

## Background Notes

# Meeting the Challenges of Global Recession and Its Impact on Domestic Economy

## Recommendations for the National Budget 2009/2010

- How to Make the Budget Pro-Poor?
- Subsidizing Crop Agriculture and R & D in Agriculture, Climate Change, and Resource Mobilization
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**Bangladesh Institute of Development  
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# How to Make the Budget Pro-poor?

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## 1. Sectoral Balance of Manufacturing and Agriculture

According to conventional economic wisdom, an acceleration of GDP growth in an economy is expected to be associated with a change in the sectoral composition of GDP. Acceleration of growth in the manufacturing and the tertiary sectors offer prospects of sustained increases in GDP growth rate because of the technological progress associated with such production. The higher productivity also offers promises of higher wage rate than in traditional agriculture.

However, the conventional wisdom should not overshadow agriculture's role in the development process. It will help keep food prices low and will have a large impact on GDP growth of Bangladesh because it has the largest share in GDP of the country.

The lack of complementarity in sectoral growth pattern in Bangladesh is shown by the annual growth rates of GDP from agriculture and manufacturing. In the recent period, in nine out of fifteen years, the annual growth rate of the two sectors moved in the reverse direction. In four years the growth rates of both agriculture and manufacturing declined. Only in three years both agriculture and manufacturing have experienced acceleration of growth rate. In the last four cases GDP growth also accelerated.

**Table 1**  
**Annual GDP Growth Rate in Agriculture and Manufacturing: 1992 to 2008**  
**(at constant 1995/96 Prices)**

Year	Agriculture	Manufacturing
1992	1.39 (+)	7.38 (+)
1993	1.35 (-)	8.62 (+)
1994	-0.65 (-)	8.15 (-)
1995	-1.93 (-)	10.48 (+)
1996	2.03 (+)	6.41 (-)
1997	5.57 (+)	5.05 (-)
1998	1.64 (-)	8.54 (+)
1999	3.24 (+)	3.19 (-)
2000	6.92 (+)	4.76 (+)
2001	5.53 (-)	6.68 (+)
2002	-0.62 (-)	5.48 (-)
2003	3.29 (+)	6.75 (+)
2004	2.41 (-)	7.41 (+)
2005	1.80(-)	8.19(+)
2006	5.23(+)	10.77(+)
2007	4.69(-)	9.72(-)
2008	3.47(-)	7.42(-)

Source: BBS various years.

This inverse relationship is the result of fluctuations in the growth rates of both agriculture and industry. While the fluctuations in agricultural growth have been associated with natural calamities and lack of public investment, the fluctuations of industrial growth have been linked with a variety of factors, including both natural factors, investment and the demand-side forces.

The negative association between GDP growth in agriculture and manufacturing also reflect a natural response of the economy where the work force are involved in diversified occupations. When one type of activity faces a setback, they automatically resort to other types and thus the change of sectoral GDP growth is, at least partly, a reflection of the resilience of the large majority of the small producers and low income groups. However, the magnitude of such automatic response is not expected to be so large as to have a sufficient counter cyclical impact.

It should be highlighted that a much higher GDP growth rate could be achieved if acceleration of GDP growth in agriculture and industry took place simultaneously. In fact, such speeding up of growth in both sectors is essential if the country's economy has to move to a higher growth path. Lack of complementarity in the growth process cannot be afforded if a sustainable growth of the economy is to be achieved. Policy efforts should not, therefore, slacken in one sector when the other sector is observed to perform well.

## **2. Prospects of Labour Intensive Growth**

Pro-poor growth can be achieved through more labour intensive investment. This is essential because LFS data of 1999-2000 and 2006 shows an increase in underemployment rate. In this context growth of agriculture and small and medium industries can have a positive impact. In fact many of the export sectors have higher capital intensity compared to those producing for domestic market. Therefore, in the coming years, if world economic recession slows down our export sectors, policies for encouraging labour intensive sectors oriented to domestic demand can help achieve both ends: acceleration of GDP growth and pro-poor growth through higher employment growth.

## **3. Safety net Employment: 100 Day Employment Generation Programme**

The recent programme of 100 days employment generation has generated substantial debate about its prospects. The second round of the programme has been postponed till next FY. It gives a scope for proper planning and implementation in the next round. Most of the

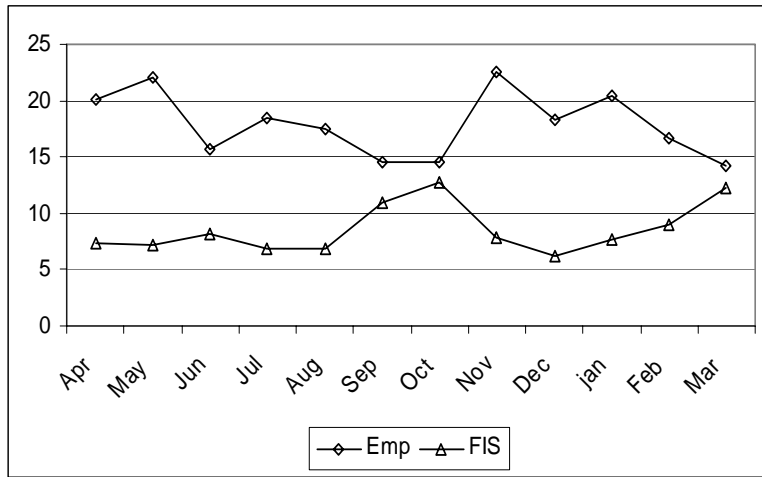
discussions on the subject highlighted two sources of problem: Lack of success in proper targeting and leakage of funds.

Another major problem did not receive attention: this is related to choice of activities where employment could be provided. In the first phase most employment was in earth digging work for building/repair of roads. But where is the place for digging? When the lands close to the road are privately owned, the possibility of sacrifice of surface soil without any compensation would be bleak. Therefore more innovative activities must be pre-planned so that after given employment, the workers are not sitting idle. For adopting useful projects, LGED may be consulted. Local NGOs can help identify waterbodies which can be cleaned, or re-excavated.

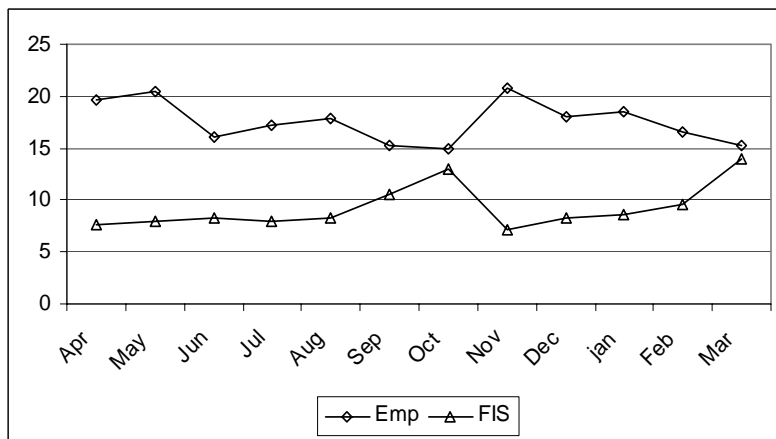
Unemployment among youth with some education is assuming a serious magnitude. For this group, earthcutting may not be attractive. Repair of school buildings, afforestation programmes or even nursery building (growing seedlings) and horticultural activities (in school and college premises etc.) may generate interest.

