries, major remittance inflows are still originating from the traditional sources such as the US (13.9 per cent), Malaysia (7.3 per cent), the UK (7.2 per cent) and Italy (4.9 per cent). A review of past records evince the following: (a) migration to some of the destination countries such as Malaysia and Italy has declined while it has stagnated in South Korea and Singapore; (b) remittance from the Middle East was on a relative consistent decline—one of the reasons is felt to be greater movement through informal channels; (c) the share of remittance from non-traditional markets increased to 33.2 per cent over the last three fiscal years (FY2015 to FY2017) compared to the earlier six fiscal years (FY2009 to FY2014). These are more of diaspora remittances rather than workers' remittances (Figure 3.19). The share of remittance channeled through state-owned commercial banks (SCBs) and Islami Bank Bangladesh Ltd. (IBBL) have declined at a time when NRB commercial banks are not performing well.[32]

Generation of adequate data and information, skills upgradation, destination diversification, skills upgradation, destination diversification, formalisation of inflows and safety assurance continue to be major concerns for Bangladesh. In addition, the initiative of generating a database on returnee migrants has also made no significant progress. In order to make appropriate and strategic policy interventions, accurate data generation and proper data analysis will be critical for Bangladesh to sustain its migration growth in the international labour market and thereby, attain commensurate remittance earnings.

[31]Of which, 17.3 per cent is from Saudi Arabia and 16.4 per cent from the United Arab Emirates (UAE).

[32]During January–September of 2017, IBBL collected 19.7 per cent of remittances, which was 24.1 per cent during January–September of 2016. At the same time, the share of remittances collected by SCBs fell by 4.3 per cent (from 30.6 per cent to 26.3 per cent). The combined remittance collection by the three non-residential Bangladeshi banks (NRBs) is less than 0.1 per cent of the overall remittance inflows to Bangladesh.

Figure 3.19
Period-wise Share of Migration Outflows from and Remittance Inflows to Bangladesh



Source: Authors' calculations from Bureau of Manpower, Employment and Training (BMET) and Bangladesh Bank data.

CPD's earlier claim of digital hundi – proves to be a real factor behind remittance diversion

CPD (2017a) in its first reading on January 2017, highlighted that remittances were diverted from formal to informal channel through the misuse of digital (mobile) technology. Later, similar results were found by an investigation team of Bangladesh Bank; however the final investigation report was not disclosed publicly. It is highly recommended to assess the efficacy of the measures taken. Since then, Bangladesh Bank increased their vigilance on mobile banking transfer. In September 2017, Bangladesh Financial Intelligence Unit (BFIU), the anti-money laundering wing of Bangladesh Bank, ordered bKash to suspend activities of 2,887 agents for breaching the laws and sent the account details of the agents to law enforcers for further probe and legal actions. Later, in the first week of January 2018, eight bKash agents were arrested for money laundering[33]. bKash has come up with public pronouncement denying any association with fake agents using its logo. These interventions may have helped to improve Bangladesh's remittance earnings and also to bring more transparency to mobile banking transfers.

Foreign loans availed by private sector

An analysis of the trends in foreign loans availed by the local private companies between 2011 and 2017 reveals that the total number of foreign loans has increased dramatically over the years—from a total 24 loans in 2011 to 134 loans in 2017 (Table 3.21). Similarly, the corresponding monetary value of the foreign loans also increased from a total of USD 909.3 million to USD 1,494.3 million, exhibiting a growth of almost 63 per cent over the aforementioned period. Reliance of the local companies to avail loans from the Off-shore Banking Units (OBUs) of the local banks also evinced a persistent rise between 2011 and 2016, but decreased to some extent in 2017. The share of number of loans extended by the OBUs, in the total number of foreign loans, has gradually increased, from 29.2 per cent in 2011 to 61.5 per cent in 2016. However, the amount has experienced a slight fall in the year 2017.

In view of the above, as further analyses reveal, it was the RMG sector which dominated the scenario. In terms of the sectoral breakdown, the RMG sector accounted for 60.2 percent of the total number of foreign loans, followed by the power sector with a share of 11.4 per cent. Furthermore, hard loans have been identified based on the methodology suggested by Organisation for Economic Co-operation and Development (OECD, 2013). It was observed that, the number of hard loans from the foreign sources has jumped significantly since 2016. The average maturity period has exhibited a fluctuating trend and increased from 5.2 years

[33]Available from: http://www.thedailystar.net/backpage/breaching-laws-bb-asks-bkash-suspend-2887-agents-1462567 and http://www.observerbd.com/details.php?id=115040

Table 3.21
Analysis of Foreign Loans Availed by the Local Companies (2011 to 2017)

Year	Total No. of Loans	Share of No. of Loans from OBUs	No. of Hard Loans	No. of Soft Loans	Average Maturity Period (Years)	Average Interest rate (%)	Total Amount of Foreign Loans (Million USD)
2011	24	29.2	7	14	5.2	4.6	909.3
2012	62	32.3	5	50	5.1	4.2	1466.2
2013	103	49.5	1	100	5.2	4.2	1182.3
2014	129	52.7	6	99	4.5	4.7	1771.1
2015	129	52.7	3	98	5.0	3.1	1930.2
2016	148	61.5	11	108	5.0	3.3	1386.5
2017	134	59.0	40	67	5.5	3.6	1494.3

Source: Authors' calculations from Bangladesh Investment Development Authority (BIDA) data.
Note: Some key assumptions were made while carrying out this exercise. These are the followings: discount rate was considered to be 5 per cent; when grace period was not mentioned it was assumed to be 0; when payment per annum was not mentioned it was assumed to be 1; other fees and maintenance cost was excluded due to lack of uniformity and complexity of the involved issues, which was likely to lead to underestimation of the cost of borrowing to some extent; in case of multiple interest rates for different periods of loans, the weighted average interest rate was used; foreign financing directed to the borrower in the form of deferred payment, repaid in installments, was not counted as loans while calculating weighted average interest rate.

to 5.5 years between 2011 and 2017. In contrast, the average interest rate payable on the borrowed funds reveals a generally declining trend—from 4.6 per cent in 2011 to 3.6 per cent in 2017.

Increasing the number of hard loans in recent years, alongside increasing average interest rates, imply higher payment obligations in foreign currency over the coming years. Additionally, depreciation of BDT in the recent past against the USD will put further pressure on debt servicing liabilities. In this changing scenario, the current policy of allowing foreign loans, on a case by case basis, should be re-evaluated. This is also justified on account of a falling interest rate in the domestic market and the need to bring back good investors within the fold of the domestic financial system.

Balance of payments (BoPs)

Current account balance was negative [USD (-) 3,311 million] for the July–October period of FY2017-18. While the balance was negative for the corresponding period of FY2016-17, this was only USD (-) 44 million. This downward pull was mainly driven by the negative trade balance of USD (-) 5,791 million which was USD (-) 2,774 million for the corresponding period of FY2016-17. As was noted above, during this period there was significant growth (28.7 per cent) of import payments. Although growth in export earnings (7.0 per cent) picked up, it was relatively subdued compared to that of import payments. As remittance inflow was USD 262 million higher in this period, this compensated for only a part of the growing trade deficit. The latest figures (July–December of 2017) released by the Export Promotion Bureau (EPB) showed that export growth marginally increased to 7.2 per cent while the growth of L/C opening for import payments (for July–November of 2017) was nearly 30 per cent (if one excludes USD 11,380 million equivalent of L/C opening for the import requirements of Rooppur Nuclear Power Plant[34]).

The overall balance for the July–October, FY2017-18 was negative as well, at USD (-) 225 million (the corresponding figure was USD 2,037 million in FY2016-17). The overall BoP situation was helped by the 107.2 per cent growth of medium and long-term (MLT) foreign loans received during the corresponding

[34]In November 2017, at one go, USD 11.4 billion equivalent of L/C was opened for the import requirements of Rooppur Nuclear Power Plant project. Although the real import will take place (as planned) from now to 2024, policymakers should be aware of the fact, any large 'one-shot' import settlement may create additional pressure on BoP position.

period. The analysis above pointed out that private sector external debt had been on the rise since 2011. In addition, a significant growth in the foreign aid disbursement also contributed to the increase in MLT.[35] Besides, there was also 9.4 per cent period-on-period growth in FDI flow during July–October of 2017.

The indications are that, trade deficit will continue to rise in the second half of the current fiscal year despite signs of improved export and remittance performance. Flow of MLT and FDI will likely gain some momentum. However, the pressure on overall balance and foreign exchange reserves will likely rise, requiring a cautious approach on the part of the central bank in pursuing its monetary policy for the second half of FY2017-18, particularly in terms of its management of exchange rate, forex reserves and foreign loan. The forex reserve is likely to fall further as the growth of incoming sources of foreign funds may not be substantially picked up to balance the high growth of import payments.

Exchange rate

Following protracted stability, spanning over three years (notwithstanding some short-term volatility), BDT started to experience some depreciation since the second quarter of FY2016-17. This continued in the early months of FY2017-18. The monthly average nominal exchange rate (NER) in the first half of FY2017-18 was USD/BDT 82.57 (December 2017)[36]. Real effective exchange rate (REER), has declined in the first five months of FY2017-18[37] from 153.4 in July to 150.7 in November 2017.

An analysis of the cross-currency rate with Bangladesh's major trade competitors[38] reveals that BDT is regaining its pre-appreciation level. For instance, Indian Rupee (INR)-BDT exchange rates, now 1.25 (INR to BDT), has reached the rate posted in 2015.

Table 3.22

Cross-currency Comparison with Trade Competitors[39]

Competing Country	Currency Rate	Current NER*	Same Level Previously**	Current REER	Same Level Previously**
Cambodia	KHD/BDT	0.02002	July 2012	0.8911	March 2015
China	CHN/BDT	12.52	March 2013	0.8828	May 2016
India	INR/BDT	1.25	January 2015	0.8000	April 2015
Vietnam	Dong/BDT	0.003640	August 2014	0.9329	March 2016

Source: Authors' calculations using data from Bangladesh Bank, National Bank of Cambodia, Vietnam Customs and Bruegel Centre.
Note: *As of December 2017 for China and Vietnam, as of November 2017 for India and as of October 2017 for Cambodia.
**The time has been noted for which the exchange rate was approximately similar to the current rate.

Thanks to the recent depreciation of BDT, its erosion in terms of REER against currencies of some of Bangladesh's competitors appears to have been checked, and reached the REER levels of a few years back (Table 3.22). A recent study by the Bangladesh Bank (Hassan *et al.*, 2016) found the existence of a direct relationship between REER and Bangladesh's export earnings both in the short-run and long-run. The

[35]During July–September 2017, foreign aid disbursement was USD 857.1 million which was USD 578.3 million in the corresponding period of the last fiscal—a significant growth of 64.5 per cent was recorded. After principle repayment of USD 278.8 million, the net receipt of foreign aid stood at USD 578.3 million during July–September 2017 as compared to USD 220.2 million of the same period of the previous year, a rise to the tune of 162.7 per cent.

[36]Last time Bangladesh had the nominal exchange rate within the range of USD/BDT 81.5 to 83 was in 2012 (March–September 2012)

[37]REER used for this analysis is estimated from a 138 currency basket (Bruegel Center Working paper, 2016), whereas Bangladesh Bank's REER estimates stem from a 10 country currency basket which accounts for over 80 per cent of Bangladesh's total trade (these set of countries constitute 80 per cent and 99 per cent of Bangladesh's total trade, respectively). The estimates by the Bruegel Center has been used on the basis of availability.

[38]Cambodia, China, India and Vietnam

[39]The analysis has been done for the period FY2013–FY2018 (first half, up to December 2017)

study supports the established theory of adverse effect of REER appreciation on export earnings. The same study shows that upon the induction of a shock, it takes approximately forty days for the REER-export earnings nexus to reach a steady state level. Keeping this in mind, one can expect the exports to benefit from REER movement in the coming months[40].

Foreign exchange reserve has dwindled to USD 32.0 billion as of 3 January 2018, from USD 33.5 billion as of 30 June 2017. This depletion of forex reserve can be explained by the high growth of import payments, relatively lower export growth and sluggish recovery of growth in remittance. Moreover, Bangladesh Bank has seemingly refrained from intervening in the form of large scale foreign exchange purchases of USD in the past few months.

Policy stance

Overall, trends of such key monetary sector variables such as inflation, interest rate, export and imports, trade, current and overall balance, debt servicing and foreign exchange reserves, suggest that Bangladesh should pursue a cautious monetary stance during the second half of FY2017-18. The widening trade deficit in the backdrop of high imports, and the depressed current account and overall BoPs scenario was likely to put pressure on the foreign exchange reserves. In view of this, renewed efforts to stimulate export earnings and remittance flows, maintain exchange rate stability and steps to rein in imports should inform Bangladesh's external sector management.

