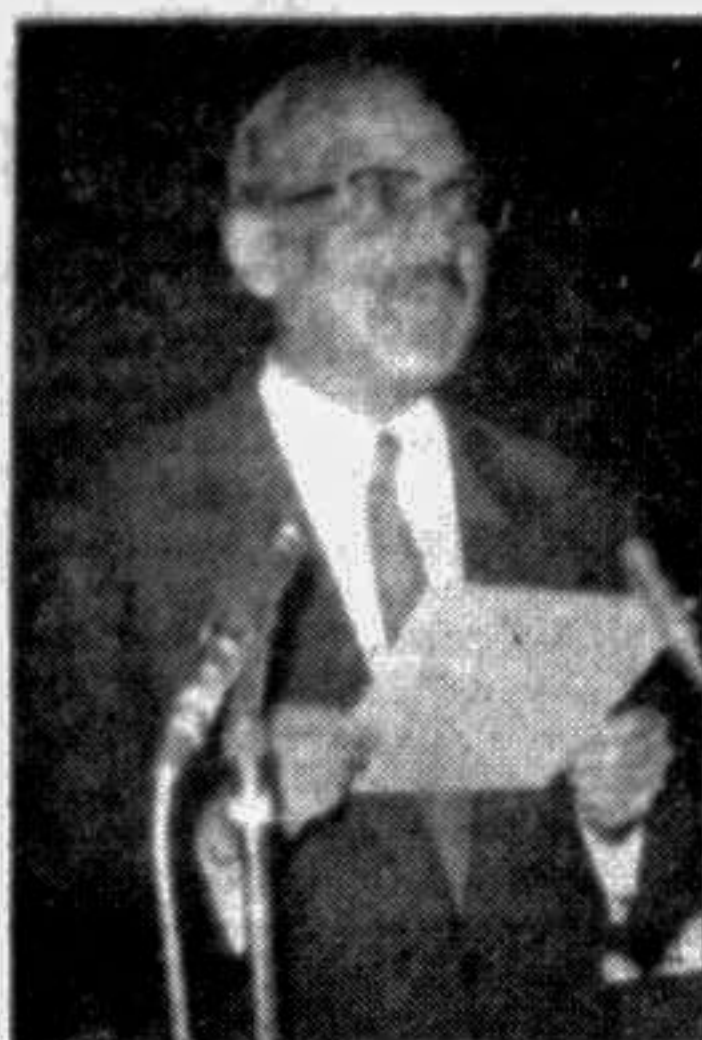


# Export led growth policy more appropriate for us



Finance Minister delivering his budget speech.

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economy is quite low, it assumes a leading role in organised employment generation and in export and import trade. But for a number of reasons, growth in this sector is declining. Except for a few industries, most of the sector is burdened with a number of problems. In particular, the public sector industries are incurring losses. Labour productivity in these industries is quite low and in many places there is excess labour. The Government has taken steps to implement voluntary labour reduction plan and their rehabilitation where possible. A lump provision of Tk 150 crore has been made in the budget next year for payment of retirement benefits for such employees. A provision for Tk 100 crore has been made in the ADP next year to create a fund for rehabilitation of industrial units.

## Savings And Credit Management

29. In a competitive economy proper management of financial institutions is a pre-condition for growth. This Government inherited a very weak and ill-managed banking sector. We have introduced far reaching reforms in the economic sector in order to strengthen the role of these institutions in financial management. Under the financial sector programme, policies measures have been adopted regarding classification of loans of the banks, bad debt provisions and stoppage of payment of interest. Financial institutions of Bangladesh have been made free from the restrictions on interest rates and on direct control over loans. Banks have been given powers to determine interest rate except for export small and cottage industry and agricultural loans. Bangladesh Bank lowered bank rate from 9.25% to 8.5% in the context of low inflation and to stimulate investment. Interest rates on savings certificates and on bonds of the National Saving Directorate have been lowered in line with the lowering of bank rates. It is expected that due to lowering of interest rate on deposits, banks will also lower their lending rates substantially and as a result investment will be encouraged and industrial sectors will gain momentum. This is so because with the lowering of inflation there has been no reduction in interest rate in real terms. In respect of currency regulation the Central Bank has introduced indirect regulations in place of direct control. There will be no more sale of treasury bill on administrative instruction. As a first step towards establishment of competitive capital market, interest rate on treasury bills will be fixed on the basis of competitive auctions and different time bound treasury bills will be introduced. Consequently, a first step towards laying the foundation of an active capital market has been taken.

