

TURNING THE TIDE

Critical reforms to correct 15 years of misrule

STAR BUSINESS REPORT

As Bangladesh enters a new era following the ouster of the Sheikh Hasina-led Awami League government, which ruled over the nation for 15 years and is responsible for countless financial wrongdoings, the need of the hour is to reform the overall system of governance.

Nearly all sectors became corrupt in the hands of cronies who weaponised their political influence and carried out misdeeds, negatively impacting the economy.

In recent years, Bangladesh's economy has been under tremendous pressure due to fast-depleting foreign exchange reserves and stubbornly high inflation.

Alongside that, job creation is falling, income inequality is widening, GDP growth has slowed and the tax-to-GDP ratio has not registered an uptick.

The banking sector is struggling with a record level of non-performing loans while the stock market has remained sluggish due to a confidence crisis.

Additionally, the energy sector is eating up huge chunks of subsidies from government coffers, and there has been little progress in export diversification, with the RMG sector continuing to dominate the export basket.

However, the biggest hurdle to the overall business environment is the fact that corruption has permeated all facets of society, posing a significant barrier to attracting foreign investors.

After the political changeover, people's demands to implement reforms are at an all-time high. In fact, reforms are the primary demands of the people expected from the interim government.

The following is a sector-by-sector breakdown of planned reforms along with measures that experts suggest should be taken to restore good governance.

Reforming the banking sector

The banking sector has been debilitated by rampant corruption and irregularities over the past 15 years.

Non-performing loans (NPLs) have soared, with many banks now in the red due to scams executed by influential individuals who weaponised their political affiliations.

In 2008, when the Awami League won the first of four consecutive general elections, soured loans in the banking sector stood at Tk 22,480 crore.

By the end of June this year, the amount had soared to over Tk 200,000 crore, accounting for over 12 percent of the total disbursed loans in the banking system, as per Bangladesh Bank data.

Non-bank financial institutions (NBFI)s are in a similarly fragile situation.

However, under newly-instated Governor Ahsan H Mansur, the central bank has moved quickly, reconstituting the board of directors of several troubled banks.

Furthermore, the interim government announcing its intention to fulfil a long-standing demand by forming a banking commission is expected to go a long way to restoring good governance to the sector.

Another measure, as revealed by the central bank governor, will be the formation of three task forces to ensure good governance.

However, there remain areas in urgent need of attention.

Industry insiders opined that forming new boards for troubled lenders would not be enough by itself.

new boards should be held accountable, such as by being asked to provide specific timeframes and plans to revive the ailing lenders, they said. The BB should then analyse the plans and gauge whether those measures alone will be enough.

Analysts said speeding up default loan recovery and bringing back laundered money should be prioritised.

They added that the central bank's focus should also be on NBFIs.

Exchange rate management, boosting forex reserves and reducing irregularities at banks are among the other challenges that the central bank must combat.

Ensuring full autonomy of the Bangladesh Bank and formulating a plan for the reduction of NPLs are also imperative.

Another piece of advice from experts is to prevent a single person or business from securing ownership at multiple banks.

Rebuilding confidence in stock market

The stock market of Bangladesh has been suffering from a dearth of investor confidence, chiefly stemming from a lack of good governance. As such, massive reforms are urgently required.

The interim government has made some changes to reverse the grim scenario, moving swiftly to appoint former top banker Khondoker Rashed Maqsood as the chairman of the Bangladesh Securities and Exchange Commission (BSEC).

At the start of September, the BSEC also formed a five-member committee to investigate irregularities and corruption of the past.

It formed another committee specifically to investigate the market involvement and activities of Mohammad Saiful Alam and Salman F Rahman – owners of controversial conglomerate S Alam Group and Beximco Group, respectively.

However, while the measures were appreciated, there remains a lot of ground to cover.

Experts believe the commission should first investigate the involvement of those within its ranks in illicit activities such as manipulation and punish them accordingly.

They added that the BSEC's main priority is to ensure the entry of good companies, meaning that quality initial public offerings (IPOs) should be prioritised.

In order to do so, they said the regulations regarding book-building methods must be revisited.

Additionally, it must ensure that all stakeholders and the regulator play a proper role in the IPO process.

Another long standing demand to attract good companies is to widen the tax gap between non-listed and listed companies.

At the same time, if any company ceases production for a long time, it should be delisted from the stock exchange.

They added that this is the best possible time to bring all profitable state-run companies to the stock market.

Along with that, the BSEC should monitor mutual funds stringently so general investors are attracted to such investments.

The BSEC should also decide to implement policy changes only after conducting thorough research.

Surveillance and monitoring should be strengthened to bring vibrancy back to the secondary market and reduce insider trading and other forms of manipulation.

Other suggestions include ensuring good quality financial reports and keeping track of intermediaries' activities so they cannot embezzle investor funds.

Most of all, the BSEC should not consider what impact its decision may have on the stock index. Its sole consideration when making decisions should be to ensure good governance.

serve as a salve for certain ailing sectors, entrepreneurs also urged measures to improve the general business environment.

One key demand is to improve the ease of doing business, which would encourage more investment and result in more jobs.

They said the government can achieve this by focusing on curbing extortion at every level and removing bureaucratic tangles.

Another suggestion is to update commercial laws with the aim of fully digitalising processes relating to international trade, such as issuance of invoices and signing of contracts, to reduce the scope for fraudulence and money laundering.

Most businessmen, citing that they often had to pay bribes, also demanded massive reforms to service-oriented government entities like the Registrar of Joint Stock Companies and Firms, and the Department of Environment.