3.4 SELECTED ISSUES FOR FY2017-18

3.4.1 Crisis in the Banking Sector

Introduction

Performance of the banking sector of Bangladesh has been quite disappointing in recent times (Table 3.23 and Figures 3.20-3.21). Track record of many of the banks has been unsatisfactory. There is a wealth of empirical research which indicates that the relationship between financial development and economic growth is positive (Ahmed and Ansari, 1998; Jokipii and Monnin, 2013; McKinnon, 2010; Shaw, 1973; Calderón, 2003; Rahman, 2004; Chakraborty, 2008; Khan, 2008 and Senhadji, 2000). However, the banking sector of Bangladesh has been plagued by financial scams, NPLs, inefficiency, and slack monitoring and supervision.

Table 3.23
Overall Banking Sector Performance during 2012–2017

(in Per cent)

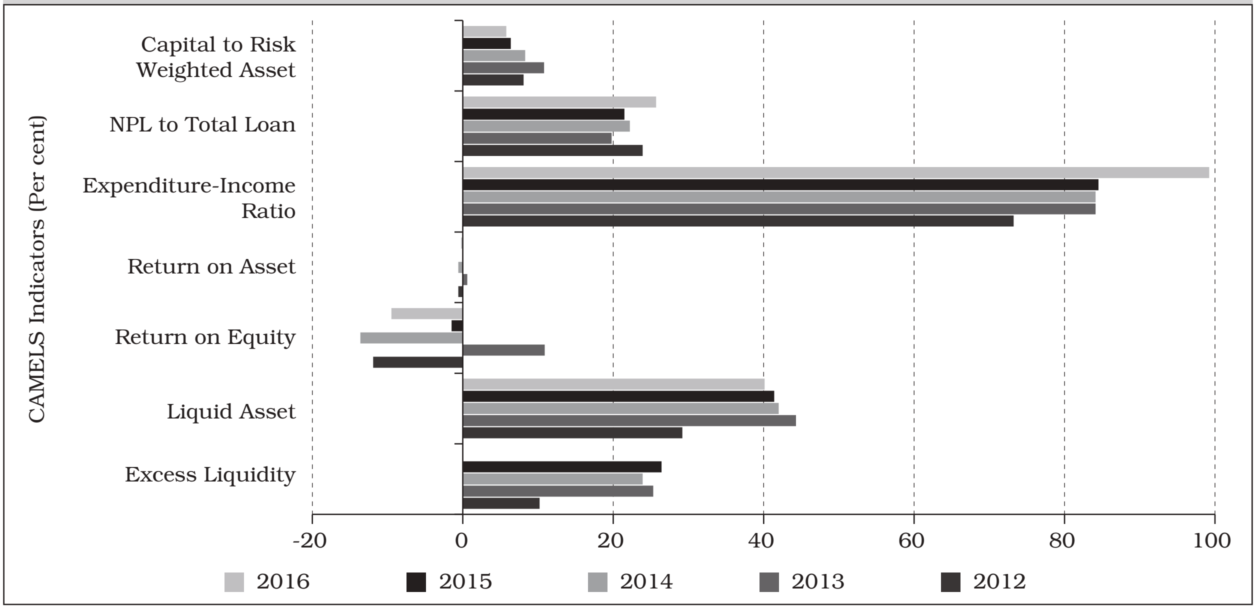
Soundness Indicator	2012	2013	2014	2015	2016[J]	2017[P]
Capital to risk weighted asset	10.5	11.5	11.3	10.8	10.7	10.9
NPL to total loans	10.0	8.9	9.7	8.8	10.1	10.1
Expenditure-income ratio	74.0	77.8	76.1	76.3	79.8	NA
Return on asset	0.6	0.9	0.6	0.8	0.4	0.3
Return on equity	8.2	11.0	8.1	10.5	7.1	4.7
Liquid asset	27.1	32.5	32.7	26.5	25.3	21.6
Excess liquidity	9.9	15.4	15.7	16.9	NA	NA

Source: Bangladesh Bank Annual and Quarterly Reports.

Note: 'J' refers to June; 'P' denotes provisional.

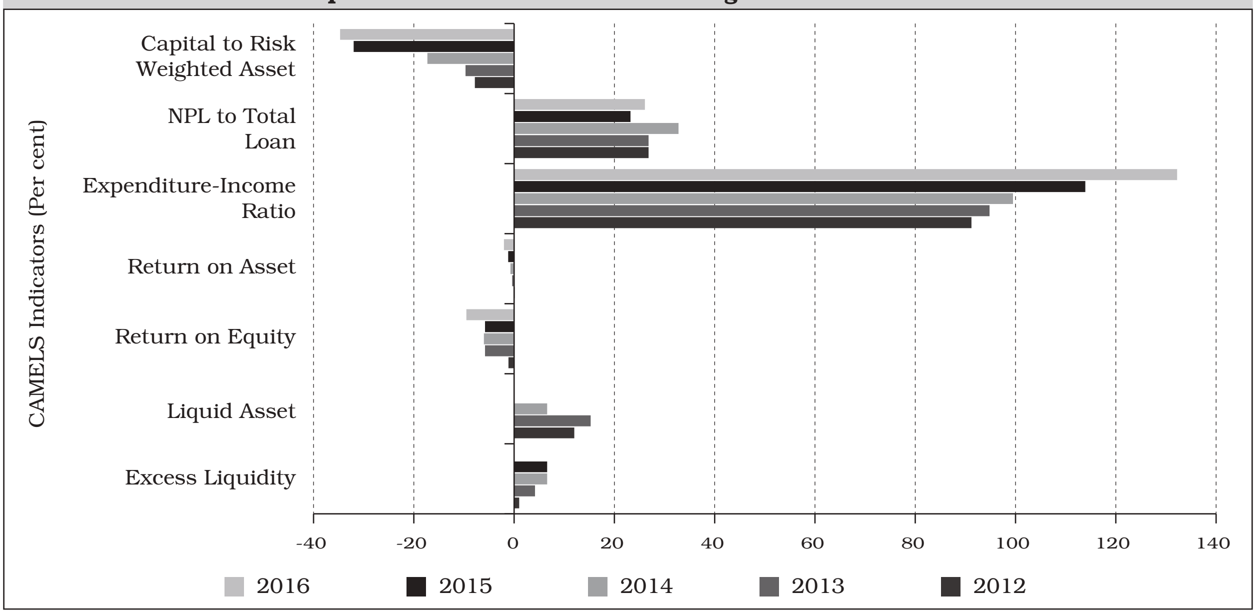
[40]A CPD study employing an augmented gravity model to estimate the impact of Brexit on Bangladesh's exports suggests that the exchange rate elasticity of exports is 0.02 per cent. When this is factored in for the July–December FY2017-18 period, we observe that depreciation of REER by 1 per cent would lead to an increase of about USD 200 million in the export earnings. (Rahman *et al.*, in press)

Figure 3.20
Performance of the State-Owned Commercial Banks 2012–2016



Source: Bangladesh Bank.

Figure 3.21
Performance of the Development Finance Institutions during 2012–2016

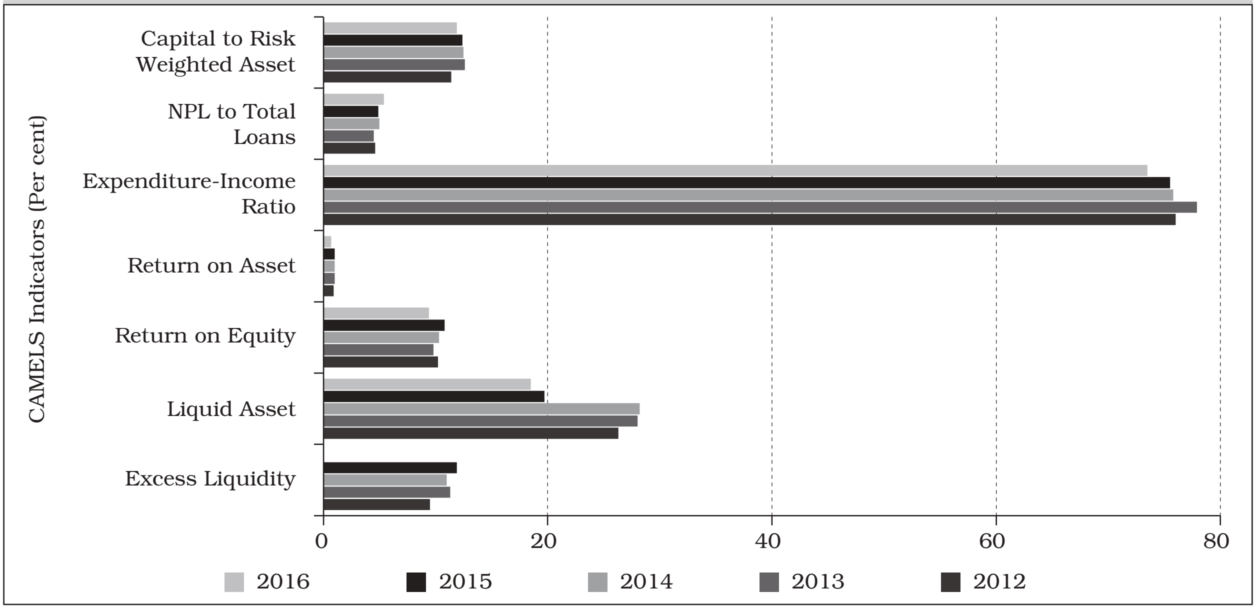


Source: Bangladesh Bank.

This has posed serious threats to the sustainability of the sector. This section of the IRBD report provides a brief overview of the situation of the banking sector, highlights a few issues that are detrimental to the development of the sector and makes recommendations for way forward.

Figure 3.22

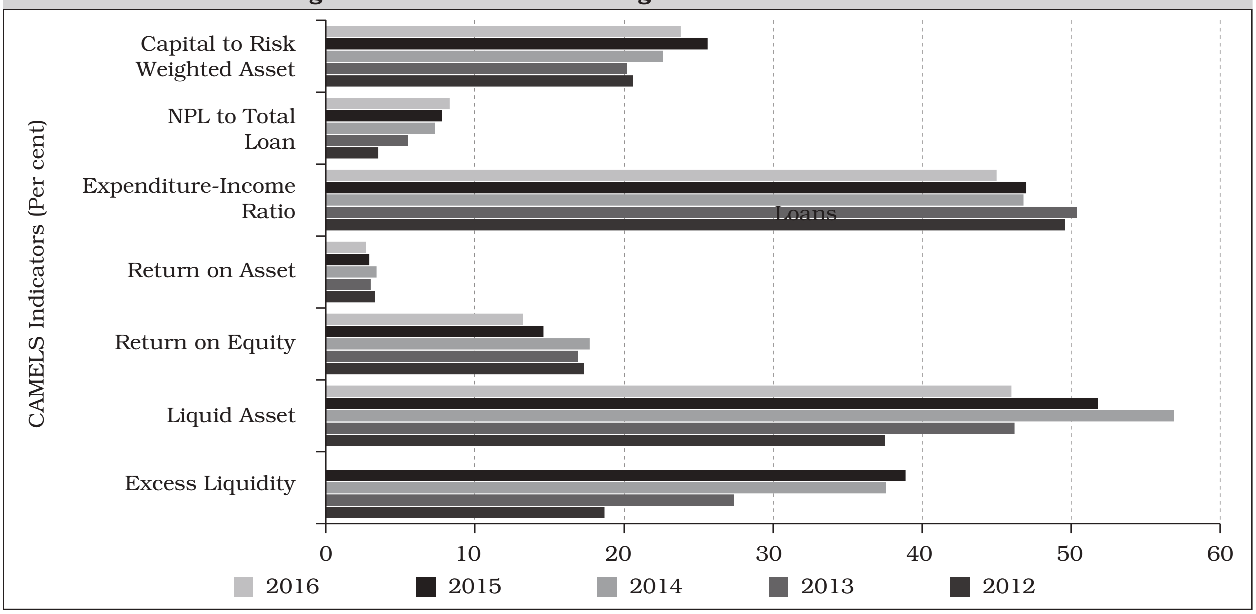
Performance of the Private Commercial Banks during 2012–2016



Source: Bangladesh Bank.

Figure 3.23

Performance of the Foreign Commercial Banks during 2012–2016



Source: Bangladesh Bank.

