

Review of Bangladesh's National Budget

FY2009-10

Edited by

Syeed Ahamed
Jyoti Rahman



drishtipat
writers'
collective

[This page left intentionally blank]

Review of Bangladesh's National Budget FY2009-10



drishtipat
writers'
collective

Edited by
Syed **Ahamed**
Jyoti **Rahman**

© 2009 Drishtipat Writers' Collective (DWC)
All rights reserved.

This e-book or part of it may be electronically reproduced, printed and photocopied ONLY for research, education or non-commercial purposes provided that due credit to the author(s) and publisher(s) is cited. Any commercial publishing or dissemination is strictly prohibited.

Published by
Drishtipat Writers' Collective (DWC)
Dhaka, Bangladesh

Cover and inner design
Sajal Swaroj

Printed by:
Arka, Bangladesh

For more information on Drishtipat Writers' Collective, please visit
<http://www.drishtipat.org/dpwriters>
Or email: dpwriters@drishtipat.org

Price: BDT 70.00
US\$ 5.00
UK£ 3.00

Foreword

Drishtipat Writers' Collective started in early 2007 as a collection of bloggers pulling resources to write on 'all things Bangladesh'. Since then, we have written well over 100 articles in Bangladeshi as well as overseas media. In 2008, we published an e-book on the National Security Council idea. And during the parliamentary election of December 2008, we led a campaign on three issues: public availability of polling centre level data, keeping mobile network on during the Election Day, and safeguarding the rights of minority voters.

Our analysis of previous election irregularities attracted a lot of public attention and prompted the Election Commission to address the possible loopholes in the system, which contributed to a free and fair election, and a smooth transition to an elected government. It is therefore fitting that the Collective is active in analysing the first National Budget of the government elected on 29 Dec 2008.

We congratulate the Government in putting together a Budget that claims to reflect its electoral promise of *din bodol* (*change*). We support the Government in its aim. However, we also provide concrete and constructive criticism where we feel the Government is falling short in keeping its promise. We believe not only is this necessary for a healthy democracy, such criticism will also benefit the Government, and ultimately the people.

This Review contains exactly such constructive criticism on the National Budget. Drishtipat Writers' Collective is committed to engaging with the policymakers, commentators, academics, and other stakeholders in government or private institutions to expand on any of the ideas contained in the Review.

We thank Zafar Sobhan and his team for their help with the publication at the Daily Star and the Arka publishers for their help in putting together this Review.

Sincerely

Asif **Saleh**
Executive Director
Drishtipat

Preface

'Once upon a time' the days of the national budget announcements were big political events where both the incumbent and opposition parties used to run street campaigns for and against the budget proposals. The processions used to attract more media coverage compared to the actual budget proposals. Encouragingly, the post-budget reaction has gradually moved away from street demonstrations to constructive criticisms. Editorials, media briefings and analytical commentaries now dominate the post-budget coverage of print and electronic media. And these have proved to be very effective in influencing the finance ministers in amending and adjusting various budget proposals.

This year, some of the budget proposals were in the public domain for discussion even before the actual announcement. Both the pre and post budget discussions have proved to be successful in altering some of the budget proposals (the proposal regarding black money for an instance). Analysis of the budget proposals should only be the commencement of a public discourse, and for the efficient implementation of these proposals, the budget 'hype' should continue through to mid-year review and post-implementation follow-ups.

To help stimulate the public monitoring of the national development process, Drishtipat Writers' Collective (DWC) has been contributing to the pre and post budget discourse. This compendium puts various articles published during the 2009-10 Budget session within one cover, just as the country prepares itself for the next round of discussions on monitoring and implementation of Budget proposals.

The report is divided into three parts: the first part is the pre-budget discussion and sets the context of the Budget; the second part provides an overall analysis of the Budget proposals; and the third part explores some specific issues related to the Budget.

The first article of this compendium summarises the key issues that are fundamental in assessing this year's Budget. Highlighting the significance of the legal framework of private-public partnership (PPP), record high budget deficit and the politics of rice price, the article calls for drastic measures to be taken during the initial years of the incumbent government. The second article sets the economic context of the Budget and analyses Bangladesh's performance during the early phase of the Great Recession, arguing that while Bangladesh may survive the recession (thus far) relatively unscathed, further economic development and poverty alleviation will largely depend on the policy approaches of the government.

The second part of the compendium analyses the major features of the 2009-10 National Budget. The first article draws attention to a policy paradox during Bangladesh's transition from Poverty Reduction Strategy Program (PRSP) to Five Year Plan (FYP) that which may affect the proper implementation of the Budget proposals. It also questions the much debated black money recycling scheme and the appropriateness of Keynesian stimulus

during the economic downturn. The second article examines the economic growth projections and the fiscal outlook of the country while addressing some medium term challenges that are more likely to affect growth and revenue prospects. Although the economic growth forecasts underpinning the Budget appear practical, the author notes that how the government steps up to these challenges will prove lot more important than any specific measures contained in this budget. As the title of the third article suggests, the author evaluates both the commendable and condemnable proposals of the Budget. Acknowledging the focus on growth recovery, economic devolution and pro-poor strategies, the author raises concerns over the reprehensible proposals such as the black money recycling scheme and calls for greater vigilance on deficit financing and public private partnership projects. In the last article of part two, the author identifies some of the “road-blocks” that may impede the overall implementation of this year's Budget improvement of the law and order situation, “demystification” of bureaucracy, administrative and economic decentralisation, and regulatory reform are identified as the key to successful implementation.

Part three explores some selected issues of the National Budget. The first article focuses on risks to the key macroeconomic forecasts that underpin the Budget, while the second article looks at six prerequisites of a successful PPP Budget. The third article focuses on “Digital Bangladesh”. The author argues that though the Budget proposals may have reflected the political commitment towards a “Digital Bangladesh”, the approach and operational modality to realise this goal is absent in the Budget documents. The final article weighs the Budget proposals against the election manifesto of the Awami League with specific focus on decentralisation. Highlighting the government's election pledges for decentralisation and local democracy, the author raises concerns over some recent government decisions that may adversely affect the decentralisation process and calls for the government to stay true to their word, fiscally and politically.

Contents

Foreword	3
Preface	4
Acronyms	7
Part 1: Pre-budget Discussions	
The first cut is the deepest Syeed Ahamed	9
Surviving the great recession Jyoti Rahman	11
Part 2: Analysing the National Budget for FY2009-10	
Policy paradox and the budget for recession and recovery Syeed Ahamed	17
The long view Jyoti Rahman	19
The good, the bad, and the uncertain Syeed Ahamed	24
The devil is in implementation Asif Saleh	29
Part 3: Analysis of the National Budget: Selected Issues	
Risks to the economic outlook Jyoti Rahman	32
The public-private partnership budget Syeed Ahamed	34
Digital Bangladesh in the budget: a reflection of unpreparedness? Mridul Chowdhury	36
Going back on their word Jalal Alamgir	38
DWC and the authors	40

Acronyms

ADB	Asian Development Bank
ADP	Annual Development Programme
AIG	American Insurance Company
AL	Awami League (Bangladesh Awami League)
BBF	Better Business Forum
BCC	Bangladesh Computer Council
BNP	Bangladesh Nationalist Party
CC	Cubic centimetre (also known as cm^3 . $1 \text{ cm}^3 = 1 \text{ ml}$)
DWC	Drishtipat Writers' Collective
EEF	Equity and entrepreneurship fund
FBCCI	Federation of Bangladesh Chamber of Commerce and Industry
FY	Fiscal year/Financial year
FYP	Five year plan
GDP	Gross domestic product
ICOR	Incremental capital output ratio
ICT	Information and communication technology
IMF	International Monetary Fund
LGED	Local Government Engineering Department
LGRD	Local Government and Rural Development
MP	Member of Parliament
NBR	National Board of Revenue
NGO	Non-government organisation
OECD	Organisation for Economic Co-operation and Development
PPP	Public private partnership
PRSP	Poverty reduction strategy papers
PSPP	Public social private partnership
RMG	Readymade garments
SME	Small and Medium Enterprise
Tk	Taka
UK	United Kingdom
UNDP	United Nations Development Programme
US	United States
VAT	Value added tax
VfM	Value for money

Part 1

Pre-budget Discussions

The first cut is the deepest

Syeed Ahamed¹

The Finance Minister is set to put forward the National Budget for fiscal year 2009-10 today. This is the first budget of this Government, the first since the restoration of political democracy after the emergency, and also the first budget of the Finance Minister AMA Muhith under a democratically elected government.

Over the last few months, numerous proposals/demands have been made to the Minister from different stakeholders. At the same time, scores of speculations have been made about the probable size and composition of the Budget. Today, as the Minister rehearses his budget speech, this article goes over some of the key issues that will be fundamental to assess the new Budget once it is announced.

Legal framework of PPP

The Government is announcing public-private partnership (PPP) an off-budget financing feature for development programmes in its budgetary mechanism that may account for about 15 percent of total National Budget. As discussed in the specific article on PPP in this compendium², the success of the PPP initiative will depend largely on how transparently and efficiently the Government sets the legal mechanism.

The budget speech and the budget documents thus should outline:

- how the Government plans to formulate the legal framework of PPP projects;
- how the risks, resources and rewards of the projects will be shared among the public and private partners;
- how the procedural delays and bureaucratic bottlenecks of such complex schemes will be reduced; and
- how the preference of social responsibility over profit will be ensured in the PPP projects.

Record high deficit

Economies, large and small, around the world are counting high budget deficits due to falling revenue emanating from the global economic recession, and increasing expenditures to tackle the same recession. Bangladesh is most likely to follow the trend, and a record high budget deficit of over 5 percent of GDP has already been anticipated. Implementation of social safety net programs, block allocation for the PPP initiatives, implementation of new salary scale, and supplementary allocation to previously announced stimulus package will add up to this record high budget deficit.

The government is likely to seek foreign sources to finance up to three-fifths of its total budget deficit. The Finance Minister may also increase the duties on luxury imports, target

*Budget documents
should outline
how the
preference of
social responsibility
over profit will
be ensured in the
PPP projects*

¹ An earlier version of this article was published in the Daily Star on 13 June 2009. Available at: <http://www.thedailystar.net/newDesign/news-details.php?nid=92295>.

² See the article on page 34 for more on PPP scheme.

new income tax payers, broaden the tax base for VAT, and bring an end to sectoral tax holidays to reduce the revenue earnings-expenditure gap.

