Mustafizur Rahman

Widen tax net, cut leakages to ease fiscal pressure

Mustafizur Rahman, distinguished fellow at CPD, says the revenue sector requires immediate attention

REJAUL KARIM BYRON *and* AHSAN HABIB

Ahead of the fiscal year 2026-27 (FY27) national budget, the government faces mounting fiscal pressure amid high inflation and low investment at a time when the global geopolitical situation remains volatile, said Prof Mustafizur Rahman, distinguished fellow at the Centre for Policy Dialogue (CPD).

In an interview with The Daily Star, he said the revenue sector requires immediate attention, while trade challenges and inefficiencies in the Annual Development Programme (ADP) must also be addressed.

FISCAL PRESSURES MOUNT

Bangladesh's upcoming national budget will be one of the most challenging in recent years, as the government grapples with inflation, debt pressure, global uncertainty, and rising public expectations, he said.

The FY27 budget will need to address "multi-dimensional challenges" amid persistently high inflation, rising living costs, weak investment, and external vulnerabilities.

He said the government inherited significant economic difficulties that cannot be ignored while preparing the budget. At the same time, it must fulfil election pledges related to healthcare, education, social protection, and employment generation.

"The government is presenting the budget against the backdrop of a difficult global environment," he said, referring to the ongoing Middle East conflict and its impact on energy prices, import costs, and macroeconomic stability.

Rahman said people expect relief after years of inflation that have eroded purchasing power and living standards, particularly among low-income groups.

"People now expect better public services and stronger social protection from the government," he said.

To meet those expectations without excessive borrowing, the government must prioritise domestic resource mobilisation, he argued, adding that Bangladesh cannot continue relying heavily on bank borrowing and external lenders to finance expenditure.

THREE PRIORITIES FOR REVENUE

Rahman identified three immediate priorities for the revenue sector: reducing leakages, broadening the tax base, and finding innovative sources of revenue.

He said corruption, weak governance, and inefficiencies continue to undermine tax collection, depriving the government of resources needed for public spending.

Bangladesh must expand the tax net instead of repeatedly burdening the same taxpayers, he argued. Many individuals and businesses remain outside the system, while VAT collected from consumers often does not fully reach the treasury because of leakages and weak enforcement.

"I fully endorse the proposal that rates should remain relatively low but become more universal," he said while discussing VAT and income tax reforms.

The economist also stressed the importance of technology-driven tax administration. He welcomed moves towards online VAT registration and digitalisation but warned that isolated systems would not be effective unless they are integrated and interoperable.

Drawing comparisons with India, he said tax authorities there can compare declared income with spending patterns through integrated databases. Bangladesh could adopt similar systems to strengthen compliance and reduce tax evasion.

Rahman also suggested gradually introducing new forms of taxation, including wealth and inheritance taxes, to address widening inequality. Fiscal policy, he said, should not only raise revenue but also reduce disparities in income, consumption, and assets.

REPRIORITISE SPENDING, IMPROVE IMPLEMENTATION

On the expenditure side, Rahman said the government would need to reprioritise spending to fulfil commitments related to education, healthcare, and social safety net programmes.

The ruling party has pledged to raise spending on health and education to 5 percent of GDP each and increase social protection expenditure to at least 3 percent of GDP.

Current spending remains far below those targets, meaning resources may need to be shifted from other sectors over time, he said, warning that such decisions would be politically sensitive.

He argued that infrastructure spending could be rationalised by reducing waste, corruption, delays, and cost overruns.

"If we can ensure good value for money, then infrastructure spending as a share of GDP can be reduced without compromising outcomes," he said.

Rahman stressed that higher allocations alone would not improve public services without better implementation and governance.

He was particularly critical of inefficiencies in the ADP, saying public projects in Bangladesh frequently suffer from inflated costs, delays, and weak oversight. On average, project costs and implementation periods rise by 30 percent to 40 percent, he said.

He called for stronger feasibility studies, tighter monitoring, and greater accountability. Projects nearing completion should receive priority, while approval of new projects should be approached more cautiously given rising debt and fiscal pressure.

The economist also warned against expanding the ADP aggressively without improving institutional capacity, procurement systems, and implementation quality.

INFLATION, TRADE CHALLENGES REMAIN KEY CONCERNS

On inflation and monetary policy, Rahman said Bangladesh faces a difficult balancing act. While high interest rates are hurting investment and job creation, inflation remains too high to justify aggressive monetary easing.

However, he argued that inflation is not driven solely by monetary factors. Weak market management, high logistics costs, inefficiencies at ports and customs, and poor supply-chain governance are also contributing to rising prices.

"If the government can improve market management and reduce the overall cost of doing business, inflationary pressure can ease even without relying only on monetary policy," he said.

Rahman also discussed Bangladesh's external trade challenges as the country prepares to graduate from the least developed country (LDC) category.

He said export diversification, free trade agreements, and stronger compliance standards would become increasingly important in the coming years.

Bangladesh still depends heavily on a limited number of products and export markets despite years of discussion about diversification, he noted. Meanwhile, competitors such as India and Vietnam are moving aggressively to secure free trade agreements and attract foreign investment.

To remain competitive, Bangladesh must improve logistics, reduce lead times, strengthen labour and environmental standards, and create a more investment-friendly environment, he said.

He also urged the government to treat any extension of the LDC graduation transition period as an opportunity to accelerate reforms rather than delay them.