Overview of performance of the banking sector

SCBs performed miserably (Annex Table 3.5) with a dismal record of large NPLs, bad governance, and embarrassing recapitalisation. The setback from several major financial scams was taking a heavy toll on both the health and reputation of SCBs. The fourth generation banks (9 newly approved commercial banks) are beset with large amounts of NPLs (Annex Table 3.6) and are making losses. Research has shown that 65 per cent of banks faced financial crimes during the years 2014–2016 (Habib 2017), whilst financial statements of borrowers was always available to the banks only 17 per cent of the time (Siddique, 2017). Capital adequacy was still below BASEL III requirements for some banks, and the prospects of full BASEL III implementation by 2019 seem bleak. Two detrimental amendments of dubious nature have been proposed to the Banking Company Act which undermined the cause of good governance. The tenure of board of directors is proposed to increase from 6 years to 9 years, and up to four family members would be allowed to be on the Board, instead of the earlier two per family. These changes are apprehended to reinforce crony capitalism in a sector of the economy already impaired by poor governance. Major changes were made to the management of Islami Bank, which had already been suffering from poor governance, on allegations of terror financing and political violence. A bank once known to be a high performer in the banking sector was now in disarray.

The tale of fourth generation banks

In 2013, the government approved licenses of nine new private commercial banks: Meghna Bank Limited, Midland Bank Limited, Modhumoti Bank Limited, NRB Bank Limited, NRB Commercial Bank Limited, NRB Global Bank Limited, South Bangla Agriculture and Commerce Bank Limited, The Farmers Bank Limited, and Union Bank Limited. All of these banks had two things in common: they were all backed by politically powerful owners and the economic rationale of these banks was very weak. For example, a study showed that 95 per cent of the bankers believed that the new banks were redundant (Nabi, 2016). Despite such findings, nine new private commercial banks were still given the green signal.

The logic of reaching out to the unbanked in remote areas, for bringing in new banks, was a weak one. First, new branches could also be opened by the existing banks. Second, banking and financial services could be provided digitally. Indeed, the Index of Financial Inclusion (IFI) in Bangladesh had increased from 27.5 per cent in 2010 to 65.5 per cent in 2014, mainly due to the opening of a large number of mobile banking accounts (Rabbi, 2016). Despite having a number of feasible options on the table, the new banks were allowed into the market at a time when the banking sector was already reeling from corruption and scandals.

According to conventional economic theory, firms want to enter a market when they see that there are potential gains to be made (Rubinfeld and Pindyck, 2013). An investor who would be willing to spend Tk. 400 crore to start a business would undoubtedly undertake meticulous calculations of cost-benefit ratio, internal rate of return, and net present value. One wonders, how much effort has actually gone into such exercises before launching a new bank and how much time was spent to devise ways and means of misappropriation of depositors' money.

Farmers Bank is now on the verge of collapse after being hit by scams and scandals. Due to acute liquidity crisis, the bank is unable to pay its depositors. This is creating panic amongst the depositors who are desperately trying to take their savings out of the bank. The central bank has allowed Farmers Bank to float subordinated bonds worth Tk. 500 crore, and also given it a short-term loan of Tk. 96 crore. However, the situation in Farmers Bank is getting worse every day (Annex Table 4.3). The crisis in Farmers Bank reminds the depositors about the erstwhile Oriental Bank which collapsed due to massive insider lending and malpractices (Annex Table 3.4).

NPLs cast shadow on banking sector

NPLs are a direct threat to the financial health and development of a country. It may appear that NPLs are rather innocuous, and that they occur merely because borrowers are unable to pay back loans which are associated with high interest. However, studies have shown that in general high interest rates are not causally related to high level of NPLs in Bangladesh (Ahmed, 2006; Mujeri, 2009; Hossain, 2012). Evidently,

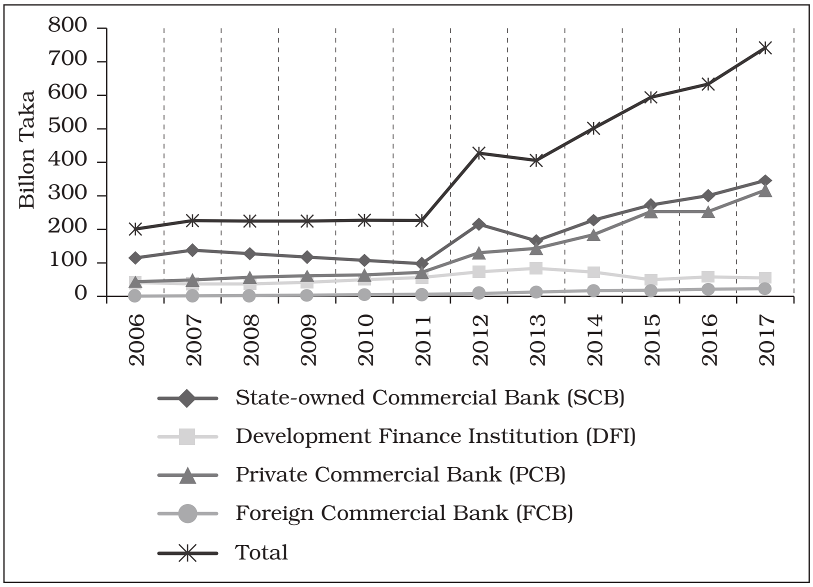


Figure 3.24

Amount of NPLs in Bangladesh by Type of Bank

Source: Bangladesh Bank.

for small and medium enterprises (SMEs) high interest rates could be a reason behind NPLs (Jahan, 2016). However, the amount of loans by SMEs is rather small compared to the total amount of loans by banks in Bangladesh.

The reality is that NPLs originate from uncertainty and corruption, both of which have detrimental effects for the growth of the banking sector of a country (Park, 2012; Moshirian, 2012; Lin, 2012; Serwa, 2010). Research has shown that the reasons behind high amount of NPLs in Bangladesh include political instability, corruption, poor governance, and weak rule of law (Banerjee, 2017; Alam *et al.*, 2015).

The amount of NPLs in Bangladesh has been rising at a fast pace over the past years (see Figure 3.24). Poor management of SCBs, coupled with malpractices and corruption, has contributed to the high levels of NPL. Contrary to all established norms of banking, SCBs have been awarding loans based purely on political grounds (Habib, 2017). Consequently, even routine assessment of the potential risks associated with the borrower is not carried out by these banks. Credit-worthiness is judged mainly by political worthiness. As a result, having good political credentials is perceived to be adequate to obtain large loans. Additionally, the government's tendency to fund loss making state-owned enterprises, through SCBs, has aggravated the problem of NPLs even further. Research has shown that on average only 33 per cent of first time rescheduled loans, and 30 per cent of third time rescheduled loans were recovered during 2011–2014. Over the same time period, loans worth Tk. 45,527.4 crore were written off by the banking sector. Evidence has also emerged that only 14 per cent of bankers consider the borrower selection process to be extremely effective (Habib, 2017).

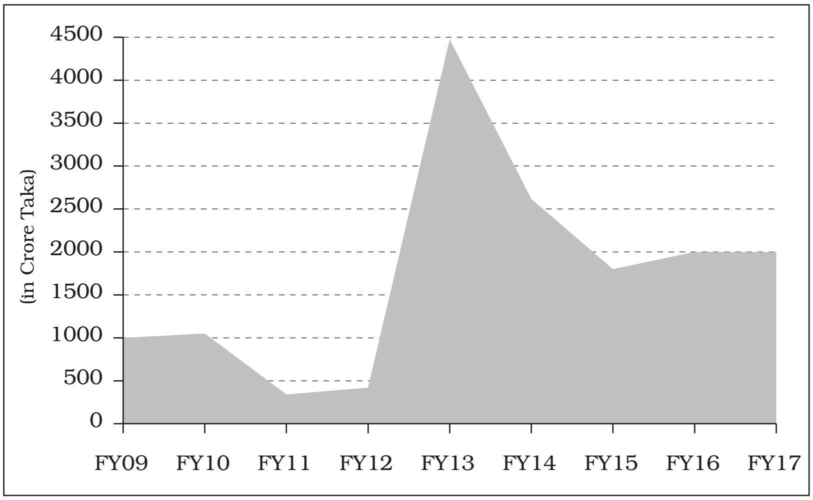
Recapitalisation of SCBs at whose cost?

Recurrent recapitalisation of SCBs by the government has emerged as an issue of grave concern, and the government has taken recourse to this measure on a regular basis. It has been estimated that the GoB has spent Tk.15,705 crore (Monthly Fiscal Frameworks, Budget Briefs, Finance Division) in recapitalising the banks during the period FY2009–FY2017 (Figure 3.25). This amount is roughly half of the cost of the construction of the Padma Bridge. Most of these funds were allocated to the ailing and failing SCBs.

Instead of government-funded recapitalisation, banks suffering from capital inadequacy should be instructed to take recourse to other measures. Such options include, but are not limited to, using revenue to increase capital, searching for investors to buy bank shares, or merging with other commercial banks.

Figure 3.25

Amount of Recapitalisation



Source: Monthly Fiscal Frameworks, Budget Briefs, Finance Division.

Way forward

Embezzlement of public money by a handful of corrupt people and escalation of financial crimes in Bangladesh indicate that the banking sector is in dire straits. Immediate attention and decisive actions are required on the part of the government to rescue the banking sector from this dismal situation. It is just not about formulating new laws, but about punishing those who are responsible for the mismanagement among a section of the banking sector. Ironically, recommendations to overcome the challenges of the sector remain the same as before. Some of those are flagged once again, along with a few immediate ones.

i) Immediate Measures for the Failed Banks: The central bank should act proactively towards resolving problems of the failed banks, such as Farmers Bank. Bangladesh Bank should appoint a strong administrator immediately to oversee the operation of the bank. A proper audit of the bank should be performed to understand the real health of the bank. Most importantly, the depositors should be paid back.

ii) No permission for new banks: The culture of giving licenses to new banks on political grounds should be stopped. Given the size of the economy there is no need for new banks. The government should not give license to open any new banks. Rather, the existing banks should be supervised and monitored closely. They can expand services to the unbanked ones.

iii) Implementing Risk Management Guidelines: All banks, especially the SCBs, need to implement the risk management guidelines of Bangladesh Bank. The central bank has outlined six core risks, and requested banks to adopt appropriate measures to address them (Bangladesh Bank, 2012). These risks include: i) Credit Management Risk, ii) Foreign Exchange Risk Management, iii) Asset-Liability Risk Management, iv) Internal Control and Compliance Risk Management, v) Money Laundering Prevention Risk, vi) Guidelines on Information and Communications Technology. Banks must be instructed to strictly comply with these guidelines at all times.

iv) Improving Internal Control: The internal control department of SCBs is in need of a serious overhaul. Due to lack of sufficient information technology (IT) infrastructure, the majority of the work has to be done manually, with the consequence of delays and inefficiency. During financial scams of the past, it was discovered that the internal control departments either willingly or unwillingly had failed to inform the Board of Directors regarding large losses.

v) Combating Cronyism in Banking: In order to truly bring about a profound change in the banking sector, the most important emergent task is to combat cronyism. The current practice of recruiting Board of Directors on political grounds has to be discontinued. Studies have shown that financial reporting fraud in banks is more likely if the Board of Directors is dominated by insiders (Beasley, 1996; Dechow *et al.*, 1996; Farber, 2005; Song and Windram, 2004; Uzun *et al.*, 2004). Despite being cautioned by the central bank in 2014, two private commercial banks still had four or more members from the same family in their Board of Directors, as of 12 January 2018. Only unbiased, competent, and honest individuals should be appointed as Member of the Board of SCBs. Of course, they should be allowed to work without fear and favour. The central bank has a clearly defined mandate regarding the appointment of directors of banks. These regulations must be followed without exception in order to ensure good governance and operational independence of the bank. Unless political interference can be reduced, there is scant possibility that the banking sector will be able to play its role in the economy.

vi) Capacity Building of SCBs: Lack of capacity building is a perennial problem that besets the SCBs in Bangladesh. Without human resource development through enhanced skills, SCBs will not be able to handle the emerging challenges facing the sector.

vii) Upholding Central Bank's Independence: The role of the central bank in overseeing the anomalies of the banking sector and for taking stern measures against the loan defaulters, perpetrators of financial crimes, and rule breaking banks and individuals has been rather weak. Interference in Bangladesh Bank's activities goes against the spirit of Bangladesh Bank Amendment Bill 2003 which was geared to guarantee the central bank with autonomy. Unfortunately, the central bank has gradually become silent in the face of political interference and pressure.