Another aspect of employment schemes is the timing of the activity. Initially the second phase was planned for February. Then it was pushed to May-June which implied a great risk in terms of availability of target group persons for the scheme. May-June are months of peak activities for boro crop. If some workers are drawn to EG programme, boro producers would suffer from lack of labour and/or high wages pushing up production cost. Therefore it has been a wise decision that the scheme has been further postponed. Recent BIDS research shows that the months of low employment are Mid-September to November and February to March. These are also the periods of higher incidence of food insecurity as well (Figure 1).

**Figure 1 : Employment Days (EMP) & Food Insecurity (FIS)**



**Netrokona**



**Mymensingh**

Source: 'Impact of paid employment and self employment on income and prospects household food security', Rahman R. I; Begum A and Bhuyan, H.R., Draft Report prepared for NFPCSP

The figure clearly shows that during May June, employment reached a peak and in these months there is unlikely to be much demand for employment at lower wages. In this period the incidence of food insecurity is also lower than in other periods.

Therefore, the 100 days EG scheme has a good potential for poverty reduction if it is adopted at the right period of time and for right activities. Some recent studies went further to suggest that the activity may remain in operation for whole year, which is not a practical proposition as it will overstress the implementation capacity and may not find enough supply of workers leading to further leakage of funds.

Background note 2

# Subsidizing Crop Agriculture and R & D in Agriculture, Climate Change, and Resource Mobilization

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Support to agriculture comes in various forms. The most popular manner in which it is given is to subsidize the costs of inputs, particularly fertilizer and fuel for irrigation. Of course, various other fiscal measures may also be used including provision of easy credit, the relative efficacy of these other measures have hardly been researched in Bangladesh. We will therefore discuss here the issues mainly of subsidy in irrigation and for fertilizer.

Electricity for irrigation is subsidized while till last year, diesel for irrigation was not. As diesel run irrigation equipments accounted for the bulk (nearly 70%) of total area irrigated, the lack of support for diesel run irrigation creates an asymmetry in the system. There thus had been a demand for long for subsidizing diesel for irrigation. Last year as the oil prices soared record high, the Government finally decided to provide subsidy for diesel for irrigation. A final amount of Taka 250 crore (initial allocation was Taka 750 crore) was released. Question is should this subsidy be continued, and if so, in what form? Secondly, irrigation in itself is not of much use unless fertilizer is also available adequately and in a cost-effective manner and hence the issue of fertilizer subsidy also should be considered together.

On diesel subsidy last year, there had been certain leakages. But, if the lower value of leakage is used, still some Taka 200 crore or something like 80% of the allocated money had been distributed. But the main problem lied in its distribution system. This was announced rather late, distributed almost at the fag end of the boro period and the listing system was not well-monitored and administered. As a result, while most of the eligible farmers (owning up to 2.5 acres and cultivating no more than 2.5 acres under diesel-irrigated boro) were listed and did receive some money, not much could be used for irrigation or for other production-related purposes. If the Government wishes to continue with such diesel subsidy, alas, again the time is almost up as the boro period will soon end. The thought process, therefore should turn to what can be done for the next boro.

If diesel subsidy has to continue in cash form, the principle should be that it may be given as fixed amount per acre of land. Given that, costs of irrigation with diesel run equipments is estimated to be Taka 5613 per acre (for the eligible farmers), while the costs under electricity-driven irrigation equipments is about one-third less, equalization (under alternative fuel mode) means that the average subsidy per acre for diesel should be around Taka 1500 per acre. This does not take into account the leakage. How to take care of that is another matter. If rather than providing cash, the Government wishes to lower the price of diesel, it will have to be determined in a manner that the subsidy equivalent is similar to taka 1500 per acre. Lowering prices of diesel has two disadvantages, though. First, as most farmers buy water this does not guarantee

that the pump owners will fully pass on the lower costs to water buyers. Secondly, this may induce informal trade across the porous border if prices on the Indian side are higher.

If cash subsidy is given for fertilizer and diesel together, (or fertilizer and electricity together), these two may be combined together into a general farm subsidy. Unfortunately, while fertilizer is available in general, problem does not arise in a price-based subsidy. It is when these are not available easily and supply is limited, that problems of high costs, and others arise. For the time being, therefore, fertilizer may be subsidized in the present manner but inefficient domestic factories should not either be allowed to run or be told to gear up efficiency.

### **R&D in Agriculture, Climate Change and Resource Mobilization**

Bangladesh has an extensive National Agricultural Research System (NARS). This has so far stood her in good stead. But new challenges have cropped up and the NARS will have to perform in terms of development of varieties which are of shorter maturity, drought and salinity resistant and new cropping systems which are capable of producing much more than before from even tinier plots. Many of these challenges remain under a climate change regime in the country. In fact, climate change and the uncertainties that this brings make these tasks of the NARS even more urgent. The whole R&D effort will, however, truly gigantic and would necessitate resources which are possibly beyond the present capacity of the country.

The Government has created a Krishi Gobeshona Foundation (agricultural research foundation) which for the time being is having nearly Taka 80 crore from a project NATP-1). Later it is expected to have the proceeds of the investment from another trust fund of Taka 350 crore. These monies are expected to be utilised for research under competitive grants. However, the grants are likely to be small and used for adaptive research, not the fundamental cutting edge research that has been described in the preceding paragraph. This will necessitate much larger funding than at present. We think that the Government can make a beginning by substantially increasing the resources at the disposal of the NARS, possibly doubling it within 3 years or so. This should, however, be the catalyst for generating more funds from abroad, particularly developed countries.

The adaptation to climate change in developing countries including LDCs is due mainly to the green house gas emission in developed countries and consequent global warming. It has now been accepted as a general principle in climate change negotiations which are expected to be finalised in Copenhagen in December this year that such adaptation has to be fully financed by flow of resources from developed countries. While all the modalities are still being worked out, there are scopes for substantially augmenting external resources over and above the

normal funding. Bangladesh must tap into these resource pools. In fact, this applies to any kind of adaptation like say establishment of desalinization plants along the coast where salinity may have increased due to creeping sea level rise. It is only that Bangladesh has to play her cards well and with substantiated data and analyses.

The Bali Action Plan which has given rise to the present intense phase of negotiations has mandated that every country including LDCs will have to do its bit to lower green house gas emission. Several mechanisms exist for generating funds for such activities. Bangladesh has hardly accessed such funds so far including Clean Development mechanism (CDM), carbon credits and trade etc. It is high time that these avenues be explored. It should also be noted that while grants for mitigation was not much discussed before, this has now been raised by several countries because, LDCs, particularly, were initially exempt from mitigation activities.

There is similarly a huge scope for generating funds for afforesting degraded forests under the REDD principle. For this to happen, however, the forestry officials have to know and be trained in designing such projects.

