Independent Review of Bangladesh's Development

বাংলাদেশের উন্নয়নের স্বাধীন পর্যালোচনা

State of the Bangladesh Economy in FY2022-23

(Third Reading)

(Draft)

Released to the Media on
27 May 2023, Dhaka

Centre for Policy Dialogue
Celebrating 30 1993-2023
Generating Knowledge, Giving Voice, Challenging Injustice

cpd.org.bd cpd.org.bd cpdbd CPDBangladesh

Contents

CPD IRBD 2023 Team

Lead contributions were provided by *Dr Fahmida Khatun*, Executive Director; *Professor Mustafizur Rahman*, Distinguished Fellow; *Dr Khondaker Golam Moazzem,* Research Director; *Mr Towfiqul Islam Khan*, Senior Research Fellow; *Mr Muntaseer Kamal,* Research Fellow; and *Mr Syed Yusuf Saadat,* Research Fellow, CPD.

Other team members include *Mr Abu Saleh Md. Shamim Alam Shibly*, Senior Research Associate; *Mr Foqoruddin Al Kabir*, Research Associate; *Ms Nadia Nawrin,* Research Associate; *Ms Maesha Rashedin Joita*, Programme Associate; *Ms Lubaba Reza,* Programme Associate; *Mr Mohammad Abu Tayeb Taki;* Programme Associate, and *Mr Mahrab Al Rahman*, Programme Associate, CPD.

Mr Muntaseer Kamal was the Coordinator of the CPD IRBD 2023 Team.

Acknowledgements

The CPD IRBD 2023 Team would like to register its profound gratitude to *Professor Rehman Sobhan*, Chairman, CPD for his advice in preparing this report.

The CPD IRBD Team also expresses its sincere thanks to *Dr Debapriya Bhattacharya,* Distinguished Fellow, CPD for his guidance and support to the team.

Concerned officials of several government agencies have extended valuable support to the CPD IRBD Team members. In this connection, the Team would like to register its sincere appreciation to Bangladesh Bank (BB), Bangladesh Bureau of Statistics (BBS), Export Promotion Bureau (EPB), Ministry of Finance (MoF), Ministry of Food (MoFood), National Board of Revenue (NBR), and Planning Commission.

The Team gratefully acknowledges the valuable support provided by the Dialogue and Communication Division, CPD in preparing this report. Contribution of the CPD Administration and Finance Division is also highly appreciated. Assistance of *Mr A H M Ashrafuzzaman*, Deputy Director, IT is particularly appreciated.

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

State of the Bangladesh Economy in FY2022-23

(Third Reading)

SECTION 1. INTRODUCTION

The assessment of key macroeconomic correlates of Bangladesh being carried out by the CPD as part of its flagship IRBD programme comes at a crucial juncture in the country's development journey. The measures required to correct some of the long-standing as also the newly emerging disquieting trends informing the management of the economy warrants in depth analysis to arrive at possible solutions. As is known, the Bangladesh economy had to face formidable difficulties owing to the adverse fallouts of the COVID-19 pandemic. At a time when the economy was coming out of the worst impacts of the pandemic, the situation was exacerbated by the Russia-Ukraine war which started in late February 2022 and was manifested in high global commodity prices, high imported inflation, and supply chain disruptions. While these exogenous factors have definitely left their footprints, embedded structural weaknesses, sub-optimal policies, lax policy implementation, lack of good governance, and inability to implement the required reforms have compounded the difficulties facing macroeconomic management in recent times. In July 2022, CPD had cautioned that these weaknesses would aggravate the pressure points in managing the Bangladesh economy (CPD, 2022).

Indeed, the Bangladesh economy has remained under considerable pressure throughout the first three quarters of FY2023. This was manifested through, inter alia, subdued momentum in revenue mobilisation and consequent shrinking of the fiscal space, high reliance on borrowings from the central bank for financing budget deficit, tightened liquidity position of scheduled banks, high prices of essentials, deteriorating external sector balance and foreign exchange reserve (CPD,2023). In view of these challenges, the Bangladesh government has resorted to a 42-month International Monetary Fund (IMF) supported programme under the Extended Credit Facility (ECF) and Extended Fund Facility (EFF) in an attempt to restore macroeconomic stability[1]. As IMF itself mentions, 'Bangladesh would risk falling into a subpar equilibrium of low growth, low investment, and weak human development, if left to restore macroeconomic stability on its own' (IMF, 2023, p.5). Furthermore, to meet the large climate financing requirements, the government in parallel sought support from the Resilience and Sustainability Facility (RSF)[2] of the IMF. Bangladesh has also sought budget support of USD 500 million form the World Bank in April 2023.

The timeline of the IMF programme coincides with the preparatory phase of Bangladesh's LDC graduation and the second half of the period to attain the SDGs. Given the juxtaposition of current developments and upcoming milestones, it is critically important to focus on consolidating the gains of the past, restoring macroeconomic stability, and adjusting to new realities taking the growth and stability trade-offs into cognisance. It is also to be noted that the IMF programme is

[1] The key objectives of the ECF/EFF arrangement are to restore macroeconomic stability and prevent disruptive adjustment (i.e., strict demand and import management measures which are disproportionately affecting the poor and the vulnerable and are likely to adversely impact medium-term growth prospects if they remain in place). The ECF/EFF programme is also expected to induce momentum in implementing source of the overdue macroeconomic reforms.

[2] The programme objective of the RSF is to improve the climate investment potential of Bangladesh.

being implemented on the eve of presentation of the FY2023-24 budget and when the country is preparing for its next national elections.

As experience shows, any attempt to restore macroeconomic stability under a predetermined set of conditions inevitably entails some hard choices and limits the options available for policy manoeuvring. The below examples could be useful to highlight this point.

1. If maintaining fiscal balance via lowering the budget deficit is the policy objective, then exploring new avenues of revenue mobilisation or reducing public expenditure might be unpopular for a political government. Also, continued bank borrowing to finance the growing budget deficit may crowd out private investment.
2. If improving the external sector balance is considered, then pursuing a free-floating exchange rate regime may entail inflationary implications. On the other hand, maintaining a managed exchange rate regime may not bode well for the foreign exchange reserve situation.
3. As a way of containing inflation, if a market-based interest rate is pursued, then it will imply higher cost of funds for the businesses. Counter inflationary measures such as providing direct fiscal support to the vulnerable groups via social safety nets may contradict the objective of maintaining a healthy fiscal balance.
4. Similarly, providing subsidy on agriculture and allocations for public procurement to ensure food security may not go hand in hand with the objective of maintaining fiscal balance. The subsidy required to ensure food security will depend on the import price of agricultural inputs, which, in turn, will be impacted by the exchange rate regime and global commodity prices.

Such intertwined nature of policy options calls for a concerted and coordinated effort towards macroeconomic management. At the same time, it raises further questions regarding how the very concept of macroeconomic stability should be perceived. Past experiences from the developing countries show that stabilisation packages prescribed by the multilateral agencies share many common elements. However, there are divergences in the results of such packages (Abbott, Andersen and Tarp, 2010; Taylor, 1988).

In this backdrop, the present report identified four sets of critical issues which should receive heightened attention in the current policy discourse, particularly from the macroeconomic management viewpoint. These are: maintaining fiscal balance, improving external sector equilibrium, containing inflation, and ensuring food security. While this report acknowledges the presence of several other critical issues, the aforementioned four were consciously focused upon given their significance in restoring macroeconomic stability, disciplining macroeconomic management, and identifying development priorities. Each of the selected four blocks of issues takes note of the IMF conditionalities (e.g., subsidy management, reserve estimation and milestones, market alignment) and their implications, data-related concerns etc. Furthermore, findings from recent nationally representative surveys such as HIES and LFS have been made use of as required.

References

Abbott, P., Andersen, T. B., & Tarp, F. (2010). IMF and economic reform in developing countries. *Quarterly Review of Economics and Finance, 50*(1), 17–26.

CPD. (2022). *Recent Challenges Facing the Bangladesh Economy: A Brief Overview* [PowerPoint slides]. Dhaka: Centre for Policy Dialogue (CPD).

CPD. (2023). *CPD's Recommendations for the National Budget FY2023-24: Weathering the Storm, Containing the Risks*. Dhaka: Centre for Policy Dialogue (CPD).

IMF. (2023). *Bangladesh Requests for an Extended Arrangement under the Extended Fund Facility, an Arrangement under the Extended Credit Facility, and an Arrangement under the Resilience and Sustainability Facility*. Washington, D.C.: International Monetary Fund (IMF).

Taylor, L. (1988). *Varieties of Stabilization Experience: Towards Sensible Macroeconomics in the Third World*. New York: Oxford University Press.

SECTION 2. FISCAL BALANCE OF BANGLADESH: SIX KEY AREAS OF POLICY INTERESTS

The fiscal framework of Bangladesh has shown signs of considerable stress all through the ongoing FY2023. This has been manifested in, inter alia, subdued growth in revenue mobilisation, slow implementation of the annual development programme (ADP), and increased reliance on bank borrowings to finance budget deficit – particularly from the central bank. The government also had to resort to an IMF-supported programme in the backdrop of discernible macroeconomic instabilities. The key objectives of this support programme include enhancement of revenue mobilisation, reduction of NSD certificate issuance, containment of subsidies, and increase of public expenditure efficiency with fiscal and institutional reforms. It must also be mentioned in this regard that the IMF programme comes with a set of time-bound milestones and conditionalities; the extent of availability of the support will hinge on Bangladesh's ability to meet those. Such conditionalities, on the one hand, will provide some form of policy predictiveness. On the other, these will entail some hard choices on the part of the policymakers. In this backdrop, the present chapter spotlights some key areas that require urgent policy attention.

2.1 Major Observations on the Fiscal Framework during FY2023

Targets of revenue mobilisation for FY2023 will be missed by a large margin.

The revenue mobilisation scenario in FY2023 appears to be quite dismal. According to the Ministry of Finance (MoF) data, during July-February of FY2023, total revenue collection decreased by (-) 0.1 per cent over the corresponding period of FY2022. However, the targeted growth of total revenue for the entire fiscal year was 29.5 per cent. This implies that an unprecedented 98.3 per cent growth will be required during March-June of FY2023 if the target of revenue mobilisation is to be achieved. According to the MoF data, revenue collected by the National Board of Revenue (NBR) decreased by (-) 1.3 per cent during the July-February period of FY2023[3]. Since NBR is tasked to mobilise more than 85 per cent of the total revenue envelope, this state of collection undoubtedly points towards a large shortfall in revenue earnings (i.e., the gap between targeted and actual revenue mobilisation) at the end of the fiscal year. Indeed, CPD in March 2023 projected that the total revenue shortfall (including tax and non-tax) at the end of FY2023 would be approximately Tk. 75,000 crore (CPD, 2023). Hence, it can be said with certainty that it is not possible to attain the ambitious revenue mobilisation targets set out in the national budget for FY2023 as well as the IMF conditionality.

Full utilisation of the budgetary allocations remains elusive.

The inability to deliver on the programmed budgetary allocation has continued in FY2023. During the first eight months of FY2023, only 37.6 per cent of the total budgetary allocations could be utilised. The corresponding figure for FY2022 was 38.3 per cent. Alarmingly, annual development programme (ADP) expenditure fell both in terms of monetary value and implementation rate during the aforementioned period as far as the MoF data is concerned[4]. The utilisation rate of

[3] Curiously, as per NBR data, revenue collected by NBR increased by 8.9 per cent during the July-February period of FY2023 compared to the corresponding period of FY2022.

[4] According to data from Implementation Monitoring and Evaluation Division (IMED) of the Ministry of Planning, ADP implementation rate was 32.3 per cent during July-February of FY2023. IMED also provides

non-ADP expenditure rose albeit significantly, from 47.5 per cent during July-February FY2022 to 47.9 per cent during July-February FY2023 – indicating a 15 per cent growth. This was driven primarily by increases in expenditure owing to interest payments, subsidies, incentives, and current transfers. Due to the depreciation of the Bangladeshi Taka (BDT), the expenditure incurred for interest payments is likely to face upward pressure during the remainder of FY2023.

While the budget deficit widened, the composition of deficit financing has become a more problematic issue.

According to the MoF data, in the first eight months of FY2023, the budget deficit (excluding grants) reached Tk. 21,201 crore compared to the budget surplus of Tk. 2,937 crore in the corresponding period of FY2022. Net sales of National Savings Directorate (NSD) certificates decreased by (-) 63.4 per cent during the July-February FY2023 period thanks to reduced interest rates and additional regulatory requirements, including the obligation to provide income tax return submission receipts. Net borrowing from the banking sector, including the Bangladesh Bank, increased by nearly 70 per cent during the aforementioned period[5]. Net foreign financing has declined by (-) 24.8 per cent during the first eight months of FY2023, and the government has sought increased budget support from multiple development partners for FY2023.

2.2 Six Key Areas of Policy Interests

NBR will need to identify new sources to mobilise the required revenue.

Enhanced economic activities will induce natural growth in revenue collection. To find out its extent, an OLS estimation was carried out. The model considered is provided in the following equation.[6]

Log Tax revenue = $\alpha + \beta_1$ *Log GDP* + β_2 *Log Import* + β_3 *Inflation rate* + ε

From the estimation, it was found that a one per cent increase in real GDP and import will increase the tax revenue collection by 0.59 per cent and 0.65 per cent, respectively; the coefficient values are positive and statistically significant (Annex Table 2.1). On the other hand, the coefficient for inflation is found to be negative (-0.02) and statistically significant. This implies that a one per cent increase in inflation will result in a decrease in tax revenue collection by 0.02 per cent (Annex Table 2.1). As have been reported in several media outlets, targeted GDP growth and anticipated inflation in the upcoming FY2024 are 7.5 per cent and 6.0 per cent, respectively. Also, IMF (2023) projected that imports would increase by 14.2 per cent in FY2024. If these values are taken into consideration, then using the aforesaid coefficients, it can be forecasted that the tax revenue collection in FY2024 will increase by 13.5 per cent. As previous experience shows, growth targets of revenue mobilisation for a particular fiscal year are set considering the revised budget figures of the previous fiscal year. However, if the actual collection of the previous fiscal year is taken into account, then the growth targets for the following year become much higher. This ultimately contributes towards a considerable amount of revenue shortfall. If the potential shortfall in tax

---

more updated data for up to April FY2023. According to this, the ADP implementation rate during July-April FY2023 was 46.7 per cent – the second lowest in the last decade.

[5] The MoF data does not show how much money was borrowed from the Bangladesh Bank. However, according to Bangladesh Bank statistics, the government's net borrowing from the central bank during the July-February period of FY2023 stood at Tk. 54,501.2 crore. The corresponding figure for FY2022 was negative Tk. (-) 11,130.5 crore.

[6] Using data from Bangladesh Economic Review, the model considered the FY1993-FY2020 period.

revenue is considered, the likely target will be expected to generate around 37-40 per cent growth. This implies that a natural course of action will not work for the government, particularly with respect to the NBR. Hence, it can be unambiguously stated that, without new sources, the revenue shortfall will remain very high and will constrain the fiscal space significantly. As has been reported in the media, the government is planning to, inter alia, raise taxes on cigarettes, introduce some form of a carbon tax, impose a minimum tax on individuals who will file tax returns even if they do not have taxable income, increase capital gains tax, impose VAT on mobile phone at the manufacturing stage etc. More potential sources of revenue collection, such as property tax, inheritance tax, and taxes on digital economic activities, can be explored[7], not to mention going for better enforcement to deal with tax avoidance and corruption in the system.

***Strategising rationalisation (gradual withdrawal) of tax exemption provisions will need to be objective*.**

CPD has long been urging the need for rationalisation of tax exemptions which have become rampant over recent years. As part of IMF conditionalities, reduction of exemptions in the areas of income tax, VAT, and customs will have to be carried out. The extent and sequencing of the withdrawals will be key in balancing the needs of meeting the conditionalities and supporting domestic industries. There are many debates that inform the discourse concerning the provision of tax exemptions. In an ideal situation, all types of tax exemptions should respond to well-defined and clearly articulated policy objectives. However, in reality, this is often not the case. In some instances, certain exemptions benefit only the target groups instead of the whole society. In some cases, the exemptions may have been beneficial at the time of their introduction but, over time, lost their relevance in the wake of declining social returns. Many tax exemptions are introduced to appease various interest groups rather than to meet actual needs. This results in significant efficiency loss. In Bangladesh, many exemptions are not time-bound, and those that have time limits keep getting extended. Thus, a medium-term plan and timeline to phase out the various tax exemptions have emerged as an exigency. The next budget should lay out an action plan to this end. Some fundamental questions ought to inform this phasing-out process: whether new or existing sectors should be prioritised; whether export-oriented or domestic market-oriented industries should be prioritised. Whether households or businesses should be prioritised? The policy related to the rationalisation of tax exemption provisions should not be left to the vested interest groups and should prioritise small and medium businesses and general people.