## Financial Sector

30. After the Banking Company Act, 1991 was put into operation, supervision of the commercial banks was strengthened. In order to improve management of deposits, strict standards have been fixed for lending of capital. Government has floated bonds for taka 1,730 crores to augment capital and to make provisions for bad and doubtful debts of the four nationalised banks. In the meantime an expert committee is reviewing the banking company law. Amendments will be made in banking law soon to further strengthen provisions of supervision. In the context of liquidation of BCCI internationally, transactions in all its branches in Bangladesh have been postponed. Reorganisation of Bangladesh branches are nearing completion and it is expected that the reorganised bank will start operation from next month. Because of the uncertainty and complexity of the ownership of BCC Foundation, Small Industries and Commerce Bank known as 'BASIS' has been acquired under the Banking Companies Act.

31. Different non-banking

financial institutions have grown irregularly in the last 9 years under the umbrella of an autocratic rule. For such institutions, legal supervision was loose as their number was very small and their operations limited. Recent experience of corrupt and bad management of some of these financial institutions demonstrates the necessity of supervision and monitoring of such institutions. Framing of a new law for non-banking financial institution is now in the final stage.

32. Without an effective capital market, success of market oriented free economy is not possible. Activities of institutions in the capital market are not encouraging at all. In the current year, Government has withdrawn restrictions on non-governmental share sale, bonus share, right share and on salary and allowances of the chief executive. For the capital market, organisational framework is being recast and drafting of new law for an independent Securities and Exchange Authority is in final shape.

In the first stage of reactivating the development of financial institutions, Government has decided to privatise Bangladesh Shilpa Rin Sangstha. The problem of housing for the lower and middle classes is becoming acute. We are aware of the problems and prospects in this sector. In order to encourage investment in the housing sector government has decided to reactivate Bangladesh House Building Finance Corporation. For this purpose the capital of this Corporation has been substantially increased. The Corporation will once again be able to start lending operation soon.

## Exchange rate management policy

33. In case of foreign exchange management, Bangladesh Bank has been pursuing a Policy of Flexible Exchange Rate. The aim of this policy is to expand export trade keeping competitive strength of taka to reduce the gap in balance of trade, to develop and efficient import substitution industry. Keeping this aim in view the Real Effective Exchange Rate is fixed which is readjusted in case of necessity with the intervention currency. From July, 1991 to April, 1992, the value of taka has been readjusted against US Dollar. As a result, at the end of April, 1992, adjusted exchange rate stood at 39 taka for one US Dollar. Consequently taka has been devalued 9% against US Dollar in the period under consideration. I consider it pertinent to emphasise here, Mr Speaker, that an active Exchange Rate Policy can be helpful only in production of exchangeable commodity and in increase of export. But real benefits will not come unless reforms are made in those sectors where low productivity, adverse labour-owner relationship, excessive regulations and other distortions are existing. Besides, in long time perspective, flow of capital, liability of entrepreneurs which increases manifold due to change of exchange rate and such type of encompassing factors should be considered while framing Exchange Rate Policy. As such adjustment of Exchange Rate can be considered as an effort to remove structural imbalance but not as an alternative to sectoral reform programme.

34. While pursuing a policy of Real Effective Exchange Rate (REER) there was no rationale for keeping dual rate in the Secondary Exchange Market. As a result, from 1st of January, 1992, one effective unified currency exchange rate has been introduced merging official rate and the secondary exchange rate. The foreign exchange reserve increased from 881 million at the end of June, 1991 by 656 million dollars and has reached 1537 million dollars at the beginning of the month which is an all time high (Annexure V). However, receipts of 766 million dollars received under different assistance programme are included in this figure.

35. In July—March period in FY 1991-92 the balance in foreign trade of the country showed some improvements. During this period deficit in the balance of trade stood at 693 million US dollar which was US dollar 1290 million during the corresponding period of last year. The export target has been fixed at US dollar 2151 million for FY 1991-92. Thus export earnings stands at 63% in terms of dollar for the first nine months of the financial year. But the effect of the recession prevalent for sometime in the economy and the trade throughout the world is still continuing. Besides, there has been a shortfall in couple of our export items especially frozen food, tea and raw jute. In spite of these impediments, shortfall in export earnings is expected to be marginal due to improvement in export of ready-made garments and hosiery products. In FY 1991-92 the target for expenditure on ac-