**SIZE AND QUALITY OF  
ANNUAL DEVELOPMENT PROGRAM**

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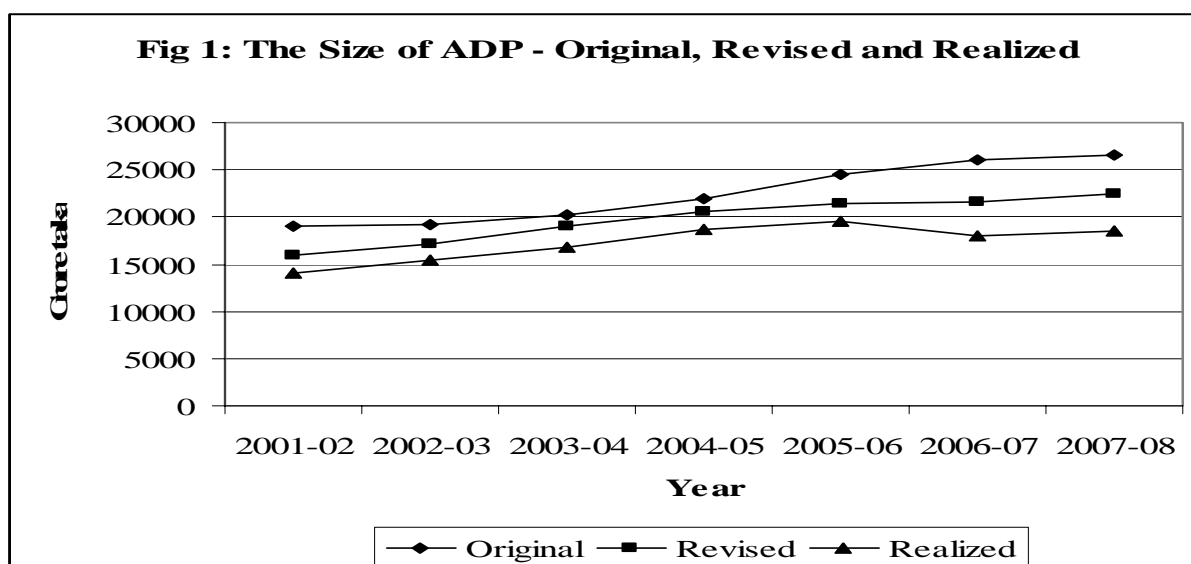
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The Annual Development Program (ADP) is the main conduit through which public investment is channeled in Bangladesh. In recent years, there has been a tendency to set the size of the ADP at a relatively high level. While the main consideration behind larger ADP was achievement of faster economic growth, the use of development projects as vehicles of patronage politics and rent seeking also contributed to the inflated size of the ADP.

Because of weak institutional and absorptive capacity, actual implementation of ADP often fell far short of the target. As shown in Table 1 and Figure 1, since 2001-02, there has always been a downward revision of the original ADP but actual implementation fell short of even the revised ADP target, although as % of GDP the ADP size remained rather modest.

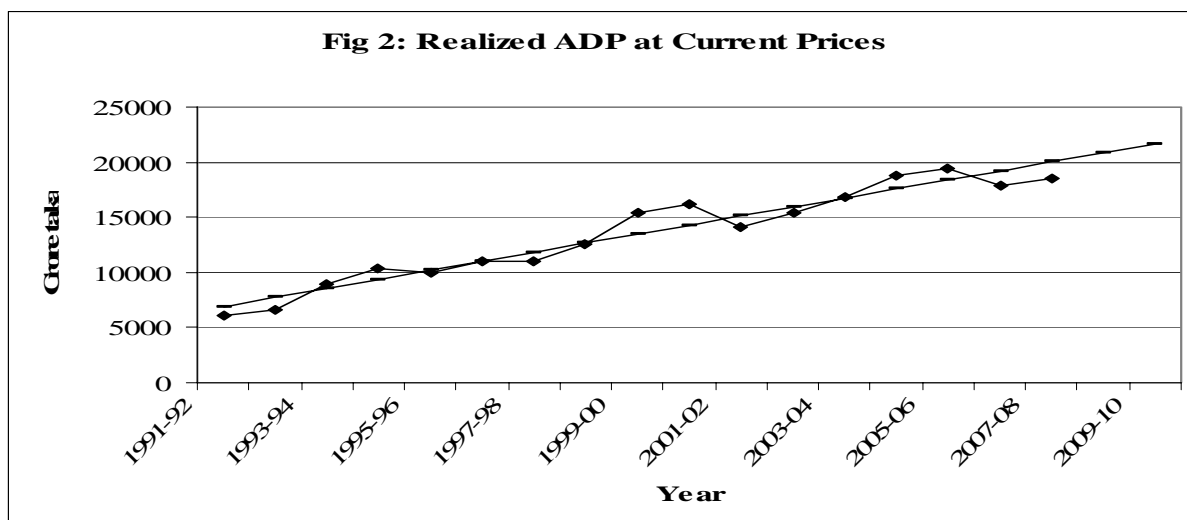
**Table 1: The Size of ADP – Original, Revised and Realized**

Year	Size of ADP (crore taka)			Realized ADP as % of revised ADP	Realized ADP as % of GDP
	Original	Revised	Realized		
2001-02	19000	16000	14090	88.1	5.16
2002-03	19200	17100	15434	90.3	5.13
2003-04	20300	19000	16817	88.5	5.06
2004-05	22000	20500	18771	91.6	5.06
2005-06	24500	21500	19473	90.6	4.68
2006-07	26000	21600	17916	82.9	3.79
2007-08	26500	22500	18492	82.2	3.41



In 2008-09, the original size of ADP was set at Tk. 25,600 crore. As of February 2009, only 34 per cent of the ADP has been implemented. The government is now contemplating slashing down the ADP to about Tk. 23,000 crore. But if past performance is any guide, the realized ADP is likely to be between Tk. 20,000 to Tk. 21,000 crore, falling significantly short of even this revised ADP.

To determine the likely size of realizable ADP in 2009-10, we fitted a straight line to the data on realized ADP at current prices for the period 1991-92 to 2007-08 (Fig 2). On the basis of the estimated parameters, the trend line ( $R^2 = 0.93$ ) suggested realizable size of ADP in 2009-10 to be Tk. 21,679 crore.