***The guiding principles behind the austerity measures should be clear*.**

The government has already taken some austerity measures, which include expenditure cuts across the sectors and not undertaking new expenditures. In the FY2023 ADP, projects were divided into A, B, and C categories based on priority to ensure proper utilisation of limited resources. The A-category projects were planned to be implemented as usual, while up to 75 per cent of the allocation for the B-category projects could be spent. All C-category projects were put on hold. However, some of these restrictions were relaxed later. Whether the proposed categorisation was followed in view of the austerity measures remains a question. An account of cost savings owing to the categorisation of ADP projects and subsequent implementation can be provided in the FY2024 budget to bring some clarity. CPD, in December 2022, urged the government to prioritise the implementation of all foreign-funded projects in view of the foreign currency crisis. At the same time, projects which are closer to completion also needed to be

[7] See Bhattacharya (2023) and Rahman (2023) to this end.

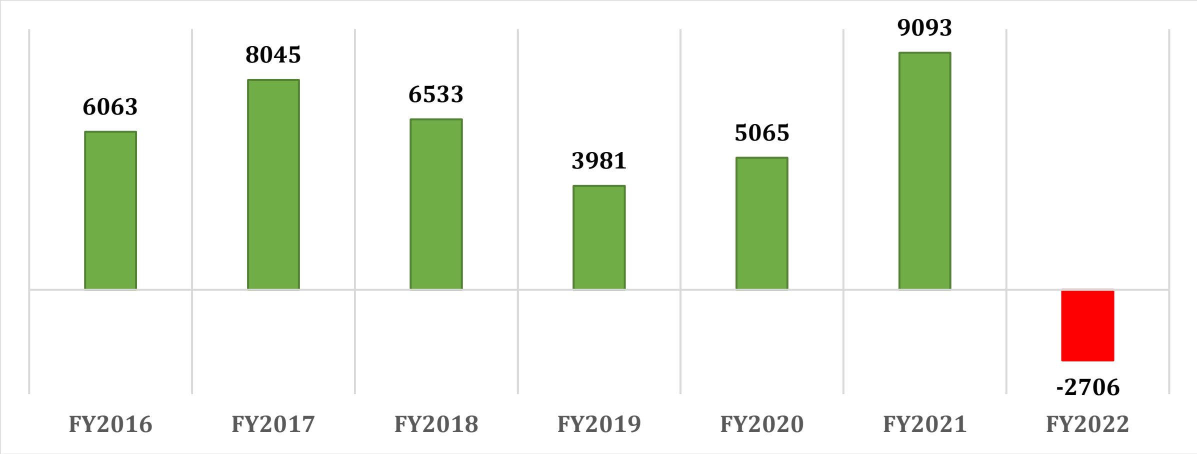
prioritised (CPD, 2022). An incentive mechanism, following a carrot-and-stick principle, could be introduced to facilitate the timely implementation of ADP projects. It needs to be ensured that project costs are not abnormally inflated, citing the devaluation of the BDT as a reason. Finally, the austerity measures should be taken in a way that the impact on the social safety net, health and education sectors, agriculture, and small and medium enterprises (SMEs) is less onerous.

Prioritisation, pacing, and consideration of distributional impacts will be key in case of subsidy management.

Adequate subsidies in the agricultural sector, particularly for fertilisers and pesticides, will need to be ensured. As the international commodity prices have come down, budgetary allocation for agriculture and food should be lower than the ongoing fiscal year; and hence, should not be a major concern. Indeed, a review of the agricultural subsidies will be necessary to see if such incentives can be extended beyond foodgrains and to other promising rising areas of agriculture, particularly in view of the ongoing commercialisation of agriculture. Food subsidy, if required, may be increased to expand public food distribution in the backdrop of high prices of essentials which should be directed towards the disadvantaged population groups in need. The current provisions of the fiscal incentives towards exports and remittances should be maintained to start with. However, exit plans will need to be formulated in both cases. For example, if the exchange rate is made market-based, the resultant depreciation should cover the fiscal incentives provided now. This is also true for export subsidies. While allocating the budget, the possible impact of a future depreciation of BDT needs to be taken into cognisance.

The most critical policy decisions in the areas of subsidy will need to be in the energy and power sectors. If the periodic formula-based price adjustment mechanism for petroleum products is adopted as per IMF suggestion, then no subsidy will be required for Bangladesh Petroleum Corporation (BPC). To this end, there is a need to review the tariff and tax structure. An institutional audit of BPC should be carried out to ensure transparency and accountability. Currently, of the retail selling prices of diesel (Tk. 109/litre) and octane (Tk. 130/litre), the government collects about 17-18 per cent as customs duty, VAT, advance income tax and advance tax. According to media reports, the government is considering the withdrawal of advance tax (5 per cent). However, this may not have an impact on the retail price as paid advance tax at the import stage is adjusted with the VAT collected at the domestic stage. According to CPD's estimation based on available information, BPC is likely to make profits to the tune of about Tk. 5 per litre from selling a litre of diesel and about Tk. 13 per litre from selling a litre of octane. So, there may be an opportunity to reduce petroleum prices between Tk. 5-10/litre. It is to be noted that the windfall gain made by the BPC comes at the price of consumers' reduction in purchasing power. Indeed, BPC's total profit in the last seven years (FY2016-2022) was about Tk. 43,804 crore (Figure 2.1). After paying Tk. 7,727 crore as income tax to the government, the total net profit of BPC over the said period (FY2016-2022) was Tk. 36,074 crore. Being a monopoly in the sector and as it is a state-own enterprise, penalising the citizens of the country cannot be justified. As the government may opt for a periodic formula-based price adjustment mechanism for petroleum products, the pricing mechanism, tax policy, and profits should be analysed publicly, objectively and transparently. Indeed, the government is also collecting additional revenues from the windfall gains of BPC as VAT and income tax. The windfall gains of a (state-owned) monopoly should not be considered as 'value-added' on which VAT is to be imposed. Also, income tax is collected from the profit originating from the windfall gains of BPC. Indeed, with reduced prices of petroleum products, the demand for subsidies for the power sector will also decline.

Figure 2.1: Net profit of BPC after tax in the last seven years (crore Tk.)



Source: Audit Reports of BPC.

The subsidy on power cannot be phased out overnight, given the inflationary effect of the power price rise[8]. Power sector subsidies should be rationalised not only by the upward revisions of electricity prices but also reducing the burden of capacity payments provided to IPPs and quick rentals. At the same time, the energy mix for power production and the associated deals in the power and energy sector will have to be scrutinised further. There must be a pathway to phase out of the costly quick rental power plants. The next national budget for FY2024 should refrain from making budgetary allocations for subsidies (or loans) to other state-owned enterprises.

A rethinking regarding the classification of social safety net programmes (SSNPs) is necessary if their expansion, both in terms of coverage and rates, is to be carried out in a transparent and meaningful way.

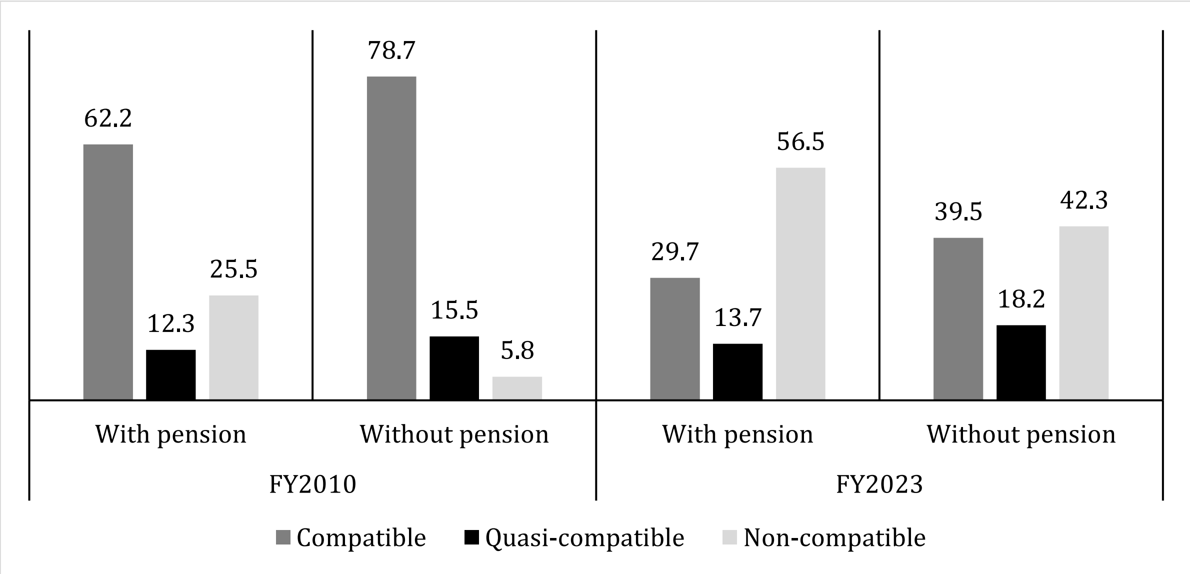
Valid concerns remain regarding the transparency of SSNP implementation. Publicly available data only shows targeted coverage and allocation but never the actual implementation figures, which hinders comprehensive evaluation and understanding of their impact. One matter of contention is the inclusion of loosely related programmes that inflate the total number of SSNPs and the concerned budgetary allocations. While it can be argued that fringe elements need to be included to make a comprehensive list, the inclusion of completely unrelated programmes (e.g., pension for retired government officials, agriculture subsidies, various credit programmes, infrastructure projects etc.) raises questions as to whether the intention was to inflate the statistics in the first place.

In this context, CPD has classified the different SSNPs for FY2010 and FY2023 into three categories viz. compatible (i.e., the SSNPs that should naturally be included in the aggregate list), quasi-compatible (i.e., those that fall somewhere in the 'grey' area), and non-compatible (i.e., those that should be excluded from the SSNP list). In FY2010, the number of compatible, quasi-compatible, and non-compatible SSNPs was 40, 17 and 10, respectively. The corresponding numbers for FY2023 increased to 57, 29 and 29, respectively. As can be seen from Figure 2.2, compatible SSNPs constituted 62.2 per cent of the total SSNP budget in FY2010, whereas the corresponding share was 29.7 per cent in FY2023. In contrast, the share of non-compatible programmes in the total SSNP budget increased from 25.5 per cent in FY2010 to 56.5 per cent in FY2023. If pension for retired government employees is not considered, then the situation

[8] As reported in the media, the removal of subsidies from the power sector will result in a 65 per cent increase in retail electricity price (Sharebiz, 2023).

becomes even worse – the share of non-compatible programmes rising from 5.8 per cent in FY2010 to 42.3 per cent in FY2023. Indeed, the allocation for the compatible SSNPs as per cent of GDP declined from 1.6 per cent of GDP in FY2010 to 0.8 per cent of GDP in FY2023. As a share of the total national budget, this declined from 9.5 per cent in FY2010 to 5.0 per cent in FY2023.

Figure 2.2: Composition of SSNP budget (in per cent)



Source: Author's calculation from MoF data.

Within the non-compatible programmes, a change of composition can also be observed. In FY2010, the non-compatible SSNPs mostly consisted of disaster management, construction, pension, and agriculture-centric programmes. On top of such programmes, the SSNP budget of FY2023 included several non-compatible programmes which are related to credit support and COVID-19 recovery, which are expected to be mostly discontinued in the budget for FY2024. CPD recommends that the incremental SSNP budget be made for the compatible programmes in FY2024 that directly benefit the disadvantaged population groups.

***If the government continues to borrow from the central bank, it will further deteriorate the macroeconomic discipline*.**

It can be argued that the government can run a perpetual budget deficit, paying interest accrued on the growing debt load simply by issuing new debt. However, this is far from reality, as the government is bound by a number of constraints (Hamilton and Flavin, 1986). Both governments and central banks face structural constraints that limit their financing possibilities; going beyond a certain limit may result in explosive debt growth or serious inflationary problems (Leone, 1991). A cross-country literature survey reveals that country practices vary when it comes to limiting the central bank's credit to the government. A universal golden rule or limit is perhaps elusive. However, many countries have put legislative limits to this end. Most countries cap credit, overdrafts, or advances to less than 10 per cent or, at best 20 per cent of the government revenue in the previous fiscal year. Alternative relative measures are also applied by a few countries to limit government borrowing from the central bank, for instance, 5 per cent of government expenditure in Costa Rica or 12 per cent of the monetary base in Argentina (Jácome et al., 2012). As of February 2023, the government's borrowing from the central bank stood at Tk. 54,501 crore (Bangladesh Bank, 2023). If media reports are taken into consideration, then this figure reached as high as Tk. 74,393 crore in April 2023 (Newage, 2023; The Business Standard. 2023). A comparison between the aforementioned thresholds and the actual government borrowing from the Bangladesh Bank is presented in Table 2.1. The government's borrowing from the central bank surpassed all the thresholds for each criterion by a considerable margin. Indeed, it is apprehended that during the last quarter of the fiscal year, government borrowing will increase further (as it happens every year) as the demand for financing the budget deficit tends to rise. With limited funding available from other sources (i.e., foreign borrowing, non-bank borrowing and borrowing from commercial banks), the government will continue to borrow from the central bank if no discipline is applied. Curiously, the central bank has not made any clear policy stance to this end. Given that borrowing from the central bank is high-powered money, it has an inflationary impact on the economy. Applying the money multiplier (5.15 as of March 2023), the borrowing from the central bank so far (as of April 2023) may have created about gross new money to the tune of Tk. 383,124 crore. Thanks to net sales of foreign exchange (resulting in a decline in foreign exchange reserve), the net foreign assets declined, which helped to keep the broad money growth in check. However, the central bank is no longer in a position to continue such release of foreign exchange reserves. Indeed, the government will need to build up foreign exchange reserves in the coming months, including throughout FY2024, which will release more money in the market. At the same time, in FY2024, there is an apprehension that borrowing from the central bank to finance the budget deficit may continue, particularly if the interest rates remain administrative. Hence, continuing borrowing from the central bank will surely create a higher flow of money supply and hence, create inflationary pressure. This inflationary impact, in turn, may deteriorate the balance of payments scenario by creating more aggregate demand. It will also be critical for the government to mobilise the foreign-funded budgetary support under negotiation with several multilateral funding agencies.

Table 2.1: Government borrowing from Bangladesh Bank (thresholds vs actual)

Threshold criteria	Threshold values for Bangladesh	Govt. borrowing from Bangladesh Bank		Overshoot	
		As of Feb 2023	As of Apr 2023	As of Feb 2023	As of Apr 2023
	In crore Tk.			*In per cent*	
10 per cent of total revenue in the previous fiscal year	33,437	54,501	74,393	63.0	122.5
20 per cent of total revenue in the previous fiscal year	66,874	54,501	74,393	(-)18.5	11.2
5 per cent of public expenditure	25,910[a]	54,501	74,393	110.4	187.1
12 per cent of the monetary base	41,263[b]	54,501	74,393	32.1	80.3

Source: Author's calculation based on MoF and Bangladesh Bank data.
Note: a: FY2022 value, b: As of March 2023.

References

Bangladesh Bank. (2023). *Monthly Report on Government Domestic Borrowing (February, 2023)*. Dhaka: Bangladesh Bank.

Bhattacharya, D. (2023). *State and Scope of Property Taxation in Bangladesh* [PowerPoint slides]. Available at: https://cpd.org.bd/resources/2023/05/Presentation-on-State-and-Scope-of-Property-Taxation-in-Bangladesh.pdf

CPD. (2022). *Managing the Economic Crisis: CPD's Policy Recommendations* [PowerPoint slides]. Available at: https://cpd.org.bd/resources/2022/12/Managing-the-Economic-Crisis_CPDs-Policy-Recommendations.pdf Dhaka: Centre for Policy Dialogue (CPD).

CPD. (2023). *CPD's Recommendations for the National Budget FY2023-24: Weathering the Storm, Containing the Risks*. Dhaka: Centre for Policy Dialogue (CPD).

Hamilton, J. D., & Flavin, M. A. (1986). On the Limitations of Government Borrowing: A Framework for Empirical Testing. *The American Economic Review*, *76*(4), 808–819.

IMF. (2023). *Bangladesh Requests for an Extended Arrangement under the Extended Fund Facility, an Arrangement under the Extended Credit Facility, and an Arrangement under the Resilience and Sustainability Facility*. Washington, D.C.: International Monetary Fund (IMF).

Jácome, L. I., Matamoros-Indorf, M., Sharma, M., & Townsend, S. (2012). Central Bank Credit to the Government: What Can We Learn from International Practices? (IMF Working Paper 12/16). Washington, D.C: International Monetary Fund (IMF).

Leone, A. (1991). Effectiveness and Implications of Limits on Central Bank Credit to the Government. In P. Downes & R. Vaez-Zadeh (Eds.), *The Evolving Role of Central Banks* (pp. 363-413). Washington, D.C: International Monetary Fund (IMF).

