Who are these loans for?

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The incumbent government has decided to receive a loan worth $1 billion from the International Monetary Fund (IMF) as support to prevent deterioration of the balance of payment.

However, the IMF loan is always tagged with hard terms and full disbursement of loan amount finally depends on complying with the hard terms. Although the terms or conditions are yet to be made public, several indications make it clear that the government has to go for some fiscal austerities and monetary tightening.

In fact, during a visit a few months back, a mission from IMF made it clear that without commitment to such hard terms, including a series of reforms, the international financial institutions would not finalise the deal. And it is also clear that the government has agreed to comply.

The recent monetary tightening by Bangladesh Bank (BB) is nothing but a reflection of that. To fight inflation, IMF always relies on monetary tightening by raising the interest rate. An annual average inflation rate of above 8 percent is a strong ground for the fund to put pressure on BB to hike rates. By raising the credit requirement ratio and statutory liquidity ratio in mid-December, the country's central bank has actually complied with IMF's requirements and that may help the government to get $1 billion.

The move to increase the energy price is also in line with IMF's requirement. The government has already raised the price of furnace oil and is actively considering petroleum prices. The argument backing such a price hike is to align with international prices.

Reforms in the financial sector include privatisation of the government-owned commercial banks, which will be another condition presumably going to be placed by IMF.

But the basic question is, what are the actual benefits that the country will get by such a small credit from IMF?

One should keep in mind that the whole amount will not be disbursed in an instant. Rather, it will be made in instalments. For instance, each instalment may be worth around $150-$200 million and every instalment will be disbursed every quarter or four months. Thus, it will take one and half years or more to get the full amount.

Most importantly, the measures taken by the government to fulfil the commitments will be reviewed. For this, several targets have to be set for each period. No fund will be disbursed if the fund's review finds that targets are not achieved in the stipulated time. And there is a wide possibility that the government will not be able to comply with some commitments.

So, there will be a chaotic situation in the middle of the loan programme due to half-done steps or measures. Obviously, the government will lose interest to carry some so-called reforms when the IMF will reject to disburse further funds. But the country has to repay the loans already taken in the near future.

One presumption for the IMF loan is that it would not create any inflationary pressure as the amount will not be added to broad money (M2) as the central bank will absorb it. It appears that the central bank governor has already lost his enthusiasm on the '$10 billion plus' foreign exchange reserve.

It is true that the balance of payment is already under pressure. In the first five months (July-November 2010) of the fiscal 2011, the current account surplus declined to $56.3 million, which was $167.4 million in the same period in fiscal 2010. The overall balance turned into the red by $58.4 million in the period under review, which recorded a surplus worth $215.6 million in the July-November period of 2010.

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Another contentious loan is the $1 billion credit from India, which is basically a suppliers' credit. A suppliers' credit binds the loan recipient to purchase or import goods from the selected firms of the country that is financing the credit. Under the arrangement, the supplier (India) issues a line of credit ($1 billion) to the importer (Bangladesh), assuming that the client can demonstrate to the supplier that the importer is credit worthy.

The $1 billion credit line was announced in the joint-communiqué issued during Prime Minister Sheikh Hasina's visit to New Delhi in January 2010. Initially, the Bangladesh government kept the details of the credit arrangement a secret. Even the economic relations division (ERD) was kept in the dark.

But when official negotiations began, it was revealed that the credit line focused on building and improving infrastructure that is essential for the transit India is likely to get from Bangladesh. EXIM Bank is financing the loan on behalf of the Indian government. The terms agreed upon by some over-enthusiastic policy-makers of the country make it difficult to implement the projects by using the Indian loan.

For instance, once a project is approved, Bangladesh has to procure goods and materials and it will take a longer time in some cases. It is due to some bureaucratic complexities between the two governments. This will ultimately delay project implementation and Bangladesh has to pay commitment charges.

In fact, the 20-years loan, with a 5 year grace period, is subject to 1.75 percent in annual interest, which is, no doubt, low. But the annual commitment charge of 0.25 percent is applicable for the non-implementation of any project within a year of approval. And there will be complexities, as prior approval of the Indian foreign ministry in every project is a must.

Against this backdrop, a logical question can be put in front of the policymakers -- does Bangladesh really need these two loans? Or, does the country not have the capacity to take reforms or construct infrastructure without such small loans? Even if the loans are essential, why have the policymakers failed to strongly negotiate, so that the terms and conditions become more favourable to Bangladesh?

Policymakers definitely have their own arguments, no matter how irrational those are. But one thing is clear. The government has not expedited local resource mobilisation with proper planning. Rather, it looks for costly credit as an immediate solution.

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China's drought could have serious global impact

AFP, *Beijing*

Wide swathes of northern China are suffering through their worst drought in 60 years -- a dry spell that could have a serious economic impact worldwide if it continues much longer, experts say.

Some areas have gone 120 days without any significant rainfall, leaving more than five million hectares (12.4 million acres) of crops damaged -- an area half the size of South Korea -- China's drought control agency said Sunday.

There are fears that the problem could send global prices soaring at a time when food costs are already causing governments headaches. According to the UN last month world prices broke their peak levels of 2008 to hit a record high.

"If the dry spell continues into March or April, wheat production could be seriously affected, with losses of more than 10 million tonnes," Ma Wenfeng, an analyst at Beijing Orient Agribusiness Consultants, told AFP.

"China would be forced to boost its imports."

More than 2.5 million people lack drinking water, particularly in the eastern and central provinces of Shandong and Henan, which each have around 95 million inhabitants.

Weather authorities are not forecasting much rain over the next two months for the regions around Beijing, in the Yellow River basin and along the Huai, the waterway that divides the rice-plenty south and the wheat-growing north.

Shandong's Rizhao city, which means "sunshine", has suffered from its longest drought in 300 years, stretching back to September 11, according to local media.

Beijing meanwhile has not seen any rain or snow for 100 days -- its worst run since 1951. The water shortage is also expected to worsen as warmer weather kicks in after two months of particularly cold temperatures.

In some areas, the earth is all cracked up and if rain does not fall in the next few weeks, the wheat that farmers sowed in autumn might not even germinate when the weather warms up.

Around the world, wheat exporters such as the United States, Russia or France are closely monitoring the weather forecast not only for China but also for India, which is experiencing an even worse drought, according to Ma.

AFP

A Chinese farmer shows the dried vegetable seeds at his drought-stricken fields in Zhouping, east China's Shandong province.

China and India are both the world's largest producers and consumers of wheat.

"If production goes down in both countries at the same time, the impact on prices will be considerable," he warned.

Chen Lei, minister for water resources, said Sunday that two-thirds of Chinese cities are short of water. The nation's per capita water resources only amount to 28 percent of the global average.

For the moment, the economic impact of the drought has been mitigated by China's "big stocks of wheat and rice", Ma said.

These are the result of a rise in prices both in China and abroad over the past few years, which has encouraged farmers to grow grain.

But with soaring food prices already weighing on people's minds, the psychological impact of the drought -- and its potential effect on prices -- is quite big, said Ren Xianfang, a Beijing-based analyst with IHS Global Insight.

China's consumer price index rose 5.1 percent year-on-year in November -- the fastest rate in more than two years. Cereal prices increased 14.7 percent year-on-year.

The government has said it will hand out 2.2 billion yuan ($334 million) in immediate drought relief aid.

It will also invest four trillion yuan over the next decade to improve water stocks and distribution, amid warnings of worse to come.

"With the urbanisation planned for the next five years, the shortage will become even more acute," warned Ren.

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