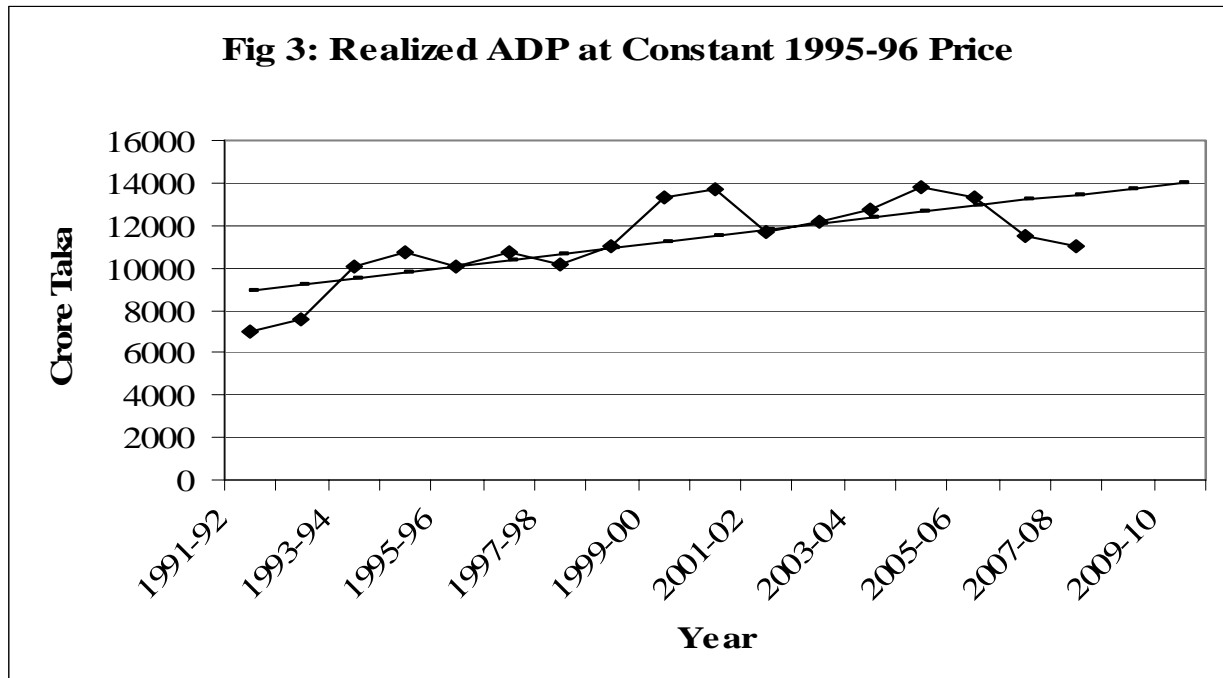


A slightly more optimistic picture emerges if estimation is done on the basis of realized ADP at constant price. Table 2 shows realized ADP at constant 1995-96 price after deflating with GDP deflators. The trend line fitted to the constant price data (Fig 3) shows realizable ADP in 2009-10 at constant 1995-96 price to be about Tk. 14020 crore ( $R^2=0.50$ ). With GDP deflator for 2008-09 estimated at around 181 (1995-96=100), the realizable size of ADP at the beginning of the year 2009-10 works out at Tk. 25,376 in current price. A realized ADP of Tk. 25,376 in 2009-10 would imply growth in ADP at constant price to be almost 22 per cent, which is quite high in relation to recent growth performance of realized ADP (Table 2).

**Table 2: Realized ADP at Constant 1995-96 Price**

Year	Realized ADP at current price (crore Tk.)	GDP Deflator (1995-96=100)	Realized ADP at constant 1995-96 price	Rate of growth of realized ADP (%)
1991-92	6024	86	7005	-
1992-93	6550	86	7616	8.7
1993-94	8983	89	10093	32.5
1994-95	10303	96	10732	6.3
1995-96	10016	100	10016	-6.7
1996-97	11041	103	10719	7.0
1997-98	11037	109	10126	-5.5
1998-99	12509	114	10973	8.4
1999-00	15471	116	13337	21.5
2000-01	16151	118	13687	2.6
2001-02	14090	121	11645	-14.9
2002-03	15434	127	12153	4.4
2003-04	16817	132	12740	4.8
2004-05	18771	136	13802	8.3
2005-06	19473	146	13338	-3.4
2006-07	17916	156	11485	-13.9
2007-08	18492	168	11007	-4.2
2008-09*	20859	181	11520	4.7

\*Estimated



The policy implication of the above analysis is that the size of the ADP in 2009-10 should be limited to about Tk. 26,000 crore. A divergent view may be that given the low implementation rate of ADP in recent years the target ADP should be set at a higher level, say at around Tk. 30,000 crore so that about 85 per cent implementation level would mean a realized ADP of about Tk. 26,000 crore.

The problems of setting ADP significantly above realizable level are two fold. First, it causes resources to remain tied down to the slowly implemented projects resulting in unnecessary borrowing on the part of the government. Second, the downward revision of the ADP that will be necessary towards the end of the fiscal year will result in considerable wastage of resources in the form of unfinished project works. Therefore, the government should set ADP size at a more manageable level and seriously address the capacity constraint and interagency and aid coordination problems to push ADP implementation to maximum possible limit.

#### *Quality of ADP*

The Public Expenditure Review Commission identified several factors that affect the quality of the ADP. The budget 2009-10 should attempt to address these issues.

One of the major weaknesses of successive ADP has been the pre-dominance of road projects. A large number of road projects are often taken up on political considerations resulting in very thin distribution of resources over many road projects and consequent slow rate of project implementation.

In 2008-09, road projects accounted for 8.64 per cent of total ADP allocation. Of the total 133 projects under the transport sector 96 belonged to road sub-sector. Table 4 provides a list of 24 projects which were initiated before 2006 and which constitute 25 per cent of all projects in the road sub-sector. As is evident from the Table, these projects have been receiving allocations in very small amounts causing long delays in their implementation. Despite slow implementation of the above mentioned projects, 27 new road projects have been initiated since 2006 and many of these new projects have also been receiving inadequate allocations.

A moratorium should, therefore, be imposed on inclusion of new road projects until a substantial part of the backlogged projects get cleared. The budget 2009-10 should prioritize existing road projects and allocate resources in a way so that priority projects that are nearing completion can be wrapped up swiftly. Instead of thinly distributing resources on all existing road projects allocations should be held off from all low priority and slowly implemented projects.

**Table 4: Road Projects Initiated before 2006 and Experiencing Slow Pace of Implementation**

*(Value in lac taka)*

Sl. No. & Name of the Project	Year of initiation	Project size	Cumulative expenditure up to Dec 2007	Average yearly expenditure	Years required for project completion at current rate of implementation
(54) Bridge construction on Dhawleshwari river at Tangail-Alison	2005	9436	69	28	339
(78) Pabna-Bandherhat-Nazirganj-Rajbari link road construction	2004	4137	135	39	103
(83) Panchaghar sugar mill-Benghari-Madia-Shaldanga-Deviganj road development	2001	2463	342	53	40
(68) Niyamotpur-Tahirpur & Dharmapasha-Modhyanagar road construction	2004	5297	572	163	29
(53) Shaheed Ziaur rahman Medical College Hospital link road	2004	1371	150	43	28
(64) Flyover construction at Tongi-Kailganj-Ghorashal road	2005	2000	199	80	23
(66) Sylhet-Jakiganj road development	1998	9617	2995	315	21
(44) Bogra-Sariakandi road development	2003	2861	514	114	21
(23) Lichutola-Kadamtoli & Nanglu-Balidighi link road development	2001	12097	3415	525	17
(31) Construction & development of 6 roads in Chittagong Hill Tracts	1999	19626	6883	810	16
(15) Dapdopia bridge construction at Barisal-Patuakhali road	2000	19605	6328	844	16
(21) Constuction of new cable stand bridge on Surma river & Ambarkhana by-pass road	2001	9888	3027	466	15
(33) Third Karnafuli bridge construction	2003	59000	14256	3168	14
Sl. No. & Name of the Project	Year of initiation	Project size	Cumulative expenditure up to Dec 2007	Average yearly expenditure	Years required for project completion at current rate of implementation
(60) Construction of bridge and culvert on Chittagong-Kaptai road	2005	874	133	53	14
(28) Sarail-Nasirnagar--Lakhai road construction	1999	9786	4112	484	12
(38) Baitiaghat bridge construction on Gallamari-Batiaghata-Dakop road	2001	2017	750	115	11
(94) Development of upazila roads of public importance	2004	43453	11129	3180	10
(34) Construction of third Buriganga bridge, second Shitalkhya bridge & Tista bridge with Kuwait fund	2003	26502	8181	1818	10