count of imports was fixed at 3854 million US dollar against which real imports took place for 2308 million dollars representing 58% of the target. If the current trend for imports continues, volume of imports at the end of FY will remain substantially below the target level. The import contraction is basically a reflection of the recession prevalent during the first six months of the year. Import trade will further be liberalized keeping in view production and expansion in exports and in harmony with international market environment but the genuine interests of local industry will be protected. We have noted a declining trend in the utilisation of project and commodity assistance. This had an adverse impact upon the economy. Considering our good foreign exchange reserve position we are adopting some specific measures to stimulate imports of capital machinery spares, intermediate goods, industrial raw materials etc. We will also encourage imports for the transport and construction sectors. Beside generating revenues, such measures will contribute to buoyancy of the economy. Our objective is essentially a trade-related and not aid dependent growth for the country. The second part of my speech includes specific measures to be adopted in this regard.

36. Our trade policy aims at developing export-oriented industries and making them internationally competitive in terms of quality and price. We have to diversify trade by rationalizing and reducing tariffs and wherever possible by withdrawing restrictions including quantitative restrictions on imports. The Government has already measures along these lines. Exporters will be allowed to retain greater percentage of their export earnings to expand their own exports. This rate now stands at 2-2.5% of export earnings. We have decided to increase the retention rate to 10% in the next financial year. However, this rate will be limited to 5% for exports where value addition is low.

37. In the past, ultraprotectionist policies encouraged wasteful, mismanaged and inefficient industries. As a result more efficient sectors, specially in the rural economy, were deprived of loan and investment. Consequently it has led to distortions in resource management and inevitable contributed to a fall in productivity of investments. We hope that trade liberalization will make our industries competitive in the international market and this will contribute to a shift of resources from the inefficient to efficient sectors. The ultimate aim of our trade policy and trade liberalization is to stimulate economic activities to generate employment and to make the external sector competitive and viable. In implementing this policy, we hope to encourage backward integration and higher value addition through necessary investment and technology transfer.

## Mr Speaker

38. We believe that people, particularly the youth of our society, are an invaluable resource. We have a comprehensive programme for imparting vocational skills and dissemination of production-oriented education. Open university will be one of many institutions devoted to this purpose. Manpower development sector has the high priority in our national plan. By stimulating productive investment in agriculture and agro-based industry employment opportunities will be created. Further, the planned development and diversification of the external sector and exploitation of our comparative advantage in labour intensive industries will result in employment and in-

come generation which is a sine-qua-non for freeing our people from the poverty trap.

39. Despite our success in macro-economic management much of its beneficial impact has been eroded by out unsatisfactory performance in

mined that our energies should be devoted towards optimisation of our growth potentials and betterment of the quality of life of the people with particular attention to the most deprived and least privileged segment of our society.



Prime Minister Begum Khaleida Zia giving her sign of approval to the budget.

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some key micro sectors such as power, jute, textile, light engineering, railways, etc. These important sectors are bedevilled by high system losses, pilferage, and inefficiency. Excess capacity has been a major problem in manufacturing sectors — both public and private. These are the results of ill-conceived investment and rent-seeking. Declining labour productivity and indiscipline as well as management incompetence have further exacerbated the situation. Unless we take stern corrective action in these micro sectors we cannot achieve our economic objectives.

40. As the nation looks to the future, we perceive the task before us is difficult and challenging. Our efforts in the direction of institutional reforms and restructuring of the key sectors of the economy will be inspired by the ideals of freedom, self-reliance and recognition of human rights and dignity. We are deter-

mined that our energies should be devoted towards optimisation of our growth potentials and betterment of the quality of life of the people with particular attention to the most deprived and least privileged segment of our society.

41. In very recent past we have witnessed the collapse of the socialist economies and the appalling inefficiency and waste of resources, both human and material, in such systems. We believe that on the efficacy of a market economy free from rigidities and regulatory constraints a consensus has emerged amongst people of divergent political views.

This is a source of great strength. Our people have amply demonstrated fortitude and courage to struggle unitedly against impossible odds and emerged triumphant. Thus I can say with all emphasis that given the political will and unquenchable faith in the commonwealth we will reach our goal. Let us, therefore, eschew our petty differences and respond to the challenges that lie ahead with common resolve

and purpose.

## Mr Speaker

42. There is no alternative to reform. Through a well-organised structural adjustment programme, all distortions, rigidities and imbalances of the economy must be eliminated; otherwise Bangladesh will remain marginalised and locked up in the vicious circle of poverty. The economic strategy and the policy for resource mobilization that will be followed to achieve that objective will be dealt with in the second part of my speech.

