

STATE OF BANGLADESH ECONOMY IN FY2002: AN EARLY ASSESSMENT

I. INTRODUCTION

The Bangladesh economy is currently facing possibly the most severe exigency since the macro-economic crisis of the late 1980s. The twin shocks emanating from the yawning fiscal deficit and deteriorating balance of payments have exposed the entrenched vulnerabilities of the Bangladesh economy, putting under threat the achievement of the 1990s.

It may be recalled that, thanks to the introduction of a host of stabilisation measures in the early 1990s, macro-economic stability was largely restored in the country. Subsequently, the economy experienced above the trend economic growth rates during the second half of the decade. Today, it seems that both the pillars of success of the macro-economy, viz. stability and growth, are in peril. A large part of these stresses and strains are underpinned by the fundamental structural weaknesses which characterise the Bangladesh economy. But the pressures have been accentuated by a benign neglect in undertaking necessary reform measures to improve the competitiveness of the economy. However, the obtaining situation has been aggravated further by a confluence of external factors ranging from global recession and practices of discriminatory trade preferences to terrorist attacks in the USA on September 11, 2001.

The *Independent Review of the Bangladesh's Development* (IRBD) for FY2000-01 prepared by the Centre for Policy Dialogue (CPD) pointed out that the “scissors effect” of the fiscal disequilibrium and weakening of the balance of payments is once again going to put to test the limits of the resilience of the Bangladesh economy in FY02. In this regard the recent developments in the global scene only compounded the challenge.

The fundamental question which is currently haunting Bangladesh is whether the present problems afflicting the economy are a short-run phenomenon which the country will be able to overcome through prudent policy management and institutional reforms. Alternatively, whether the emerging negative trends in the

macro-economy will precipitate a situation which will threaten the achievements recorded during the 1990s leading to an extensive loss in employment and income for a protracted period.

It is a unique coincidence that the disquieting developments in the domestic and global economy became apparent during a regime of governance flux in Bangladesh which is associated with the country's democratic transition. With a view to address the situation, the new government which took office in October 2001 declared a series of appropriate measures within and outside its first *100 Days' Package* of Programmes.

Most of these measures recently announced by the incumbent government are in the right direction and comprise of discrete steps in the areas of monetary, fiscal and financial sector policy. Notwithstanding these initiatives, a cogent and feasible *Recovery Package*, designed to effectively arrest the backsliding of the economy, with minimal costs to public welfare, is yet to take shape.

To obtain some clues about what may constitute a sensible macro-economic policy underlying such a *Recovery Package*, it will be useful to review the recent behaviour of the major indicators of the Bangladesh economy.

The present review, in the backdrop of the observed trends during the 1990s, thus, focuses on the performance of the economy during the elapsed fiscal year and seeks to identify the early signals of the current fiscal year, i.e. FY2001-02. The scope of the review is, however, limited to analysis of the fiscal and monetary aggregates, trends in the real economy and developments in the external sector.

II. PUBLIC FINANCE

Revenue Receipts. One of the major factors which has contributed to the current fiscal imbalances relates to the historically low revenue effort of the country. Following a steady rise in the share of revenue (tax and non-tax together) in the GDP from 7.08% in FY91 to 9.49% in FY97, the revenue mobilisation process started to show signs of exhaustion. While the success of the early 1990s in this regard was largely triggered

by the introduction of VAT, the dip in FY99 largely originated in the devastating floods of 1998. Signs of some recovery were observed in FY01, when the total revenue collection recorded a refreshing 13.25% growth-resulting in a revenue-GDP share of 9.37%.

According to the original budget estimates for FY02, the government is programmed to collect a total of Tk. 272.39 billion as revenue, more than 80% of which is to come from the NBR sources. In order to achieve the target, the collection has to be 12.6% higher than the preceding year's (FY01) benchmark and it will push the revenue-GDP share to 9.6%.

Early information on revenue collection reveals that the tax receipts from NBR sources during the first half of FY02, in spite of being 8.7% more than the comparable figure for FY01, have been 2.08% below the target. In this connection what is important to note is that the total *internal trade-related revenue* collection has grown during the period July-December, 2001 by 21.16% as against the marginal increase (1.03%) of total *import-related revenue*. Thus, one observes that whilst the collection on account of internal trade related revenue surpassed the target by about 7.9%, the shortfall from target in case of total import-related revenue was about 7.3%.