# Domestic Procurement Program and Public Stock Management

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- Although maintaining “adequate” public stock is essential to meet the needs of PFDS for (a) emergency food distribution in times of natural disasters (b) targeted food distribution to vulnerable groups under different safety-net programs and (c) stabilization of food prices, it should be remembered that the costs of procuring, storing and distributing large stocks of grain are high. Hence it is important that the government does not hold more stock than it needs for an “adequate” national food reserve.
- Although the remarkable changes in agriculture sector and food market since independence (expansion of boro output due to dissemination of HYV technology, reduced seasonality of prices due to multiplicity of harvests, increased marketable surplus, long-term decline in prices of foodgrain, liberalization of foodgrain trade etc.) reduced the need for government to intervene in the market to stabilize price and allowed it to keep a low food stock of around 5-6 lakh tons in the past, this is no longer true in view of the increased volatility of the world grain market including price spikes and imposition of outright export ban by major rice-exporting countries. This along with the increased need to expand safety net programmes and provide emergency relief due to erratic monsoon, and incidence of floods/cyclones presumably due to climate changes implies that the “adequate” national food reserve should now be much higher than before, ranging between 10-15 lakh tons.
- Although the public storage capacity is claimed to be 17 lakh tons, the effective storage capacity, due to dilapidation, has been reduced to around 12 lakh tons in recent years. The government, therefore, needs to invest in creation of additional storage capacity. In the interim period, the government can explore the possibility of using the private storage facilities on a (temporary) rental basis.
- Following bumper harvests, the government needs to procure surplus grain domestically to provide price support to the farmers in order to maintain adequate production incentives. However, setting a procurement price that sends adequate production signals to the farmers while at the same time minimize costs to the government exchequer is a real challenge. In fixing procurement price, in addition to the costs of production, the expected market price should also be taken into consideration. It is easier to forecast the size of the irrigated boro rice harvest and future price than it is for the aman, which is grown during the monsoon. Procurement price set at below market price would invariably

result in failure in achieving the procurement target while setting the procurement price excessively high in relation to market price would not only result in excessive cost for the government but would encourage rent-seeking behaviour and corruption amongst public officials involved in public procurement system.

- The government should recognize that output price support and input subsidies are complementary policies, not substitutes. Fertilizer subsidies may be superior to output price support for stimulating agricultural production but an input subsidy cannot stabilise prices or prevent the collapse of post-harvest prices. Both policies are needed and overall costs of these complementary policies should be taken into consideration in planning government interventions.
- Policy makers in Bangladesh, as in many developing countries, face the dilemma of keeping the prices low for consumers, specially for people with low/limited income, while ensuring that prices are high enough to provide farmers the incentive to produce more. In the short run, the government can resolve this dilemma by providing input subsidies which will reduce farmers' cost of production that can be passed on to the consumers in the form of lower prices. In the medium to long term, this problem can be satisfactorily addressed by raising the productivity of agriculture so that food can be produced more cheaply. This calls for allocation of adequate funds for agricultural research to foster technological innovation through generation of technologies with tolerance against biotic stresses such as pests and diseases and abiotic stresses such as drought, salinity and submergence.

## Some concerns for the budget 2009-10

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- March-April is the time when orders for the RMG sector are finalized. It should be easy to determine how bad the impact of the recession will be, how many firms are likely to be affected seriously (i.e. forced to lay off workers) and how many have to tighten their belts. If orders are not forthcoming, handing out cash will not bring those orders back. The only reasonable objective would be to attempt to expand market share through greater competitiveness. This means costs will have to be cut wherever possible. Reduction of import duties on raw materials and machinery announced by the government is a good step. Interest rate reduction is also a welcome step. These should be enough. In addition, export incentives could be considered for firms passing a stringent eligibility test, including size and previous performance (i.e. before the recession). A free-for-all would be costly and unhelpful and inefficient. Firm-level objective should be to stake out new opportunities with an eye to the future while staying afloat in the short-run. Those firms who are able to obtain orders in new destinations may be singled out for special assistance.
- For frozen fish, strict adherence to phyto-sanitary standards would seem to be more important than direct incentives. Here, the government needs to strengthen monitoring mechanisms.
- For the labour market, a big part of the problem of returnee-migrants is the corrupt nexus that seems to operate between local and foreign manpower businesses, and the connivance of officials in both countries. The budget should allocate resources to strengthen the relevant departments to develop a strategy to weed out such corruption.
- The main victim of the recession is the farm sector which is now reeling under low prices. The problem is being compounded by supply-driven policies related to OMS and safety nets for which the demand seems low. In part this is due to the urgent need to create storage space for procurement of the *boro* crop. Whatever the strategy, it is clear that farmers will not get a good price, and there is nothing much that can now be done now. We therefore must develop a strategy for the next Aman crop to ensure that it does not suffer. We remain obsessed with high prices although in all likelihood the main enemy for us over 2009-10 will be low food prices. An expansionary monetary and fiscal policy is suggested as under the circumstances, a certain amount of inflation would be quite manageable.
- Re-inventing the public sector? We now seem to be veering to the other extreme where we are even considering direct ownership and operation of enterprises by the public sector. While the government must retain some control over critical markets (especially

food) it should not spread out too thinly into too many areas. Given scarce government capacity and resources it should try to enhance its efficiency in basic areas of governance and in meeting the demand for crucial public goods. The idea should not be to replace the public sector but to complement it. The notion of “unscrupulous traders” causing a crisis needs to be re-examined very carefully.

- There are far too many safety net programmes. The most efficient ones need to be retained and expanded rapidly to cover say 50 percent of the most vulnerable.