3.4.2 An Assessment of Flood Damage and Post-flood Management 2017

Rationale

During the post-independence period, Bangladesh has experienced several floods of various magnitude. Despite there being no standard definition of a major flood, considering the scale of loss and damage, floods of 1974, 1987, 1988 and 1998 are generally regarded as major floods that visited Bangladesh. The estimated asset losses of the 1974 flood was equivalent to as high as 7.5 per cent of GDP (Mechler and Islam, 2013). Although the spatial coverage and magnitude of 1988 and 1998 floods were higher than those of 1974, the overall asset losses were estimated to be equivalent to 5.5 and 4.8 per cent of the respective year's GDP (Mechler and Islam, 2013). In 2004, the estimated asset loss due to flood was equivalent to USD 8.8 billion, almost four times than that of the 1998 flood which was about 3.3 per cent of the corresponding year's GDP (Mechler and Islam, 2013; CPD, 2005). In a similar vein, while subsequent major floods were larger in scale, these resulted in lower amount of losses. A key reason of improved flood resilience in Bangladesh was the significant investment in disaster and risk management (Mechler and Islam, 2013). Indeed, with the progression of time, the attained economic progress with attendant higher standard of living, higher educational attainment, and a growing financial strength have helped Bangladesh to improve her overall resilience against all types of natural calamities including flood (Toya and Skidmore, 2007). In addition to these, community awareness and preparedness programmes undertaken by the government and other non-government organisations (NGOs) have also contributed to Bangladesh's strengthened resilience capacity to deal with natural disasters.

However, being one of the most climate vulnerable countries in the world, coping with pre-during-post food management remains a daunting challenge for Bangladesh. As the signs of climate change impact become ever more evident[41] (Woodward *et al.*, 2011; Wirtz, 2013; Santos, 2013, Navrud and Magnussen 2013; Chibber and Laajai, 2013; Surminski and Eldridge, 2015; Zeleňáková *et al.*, 2017; Pant *et al.*, 2017; HCTT, 2017), the task of reducing risks and tackling the impacts are becoming ever more demanding and daunting. These increasingly higher risks were in evidence when Bangladesh experienced the two successive floods in 2017. During the early flash flood in March–April, 2017 people living in six districts of the *haor* and low-lying areas of northeastern region of the country were affected adversely. Later on,

[41]In the 1990s worldwide, the average number of natural catastrophes had increased to 630 per year from the average number of 430 per year in the 1980s. Over the period of 10 years (2002–2011) 800 such events were recorded on average every year. Experts recorded (and analysed) the highest number of events—820 natural hazards/events in one calendar year (Wirtz, 2013).

during the monsoon flood of August 2017, people in 32 districts of Bangladesh came to be affected (DDM, 2017b). When compared with other major floods of the past, five distinctive features are discernible, which emerge from the authors' observations: (a) early flash floods in *haor* and low-lying northeastern districts; (b) relatively lower scale of spatial coverage; (c) a part of urban areas having been affected (after a long time); (d) lower number of people affected and (e) relatively low death toll.

On the other hand, the two successive floods of 2017 led to inundation of significant amounts of agricultural land and crop damage; a large of number of houses and homesteads, and public infrastructures was partially or fully damaged; a significant number of livestock was lost; economic opportunities had to be forgone. As a response, the GoB and the NGOs have taken several measures during and post-flood period to address and mitigate the after effects and address the adverse impacts. As a post-flood management measure, the GoB declared a number of packages of support (both cash and kind) to the flood-affected farmers to raise crops in the subsequent harvesting season. However, despite the various initiatives, questions were raised by flood-affected people, media and social groups about the adequacy and efficacy of both pre- and post-flood management. These covered a broad range of areas: embankment management, corruption and leakage, rice stock mismanagement by the government, inadequacy of relief activities during and after the flood—these have been convoluted with the discussion of climate change. In the backdrop of the above, the CPD study has made an attempt to assess the impact of the 2017 floods from various dimensions, including an assessment of the pre- and post-flood management by the government, to come up with a set of policy recommendations to improve government's future flood management efforts and initiatives.

Damage from early flash flood in Northeastern haor region

It is well known that the *haors* are low-lying river basin areas of Bangladesh. Generally speaking, most parts of the six districts of the northeastern *haor* areas (*Habiganj, Kishoreganj, Moulavibazar, Netrokona, Sunamganj and Sylhet*) remain inundated for about six to seven months, from June to mid-December. Usually, water level in the northeastern *haor* region starts to rise from late April and within a month or two the area is inundated by water. Between December to April, farming households in this region harvest *boro,* which is the main crop for this mono-cropping region.

In late March 2017, the aforementioned six districts in this region came to be affected by an early flash flood. The floods came at least a month earlier than the regular flood season. Excessive rainfall, both in the affected region and also the Indian-upstream (which led to sudden rush of water from the upstream) was identified as the primary cause of the flood. The water level had surpassed the danger level within the next 3–4 days and inundated the majority of the harvested crop lands of the region. In addition, the delayed start of the annual repair work concerning the embankments by relevant authorities and corruption in the process were cited by the local people in exacerbating the adverse effects of the flash flood. In the course of the flash flood about 46.7 lakh people from 10.3 lakh households came to be affected (DDM, 2017a). This was about one-fourth of the total population of the six affected districts; however, the number of recorded fatalities was relatively low (ten people in all) when compared to such floods of the past. On the other hand, since most of the flood affected are farming households, significant loss of crop production was inevitable.

Value of rice production losses and damage

According to the DDM, about 0.4 hectare *boro* harvested area were completely damaged by the flash flood in the *haor* and low-lying northeastern region of Bangladesh. Assuming district-wise average of (previous) two year's yield rate of rice production remaining the same also in 2017, authors' have estimated that the loss of *boro* rice production was to the tune of 15.8 lakh MT[42]. The estimated *boro* rice production was equivalent to 8.3 per cent of national average of *boro* production in FY2015–16. At the regional level

[42]BBS has reported that damaged *boro* rice production in the flash flood was about 9.8 lakh MT. However, authors' stand with their estimated results as government relief activities and rehabilitation programmes were implemented based on the preliminary statistics published by DDM.

(affected *haor* areas), it was about 52.2 per cent of the total *boro* rice production of the years in FY2015–16. Among these districts, Sunamganj experienced the highest production loss—about 86.2 per cent of its rice production was damaged. The value of estimated rice production loss was about Tk. 5300 crore[43] (or USD 663 million)[44]. This was equivalent to 3.7 per cent of agriculture crop sector GDP in FY2016–17. According to DDM[45], in addition to extensive losses of the boro crop, another 460 hectares of vegetable cultivation areas were damaged by the flash flood (DDM, 2017a).

Monsoon flood damage in 32 districts

Excessive rainfall which had resulted in a significant rise in the water level above the danger level in various rivers of the northern part of Bangladesh, led to extensive monsoon flood in 2017. Continued rainfall since late June and excessive flow of water from upstream in the mid-August aggravated the situation. The flood was a prolonged one, lasting for nearly 20 days. Excessive water flow above the danger level in some cases had severely damaged the town protection embankments and flooded some urban areas, unseen in several decades (e.g. Dinajpur, Naogaon, etc.). As a matter of fact, the water level of the *Jamuna* reached a record of 20.78 meters, even surpassing the level of 20.62 metres recorded at the time of the 1988 flood[46]. In the monsoon flood of August 2017, about 82 lakh people were affected (DDM, 2017b). This was about 8 per cent of the total population living at the 32 affected districts. About 147 people lost their lives due to the monsoon flood in 2017 (DDM, 2017b). However, the number of fatalities were lower than comparable figures for the earlier years.

Estimated damage of monsoon flood

Similar to the earlier flash flood, a considerably large tract of agricultural crop land was inundated during the monsoon flood. According to the authors' calculations, about 9 per cent of *aman* crop land was inundated by the flood. Because the monsoon flood came in the period between early and mid-August, farmers were able to go for replantation of the *aman* crop which they did till late September. If this was not the case, the forgone value of *aman* rice production could have been about Tk. 2,700 crore (or about USD 338 million). Assuming that replantation of the *aman* crop ranged between 40 per cent and 80 per cent, according to the authors' calculations, the forgone production value could come down to between Tk. 1,800 crore (or USD 225 million) and Tk. 700 crore (or USD 87.5 million), respectively. Besides the loss of *aman* crop, flood-affected households lost a fairly large amount of homestead vegetable production which could not be quantified in this study.

During the monsoon flood in 2017, about 0.10 million and 0.63 million homesteads respectively were completely or partially damaged (DDM, 2017b). According to authors' calculations, repairing and rebuilding of these damaged dwelling houses to pre-flood state will cost the flood-affected households about Tk. 2,600 crore (or USD 371.4 million). In addition to loss of private properties, a large number of public properties were also damaged. About 890 km of public roads were completely damaged, while another 10,469 km roads were partially damaged; 949 bridges and culverts were either destroyed or damaged (DDM, 2017b). About 132 km long embankments were completely destroyed while about 664 km were partially damaged (DDM, 2017b). According to authors' calculations, to get back to pre-flood condition about Tk. 4,500 crore (or USD 526.5 million) will be required for purposes of repairing and rebuilding damaged roads, culverts and embankments. The total value of losses incurred on account of *aman* rice production and damage

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[43]National average of one kilogram coarse rice was BDT 35.4 in April 2017. It may be argued that putting the market price of rice may overestimate the value of production loss while in the field, paddy has been damaged instead of rice due to flood. However, authors' have used the market price of rice instead of the paddy to address the opportunity cost incurred by the flood-affected people due to early flash flood.

[44]1 USD equivalent to BDT 80.

[45]Preliminary report released by DDM on 12 May 2017 (DDM, 2017a).

[46]This piece of Information was taken from Statistical Year Book Bangladesh 1993 and Flood Forecasting and Warning Centre (FFWC) 2017.

to physical assets such as houses, roads, culverts and embankments were between Tk. 7,800 (USD 975 million) to Tk. 8,900 crore (USD 1,112.0 million). This estimated value was equivalent to about 0.35–0.44 per cent of the Bangladesh's projected GDP for FY2017–18. However, this figure is an underestimation since authors were not able to put a figure on most social costs as also some of the other costs (e.g. value of damaged schools and other institutional buildings).

Review of government interventions during and post-flood period and observations from field visits

In the course of both the floods, the government provided support in the form of rice, cash and corrugated iron sheets as relief among the flood-affected households through gratuity relief (GR) programmes. Apart from this, in *haor* areas the government has provided rice (30 kg per month) support to 3.8 lakh flood affected families in *haor* areas for nine months, in three phases, through vulnerable group feeding (VGF) programme[47]. However, during the focus group discussions (FGDs), the responses from the poorer section of flood-affected people had been mixed as regards proper identification of recipients and distribution of relief. Some claimed that they have received lower amounts of rice support than what they were supposed to receive, while some others mentioned that they received support for only one phase. As a post-flood measure, the government has announced four support programmes for the 2017 flood-affected farmers of which, one was dedicated to the affected farming households in the *haor* areas.

Review and analysis of the government's flood relief, rehabilitation, and agricultural support measures allows the authors to come up with a number of observations as regards efficacy of the steps taken during and post-flood period: (a) government's flood relief activities and assistances had been timely but inadequate; (b) under-utilisation of relief allocations made for both cash and rice; (c) government relief did not reach remote areas and small clusters in the affected areas; (d) agricultural support measures for farmers were not adequate; allocated budget was not properly utilised; (e) some agricultural support measures went to non-targeted areas as well; (f) some flood-affected areas have remained outside the purview of the agricultural support programmes even though the concerned areas had significant land covered under the respective crop support programme; (g) there were inefficiencies in the planning of the government's agricultural support programmes and distribution of assistance; (h) the logic of proportional distribution of crop inputs was flawed; (i) no or insignificant assistance for non-crop agricultural sectors.

In addition to the above, during FGDs and key informant interviews (KIIs) several other policy concerns were identified which could not be assessed quantitatively. However, these were of no less importance. Some of the concerns articulated are as follows: (i) maintenance of the existing infrastructure is not a priority for concerned authorities; (ii) infrastructure restoration programmes do not receive adequate priority and attention; (iii) lack of coordination among responsible authorities; (iv) local people are not well-embedded in the decision making process; (v) no coordinated approach was followed to generate data on disaster-related damage; (vi) the focus of flood relief and post-flood support by the NGOs is primarily centered towards their respective clients.

Recommendations

Short-term

- Adequacy and coverage of the government's relief and rehabilitation activities can be improved through better utilisation of allocated budget for relevant programmes.
- Adoption of digital tools may help the government to improve the efficiency and efficacy of flood relief activities by reducing misidentification, overlaps and by helping to put in place an improved monitoring system.