Newage. (2023, 18 May). Govt borrows from banks Tk 82,056cr in July-April. Available at: https://www.newagebd.net/article/201997/govt-borrows-from-banks-tk-82056cr-in-july-april

Rahman, M. (2023). *Taxing the Digital Economy: Trade-offs and Opportunities* [PowerPoint slides]. Available at: https://cpd.org.bd/resources/2023/04/Presentation-on-Taxing-the-Digital-Economy-Trade-offs-and-Opportunities.pdf

Sharebiz. (2023, 21 May). ভর্তুকি তুলে দিলে বিদ্যুতের দাম বাড়াতে হবে ৬৫%. Available at: https://sharebiz.net/%E0%A6%AD%E0%A6%B0%E0%A7%8D%E0%A6%A4%E0%A7%81%E0%A6%95%E0%A6%BF-%E0%A6%A4%E0%A7%81%E0%A6%B2%E0%A7%87-%E0%A6%A6%E0%A6%BF%E0%A6%B2%E0%A7%87-%E0%A6%AC%E0%A6%BF%E0%A6%A6%E0%A7%8D%E0%A6%AF%E0%A7%81-2/

The Business Standard (2023, 15 May). April saw highest Tk29,697cr govt borrowing from banks in FY23. Available at: https://www.tbsnews.net/economy/banking/april-saw-highest-tk29697cr-govt-borrowing-banks-fy23-632434

SECTION 3. TAMING INFLATION: HARD CHOICES TO BE MADE

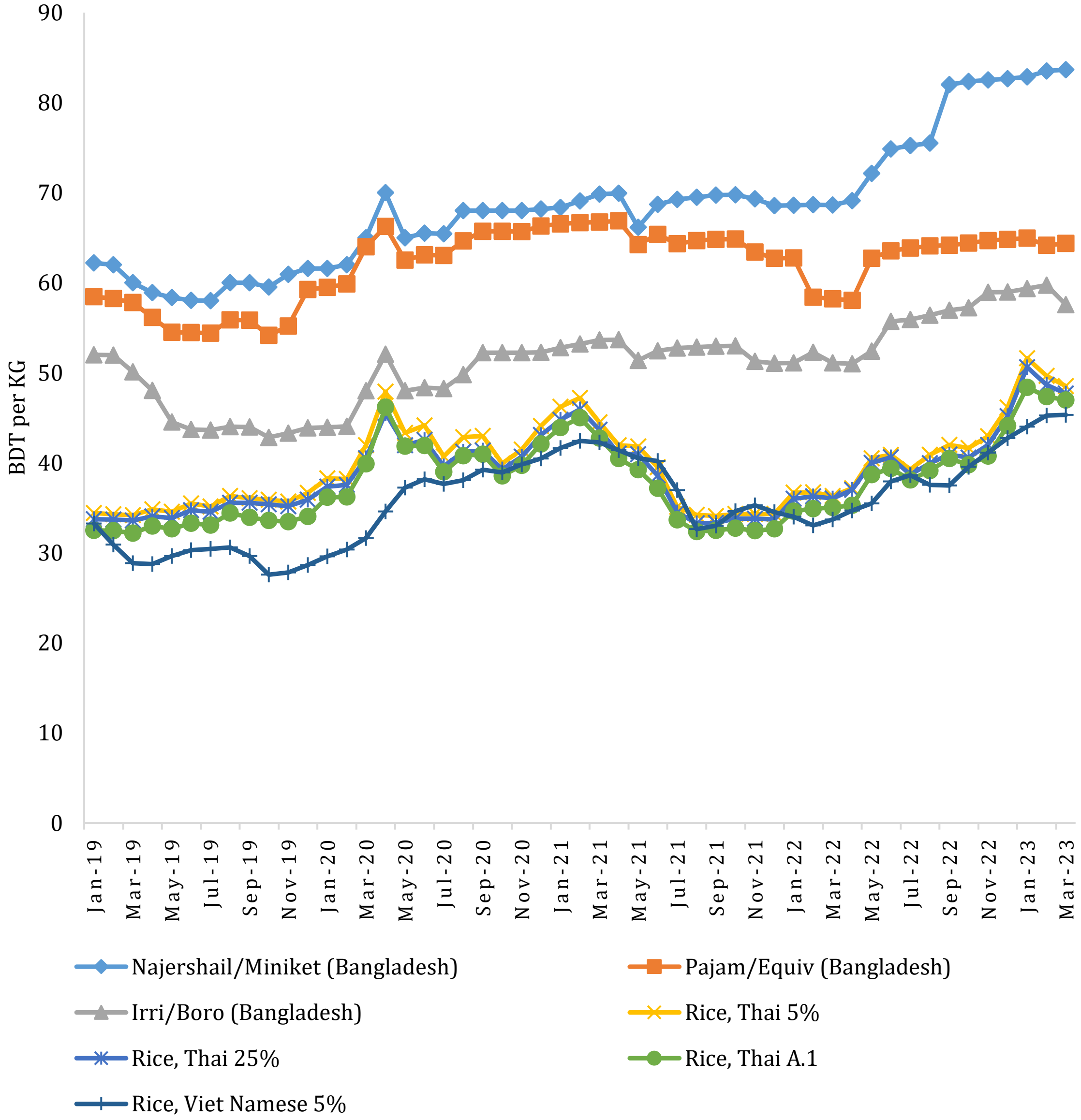
The persistent inflation crisis remains a major pressure point as far as managing the Bangladesh economy in the current context. This is evident through surge in prices observed since June 2020, following the onset of the pandemic. Despite minor fluctuations, high inflation has persisted the recent time. According to the Bangladesh Bureau of Statistics (BBS) inflation has soared to 9.24 per cent in April 2023, surpassing the government's projected rate of 5.6 per cent for FY2023, as stated in the Budget Speech and Bangladesh Bank's 7.5 per cent as projected in central bank's Monetary Policy Statement for January – June 2023. As the surging inflation continues to be a significant pain-point for Bangladesh economy, identifying the sources of inflation is crucial for prudent policymaking.

High prices are not fully an external phenomenon

The policymakers are attributing high prices to exogenous factors since Bangladesh relies on imports of fuel and a number of other essential commodities. However, the increased global prices of these items, coupled with the rising costs of transportation and logistics due to global inflation, also have an impact on locally produced goods. Also, this pass-through effect is only observed during price increases, while the consumers are not able to reap the benefits when the global prices experience a decline. Importers argue that their current stocks were purchased at higher prices, preventing them from immediately lowering prices in response to a drop in global prices. They can only sell products at a lower price once their old stocks are cleared, and new stocks are imported at the new and lower prices. If this argument is logical, then the reverse should also hold – when commodities are imported at cheaper prices, these should also be sold at lower prices till old stocks are depleted, even if there is a price hike in the international market. As a general rule, this is not the case. When international prices rise, importers immediately raise prices, even for their old stock. Currently, importers are attributing the increased cost of imported goods to the expensive USD compared to the BDT. Lack of competitive environment, market syndication, absence of necessary monitoring and lax enforcement of existing laws by concerned institutions are key factors in this connection. This is related to the presence of an imperfect market mechanism, where market rules fail to operate optimally, has contributed to this inflationary trend. The government attempts to periodically reduce duties on particular commodities, but traders argue that this does not help narrow the gap caused by the sharp depreciation of the Taka in recent months.

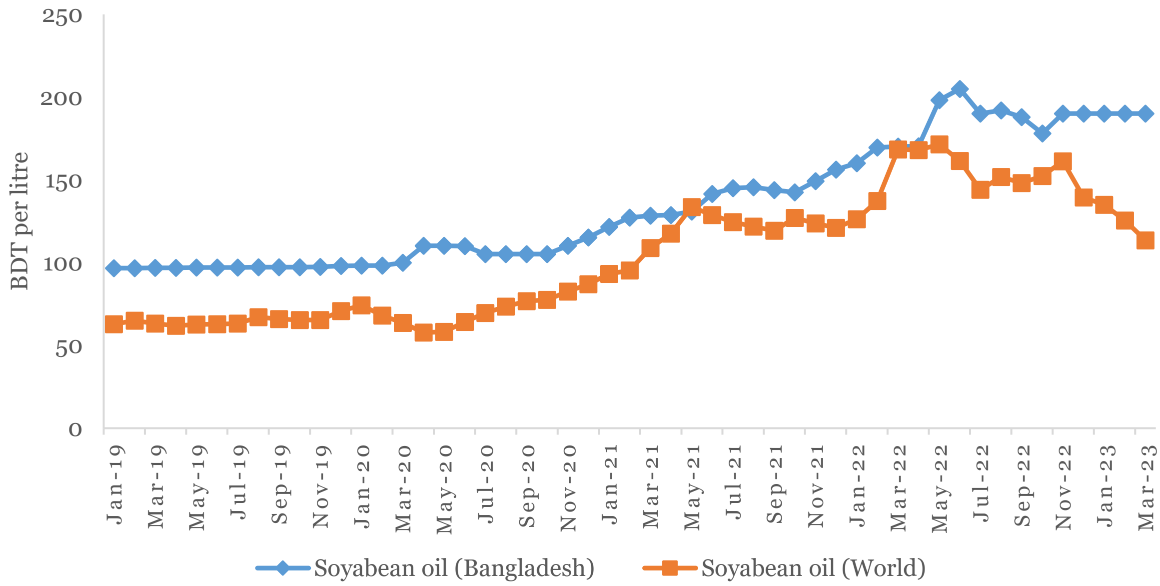
To better understand the situation, price differences between local and international markets of a few commodities such as rice, soybean oil, sugar and beef have been mentioned below. An international comparative analysis reveals that the prices for basic food products in Bangladesh exhibit no decline, despite a decrease in international prices. Furthermore, the data indicates that certain essential food items show a persistent tendency to exceed global prices. Among these four commodities, rice and beef are primarily domestically produced, while soybean oil and sugar are predominantly imported. However, it has been observed that the cost of all these commodities in Bangladesh remains high compared to the global market prices. The price of three common types of rice have been consistently higher than price of both Thai and Vietnamese rice (Figure 3.1). The price of soyabean oil has been falling in the international market from November 2022 to March 2023, whereas there has been no decrease in the price of soyabean oil in the local market during the same period (Figure 3.2). The price of sugar in March 2023 was BDT 124 per kilogramme (kg) in Bangladesh, but only BDT 85 per kg in the US market, BDT 46 per kg in the world market, and BDT 36 per kg in EU market. Even if we consider transport costs, import tariffs, and other trade-related expenses, the differences in prices appear to be high (Figure 3.3). The international price of beef decreased from July 2022 to December 2022, whereas the price of the item in Bangladesh increased during the same time. As of March 2023, the price of beef per kg in Bangladesh was BDT 180 higher than the price of beef per kg in the world market (Figure 3.4).

Figure 3.1: Price of rice in Bangladesh and international markets (in BDT per kg)



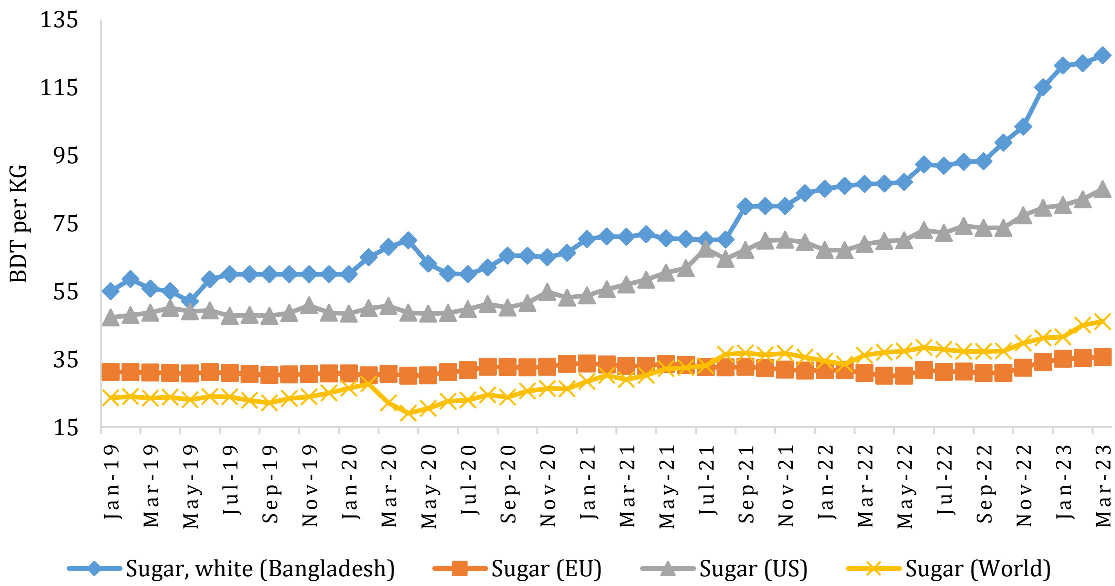
Source: Author's illustration based on data from Bangladesh Bureau of Statistics (BBS 2023) and World Bank (World Bank 2023).

Figure 3.2: Price of soyabean oil in Bangladesh and international markets (in BDT per litre)



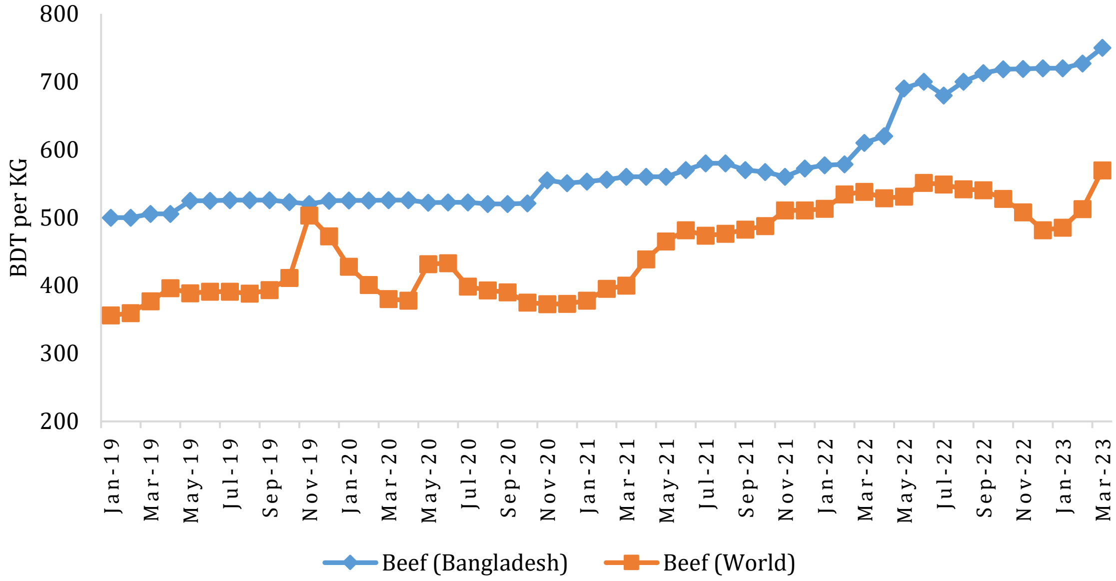
Source: Author's illustration based on data from Bangladesh Bureau of Statistics (BBS 2023) and World Bank (World Bank 2023).

Figure 3.3: Price of sugar in Bangladesh and international markets (in BDT per kg)



Source: Author's illustration based on data from Bangladesh Bureau of Statistics (BBS 2023) and World Bank (World Bank 2023).

Figure 3.4: Price of beef in Bangladesh and international markets (in BDT per KG)



Source: Author's illustration based on data from Bangladesh Bureau of Statistics (BBS 2023) and World Bank (World Bank 2023).

Policy measures are inadequate to tame inflation as the real reason for price hike is not recognised by policymakers.

The notion that global prices rather than domestic factors have raised domestic inflation has influenced the policy measures taken by the government. Hence, domestic policy interventions to rein in inflation had hardly worked till now. A few policy shortcomings are highlighted here.