# External Sector: Concerns for the National Budget 2009-10

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## 1. Recent performance of external sector and concerns

- External sector is the most important channel through which global melt down will extend influence on the Bangladesh Economy. As a result of fall in demand in the developed market (mainly USA and EU in connection with Bangladesh's export), different export products of Bangladesh may face down turn and thus shrinking of those industries. Changes in imports of consumer goods, industrial raw materials and capital machineries may also influence local market and industrialization. Remittance, which has been acknowledged as a critical source of foreign exchange and macro-economic stability, is another channel through which global financial crisis may impact upon Bangladesh. All these possible impacts have close concerns for employment and poverty situation.
- During the first half of 2008-09 fiscal year, Bangladesh experienced 16.7 percent growth in its export earnings compare to the same period in previous year, while the corresponding growth rate was 6.88 percent in the same time of 2007. Overall export performance is different in two big markets for Bangladesh- EU and the USA (tables 1a and 1b). In the EU market the growth was only 3.6% and in the USA in was 13.6% during the first half of the current fiscal year. Bangladesh has experienced 25 percent export fall for rawhides, 20 percent export fall for headgears, 16 percent export fall for fish and 2% for woven RMG in EU. In the USA market, share of Bangladesh is rising. Still, negative export is observed for fish (16.46%), head gear (11.53%) and jute (19.76%). It is encouraging to observe that main export item of Bangladesh, RMG, is performing well during the first half of the current fiscal year.
- The total import payment (cif) during July-November of FY09 is 27.9 percent higher than the import payments at the similar period in the previous year (the growth during July-January of FY09 became 19.35 percent higher, though disaggregated data for this period could not be collected). Crude petroleum products, cotton, yarn, and fertilizer, textiles & its articles are the key commodities that contributed to the overall growth of import payments in July-November period (table 2). Import of food grain has declined (due to bumper crop and self sufficiency). Prices of various commodities have declined in the international market (table 3). It is expected that the lower price of industrial raw materials at the international market will make the imported raw materials cheaper and is expected to increase the import of industrial raw materials. However import of capital machinery has declined (table 3), while there has been significant growth in Intermediate and capital goods imports.
- Sectors received cash subsidy for export in the last FY were export oriented local textile (5%), frozen shrimp and fish (10%), leather product (15%), straw and cane made handicrafts (15% to 20%), vegetable, fruit and agro-processed products (20%), potato (10%), bicycle (15%), jute product (7.5%), hatched egg and day old chicken (15%), light engineering (10%), liquid glucose (20%) and 100% halal meat (20%).
- A large part of government's revenue comes from duties collected from imported commodities. Although overall import duty of July-February, FY2009 is higher than the same period of FY'08,

month-on-month growth trend is negative. For example, month-on-month growth trend of customs duty during the July-February of FY 2009 over 2008 shows a downturn (in february'09 it was 15 % lower than same month of 2008, similar down turn can also be noticed in October, January, December). This is because import duty on food grains has been abolished in the budget of FY'09.

- It is observed that an increasing number of migrant workers from Saudi Arabia, Dubai and Malaysia are coming back in recent months. According to Bureau of manpower export and training (BMET), number of returnee from Middle East mainly from U.A.E was 8022 in February, 09 and 4817 in January, 09. Whether this return is fully/partially because of financial crisis or regular phenomena has not yet been verified. Another observation is slow down in new migration. Recently Malaysia has cancelled 55000 visas of Bangladeshi workers.
- If the current trend of return of workers from abroad, and stagnation in out –migration continues, then in year 2010, the inflows of remittance earnings are expected to fall.

## **2. Highlights from proposals made by different business bodies to cope with the financial crisis**

To cope with impacts of global financial crisis various business bodies have demanded support from the government, which has budgetary implications.

- Tk6000 crore is demanded by FBCCI, which is based on 5% cash incentive for all export sectors.
- 10% Cash incentive on exports of RMG products is demanded by BGMEA and BKMEA. Moreover, BGMEA has demanded 10 Taka per USD devaluation for thirty percent of Export Value.
- BGMEA and BKMEA have asked for reduction of interest rate on industrial credit to 7 percent from more than 15 percent. Moreover they have demanded two year moratorium facilities for term loans.
- BGMEA and BKMEA have demanded withdrawal of VAT from RMG sector.
- BGMEA and BKMEA have also demanded subsidized Diesel for RMG sector like farm sector.
- Enhancing cash subsidy to 20% from the existing 10% is demanded by Bangladesh Frozen Food Exporters Association (BFFEA)
- BFFEA have asked the government to provide interest-free loan as it was given in 2001 following the adverse situation stemming from the twin tower attack.
- 25% cash incentive has been demanded by Bangladesh Finished Leather and Leather Goods Exporters Association and they also demand the reduction of interest rate for credit.
- BTMA have demanded a hike in the cash incentives from the current 5% to 10% and introducing a 5% R&D fund on the lines done by Pakistan. BTMA's main demand is to reduce rate of interest which is currently around 14 percent. BTMA has also demanded to create a fund for R&D sector

whereby, some work can be carried on to give benefit to the textile industries. They have also demanded for extension the terms of bank loans given to the spinning mills.

- MCCI has demanded a supportive monetary policy and conducive tariff regime rather than direct cash incentives to exporters as stimulus package. The supportive monetary policy and conducive tariff regime include reviewing and keeping the exchange rate stable and competitive, keeping interest rate supportive to export and production, ensuring priority distribution of bank credit to agriculture, manufacturing and service sectors and limiting government's borrowing from the banking sector.

It is observed that there are anomalies in the demands of different business bodies. Different bodies demand different amount of cash subsidies. The main objective of such incentives to the industries is to mitigate the negative effects of global melt down. However, it is to be remembered that not all enterprises of an industry will suffer from global melt down, specially, in case of the RMG (both woven and knit) sector. Among important export sectors, leather and frozen food are going to be effected the most as a result of economic crisis. Therefore, starting new incentives or increase existing incentives for export industries should be based on actual needs. To mitigate the possible negative impacts of global crisis on our export industries and employment situation, domestic industries and agriculture should receive much attention.

### **3. Suggestions for the budget 2009-10**

- A 'fund for crisis coping' may be created (may be for 3 years), which will have three parts – a) low cost loan for export enterprises having difficulties with working capital (payment of salary, settling cost of raw materials etc.) upon submission of proof that the problem is a recent phenomenon due to demand fall in export markets; b) employment loan fund, specially for retrenched domestic workers, from where they can have very low cost fund for survival upon producing papers of losing job due to lay off or closing down of factories. c) low cost fund for returnee migrant workers, from where migrants returning from abroad may take loan to start some small business or settling their loans taken during migration. A small part of the fund may be allocated for creating a database on returnee worker.
- Tk1,050 crore has been kept in the budget for FY2008-09 as export subsidy for 13 export-oriented industrial products. Current cash subsidy should continue for the sectors which were receiving this in last fiscal. For most of the sectors, cash subsidy should continue at the current rate, however, the efficiency in the disbursement mechanism needs to be improved. This year's arrear is about Tk. 243 crore (i.e. 23% of the allocated cash subsidy). Cash subsidy may be increased to 10% (from the current rate of 5%) for cotton yarn manufacturing enterprises as they are facing serious crisis due to competition from Indian yarn.
- A fund needs to be allocated for upgrading skills of workers and entrepreneurs of export industries. Part of this fund may be utilized for of the workers of export industries, especially for RMG workers

and part of the fund may be utilized for entrepreneurs of sectors like leather, light engineering, agro-processing etc.

