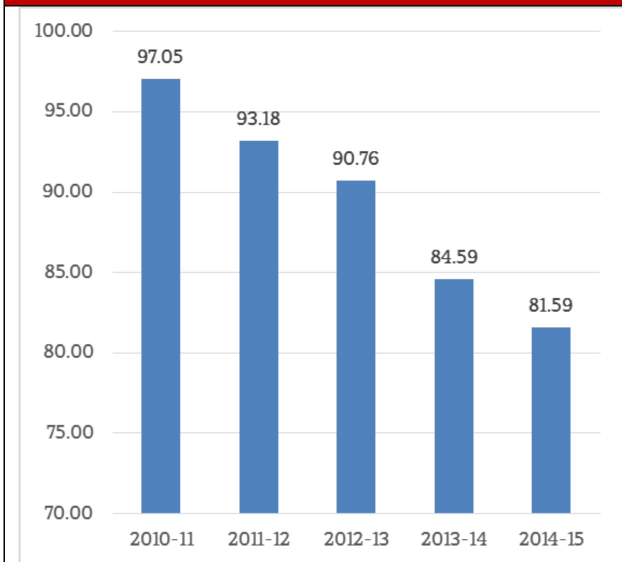
Bangladesh Economic Update

A Pre-Budget Analysis of Major Economic Challenges

April, 2017

Budget Implementation Status (in %)	**Status of ADP Implementation (up to April'17)**
	

Source: Unnayan Onneshan, *A Pre-Budget Analysis of Major Economic Challenges*, Bangladesh Economic Update, Volume 8, No. 4, April 2017.

The Unnayan Onneshan (UO), an independent multidisciplinary think tank, in its pre-budget issue of Bangladesh Economic Update calls for prudent fiscal management in dealing with potential economic risks and vulnerabilities in the year ahead.

In identifying the major economic challenges as regards the national budget 2017-18, the UO notes that waning capacity of the authority in implementing budget is looming large.

Both the collection of revenue and implementation of expenditure, especially Annual Development Program (ADP), have fell short of target in the current fiscal year.

The private investment stagnates, and public investment lacks quality resulting in cost escalation in projects. In addition, upsurge in illicit capital outflows bars capital formation in the economy.

Inadequate spending on social sector is likely to limit improvements in human development. Higher allocations for health, education and social security are indispensable to sustainable development.

Underperformance in external sector causes worry as current account balance records continual deficit and inflow of remittance declines substantially in recent times.

Recapitalization of state-owned commercial banks does not pays off as institutional fragility intensifies in the banking sector resulting in meteoric rise in the default loans.

Jobless growth menaces the fiscal discipline. Youth unemployment takes its toll on the economy by limiting its capacity to capitalize on once-in-a-lifetime demographic dividend.

The causes of elapsing prospects are more of institutional. The gradual corrosion of institutions have constrained allocation of resources to be channeled efficiently into productive sectors in order for the economy to get higher returns in terms of expanded productive capacity, notes the UO.

The status of budget implementation is on the decline since FY 2010-11. Of the total budget outlay, 97.05 percent was implemented in FY 2010-11, whereas the rate subsequently decreased to 93.18 percent, 90.76 percent, 84.59 percent, and 81.59 percent in FY 2011-12, FY 2012-13, FY 2013-14, and FY 2014-15 respectively.

In terms of the current year's status, the research organization shows that only 33.7 percent of the total government expenditure has been implemented during the first six months of FY 2016-17 while only 54.56 percent of the total annual development program (ADP) has been implemented during the July-April period of the current fiscal year.

Meanwhile, the collection of tax revenue lags far behind the target set in the budget 2016-17. Only 53.79 percent of the total target of National Board of Revenue (NBR) tax revenue has been collected during the first eight months of the current fiscal year.

Observing the shortfall in collecting revenue vis-à-vis the target, the UO finds that in FY 2016-17, the target of the collection of revenue was set at Tk. 242752 crore, whereas the actual amount of revenue collection has stood at Tk. 82987.57 crore during the first half of the current fiscal year, representing only 34.19 percent of the target compared to 37.05 percent in the previous fiscal year.

Taking account of unsatisfactory implementation of government expenditure, the research organization evinces that the total government expenditure has stood at Tk. 114730 crore during the first half and total ADP stood at 65083 crore during the first eight months of FY 2016-17 against the whole fiscal year's target of Tk. 340605 crore and Tk. 110700 crore respectively.

Referring to higher rate of growth in non-development expenditure, the UO shows that while the rate of growth in non-development expenditure has stood at nearly 17 percent in the budget of FY 2016-17 compared to the budget of previous fiscal year, the rate of growth in development expenditure stood at 14 percent in the budget of FY 2016-17 compared to that of FY 2014-15.

In terms of fiscal deficit, the think tank finds that overall fiscal deficit stood at Tk. 3910 crore during second quarter of the current fiscal year (representing 0.2 percent of GDP) compared to Tk. 2300 crore (representing 0.13 percent of GDP) in the corresponding period of the previous fiscal year. However, the total fiscal deficit in the first half of FY 2016-17 stood at Tk. 15980 crore (0.8 percent of GDP), compared to Tk. 17400 crore (1.0 percent of GDP) in first half of FY 2015-16.