## SECOND PART

### Mr Speaker, Sir,

While, presenting the budget for 1991-92 fiscal year in this Parliament, I referred to the anarchy, depression, indiscipline and irregularities in the economic sphere prevailing at that time and indicated the ways to get out of that crisis. We proposed through reforms of the fiscal system in order to gear up domestic resource mobilisation. At that time, many people had fears and reservations; in the light of experience we can now say that these fears and reservations were unfounded. The fiscal reform measures undertaken by the government in the previous budget have already started giving desired results. A dynamism has been generated in our worn-out tax system. This achievement was made possible by the strong leadership of Prime Minister Begum Khaleida Zia and the spontaneous support of the people. But there is no room for complacency, for our destination is still far away.

2. The aim of the reform measures proposed by us was to raise the revenue-GDP ratio through enhancing the growth rate of revenue. For achieving this we proposed to rationalise fiscal laws and structures, improve fiscal management and expand computerization. During 1990-91 fiscal year, the revenue-GDP ratio stood at 10 per cent. We expect that during the current fiscal year this ratio will increase to 11 per cent. During the time of President Shaheed Ziaur Rahman, the annual growth rate of taxes and duties under the National Board of Revenue was more than 20 per cent. This rate declined to 15 per cent during the past decade. We have been able to reverse this declining trend of tax collection and internal resource mobilisation. The realisation of tax revenue up to May of the current fiscal year has been 25 per cent higher than that of the same period in the previous year.

3. Like many other countries of the world, a policy of economic development through import substitution industries has been pursued in Bangladesh for a long time. It was hoped that local industries would flourish behind the high tariff wall applicable for final products. In certain cases, administrative bans and quantitative restrictions were imposed to protect domestic industries. It is now apparent from the experience of a number of countries that, in many cases, this policy has retarded overall economic development. It has been seen that inefficient industries incapable of international competition grow up, sheltered by the high tariff wall and administrative control. Although these industries may be profitable from a private entrepreneur's point of view, optimal and efficient utilisation of domestic resources does not take place in these industries. In general, these open up opportunities for 'rent seeking' at the cost of the genuine interests of the consumers.

4. Import substitution industries artificially compress demand for foreign exchange

which leads to misalignment of exchange rate; and because of the resultant artificially overvalued exchange rate, the prices of Bangladeshi products become too high in the world market. It becomes difficult for export goods to be competitive internationally. On top of this, the existence of monopoly and opportunities for rent makes import trade and investment in import substitution industries more attractive, which discourages investment in export-oriented industries.

5. An important obstacle to industrialisation and economic development through expansion of import substitution industries is the limited size of the domestic market. On the other hand, the export market is large for small countries like Bangladesh. Thus, an export led growth strategy is more appropriate for us. It is possible to sell goods of international standard in the vast world market at competitive prices. If an export led growth strategy is adopted, domestic industries will have to maintain efficiency at international levels; and the environment unfavourable to attaining high efficiency will have to be removed gradually. The reduction of high tariff rates will eliminate the exchange rate misalignment. On the basis of a realistic and appropriate foreign exchange rate, supportive environment and dynamic comparative advantage, efficient industries will develop which can compete in the export market or meet domestic needs. It is observed from the recent experience of developing countries that export growth, economic development and poverty alleviation are correlated; on the other hand, a closed door or inward looking economy is a deterrent to development and poverty alleviation.

6. Our views are supported by the recent international experience on economic management and development strategy. The Government controlled economies of the former Soviet Union and Eastern Europe have disintegrated the moment they came in contact with the outside world. Contrary to this, many countries of the world achieved socio-economic development through export led growth strategies. Our neighbouring countries like India, Pakistan, Sri Lanka, Vietnam, Thailand and Indonesia have adopted well designed policies for setting up liberal and competitive economic systems. The favourable impact of these policies are already visible; investment has been encouraged and foreign investment attracted. In step with the countries of this region and the rest of the world, we have to effect reforms and inject dynamism into the process of economic development. Export led growth strategy, liberal competitive economy and minimisation of bureaucratic control by the government are all parts of this process.