Politics of rice price

Too often Bangladesh's politics circles around the price of rice. During the run up to the last national election, rice price was a highly contested issue. And since the election, the two political parties have exchanged barbs on an alleged promise to bring the rice price to Tk 10 per kg, forgetting how a farmer would survive after selling the crop at such price when the production cost was higher than the current market price. However, the fall in rice price in international markets and subsequent bumper crop in Bangladesh has already brought down the price of rice.

To help the farmers sustain this widening gap between production cost and rice price, a series of suggestions has been made over the past couple of months, including imposing duty on rice import, purchasing the grains directly from the farmers, and increasing government's storage capacity to develop buffer stock. As the country awaits another good harvest of boro, it would be very challenging for the Minister to safeguard the farmers from further decline in price without worsening the inflation scenario.

Election manifestos and budget proposals

It is expected that the first budget of a newly elected government will address its election promises. As the Finance Minister prepares the budget speech, let's revisit the Awami League's election manifesto one more time to see if it resonates with budget proposals.

AL's election manifestos promised that:

- highest budgetary allocation will be given to education, science and information technology sectors;
- power production will be increased to 5,000 megawatt by 2011;
- special emphasis will be placed on expansion of facilities for research in agriculture;
- subsidy for agricultural inputs will be enhanced;
- employment guarantee scheme will gradually be made effective to provide 100 days employment to one youth per family; and
- a project will be undertaken for young men and women with HSC degrees for appointment in the "national service" for two years.

Traditionally, major reforms are initiated during the initial years of an incumbent government, since governments seeking re-election become reluctant to take drastic approaches towards the end of their tenure. The first budget of this Government is being announced at a desperate time when our exports and jobs are threatened by the global economic recession and worsening power shortage. Desperate time calls for desperate measures, and what better time than now for the Finance Minister to take the bold steps to address these concerns?

The first cut should be the deepest.

Surviving the great recession

Jyoti Rahman³

By the time this piece is read, the first budget of the Grand Alliance Government will have been finalised. At the time of writing, it is not clear what the Budget for FY2009-10 entails in terms of policy details. However, macroeconomic conditions and outlook facing our policymakers are relatively well understood.

The Budget will be brought down as the world economy passes through the most turbulent times since the era of silent movies. Pundits are calling the current slump the Great Recession – perhaps not as dire as the Great Depression, but far worse than any recession since.

The IMF's forecasts for the world economy are discussed first in this article. Then the focus shifts to Bangladesh: how have we managed thus far, and what are the forecasts for 2009-10? While Bangladesh has proved remarkably resilient thus far into the recession, a slowdown is nonetheless expected.

More importantly, there are good reasons to think that the world economy will have markedly different contours when this recession ends, and our ability to grow strongly in the post recession world may well require carefully crafted policy support. These are briefly explored in the final section.

World economic outlook

In late 2007, a number of large American and European banks were found to be in difficulty because of exposures to the worsening housing market in the United States. At that time, the cognoscenti view was that such difficulties would, at most, lead to a moderate recession in the US and some other advanced economies.

Then things changed dramatically in September 2008, when a large American bank (Lehman Brothers) failed and the largest American insurance company (AIG) was bailed out by the US government. In a matter of days, credit flows dried up and financial markets worldwide stopped operating as perceived counterparty risks spiked. In a matter of weeks, trillions were lost from global stock markets.

No economy with external links – large or small, rich or poor – was spared. Confidence slumped. Households in the rich world stopped spending. And then the financial crisis hit the docks in the last months of 2008. Industrial production and trade plummeted. The world economy shrank by an annualised rate of 6¼ percent in the last quarter of 2008, and then by a similar magnitude in the first quarter of 2009.

While the crisis started out from the US housing market, the US economy hasn't been the worst hit. That unfortunate fate befell the export dependent rich countries – Japan's GDP has shrunk to its 2003 level, economies of Taiwan, Singapore, and Hong Kong have

While the crisis started out from the US housing market, the US economy hasn't been the worst hit. That unfortunate fate befell the export dependent rich countries

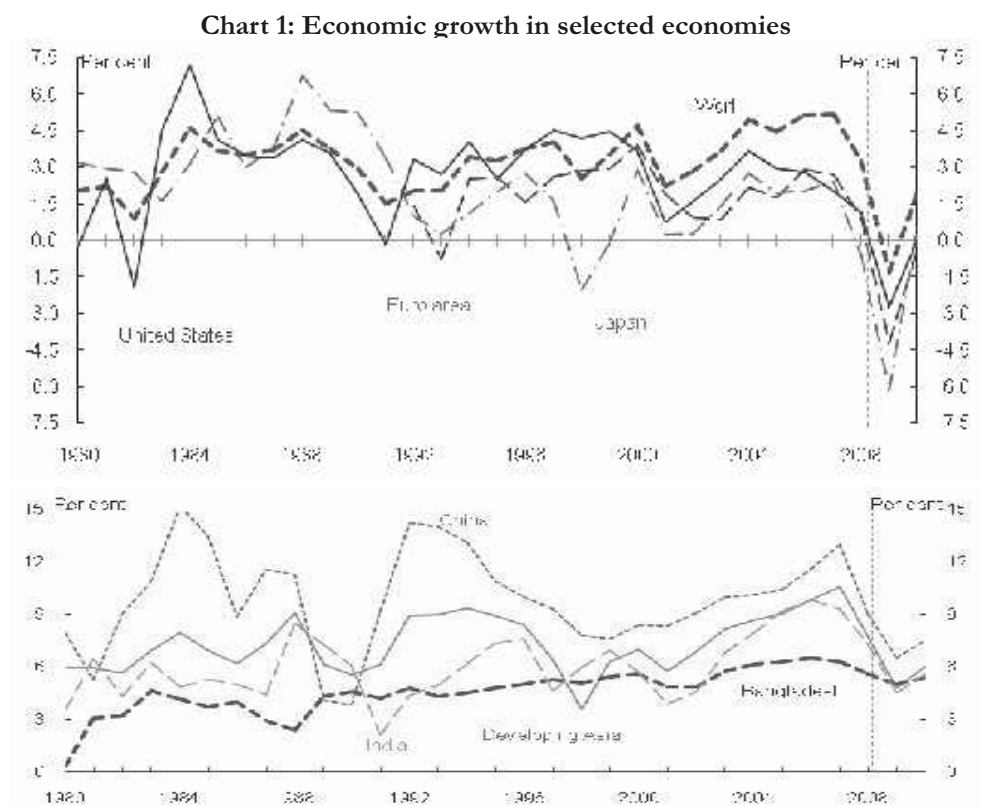
³ An earlier version of this article was published in the June issue of the Forum magazine. Available at: <http://www.thedailystar.net/forum/2009/june/surviving.htm>.

declined by 10 percent or more, similar contractions are being experienced by Germany and Spain, while smaller European economies are shrinking by double digit rates. The developing economies have done slightly better, but only just.

By any reckoning, this has been the sharpest synchronised slowdown the world economy has witnessed since World War II. The IMF forecasts the global GDP to shrink by 1.3 percent in 2009 – the first contraction in the post-war era⁴. Advanced economies are expected to suffer the most – the US is expected to contract by 2.8 percent, the euro area by 4.2 percent, Japan by 6.2 percent.

The developing world will not be immune. China is expected to grow by 6.5 percent in 2009, India by 4.5 percent – both half their 2007 rates. Major South-East Asian economies are collectively expected to record no growth at all this year. Developing Asia is expected to grow by only 4.8 percent, compared with the 10.6 percent recorded in 2007.

Chart 1 shows economic growth in major advanced as well as key Asian economies.



Source: IMF World Economic Outlook, April 2009; forecasts beyond 2008.

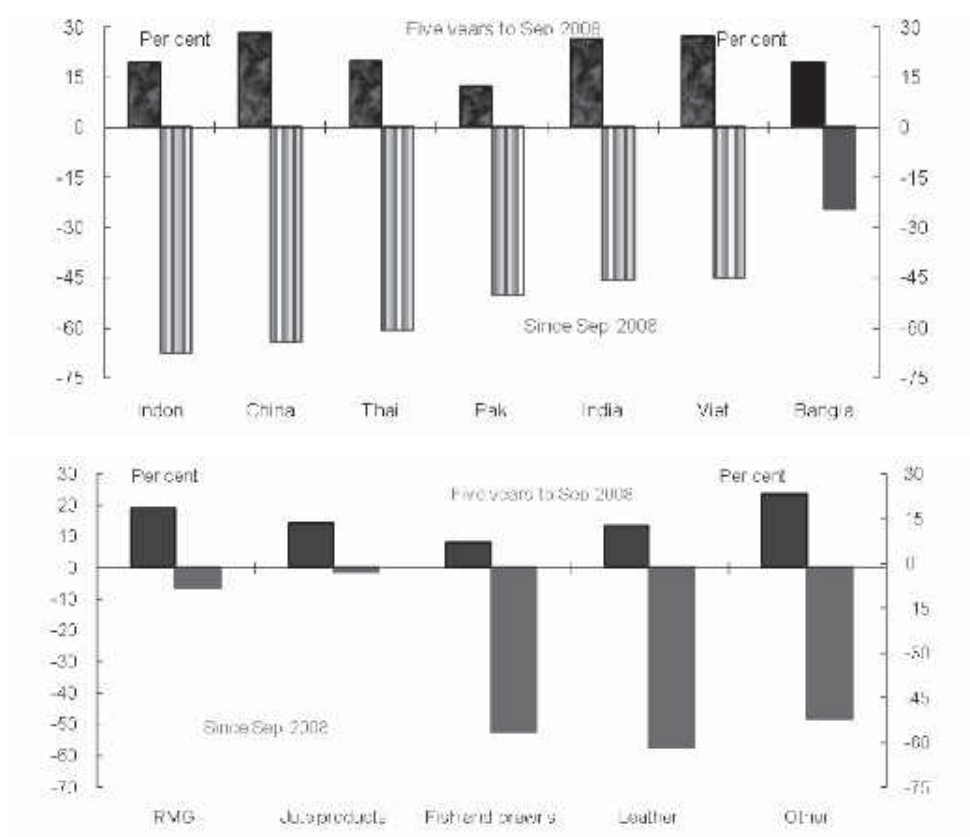
Chart 1 also shows that relative to our neighbours, Bangladesh is not expected to suffer as much. The IMF expects Bangladesh's economy to grow by 5 percent in 2009, a modest slowdown from the 2007 rate of 6.3 percent.

⁵ These forecasts are from the IMF World Economic Outlook, April 2009. Updated forecasts are available at: <http://www.imf.org/external/pubs/ft/weo/2009/update/02/index.htm>.