[47]This programme is still continuing and the government has planned to carry forward this programme till April 2018.

- The government should make use of the NGO networks to reach the remotest and farthest flood-affected areas.
- A GO-NGO partnership geared towards flood management will raise the efficiency of the post-flood management programmes (e.g. to address multiple dimensions of health and other social hazards due to flood).
- Effective participation of local people in the decision making process should be ensured in project implementation committees.
- Adequacy and coverage of agricultural rehabilitation programmes can be extended through better use of agriculture subsidy budget.
- A special financing scheme should be considered for rural (affected) people to get access to low cost formal credit.
- Non-crop sector rehabilitation programmes should be introduced and implemented in a coordinated manner rather than following fragmented procedures (e.g. affected fishermen were in urgent need of fingerlings to start fish culture anew).
- Although more accurate disaster data were available with various government departments, there is no system to integrate these fragmented data into one integrated data portal. This integrated data portal should not be a separate government initiative, rather DDM should get the mandate to integrate all disaster related data from relevant government departments and offices.
- District officers of various government departments (e.g. Department of Agricultural Extension (DAE), Department of Livestock Services (DLS), Local Government Engineering Division (LGED), Bangladesh Water Development Board (BWDB), etc.) should be asked to prepare independent reports which should include: the damage incurred in their respective districts due to flood, information about measures they have taken, a list of the challenges they faced in their activities on the ground and come up with concrete policy suggestions to improve the situation.

Medium-term

- Government must come up with an effective framework to improve the maintenance of existing embankments and flood protection infrastructure. Rebuilding and repairing of embankments and dams need to be carried out in a timely and coordinated manner.
- Projects need to be undertaken as part of an integrated flood management framework on a priority basis to repair damaged road networks.
- Structural flaws of road, bridge and culvert networks in many rural areas adjacent to farm lands, which cause water logging, need to be remedied.
- A joint work plan needs to be chalked out by the Ministry of Water Resources, Roads and Highways Division, LGED, Ministry of Agriculture, Ministry of Food, and Ministry of Finance with support from other local institutions.
- There is a need to undertake a project to establish protection walls at *haor* areas after proper technical and feasibility assessment.
- Periodic dredging of various cannels and rivers linked to *haor*s is a must to protect the ecosystem of the *haor* wetlands.
- Good governance in the flood (disaster) management and strengthening institutional capacity in implementing the projects ought to be seen as priorities by policymakers.

3.4.3 Implications of *Rohingya* Crisis for Bangladesh

Background

The *Rohingya* problem has emerged as a new challenge for Bangladesh. The brutal killings and torture, the violence against women, the deaths and sufferings of children and the consequent large-scale displacement of the *Rohingya* people were termed as 'ethnic cleansing' by the United Nations High Commission for Refugees (UNHCR). It may be recalled that the *Rohingya*s had been stripped off their citizenship way back in 1982 as per the Citizenships Law of Myanmar which severely restricted their day to day life. Over the last several decades, *Rohingya* people have been forced to leave their country on several occasions, and by various means. While some have taken refuge in a few neighbouring countries including India, the majority have fled to Bangladesh. This forced displacement of the *Rohingya* people reached its peak in 2017 when hundreds of thousands of them crossed the border and sought refuge in Bangladesh. Their houses were burnt, many were killed and physically tortured, and many were asked to leave by the Myanmar authority. In August 2017, the torture and killing of the *Rohingya*s started afresh and reached the peak, leading to their massive influx into Bangladesh. According to the information of District Commissioner of Cox's Bazar, within a span of two months (from 25 August 2017 to 25 October 2017), a total of 6 lakh *Rohingya*s had arrived in Cox's Bazar, while around 2 lakh *Rohingya*s were already living in Ukhiya and Teknaf Upazila in Cox's Bazar. Latest figures show that about 6.55 lakh *Rohingya*s had arrived in Bangladesh between 25 August 2017 and 7 January 2018.[48]

While Bangladesh had to deal with the earlier influx of about 2 lakh *Rohingya*s for several years, the new influx of *Rohingya* people seeking refuge in Bangladesh since August 2017 has given rise to new challenges for the country from a number of dimensions. These involve issues related to humanitarian, economic, security, strategic, diplomatic and subregional, regional and international aspects of the crisis which are complex in nature and significant in scale.

In this context, the CPD undertook a study with the objective to understand the economic, social and environmental dimensions of the *Rohingya* crisis based on field level investigation. Given that Bangladesh is a country with limited resources, the inflow of *Rohingya*s is likely to put significant pressure on the economy. Hence, there is a need to develop an appropriate strategy by taking cognisance of the critical involved issues with the objective to resolve the crisis in a pragmatic manner.

In this report, we have made an attempt to estimate the concerned *Rohingya*-crisis related costs under different scenarios. We have also made a partial assessment of the cost of deforestation arising from the influx of *Rohingya*s in the Cox's Bazar area.

The underlying objective is to understand the fiscal implications of the problem and make commensurate recommendations. In order to carry out the exercise, we have collected data from both primary and secondary sources. Primary sources include KIIs of government officials, development workers, and local staffs; FGDs with both old and new entrants living in the camps in Ukhiya and Teknaf; informal discussions with the local people; and first-hand observations at the camp-sites.

Initiatives to resolve the *Rohingya* crisis

Following the recent influx of *Rohingyas* since 25 August 2017, the GoB along with various international organisations have taken several initiatives in view of the crisis. These are summarised in Table 3.24:

Table 3.24
Initiatives Taken by the GoB and Various Organisations

Initiative	Between August and November	After November
International initiatives	Prime Minister of Bangladesh Sheikh Hasina presented the five-point proposal at the United Nations	A Memorandum of Understanding was signed between India and Myanmar on 20 December 2017 to develop the Rakhine state and

Table 3.24 contd.)

[48] https://reliefweb.int/report/bangladesh/bangladesh-humanitarian-situation-report-no17-*Rohingya*-influx-7-january-2018

Table 3.24 contd.)

Initiative	Between August and November	After November
	The EU has renewed its sanctions against Myanmar until 30 April 2018	facilitate the safe return of the *Rohingyas*.[49]
	The US declared withdrawal of military assistance from Myanmar	
Bilateral initiatives	Bangladesh's home minister visited Myanmar on 24–27 October 2017 and discussed possible ways to repatriate the *Rohingyas* back to Myanmar	Myanmar State Counsellor said they would take back daily maximum 300 Rohingyas
	Bangladesh and Myanmar signed two agreements on security and border cooperation.	The Terms of Reference signed between Myanmar and Bangladesh restated starting the repatriation process of the *Rohingyas*

Source: Various newspapers.

Impacts of *Rohingya* crisis

As has been mentioned, Bangladesh will face several challenges due to the unfolding crisis of the *Rohingya* influx. These will have three dimensions—economic, social and environmental. The adverse effects will likely have an impact on local commodity prices, tourism, employment opportunities and wages and will put a strain on the natural resources, which will, in turn, have a negative impact on the environment.

Economic

Unless the *Rohingya*s are repatriated soon, the influx will put a burden on the Bangladesh economy, more particularly at the local level, depending on the length of their stay. Cost of various essentials and services such as transport have already increased manifolds, mostly due to the surge in demand from aid workers.

During our field investigation, host communities and other local stakeholders complained about the fall in daily wages. For example, for a full day's work, a day-labourer earned Tk. 400–500, but in the camps, it is as low as Tk. 150–200. However, jobs are readily available inside the camps for the day labourers since for the relief projects, workers are needed for building makeshift houses, setting up latrines and tube-wells and other similar activities.

The camps have opened some job and business opportunities for a certain segment of the local people. Some have set up small businesses to sell fish, vegetables, dry sticks for cooking, and bamboo inside the camps. Moreover, local students, with education up to higher secondary level, are now working with the development partners in various capacities. This raises concern as most of these students are foregoing education for temporary income.

Social

The detrimental effects of the *Rohingya* crisis may translate into social problems due to population growth, health concerns, and local perception about the new arrivals. The law and order situation may also become an issue. Aid workers reported that the *Rohingya*s have a high birth rate as they lack knowledge about family planning. Moreover, around 3 per cent of *Rohingya* women are pregnant and 7 per cent are lactating who require targeted food support.[50] Thus, the size of the population is going to increase which will put further strain on food, employment, health and other basic needs.

[49]http://www.thedailystar.net/Rohingya-crisis/india-myanmar-sign-mou-to-build-houses-for-Rohingya-The refugees-1507864
[50]https://reliefweb.int/report/bangladesh/bangladesh-humanitarian-situation-report-no17-*Rohingya*-influx-7-january-2018

Health issues might arise due to unhygienic water and sanitation. According to one of the NGOs working on water, sanitation and hygiene (WASH), each latrine covers 60 people while each tube-well provides water for 50 families. As some latrines have only 2–3 rings, they get filled up fast and becomes unusable, causing many of the *Rohingya*s to resort to open defecation. The children in the camps either have no shoes or do not want to wear them at all. Hence, there is a high risk of diseases. Moreover, the makeshift shelters do not have any windows. As cooking is done mostly indoors, the risk of respiratory infection is high, particularly among women and children.

Regarding local perception, discussions with the locals and the *Rohingya*s revealed that the locals were discontent with the *Rohingya*s as the former blame the latter for price hike of essentials, being beneficiaries of aid, cause for loss of local people's income and reasons for increased security concerns. Many locals had complained that they do not receive an erstwhile stipend from NGOs; and that they lost their grazing lands. They were unhappy that they had incurred significant losses because the social afforestation programme was discontinued since land was being used for providing shelter to the *Rohingya*s.

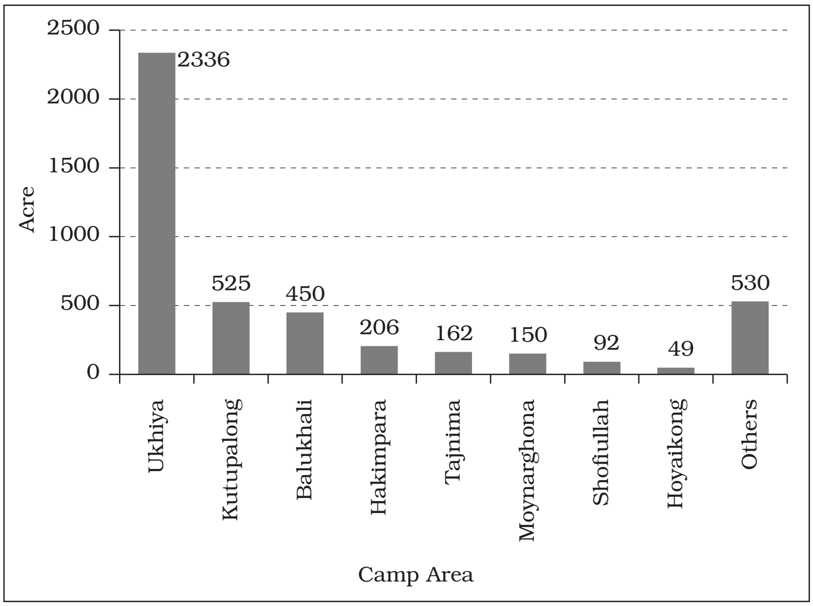
During field investigation, the locals and the aid workers echoed concerns over the prospect of future deteriorating law and order situation in the area. They reported that the *Rohingya*s slip out of the camps despite the restrictions in place. Reports indicate that syndicates charge *Rohingya*s between Tk. 20 thousand and Tk. 50 thousand to smuggle them out of the camps.[51] Furthermore, according to the locals, many previous entrants have received Bangladeshi identification cards through bribes, and many are involved in drug peddling. Several aid workers have also pointed out similar concerns as regards social problems, particularly in connection with the threat of women being trafficked outside of the country for unethical purposes.

Environmental

The *Rohingya* problem will create an environmental problem for the area which will have to be largely borne by the local community. Deforestation for settlement and burning of wood will have a direct cost on the ecology, economy and society. According to the District Commissioner's Office of Cox's Bazar, 3500 acres of

Figure 3.26

Size of *Rohingya* Camps as of 10 November 2017



Source: Department of Forestry, Government of Bangladesh (GoB).

[51] http://www.dhakatribune.com/bangladesh/nation/2017/09/17/pirates-mafia-help-*Rohingya*-flee-price/

forest land have been occupied for setting up *Rohingya* camps. This is equivalent to 1.67 per cent of Cox's Bazar's total forest area and 0.05 per cent of the national forest area. Figure 3.26 below provides a summary of the size of different camps in various sites in the Cox's Bazar district.