While one can only speculate about the reason behind the former, the latter was largely the result of significant slowdown in import growth during the first half of FY02 (we return to the issue of import growth later).

If the import growth continues to remain modest in due to the sluggishness domestic economic activity, it will be a formidable challenge to achieve the target revenue figure by the end of the year. Inability to increase revenue flow will increase the demand for downsizing of public expenditure basket with a view to contain further deterioration in the fiscal balance.

A sensible approach in this regard, to fiscal management would entail intensification of the institutional measures designed to broaden the tax net, plugging the leakages in the current collection system, strengthening the *non-NBR tax* component of receipts

and addressing the weaknesses in *non-tax sources* of revenue generation. Upward revision of the public utility rates is also an imperative in this regard.

Public Expenditure. Public expenditures as a share of GDP experienced a rise in the early 1990s from the benchmark level of 12.94% in FY91 and hovered around 14% during the mid-1990s. The indicated share once again started to increase in the second half of 1990s, recording its peak in FY01 (15.36%). According to the original budget figures for FY02, a mild fall has been projected for the public expenditure ratio in the current fiscal year.

Inability to adhere to the target figure in this respect will further intensify the strains currently underpinning the fiscal balance. The recent move by the government to scale down the ADP package will address the situation upto a point. However, one would expect that the burgeoning revenue expenditure (RE) should be the prime candidate for such a cutback. To this end, the government should subject its total expenditure package to the scrutiny of a *Public Expenditure Review Commission*.

Revenue Expenditure. From the initial level of 6.61% in FY91, the revenue expenditures as a share of GDP have experienced a secular rise throughout the 1990s (excepting a marginal fall in FY97). The RE share reached its peak in FY01 accounting for more than 8% of GDP. According to original budget projections, the revenue expenditure-GDP ratio is slated to fall to 7.76% in FY02.

In the absence of any readily available data, it is difficult to comment on the trend in revenue expenditure during the first half of FY02. Whilst it has been reported that the government contemplate curbs on some “avoidable” revenue expenditures, it will definitely be a formidable achievement if it can do so given the rigidity in the composition of the recurrent expenditures. It may be recalled that “salary and allowances”, “interest payment” on domestic debt and foreign loans accounted for about 50% of the public expenditures in FY01.

The recent decision to reduce the *bank rate* as well as the yield rate on the public savings instruments will reduce to some extent, the domestic debt servicing liability of the government. The issue of contingent liabilities, particularly to the International

Oil Companies (IOCs) and Independent Power Producers (IPPs) will also demand attention. However, in order not to aggravate the situation further, the government will have, in the coming months, to check the temptation of announcing any populist decisions having expenditure increasing implications (e.g. enhanced benefit package for the public sector employees), prune the losses in the state-owned enterprises (SOEs) and, in the process, decrease its borrowing need.

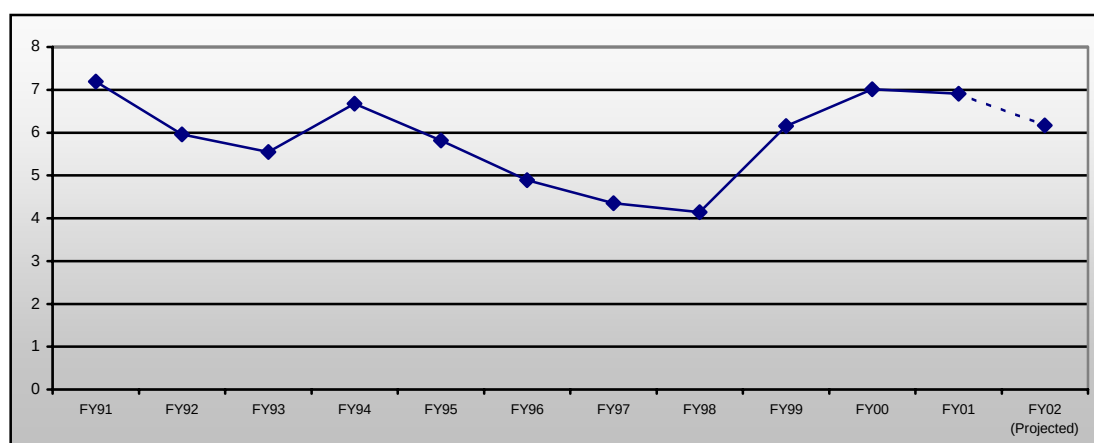
Annual Development Programme. The size of the ADP rose steadily during the 1990s with the peak recorded in FY95 (7.3%). Following a short respite, the ADB share again picked-up in the late 1990s, particularly following the floods in 1998 when the government sought to boost domestic demand through an enhanced public expenditure programme. As a result, one observes that the revised ADP package accounted for 7.05% of the GDP in FY01. According to the original budget projections, the said share is programmed to decline to 6.69% in FY02.