Bangladesh economic outlook

Indeed, the Bangladesh economy has proved remarkably resilient so far during the Great Recession. At the outset of the recession, exports and remittances were identified as the two main channels through which the global slump could affect Bangladesh. As far as is discernable from data, both are holding up.

Consider exports first. Between September 2008 and February 2009, exports from Bangladesh fell by an annualised rate of less than 4 percent while this is an unwelcome reversal from about 20 percent a year growth witnessed in the recent years, it is still a significantly better performance than 70 percent or so annualised fall in the East Asian region over the same period. Monthly exports figures are, however, highly volatile and often exhibit strong seasonal patterns. To mitigate against this, the data are often averaged over three months. When the smoother data are used, it appears that Bangladesh's exports have fallen, but by nowhere near as much as has been the case for our neighbours (Chart 2a).



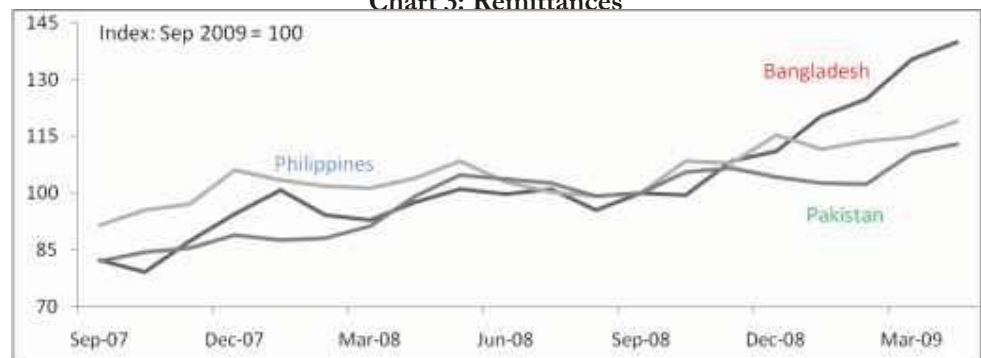
Fish and prawn, leather goods, and other products have driven the fall in export growth (Chart 2b). Ready-made garments (RMG), which account for nearly two-thirds of the country's exports, exhibit a much smaller fall than total exports in the months since the recession entered its most virulent phase. Before the recession hit, there was a lot of discussion about the Bangladeshi RMG sector being relatively less affected because the products are mainly sold in the relatively low-priced end in the rich world, a segment of the

At the outset of the recession, exports and remittances were identified as the two main channels through which the global slump could affect Bangladesh. As far as is discernable from data, both are holding up.

market has not done as bad as the rest of the economy the so-called Wal-Mart Effect, after the American retailer that specialises in cheap consumer items. Results thus far may have validated this thesis.

An even more sanguine picture emerges when we consider remittance. Since September 2008, remittances to Bangladesh have grown by 40 percent far ahead of Pakistan and the Philippines, two other countries that depend on remittances (Chart 3).

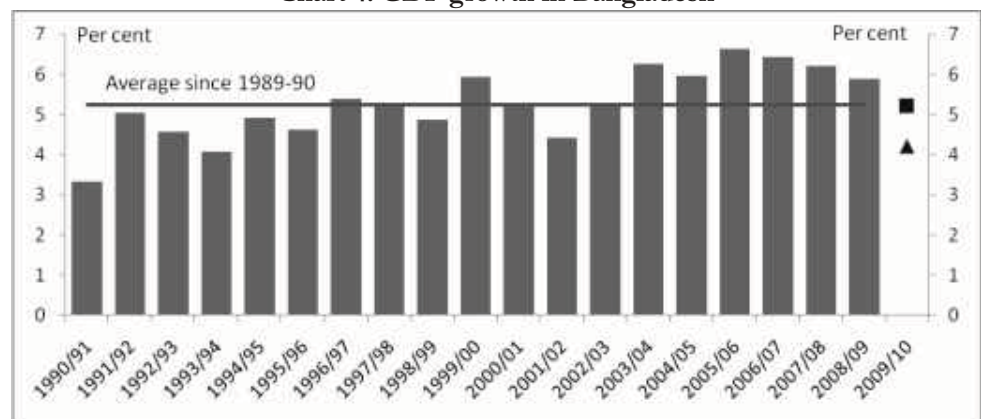
Chart 3: Remittances



Source: CEIC Asia database. Data are three month moving average.

The tenacity of exports and remittances are reflected in the advance estimates of the national accounts, which show that Bangladesh's GDP is estimated to have grown by 5.9 percent in 2008/09. While this is slower than 6¼ percent or so averaged in recent years, this is, indeed, a mild slowdown compared with what is being witnessed around the world.

Chart 4: GDP growth in Bangladesh



Source: Bangladesh Bureau of Statistics, ADB (square), Consensus (triangle).

However, a number of worrying signs are emerging. In recent months, export orders for knitwear have been falling or are being deferred. Given the lag between orders and shipments, exports may be shrinking by a faster pace in the coming months. Buyers are also negotiating for higher discounts, squeezing profit margins. Meanwhile, there are reports of a sharp slowdown in the outflow of migrant workers, suggesting a future slowdown in remittance flows.

Such dark clouds suggest a further slowdown in GDP growth in 2009-10 the question is, by how much? The Asian Development Bank forecasts GDP growth of 5.2 percent in the next fiscal year, while Consensus Economics a collection of private sector forecasters expect growth of 4.2 percent. Chart 4 shows the slowdown in historical context.

The ADB assumes normal weather conditions, and expects buoyant agriculture growth to continue next year. However, both industry and services sectors are expected to grow at a more subdued pace the first reflecting weaker exports sector, the second because of weaker income and remittances growth.

Beyond the recession

Research by the IMF show that synchronised recessions that begin with a financial crisis end with a delayed and weaker recovery process, and quite often potential growth path are marked down in the recession hit economies are marked down. The Great Recession is not likely to be an exception.

The recession has its source in excessive leveraging by the financial sector of the advanced economies. Even when a sense of normalcy returns, advanced economies' banks will not issue as many loans as they did in the pre-recession era. The de-leveraging process will lead to subdued credit creation and capital flows, prohibiting a strong recovery in business investment. This will have flow on effects on jobs and household income in the rich world.

Meanwhile, overly indebted households in a number of advanced economies, faced with tighter credit conditions and a tougher job market, will tighten their belt. This consolidation of household balance sheet will mean a subdued demand profile for exports from the developing world.

There is a risk that demands for the developing world's manufactures may also be hit by rising protectionism in the rich countries. With massive budget deficits and likely double-digit unemployment rates, governments facing re-election in the coming years may well find it easier to hide behind populist protectionism than enact tough fiscal consolidation.

In the post-war era, the most successful development model has been to rely on manufacturing exports to the advanced world, use the income generated from the trade to invest in physical and human capital, and improve living standards. Even without protectionism, the de-leveraging process in the rich world will make this formula less feasible for Bangladesh.

That is, even if Bangladesh survives the Great Recession relatively unscathed, economic development and poverty alleviation in the coming years will require innovative policy approaches. It will be interesting to see how the challenges ahead are reflected in the Budget.

even if Bangladesh survives the Great Recession relatively unscathed, economic development and poverty alleviation in the coming years will require innovative policy approaches.

Part 2

Analysing the National Budget for FY2009-10

Policy paradox and the budget for recession and recovery

Syed Ahamed ⁵

When the manifestos for the 2008 national election were being prepared, the world economy was already in recession and the election promises were linked with the recovery. This must have facilitated the Budget to address the recession and election promises in chorus.

The Budget admits the challenges ahead, forecasting a 5.5 percent GDP growth for 2009-10. But it also aims to change that pessimistic scenario by promoting investment, decentralisation and infrastructural development. The Finance Minister has received largely positive, albeit mixed, responses for various proposals. This article, however, underscores few uncertainties surrounding the Budget proposals.

The policy paradox

In recent year, Bangladesh's economy has been an orphan without a long-term perspective plan, much like a vessel without a compass. The poverty reduction strategy paper (PRSP) has failed to fill the gap of a medium or long-term plan, without which the development promises of annual budgets can easily get off course.

The Finance Minister has proposed that the PRSP will be withdrawn by 2011 to be replaced by a five-year medium term plan for 2010-2015, and a long-term perspective plan for 2010-2021.

The Minister has also announced that the five-year plan will influence annual budget objectives, while the current PRSP will affect the budget for the intervening period. While this will end the disappointing "policy-paradox," the transition period, however, may affect this year's Budget proposals. Since both the FYP and the long-term perspective plans are under preparation, how will this budget, which has already been announced, follow those yet to come?

Recycling black money

The Finance Minister has made a moral compromise by offering a three-year amnesty to "recycle" (we have reservation calling it 'whitening') black money into the mainstream economy without any question.

In a time of global recession, such decisions could merit some justification if it was at all an effective approach. But earlier attempts at such schemes have been hardly successful. While this kind of policy provides huge disincentive for the genuine tax payers, the major problem of this year's proposal is its duration⁶. In the past, there was an uncertainty about the duration of the scheme. But now that the scheme has been announced for the next three years, otherwise law-abiding tax payers will now be encouraged to evade 25 percent

Bangladesh is a passive victim of the global recession and cannot blindly follow the steps of developed economies. However, the Keynes model can create an opportunity for Bangladesh to finally decentralise the economy.

⁵ An earlier version of this article was published in the in the Daily Star on 15 June 15, 2009. Available at: <http://www.thedailystar.net/newDesign/story-details.php?nid=275>.

⁶ Following the criticism, the Finance Minister has subsequently modified these policies in the final bill and reduced the duration of the recycling opportunity from three years to one year only.

regular income tax during the next few years, and pay the minimum 10 percent penalty under this scheme.

The operations of Central Intelligence Cell of the National Board of Revenue and Anti-Money Laundering Department of the Bangladesh Bank should be strengthened to keep pressure on the tax evaders to recycle their black money now and discourage future tax evasions.

Are we all Keynesians now?

At a time of recession, John Keynes suggested that economic policy should increase the aggregate demand through consumption, investment, and government purchases. That's why major economies around the world are announcing big budgets and starting unprecedented investment programmes. Bangladesh's National Budget for 2009-10 seems to have appreciated the Keynesian need for investment.

Admittedly, Bangladesh is a passive victim of the global recession and cannot blindly follow the steps of developed economies. However, the Keynes model can create an opportunity for Bangladesh to finally decentralise the economy.

In the proposed annual development program of Tk 305 billion, 22.1 percent has been allocated to the local government, 14 percent for the power-energy and 15.7 percent for communication, including roads, highways and waterways.