During the period of (late) August–December 2017, around 4 thousand acres (equivalent to about 2.4 thousand hectares) were deforested. Another 2 thousand acres are to face the same fate following an influx of the *Rohingya*s[52]. The situation has further worsened as the *Rohingya*s are felling trees in the forest to collect firewood for cooking due to lack of alternatives. It is apprehended that the collection of fuel wood will naturally increase in the dry season. According to a newspaper report, the value of lost forest land would be equivalent to Tk. 500 crore.[53]

Estimating the cost of deforestation

In this report, we have estimated the cost of 6,000 acres of deforested land which has already been lost due to the influx of the *Rohingya*s since August 2017. Four types of costs are taken into consideration for this exercise. These are (i) loss of timber and fuelwood; (ii) loss of carbon stock; (iii) loss of non-timber forest products (NTFPs); and (iv) loss of fodder yield.

Our estimation shows that the total value of 6,000 acres of deforested land in the *Rohingya* camps is equivalent to Tk. 741.31 crore or USD 86.67 million. Table 3.25 presents details of the exercise.

Table 3.25
Direct Cost of Deforestation due to *Rohingya* Influx

Amount of Loss due to Deforestation*	**Quantity/ Volume**	**Cost in Tk. (Crore)**
Loss of timber and fuelwood	46.57 m^3/ha	723.5
Loss of carbon stock	87,000 ton $C0_2$	14.5
Loss of NTFPs	-	2.1
Loss fodder yield	-	21.0
Total Direct Loss (est.)		**741.3**

Source: Authors' estimation.
Note: *The value of each type of services provided by forests has been calculated based on standard assumptions made in similar studies.

In addition to the above cost, there are several types of direct and indirect costs of deforestation which cannot be expressed in monetary terms. These will have a long-term impact on biodiversity and ecological balance.

Waste generation is another problem; most shelters in the camp area are made of tarpaulin, bamboo and tin shed, which will create problems for the environment because many of them are non-disposable items.

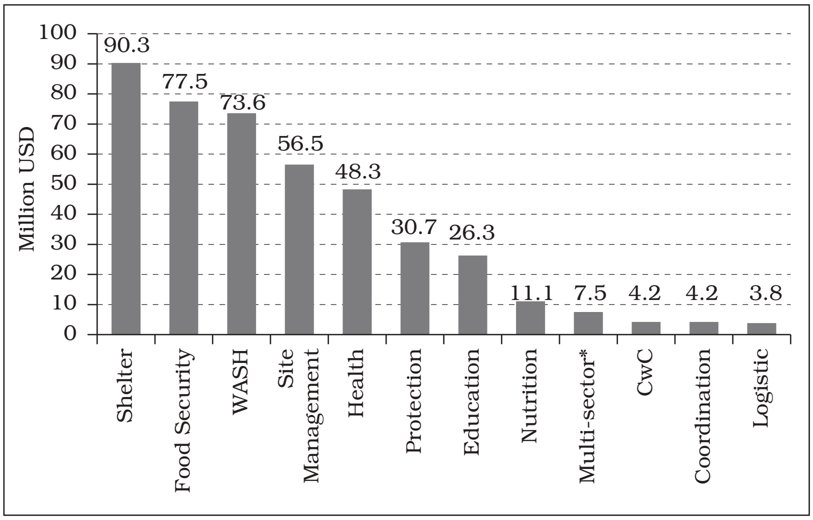
Fiscal implications

According to OCHA, USD 434 million will be required for the period September 2017–February 2018. The sectoral requirement is shown in Figure 3.27.

In addition to this, UNHCR sought USD 83.7 million as additional funds for September 2017–February 2018. In this regard, total fund requirement for the six month period would be USD 517.78 million.[54] Based

[52] http://www.thedailystar.net/backpage/shrinking-elephant-habitat-deforestation-largely-blamed-1506514
[53] http://new.bonikbarta.net/bonikbarta/news/2017-11-09/137687/৫০০-কোটি-টাকার--বন-উজাড়/
[54] http://reporting.unhcr.org/sites/default/files/UNHCR%20Myanmar%20Refugee%20Emergency%20Response%20in%20Bangladesh%20Supplementary%20Appeal%20-%20Sept2017-Feb2018%20%28September%202017%29.pdf

Figure 3.27
Fund Requirement for September 2017–February 2018



Source: Humanitarian Response Plan, OCHA (2017).
Note: CwC stands for Communication with Communities; *(Registered Refugee Response)

on the UNHCR numbers, CPD estimates that USD 882.0 million will be required for 10 months, for the period September 2017–June 2018.

Recent bilateral and political developments have shown positive signs as regards repatriation of the *Rohingya*s. As noted before, Myanmar is to take back at most 300 *Rohingya*s each day starting from 23 January 2018. Based on this information and the assumption that the whole process of repatriation will be carried out smoothly, we find that it will take almost eight years to repatriate the new wave of *Rohingya*s staying in Bangladesh since 25 August 2017.

In this context, CPD has carried out the cost of hosting the *Rohingya*s in Cox's Bazar throughout the repatriation process based on four scenarios (Table 3.26).

Table 3.26
Description of Hypothetical Scenarios and their Underlying Assumptions

Scenario 1	Assuming 300 *Rohingyas* are repatriated every day, the cost for the whole period without incorporating population growth and inflation rate	Common Assumptions: – Total *Rohingyas*: 860,000 – *Old Rohingyas*[55]*: 205,000* – *Newly arrived Rohingyas: 655,000* – Working days: 25 days per month – Inflation rate: 6 per cent every year – Population growth rate: 1.5 per cent per year – Cost is estimated based on UNHCR calculations – The estimated requirement is only indicative as those are direct costs to be incurred on account of the *Rohingyas* – Implicit costs for the loss of ecosystem due to deforestation and morbidity and mortality due to health problems and social costs could be significant – Repatriation and relocation costs not included
Scenario 2	The first scenario is repeated while adjusting for population growth and inflation rate	
Scenario 3	Assuming 200 *Rohingyas* are repatriated every day and the calculation of cost incorporates population growth and inflation rate	

Source: Authors' assumptions.

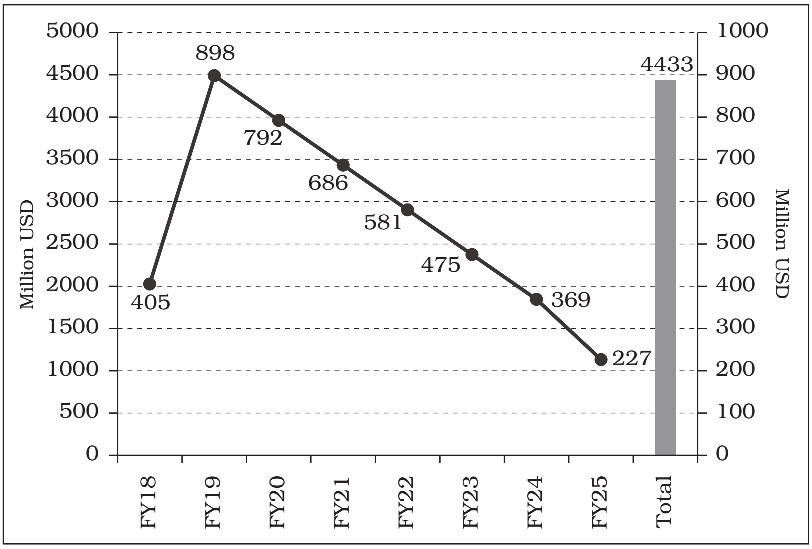
[55]Old *Rohingyas* are the one who came to Bangladesh before 25 August 2017.

Scenario 1

In this scenario, it will take 7 years to repatriate the new wave of *Rohingya*s. According to estimates by CPD, it will cost USD 4,433 million from FY2017-18 to FY2026. Estimated annual costs are presented in Figure 3.28 below.

Figure 3.28

Cost of Hosting the *Rohingyas* throughout the Repatriation Period (Scenario 1)



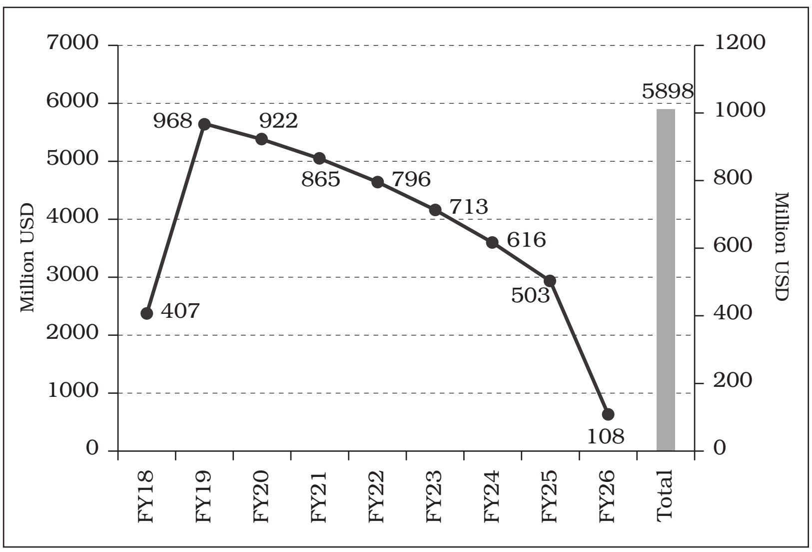
Source: Authors' calculations based on United Nations High Commission for Refugees (UNHCR) estimates.

Scenario 2

In this scenario, population growth rate and inflation rate have been adjusted in order to calculate the cost. It is estimated that during the period FY2017-18 to FY2026, it will cost USD 5,898 million[56] to host the *Rohingya*s in Bangladesh (Figure 3.29).

Figure 3.29

Cost of Hosting *Rohingyas* throughout the Repatriation Period (Scenario 2)

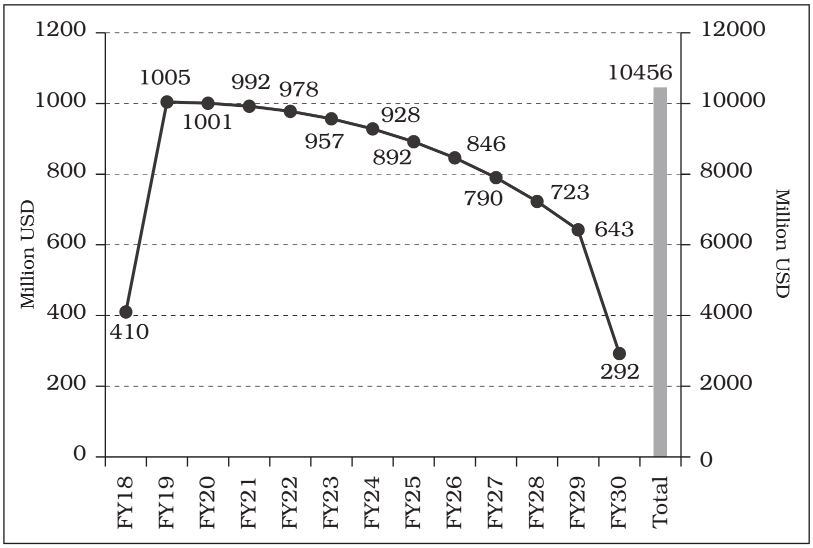


Source: Authors' calculations based on United Nations High Commission for Refugees (UNHCR) estimates.

[56] Adjusted for inflation and population growth.

Figure 3.30

Cost of Hosting *Rohingyas* if 200 People are Repatriated on a Daily Basis



Source: Authors' calculations based on United Nations High Commission for Refugees (UNHCR) estimates.

Scenario 3

If the repatriation process is not carried out smoothly, and the government is able to send only 200 persons per day, the cost is estimated to be USD 10,456 million[57] and it will take 12 years to repatriate all of the newly arrived *Rohingya*s currently staying in Bangladesh (Figure 3.30).

Summary Findings

In Table 3.27, the time required for repatriation of all (new+old) *Rohingya*s, cost of hosting all *Rohingya*s and cost of remaining *Rohingya*s (old) who came before 25 August 2017 are presented.

Table 3.27

Summary Findings on Repatriation Time and Cost of Hosting *Rohingyas*

Scenario	Assumption	Required Years for Repatriation	Cost of Hosting *Rohingyas* (Million USD)	Previous *Rohingya* Entrants*	
				Remaining after Repatriation	Cost of Hosting in the following Period (Million USD)
Scenario 1	-300 *Rohingyas* per day -no inflation or population growth	**7** *(up to FY25)*	**4,433** *(up to FY25)*	**205,000** *(up to FY25)*	**384** *(in FY26)*
Scenario 2	-300 *Rohingyas* per day -population growth and inflation rates included)	**8** *(up to FY26)*	**5,898** *(up to FY26)*	**231,000** *(up to FY26)*	**466** *(in FY27)*
Scenario 3	-200 *Rohingyas* per day -population growth and inflation rates included	**12** *(up to FY30)*	**10,456** *(up to FY30)*	**245,000** *(up to FY30)*	**625** *(in FY31)*

Source: Authors' calculations based on United Nations High Commission for Refugees (UNHCR) estimates.
Note: *Those who came before 25 August 2017.