First, various policy tools deployed by the policymakers have failed to attain their objectives. This is observed in many cases. The most obvious case is the issue of interest rate which has been fixed by the Bangladesh Bank. In order to curb the current inflation, various central banks worldwide have made use of interest rates as a means to regulate credit expansion and contain consumer demand. This approach has yielded positive outcomes not only in advanced countries like the USA and countries within the European Union (EU), but also in developing countries such as India, where interest rates were raised. The lending rate is fixed at 9 per cent since April 2020. This makes the borrowing rate cheaper as inflation rate is higher than lending rate. Recently, the central bank has raised the interest rate on consumer loans from 9 per cent to 12 per cent. However, it is noteworthy that the interest rate cap on other types of loans, has remained unchanged at 9 per cent. Regrettably, policymakers face persistent opposition from entrepreneurs whenever interest rates are proposed to be increased. Their resistance is further bolstered by recent surge in production costs resulting from higher energy prices, which they argue would undermine their competitiveness. However, competitiveness is contingent upon multiple factors, including the business environment, efficacy of institutions and the state of overall good governance. These elements are crucial for enhancing productivity and efficiency of the private sector, initiating level playing field, creating competitive environment and in the end facilitating cost reductions. By addressing these concerns, the remaining issues can be resolved. Unfortunately, economic decisions in Bangladesh are frequently influenced by non-economic factors. A lack of significant monetary policy shift has led to an ineffective attempt to curb inflation in Bangladesh. The Bangladesh Bank raised its key interest rate - the repurchase agreement (repo) in May 2022 from 4.75 to 5 and then gradually to 5.5, 5.75 and 6 at various points in time till March 2023 - to contain price pressures. However, this did not generate the expected impact in terms of reduced inflationary pressure (Table 3.1).

Table 3.1: Repo, reverse repo, and call money lending/borrowing rate

Period	Repo	Reverse Repo	Weighted average monthly call money lending/borrowing rate
Jan-22	4.75	4	2.43
Feb-22	4.75	4	2.8
Mar-22	4.75	4	2.66
Apr-22	4.75	4	4.58
May-22	5	4	4.73
Jun-22	5.5	4	4.88
Jul-22	5.5	4	5.34
Aug-22	5.5	4	5.49
Sep-22	5.5	4	5.53
Oct-22	5.75	4	5.79
Nov-22	5.75	4	5.80
Dec-22	5.75	4	5.8
Jan-23	6	4.25	6.66
Feb-23	6	4.25	6.15
Mar-23	6	4.25	6.03

Source: CPD compilation based on data from Bangladesh Bank (Bangladesh Bank, 2023).

Second, several imported items face high duties and taxes. The NBR relies on indirect taxes for meeting its target of revenue collection. There was hardly any attempt to reduce these duties and taxes albeit for a limited period (Table 3.2).

Table 3.2: Import tariff on essential food items

	HS Code	Description	Unit	TTI
1	2012090	Fresh Or Chilled,Other Cuts Of Bovine Meat With Bone In, Nes	KGM	58.60
2	2012010	Fresh Or Chilled,Other Cuts Of Bovine Meat With Bone In, Wrapped/Canned upto 2.5 kg	KGM	89.32
3	2042290	Fresh Or Chilled Other Cuts Of Meat Of Sheep,With Bone In, Nes	KGM	58.60
4	2071410	Frozen Cuts And Offal Of Chicken, Wrapped/Canned upto 2.5 kg	KGM	89.32
5	3021990	Fish...ruhi,katla,......,pangash, karp & alike, excl. wrapped/canned upto 2.5kg Other	KGM	58.60
6	3028919	Hilsha fish (EXCL.wrapped/canned upto 2.5 kg)	KGM	89.32
7	4012010	Milk & Cream Of>1%But<=6%Fat,Not Concentrated Or Sweetened,Wrap./Cann. upto 2.5 kg	KGM	58.60
8	4021010	Milk&Cream In Powder Forms<=1.5%Fat,Con... Or Sweet.,In Reta.Pk.Upto 2.5kg	KGM	89.32
9	4021091	MILK AND CREAM IN SOLID FORMS OF =<1.5% FAT IMPORTED BY VAT REG. MILK AND MILK PRODUC	KGM	37.00
10	4021099	MILK AND CREAM IN POWDER EXCL. POWDER, GRNULES OR OTHER SOLID FROM AND IMPORTED VAT REGG	KGM	37.00
11	7020019	Tomatoes, Fresh, Nes	KGM	58.60
12	7031019	Onions, Fresh Or Chilled, Nes	KGM	10.00
13	7032090	Garlic, Fresh Or Chilled, Nes	KGM	7.00

	HS Code	Description	Unit	TTI
14	8041019	Dates, Fresh, Nes	KGM	10.00
15	9041190	Pepper, Neither Crushed Nor Ground, Nes	KGM	58.60
16	9083190	Cardamoms :Neither Crushed or ground. EXCL. Wrapped/canned upto 2.5 Kg	KGM	58.60
17	9093190	Seeds of Cumin : Neither crushed or ground EXCL. Wrapped/canned upto 2.5 Kg	KGM	58.60
18	9101190	Ginger : Neither Crushed or ground EXCL. Wrapped/canned upto 2.5 Kg	KGM	10.00
19	9103090	Turmeric(Curcuma), Nes	KGM	10.00
20	10059090	Other Maize, Excluding wrapped/canned upto 2.5 kg	KGM	2.00
21	10062000	Husked (Brown) Rice	KGM	62.50
22	10063011	Semi-Milled Or Wholly Milled Rice	KGM	85.00
23	11081200	Maize (Corn) Starch	KGM	67.00
24	15111010	Crude palm oil imported by VAT registered edible oil refinery industries	KGM	32.00
25	15119090	Palm Oil(Excl.Cude)&Its Fractns....Nes.Incld.Refiend Palm Oil	KGM	20.00
26	15132900	Refined Palm Kernel/Babassu Oil & Fractions,Not Chem.Modifd	KGM	55.00
27	25010020	Salt (other than pure sodium chlo.)...solution ..salt boulder for crushing & salt in bul	KGM	89.32

Source: CPD compilation based on data from National Board of Revenue (NBR) (NBR, 2023).

Third, the ongoing fiscal year has presented substantial challenges for revenue collection due to diminishing business profits, leading to a decline in direct tax contributions. Furthermore, reduced imports have resulted in a decrease in customs tariffs. Another source of government funding is investments in national savings certificates which has declined drastically for several reasons including ceiling on NSD purchase by individuals, and reduction of savings by low-income groups due to increased cost of living. As a result of consistently low levels of domestic resource mobilisation through taxation, the government is increasingly relying on the central bank to obtain additional funds. The increased borrowing of high-powered money has the potential to fuel inflationary pressure. This may have serious macroeconomic implications (please see Section 2 of this report).

Fourth, though an important source of imported inflation in Bangladesh is high fuel prices, the skyrocketing inflation has been further worsened by frequent energy price hikes in the country. From early November 2021 till recent times, various fuel types have witnessed upward adjustments. Even though the global fuel prices are on a downward trend, one does not see this reflection of this low prices in Bangladesh. Given IMF loan equivalent to USD 4.7 billion f the government is under pressure to withdraw all types of subsidies. Consequently, increased costs due to subsidy withdrawal will be passed on to consumers, further burdening their cost of living. Despite profits made by Bangladesh Petroleum Corporation (BPC) during periods of low global energy prices, particularly between FY 2015 and FY 2022, the common people did not reap the benefits. This is because the government controls and determines energy prices in Bangladesh, leaving consumers vulnerable to the decisions of policymakers. In early August 2022, despite the decline in global fuel prices, the government raised prices for various l types of fuel. Ironically, when global energy prices rise, the government adjusts prices accordingly, but consumers do not enjoy the same benefits when global prices decrease because the government does not lower prices in line with global trends. In 2016, energy prices were only slightly reduced despite a significant decline in global prices. Therefore, consumers could not benefit from the profits made by BPC due to lower global prices of fuel in the past. One sees a similarity in the way private sector and the government behave, vis-à-vis the consumers.

Fifth, structural problems are also responsible for the price hike. Lack of strict enforcement of competition laws gives rise to unfair practices. In the absence of a pricing system that is based on transparency and takes strong stance to eliminate the involvement of middlemen in the supply chain, prices cannot be controlled with only monetary and fiscal tools.

Synchronised measures are needed to tackle persistent inflationary pressure.

To mitigate the impact of inflation and provide support to those in need, it is of utmost importance that the government implements a range of measures. These should encompass direct cash support for individuals living in poverty including the new poor, augmenting allowances within social safety net programmes, enforcing stronger social protection measures for low-income families, and introducing tailored stimulus packages to aid small businesses during these challenging times.

It is crucial to establish an integrated policy framework that facilitates the coordination of fiscal and monetary policies, thus ensuring their efficacy. It is also necessary to address non-economic and distortionary practices in the market to bring down prices. This necessitates the implementation of bold and coordinated measures.

The Bangladesh Competition Commission should strengthen its role and take proactive measures. This includes establishing a comprehensive database, conducting regular surveillance of dominant market players' activities, closely scrutinising market manipulation, and promptly taking necessary actions. To effectively address monopolies and promote fair competition, the Competition Act of 2012 needs to be updated with explicit anti-trust provisions and clear penalties for those who violate those. Additionally, rigorous monitoring and supervision are essential for efficient market management, ensuring that commodity prices remain under control.

References

Bangladesh Bank. (2023). *Major Economic Indicators*. Retrieved May 26, 2023, from Bangladesh Bank: https://www.bb.org.bd/en/index.php/publication/publictn/3/11

BBS. (2023). *Price and Wages (CPI, QIIP)*. Retrieved from Bangladesh Bureau of Statistics: http://www.bbs.gov.bd/site/page/29b379ff-7bac-41d9-b321-e41929bab4a1/-

NBR. (2023, May 26). *Duty Calculator*. Retrieved from National Board of Revenue (NBR): http://bangladeshcustoms.gov.bd/trade_info/duty_calculator

US EIA. (2023, May 24). *Petroleum and other liquids*. Retrieved May 26, 2023, from U.S. Energy Information Administration: https://www.eia.gov/dnav/pet/pet_pri_spt_s1_d.htm

World Bank. (2023). *Pink Sheet*. Retrieved from World Bank: https://www.worldbank.org/en/research/commodity-markets

SECTION 4. EXTERNAL SECTOR: MANAGING RISKS, COMBATING HEADWINDS

4.1 The Context: An Unprecedented Scenario

A significant part of the ongoing macroeconomic challenges facing the Bangladesh economy originates in the formidable difficulties facing the external sector of the country and the nature of current trends in the external sector balances which have emerged as a major concern for the policymakers. Accordingly, the likelihood of success of coming out of the current situation also lie, to a large extent, in whether the policymakers are able to manage the attendant risks and tackle the headwinds confronting the country's external economy and external balances. When the increasingly open and globalising economy of Bangladesh came under pressure immediately after the start of the Russia-Ukraine war, the prevailing comfort zone came under pressure. As is known, Bangladesh has been able to maintain strong external sector balances over the recent past years. Even in years of depressed export performance or low remittance growth, external balances tended to remain stable, allowing policymakers considerable policy flexibility and manoeuvrability. Regrettably, Bangladesh's policymakers failed to appreciate the likely consequences of the war – induced external shocks on the economy, and could not adequately anticipate the adverse impacts these could have on the country's overall macroeconomic management.

One sign of the lack of the aforesaid appreciation is that the FY2023 budget was formulated in a *business as usual* manner- the GDP growth was planned at 7.5 per cent, and the inflation target was set at 5.6 per cent; the pressure on import payments, reserves, exchange rate and external sector balances was not forecasted with analytical rigor and the policy acumen that these deserved, even though the tell-tale signs of this was becoming increasingly evident for some time even before the budget was formulated. Thus, the current external sector scenario reflects both the ramifications of the external shocks as also the failure of domestic policymaking at a critically important juncture of Bangladesh's development journey. True, as the fiscal year FY2023 moved on, policymakers were compelled to resort to various fire-fighting measures to contain the adverse impacts that afflicted the economy: the taka was allowed to significantly depreciate since the central bank was no more able to sustain the managed float regime at the prevailing state; imports were selectively curtailed; L/C margins were raised, whilst the central bank supported import of essentials albeit at depreciated but managed exchange rate. Private sector found it difficult to open L/Cs for imports of both consumers' and producers' goods and this disrupted the supply chain of many commodities, leading to supply shortages and fuelling demand-push high prices. Because of high commodity prices, resulting in rising subsidies, policymakers had to raise domestic administered prices of a number of essentials to ease the subsidy pressure. This led to rising prices of many essential items, leading to erosion of purchasing power. Public expenditure had to be curtailed also because domestic resource mobilisation through custom duties and VAT was also under-performing at a time when imports were coming down and lower government expenditure (e.g., in case of ADP implementation) resulted in lower VAT collection.

All these had adverse impact on private sector investment whose share has been stagnating (as a percentage of GDP), led to lower than planned private sector credit uptake and resulted in lower GDP growth projections for FY2023 (at 6.03 per cent compared to the earlier set target of 7.5 per cent for FY2023). The actual inflation turned out to be about 9.0 per cent instead of the projected 5.6 per cent. Thus, the weak external sector performance and the consequent imbalances had a knock-on negative implications for the overall performance of the domestic economy of Bangladesh. In the end, Bangladesh had to resort to IMF programme which came with a number of quantitative milestones and qualitative conditionalities. In short, the impacts of the external shock, weak resilience capacity to deal with shocks, muted policy response and embedded weaknesses and fault lines in the economy created a vicious cycle which underpins the current challenging macroeconomic scenario.

In view of the above, Bangladesh's macroeconomic stability will critically hinge, as was noted, to a large extent, on how successfully the external sector regains its lost stability, to what extent the balance of payments situation improves, how the economy will adjust to the market aligned exchange rate regime (towards a unified market determined rate) and the capacity of economy to arrest the fall in forex reserves. Restoration of external sector stability will help improve macroeconomic management and arrest the dreaded twin trends of falling GDP with high inflation –a precursor of stagflation. A reversal of the current scenario will help restore investor confidence, give relief to consumers and help the economy regain its growth momentum. This is the key challenge facing the policymakers as the budget for FY2024 is presented before the Parliament on June 1, 2023.

The next section examines the current external sector trends in FY2023 and makes an attempt to capture the drivers of the movements of the relevant correlates. The third section comes up with a number of measures to restore external sector stability over the immediate and medium term.

4.2 The Current External Sector Trends: Disquieting and Disturbing

Export sector performance has been rather muted, with adverse implications for net export earnings.

Bangladesh's external sector performance over the first 9-10 months of FY2023 has been lacklustre. Growth of export earnings during July-April, FY2023 was 5.4 per cent compared to the corresponding period of FY2022; this was indeed 3.5 per cent lower than the strategic target for the corresponding period. It is obvious that the strategic growth target for FY2023, set at 11.5 per cent , is not going to be achieved –exports will need to rise by 41.4 per cent in the remaining two months (May and June) of FY2023 over the corresponding period of FY2022 if the strategic export target for FY 2023 (which was set at USD 58.0 billion) was to be attained, an impossible task.

It is to be noted that, if over this period (July-April of FY2023) RMG export earnings were 9.1 per cent higher, the earnings from non-RMG exports were (-) 11.1 per cent lower than the corresponding period of FY2022. The significantly low growth of exports in April at (-) 16.5 per cent, with export of RMG falling by about 16.1 per cent transmits a truly disturbing signal. If the RMG export target of 11.0 per cent is to be attained, exports will have to rise by 19.4 per cent over the next two months (May and June) compared to the corresponding period of FY2022; this is not going to be achieved. Interestingly, analysis of price trends of RMG products in key markets of the US and the EU indicates a rise in average prices: average price of apparels (per dozen) in the US went up by 23.3 per cent in July-March period of FY2023 compared to corresponding period of FY2022 (however, the volume has decreased by 17.6 per cent, indicating a slump in demand). The average price of apparels in the EU also went up by 24.8 per cent (per 100kg) over the same period (with the volume also rising by 9.8 per cent). The significant depreciation of the BDT should have enhanced export competitiveness of apparels (as also other items of exports from

Bangladesh) in the global market. The rising price should also have helped. It is in this backdrop that the slow growth of RMG exports and the recent fall in export earnings from the RMG sector have emerged as a matter of concern. The accumulated risks of lack of export and market diversification are showing up in export performance of recent times.

The negative growth of non-RMG exports has an adverse implication for net exports and the forex reserves. Since domestic value addition for RMG is about 55-60 per cent, whilst that of non-RMG items varies in the range of between 80 and 95 per cent, the compositional aspect of recent export performance has an adverse impact on growth of net domestic value retention, net export and forex reserves. Policymakers should take note of this.

There are signs of improvements in terms of trade, but depressed demand in major markets has emerged as a concern.

If the purchasing power of RMG is taken as a reference point, it is seen that Bangladesh's terms of trade has somewhat improved, both in the EU and in the US markets if measured against most of the commodities, excepting for LNG (Table 4.1 and Table 4.2). This should have a positive impact on trade balance in the BoP. However, as was noted export performance over recent months has been particularly disturbing and the (depressed) demand side impacts have started to be felt in a strong way as FY2023 draws to a close. The significant decline in the quantity of RMG items in the US market is particularly disquieting.

