

Decline in savings downs investment

Govt's greedy tax policy may drive away small savers from formal banking

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Each month, Ayesha Amin, a housewife, aims to put Tk 5,000 of the money her husband hands over to her for the running of the house, in her savings account.

She puts the amount into a deposit pension scheme (DPS) with a local bank in her two-year-old son's name. As a housewife, she has no independent source of income, so this is her way of contributing to her son's higher education in a foreign university.

On some months, she even manages to save away Tk 7,000. But such amounts of savings from monthly expenses are set to become a distant

segment of society means a big chunk of investment that is lost.

Because, in economics, it is said that the level of savings equals the level of investment as investment needs to be financed from savings. If people save more, it enables the banks to lend more to firms for investment.

An economy where savings are very low means that the economy is choosing short-term consumption over long-term investment. To starve the economy of investment can lead to future bottlenecks and shortages.

And the Harrod-Domar model of economic growth suggests the level of savings is a key factor in determining economic growth rates.

more efficiently through technological advances.

Whilst in the long-term savings are an important factor in determining investment, in the short-term a rapid rise in savings can cause a fall in consumer spending—which can lead to a recession.

Bangladesh's tremendous growth momentum in the past three years is down to consumption for the most part, so policies that encourage savings can take the winds out of the economy's sails.

Subsequently, a rapid rise in savings would not cause an equivalent rise in investment. Although banks would see a rise in their deposits, they would become reluctant to lend to firms because the economic outlook would have become pessimistic by then.

Also, in a recession, firms may not want to invest even if banks are willing to lend at low rates.

In short, a happy medium has to be reached—and that is where the government fell short this time and in the past.

Asheen Hossain, a first-year student at Dhaka University, stows away half of the salary he draws from a part-time job he secured six months ago in a high-interest-bearing savings account with a local bank.

He was hoping to buy a top-of-the-line mobile phone with part of the amount saved.

But, the bank deducts 15 percent of his interest income as tax, which is extremely unfair given that his annual income falls comfortably below the income-free tax ceiling of Tk 2.50 lakh.

The taxes on his savings account do not end here: he has to pay 15 percent value-added tax on the account maintenance fee.

"I am starting to see no merit in keeping the money in the bank. I might as well keep it under my mattress," says the disappointed young saver.

His enthusiasm for saving was further damped after he learnt that imported smartphones will become costlier from this fiscal year for the hike in customs duty from 15 percent to 25 percent.

Besides, with the new budget, he all of a sudden found himself with a lower capacity to save, like Amin. Many of the goods and services that he uses regularly have become dearer, like ride-hailing services and mobile phone use.

"I would be pleased if I manage to save Tk 3,000 every month now," said the 18-year-old.

Amin, too, echoed the same.

"It's always the middle-class that has to bear the brunt of government experiments," sighed Amin.

Tax measures anti-savings

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"The excise duty, which is levied in balances in bank accounts, can also be reduced to improve the liquidity situation in the banking sector," he said.

Zahid Hussain, former lead economist at the World Bank Dhaka office, said income, be that corporate, personal income or other, is generally taxed worldwide.

"The point is whether people are benefiting from the expenditures in terms of improvement in public service delivery. Public policies can incentivise saving by taxing consumption through a well-designed value added tax," he said.

"However, he said, tax deduction at source of interest income on accounts of students, and women who are not part of the labour market should be exempted."

On excise duty on bank account, Hussain said excise taxes are sometimes used to implement the "ability to pay" approach to taxation. By taxing items consumed disproportionately by the affluent, excise taxes can help make the taxation system progressive, he said.

Other uses of excises include discouraging consumption of sin products such as alcohol or tobacco, mitigate negative externalities such as pollution and congestion, and apply the benefit principle such as taxing gasoline to link taxes with benefits received from roads, he added.

"Excise tax on bank accounts in Bangladesh has some progressivity but only weakly so. But it is subversive to the financial inclusion agenda and a disincentive for channelising small savings into large investments through the formal banking system. The costs far outweigh the benefits," said Hussain.

On taxing savings, NBR Chairman Md Mosharraf Hossain Bhuiyan said tax on interest earnings has been there for a long time and there is no plan at this moment to waive tax on interest income from deposits of small and marginal savers.

He said tax on interest on savings certificates has been increased to 10 percent from 5 percent in the current fiscal year to discourage purchase and keep the government's borrowing from this high-interest-bearing instrument within target.

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