Recently the government has announced its decision to initiate some project pruning exercise amounting to around Tk. 10 billion. Review of some of the projects funded by Suppliers Credit are also in order. While such moves are welcome, in the face of the current fiscal situation, what needs to be kept in view is the possible impact of cutbacks in government development expenditures on aggregate demand given the present depressed state of economic activities.

The three major issues which need to be kept in focus in this respect are the improvement of the quality of the ADP, discouraging expenditures on account of the non-ADP projects, and the ability to more effectively draw upon the \$6 billion of foreign project aid locked in the pipeline. It is maintained that a *Core-ADP* may be designed predominantly drawing upon projects underwritten by committed foreign aid.

Budget Deficit. From its high level in FY91 (7.1%) the overall budget deficit, as a percentage of GDP, experienced a steady decrease (barring FY94) upto FY98 (4.14%). Since then the indicator has recorded an accelerated growth reaching 6.91% of GDP in FY01. In the original budget figures for FY02, a modest fall (6.17%) has been programmed for the overall budget deficit.

FIGURE 1: GROSS BUDGET DEFICIT AS PERCENTAGE OF GDP



It may be pointed out that it is not only the magnitude of the fiscal deficit, but also its mode of financing which is a matter of concern in the current backdrop of fragile macro-economic balances of the Bangladesh economy. The changing composition of the budget deficit in favour of domestic sources, particularly during the second half of the 1990s, reaching 3.28% of GDP in FY00, emerged as an expression of fundamental weakness in macro-economic strategy.

Whilst debate continues on what constitutes a “safe limit” for the fiscal deficit in Bangladesh, it goes without saying that the behaviour of the fiscal deficit in FY02 is, to a great extent, going to define the health of the country’s macro-economy in the days ahead. In the near future the government, however, should initiate measures to enact a *Fiscal Transparency and Responsibility Act* with a view to disciplining the borrowing behaviour of the government.

III. MONETARY AGGREGATES

Domestic Credit Expansion. A moderately expansionary monetary policy was being pursued during the later part of the 1990s. Thus, aggregate credit flow grew by 12.64% in FY98, then by 13.06% in FY99 and 13.64% in FY00, and subsequently, recorded an expansion of 17.65% in FY01. Two features are noteworthy in this respect. *First*, throughout the second half of the 1990s the growth of domestic credit in the government sector has been systematically higher than that of in the private sector. For example, even after a significant slowdown, in the last fiscal year (FY01), the rate of domestic credit expansion in the government sector was 19.7% as against

16.9% in the private sector. *Second*, in FY01, one observes an extraordinarily high growth in credit flow to “other than government public sector organisations”. Both these trends indicate the aggravating fiscal imbalances in the Bangladesh economy as well as highlighting one of the constraints on stimulating private investment.

Deepening of the abovementioned two trends is further evidenced by the early figures relating to domestic credit expansion in the current fiscal year. The overall (point-to-point) domestic credit expansion rate, as of end December 2001, has been as high as 17.93%. With the government sector recording the highest growth (25.25%), credit flow to private sector and to “other government bodies” grew by 15.74% and 12.30% respectively.

This implies that the broad money growth has remained very high during the first half of FY02 and containing it, particularly without impinging on credit flows to the private sector, would definitely pose a challenge to the government in the coming months. It may be pointed out that due to the adverse differentials characterising the domestic credit expansion rates, the credit flows to the private sector, during the first half of FY02, have decreased to less than 69% of the total credit flow compared to its historical average share of 72%.

Government Borrowing. A high rate of domestic credit expansion in the government and related sectors suggests that the spree of government borrowing from the banking system, as well as from the public, through sale of savings instruments, continues unabated. At the end of the first half of FY02 (December 31, 2001), the government shouldered a public borrowing overhang of TK. 205.64 billion from the banking sector. In fact, between July-December, 2001, the net increase in government borrowing from the banking system amounted to Tk. 41.46 billion which is about 1.25 times higher than that of the comparable figure for FY01.