Table 4.1: Terms of Trade taking RMG price per 100kg as reference (EU)

Commodities	Units	FY 22 (July-March) Average	FY 23 (July-March) Average
Cotton, A Index	kg	602.96	745.65
Rice, Thai A.1	mt	4.07	4.05
Wheat, US HRW	mt	4.32	4.46
Palm oil	mt	1.20	1.85
Soybean oil	mt	1.05	1.22
Crude oil, average	bbl	19.38	20.38
Liquefied natural gas, Japan	mmbtu	117.15	88.32

Source: Author's estimation based on The Pink Sheet and Eurostat.

Table 4.2: Terms of Trade taking RMG price per dozen as reference (U.S)

Commodities	Units	FY 22 (July-March) Average	FY 23 (July-March) Average
Cotton, A Index	kg	15.45	21.14
Rice, Thai A.1	mt	0.10	0.11
Wheat, US HRW	mt	0.11	0.13
Palm oil	mt	0.03	0.05
Soybean oil	mt	0.027	0.035
Crude oil, average	bbl	0.50	0.58
Liquefied natural gas, Japan	mmbtu	3.00	2.50

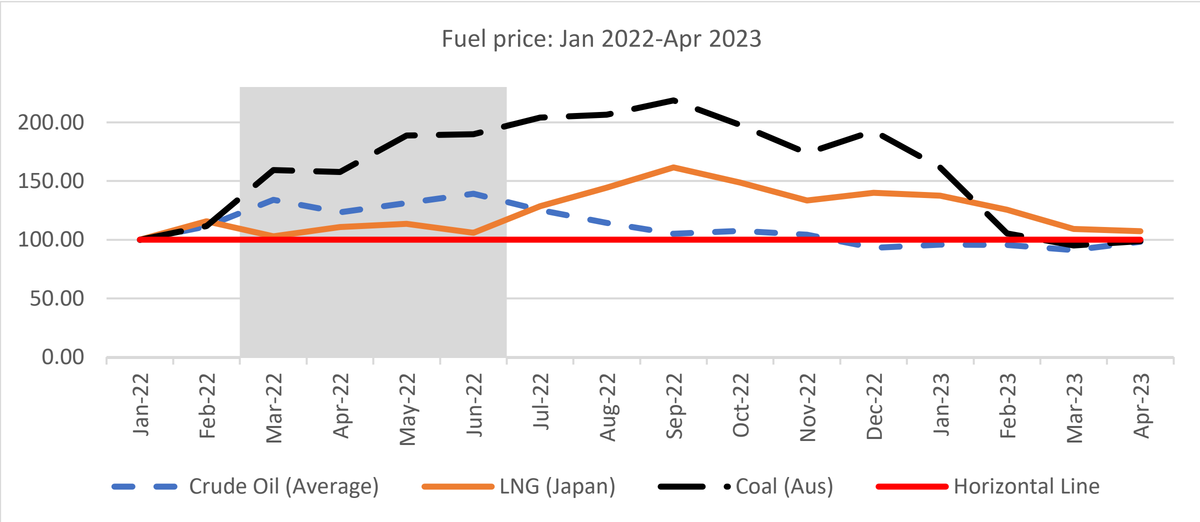
Source: Author's estimation based on The Pink Sheet and USITC.

Import payments have come down both owing to policy interventions and because of falling global commodity prices, but the bill will likely go up if the economy is to regain growth momentum.

Imports during the first nine months (July-March) of FY2023 was more than USD 8.3 billion dollar less than corresponding period of FY2022 i.e. lower by 12.4 per cent (for EPZ this was 19.6 per cent lower compared to the corresponding period of the previous year). In quantitative terms, import payments have declined by about USD 7.6 billion during July-March FY2023 compared to the corresponding period of FY2022 (the matched figures are USD 61.5 billion and USD 53.9 billion). What is to be noted in this connection is that all key components of imports have demonstrated negative trends: intermediate goods (-14.7 per cent); RMG related goods (-19.6 per cent); capital goods (-17.8 per cent) including capital machineries (-11.9 per cent). Demand-side factors (depressed demand, in part because of high prices) may have played a role. However, the policy of selective import restrictions, difficulties in accessing foreign currency to open L/Cs and dampening affect of a significantly depreciated taka have played no less an important role in this backdrop. Supply chain disruption and the adverse impact domestic investment in the end has contributed to the lower GDP growth. If the economy is to regain its growth momentum import payments will go up (IMF projects a 14.2 per cent rise in import in FY2024), creating pressure on trade and current account balance if export and remittance earnings do not rise in tandem.

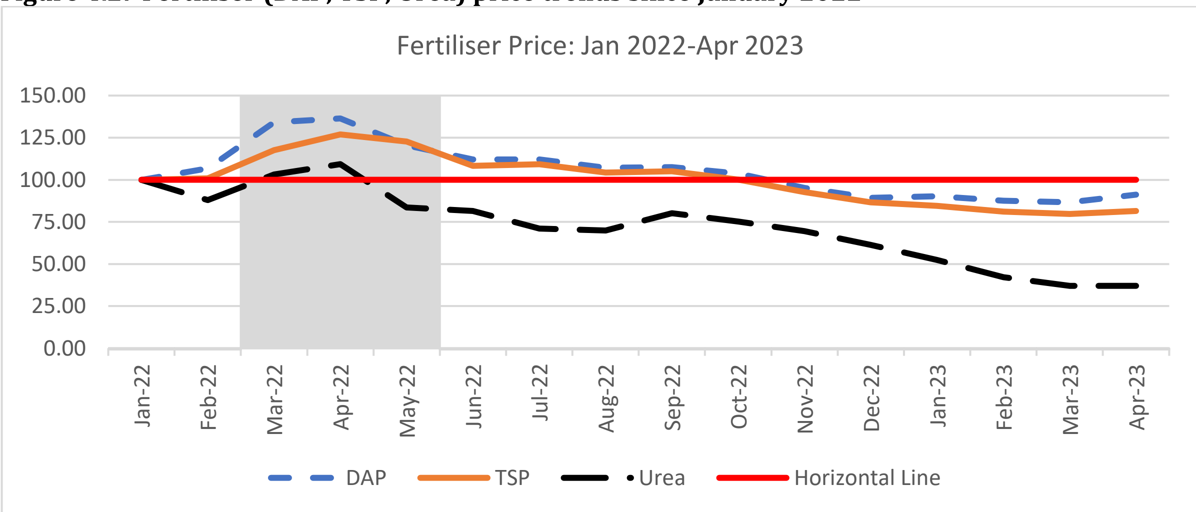
Global Price Trends

Figure 4.1: Fuel (Crude Oil, LNG, Coal) price trends since January 2022



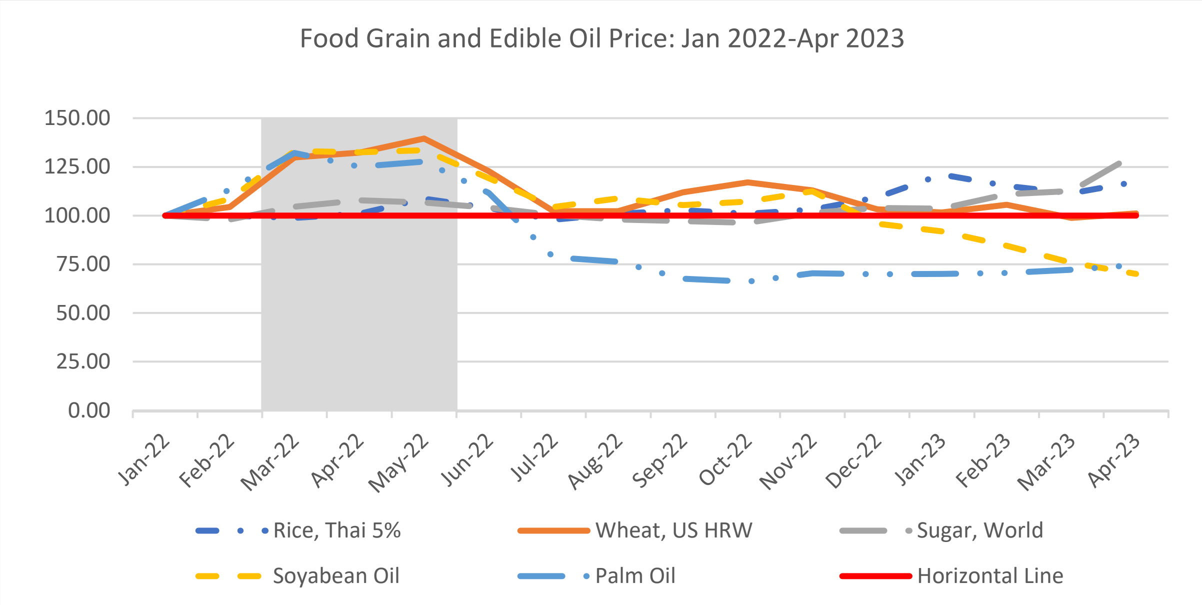
Source: The Pink Sheet, World Bank (May 2023).
Note. Prices in January 2022 or the base price is assumed to be 100 for the ease of comparison.
Shaded region represents the four months starting from start of Russia-Ukraine war in February 2022.

Figure 4.2: Fertiliser (DAP, TSP, Urea) price trends since January 2022



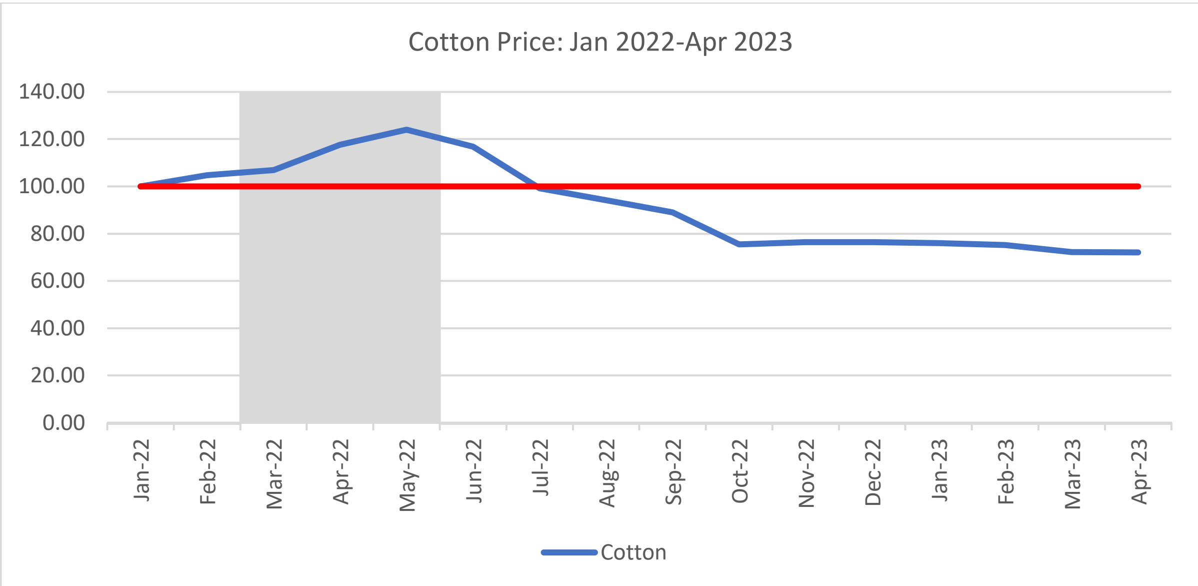
Source: The Pink Sheet, World Bank (May 2023).
Note. Prices in January 2022 or the base price is assumed to be 100 for the ease of comparison.
Shaded region represents the three months starting from start of Russia-Ukraine war in February 2022.

Figure 4.3: Food grains (Rice, Sugar, Wheat) and Edible Oil (Soybean Oil, Palm Oil) price trends since January 2022



Source: The Pink Sheet, World Bank (May 2023).
Note. Prices in January 2022 or the base price is assumed to be 100 for the ease of comparison.
Shaded region represents the three months starting from start of Russia-Ukraine war in February 2022.

Figure 4.4: Cotton price trends since January 2022



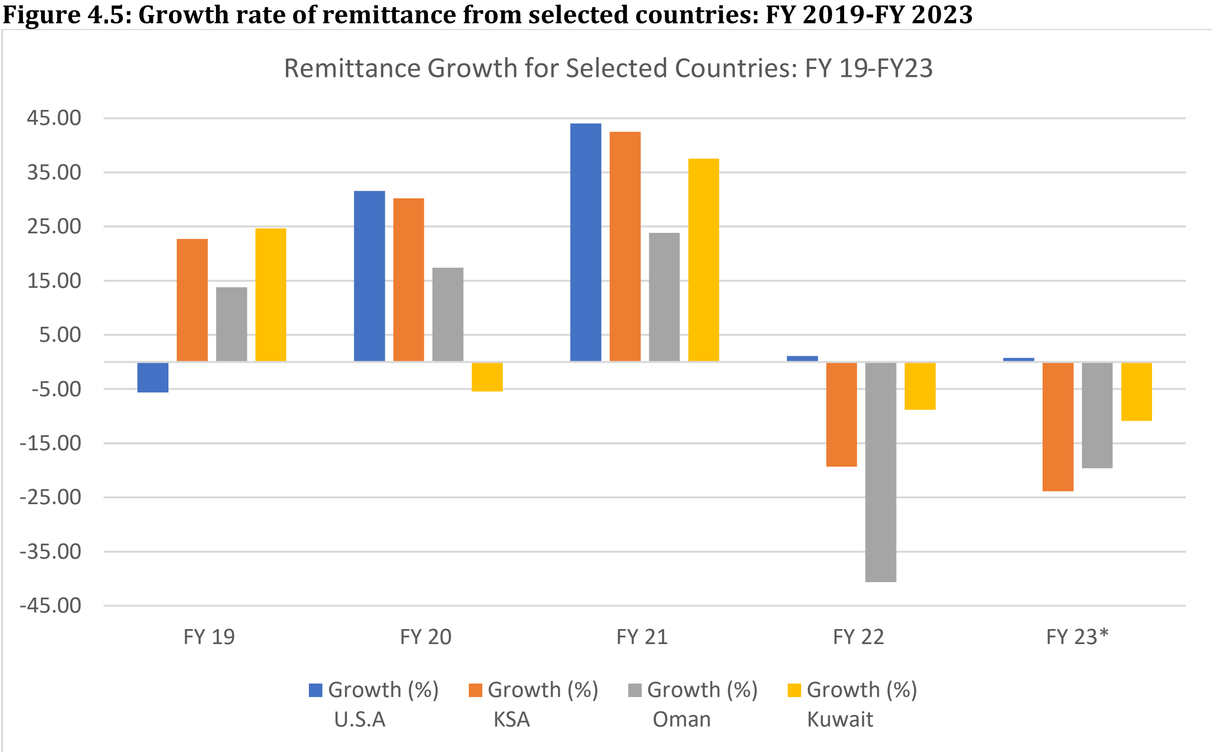
Source: The Pink Sheet, World Bank (May 2023).
Note. Prices in January 2022 or the base price is assumed to be 100 for the ease of comparison.
Shaded region represents the three months starting from start of Russia-Ukraine war in February 2022.

One comforting development is that global commodity prices are showing downward trend from their peak of April-June 2022; at present prices of majority of the commodities are lower than pre- Ukraine-Russia war levels. The only exceptions are the prices of LNG and wheat (Figures 4.1, 4.2, 4.3 and 4.4). Thus, the decline in value terms in import payments does not necessarily reflect a proportionate decrease of imports in quantitative terms, a good sign. However, because of the growing dependence of Bangladesh on LNG imports, the rise in prices of this critically important import item does not augur well for Bangladesh.

The trends in remittance flows do not match the growing number of migrant workers leaving for overseas job markets and consequently the trends in sources of remittance flows raise serious concerns.

One disquieting development of recent times relates to remittance flows. Remittance earnings has risen by only 2.4 per cent during July-April, FY2023 compared to the corresponding period of FY2022. Even in April of this year (a time of traditionally high flow of remittance on occasion of Eid ul Fitre), remittance flow was 16.3 per cent lower in 2023 compared to the corresponding month of 2022. Three factors are to be kept in mind in this context. The number of people going abroad for work during the first 10 months of FY2023 was significantly high at 9.22 lac; majority of these people went to the Gulf countries, but the remittance flows from this region did not match this rising number. Secondly, The USA has replaced Saudi Arabia as the foremost source of remittance in this period. CPD has drawn attention to this new phenomenon in its previous IRBD. In spite of 12.3 lac people going to Saudi Arabia during January 2021- April 2023 (56.9 per cent of the total of 21.5 lac during this period), the remittance from Saudi Arabia has come down from USD 3.86 billion in FY 2022 (July-April) to USD 3.04 billion in FY2023 (July-April) while that from the U.S.A increased from USD 2.87 billion to USD 3.05 billion over the corresponding period. To note, the share of migrant workers travelling to the USA in this period was negligible. Remittance from Oman (USD 628.8 million and USD 849.9 million over the corresponding period of FY 2023 and FY 2022), declined by 26.0 per cent and that from Kuwait (USD 1322.2 million and USD 1384.8 million) declined by 4.5 per cent in spite of 43.9 thousand and 31.5 thousand migrant workers travelling between January 2021 and April 2023 respectively to these two countries.