In addition, an Infrastructure Investment Fund of Tk 21 billion and an employment generation programme for the hardcore poor have been announced. These programmes can be used to build infrastructures at the local level, which in turn may assist decentralising the economy.

The double-trouble

The proposed budget has twin-risks in both its revenue management and in its expenditure plans for development programmes.

William Vickrey, a Canadian economics Nobel laureate, argued: "Budget deficits do not in themselves produce inflation, nor does a balanced budget assure a stable price level."

Bangladesh's national budget aims to finance two-fifths of its Tk 340 billion deficits through foreign financing. Securing that money might become uncertain amid the global economic downturn. And poor management of deficit financing may endanger the whole purpose of a Keynesian budget by increasing inflation and reducing private investment.

Then again, some expenditure programs, based on block allocations, may also create uncertainties. The government should remain cautious about these allocations for social safety net programmes, which often remain unused or gets wasted in corruption. In the words of Benjamin Franklin "beware of these little expenses; a small leak can sink a great ship."

The long view

Jyoti Rahman⁷

This article reviews the National Budget for FY2009-10 the third Awami League Government's first one focussing on three issues.

First discussed are the economic growth projections. Contrary to some commentary that the budget forecasts are "too conservative" or "not ambitious enough," 5.5 percent is, on balance, a prudent growth forecast for 2009-10.

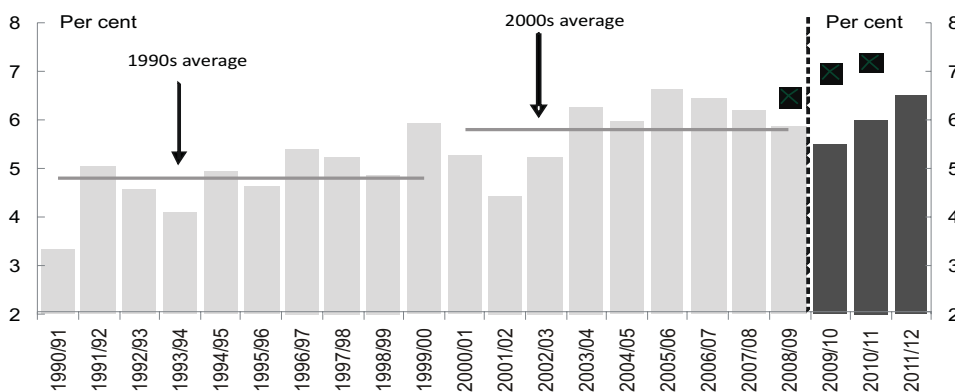
Then the fiscal outlook is discussed. While much is said about the implementation of the Government's development expenditure targets, implementation of its medium term revenue enhancement measures deserves greater attention.

The final section analyses a few medium term growth issues that are alluded to in the Budget. How these issues are resolved will perhaps prove lot more important than any specific measures announced on 11 June.

A steady boat

Buffeted by a number of shocks political uncertainty, natural disasters, global commodity price spike, and now the global recession Bangladesh's economy has proved surprisingly resilient in recent years, and the Budget forecasts only a modest easing in growth in 2009-10 (Chart 1).

Chart 1: Economic growth



Source: CEIC Asia database, Budget. Red bars are 2009-10 forecasts. Green squares are 2008-09 forecasts.

On a sectoral basis, agriculture is expected to contribute about 1 percentage point to forecast growth. Agriculture makes up slightly over a fifth of GDP. To contribute 1 percentage point to 5.5 percent growth, agriculture will need to grow by about 4.8 percent in 2009-10.

Let's put this in context. Agriculture is a volatile sector, with annual growth in the past

Buffeted by a number of shocks political uncertainty, natural disasters, global commodity price spike, and now the global recession Bangladesh's economy has proved surprisingly resilient in recent years

⁷ An earlier version of this article was published in the July issue of the Forum magazine. Available at: <http://www.thedailystar.net/forum/2009/july/budget.htm>.

couple of decades ranging from 0.3 percent to 7.4 percent. In the past four years, the sector has grown at an annual rate of 4.3 percent, while it grew at 4.9 percent a year under the second Awami League Government.

This suggests that a 4.8 percent growth rate for agriculture may not be unreasonable. Of course, there are risks – natural disaster being the most obvious one. The forecast explicitly assumes improved agricultural productivity, diversification of crop production, and improved disaster management capacity.

The industry sector is expected to contribute about 1.75 percentage points to 2009-10 GDP growth. This translates into a forecast of about 5.9 percent growth for the sector, the same rate achieved in 2008-09, but slower than 7.8 percent achieved annually in the past half decade. Indeed, if realised, this will be the most prolonged slowdown in industry growth since the early 1990s.

It's obvious that the slowdown in the industry sector has its roots in the global recession. About three-fifths of the industry sector is manufacturing, which grew by 5.9 percent in 2007-08 – a sharp slowdown from the 8.6 percent a year achieved in the previous half decade. Undoubtedly, through an export slump, it is manufacturing that has borne the brunt of the global recession. But, compared with sharp falls in industrial production witnessed around the world – the biggest contractions since the 1930s in many countries – our manufacturing sector seems to have held up reasonably well.

If the rest of the industry sector (30 percent construction, the rest nearly evenly split between mining and utilities) grows at the average rates recorded in the past two decades, manufacturing will need to grow by about 5 percent for the whole sector to achieve the Budget forecast. Given the severity of the global recession, risks to the manufacturing sector seem to be firmly weighed to the downside.

On the other hand, there may well be upside to construction, which has grown at 5.7 percent a year since 2006-07, compared with an annual growth of 8.4 percent in the previous decade. The recent construction slowdown has been attributed to political uncertainty and associated low confidence, as well as high costs of building materials. To the extent that both these factors have dissipated, a construction boom may well be on the cards. Construction could get further fillip from various infrastructure investments being unrolled.

Finally, the services sector is forecast to contribute about 2.75 percentage points to economic growth. This translates to an implied sectoral growth forecast of 5.5 percent in 2009-10 – a percentage point slowdown from the average over the past half decade, but on par with what was achieved in the previous half decade.

Retail and wholesale trade, as well as transport and communication services, have driven the services boom during the past half decade. These services, indeed the entire services sector, have benefited from high remittance inflows over this period. Defying expectations, remittance inflows have held up thus far into the recession. While the Budget forecasts assume renewed remittance inflows, should remittances dip, the service sectors will be hurt (a remittance slowdown could hurt construction too).

Social services – health, education, community services – have also contributed to the services boom. With a favourable business environment and various government programmes supporting them, these services should see robust growth, partly off-setting potential negative impacts of the global recession.

From the GDP (expenditure) perspective, the economic slowdown is driven by an investment downturn. Investment-to-GDP ratio is forecast to dip in 2009-10, implying investment growth will be at half the rate recorded in 2008-09. The predicted investment slowdown has been questioned by some commentators. However, such a slowdown would hardly be unusual in the current global economic climate.

Possibly more at risk are the export forecasts. Exports are estimated to have grown by 12 percent in 2008-09, down from nearly 16 percent the previous year. Exports are projected to grow by 12.5 percent in 2009-10, and then by 18 percent a year in the following two years. As discussed in the final section below, there is reason to be sceptical about this medium-term outlook for exports.

In summary then, the forecast slowdown in growth in 2009-10 is, on balance, prudent.

There are, of course, risks around this forecast⁸. In addition to the global recession, the most significant economy-wide risk to the forecast is perhaps energy shortage. The Budget explicitly assumes "increased private sector investment in response to measures to eliminate power and gas shortage..."

This assumption, plus the election pledges for the energy sector, provides benchmarks against which the Government's performance should be assessed.

Enter taxman

A budget deficit of 5 percent of GDP is forecast for 2009-10. To put this in context, the budget deficit is estimated to have been 4.1 percent of GDP in 2008-09, while in the previous year, the army-backed regime presided over a deficit of 5.1 percent of GDP. At 4.7 percent of GDP in 2011-12, the deficit is expected to continue to exceed the Government's target of 4 percent of GDP over the forecasting horizon.

Higher development expenditure appears to be the major reason why the budget deficit is rising. In 2008-09, development expenditure is estimated to have been 3.7 percent of GDP. This is projected to rise by a percentage point by 2011-12. Non-development expenditure, on the other hand, is expected to dip by 0.4 of a percentage point relative to GDP over the same period.

Much has been said about the failure to implement ambitious Budget targets. Particularly, development programmes seem to repeatedly miss the target. Two points need to be made here.

First, a major impediment to full implementation of development programmes is the lack of local government authority over, and responsibility for, development work⁹. The Government seems to betray a degree of bipolarity when it comes to local empowerment. On the one hand, lofty promises reiterate its commitment to strong local government. On the other hand, its actions – power grabbing by the MPs in local affairs – belie that commitment. Failure to resolve this internal contradiction will not only affect development expenditure, but in time could also engulf the government in a political crisis.

Second, it was not always the case that development expenditure missed targets. Indeed, under the stewardship of SAMS Kibria, development programmes were implemented in a better manner than has been the case since.

Moving from implementation to financing, how does the Government propose to pay for

⁸ The article on [page 32](#) discusses the risks in detail.

⁹ See the two articles on implementation and local democracy on [page 29](#) and [page 38](#)

In addition to the global recession, the most significant economy-wide risk to the forecast is perhaps energy shortage

the additional development expenditure?

Revenues have been marked down in the Budget because of slower GDP, imports, and remittance growth. Nonetheless, at around 11.5 percent revenue-to-GDP ratio is projected to be higher throughout the forecast years than in the recent past in 2006-07 revenues were only 10.2 percent of GDP.

Again, there are implementation concerns it's easier to promise that revenue collection will rise than to implement it. Nonetheless, it is possible to increase revenue collection. Tax revenue relative to GDP has already risen by 1 percentage point since 2006-07. Potentially bigger risks to revenue growth are from slower GDP, import, and remittances growth.

Even if revenue were to grow as forecast, it will still not be enough to arrest the rise in budget deficit. Two-fifths of the deficit is expected to be financed from foreign borrowing in 2009-10, rising to over half by 2011-12. The concern over the foreign borrowing is not so much about the cost of debt-servicing, which appears to be modest by international standards. Rather, it is the strings and conditionalities that may come with the debt that should worry us.

To be sure, conditionalities suggested by donors and international agencies can anchor credibility of commitments to difficult but needed reforms. However, for this to happen, such conditionalities have to be carefully negotiated. And therein lies the test of leadership for the Finance Minister and his officials.