"The country's quest for self-reliance based upon domestic resource mobilization has been marred by the policy shift towards 'debt-financed-debt-trapped development financing.' The current year witnessed the same level of debt dependence due to failure in providing strategic direction in overhauling the domestic resource mobilization to expand and increase the tax base," notes the Unnayan Onneshan.

In the first seven months of the current fiscal year, total foreign aid decreased to USD 1464.88 million from USD 1754.92 million in the corresponding period of FY 2015-16, a 16.53 percent decline, due to a substantial decline in grants. For instance, grant receipts fell by 45.03 percent in FY 2015-16 compared to FY 2014-15, finds the think tank.

Pointing out the declining inflows of remittance, the research organization shows that remittance receipts decreased by 16.03 percent during the July-April period of FY 2016-17 and stood at USD 10287.23 million compared to USD 12250.83 million in the corresponding period of the previous fiscal year. On year-on-year basis, remittance receipts also decreased by 8.27 percent in April 2017 compared to April 2016.

A large portion of expenditure on consumption, education and health in rural households is financed by remittance. Decrease in inflow of workers' remittance is therefore likely to exert an adverse impact on socioeconomic status of rural households, comments the UO.

Referring to the deficit in current account balance, the think tank finds that the current account continues on a deficit of USD 0.75 billion during July-January period of FY 2016-17 due mainly to a significant trade deficit and lower income from services and secondary income accounts. To deal with external sector's underperformance, export diversification is indispensable, suggests the UO.

Observing poor quality of public investment and sluggish implementation in infrastructure development, the research organization evinces that during July-April of FY 2016-17, only 59.84 percent of total ADP allocation for roads and highways division has been implemented while ADP implementation rate stood at only 37.86 percent for bridge division.

Taking account of slow implementation against the planned duration of the infrastructure development projects and resultant rise in allocation than target, the UO comments that periodical increase in allocation for infrastructural projects implies rising cost induced economic rent, which has made the public investments inefficient.

The Unnayan Onneshan points out that private investment has remained stagnant and has stood at 22.07 percent of GDP in FY 2014-15 and 21.78 percent in FY 2015-16, while increase in public investment from 6.82 percent in FY 2014-15 to 7.6 percent in FY 2015-16 has not succeeded to create much needed crowding in for private investment in the economy.

In addition, lack of adequate capital formation due to large scale illicit capital outflows every year causes national savings and investment not to rise significantly. Highest estimates by the Global Financial Integrity suggest that during the period of 2005 to 2014, illicit capital outflow amounted to USD 7.5 billion every year on average. As the latest count shows that the amount of illicit capital outflow from Bangladesh was USD 9 billion in 2014.

Observing institutional fragility in the banking sector due to monumental rise in writing off of loans, meteoric rise in the default loans and nose-dive in risk and capital adequacy ratio, the research organization comments that the public in general has to pump their tax money to rescue the stripped nationalized commercial banks through recapitalization due to loots in these banks.

Pointing to the fact that Bangladesh lags behind its South Asian counterparts in social sector spending, the think tank expresses concern over inadequate development expenditure on health, education, and social security and welfare, and calls for channeling adequate resources into social sectors that give particular impetus to the improvement in human development.

Health expenditure assumes a declining trend in recent years resulting in high out-of-pocket expenditure in the sector. Development expenditure on health stood at 9.7 percent of the total development expenditure in FY 2009-10, which declined subsequently to 8.7 percent in FY 2010-

11, 7.5 percent in FY 2011-12, 6.8 percent in FY 2012-13, 5.3 percent in FY 2013-14, 5.3 percent in FY 2014-15, 5.4 percent in FY 2015-16 and 5.5 percent in FY 2016-17.

In terms of education expenditure, the UO shows that development expenditure on education stood at 13 percent of the total development expenditure in FY 2009-10, which declined to 12.4 percent in FY 2011-12, 12.3 percent in FY 2015-16, and then slightly increased to 15.3 percent in FY 2016-17. Low allocation along with slow implementation will create skill shortages and unemployment in addition to deteriorating quality of education, adds the research organization.

Referring to the declining allocation for social security and welfare, the UO evinces that development expenditure on social security and welfare stood at 5.4 percent of the total development expenditure in FY 2009-10, whereas the allocation was 5.3 percent in FY 2011-12, 4.5 percent in FY 2012-13, 4.7 percent in FY 2013-14, 4.5 percent in FY 2014-15, 3.8 percent in FY 2015-16, and 3.4 percent in FY 2016-17.

Referring to Labor Force Survey data, the research organization finds that the number of unemployed population increased at an annual rate of 5.29 percent during the period of 2000-2010, and increased from 1.70 million in 2000 to 2.60 million in 2010 while 10.6 million people were day laborers who did not have job security.

Income inequality together with inequality in access to health and education, multidimensional poverty, and joblessness particularly among the youth as 9.1 percent of youth labor force (15-24 years) is unemployed is likely to undermine the development already achieved by the county, comments the UO.

In view of the present economic challenges, the research organization urges adoption of a medium-term strategy, encompassing employment enhancement and skill development programs, expansion of the tax base through higher revenue from income tax than from VAT, institutional reform in financial sector, increased private investment through improved business confidence, effective harmonization of macroeconomic policies, and development of a functional social security system.