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Zahid Hussain

Budget should prioritise resilience over expansion

Zahid Hussain, former lead economist of World Bank's Dhaka office, says economy is facing prolonged external pressures

REJAUL KARIM BYRON *and* AHSAN HABIB

Bangladesh's next national budget should focus on strengthening economic resilience rather than increasing spending, said Zahid Hussain, former lead economist at the World Bank's Dhaka office.

He warned that weak fiscal buffers, high inflation, and serious vulnerabilities in the financial sector have left little room for a large or expansionary budget.

In an interview with The Daily Star, Hussain said the economy is facing prolonged external pressures stemming from elevated global fuel, fertiliser, and commodity prices, limiting Bangladesh's ability to absorb further shocks.

"The economy is now facing a global trade shock," he said, noting that import costs have risen sharply while access to essential goods has become increasingly difficult. Even if geopolitical tensions ease, prices are unlikely to return to pre-war levels anytime soon, he added.

Hussain explained that Bangladesh is paying more for imports but receiving less in return, resulting in a net income loss. "The key question is how we will absorb these losses," he said.

He added that policy choices are increasingly constrained by limited fiscal space.

"Except for foreign exchange reserves, most buffers are nearly exhausted," he said, noting that inflation remains above 9 percent and the banking sector is under severe stress.

He said the economy is now facing stagflation -- high inflation, low growth and weak shock absorption capacity -- while election promises and the new government's budget plans are increasing pressure to raise spending.

"How do we balance these conflicting pressures?" he asked.

LIMITED SPACE FOR EXPANSIONARY BUDGET

Hussain said printing money is not a viable option because inflation is already high and could rise further.

"If inflation were very low, money financing might have been considered, but that is not the case," he added.

He also said domestic borrowing is constrained as interest rates are already high, with businesses facing double-digit lending rates. Higher government borrowing would push rates up further and restrict private credit.

A large portion of the budget is already locked into mandatory spending.

IMF projections suggest interest payments could reach Tk 1.7 lakh crore in FY27. In FY26, salary expenditure is close to Tk 85,000 crore, while pension payments exceed Tk 35,000 crore.

"These are mandatory costs that are difficult to reduce," he said, adding that many development projects are already in advanced stages and cutting them would waste past investment.

World Bank studies show that 70 to 80 percent of Bangladesh's public spending is pre-committed, compared to 50 to 60 percent in other lower-middle-income countries and 40 to 50 percent in better-governed Asean economies.

With inflation eroding purchasing power and weak real wage growth, Hussain said tax revenue cannot rise sharply. Bangladesh typically struggles to collect even Tk 4.5 lakh crore.

Given the constraints, he said, "If we respect these constraints -- no money printing, limited domestic borrowing, large fixed expenditures, and rising interest costs -- then a realistic revenue target would be around Tk 5 lakh crore, with a deficit of about Tk 3 lakh crore."

"That would put the maximum feasible budget size at roughly Tk 8 lakh crore."

He warned that financing even this deficit would be challenging. Domestic borrowing needs could exceed safe limits unless external financing rises significantly.

Net external financing may need to reach Tk 1.1 lakh crore, while domestic borrowing of around Tk 1.9 lakh crore would still pressure financial stability.

"For this reason, the overall budget size would need to remain tighter," he said.

He added that concessional financing from the World Bank, ADB, IMF, JICA and other development partners could allow a slightly larger budget without stressing domestic banks.

"Even so, under realistic assumptions, I do not see the government implementing a budget much beyond Tk 7.5 to Tk 8 lakh crore," he said.

STRUCTURAL REFORMS OVER SPENDING PUSH

On the IMF programme, Hussain said challenges go beyond subsidy cuts or electricity price adjustments.

Key reforms in tax policy, exchange-rate management, banking sector restructuring, Bangladesh Bank governance, and separating the National Board of Revenue remain incomplete.

"I don't think simply increasing electricity prices will bring the IMF programme back on track," he said.

Hussain said Bangladesh no longer has the option to prioritise either inflation control or growth.

The problem, he said, is supply-side constraints rather than weak demand.

"If you don't have diesel, LNG, or fertiliser, higher government spending will not increase growth," he said. "Instead, it will mostly lead to higher prices or exchange rate pressure."

He said the budget should prioritise resilience by protecting food security, energy security, healthcare, and social protection.

"You cannot cut spending on vaccinations, medicines, schools, or support for the poor and vulnerable," he said.

However, he warned against broad subsidies that often benefit higher-income groups more than those in need.

Hussain said low tax collection is mainly due to a complex tax system and weak administration.

Multiple VAT and customs duty rates, he said, create corruption risks and revenue leakage.

"If the rate structure is simplified and the tax system is automated, revenue can increase without adding pressure on taxpayers," he said.

He called for urgent reforms in energy, banking, ports, regulation and skills development.

Bangladesh has around 30,000 megawatts of installed power capacity, while peak summer demand is about 18,000 megawatts.

"The problem is not power generation capacity," he said. "The real issues are fuel supply and limitations in the transmission grid."

He also highlighted inefficiencies in ports, complex regulations, and weak vocational training.

"Bangladesh exports labour but imports skills," he said.

Hussain said structural reforms, rather than higher spending, now offer the most practical path to improving investment, lowering costs, and stabilising the economy.

He said Bangladesh is still facing a global trade shock, with both import prices and volumes under pressure.

"Prices have increased, and even if you are willing to pay more, it is still difficult to get the required quantities, especially as global supply chains remain strained," he said.

He concluded that Bangladesh needs a more productive economy driven by reforms, not a larger budget based on fragile borrowing.

"Without such reforms, the economy could remain stuck in repeated crisis management, while private investment confidence continues to weaken," he said.

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