Should foreign borrowing prove too dear whether in financial terms or in terms of political economic costs the deficit will have to be financed from domestic sources. As it is, the Budget forecasts that nearly half of the deficit will be financed by bank borrowing in 2009-10. Bangladesh Bank will have to be extremely careful in the coming period about not monetising the deficit and fuelling inflation in the process.

The appointment of someone closely linked to the political side of the ruling party's election campaign to the governorship of the central bank does not bode well for the autonomy of that institution¹⁰. Governor Atiur Rahman will have an opportunity to prove the sceptics wrong if he can resist printing money to pay for the debt (as an aside, a more immediate risk of inflation may well be commodity prices, which could start rising rapidly as the Chinese economy recovers).

Continued budget deficit is, of course, not sustainable over the long term, and there is no alternative to raising revenue. The government seems well aware of this. The Budget acknowledges that revenue-to-GDP ratio is much lower in Bangladesh than in neighbouring countries. Over the medium term, the Government plans to raise revenue by a combination of: expanding tax coverage; rationalising the tax system; decentralising the collection operations; and institutional reforms separating tax policy from tax administration.

These ideas may not have political glamour but, if properly followed through, they could significantly boost public finances and our ability to invest for growth and development. As such, the Government's performance on this front should be closely monitored. Of course, "political compromises" such as the "black money deal" raise concerns about the credibility of the Government's commitment on tax reform.

¹⁰ For a detailed discussion, see: <http://jrahman.wordpress.com/2009/06/23/the-year-of-living-dangerously-on-the-selection-of-the-bank-governor-and-his-challenges/>

Growing pains

To recap then, the economic growth forecasts underpinning the Budget are rather prudent. While there are serious concerns about implementation of various expenditure and revenue measures, these challenges are not insurmountable. And finally, the Government should be held to account for its promise to reform the tax system over the medium term so that ambitious development programs can become sustainable. It is the medium term growth prospects that this section focuses on.

Recall from above that an export boom is forecast for 2010-11 and 2011-12.

Is this sensible?

This forecast appears to be rather rosy if one considers that Bangladesh's major export markets – the United States, the United Kingdom, the euro area – are likely to remain mired in a sluggish recovery over these years. True, our ready-made garments and knitwear, servicing the budget end of the market, have proved resilient going into the recession. But there is no reason to think that the so-called Wal-Mart effect will underpin an exports boom.

That said, there is an interesting assumption that may explain the forecast export revival. The economic growth, and by extension fiscal forecasts, rest on a number of medium term assumptions. One of them is: "sustained high growth rates in exports through exploitation of new market opportunities and export market diversification."

It's not clear what exactly "new market opportunities" and "export market diversification" refer to. However, the giant economies of China and India – among the first to recover from the global slump – appear to be natural candidates. Rightly or not, there is a perception that the Government enjoys a special relationship with India, while the Chinese alliance has been a constant in our foreign policy since the 1970s. It is about time that the Government cashes in those friendship chips so that Bangladeshi goods can enter these massive markets.

In addition to exports diversification, there is a lot of emphasis on small- and medium-sized enterprises being an engine of economic activities. While this is a welcome focus, many impediments – from infrastructure bottleneck at the broadest level to access to finance, market, business skills, and supply network at the micro level – need to be addressed for the SMEs to be serious driver of sustainable growth.

And, finally, the budget assumes "greater efficiency and technological progress across the economy, partly driven by increased investment in information and communication technology."

Political gimmickry such as the term "Digital Bangladesh" notwithstanding, a lot could be done to streamline service provision and reduce transaction costs, thereby enhancing economy-wide productivity growth that could sustain a growth pick up into the next decade. However, measures such as digitising the land records that could underpin this growth spur will require significant political courage. Meanwhile, specific "digital policies" suggested in this Budget betray a sense of unpreparedness on the Government's part¹¹.

In the long term, how the Government steps up to these challenges will prove lot more important than any specific measures contained in this budget. As they put the Budget behind them and start working on the five-year plan, the Finance Minister, the Planning Minister, and their officials, should keep that in mind.

*Political gimmickry
such as the term
"Digital Bangladesh"
notwithstanding, a lot
could be done to
streamline service
provision and reduce
transaction costs,
thereby enhancing
economy-wide
productivity growth
that could sustain a
growth pick up into the
next decade.*

*These ideas may not
have political glamour
but, if properly
followed through, they
could significantly boost
public finances and our
ability to invest for
growth and
development*

¹¹ see the next article for an overall analysis of the budget.

The good, the bad, and the uncertain

Syed Ahamed¹²

The Budget for the fiscal year 2009-10 (FY2010) has attracted a mixed response. It has been termed as bold as well as exaggerated, conservative as well as ambitious, and challenging as well as full of rhetoric by different quarters. While pro-poor allocations and taxation have been appreciated, controversial proposals such as the black money recycling scheme invited widespread criticism. While the Budget has taken some traditional stances such as block allocations and high government borrowing, it has also introduced some new approaches such as the public private partnership and economic decentralisation.

This article will analyse some good, bad and uncertain issues of the Budget by exploring different Budget proposals and post-Budget discussions.

The good

Growth recovery

Bangladesh's GDP growth slowed down by 0.31 of a percentage point during FY2009 (from 6.19 percent achieved during FY2008) owing to multiple disruptions, political uncertainties and consequential low public investment, as well as the global recession. While the global recession seems to be bottoming out, its delayed impact may continue to hurt Bangladesh's growth prospects during the coming quarters. Keeping in mind the slowing down of demand in our exporting markets, performance of neighbouring economies, and projections of ADB/IMF, any growth figure over 5.5 percent in FY2010 would suggest a resistance to further slip, and a 6 percent growth would mean a good resurgence. Hence, while the growth target for FY2010 set at 5.5 to 6 percent may appear unadventurous, attaining this target will be quite an adventure itself¹³.

To achieve this growth target, the Government's forecast of investment efficiency, measured by incremental capital-output ratio (ICOR), may seem odd. It is predicted that the ICOR will increase in 2010, meaning more investment will be required to achieve a similar level of production. There are possibly two explanations behind this projected drop in investment efficiency – the recession-recovery dynamics, and the lagged response of rural investment.

During a recession, the private sector is typically reluctant to invest and governments often adopt expansionary fiscal stance to revive GDP growth. As a result, the 'projected' ICOR appears low in the context of a modest GDP target. Once stimulus packages and public investment programmes are put into effect, the private sector recovers and the actual investment efficiency looks better in the backdrop of a moderate growth attainment and (downward) revised public investment figures. This may well be the case for Bangladesh in 2009-10.

In addition, budget allocations, which shifted focus from urban-industrialisation to economic devolution and rural development, may reduce the investment efficiency in the

During a recession, the private sector is typically reluctant to invest and governments often adopt expansionary fiscal stance to revive GDP growth. As a result, the 'projected' ICOR appears low in the context of a modest GDP target.

¹² An earlier version of this article was published in the July issue of the Forum magazine. Available at: <http://www.thedailystar.net/forum/2009/july/good.htm>.

¹³ See articles on page 19 and 32 for more on Bangladesh's growth outlook.

short-run as rural development shows a delayed (but sustained) response to investment. A study on China's economic growth between 1978 and 2000 (Journal of Asian Economics, 14, 2003) shows that in the long run, investment efficiency can be reaped through rural industrialisation and proliferation of small firms in non-state sector. The current Budget seems to have addressed this stance. Hence, an annual fall in projected ICOR can be ignored if economic devolution can be ensured and a reasonable growth rate is achieved in the coming fiscal years.

Economic devolution

The Budget, in allocation and in principle, has aimed to promote economic devolution by advancing the local bodies to set and administer their own economic goals. Development of the regulatory framework is already under preparation as the Upazila Parishad Act has been passed in the Parliament, the Pourashava Act is awaiting parliamentary approval, the Union Parishad Act has secured cabinet approval, and the City Corporation Act has been tabled. The Finance Minister has promised to introduce a district level budget for FY2011, initially for one district in each division. Ministries and divisions have been asked to create a Budget and Planning Wing or Branch within their organisational structure for faster approval and effective monitoring of projects.

On the expenditure side, subsidy for fertiliser and agricultural inputs has been reduced by 37.7 percent from last year's revised Budget. Since the price of different fertilisers declined by 30 to 70 percent in the world market over the past several months, the proposed subsidy seems reasonable for the new fiscal year. To facilitate multiple crop production and to expand the cultivable land by improving drainage system in the haor areas, Tk 4000 crore has been allocated. In addition, Tk 280 crore and Tk 185 crore have been allocated for development of high yielding variety seeds and for agricultural research and agricultural rehabilitation assistance. The Budget has recapitalised the micro credit institutions (Krishi Banks and Karmashangstan Bank), increased the fund for housing and SME, and has allocated Tk 3,575 crore for investment in the construction and reconstruction of roads and bridges under LGED.

While the proposed decentralisation of police administration seems pertinent, the setting up of a Public Representative Board to oversee police forces may raise concerns and should be implemented with transparency to stop unwarranted politicisation.

Against the above Budgetary measures and aims, there are potential worries about economic devolution. Recently, Bangladesh's decentralisation dilemma has taken a new turn. We have moved from the traditional conflict between administrative and political representatives. Now the conflict is between central and local political representatives that is, between MPs and upazila chairpersons. The major constitutional duty of an MP is to work on policy issues in the legislature, not handling the development programmes. However, given the socio-political context of the country, if the government wants to provide some spending power to the MPs, this should be done under transparent framework without undermining the duties of the upazila representatives¹⁴.

Pro-growth, pro-poor revenue

The Budget proposes to widen the tax net instead of increasing tax rates, increase tax on luxury consumptions while reducing tax on essential and production related items, and offers tax reduction to specific industries while withdrawing the largely misused tax-holiday scheme. Overall, the changes in duty rates and duty structures seem pro-poor and pro-growth.

¹⁴ The article on page 38 analyses this issue of decentralisation in detail.

The tax rate for deductions of income tax at source against capital gain from the sale of land has been slashed from 5 percent to 2 percent in urban areas, whereas a further reduction to 1 percent has been proposed for other areas. It has also reduced the income tax burden on senior citizens by lowering the age bar from 70 years to 65 years. While major food items and fertilisers will continue to enjoy the zero-rate tax, additional duty exemption has been offered for the import of phosphoric acid used for fertiliser production. Duty rate on books has been reduced from 12 percent to 5 percent. More importantly, the Budget has reduced the duty on basic raw materials from 7 percent to 5 percent, which will stimulate the local industries. The Budget also increased the threshold level for VAT from Tk 24 lakh to Tk 40 lakh to encourage small and medium enterprises. The threshold level for imposing excise duty on bank deposits also increased from Tk 10,000 to Tk 20,000 to encourage small savers.