Figure 4.5: Growth rate of remittance from selected countries: FY 2019-FY 2023



Source: Author's estimation based on Bangladesh Bank (May 2023).
Note. *FY 2023 figures compare growth rate of remittance flows from selected countries for July-April period of the fiscal year.

The overall slow growth of remittance flows and relative decline in remittances from some countries in the Middle-East, as is discernible from Figure 4.5, merits careful investigation. The likelihood of transfer through hundi/hawala as also repatriation of money to take advantage of incentives provided for remittance flows and the scope of whitening of black money taken out of the country illegally via the remittance route should come under proper scrutiny by concerned authorities, and appropriate steps ought to be taken to deal with the emergent scenario.

Trade and Current Account Balances are showing some improvement but Financial Account Balance has emerged as the villain of the piece. Consequently, the fall in reserves has persisted.

The fall in import payments has helped improve the balance of trade significantly, from (-) USD 25.0 billion in FY2022 (July-March) to (-) USD 14.6 billion in FY2023 (July-March). The current account balance has also registered some improvement, from USD (-) 14.3 billion to (-) USD 3.6 billion over the corresponding period, a decline of about USD 10.7 billion. However, the gross reserves have come down from USD 44.1 billion to USD 31.1 billion between FY2022 (March 2022) and FY2023 (March 2023), by about USD 13.0 billion. If this trend continues it will lead to a highly risky situation (not to mention that according to the IMF estimates the net reserves were about USD 24.0 billion).

The villain in the piece as far as forex reserves are concerned appears to be the balance in the Financial account. The major driving force in this regard is the significant deterioration in the balance, from USD (+) 11.9 billion to USD (-) 2.2 billion, a fall of about USD 14.1 billion. If the trend cannot be arrested the pressure on reserves will lead to serious difficulties with import payment, debt servicing and exacerbate macro-economic challenges.

4.3 Suggested Policy Measures

Bring transparency in external sector earnings data and deal with illegal transfers.

Can slowdown in export earnings be explained only by the demand side factors? The IMF has recently raised the question about the mismatch between the amount of what should have been earnings from exports and the earnings that were actually repatriated. The central bank has come up with an explanation in recent times as regards this mismatch, but this need to be looked at more closely. There is also a significant difference between the EPB export earnings figures and Bangladesh Bank figures which has been persisting for a long period. In recent times, the Bangladesh Bank has also unearthed a number of anomalies with regard to under invoicing in exports and both over (for purposes of illicit money transfer) and under invoicing (to avoid customs duties) in case of imports. This needs to be looked into carefully to improve the trade balance and consequently the reserve situation. Why the services export target for FY2023 (at USD 9.0 billion) was set at only 2.2 per cent higher than the previous year also raises a question. It appears that a large part of the earnings from services export remains unaccounted for in the balance of payments record. The concerned authorities should take urgent steps for repatriation of services earnings through formal channel. Introduction of PayPal may be considered in this connection. By all possibility, a large part of remittances is being channelled through the hundi/hawla channels. This must be tackled through demand side and supply side measures including enforcement of current-laws and signing of bilateral treaties with concerned countries.

Take steps to improve Finance Account Balance to Improve Overall Balance and reverse the falling forex reserves trend.

In this backdrop, both the short- and medium-term measures will be required to reverse the situation. Several steps will need to be undertaken to ease the pressure on reserves and reclaim external sector stability. The balance of (other) investment component of Finance Balance has emerged as a major concern in view of the disquieting reserves scenario, declining in the first nine months from (+) USD 10.4 billion to (-) USD 3.5 billion, a fall of about USD 13.9 billion – medium to long term loans declined by about USD 1.6 billion, while the departure in trade credit (net) was to the tune of USD 2.5 billion, of DMBC and NBDC (net) was about USD 4.0 billion and in case of other short term loan (net) was about USD 4.0 billion; liabilities has increased by USD 3.5 billion. Interest on trade credit, which was received at almost zero, had gone up to 6-7 per cent (in the backdrop of uncertainties about reserves and payments capacities) and traders had tried to repay the credit as soon as possible, leading to the significantly high negative figure.

Why is error and omission, at USD (-) 2596 so high when this was only USD (-) 697.0 million in FY2022 also needs to be looked into carefully.

Every effort should be taken to mobilise foreign funds and expedite the disbursement of loans in the pipeline. The GoB has negotiated significant loan amount with the World Bank, ADB and other development partners, both as budgetary support and for project implementation. Foreign funded projects in the ADP and in the aid pipeline should be prioritised for implementation. The Bangladesh Bank is shedding its disbursement of trade credit from the Export Debt Fund (EDF), which, on the one hand, will help improve the overall reserves situation and, on the other hand, help meet the IMF-set target of forex reserves for June 2023 at (USD 24.46 billion; the target for December 2023 is USD 26.81 billion). However, support to exporters, through the newly created credit line and other measures of support must be ensured to deal with the likely shortfall in supply of trade credit against demand, at a time when Bangladesh is having to reduce the size of EDF significantly to protect net forex reserves.

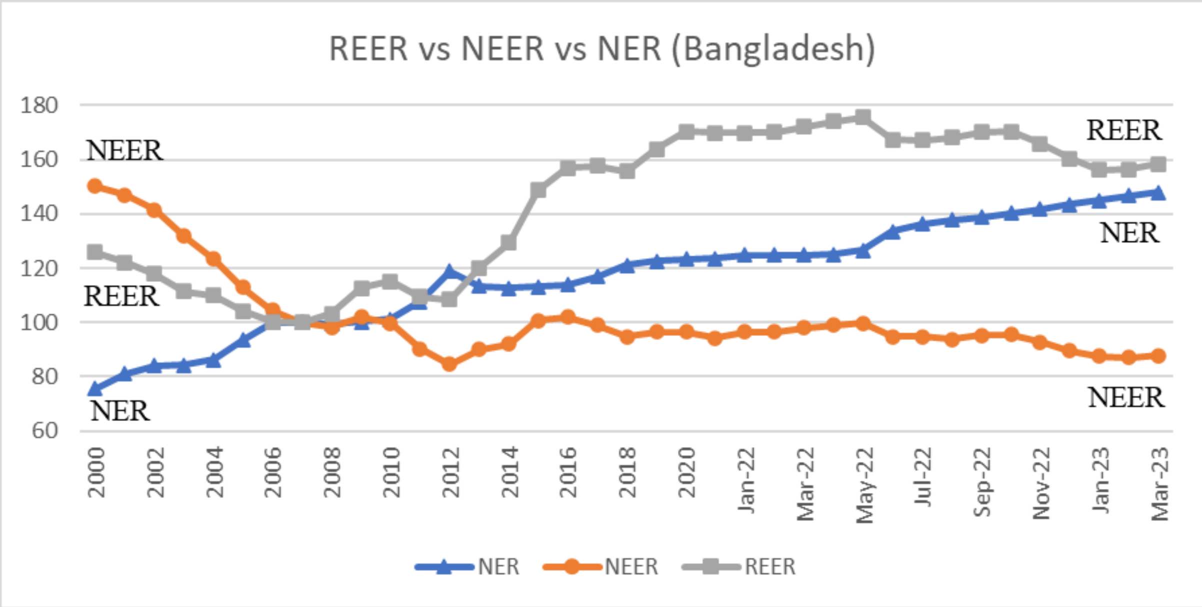
The medium-term target should be to attract higher amount of FDI. In recent years, a large part of the FDI has been on an account of reinvested profit when net new flow of FDI has been very low. The SEZs could be a game changer in this connection. However, the service promised under the One Stop Service Act of 2018 must be offered and overall cost of doing business and business environment (including dispute resolution mechanisms) must be put in place on an urgent basis.

Move towards market aligned exchange rate must be carefully monitored and the monetary policy will need to be well coordinated with fiscal policies. However, major disruptions in currently prevailing exchange rates is not anticipated as market corrections have already taken place, to a significant extent.

The IMF programme requires Bangladesh to move towards a unified exchange rate policy, by moving away the current multiple exchange rates (selling rate by the Bangladesh Bank, inter-bank exchange rate, rate for L/C opening, export repatriation rate, rate applicable for remittances) to a single rate.

Our analysis indicates that, already the significant depreciation of taka is having an impact and the difference between REER and NER has come down quite significantly in recent times (Figure 4.6).

Figure 4.6: REER vs NER vs NEER in Bangladesh



Source: Based on Bruegel (May 2023).

CPD has carried out an exercise based on a Dynamic OLS model[9] to examine the misalignment between the REER[10] and equilibrium REER (EREER)[11] and estimated what would be the range of the nominal exchange rate (BDT/ USD) if the two were to be aligned. The model indicates that the REER (in December 2022) was misaligned to the extent of 3.4 per cent from the EREER. Accordingly, the nominal market-based exchange rate, if an alignment is reached, would be in the range of BDT 105 to 116 per USD (considering 95 per cent confidence interval). As was noted, the gap between the REER and NER is closing down in recent months. Actual exchange rate of BDT will, however, depend on various factors including the extent of intervention by the Bangladesh Bank in the forex market, export and remittance performance, demand for imports and global commodity prices, capital and financial flows. Also, the estimates are based on 2022 figures; there has been some developments in the forex exchange market since then. However, the indications are that if a move is taken towards a single exchange rate, the forex market is currently in a position to adjust to it without significant disruption. The central bank should undertake rigorous analysis and take decisions in this regard based on evidence and data and closely monitor the exchange rate movement.

[9] The EREER was estimated using a Dynamic OLS model with a fixed lead and lag of 1. The model used the REER as the dependent variable and Productivity Proxy (GDP/Capita), Government Consumption Expenditure, Net Foreign Asset, Remittance and Trade Openness as independent variables. REER was extracted from Bruegel and the other variables were extracted from World Development Indicators. Results of our estimations correspond with the Balassa Samuelson effect. The output table is given in Annex Table 4.1.

[10] REER: Real Effective Exchange Rate.

[11] EREER: Equilibrium Real Effective Exchange Rate

References

Country-Wise Yearly/Monthly Overseas Employment and Remittance Data. (2023). BMET. http://www.bmet.gov.bd/site/page/1baff8ec-27eb-48e0-9ec6-1751cd5411d8/http%3A%2F%2Fwww.bmet.gov.bd%2Fsite%2Fpage%2F1baff8ec-27eb-48e0-9ec6-1751cd5411d8%2F-

Database Eurostat. (2023). Eurostat. https://ec.europa.eu/eurostat/web/main/data/database

Dataweb USITC. (2023). USITC. https://dataweb.usitc.gov/

Economic Trends. (Various Years). [Monthly]. Bangladesh Bank. https://www.bb.org.bd//pub/monthly/econtrds/

Export Statistics. (2023). Export Promotion Bureau. http://epb.gov.bd/site/view/epb_export_data/-

Major Economic Indicators. (Various Years). [Monthly]. Bangladesh Bank. https://www.bb.org.bd//pub/monthly/selectedecooind/

REER Database. (2023). Bruegel | The Brussels-Based Economic Think Tank. https://www.bruegel.org/publications/datasets/real-effective-exchange-rates-for-178-countries-a-new-database

The Pink Sheet. (2023). World Bank. https://www.worldbank.org/en/research/commodity-markets

SECTION 5. FOOD SECURITY DURING THE PERIOD OF MACROECONOMIC INSTABILITY

5.1 Introduction

Food security in net-food importing countries is likely to be adversely affected during macroeconomic instability (e.g., high inflation, currency devaluation, or economic recession). Bangladesh, for having macroeconomic instability during FY2023, may experience food security-related challenges during this period. It is to be noted that food security has two macroeconomic determinants – (a) food supply (i.e., availability) and (b) households' demand for food (i.e., access). The former depends on the abundance of per capita food supplies from domestic production, stocks, and imports (Pescatori, *et.al.*, 2021). Lack of food grain availability negatively and significantly impacts food price inflation in both the short and long run. Increased volatility of commodity prices is likely to weigh on increased volatility in food production and food inflation (IMF, 2023). Small farmers and poor consumers in developing countries get affected due to high inflation as poor people spend a major portion of their income on food consumption (Samal *et al.*, 2022). The purchasing power of the consumers determines how much food security the consumers would avail during the period of macroeconomic instability. This section aims to review the state of food security in Bangladesh during the macroeconomic crisis that Bangladesh is currently experiencing and to identify reasons behind this and possible way out in order to better manage the food security situation.

5.2 State of Food Supply during Macroeconomic Instability

5.2.1 State of country's food self-sufficiency

Bangladesh's state of food self-sufficiency – mainly domestic production of rice and wheat, needs to be analysed first as it largely determines the level of the country's food security. After the official announcement of food self-sufficiency in 2000 (Bokhtiar & Samsuzzaman, 2023), over the years, the demand for the import of rice and wheat has decelerated. Despite the positive development, the import of rice and wheat did not stop; rather, it has continued intermittently (Table 5.1). The per capita food availability is found to be higher than per capita food demand, although it has significantly dropped in FY2022 (Table 5.2). In other words, the official announcement of food self-sufficiency still seems 'elusive'. The Ukraine-Russia war had made the 'self-sufficiency' claim weaker. Due to war, the country has experienced multiple macroeconomic challenges which negatively impact domestic production and capacity to import (Table 5.1). Hence, the food security challenges need to be handled by the government from the perspective of a 'net food importing country'.

Table 5.1: Production and import of rice & wheat (in 000 m. tons) and average growth rate per year

Fiscal Year	Production				Imports			
	Rice (000 m tons)	Δ Rice annual growth	Wheat (000 m tons)	Δ Wheat annual growth	Rice (000 m tons)	Δ Rice annual growth	Wheat (000 m tons)	Δ Wheat annual growth
FY2000	23067	7.4	1840	8.9	433	391.2	1,671	26.4
FY2005	25157	-3.9	976	-22.1	1295	61.7	2078	4.6
FY2010	32257	3	969	14.1	93	-84.6	3364	38.7
FY2015	34710	1.0	1348	3.6	1490	297.3	3784	40.6

Fiscal Year	Production				Imports			
	Rice (000 m tons)	Δ Rice annual growth	Wheat (000 m tons)	Δ Wheat annual growth	Rice (000 m tons)	Δ Rice annual growth	Wheat (000 m tons)	Δ Wheat annual growth
FY2019	36391	0.3	1017	-7.4	206	-94.7	5629	-4.3
FY2020	36604	0.6	1029	1.2	4.3	-97.9	6435	14.3
FY2021	39644	8.3	1299	26.2	1359	31507	5343	-17
FY2022	39481	-0.4	1226	-5.6	987	-27.4	892	-83.3

Source: FPMU database (n.d.); Note: Import includes GoB commercial import, GoB import for public stock, private import, and food aid; gradually, food aid is decreasing, and during the last decade, it accounted for around 1% of total import.

Table 5.2: Per capita availability against per capita demand (consumption as a proxy of demand)

Fiscal Year	**Per Capita Availability (gram/day)**			**Per Capita Consumption (gram/day)**		
	Total	**Rice**	**Wheat**	**Total**	**Rice**	**Wheat**
FY1997	430	384	46	502	447	55
FY2000	522	453	70	591	530	61
FY2005	529	471	57	626	568	58
FY2010	614	535	79	674	598	76
FY2015	634	548	87	709	609	101
FY2020	687	564	123	723	592	131
FY2021	834	718	97	726	592	135
FY2022	653	576	76	709	601	108

Source: Author's calculation based on the FPMU data on PCA and index mundi for PCC.

5.2.2 Food Production and Import: Factors Behind the Trend

The production, import and availability of foodgrains had a mixed trend during the pre-pandemic period. However, the trend is negative in the post-pandemic period. The per capita availability of rice and wheat has significantly decreased during the post-pandemic period. Compared to the pre-pandemic period, wheat's per capita availability is much lower during the post-pandemic period. A significant drop in wheat imports due to high wheat prices caused by an interruption in the global supply chain due to the Ukraine-Russia war and less availability of dollars for importing the required amount of wheat were the main reasons behind the low per capita availability of wheat (Table 5.3).

Table 5. 3: State and growth in food production, import and availability

Product	Fiscal year	production		Import		Per capita availability	
		In 000 m. tons	% Changes	In 000 m. tons	% Changes	Gram/ day	% Changes
Rice	FY2019	36391	0.3	206	-94.7	528	-9.7
	FY2020	36604	0.6	4.3	-97.9	564	6.8
	FY2021	39644	8.3	1,359	31507	718	27.3
	FY2022	39481	-0.4	987	-27.4	576	-19.8
Wheat	FY2019	1017	-8.0	5,629	-4.3	106	-5.4
	FY2020	1029	1.2	6,435	14.3	123	16.0
	FY2021	1299	20.8	5,343	-17.0	97	-21.1
	FY2022	1226	-6.0	892	-83.3	76	-21.6

Source: Author's calculation based on FPMU database, (n.d.).