- The rate of import duty for capital machinery and spare parts was 3% for the FY'09. Though 100% export industries don't face this duty, the facility may be extended for local industries to encourage industrialization and diversification of future exports. Therefore import duty of capital machinery and spare parts may be made zero. Besides, 1% Supplementary Duty on capital machinery (SD) may be removed. This will also save resource and time for managing duty draw back for capital machinery.
- Current customs duty on agricultural equipment like irrigation pumps, diesel engine and tractors is 3%. In order to reduce the cost of production of agricultural products, this may be made zero.
- In order to protect the health and to reduce environment pollution and revenue earning customs duty or SD should be increased to 60% on the raw materials for manufacturing of cigarettes and 20% on the papers used in producing packaging materials of cigarettes.
- In order materialized the mandate of a digital Bangladesh effective, duty on computers and peripheral devices should reduce from 3% to zero.
- Duties on luxuries good should increase. e.g duty on luxury vehicles should be made progressive with the value of vehicles.
- Duties on printing paper are 12 %. For the sake of reducing cost of education and expansion of knowledge, this may be reduced to 7%.

**Table 1a: : Quarterly Growth of Exports of Major Items to USA**

	Growth of Exports(Jul-Dec 2008 on July-Dec2007) (Year-on-Year)							
	BD	USA*	China	India	Pakistan	Philippines	Sri Lanka	Vietnam
Woven	12.49	-3.62	5.06	-8.88	4.08	-23.44	-3.87	7.82
Knit	25.88	-1.57	4.71	0.24	-0.89	-3.18	-25.23	0.57
Fish	-16.46	3.48	19.42	-17.99	-6.51	-20.58	-41.30	7.44
Home Textile	16.93	-3.99	-2.46	2.92	-9.39	1.34	-21.42	-25.36
Headgears	-11.53	3.12	5.44	-23.22	44.28	8.46	-11.47	7.89
Jutes	-19.76	2.55		-2.95	3.24	7.95	-7.71	-
Plastics	6.69	2.02	10.48	33.61	-	-13.26	-0.04	15.31
Total	13.57	2.59	5.48	4.93	2.49	-12.21	-3.10	20.19

Source: Calculated based on data accessed from USITC, 2009.

**Table 1b: Growth of Exports to EU (July-Oct 2008 over July-Oct 2007)**

	Bangladesh	China	India	Pakistan	Sri Lanka
Woven	-2.04	6.46	4.56	1.88	3.92
Knit	6.66	32.11	-4.48	-1.57	2.07
Fish	-15.88	4.51	-11.96		0.93
Home Textile	4.28	1.50	-4.33	0.15	-14.23
Headgears	-20.02	5.08	12.91	10.09	-0.16
Plastics	33.13	7.45	-3.72	127.99	-2.69
Jutes	-13.30	2.64	-2.48		-4.87
Rawhide	-25.44	-26.96	-12.20	-23.94	-35.00
Leather Products	15.23	-1.12	11.32		14.57
Total	3.58	7.23	10.91	7.45	1.57

Source: Calculated based on data accessed from Eurostat, 2009

**Table 2: Composition of imports** (In million US dollar)

Items	2007		2008	% change (4 over 2)
	July-Nov	July-Oct	July-Nov	
1	2	3	4	5
<b>A. Food Grains</b>	492.2	239.7	367.2	<b>-25.4</b>
Rice	252.3	158.5	187.5	-25.68
Wheat	239.9	81.2	179.7	-25.09
Edible oil	411.1	311.6	368.9	-10.27
Sugar	130	156.4	182.9	40.69
<b>C. Consumer &amp; Intermediate Goods</b>	3465	4365.4	5162.9	<b>49</b>
Clinker	137.3	97.4	119.8	-12.75
Crude petroleum	219.7	403.1	403.1	<b>83.48</b>
Fertilizer	196.9	597.5	694.1	<b>252.51</b>
Dyeing and tanning materials	84.2	112	129	<b>53.21</b>
Raw cotton	425.3	460.1	563.7	<b>32.54</b>
Yarn	260.6	305.5	366.4	<b>40.6</b>
Textile and articles thereof	785.1	747.5	905.7	15.36
<b>D. Capital Goods &amp; Others</b>	2740.6	2762.9	3439.7	25.51
Capital machinery	752.2	541.5	661.9	-12
Grand Total (A+B+C+D)	7999.4	8417.9	10231.1	27.9

Source: Bangladesh bank

**Table-3: World commodity prices**

	% Change of in commodity price index			% Change
	Dec/Nov	Jan/Dec	Feb/Jan	Feb 09/Feb 08
Commodity	-14.4	4.2	-4.3	-43.0
Non-Energy	-6.8	4.4	-2.4	-31.6
Energy	-18.5	4.0	-5.6	-49.1
Crude	-23.2	5.7	-4.9	-55.5
Agriculture*	-4.0	8.1	-0.8	-23.7
Food	-2.7	6.9	-2.4	-24.6
Corn	-3.0	9.5	-5.8	-25.8
Wheat	-3.6	8.7	-6.1	-47.1
Soybean Oil	-6.5	10.8	-7.0	-46.3
Soybeans	-3.1	15.6	-5.2	-19.1
Sugar World*	-3.2	-2.9	-0.2	-26.6
Industrial Metals	-10.9	1.0	-3.0	-46.9
Copper	-16.7	5.0	2.1	-58.1
Gold*	7.3	5.2	9.8	na
Fertilizers*	-17.3	-3.0	-9.6	-4.7
<i>na Not available</i>				

Sources: IMF; Estimations based on data provided by the IMF.

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# A Brief Note on National Budget for Education

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Sl. No.	PRSP Requirements and GoB's AL Manifesto/Agenda	Budgetary Allocation	Rationale
1.	<p>Raising budgetary allocation for education</p> <ul style="list-style-type: none"> <li>• Year 2011: 100 % children in school</li> <li>• Year 2021: Total Eradication of Illiteracy</li> <li>• Problems: Dropped out, missed out, Disadvantaged, Differently abled, Ethnic, Remote, Inaccessible, street children (20 lac), Sidr affected children (18 lacs), tea garden, working children</li> </ul>	<p>Considering the national and international commitments and to enhance the quality of education additional resource allocation is essential. Keeping this view in mind, at least 19 % of total budget needs to be allocated for education and ICT for the fiscal year 2009-2010.</p> <ul style="list-style-type: none"> <li>▪ Pilot program required for mainstreaming education of the disabled learner</li> <li>▪ Increase budgetary allocation for Adivasi and community teachers working in hard to reach areas</li> <li>▪ Build Residential schools to provide access to education where distance and geographical location is a problem</li> <li>▪ Create provision for education of street children</li> </ul>	<ul style="list-style-type: none"> <li>▪ To comply with the election manifesto incising allocation for education is essential. Urgent need to harness dropout, missed out, excluded and full attendance in the school.</li> <li>▪ Digital Bangladesh and e-learning is absolutely essential for “Din Badal” and Progressive Bangladesh, which must inevitably include the excluded and vulnerable, who are the majority</li> </ul>
2.	<p>Extend education opportunity for the geographically, socially (low caste Hindus and sweepers), and marginalized first generation learners</p>	<p>At least one school per village particularly in the 2000 villages that have been identified and meet the required criteria</p>	<ul style="list-style-type: none"> <li>▪ There are areas where school is needed. Renewable energy in the form of solar, wind, biomass, etc. may be considered for non-grid generation of electricity. This would connect people to the world of work.</li> <li>▪ Despite many successes, dropouts are not being controlled. Meal, social security for the girl child, child labor, and cost associated with the distance of school (in particular, Char, ethnic minority and disabled learners)</li> <li>▪ Cost of private tuition and</li> </ul>