On the other hand, the Budget imposed progressive tax on personal cars and increased supplementary duty on the imports of luxury vehicles¹⁵. In addition, 5 percent regulatory duty has been imposed on luxury items falling under 25 percent slab of duty. It increased the supplementary duty on air-conditioners and imposed 25 percent customs duty on mobile phone sets on an 'ad valorem' basis, which will increase the cost of expensive mobile phone sets. Plus, a reduction in corporate tax rate for mobile phone operators has been offered with a condition that they will enlist in the stock exchange as a publicly traded company.

The bad

*Recycling black money*¹⁶

The Budget has renewed the debate surrounding the definition and importance of black money in the economy. The proponents of this black money recycling scheme are now making a distinction between illegally and legally earned un-taxed money by terming them black money and undeclared money. The opponents of the scheme however disagree with such differentiation and initially demanded cancellation of the scheme altogether.

The black money recycling proposal has overshadowed the post-Budget discussions, not only on moral grounds, but predominantly on an economic standpoint. Such schemes have never been successful in the past in attracting investment and only created new avenues for tax-dodgers who regularised more black money by paying less tax by showing exaggerated investment programmes. Since the penalty is only 10 percent, compared to the 25 percent regular tax, the proposed scheme will encourage the otherwise honest tax payers to 'paint' their white money black to get additional tax-cuts.

The FBCCI reaffirmed their position on black money and demanded that only legally earned 'undeclared money' should be allowed into investment. The 'no question asked' clause of the scheme should then be withdrawn to scrutinise the sources of the money and Central Intelligence Cell (of the National Board of Revenue) and Anti-Money Laundering Department (of the Bangladesh Bank) should be part of this inspection process. Given the failure of previous such schemes and the uncertainty of its prolonged duration, the Government should rethink the proposed scheme.

However, to address the lack of investment in power and infrastructure, the Government

*Bangladesh's
decentralisation
dilemma has taken a
new turn. We have
moved from the
traditional conflict
between administrative
and political
representatives. Now
the conflict is between
central and local
political representatives
that is, between MPs
and upazila
chairpersons.*

¹⁵ The final budget for the FY2009-10 set 30 percent duty on the imports of cars up to 1500 cc though a 45 percent duty was proposed in the budget. The duty for 1501cc to 2000cc, 2001cc to 2750cc and 2750cc to 4000cc remained unchanged at 100 percent, 250 percent and 350 percent respectively. However, import duty for cars over 4000cc has been increased from 350 percent to 500 percent.

¹⁶ The Finance Minister has subsequently modified these policies significantly.

a consortium could commit an amount of previously undisclosed money to invest in a specific project related to power or infrastructure. The Government will then scrutinise the sources of the money and if clean, will allow the money to be invested

may consider specific project proposals on a case-by-case basis. In this case, a consortium could commit an amount of previously undisclosed money to invest in a specific project related to power or infrastructure. The Government will then scrutinise the sources of the money and if clean, will allow the money to be invested in the project after due penalty.

Disclosed budget

For anyone wondering whether the revelation of Budget details before the due date was a leak or a means of 'testing the water before swimming', the Finance Minister has the answer: it is both. While there were some unintentional leaks of Budget documents at the Finance Ministry, the Minister himself intentionally revealed much of the proposals before the Budget day to watch public and media response. He acknowledged that the feedback he gained through such revelation helped him formulate the financial plan.

Though one might condemn the stance as an informal mean to minimise post-Budget criticism, a well-organised budget consultation can reinforce democratic responsiveness too. After all, the Budget of the Republic is an open document and some organised revelation during pre-Budget consultations can be used to better reflect public demands and expert opinions. After the announcement of the last financial year's stimulus package, we have seen the Finance Minister changing positions in response to demands from different stakeholder groups. We have witnessed how the Minister has been readjusting on black money recycling scheme amid criticism. If it is responsiveness not hesitance then pre-budget revelation of proposals and following reactions are good for the Budget. However, to limit future confusion, a formal approach towards pre-Budget consultation and revelation should be put in place.

Unspecified allocations

Block allocation is an obscure area in Bangladesh's budget. It is essential to have some block allocation in the budget for uncertain expenditures such as natural calamities, for proposed programmes that are still under preparation (for example, PPP budget, and salary increase). But block allocations often cause double jeopardy by allowing corruption when spent and by stagnating development expenditures when kept idle. Unwarranted expenditures are often observed in programmes where block allocations are made without proper budgeting. On the other hand, many development programmes based on block allocations remain just political rhetoric and never see any release of funds. Hence, disproportionate presence of block allocation in the current National Budget makes us uncomfortable.

A large amount of this year's development and revenue Budget has been kept as block allocation. Block allocation for unexpected non-development expenditure increased from Tk 800 crore in FY2009 (of which only Tk 183 crore was spent) to TK 900 crore, while a whopping TK 3,388 crore of block allocation has been kept for the new pay scale. An allocation of Tk 5,000 crore has been kept in the budget to continue the previously announced stimulus package. The LGRD ministry also proposed to keep Tk 5,000 crore as block allocation. An amount of Tk 2,200 crore is set as block allocation to aid the much-discussed public-private partnership endeavour. In addition, most of the social safety net and rural development programmes have been announced based on block allocations.

The cancellation of a previous plan to offer block allocations to MPs for development is a welcome decision. The government should now take immediate steps to set up modi operandi, monitoring mechanism and project specific budget for the remaining programmes, which have been proposed under block allocations.

The uncertain

Deficit financing

As the Finance Minister has admitted, financing and implementation of the Budget will be its biggest challenge. The low fiscal capacity and high fiscal need to implement the Budget will create a 'fiscal stress' in the economy. The budget deficit now stands at Tk 34,358 crore or 5 percent of the GDP (almost a percent of GDP higher than the previous year's revised deficit).

If the global recession and slowing down of private investment hamper the achievement of revenue target (set at Tk 79,461 crore), the deficit scenario will turn dreadful. Since import duties constitute nearly 42 percent of the total tax revenue, a decline of duties on imports as a consequence of the fall in global commodity prices may particularly jeopardise the revenue collection effort. Provisional statistics suggest a sharp fall in trade related revenue earnings during FY2009 the collection of import duties fell short of target by 11.9 percent.

The expansionary fiscal stance may also cause problems for the monetary sector if the government resorts to bank borrowing to finance its deficit. This may imperil the private sector investment either by increasing the demand for loan and thus increasing the interest rate, or by squeezing the share of private sector borrowing from the banking system. Securing foreign financing will be critical to keep the local funds available for the private sector. However, the global economic recession may turn that option all the more uncertain. Even successful financing of such a large deficit may cause long-term fiscal stress by increasing the interest payments.

*Public Private Partnerships*¹⁷

The much-discussed public private partnership in the National Budget has created some opportunity and uncertainty at the same time. As discussed in the article on PPP below, the scheme encourages off-budget financing by private sectors to meet growing public debt and support developmental needs of the country. However, this opportunity is eclipsed by the lack of a legal and regulatory mechanism.

The Budget proposes to administer the PPP projects under the Private Sector Infrastructure Guidelines, which was prepared by the Prime Minister's Office in 2004. A closer look at that document suggests that the Guideline is not comprehensive enough to govern the complex mechanism of PPP projects. For instance, the Guideline suggests forfeiting the tender security in case private partners fail to execute a contract, but it does not explain how the risks and consequences of such failure will be shared between government and private partners. That's why global experience of such scheme shows that most successful PPP projects are managed under a legal regulatory mechanism, not under executive guideline.

PPP is a synergy, not privatisation or deregulation. To ensure transparency and accountability of PPP contracts, and distribute the risks, resources and rewards among the public and private partners, setting up of an appropriate legal framework is required.

The expansionary fiscal stance may also cause problems for the monetary sector if the government resorts to bank borrowing to finance its deficit. This may imperil the private sector investment either by increasing the demand for loan and thus increasing the interest rate, or by squeezing the share of private sector borrowing from the banking system.

¹⁷ For detailed analysis of PPP budget see the article on page 34

The devil is in implementation

Asif Saleh ¹⁸

The 2009-10 Budget has received much discussion. The reality, though, is that even the best of budgets and policy initiatives can fail due to issues beyond the control of the Finance Minister. The devil will not be in the details, but in implementation. So it's important to get the potential road-blocks identified.

Order, order, order

The Government has to do considerable amount of work in bringing back people's faith in our judicial system. At least this was part of this Government's election promises. The ripple effect of this lack of confidence is reflected in the economy through buoyancy and morale of businesses, investors, and the citizenry at large.

Citizens who feel "there is no justice" and feel unsecured in the country will naturally be hesitant in saving or turning the savings into investment. Our domestic saving has been stagnant at around 20 percent of GDP during the last five years while total investment slowed down marginally.

When both local and foreign businesses express that there is no legal infrastructure to support the investment they make in this country, promoting the proposed public-private partnership will be even harder.

Notwithstanding the Government's general positive approval ratings, it is getting failing grades in maintaining law and order. Given the dismal 2001 election performance which was squarely blamed on degrading law and order situation, the Awami League should not need a reminder that even the best budget in the world will not mean much unless the trend is reversed on law and order.

Demystifying *amlatonro*

To implement the proposals of the announced Budget, the role of an efficient bureaucracy is undeniable. So the relationship and understanding between the political leadership (who makes the budget) and the public servants (who implement it) has to improve. And a guaranteed way to jeopardise the relationship is to appoint and promote on the basis of party loyalty rather than qualification.

It's not enough to just criticize the present status quo as inefficient and corrupt, as the finance minister did a few weeks ago in a pre-budget meeting. Rather one should also recognise that the kind of "people-oriented" public service that the Finance Minister wants to see has hardly been rewarded by various past governments. Should this Government also decide to award high level government posts (both in bureaucracy and in semi-government institutions) as political patronage and cast a blind eye towards efficiency and competence, disenchantment is bound to spread.

*Given the dismal
2001 election
performance which was
squarely blamed on
degrading law and
order situation, the
Awami League should
not need a reminder
that even the best
budget in the world
will not mean much
unless the trend is
reversed on law and
order.*

¹⁸ An earlier version of this article was published in the in the Daily Star on 12 June, 2009. Available at: <http://www.thedailystar.net/newDesign/news-details.php?nid=92177>.