[57] Adjusted for inflation and population growth rates.

Recommendations

- While the GoB and international and non-government organisations are playing a critically important role to provide humanitarian support to the *Rohingya*s, major global players are yet to take a strong position in resolving the crisis.
- In view of the emergent challenges, a number of measures need to be undertaken. Some of these are as follows :
  - ✓ Ensure smooth repatriation process of the *Rohingyas* as agreed between the GoB and Myanmar. To this end, preparedness on the part of Bangladesh will also be critical
  - ✓ The GoB has to continue energetic diplomacy to accelerate the repatriation process.
  - ✓ Endeavours should be taken to take advantage of extra-regional platforms such as ASEAN so that they play a proactive role in addressing the crisis.
- An in-depth study to assess the short, medium and long-term implications of the *Rohingya* crisis in terms of the needed domestic and foreign resources should be undertaken. All explicit and implicit costs related to the *Rohingya* crisis should be estimated.
- Preparation for post-Geneva follow-up meeting for resource mobilisation has to be initiated on an urgent basis.
- Support for the *Rohingyas* from development partners should be in the form of grants only. Towards this, partners' grant and loan components should be unpacked.

3.5 CONCLUDING REMARKS

The ongoing fiscal year, FY2017-18, kicked off on the back of the record-breaking GDP growth rate of 7.3 per cent in FY2016-17. Our analysis of GDP growth performance indicates deterioration of quality of the economic growth over the last five to six years (between 2010 and 2016–17). The pace of poverty reduction declined despite acceleration in average GDP growth indicating a slowdown in growth elasticity of poverty. It appears that the fruit of GDP growth is not reaching lagged regions and marginalised sections of the population. The prevailing pattern of economic growth is resulting in higher income inequality as well as wealth inequality. Indeed, the income of the poorest sections (bottom 10 per cent of total population) declined by 29.9 per cent between 2010 and 2016-17. Concurrently, employment elasticity of growth had also declined considerably, including for the manufacturing sector. Indeed, employment generation has slowed down considerably over the mentioned period. Macroeconomic policy in the country needs to refocus its objective to 'decent employment generating high economic growth' strategy from the existing 'GDP growth acceleration' strategy.

In FY2017-18, weak budgetary planning and implementation capacity continued to be a major concern. Following the retreat from implementation of VAT and SD Act 2012, efforts to bring consensus on the contested issues have been rather feeble. Revenue mobilisation gained some momentum in FY2017-18, but for obvious reasons (unrealistic programming for the fiscal framework targets), a large shortfall in revenue is a certainty. More importantly, there are signs of greater reliance on import-related revenue sources while growth of income tax collection is slower compared to other components. This is not going to address the deteriorating scenario as regards income inequality in the country. Higher utilisation of foreign aid is a positive sign in the context of budget implementation trends in FY2017-18, thanks almost solely to the Power Division. While the scale of budget deficit may not be a major concern, the high cost of borrowing will put pressure on debt sustainability in the medium term. The government has taken up a number of mega public infrastructure projects over the past years. This had implications for allocative priorities of the public expenditure portfolio, often at the expense of the social sectors. On the other hand, delayed implementation, cost overrun and institutional weakness have undermined the effectiveness of these projects, and hence these projects are yet to provide impetus to private investment. Flood and *Rohingya* crisis, the two major setbacks for the Bangladesh economy in FY2017-18, will also put some pressure on the budget for the current fiscal. The government needs to consider undertaking an assessment of implementation in the FY2017-18 budget, with a view to its early revision. In the meantime, the government should focus on raising revenue from niche areas including speedy realisation of disputed revenue claims through the ADR and recovering outstanding dues, particularly from state-owned enterprises. More emphasis must be put on arrest duty and tax evasion. With a view to bring more discipline in the macroeconomic management, the government needs to avoid all types of conspicuous public financing in this election year.

Creeping food inflation in the backdrop of high rice prices was observed during the latter months of FY2016-17. With new flood and weak foodstock management, the situation had aggravated further with consequent erosion of purchasing power of the poorest section of the society. The government will need to continue with incentivising rice imports with a view to ensure adequate market supply and to enhance public stock over the next six months. However, it may be difficult to bring down rice price to pre-crisis levels. In this connection, the government may expand safety net programmes in favour of the poor. As it is apprehended that non-food inflation may also move upward in the coming months (catch up with food inflation), the forthcoming monetary policy of the central bank may consider raising the policy rates. Raising general provisions for unclassified loans and reducing debt-equity ratio for consumer and housing loans may also be considered.

Crisis in the banking sector has become the Achilles' heel of the Bangladesh economy. The rising non-performing loan is crippling the SCBs in particular, although some of the private banks are also not immune to this malaise. The allocations of public 'tax' money in the form of recapitalisation could not bring any change in the capital inadequacy in SCBs. The 'new' commercial banks are facing multifarious difficulties. Farmers Bank is on the verge of collapse while several fourth-generation banks are in trouble. Overall, one can observe deterioration of asset quality in the PCBs. More so, more licenses for three new commercial banks are likely to be issued under 'political consideration'. 'Cronyism' in the ownership of banks has become a new challenge for banking sector governance. Proposed amendment in the Banking Company Act to increase the number of family members in the board of banks and their tenure will further undermine the quality of governance in the PCBs. Regrettably, the central bank has failed to demonstrate the quality leadership required to instill good governance in financial sector management. The reforms required in the system are being ignored, although there is apprehension about dire consequences. Regrettably, an initiative to take comprehensive banking sector reforms measure, which CPD has been harping for long, may need to wait for the next national election.

CPD in its earlier IRBD analysis cautioned the government as regards impending pressure on the BoP. Despite an upturn in growth rates of export earnings and in the inflow of remittances, significant rise in import payments led to serious deficit in current account balance. Although, higher inflow of foreign aid and other medium term foreign loans have helped to contain overall deficit in the BoP, it may not be adequate in the coming months. The central bank, throughout FY2017-18, allowed BDT to depreciate. This has helped exporters to enhance competitiveness vis-à-vis other competing countries. The central bank should now focus on bringing stability to the exchange rate market. This may deplete the foreign exchange reserve in the coming months. Such steps will also help contain money supply in the domestic market. However, this may not be enough and the central bank should consider discouraging imports in a targeted manner. To this end, raising L/C margins for import of consumer and luxurious commodities can be an option; alternatively, the time for L/C repayment may be reduced for such items.

Overall, in FY2017-18, macroeconomic stability has come under considerable pressure. The need to significantly improve the quality of macroeconomic management has emerged as an immediate and urgent concern. Over the past years, CPD has been arguing for a number of critical economic reforms. It now appears that the reform agenda of the incumbent government will not see much light till the upcoming national election. One only hopes that the reform issues will find place in the ensuing electoral debates.

Nevertheless, macroeconomic policy stance in the upcoming months should be conservative. As the national election is nearing, it may be tempting for the government to go for a more populist expansionary macroeconomic policy. However, the greater cause of maintaining macroeconomic stability should be the guiding principle for the government as it moves to the second half of FY2017-18. It is to be seen how the incumbent government manages the economy during the upcoming political transition.

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ANNEXES

Annex Table 3.1
Expenditure (July–November) Over Original ADP in the Last 10 Fiscal Years

Year	Taka	Project Aid	Total
Jul-Nov FY09	19.8	15.3	17.7
Jul-Nov FY10	22.7	22.6	22.6
Jul-Nov FY11	24.1	14.8	20.4
Jul-Nov FY12	25.3	12.8	20.2
Jul-Nov FY13	27.2	20.8	24.7
Jul-Nov FY14	21.7	17.0	20.0
Jul-Nov FY15	19.3	20.7	19.8
Jul-Nov FY16	18.5	13.6	16.8
Jul-Nov FY17	20.9	16.7	19.3
Jul-Nov FY18	18.5	22.6	20.1

Source: Authors' calculations based on Implementation Monitoring and Evaluation Division (IMED) data.

Annex Table 3.2
Implementation Record of Top 10 Ministries (July–November)

(in Per cent)

Ministry/Division	FY13	FY14	FY15	FY16	FY17	FY18
Power Division	38.9	13.2	18.3	18.8	33.3	47.6
Local Govt. Division (including block allocation)	29.8	30.9	27.6	26.6	27.9	23.8
Road Transport and Highways Division	32.4	20.3	17.4	14.2	14.1	26.8
Ministry of Railway	12.8	25.2	9.7	13.1	20.2	9.6
Ministry of Science and Technology	21.7	40.1	80.3	2.8	67.8	5.0
Bridges Division	3.9	2.4	10.2	12.5	12.3	7.2
Ministry of Health and Family Welfare	15.1	16.6	18.2	15.9	12.3	16.1
Ministry of Primary and Mass Education	36.4	30.4	29.2	21.1	24.5	23.7
Ministry of Education	30.4	25.4	23.5	17.5	15.9	15.4
Ministry of Water Resources	22.0	22.3	4.4	10.0	8.2	10.0
Top Ten Ministry	28.5	20.4	21.7	18.2	21.9	22.8
Grand Total	**24.3**	**20.0**	**19.8**	**16.8**	**19.3**	**20.1**

Source: Authors' calculations based on Implementation Monitoring and Evaluation Division (IMED) data.

Annex Table 3.3
Ministries and Divisions that Faced Cost Overrun during FY2005-06 and FY2015-16

(in Crore Taka)

Ministry/Division	FY06	FY16
Local Government Division	1,543	1,868
Power Division	1,115	112
Ministry of Communication (Transportation)	722	1,073
Ministry of Food and Disaster Management	188	661
Ministry of Water Resources	159	81
Ministry of Youth and Sports	122	2
Ministry of Primary and Mass Education	96	356

(Annex table 3.3 contd.)

(Annex table 3.3 contd.)

Ministry/Division	**FY06**	**FY16**
Ministry of Agriculture	73	66
Ministry of Environment and Forest	40	10
Ministry of Liberation Affairs	27	-
Ministry of Education	25	21
Ministry of Social Welfare	17	-
Ministry of Defence	3	5
Energy and Mineral Resources Division	3	921
Ministry of Cultural Affairs	3	3
Ministry of Jute and Textile	2	-
Rural Development and Co-operatives Division	2	48
Ministry of Fisheries and Livestock	2	78
Ministry of Housing and Public Works	1	-
Ministry of Labor and Employment	1	-
Ministry of Establishment	0.11	-
Ministry of Women and Children Affairs	0.08	12
Implementation Monitoring and Evaluation Division	0.05	-
Planning Division	0.03	4
Total	**4,145**	**5,643**

Source: Authors' calculations based on Bangladesh Planning Commission data.

Annex Table 3.4

Country-wise Comparison of Prices of Per-unit Woven and Knit Items in Key Markets

Product	**Bangladesh**	**China**	**India**	**Vietnam**	**Cambodia**
US market (July–Oct)					
Knit (61)	13.0	13.8	17.9	17.6	15.3
61102020	*14.1*	*16.8*	*19.2*	*18.2*	*16.7*
61091000	*9.1*	*10.7*	*12.3*	*17.9*	*12.6*
61103030	*13.2*	*12.4*	*24.2*	*17.9*	*15.4*
Woven (62)	16.0	16.3	26.6	23.5	17.5
62034245	*13.5*	*11.0*	*17.3*	*17.4*	*16.2*
62052020	*16.9*	*23.0*	*23.0*	*23.3*	*22.8*
62046280	*15.9*	*12.1*	*18.4*	*18.1*	*17.6*
EU market (July–Sept)					
Knit (61)	14.3	15.1	17.8	23.9	19.5
61091000	*12.3*	*17.0*	*17.6*	*23.4*	*20.2*
61103099	*14.8*	*16.8*	*24.6*	*21.3*	*19.0*
61051000	*13.8*	*16.8*	*21.4*	*27.6*	*23.7*
Woven (62)	17.2	18.6	28.5	26.8	18.4
62034231	*13.6*	*14.4*	*17.4*	*22.6*	*15.7*
62034235	*15.7*	*12.1*	*19.8*	*21.7*	*15.9*
62052000	*19.9*	*26.2*	*26.3*	*31.9*	*26.4*

Source: Authors' calculations using data from United States Integrational Trade Commission (USITC) and Eurostat.