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			<p>attitude of the parents are important factors to reduce dropout for the marginalized segment.</p> <ul style="list-style-type: none"> <li>▪ Awareness building through TV, Radio required</li> </ul>
3.	Decent share of education budget for concerned different ministries	Within the present resource availability, the government needs to allocate 50% of education and ICT budget for MoPME, 45% for MoE, and the balance 5% for MoSIT.	Different ministries could be evaluated resource allocation could be ascertained dependant upon effective actions and implementation in line with the agenda. Moreover, the related ministries like MoWCA, MoSW etc. could also be directly co-opted for cogent outcomes. Moreover, a strong public-private partnership esp. NGOs, CBOs etc. coordinated list of Donors may be linked to pool in more resources
4.	Wider coverage of ECCE	The government needs to take measures to introduce pre primary education as per the second National Plan of Action for EFA (NPA-II) by reviewing curriculum, providing infrastructural facility, creating child friendly learning environment and necessary teacher training	Education psychology stipulates that the blue-print for a child's brain is formulated in the period between 0 months to 3 years. Sri Lanka and neighbouring countries have begun ECCD from 0 months which has far reaching implications for the foetus, the future citizen and workforce of the country. This cannot be underestimated because once the sapling takes shape, no amount of bamboo support to the trunk (skill training, human capital formation) can make significant improvement (Amartya Sen and Osmani). The effects of undernourishment limits the formation of the womb based embryo brain. In Bangladesh, ECCE is being catered to (GoB) from Class 3 to 5. Poverty eradication will be bound to take a back seat by default.
5.	Improve Pupil-Teacher Ratio and enhance contact hours	<ul style="list-style-type: none"> <li>• Construct 2500 new classrooms by using unutilized funds of PEDPII fund and employ equal numbers of new teacher during the fiscal year 2009-2010.</li> <li>• Long term target would be bring down Teacher - Student ratio to 30:1 and contact hours at least</li> </ul>	<ul style="list-style-type: none"> <li>• A holistic plan for development of education sector should include the issue of education policy and attract good teacher in the system and retain them.</li> <li>• salary raise issue of the primary teachers and to introduction of a competency exam: an exam like SAT for the teacher to get additional incentive.</li> </ul>

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		<p>900 hours a year. It would require additional 75000 classrooms with same number of teachers</p> <ul style="list-style-type: none"> <li>• To enhance contact hours by merging two shifts</li> </ul>	<ul style="list-style-type: none"> <li>• Distance learning should be fostered to minimize costs related to classrooms and teacher recruitment</li> </ul>
6.	Literacy and life-long learning	<ul style="list-style-type: none"> <li>• Comprehensive Adult Literacy program linking it with the life-skills programs.</li> <li>• Special program can be taken taken-up considering the demand for the skill and semi-skill manpower requirement in the overseas employment market.</li> </ul>	<ul style="list-style-type: none"> <li>• One dedicated education channel (may be the second channel of the BTV) could play a vital role in facilitating adult literacy, in particular, life-long learning. The education channel could also facilitate the learning process at the primary and secondary level as well and reduce dependency on the private tutor through telecasting program on math, English, science subjects, ICT; Good teachers of BRAC, CAMPE Schools, other renowned schools of Dhaka city or other areas could be mobilized for conducting sessions which would enhance learning of the rural students.</li> <li>▪ Presently, the GoB has decided to earmark 600 crore for the DNFE. Basic education for 6 months (refresher course for 27 lacs between the ages of 11 to 45 years) will be given. Life skills to link to remunerated work will be given to some selected groups because of the insufficiency of money. In that case, the remote areas should be given priority as they do not have access to communication facilities. Moreover, Peer trainers in those areas could be developed who will train others groups, keeping up the sustained efforts to include more of the excluded into mainstream livelihood activities. Lack of use would</li> </ul>

Sl. No.	PRSP Requirements and GoB's AL Manifesto/Agenda	Budgetary Allocation	Rationale
			<p>lead to wastage of the training even for basic literacy. For the accessible areas too, a similar exercise should be done to build up ;learners, leaders, community cohesion, sustainability of programmes and productive human resource.</p> <ul style="list-style-type: none"> <li>▪ Without proper education we cannot fight against poverty. We need to make the illiteracy free Bangladesh by 2017-2018. Comprehensive program needs to be designed and executed where youth could play a vital role. The older generation too must be mobilized so that safety nets, climate change and disaster resistance may be more meaningfully tackled by both men and women.</li> </ul>
7.	Equity among different types of education provisions	<ul style="list-style-type: none"> <li>▪ Review competencies &amp; develop equivalency Framework</li> </ul>	<ul style="list-style-type: none"> <li>• ICT and e-learning would be the best instrument for generating enthusiasm among all the different streams and across all levels from Primary to Tertiary.</li> <li>▪ The tax policy of 1997 regarding imports of computer had an enormous impact on access to information technology so reintroduction of similar policy for creating an enabling learning environment.</li> <li>▪ Piloting of e-learning at the primary level should be considered</li> </ul>
8.	Comprehensive development of secondary education	<ul style="list-style-type: none"> <li>▪ Common core curricula at the secondary level</li> </ul>	<ul style="list-style-type: none"> <li>▪ The idea of common core curricula with provision for TVET and Vocational Education especially for girl school dropout students unable to compete, unable to shoulder examination costs plus tuition, fearful of physical security etc.</li> </ul>

Sl. No.	PRSP Requirements and GoB's AL Manifesto/Agenda	Budgetary Allocation	Rationale
9.	Technical and vocational education	<ul style="list-style-type: none"> <li>• Instead of providing general education to a large population, more emphasis on TVE is required</li> <li>• The open university and the second TV channel could play a supplementary role in TVE</li> <li>• Link TVE with the overseas employment market</li> <li>• Set up short, relevant courses with market demand. Link graduates with the world of work right from inception into skill training.</li> </ul> <p>Digital and e-learning</p>	<ul style="list-style-type: none"> <li>• Students of secondary level could forgo general education; a large portion of them could be sent to the TVE sector and nexus could be built up with the labour market, at home and abroad.</li> <li>• The economic opportunities of the TVET should be inculcated as also the dignity of labour and all forms of education. This is in conformity with the Kudrat-e-Khuda and Shamsul Haque Education Policies</li> </ul>
10.	Community engagement	<ul style="list-style-type: none"> <li>▪ Strengthening school management committees/governing bodies especially those under programs like ROSC</li> </ul>	<ul style="list-style-type: none"> <li>▪ Local person with required competencies needs to be involved in the governing bodies/managing committees – Political will is very important.</li> </ul>