Information on government borrowing through savings instruments, during the first half of FY02, was not readily available. The government has recently decided to lower the interest rates for saving certificates with the dual purpose of lowering the cost of borrowing and channelling funds to the capital market. However, the volume of sale of the savings certificates will be largely dictated not necessarily by the

relative yield from these instruments, but by the magnitude of the borrowing needs of the government and the availability of alternative secured opportunities for investment. Indeed the decision to lower the cost of public borrowing may well serve as a license to stimulate such borrowings.

What is however curious is why the government needs so much money. On the supply-side, the revenue collection is only marginally short of target. On the demand-side, the first quarter is usually a slack one in terms of expenditure and it was the time when the Caretaker Government was in power which by definition is not supposed to be a great spender. Thus, while some borrowing by the government has been built into the fiscal programme for FY02, it is surprising that the incumbent government has to borrow so much and so early. There is definitely a need for taking a closer look at the components of the fiscal balances.

Inflation. Curiously, notwithstanding uninterrupted high monetary growth during the recent past, to date there is little obvious sign of inflationary pressure in the Bangladesh economy. The inflation rate (moving average) has remained as low as 1.58% in FY01. The corresponding point-to-point figure has been 1.66%. Such a sustained low level of inflation was possibly dictated by the low level of foodgrain prices, ensured by successive good harvests. A low inflation rate may also reflect recessionary conditions in the economy which would be consistent with the weak inflationary impact of heightened public borrowing. However, in the absence of more substantive investigation of the dynamics of inflation in contemporary Bangladesh, such observations must remain largely speculative.

Incidentally, early data on FY02 indicates that the inflation rate (point-to-point) is showing sign of marginal increase. From the base rate of 1.66% (June '01), the inflation rate gradually increased to 2.0% in December, 2001. This crawling increase in the inflation rate has been underwritten by the increase in the non-food price index in both the rural and urban areas. However, during the same period the food component of the index has remained steady in both the areas.

Anticipating inflationary behaviour in the Bangladesh economy will be an intriguing exercise in the coming months. It will be interesting to observe whether the inflation

rate “finally” goes up in the backdrop of sustained monetary growth in the government sector coupled with sluggish growth in the real economic sector, including a fall in exports. It is also to be seen to what extent the recent upward revision of utility prices and devaluation of the *taka* will stimulate “cost push” inflation. The economy will definitely be in deep trouble if the current macroeconomic strains are compounded by erosion of price stability.

IV. REAL ECONOMY

Agricultural Production. Apart from the crop sector, all other components of the agriculture sector, viz. livestock, fisheries and forestry, have been demonstrating robust growth during the 1990s. However, it is the sustained impressive growth of the crop sector during the second half of the 1990s which has provided the much needed cushion to the economy in the face of the current macro-economic imbalances. During FY01, agriculture posted a 3.6% growth with “fisheries” emerging as the lead sub-sector excelling the most – recording a growth rate of 6.9%.

Foodgrains. The country produced a total amount of 26.76 million metric ton of foodgrains last year (FY01) recording a 7.5% growth in foodgrain production. Rice production during this period increased by 8.8% (25.09 million metric ton), while wheat production fell marginally to 1.67 million metric ton. The target for foodgrain production for FY02 has been fixed at 27.92 million metric tons, i.e. about 4.3% above the preceding year’s benchmark. Rice production is targetted to reach 26.08 million metric ton, i.e. 3.95% above the benchmark.

Initial figures on the *aus* harvest in FY02 show that the production had been in the order of 1.81 million ton which is less than the target figure (1.84 million metric ton). However, the *aman* and *boro* are the major crops which determine the food availability situation in the country. There was an apprehension that the *aman* production would suffer a bit due to the prevalence of a mild drought during the harvesting season. However, early forecast show that the shortfall in *aman* production will be in the range of 0.7 million metric ton, given that the target figure was 11.55 million metric ton. Thus, in order to record a positive growth in crop production

during FY02, an additional 0.5 million metric tons will have to be produced over the benchmark of 11.25 million metric ton for FY01.

Given the state of affairs prevailing in the macroeconomic scenario, the supply of cereals from domestic source has not only kept the overall price index under control, but also protected the country from further balance of payment pressure which could have been brought about by the necessity of importing foodgrains. It goes without saying that any faltering in foodgrain production in FY02 will aggravate the macroeconomic imbalances further, jeopardise the livelihoods of the vulnerable groups and lead to deterioration of the poverty situation.