Understandably, the MPs want some financial muscle to show their clout. But it should not be done through curtailing the local leader's power

Decentralisation

In the election manifesto, the AL promised to make each union the hub of development and administration and each upazila the centre of industrial growth. However, the recent changes giving MPs the power to vet each decision made by locally elected leaders are directly contrary to the spirit of the manifesto pledges¹⁹. At the least, they are bound to create conflicts, and such conflicts may well doom any development effort.

Understandably, the MPs want some financial muscle to show their clout. But it should not be done through curtailing the local leader's power but through creating a transparent legal framework where an MP can have jurisdiction over allocation over some funds in his/her constituency. The social safety net programs announced in the budget for rural and agricultural development and for the creation of new jobs at the local level will not be successful without strong local leadership.

Decentralised industrial growth

Similar to development, the focus towards industrial growth needs be decentralised as well. It needs to focus on creating special economic zones outside Dhaka. There is also a false sense of satisfaction into thinking that by removing the barriers of access to finance, local small and medium industries will thrive. Without the infrastructure, access to markets, focused market oriented approach and some level of hand holding, the small and medium sector industries in various sectors will not be able to realise its full potential.

Regulatory reform

Significant policy reform is needed in our regulatory framework to implement most of the proposals made in yesterday's budget. While the business lobby group managed to get some of their recommendations through the Better Business Forum, voices of the small and local entrepreneurs remains mostly unheard. The development projects of the budget will do little to reduce poverty and inequality in the society if the regulatory reform of land, judiciary and administration remains unresolved,

While having a development budget supported by the political will is important, it is equally important to identify the institutional bottlenecks and impediments that will make it difficult to implement these budget proposals. We hope this year's Budget will be complemented with subsequent initiatives to remove these obstacles.

¹⁹ See the article on page 10 and 39 for analysis on AL's election pledges.

Part 3

Analysis of the National Budget: Selected Issues

Risks to the economic outlook

Jyoti Rahman ²⁰

This piece will focus on risks to the key macroeconomic forecasts that underpin the Budget. The Budget rests on a forecast GDP growth of 5.5 percent and an inflation of 6.5 percent in 2009-10. These forecasts feature possible impacts of the global recession, including impacts on remittance and exports. The fiscal deficit is forecast to be 5 percent of GDP next year, of which 2 percentage points are expected to be financed from external sources.

Are these forecasts sensible?

Let's start with GDP growth. The 5.5 percent forecast growth for FY2009-10 is broadly consistent with international agencies – for example, the Asian Development Bank forecasts a growth of 5.2 percent next year.

But how confident can we be that this forecast will be realised?

Yogi Berra, an American baseball player, is said to have cleverly remarked: "Prediction is very hard, especially about the future." Macroeconomists would nod in agreement, particularly now. The speed and ferocity with which the recession ravaged through the global economy caught everyone by surprise, and forecasts were marked down heavily and frequently. The IMF marked down its forecast for 2009 world growth five times since the collapse of Lehman Brothers last September. It is self-evident that there is a considerable amount of uncertainty around any forecast, and the Budget forecasts are no exception.

And yet, there is very little discussion on any risks to the outlook in the Finance Minister's Budget speech or official documents.

Given the global recession, risks would appear to be heavily weighted towards the downside. To be sure, the forecast growth is a slowdown from this year's 5.9 percent (and 6.25 percent average in recent years). However, compared with our neighbours, the forecast slowdown is very modest. And a range of plausible developments – export slowdown leading to manufacturing stagnation, sharp slowdown in services coming from remittance drop – could slow growth significantly.

What would such a sharp slowdown mean?

Of course, it would mean less employment and income, flowing through to faltering poverty alleviation. And for the Government, it would mean less revenue and higher deficit. How that deficit is financed could have implications for the inflation forecast.

The budget forecast of 6.5 percent inflation for next year is identical to that of the ADB. With bumper harvest, falling world prices, and the taka's appreciation against the Indian rupee, food prices have been on the ease, helping disinflation. However, if budget deficit ends up being higher than expected (and/or if the 2 percent of GDP external finances are

the forecast growth is a slowdown from this year's 5.9 percent (and 6.25 percent average in recent years). However, compared with our neighbours, the forecast slowdown is very modest.

²⁰ An earlier version of this article was published in the in the Daily Star on 14 June 15, 2009. Available at: <http://www.thedailystar.net/story.php?nid=92408>.

But a remittance boom could also be a mixed blessing. Take away other opportunities and remittance growth could fuel a real estate bubble, instead of productive investment.

unavailable), then Bangladesh Bank might come under pressure to finance the deficit. And this could put added pressure on the inflation.

However, not all risks are negative. Nature could well be kind to us, resulting in yet stronger harvest. Plus, remittances which have proved surprisingly resilient could accelerate. The price of crude oil has ticked up in recent months and this could revive the Gulf labour market, and fuel remittance growth.

But a remittance boom could also be a mixed blessing. Take away other opportunities and remittance growth could fuel a real estate bubble, instead of productive investment. And at the same time, higher oil prices could mean higher inflation.

Former US President Harry Truman bemoaned the lack of one-handed economists. Bangladesh's budgets seem to be drafted by one-handed economists, because they seldom discuss risks in details.

This budget could have been different. There are many ways the forecasts underpinning the budget could be missed. A discussion of some scenarios a bumper harvest and buoyant remittance on the upside, export slump and lack of foreign financing on the downside would have only enhanced the Finance Minister's credibility.

The Government will likely reap political benefits if the future turns out to be brighter than what is predicted in the budget speech, just as it stands to face political headwinds if things turn out to be worse. However, a proper discussion on the risks would have spared us the political theatrics. And more importantly, it would have given all stakeholders a much better understanding of the economic conditions and outlooks that will shape the budget's outcome.

The public-private partnership budget

Syed Ahamed ²¹

The introduction of Public Private Partnership (PPP) to Bangladesh in the National Budget for FY2009-10 will have lasting implications for our development.

Off-budget financing of development programs is not a new phenomenon. Over the past few decades, many governments encouraged off-budget financing by private sectors to meet the growing public debt. In 1992, the Conservative government of John Major first introduced a systematic PPP program in the United Kingdom, which was later continued by the subsequent Labour governments.

The PPP initiatives may include a variety of joint ventures, including part-ownership of state owned enterprises by the private sector, private financing in government projects, and contracting out of particular services (including construction and maintenance of infrastructures).

For instance, the government may hire a consortium of private entrepreneurs to establish a power plant and in return offer the consortium a percentage of its revenue earnings. This way, the efficiency of private capital can create a synergy with the credibility of public service.

However, balancing the public sector's goal to provide quality services and the private sector's interest to withdraw return on investment is very difficult. As such, it is important to highlight some of the prerequisites of a PPP budget.

Proactive regulatory framework

It is essential to have a well-defined legal framework for the regulation and transparency of PPP enterprises. A proactive regulatory framework is required, with appropriate checks and balances, to prevent corruption.

Countries such as UK, Canada, India and Singapore instituted rigorous regulatory frameworks and responsible public bureaucracies before initiating their PPP budgets.

Bangladesh, in contrast, has a reactive legal structure, which fails to prevent corruption and aims to penalise the dishonest after a felony is committed. Since the Government aims to initiate PPP projects in the next fiscal year, prompt action will be required to establish a comprehensive policy and regulatory framework for competitive and transparent bidding, sharing risks and rewards, and dispute settlements.

Synergy, not deregulation

Bangladesh's experience with deregulation and foreign investment has not always been very encouraging consider privatisation scandals of the 1980s or treaties like Gatco for example. Therefore, ensuring transparency and accountability of the PPP contracts is vital. The objective of public private partnership is to produce an outcome greater than the sum of its individual parts. Hence, the focus should be on synergy, not deregulation.

balancing the public sector's goal to provide quality services and the private sector's interest to withdraw return on investment is very difficult

²¹ An earlier version of this article was published in the in the Daily Star on 18 May, 2009. Available at: <http://www.thedailystar.net/newDesign/news-details.php?nid=88619>.

Regulatory vigilance is required to prohibit PPP initiatives from becoming the public sector's cost cutting and the private sector's profit maximising ventures

Sharing risks and rewards

It is essential to identify the risks associated with a PPP project, and to use an appropriate legal framework to distribute the risks, resources and rewards (3Rs) among the public and private partners.

According to a 2008 OECD report, legal and political risks are most efficiently borne by the government while the demand and supply related risks are well handled by private partners.

However, if the risks are not legally allocated at the commencement, a private entrepreneur (anticipating a loss) may quit a PPP project leaving the entire burden on the government.

Procedural delay

In a 2004 Report, the US Department of Transportation noted that the government faces "an initial sharp increase in workload" in adapting and preparing the procedures for PPP projects.

Since the Government aims to initiate PPP projects in priority areas such as in power and health, with a goal to speed up the outcomes, the procedural delays of PPP may jeopardise the government's goal.

Therefore, establishing a comprehensive and transparent legal framework in the quickest possible time will be the major challenge for the PPP budget.

Value for money, not deficit and profit

During the early 1990s, when the prime focus of PPP was to reduce budget deficit, many PPP projects resulted in poor but expensive services for the citizen. Later, focus of PPP budgets shifted to efficiency in the delivery of public services.

Termed as "value for money" (VfM), this new focus aims to offer the most efficient and effective public service by combining the respective expertise of private and public sectors.

Regulatory vigilance is required to prohibit PPP initiatives from becoming the public sector's cost cutting and the private sector's profit maximising ventures.

Social responsibility

Education and health are two critical areas where the Government's responsibility to provide quality services must take precedence over the profitability of the services. If rural areas fail to attract private investment, the government may consider offering capital grants to make PPP projects commercially viable in these areas.

Bangladesh can take lessons from other countries where health and education related projects are implemented under public/social/private partnership (PSPP).

Public Private Partnership is a generic model, which can yield both positive and negative outcomes based on its usage. If the public sector's corruption and the private sector's greed create an evil twin (witnessed during some episodes of privatisation), then development will be imperilled. But if the respective expertise of public and private sectors create a synergy, it will hasten development.

The choice is ours.

Digital Bangladesh in the budget: a reflection of unpreparedness?

Mridul Chowdhury ²¹

“Digital Bangladesh” is not only a catch-phrase for the government, but is also a reflection of the common man's desire for a better and modern Bangladesh. The once popular phrase Shonar Bangla is now being replaced by "Digital Bangladesh."

The National Budget reflects the Government's commitment towards Digital Bangladesh, but possibly falls short with respect to giving a clear direction about the approach it will take to realise the goal. Its commitment is indicated by the fact that the total allocation for ICT related components has substantially increased from last year.