They also stressed the need for reforms to the Bangladesh Investment Development Authority.

Fixing fragile trust in insurance industry

Insurance companies in Bangladesh have been struggling to take off owing to low confidence in the sector as a consequence of the low claim settlement ratio.

In Bangladesh, the claim settlement rate stood at 65.19 percent in 2023, according to data from the Insurance Development and Regulatory Authority (Idra).

This is far worse than the global average of 97-98 percent. In India, the claim settlement rate stood at 98.45 percent in the fiscal 2022-23, according to media reports.

The scenario grows even bleaker when one takes into consideration that over 26 lakh insurance policies have lapsed in the last 14 years.

The industry has also failed to grow. In fact, by some metrics, it has regressed. In 2009, the total number of policies stood at nearly 1.12 crore. That number fell to 85.88 lakh in 2023.

To raise confidence in this sector, the government should strengthen the regulator, experts said.

It should also conduct a thorough investigation to find how the insurance sector was corrupted and who is responsible for that.

The Idra should regularly monitor whether any insurer spends more than permissible limits as well as where they invest their funds.

If the government takes strict action against insurers in case of failure to settle claims, consumer confidence will be bolstered.

Ensuring transparency in energy sector

The most vociferous demand in terms of the energy sector has been the abolishment of the 'indemnity act', formally known as the Quick Enhancement of Electricity and Energy Supply (Special Provisions) Act 2010.

The interim government has already stopped using the act and also formed a committee to identify the nature of the deals signed by the previous government under this act.

Instead, the interim government began using Public Procurement Rules 2008 in importing liquefied natural gas (LNG).

Another common reform proposal regarding the sector is to strengthen the Bangladesh Energy Regulatory Commission, which was largely incapacitated by the previous government.

On December 1, 2022, the government issued an amendment to the Bangladesh Energy Regulatory Commission (BERC) Act, 2003, which empowered the power and energy ministry to set fuel and electricity prices under special circumstances.

Previously, prices could only be fixed by BERC through a process that included public hearings.

The interim government has already said they will not hike energy prices just by executive orders, skipping the public hearing.

However, energy sector experts pointed out numerous other areas that need to be reworked.

For example, the Integrated Energy and Power Master Plan (IEPMP) should be revised as there are faulty energy and power demand forecasts. It also encourages coal exploration and promotes LNG imports.

They further urged the government to review all procurement and bidding processes, phase out inefficient quick rental power plants, and prioritise the identification and assessment of renewable energy resources.

Analysts recommended forming a probe body to identify anomalies in pre-paid meters.

They also suggested restructuring the Power, Energy and Mineral Resources Ministry to empower the Sustainable and Renewable Energy Development Authority and make it the sole authority to implement energy transition issues.

Some other proposals include establishing an 'Energy Sector Reform Commission', removing cadre officers from the managing bodies of energy-related companies, replacing top officials in power sector companies, limiting the ministry's role to policy regulation, ensuring government companies provide services without profit motives, and identifying and prosecuting corrupt officials.

Digitalising revenue collection

One repeated recommendation is to reform the National Board of Revenue through the establishment of two separate wings – one for policymaking and another for tax, customs duty and VAT collections.

Other suggestions include expanding the tax net, enabling online submission of income tax returns and fully digitalising the taxation process.

Zahid Hussain, a former lead economist of the World Bank's Dhaka office, said the biggest challenge is to increase the tax-GDP ratio, which stands at slightly less than 9 percent, to around 15 percent, which is typical of countries similar to Bangladesh's level of income. "This is daunting, even in

the medium term of 5 to 7 years, considering our history in revenue mobilisation. Most of the required increases will have to come from tax revenues," he said.

Rate hikes are extremely difficult when inflation is close to double digits and food inflation is even higher. The cost of doing business is also already excessive. So, the biggest challenge is to reduce leakage of tax revenues to third parties such as tax officials and expand the tax net, he said.

The budget for the current fiscal year reduced several tax exemptions and allowances, increased value-added tax (VAT) rates to the 15 percent statutory rate for several products, added a 30 percent slab for personal income exceeding Tk 20 lakh per annum and increased rates on select products like tobacco.

These must be maintained and implemented as the interim government revisits the budget.

The interim government has a unique opportunity to immediately reform tax policies and curb activities that create opportunities for "negotiation" and corruption.

The government has a commitment under an International Monetary Fund (IMF) programme to finalise the draft Medium and Long Term Revenue Strategy (MLTRS) along with a time-bound implementation framework by the end of December this year.

"We expect the MLTRS to come up with actionable measures to widen the tax net, improve compliance, reduce leakage and provide a road map for the digitalisation of tax collection," Hussain added.

Prioritising efficiency in public finance

Five key principles have been identified that should be taken into consideration for public finance management – enhancing the fiscal space, prioritising expenditure, prioritising foreign financing, ensuring good governance, and protecting the interests of vulnerable and disadvantaged groups.

Any attempt to enhance the fiscal space should focus on generating more resources as well as sealing the leakages.

Austerity measures must be maintained in a way that their impact on the social safety net as well on health, education, agriculture, and small and medium enterprises becomes less burdensome.

Exit plans will need to be formulated in the cases of fiscal incentives currently being provided.

Considering the declining foreign exchange reserve situation, the government should prioritise implementing all foreign-funded projects under the Annual Development Programme.

It should place higher priority on implementing projects that are close to completion.