7. We have to bear in mind that there is no reform process without pain. All of us, including the industrial entrepreneurs, will have to respond to this challenge by increasing efficiency. Those who enjoy opportunities for rent in an inward looking economic system subject to bureaucratic control will be naturally frightened by this change. They will try to bring undesirable pressures on the government for perpetuating the traditional system. But in the greater interest of the society and the country, we have to surmount these obstacles and follow an appropriate socio-economic development strategy. In harmony with the international trend of change, Bangladesh has to march forward in creating an open and competitive economy. It has to be remembered that the future of the democratic system and improvement of the lot of the common man are inseparably intertwined. Self-reliant socio-economic development, improvement of people's condition, evolution of our integration with the changing international environment, taking advantage of the opportunities of the expanding world trade — all these have collectively defined the context of our reform efforts.

8. Our income tax system is anachronistic and weak in a number of ways. The high rates of tax and large number of rates discourage voluntary compliance by the taxpayers. On the other hand, too many exemptions create scope for tax evasion and increase the discretionary powers of the tax officials. The number of income taxpayers is also negligible — less than 5.5 lakhs in 1991. A simple, transparent and flexible income tax system can change the present situation. The ideal objectives of such a system would be: reduction of high rates of tax; minimisation of multifarious exemptions and their rates;

simplification of return submission and tax payment procedures; and reduction of discretionary powers of the tax administration. I believe that such a modernised tax system would be administratively simple and efficient, encourage the taxpayers to perform their due responsibilities, remove tendencies to evade taxes, increase the number of taxpayers, and facilitate growth of tax collection.

9. Many weaknesses and distortions exist in case of import duties as well. In the past, in order to increase revenue through temporary measures or to meet exigencies, import duty rates were changed on an ad hoc basis and different types of surcharges and levies were also imposed. At present, the duty rates are very high and too many in number. The basic duty structures have become distorted as a result of importer specific exemptions or exemptions granted at different rates. These arrangements have, on the one hand, increased scope for evasion and, on the other, enhanced the discretionary powers of the customs authorities. I have already mentioned the adverse effects of high duty rates—e.g. rent seeking, anti-export bias and smuggling. This year we propose to adopt a special programme to rationalise the customs tariff structure through reducing high duty rates and their numbers, limiting the scope of exemptions and their rates, and simplifying valuation and duty collection procedures. This will help modernise the tariff system and attune it better to the needs of the time. Let me now describe briefly the important features of the proposed reforms of the duty structure. The existing 11 duty rates would be reduced to 7 — namely, 100, 75, 60, 45, 30, 15 and 7.5 per cent. The highest duty rate would be 100 per cent; higher rates would, however, apply to alcoholic beverages and certain luxury goods. In most cases, duties would be reduced to 75 and 60 per cent respectively from the present 100 and 75 per cent; in certain cases reduction of duty would be even more. The lowest duty rate would be fixed at 7.5 per cent and all duty exemptions would be removed. However, full exemptions may continue for a limited number of goods only by way of exception. As a result of the reduction of duty rates and their number, it would be easier to collect duties; and because of expansion of base, it would be possible to mobilise more internal resources while keeping incidence at a low level. In the end, I want to state that the programme for phased restructuring of duty rates would continue as a part of the ongoing economic reform programme; further rationalisation will be effected in future consistent with our socio-economic need and the international environment; as a result economic efficiency will increase and local and foreign investment would be encouraged.

10. Different reform measures were introduced in 1991-92 budget in the areas of fiscal policy and fiscal management. As a sequel to these, different ministries, the Tariff Commission and the National Board of Revenue have examined different aspects of the revenue system and the economy. I have also discussed these issues with my colleagues. Recently, I have discussed issues relating to tax system and overall economic condition and policies with the members of the trade and industry, professionals and political leaders regardless of their party affiliations. Our intention is not to use the tax system solely as an instrument to raise revenue, but also to use as one of the factors facilitating the process of economic development. I have benefited immensely from these discussions.

## Mr. Speaker, Sir,

11. I am now presenting the important reform measures of both the direct and indirect tax systems.

## DIRECT TAXES

### Income Tax:

12. In the realm of income tax both structural and administrative reforms have been proposed. Simultaneously with the reduction of tax rates, a transparent, simple and progressive taxation system has been proposed to replace the existing one. The scope of self-assessment has been widened significantly and the procedure made simpler. In addition, effective steps have been proposed to reduce procedural delay in framing assessment, issuing refund, registering firms and granting tax holiday. Besides changes in the statute, necessary steps are being taken to modernise tax administration and improve efficiency of tax administration. The government strongly expects that the proposed measures will broaden the tax-base

(Continued on page 8)



Awami League MPs having their lunch at the parliament cafeteria at the beginning of budget session.

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