However, there are also indications that the level of commitment may not be matched by the degree of preparation needed for creating Digital Bangladesh, since it is very much of a cross-cutting issue that permeates across almost all sectors.

One of the most talked-about components of Digital Bangladesh is the issue of e-governance, which gets vague and scattered mention in the budget. There is a statement that "we want to transform to e-governance by 2014" without an explanation of what it means. There are many e-governance projects underway so the process has already started. In that context, the meaning of this statement is unclear.

Furthermore, except for NBR automation and land record management automation, there is no specific mention of any other digitisation/automation or e-governance project. This does not necessarily indicate a lack of commitment, but possibly reflects a lack of adequate planning prior to budget presentation.

While the Government is focused on finding public-private partnership solutions for infrastructure development²³, this attention has not diffused through to issues of e-governance. The section on PPP does not mention e-governance at all, although there is significant scope for private sector partnership, and not just outsourcing opportunities, in this sector. Sustainability of e-governance projects often depends on whether the technological partner has invested in the success of the project. The Budget does not reflect that there is adequate appreciation of this aspect within the government.

An example from a neighbouring country can give a better sense of what we mean. The Bangalore One initiative by the government of the Indian state of Karnataka covers 26 citizen services pertaining to 11 government departments. There are 17 centres through which these services are provided to citizens. This entire service delivery mechanism has been made possible with little investment from the government since there are 6 private sector players involved, including software companies and banks.

The budget also does not reflect an understanding of the biggest problems of the software industry, which is the main engine for creating a Digital Bangladesh. The two biggest bottlenecks that the software industry is currently facing are financing options and availability of skilled human resources with technological and management capabilities.

This does not necessarily indicate a lack of commitment, but possibly reflects a lack of adequate planning prior to budget presentation

²² An earlier version of this article was published in the in the Daily Star on 30 June, 2009. Available at: <http://www.thedailystar.net/newDesign/news-details.php?nid=94717>.

²³ Article on page 34 discusses the public private partnership scheme in detail.

The Government has attempted to address the first bottleneck by doubling the Equity and Entrepreneurship Fund (EEF) of the Bangladesh Bank from Tk 100 crore to Tk 200 crore, although the finance minister makes no mention of the fact that there is implementation challenge in the disbursement mechanism itself, since identifying innovative software companies requires a different set of criteria and skill level on the part of the fund manager.

This EEF had remained unused in previous years so the solution is not necessarily to increase the amount of the fund but to develop capacity to disburse the funds and perhaps also link it to possible PPP initiatives in e-governance.

With respect to the second bottleneck, the Finance Minister makes no clear commitment except to "target a benchmark of 4,000 computer engineers and scientists graduating each year from the last year of our tenure." There is no clear allocation of funds associated with this commitment. The software industry has long been proposing the development of training institutes to make the computer engineers and scientists "industry-ready" since the curriculum and approach taken by most universities do not prepare their graduates for employment in the industry.

The Bangladesh Computer Council has, for many years, been subsidising internship of students employed in the software sector, but a more systematic approach to preparing human resource needs more targeted focus from the Government.

With respect to access to information and communication technologies, the Government makes high-level commitment by promising to extend the reach of fibre optic cables within the country and linking to a second submarine cable. In a time of growing access to Internet through mobile phone networks and upcoming Wimax technologies, one fails to see why the Government is still focused on building out fibre optic cables when the real issue that remains untouched is how common people will get access to computers and Internet in an affordable way. Building and extension of telecentres (or "rural cyber-cafes") is not mentioned, neither is the issue of using government post-offices as telecentres.

With regards to applications of ICT in education and health, the Budget demonstrates very little understanding of the issues involved. Even after years of advocacy by NGOs and UNDP, this year's Budget again reflects that the Government still seems to fail to appreciate the issue of use of ICT tools for general education that sending computers to school should not only be aimed at making students computer-literate. The issue of ICT tools for health services in disadvantaged areas is also not touched upon at all.

With respect to taxation, some essential drivers of Digital Bangladesh, such as mobile phones, computer monitors and printers, are taxed more than deemed appropriate by relevant quarters.

The Budget makes one wonder whether the Government is a bit unprepared when it comes to Digital Bangladesh. An emergency fund of Tk 100 crore has been allocated with no clear indication of what it will be spent for. Furthermore, the administrative mechanism for realising Digital Bangladesh is still a bit unclear since the points of decision-making and implementation monitoring seem to be scattered across several government entities.

In the Budget speech, there is mention of the Government working with IT associations for "creating a work plan." This can be seen as a positive sign to engage the private sector. But it can also indicate lack of adequate preparation within the Government. We are anxiously waiting to see which is true.

The Budget makes one wonder whether the Government is a bit unprepared when it comes to Digital Bangladesh

Going back on their word

Jalal Alamgir ²⁴

Bangladesh's democratic deficit looms large at the local level. Elected union and upazila councils have little power against top-down political and fiscal decisions. In its election manifesto, Awami League wisely promised to empower local-level decision-making. But unwisely, party MPs have moved away from empowering local communities either financially or politically.

The recent budget allocates just over a fifth of ADP to local government, which is a small proportion compared to most other countries of South Asia. Both union parishad chairmen and upazila chairmen have justifiably asked for a larger share.

But allocation is only part of empowerment; the crucial element is the ability to spend it independently. Under current convention, most local government money will be spent according to the wishes of ministries and MPs. The World Bank notes correctly that Bangladesh remains "one of the most centralised large countries in the world."

There is strong evidence from around the world that devolution and decentralisation lead to better government performance. For poverty alleviation in particular, which is the aim of the ADP, participatory decision-making has a more positive impact than do centralised approaches. Local democracy matters, greatly. But when it comes to decentralisation, Bangladesh repeatedly ends up preferring, for mainly political reasons to strengthen local government, but not local democracy.

In India, which is a federal system to begin with, constitutional amendments in 1993 further empowered local democracy, especially grassroots level panchayats. The panchayats got taxation powers, a better share of state revenues, and the elected bodies became stronger decision-makers about the development track of their respective localities.

It was not easy for Indian states to give up some of their decisional authority. Many state-level politicians continued to meddle in grassroots democracy. In places where reforms were genuinely implemented, such as Karnataka and Kerala, financial and developmental performance improved. Studies show that local communities felt, for the first time, that they had power to shape the course of their lives.

AL's manifesto clearly had the same spirit when it promised: "Union, upazila and district councils will be strengthened through decentralisation of power." Furthermore, AL's Vision 2021 assured that "self-reliant local self-government institutions will be established at upazila and zila levels." Even the recent budget speech echoed this stance: "To empower people and to decentralise the power of the central government, the union and upazila parishads will be vested with additional powers."

But what has happened on the ground threatens to relegate these pledges to mere rhetoric.

In one swift stroke, the paranoia and triumphalism of new parliament members dampened the enthusiasm for local democracy that the local elections of January 22 had created. Then, in May, the LGRD ministry published guidelines that further eroded the independence of other elected council members against the executive

²⁴ An earlier version of this article was published in the in the Daily Star on 11 July, 2009. Available at: <http://www.thedailystar.net/newDesign/news-details.php?nid=96329>.

The new parliament passed a law in April to make MPs advisors to upazila councils, stipulating further that local councils would be bound to accept the "advice" of MPs.

In one swift stroke, the paranoia and triumphalism of new parliament members dampened the enthusiasm for local democracy that the local elections of January 22 had created. Then, in May, the LGRD ministry published guidelines that further eroded the independence of other elected council members against the executive.

Elected union and upazila council chairmen strongly -- and rightly -- opposed this move. As one of the chairmen lamented: "I wouldn't have contested the upazila election had I known beforehand that parliament would make such law." Another noted: "It seems we are elected just to sit idle in our offices." Some chairmen even threatened to declare MPs as *persona non grata* in upazila complexes.

The problem is not advice. MPs should be able to influence affairs in their constituencies. The problem is mandatory advice, which will choke local independence and perpetuate the ties that keep local leaders dependent on central politicians.

In exercising their power, but not wisdom, the MPs seem to have forgotten that they rely on local leaders in their own election campaigns. The mistrust will surely affect the implementation of local aspects of the ADP. Moreover, budget 2009-10 envisions greater revenue mobilisation at the local level. How would that come to fruition without strong cooperation from locally elected bodies?

The Indian experience showed that stronger local democracy led to better checks and balances, healthier competition within governmental authorities, and better civic culture due to people's participation.

If these are outcomes that Bangladesh too has reason to value, then the parliament must reconsider its bill and take genuine steps to strengthen local democracy. The ruling party MPs were elected on a mandate of change, including empowerment of local democracy. They need to stay true to their word, fiscally and politically.

*The ruling party MPs
were elected on a
mandate of change,
including empowerment
of local democracy.
They need to stay true
to their word, fiscally
and politically.*

DWC and the authors

Drishtipat Writers' Collective formulates research and policy ideas in areas of concern that need activism for protection of the affected or improvement of the quality of life. Areas of advocacy include fundamental political and civil rights, cultural freedom, poverty, natural disasters, the economy, the environment, or any form of violation of foundational and contingent human rights.

The Collective works for a democratic polity, a liberal society and better living for all, and believes that not only is pen mightier than the sword, it is also a more civilized and effective instrument for changing the world.

Syeed Ahamed is a policy analyst currently based at the University of Melbourne, Australia. His recent publication: Ahamed, S. and Davis, G. (2009). Public Policy and Administration. In Rhodes, R.A.W. (ed.). The Australian Study of Politics in the Twentieth Century. Hampshire: Palgrave Macmillan. The author can be reached at syeed.ahamed@gmail.com

Jalal Alamgir is Assistant Professor of Political Science at the University of Massachusetts, Boston. His recent publication: Alamgir, J. (2008). India's Open-Economy Policy: Globalism, Rivalry, Continuity. New York: Routledge. The author's contact email: jalamgir@yahoo.com

Mridul Chowdhury is the CEO of a global tele-health company called ClickDiagnostics, co-founder of the youth activism group Jagoree, and Director of Driven Partnership, a social enterprise. The author can be contacted at mridulch@gmail.com

Jyoti Rahman is the Editor of Drishtipat Writers' Collective. He works as an applied macroeconomist, and has professional publications on economic growth, terms of trade shocks, and labour market issues. The author's email address is jyoti.rahman@drishtipat.org

Asif Saleh is the Executive Director of Driven Partnership and Drishtipat -- a global human rights organisation. The author can be reached at asif.saleh@drishtipat.org

[This page left intentionally blank]



drishtipat
writers'
collective

www.drishtipat.org/dpwriters