A number of factors are found to be responsible for low food availability during the post-pandemic period. These include- (a) the high price of wheat in the international market due to limited availability of wheat; (b) devaluation of the BDT against USD, which made import costlier; and (c) limited domestic supply of fertilisers due to lack of gas supply.

(a) High price of wheat in the global market

In Bangladesh, wheat and rice are considered complementary food products – fluctuation of global supply and price of one product directly affect the supply and price of another. During the post-pandemic period, the majority of food products have experienced a price rise. Among those, wheat supply has significantly dropped mainly due to the Ukraine-Russia war, which consequently shot up the wheat price in the international market (Table 5.4) – almost double compared to the pre-pandemic level. As a result, the local market has confronted shortages of wheat and a rise in the prices of wheat and rice. Hence, food availability during the post-pandemic period has confronted challenges.

Table 5. 4: World price of different agri commodities imported by Bangladesh

		2019	2020	2021	2022	Av. Yearly % change (2019 and 2022)
Tea, avg 3 auctions	($/kg)	2.6	2.7	2.7	3.1	6.3
Coconut oil	($/mt)	735.7	1010.4	1636.3	1634.6	40.7
Groundnuts	($/mt)	1337.8	1838.7	1555.0	1568.1	5.7
Fish meal	($/mt)	1448.0	1432.7	1480.9	1595.6	3.4
Groundnut oil	($/mt)	1407.4	1697.8	2075.1	2202.6	18.8
Palm oil	($/mt)	601.4	751.8	1130.6	1276.0	37.4
Soybean oil	($/mt)	765.4	837.8	1385.4	1666.8	39.3
Maize	($/mt)	170.1	165.5	259.5	318.8	29.2
Rice, Thai 5%	($/mt)	418.0	496.8	458.3	436.8	1.5
Rice, Thai 25%	($/mt)	410.4	481.8	448.3	429.7	1.6
Rice, Thai A.1	($/mt)	393.5	474.6	436.1	417.7	2.1
Rice, Viet Namese 5%	($/mt)	351.9	428.0	446.3	404.5	5.0
Wheat, US SRW	($/mt)	211.3	227.7	281.7	381.9	26.9
Wheat, US HRW	($/mt)	201.7	231.6	315.2	430.0	37.7
Sugar, world	($/kg)	0.3	0.3	0.4	0.4	15.2

Source: The World Bank, (2023).

(b) Shortages of supply of fertiliser

The fertiliser supply has significantly reduced in 2022 and is likely to be less in 2023. This is mainly because of less fertilisers imports during the said periods, though production has increased (Table 5.5). Moreover, domestic production of fertilisers is likely to be curtailed mainly in 2023 because of less supply of gas for the state–owned fertilisers companies. Given the limited availability of foreign exchange, there was a constraint in allocating funds to import fertilisers. To reduce the subsidy burden, the government has revised the fertilisers price – the decision would reduce the subsidy burden by an amount of Tk.7000 crore. However, such a move would not ensure a rise in fertilisers supply unless the necessary amount of foreign exchange is allocated for meeting the gaps in domestic requirements for fertilisers.

Table 5. 5: Fertiliser Production and Imports (thousand m. tons)

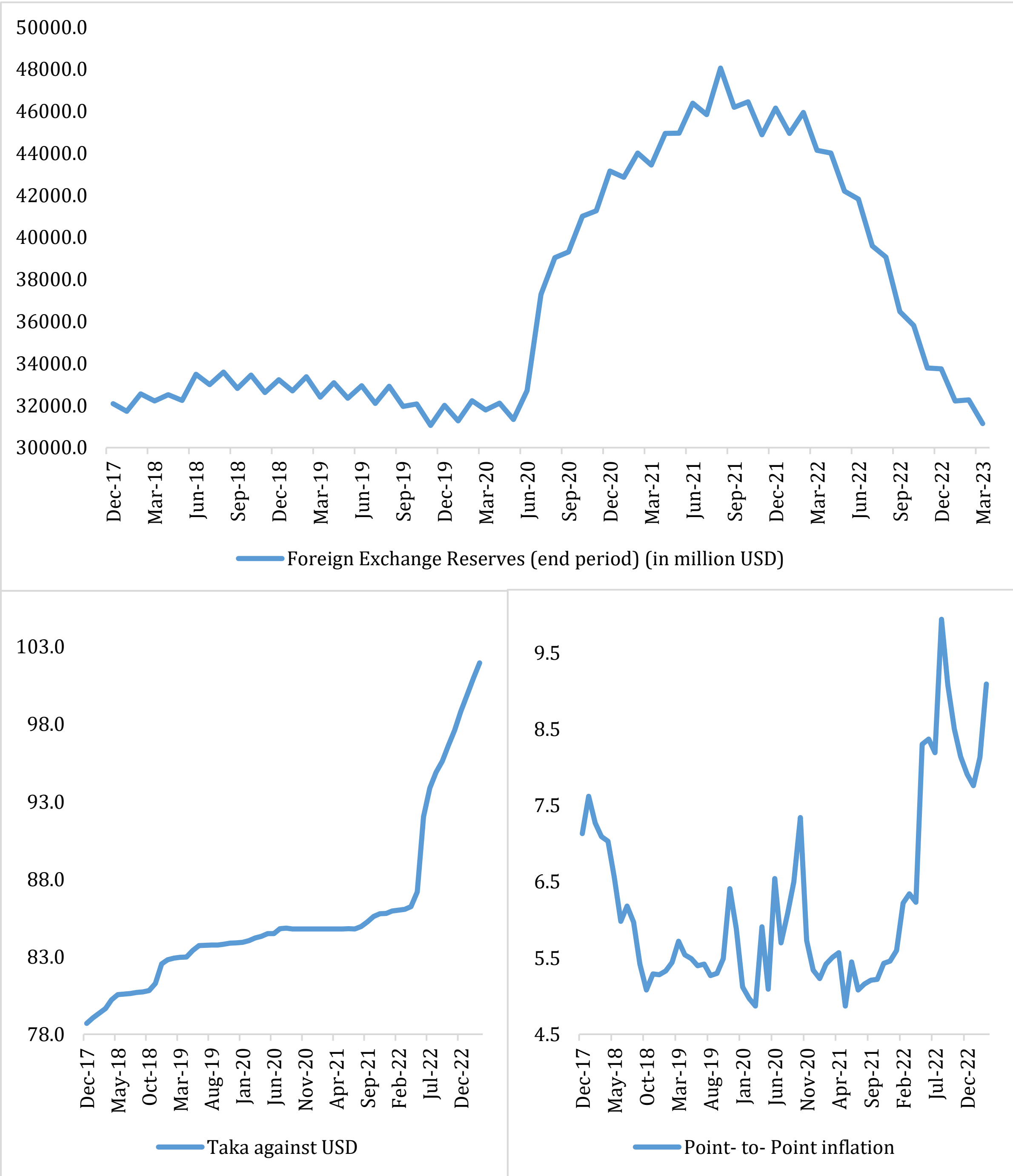
Year	Production	Import	Total
FY2019	904	4225	5129
FY2020	924	4798	5772
FY2022	1725	3220	4945

Source: FPMU database, (n.d.).

(c) Depletion of Foreign Exchange Reserve and Devaluation of BDT against USD

The gradual depletion of foreign exchange reserves has multiple impacts on food security-related issues (Figure 5.1). This has reduced the capacity to import essential food items as well as raw materials, including fertilisers, pesticides and other items required for food production. On the other hand, the depletion of the reserve has further weakened the local currency against major foreign currencies, including the USD. Hence, the import of cost for food and food-related materials has increased. Overall, the current exchange rate and inflation spike have made food imports dearer.

Figure 5.1: Trend of the exchange rate, food inflation and foreign reserve



Source: Author's analysis based on the Bangladesh Bank, (2023).

(d) Regression Analysis on Determinants of Food Import

A regression analysis has been carried out in order to identify the relationship between the import of food grains with the import price of rice and wheat, food inflation, exchange rate (BDT/USD) and foreign exchange reserve, (Table 5.6).[12] It is identified that all the variables are stationary at first difference except import of food and inflation which were stationary at level form. Therefore, the ARDL model was fit to identify the long-run equilibrium among the variables. It is found that the coefficient of the foreign reserve is significantly negatively associated with the import of food.

Table 5. 6: Results of ARDL regression

Log of import	Coefficient	P>t (significance level)
Log of import		
L1.	-0.07	0.46
Log of import price of rice	0.79	0.37
Log of import price of wheat	2.30	0.06*
Log of food inflation	0.54	0.20
Log of exchange rate	8.05	0.52
Log of reserve	-7.24	0.01**
Constant	-3.54	0.63

Source: Authors' estimate; Note: * indicates significance at a 10 per cent level and ** indicates significance at a 5 per cent significance level.

In order to identify the long-run equilibrium among the variables, the bound test has been estimated. The results in Table 5.7 indicate that the F statistics (20.45) are higher and T statistics (-10.81) are lower than their I(0) regressors which suggest rejecting the null hypothesis of no equilibrium. Therefore, there is at least one cointegrating relationship in the long run.

Table 5. 7: Results of bound test to indicate long run equilibrium

Regressors		**Critical values**	
[I_0]	L_1	2.26	-2.57
[I_1]	L_1	3.35	-3.86
[I_0]	L_05	2.62	-2.86
[I_1]	L_05	3.79	-4.19
[I_0]	L_025	2.96	-3.13
[I_1]	L_025	4.18	-4.46
[I_0]	L_01	3.41	-3.43
[I_1]	L_01	4.68	-4.79
		accept if F < I(0) & Reject if vice versa	accept if t > I(0) & Reject if vice versa
		F	T
Calculated values		***20.45***	***-10.81***

Source: Authors' analysis based on the data from FPMU and Bangladesh Bank.

The above table suggests that food import (dependent variable) is cointegrated with at least one variable. In order to identify the cointegrating equation, the error correction model is estimated in table 5.8. The model postulates that a high speed of positive adjustment is expected toward

[12] The model includes the import of food as a dependent variable, whereas the import price of rice and wheat, food inflation, the exchange rate (BDT/USD), and foreign exchange reserve as independent variables. Monthly data of different variables are used from the period of January 2014 to December 2022. Data are converted into logarithmic form in order to have the same data unit for different types of variables.

equilibrium, and the error correction term is significant. Only the import price of wheat is found to be cointegrated in the long run, whereas in the short run, causality is found with the import of food with the import price of wheat and the foreign reserve. The lag and difference operator of wheat prices and foreign reserves also cause food import in the short run.

Table 5. 8: Results of vector error correction model

D. ln imp	Coefficient	P>t
Adjustment parameter (speed of adjustment)		
Ln imp		
L1.	*-1.07*	*0.00*
Long run equation		
Log of import price of rice	0.74	0.37
Log of import price of wheat	*-0.82*	*0.01*
Log of inflation (food)	0.50	0.20
Log of exchange rate	0.34	0.88
Log of foreign reserve	0.69	0.12
Short run equation		
Long of import price of wheat		
D1.	*3.18*	*0.01*
LD.	0.72	0.55
L2D.	-3.69	0.00
Log of exchange rate		
D1.	7.69	0.55
LD.	-21.38	0.11
L2D.	-21.35	0.12
Log of foreign reserve		
D1.	*-7.97*	*0.00*
LD.	*-7.30*	*0.01*
_cons	-3.54	0.63

Source: Authors' estimate.

According to the diagnostic test of Durbin Watson autocorrelation test, normality and heteroscedasticity, the model has no serial correlation, and data is normally distributed and heteroscedastic. In terms of CUSUM stability test, the model deviates from its upper and lower range values in the short run but converges to the equilibrium within the upper and lower bound range.

(e) Food Availability for the Target Groups: Public Food Stock

The reduced availability of food during 2022 has pushed the government to take proactive measures for raising public food stock. The public food stock has significantly increased during the post-pandemic period, particularly in 2022 (Table 5.9 and 5.10), which is likely to continue in 2023. A part of the public food stock was based on domestic procurement of rice and wheat, while a major part of the stock was direct import by the government. Because of the faulty pricing policy for the public procurement of rice as well as the non-transparent procurement process, the domestic procurement of rice could not reach the target. Hence, the potential for domestic procurement could not meet the target, which ultimately affects the food security of the targeted population – i.e., poor, vulnerable and other targeted groups.

Table 5. 9: Year wise (end of June) Closing Public Food Stock

Fiscal Year	Rice	Wheat	Total	Average growth in rice stock	Average growth in wheat stock
	('000 m. tons)				
FY2001	422	445	867	-15.3	-16.8

Fiscal Year	Rice	Wheat	Total	Average growth in rice stock	Average growth in wheat stock
	('000 m. tons)				
FY2002	500	444	944		
FY2003	525	146	671		
FY2004	723	116	839		
FY2005	163	146	308		
FY2006	568	167	735		
FY2007	436	168	604		
FY2008	825	174	999	-6.5	-8.5
FY2009	930	216	1145		
FY2010	421	110	531		
FY2011	569	311	880		
FY2012	939	311	1250		
FY2013	715	306	1021	16.7	2.1
FY2014	734	419	1153		
FY2015	949	337	1287		
FY2016	458	397	855		
FY2017	123	256	378		
FY2018	963	353	1315		
FY2019	1256	418	1674	26.9	-4.7
FY2020	838	350	1188		
FY2021	1056	411	1467		
FY2022	1197	286	1483		

Source: FPMU Database.

Table 5. 10: Domestic Procurement of Aman and Boro Rice and wheat

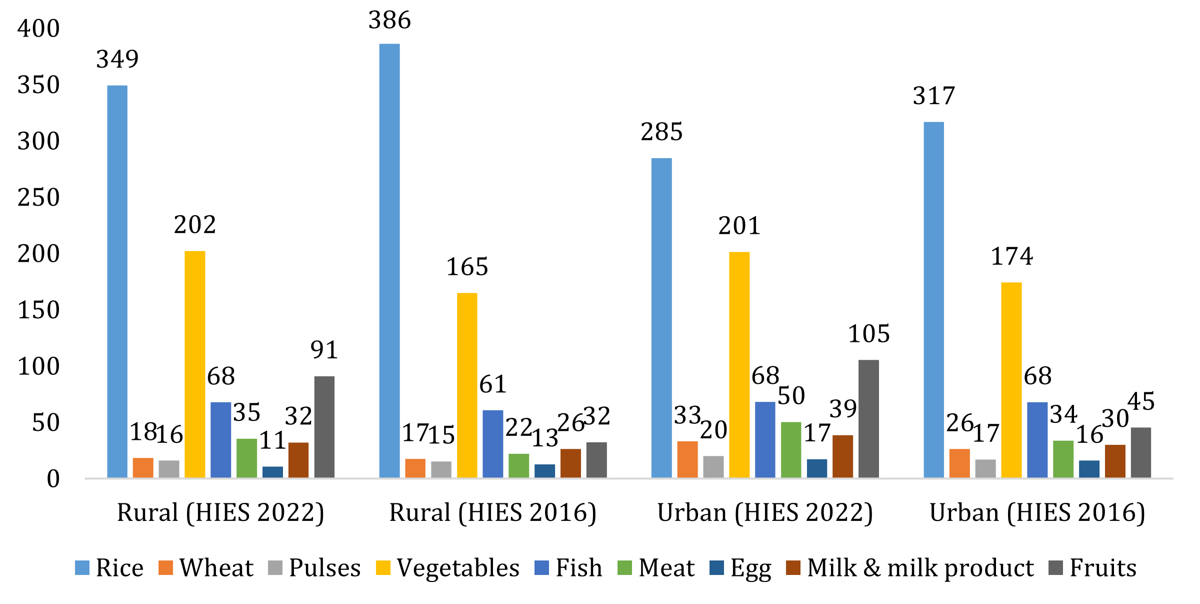
Year	Aman						Boro						Wheat	
	Target '000' metric ton)			**Actual '000' metric ton)**			**Target '000' metric ton)**			**Actual '000' metric ton)**			**'000' metric ton)**	**'000' metric ton)**
	Paddy	Rice	in Rice	Paddy	Rice	in Rice	**Paddy**	**Rice**	**in Rice**	**Paddy**	**Rice**	**in Rice**	Target	Actual
2000	73	200	250	54	199	236	154	500	600	134	513	600	250	211
2005	37	175	200	0	163	163	39	978	1000	20	919	931	50	1
2010	150	200	302	0	14	15	150	1050	1147	9	557	563	50	48
2015		320	320	0	320	320	100	1035	1100	71	1024	1070	250	205
2019		800	800	0	800	800	400	1150	1410	400	1000	150	50	44
2020	600	400	800	241	156	316	800	1000	1670	238	565	720	1000	103
2021	200	650	783	12	75	83	650	1235	1749	362	1060	1319	100	103
2022	300	500	700	0	12	12								

Source: FPMU database, (n.d.).

