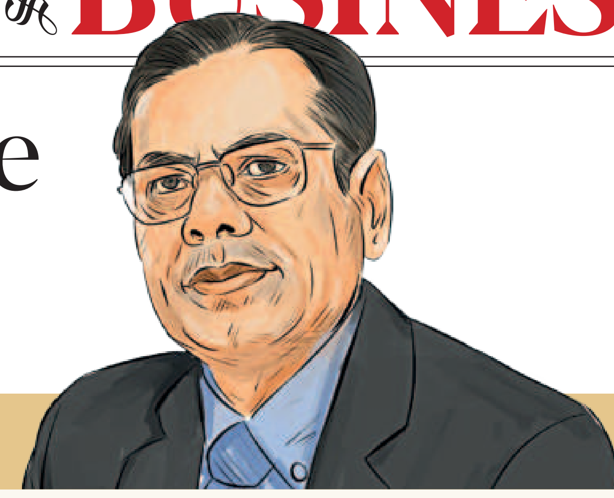
Govt not using full strength to restore macroeconomic stability



Mustafizur Rahman, distinguished fellow of CPD

REJAUL KARIM BYRON *and* MD FAZLUR RAHMAN

The government is not moving at full throttle in bringing discipline to the banking sector, implementing reforms wholeheartedly, taking measures against syndication, and bringing money launderers under the rule of law, said a top economist.

Mustafizur Rahman, a distinguished fellow at the Centre for Policy Dialogue (CPD), said the government is taking various steps and embracing reforms to mitigate challenges in the economy and lower inflation.

"My concern is that they are not going at full strength. They are going one step forward, two steps backward," he added.

"I see half-hearted initiatives, but taking the steps to its logical conclusion is not there because that will hurt a number of people. Whether it will harm those people is at the end of the day a political decision."

According to Rahman, macroeconomic management, good governance, reforms, and zero tolerance to all forms of anomalies will be required if the upcoming budget is to achieve its objective of macroeconomic stability and bringing down inflation.

The former professor of accounting said the budget should look at the pressure heaped on marginalised groups, fixed-income groups and low-income people, and how they can be helped through budgetary allocations, fiscal policies and fiscal incentives.

He requested the government go a bit slow on transport infrastructure. However, the priority should be to complete ongoing projects rather than taking up new ones.

In rural areas, the family card programme needs to be expanded and entitlements should be strengthened. In urban areas, the government should think about introducing urban rationing for workers.

Since children are becoming a major victim of the ongoing macroeconomic problems, Prof Rahman called for launching a midday meal at schools to strengthen their nutrition intake.

Also, there should be renewed effort to enhance the country's revenue GDP ratio, which is one of the lowest in the world.

He thinks digitalisation of the taxation system could be a major initiative that this budget could take and allocate money for both human resource development and technological upgradation of the National Board of Revenue.

He said almost the entire annual development programme is being financed from borrowed money. The burden of debt servicing is increasing.

"As a result, we are ending up in a situation where we are borrowing in order to pay the borrowed money. This is unsustainable."

The government should not take much money from the banking sector to meet the budget deficit as it could crowd out the private sector. A large part of it should be financed through external sources.

This is because in the case of borrowing from domestic sources, the interest payments have gone up quite significantly, from 9 percent to 14 percent.

Prof Rahman also says there might be natural contraction in demand for investable resources by the private sector because the costs have gone up. If the private sector demand for credit comes down, it will have a knock-on effect on private sector investment.

In Bangladesh, private sector investments have stagnated at 23 percent to 24 percent of the GDP over the last few years.

Prof Rahman said the interest rate is only one component of the cost of an entrepreneur. There are many other components, including the transport cost, cost of doing business and interaction with various government institutions.

If these cannot be strengthened and the costs decreased, obviously entrepreneurs, both domestic-oriented and export-oriented, will lose their competitiveness.

The good side is that because of the significant depreciation of the taka, the export sector has regained some competitiveness. If a conducive business environment is not there, the depreciation advantage will not translate into a competitive advantage.

He said the management of the supply chains is very weak and many of these supply chains have been overtaken by various corporate houses. And many of the inputs are controlled by only a few.

The government needs to see whether there are barriers to entry for import of rice or anything, he said.

He said in other countries, institutions like the commerce ministry, the consumer rights department, and the competition commission do the monitoring, surveillance and market control.

Sometimes, the supply from the government will stop in order to stabilise the market and sometimes they will go for open market sale.

"All of these should be done in an evidence-based manner and in a forward-looking manner. Imports should be done in a foreign-looking manner," the economist said.

The banking sector has been facing major problems and the measures aimed at bringing them down seem to be taking it one step forward, two steps backward.

"Good governance is essential in terms of not only ensuring value for money but also tackling the current challenges."

"At the end of the day, these are political decisions."

"Often, we hear about zero tolerance against this type of anomalies. But on the other hand, we also see contradictory steps: people are not paying taxes and taking money outside. But in the budget, they are given various incentives."

He said some are paying 30 percent in income tax while others are not paying anything and then they are allowed to whiten the money at 7 percent.

"So, this type of contradictory signal is not good for the economy."