(Annex table 3.4 contd.)

(Annex table 3.4 contd.)

Note:

61051000	Men's or boys' shirts of cotton, knitted or crocheted (excl. nightshirts, t-shirts, singlets and other vests)
61091000	T-shirts, singlets and other vests of cotton, knitted or crocheted
61091000	T-shirts, singlets and other vests of cotton, knitted or crocheted
61102020	Sweaters, pullovers and similar articles, knitted or crocheted, of cotton, nesoi, by HTS 10-digit categories
61103030	Sweaters, pullovers and similar articles, knitted or crocheted, of manmade fibers, nesoi
61103099	Women's or girls' jerseys, pullovers, cardigans, waistcoats and similar articles, of man-made fibres, knitted or crocheted (excl. lightweight fine knit roll, polo or turtleneck jumpers and pullovers and wadded waistcoats
62034231	Men's or boys' trousers and breeches of cotton denim (excl. knitted or crocheted, industrial and occupational, BIB and brace overalls and underpants
62034235	Men's or boys' trousers and breeches of cotton (excl. denim, cut corduroy, knitted or crocheted, industrial and occupational, bib and brace overalls and underpants)
62034245	Men's or boys' trousers and shorts, not bibs, not knit/crochet, cotton, not containing 15% or more by weight of down, etc
62046280	Women`s or girls` trousers, breeches and shorts, not knitted or crocheted, of cotton, nesoi, o/than rec perf outwear
62052000	Men's or boy's shirt of cotton (excl. knitted or crocheted, nightshirts, singlets and other vests)
62052020	Men's or boys' shirts, not knitted or crocheted, of cotton, nesoi,

Annex Table 3.5

Performance by Type of Bank

(in Per cent)

Indicator	Bank Type	2012	2013	2014	2015	2016[J]	2017[P]
Capital adequacy	***Capital to Risk Weighted Asset***						
	SCBs	8.1	10.8	8.3	6.4	5.8	7.0
	DFIs	-7.8	-9.7	-17.3	-32.0	-34.7	-32.8
	PCBs	11.4	12.6	12.5	12.4	11.9	12.2
	FCBs	20.6	20.2	22.6	25.6	23.8	23.3
Asset Quality	***NPL to Total Loans***						
	SCBs	23.9	19.8	22.2	21.5	25.7	26.8
	DFIs	26.8	26.8	32.8	23.2	26.1	23.8
	PCBs	4.6	4.5	5.0	4.9	5.4	5.8
	FCBs	3.5	5.5	7.3	7.8	8.3	7.9
Management	***Expenditure-Income Ratio***						
	SCBs	73.2	84.1	84.1	84.5	99.2	
	DFIs	91.2	94.8	99.5	113.9	132.2	
	PCBs	76.0	77.9	75.8	75.5	73.5	
	FCBs	49.6	50.4	46.8	47.0	45.0	
Profitability	***Return on Asset***						
	SCBs	-0.6	0.6	-0.6	-0.0	-0.2	-0.6
	DFIs	0.1	-0.4	-0.7	-1.2	-2.0	-1.6
	PCBs	0.9	1.0	1.0	1.0	0.7	0.7
	FCBs	3.3	3.0	3.4	2.9	2.7	2.2
	Return on Equity						
	SCBs	-11.9	10.9	-13.6	-1.5	-9.5	-19.4
	DFIs	-1.1	-5.8	-6.0	-5.8	-9.5	-8.1
	PCBs	10.2	9.8	10.3	10.8	9.4	7.5
	FCBs	17.3	16.9	17.7	14.6	13.2	10.8

(Annex table 3.5 contd.)

(Annex table 3.5 contd.)

Indicator	Bank type	2012	2013	2014	2015	2016^{J}	2016^{P}
Liquidity	***Liquid Asset***						
	SCBs	29.2	44.3	42	41.4	40.1	
	DFIs	12.0	15.3	6.6	0.0	0.0	
	PCBs	26.3	28	28.2	19.7	18.5	
	FCBs	37.5	46.2	56.9	51.8	46.0	
	Excess Liquidity						
	SCBs	10.2	25.3	23.9	26.4		
	DFIs	1.0	4.2	6.6	6.6		
	PCBs	9.5	11.3	11.0	11.9		
	FCBs	18.7	27.4	37.6	38.9		

Source: Bangladesh Bank Annual and Quarterly Reports.

Note: 'J' refers to June; 'P' denotes Provisional.

Annex Table 3.6

NPLs in Fourth Generation Banks (as of September 2017)

(in Crore Taka)

Name of Bank	Amount of NPL
Farmers Bank	378.0
NRB Commercial Bank	194.0
Meghna Bank	152.0
Midland Bank	46.0
South Bangla Agricultural Bank	15.0
Modhumoti Bank	1.4
Total	**786.4**

Source: The Financial Express, Bangladesh, 27 November 2017.

Annex Table 3.7

State of The Farmers Bank Limited in 2017

Date	Incidence
10 January 2018	Md. Ehsan Khasru joins as Managing Director and CEO
01 January 2018	Provisional operational profit of Farmers Bank falls by Tk. 660 million in one year, from Tk. 920 miilion in 2016 to Tk. 260 million in 2017
25 December 2017	Farmers depositors withdraw deposits of over Tk. 1200 crore in the last few days, whilst there are no new deposits
25 December 2017	A depositor of Tk. 5 crore can receive only Tk. 50,000 in Motijheel, Gulshan and Dhanmondi branch of Farmers Bank
25 December 2017	Deposits of about Tk. 5,000 crore of around 525,000 depositors remain stuck in Farmers Bank
21 December 2017	Farmers Bank fails to pay salary and allowances for the month of December of around 1500 staff and employees
20 December 2017	Bangladesh Bank removes Farmers Bank Managing Director and Chief Executive Officer AKM Shameem just 12 days before his retirement because he failed to protect the interests of depositors
18 December 2017	The newly reconstituted board of Farmers Bank injects Tk. 17 crore into the bank to help deal with the ongoing cash crunch.
18 December 2017	Farmers Bank appeals to the central bank for enhancing the yields on its subordinated bonds to 10 per cent from existing 9.0 per cent

(Annex table 3.7 contd.)

(Annex table 3.7 contd.)

Date	Incidence
18 December 2017	Savers withdraw Tk. 1,100 crore in the last 15 days putting Farmers Bank into a cash crisis.
14 December 2017	Farmers Bank fails to repay interbank short-term loans of about Tk. 700 crore to four banks in October and November 2017
14 December 2017	Farmers Bank receiving about Tk. 150 crore from the state-owned banks every working day through the interbank call money market
14 December 2017	Private commercial banks refuse to lend money to Farmers Bank in the overnight call money market even at high rates of return
13 December 2017	A standing committee of the Bangladesh Bank interrogates Managing Director AKM Shameem in a personal hearing held at the central bank headquarter
13 December 2017	Farmers Bank deposits fall to Tk. 4,700 crore, from Tk. 5,660 crore on October 30, 2017 as depositors lose their confidence in the bank
12 December 2017	Bangladesh Bank rejects requests from former Farmers Bank Chairman Muhiuddin Khan Alamgir and Audit Committee Chairman Md Mahabubul Haque Chisty to increase their shares in the bank
11 December 2017	Bangladesh Bank permits Farmers Bank to float subordinated bonds worth BDT 5 billion for increasing the bank's capital base.
7 December 2017	Farmers Bank fails to pay more than Tk. 229 crore to Bangladesh Climate Change Trust Fund on maturity of its fixed-term deposits
5 December 2017	Central bank launches a special inspection of the problem-ridden Farmers Bank Limited to assess its real financial health
December 2017	Farmers Bank delays payment of Tk. 1.07 crore on fixed-term deposits of Bangladesh Inland Water Transport Corporation
28 November 2017	Bangladesh Bank asks the reconstituted board to improve overall financial status of Farmers Bank within next three months
26 November 2017	Central bank issues a show-cause notice, asking the Managing Director of Farmers Bank, AKM Shameem, to explain the ongoing liquidity problem of the bank, and the fresh loan disbursement despite imposition of an embargo by the central bank.
27 November 2017	Awami League MP Muhiuddin Khan Alamgir, also a former minister, resigns as Farmers Bank Chairman
27 November 2017	Md Mahabubul Haque Chisty resigns as Audit Committee Chairman and Director
21 November 2017	Bangladesh Bank agrees to provide short-term loan of Tk. 96 crore at 6.75 percent interest to Farmers Bank by way of repo
20 November 2017	Farmers Bank has just Tk. 65 lakh in its current account with the central bank, according to Bangladesh Bank
20 November 2017	Farmers Bank Chairman Muhiuddin Khan Alamgir seeks to purchase 1 crore shares and Audit Committee Chairman Md Mahabubul Haque Chisty seeks to purchase 50 lakh shares in Farmers Bank at a face value of Tk. 10 per share
20 November 2017	Bangladesh Telecommunication Company Ltd finally gets back its deposit of Tk. 35.44 crore from troubled Farmers Bank's Gulshan corporate branch
17 November 2017	Farmers Bank fails to maintain the statutory liquidity ratio and cash reserve ratio and incurs penalty of Tk. 18.49 crore
17 November 2017	Farmers Bank owes Tk. 124 crore in the call money market and the amount is being rolled over since January, according to data from the Bangladesh Bank
15 November 2017	Farmers Bank twice fails to honour a cheque of Tk. 35.44 crore presented by Bangladesh Telecommunications Company Ltd, before finally making the payment
9 November 2017	Farmers Bank seeks a deposit support of Tk. 300 crore from the central bank to tackle its liquidity crunch but is denied
29 October 2017	Parliamentary Standing Committee on Finance Ministry suggests that Bangladesh Bank should further investigate irregularities and corruption in Farmers Bank

(Annex table 3.7 contd.)

(Annex table 3.7 contd.)

Date	Incidence
30 September 2017	Farmers Bank non-performing loans now worth BDT 3.77 billion or 7.45 per cent of the total loans disbursed
19 September 2017	Investigations reveal that former director of Farmers Bank, Md Mahabubul Haque Chisty's firm EFS International has defaulted Tk. 53.67 crore in loans from BASIC Bank
14 September 2017	Advance-deposit ratio of Farmers Bank at 86.23 percent which is above the safe limit of 85 per cent set by central bank for conventional banks
September 2017	Farmers Bank's weighted average interest rate on deposits is 8.79 percent in contrast to the industry average of 4.9 percent, and lending rate is 14 percent in contrast to the industry average of 9.45 percent
September 2017	Farmers Bank has deposits totaling Tk. 5,170 crore and loans totaling Tk. 5,066.39 crore, which are 97.99% of deposits
September 2017	Capital shortfall of Farmers Bank reaches Tk. 75 crore
02 July 2017	Farmers Bank posts operating profits of Tk. 420 million in the H1 of 2017 from Tk. 300 million in the same period of last year
June 2017	Farmers Bank non-performing loans worth Tk. 306.21 crore, which is 6.35 percent of its total disbursed loans
June 2017	Net loss of the Farmers Bank stands at Tk. 131.1 million; 28 out of the total 54 branches are incurring loss.
01 March 2017	Farmers Bank is among eleven banks that fail to maintain minimum capital to risk weighted assets ratio according to BASEL III framework
March 2017	Advance-deposit ratio of Farmers Bank reaches 88.70 percent, which is above the safe limit of 85 per cent set by central bank for conventional banks
21 February 2017	Farmers Bank Limited signs an agreement with Bangladesh to disburse funds under a JICA-assisted Urban Building Safety Project (UBSP)
13 January 2017	Central bank appoints an observer to the Farmers Bank after detecting irregularities in sanctioning and disbursing loans and hiding information on non-performing loans amounting to around BDT 4 billion
01 January 2017	Farmers Bank Ltd profit rises to Tk. 1.01 billion in 2016 from Tk. 650 million in 2015.

Source: Authors' compilations from various sources.

Annex Table 3.8

Comparison between The Farmers Bank and Oriental Bank

(in Crore Tk.)

Particular	The Farmers Bank	Oriental Bank
Fund embezzlement	400 (September–November 2015)	596 (2003-2006)
Net loss	13.1 (June 2017)	450 (March 2006)
Capital shortfall	75 (September 2017)	877 (March 2006)
Non-performing loan/classified loan	[Non-performing loan] 378 (September 2017)	[Classified loan] 1,100 (June 2006)
Outstanding dues from SoEs	700 (December 2017)	300 (June 2006)

Source: The Daily Star and The Financial Express, Bangladesh.

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