5.3 Household's demand for food during macroeconomic instability

As discussed, household demand for food reduces during the time of macroeconomic instability as a rise in inflation causes a reduction in a household's purchasing capacity. Hence, the household demand for food is likely to be adversely affected during the post-pandemic macroeconomic instability in Bangladesh. According to the HIES 2022, households' food and non-food consumption expenditures have increased compared to that in HIES 2016. However, the consumption of rice has declined in 2022 while the consumption of wheat has marginally increased (Figure 5.2). In other words, households have experienced changes in the consumption pattern where consumption of non-rice and non-food has been getting more important in overall household expenditure.

Figure 5.2: Comparison of the per capita consumption (gram per day)



Source: BBS, (2023).

5.3.1 Household's expenditure for food consumption

Household's expenditure for food consumption (in real term) has significantly deteriorated during 2022 compared to that in 2016 (Table 5.11). Household's expenditure for food did not rise in commensurate with their rise in real income. In other words, households are forced to spend a substantial amount of their income on non-food items. Out of the incremental rise in real income of Tk.3317 per household per month, less than one-third of that household's income is spent on food consumption. Households seem to be in a state of vulnerability from a food security point of view.

Table 5. 11: Comparison of the income of the household in nominal and real terms

Year	Income		Food expenditure		Share of food expenditure of total household's income	
	Nominal	Real	Nominal	Real	Nominal	Real
2022	32,422	10589	14,003	4207	43.2	39.7
2016	15,988	7272	7,354	3132	45.9	43.1

Source: Author's calculation based on BBS (2023).

5.3.2 Social Safety net Programmes for the Target Groups during Macroeconomic Instability

Given the weak purchasing capacity during the period of high inflation, it is important to continue the SSNPs for the target groups extensively. The food assistance-related programmes cover around 4.24 crore people. Programmes are targeted at vulnerable women, VGF, GR, hill tract people, OMS, food for work, and different types of relief. The programmes are related to food assistance, whereas the government provide food as grants or for work. Most vulnerable households who are less resilient during economic crises are covered under OMS, TR, and Food for Work programmes. In 2022, the government distributed rice and wheat at subsidised prices among one crore families registered under TCB. It is interesting to note that most of the programmes did not experience any major changes in coverage during 2022 and 2023; rather, the coverage has declined in a few programmes (such as VGF and OMS in 2023) (Table 5.12). Due to the rise in the cost of food, the budget allocation has partially increased in some of the programmes (even decreased in a few programmes, FFP in 2023). Besides, there are allegations of lack of efficiency in selecting beneficiaries for the family card programme, including the problem of 'exclusion-inclusion biases' in the programme beneficiaries. According to Moazzem and Shibly (2023), the old age allowance and vulnerable women group (widow) support programmes have a leakage of 30 and 33 per cent, respectively. Proper beneficiary targeting would cover an additional 45 lac eligible old age and widow non-beneficiaries.

Table 5.12: PFD allocation for different target groups

Food support Programmes	Beneficiaries (persons in lac)			Budget (in crore Tk)		
	RFY2021	RFY2022	BFY2023	RFY2021	RFY2022	BFY2023
Vulnerable Women Benefit (VWB) Program	10.4	10.4	10.4	1840.1	1838.5	1840.3
Vulnerable Group Feeding (VGF)	200.2	180	180	941.2	962	991.1
Gratuitous Relief (Food)	26.3	32	33	242.6	572.6	589.9
Food Assistance in Ctg-HTA	2.8	2.3	2.9	318.2	347.6	365.3
Food For Work (FFW))	0	9.6	9.8	0	826.4	876.3
Open Market Sales (OMS)	20	54	37.4	949	1943.6	1720.1
Food friendly Program	62.5	62.5	62.5	2891	2816.7	2543.9
Food Subsidy (Others)	-			1389.3	1584.6	1700.8
Relief Goods	59.1	80.3	82.9	185	185	190
Relief Works (Flood, Drought, Cyclone and Others)	36	4.8	4.8	91	181	81
Ration for Shaheed (Martyred) Family and Honourable Injured Heroic Freedom Fighters	0.3	0.3	0.3	65	70	70

Source: MoF (2022).

5.3.4 Coverage of PFDS

The distribution of rice and wheat under PFDS, particularly through OMS, FFP, and other programmes, increased during FY2022 (Table 5.13). This rise in the distribution of food has partially increased the availability of food for the target groups. However, this rise in food distribution does not necessarily mean a rise in access to a number of potential beneficiaries. Government capacity to spend for PFDS is another important issue during the period of limited fiscal space. Figure 5.3 shows a 20.5 per cent rise in food subsidy from Tk 4172 crore in FY2021 to Tk 5026 crore in FY2022. Without having the fiscal space, the rise in budget for PFDS-related expenditures and thereby ensuring more coverage is difficult.

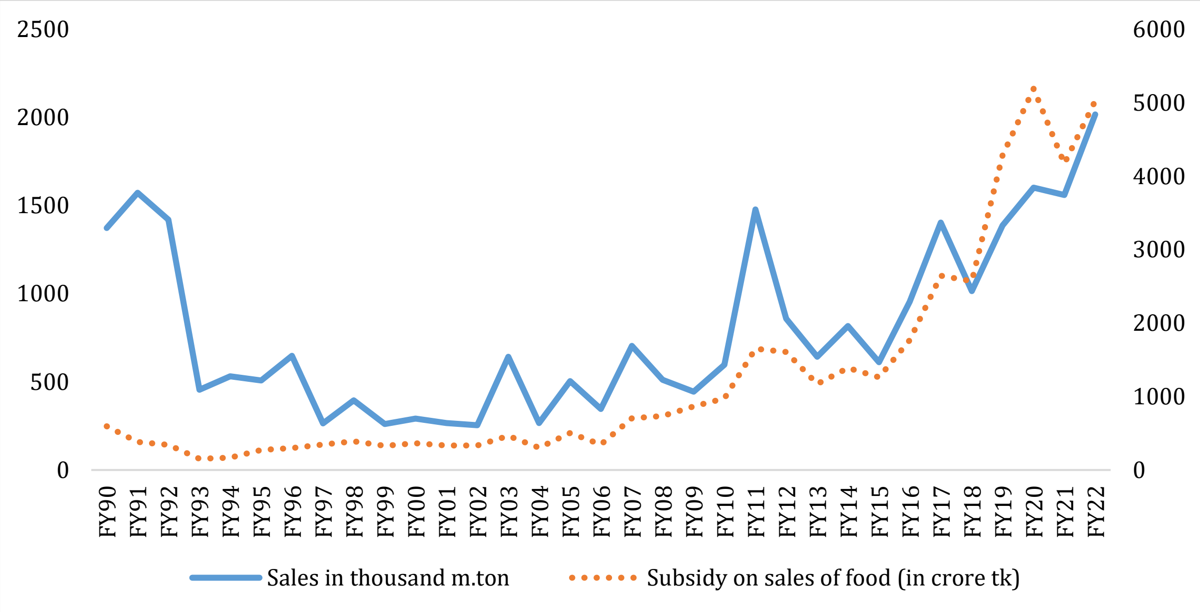
Table 5.13: Public food distribution (in '000 m. tons)

Year	Rice		Wheat	
	Distribution	% changes	Distribution	% changes
FY2015	1220	-3.3	619	-35.4
FY2016	1512	23.9	552	-10.8
FY2017	1610	6.5	631	14.3
FY2018	1702	5.7	408	-35.3
FY2019	2145	26.0	448	9.8

Year	Rice		Wheat	
	Distribution	% changes	Distribution	% changes
FY2020	2208	2.9	569	27.0
FY2021	1862	-15.7	590	3.7
FY2022	2250	20.8	636	7.8

Source: Author's calculation based on FPMU database, (n.d.).

Figure 5.3: Subsidy for sales of foodgrain and distribution amount by sales



Source: Author's calculation based on FPMU database, (n.d.).

5.3.4 Rise in Energy Prices and Its Implications on Food Security

The rise in energy prices to adjust the energy related subsidy as per meeting the conditionality of IMF is a faulty step. In fact, energy related subsidies could be reduced without raising energy prices by revising the pricing of electricity purchases from independent power producers. Because of the faulty step, farmers need to pay higher irrigation charges which would ultimately increase the harvest price of rice and wheat. A similar attempt is going to be made by setting a market-based pricing for the retail tariff of electricity, as per IMF conditionality. Without proper adjustment of the power purchase agreement, market-based pricing would deprive the consumers, including the farmers.

5.4 Conclusion: Addressing the Concerns of Food Security during the Period of Macroeconomic Instability

5.4.1 Addressing the concerns of food production

The government needs to ensure a rise in food production to ensure food security through better food availability and reduce volatility in food prices in the domestic market. It is important to keep the irrigation cost lower by reducing electricity costs or replacing diesel-based irrigation with solar-based irrigation. Hence, farmers should get subsidised rates for electricity usage for irrigation. Similarly, subsidies for fertilisers and mechanisation need to continue- it is expected that government will not make any attempt to revise the prices of fertilisers and farm machinery. A necessary allocation needs to be made to procure rice and wheat to cover the increased demand for PFDS. In this context, the necessary foreign exchange needs to be allocated for the import of essential food items, particularly rice, and wheat. It is found that other South Asian countries have taken different measures to address the food production related concerns (Annex Table 5.1).

5.4.2 Addressing the concerns of food demand

Containing food inflation is highly important with a view to reducing the pressure of declining the real income of the households. In this context, stability in the exchange rate (BDT against USD) and maintaining a stable forex reserve could partly help reducing the volatility in the import of food grains. The SSNP has yet to raise the coverage during the crisis period, although that is highly essential. A rise in PFDS could ensure the higher availability of foodgrains for existing beneficiaries, but it cannot ensure higher access to potential beneficiaries. In this context, a rise in subsidy allocation for SSNPs, particularly PFDS, is required. Better targeting and reducing the leakages and wastages could substantially increase the potentiality to raise access to the beneficiaries. Bold measures are required in order to ensure transparency and accountability in the SSNPs, particularly OMS operations. Despite having fiscal difficulties, the government needs to create fiscal space to ensure universal food security. It is expected that the next budget will take measures towards that direction. It is found that other South Asian countries have taken different measures to address the food demand and supply related concerns (Annex 1).

References

Bangladesh Bank. (2023). *Monthly Economic Trends.* May 2023. Retrieved from https://www.bb.org.bd/en/index.php/publication/publictn/3/10

BBS. (2023). *Household Income and Expenditure Survey (HIES) 2022: Key Findings.* Latest Publications. Bangladesh Bureau of Statistics (BBS). Retrieved from https://bbs.portal.gov.bd/site/page/b588b454-0f88-4679-bf20-90e06dc1d10b/-

Bokhtiar, S.M. & Samsuzzaman, S. (2023). *A Development Trajectory of Bangladesh Agriculture: From Food Deficit to Surplus*. Bangladesh Agricultural Research Council, Dhaka, Bangladesh.

FPMU. (n.d.). *Database on Food Situation.* Food Planning and Monitoring Unit (FPMU). Ministry of Food. Retrieved from http://fpmu.gov.bd/fpmu-database/MAIN.HTM

IMF. (2023). *G-20 Background Note on the Macroeconomic Impact of Food and Energy Insecurity*. International Monetary Fund. Retrieved from https://www.imf.org/external/np/g20/032823.htm

IndexMundi. (n.d.). *Bangladesh Milled Rice Domestic Consumption by Year.* United States Department of Agriculture. Retrieved from https://www.indexmundi.com/agriculture/?country=bd&commodity=milled-rice&graph=domestic-consumption

IndexMundi. (n.d.). *Bangladesh Milled Wheat Domestic Consumption by Year.* United States Department of Agriculture. Retrieved from https://www.indexmundi.com/agriculture/?country=bd&commodity=wheat&graph=domestic-consumption

Moazzem, K.G., & Shibly A.S.M.S.A. (2023). *Estimating Gap of the Social Safety Net Programmes in Bangladesh: How Much Additional Resources Required for Comprehensive Social Inclusion?* Ongoing CPD Working Paper. Dhaka: Centre for Policy Dialogue (CPD). Available at https://cpd.org.bd/how-to-improve-coverage-and-effectiveness-of-the-ssnps/

MoF. (2022). *Social Security Programs : FY 2022-23.* Social Security Programs. Finance Division, Ministry of Finance. Retrieved from https://mof.gov.bd/site/page/5f9be3bc-923f-4c27-8a65-c5e7fe417945/Social-Security-Programs

Pescatori, A., Prifti, E. Bogmans, C. (2021). *Food (in)security: A potentially underrated collateral damage of the pandemic.* (2021, June 5). CEPR. https://cepr.org/voxeu/columns/food-insecurity-potentially-underrated-collateral-damage-pandemic

Samal, A., Ummalla, M., & Goyari, P. (2022). The impact of macroeconomic factors on food price inflation: An evidence from India. *Future Business Journal*, *8*(1), 1-14. https://doi.org/10.1186/s43093-022-00127-7

The World Bank. (2023). *Commodity Markets: Pink Sheet Data.* The World Bank. Retrieved from https://www.worldbank.org/en/research/commodity-markets

SECTION 6. CONCLUSIONS

In view of the emergent scenario and keeping in perspective the upcoming national budget, there is no doubt that the primary task before the policymakers is to restore macroeconomic stability. The targets to be set for the macroeconomic (and fiscal) framework for FY2024 will need to take cognisance of the current realities. The mistakes while preparing the FY2023 budget – that is, setting the targets for major macroeconomic correlates in an unrealistic manner – must not be repeated. While the fiscal and budgetary measures are expected to be the centre of discussions in the coming days, it is critical that the government and the central bank ensure the complementarity between fiscal and monetary policies. The policy measures must prioritise the interests of the small and medium entrepreneurs and common citizens while withstanding the pressure of the vested interest groups. Keeping the IMF conditionalities in perspective and national interests in mind, reform measures should be initiated and expedited. However, the pacing, sequencing and phasing of these reform measures should be well-planned and transparent. Proper enforcement of laws and regulations against bank loan defaulters must be ensured. Instead of incentivising illicit financial flows and illegally earned money through direct and indirect measures, strict administrative steps and punishment should be imposed as per existing laws. The Bangladesh economy is at a crossroads and passing through the most difficult time in recent history. This must be recognised and addressed by appropriate policy tools.

ANNEX

Annex Table 2.1: Impact of GDP, import and inflation on tax revenue collection

Sample: 1993-2020

Included observations: 28

Methodology: Ordinary Least Square (OLS)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
LOGGDP	0.592189	0.251361	2.355928	0.0270
LOGIMPORT	0.652748	0.168807	3.866829	0.0007
INFLATION_RATE	-0.018458	0.005576	-3.310186	0.0029
C	-1.319364	0.411887	-3.203216	0.0038
R-squared	0.981431	Mean dependent var		2.649789
Adjusted R-squared	0.979110	S.D. dependent var		0.477879

Annex Table 4.1: Output Table

Variable	Coefficient	Std. Error	t-Statistic	Prob.
Productivity Proxy	0.734	0.160	4.576	0.002
Govt. Cons. Exp.	-0.245	0.129	-1.884	0.100
Net Foreign Asset	-3.488	0.666	-5.236	0.001
Remittance	-0.100	0.029	-3.332	0.012
Trade Openness	-0.212	0.049	-4.289	0.003
Constant	8.680	1.578	5.498	0.001
R-squared	0.997	Mean dependent var		4.821
Adjusted R-squared	0.992	S.D. dependent var		0.165

Annex Table 5.1: Measures taken by Nepal and Cambodia during the pandemic and post-pandemic period

Countries	Issues	Measures were taken after a pandemic
Nepal	SSNPs	Ensuring the uninterrupted supply of essential commodities, supporting smallholder farmers, strengthening market systems, and enhancing social safety nets. Implemented cash transfer programs, including targeted food assistance and provided subsidies to vulnerable households and smallholder farmers affected by the pandemic.
	Stockpiles	Emergency food stockpiles to ensure the availability of essential commodities during crises.
	Localisation	Strengthening local food systems to reduce reliance on external supply chains during the pandemic. This involved promoting local production, facilitating farmers' access to markets, supporting farmer cooperatives, and enhancing storage and processing infrastructure.
Cambodia	COVID-19 Economic Stimulus Package	Measures to support agriculture, such as providing subsidised loans, agricultural inputs, and technical assistance to farmers
	Market Support and Price Stability	Market monitoring and interventions to stabilise food prices and smoothening the supply chains
	Promotion of Urban Agriculture	Encouraging the cultivation of vegetables, herbs, and small livestock within the urban area
	Strengthening Food Processing and Storage	Improvement of post-harvest infrastructure, including food processing and storage facilities
	SSNPs	Cash transfer programmes, subsidised food distribution, and nutritional support have been implemented.