He said it is time now to gradually phase out the 2.5 percent incentive given to remitters since the taka has depreciated by more than 35 percent in the past two years.

He said predictability should be given to entrepreneurs so they know how long they would continue to enjoy it and when it will be discontinued.

Imports are being made at Tk 117 per USD against Tk 86 two years ago.

Obviously, this will have a knock-on effect on investment, employment and the purchasing power of the common people, he said.

"It remains to be seen how to bring back money that has been laundered and break the syndication in the supply chain," he added.

INFLATION BATTLE must be at the centre of budget

Selim Raihan, executive director of Sanem

REJAUL KARIM BYRON *and* MD FAZLUR RAHMAN

Fighting raging inflation and putting the economy back on track have not been taken seriously as evidenced from the government's delayed response, which set the scene for one of the worst economic crises in its history and an unprecedented prolonged period of higher consumer prices, said an economist.

Selim Raihan, executive director of the South Asian Network on Economic Modeling (Sanem), a think-tank, said the measures that were taken to curb inflation and put the economy back on track have failed because either the steps were not right or they were not taken on time. Therefore, their effectiveness weakened.

He said raising the interest rate to make funds costlier was the only tool or one of the most vital tools available to the central bank. But by the time the Bangladesh Bank started increasing the interest rate, some new complications had already surfaced.

Another wrong policy of the government was borrowing from the central bank since it did nothing but inject new money in the market system, he said.

"And it was done at a time when there was high inflationary pressure. This means the government did not understand the gravity of the situation. This fuelled inflation."

"Inflation should be at the centre point of the budget," he said during an interview with The Daily Star recently.

Selim Raihan, a professor of economics at the University of Dhaka, said there was a solid economic foundation in the decade leading up to the Covid-19 pandemic, which hit the world in early 2020. The economy has moved off track, and the foundation is getting weaker.

Currently, Bangladesh is passing through a difficult time owing to multiple factors such as the lingering impact of the coronavirus pandemic and the Russia-Ukraine war. The ongoing geopolitical tension in the Middle East has added more uncertainty.

"Therefore, it remains to be seen whether the budget can address the difficult issues and take appropriate measures."

The new budget should concentrate on expanding social safety net programmes as much as possible for the next year or so, he said.

Bangladesh has one of the lowest spending for social programmes in terms of GDP compared to many countries. Additionally, there are allegations of wrong targeting and corruption.

Bangladesh also has one of the lowest tax-to-GDP ratios in the world. Still, it has been able to limit the budget deficit to less than 5 percent year after year. It was possible by cutting important spending on health, education, and social protection.

Prof Raihan said: "The very success story of macroeconomic stability came at a very high cost and it didn't really help human capital formation."

He also touched upon the challenges facing the banking sector. "What we are witnessing is the accumulated result of the past failures."

The government has begun phasing out direct subsidies, but Prof Raihan thinks the move should have been initiated when the going was good.

He said the latest hike of the exchange rate will again add fuel to inflation. "But there was no alternative to doing that because the reserves are falling."

Now, the problem is with the current reserve position, he said.

"Even if the country wants to attract more FDI, foreign investors will not feel safe coming to Bangladesh because they will fear that if they come and want to repatriate their profits, banks will not be able to do so owing to the forex crisis."

He said the shift from a fixed interest rate to a flexible interest rate and from a fixed exchange rate regime to a more flexible exchange rate regime proves that there are some realisations among the policymakers, albeit belatedly.

The borrowing would increase as the government will face more pressure since the reserves are not going up.

"If there is indiscriminate borrowing and it is not really based on proper feasibility studies, what will happen is that you shift the burden from the present to the future," he warned.

Thanks to the International Monetary Fund (IMF) conditionalities linked to the reforms in the financial sector and taxation, there is a realisation that these sectors need to be reformed.

But there is a serious vested interest in these sectors. There is a coalition comprising a segment of businessmen, bureaucracy and political elites that do not really want any reforms because they are the beneficiaries of the current system, he said.

He said because of the IMF's pressure, the government is trying to lift tax exemptions. But imposing some taxes on people or sectors will be a cosmetic kind of change and will not really bring a structural shift in revenue collection.

"We need to widen tax coverage. For that, reforms in the NBR's are needed."

Prof Raihan said the decade of macroeconomic stability unfortunately was a lost decade of human capital formation.

"There are many mega projects to build physical infrastructure. But we never heard of mega projects for social infrastructure. No country in the world will be able to show that they achieved a high level of income and development without investing heavily on education."

Prof Raihan said unfortunately, in Bangladesh, any major reform efforts actually stem from external pressure.

He cited the example of the VAT reforms in the early 1990s and the trade policy reform in the 1980s and 1990s that came through the World Bank and IMF programmes.

When the government feels external pressure, it initiates reforms. However, in certain cases, the government does it half-heartedly because it doesn't own the reform programme.

"When you don't own the reform programme, you fill it out just to meet the conditionality. That makes me anxious."

"When you have a decision-making process like this, policymakers sometimes are unable to understand the reality, don't take the right measures at the right time, and when they don't own the programme, then what you see is very hodgepodge kind of stuff."