Industrial Production. In the 1990's, particularly its second half, performance in the industrial sector has been somewhat uneven. Growth in the industrial sector (including manufacturing, construction, electricity, gas and water supply, and mining and quarrying) in the post-flood period (FY99) plummeted to 4.92% and demonstrated gradual recovery in the subsequent period posting 5.55% and 8.68% growth in FY00 and FY01 respectively.

Manufacturing Production. Manufacturing growth also dropped to 3.2% in FY99 after the floods in 1998. The growth rates improved in the following years, recording growth of 4.76% in FY00 and 9.10% in FY01. As the impact of floods was more severe on the small scale enterprises, the recovery process was slower in this sub-sector in comparison to the large and medium scale sub-sector. In FY01, the large and medium scale sub-sector grew by 9.75% and its small scale counterpart grew by 7.46%.

A disaggregated analysis reveals that the major industries accounting for more than 68% of the industrial weight experienced growth to the tune of 6.84% during FY01. According to the production figures underlying this growth estimate, the *high performing manufacturing activities* during the last fiscal year (FY01) had been garments (17.48%), cotton cloth (15.25%), M.S. rods (10.38%), fertilizer (9.32%), drugs and pharmaceuticals (7.77%) and tea (5.29%). Major activities which registered negative growth during FY01 were cement (-5.09%), petroleum products (-3.16%)

and jute textiles (-1.05%). It is difficult to ascertain any pattern in the differential growth rates experienced by the manufacturing sector during FY01.

Information on manufacturing growth during the early period of FY02 is available upto the month of November. A point-to-point comparison shows that the *Quantum Index of Production* (QIP) for large and medium manufacturing units declined by (-)0.54% during July-November, 2001. The comparable figure for FY01 recording growth of 12.95%, indicates a quite troubling reversal of fortunes in manufacturing growth during the first half of FY02. The sluggishness in manufacturing growth is better captured once we compare performance of the sector during the eleven months (January-November) of the calendar year 2001 with that of the preceding year (2000). Such a comparison reveals a marginal growth of 0.60% during the year 2001 compared to more robust growth in 2000. This deceleration in manufacturing growth appears to reflect the declining circumstances of the RMG sector, where deceleration in their export growth (discussed in the chapter on trade) is reflected in the slow down in output growth in the sector.

The state of macroeconomic balances during FY02 to a large extent will be defined by the performances of the manufacturing sector in the coming months. Indirect evidence (for export of apparel and other commodities) suggests that manufacturing had a lacklustre performance during the recent months. One, however, finds it difficult to reconcile the figures on credit flow to private sector with the manufacturing growth records and, as we will see later, with the import data.

Foreign Investment. A record volume of foreign investment (including FDI, portfolio investment and investment in EPZs) was received by Bangladesh in FY98 - \$320.82 million. Since then the flow of foreign investment has tapered off, falling to \$157.52 million in FY01. The surge in foreign investment flow in the domestic tariff area was spurred by investment in the energy sector which subsequently fizzled out as the awards under the next round of bidding for the gas exploration blocks were delayed. Portfolio investments mostly withdrew in the wake of the stock market boom of FY97, resulting a net *outflow* of \$132 million, and has not come back since then. Investments in the EPZs took a severe beating in FY01 when it halved in one year (from \$70.61 million in FY99 to \$ 34.98 million in FY00) as the prospective Japanese

and Korean investors withheld their investments in the face of a US threat to deploy trade sanctions against Bangladesh, i.e. cancellation of GSP facilities because of absence of trade union rights in the Bangladesh EPZs. However, investment in the EPZs picked up in FY01 (\$48.41 million) as the issue of worker's rights was amicably resolved between Bangladesh and the USA.

Preliminary indications suggest that if nothing extraordinary happens in the energy sector, the foreign investment flow to Bangladesh will continue to stagnate, if not experience a further fall in FY02. Data for the months of July-October, 2001 indicate that the country has received only \$32 million worth of foreign direct investment which compares very unfavourably with the already low figure of \$113 million for July-October, 2000.

In the case of portfolio investment, the economy experienced an *outflow* of (-) \$0.80 million on this account during July, 2001. Investment in the EPZs was relatively encouraging as \$15.23 million was received during the July-September period of FY02. It goes without saying that an upturn in foreign investment flow in the coming months can have a sobering effect on the balance of payment situation.

Capital Market. Following the boom and bust of November 1996, the *All Share Price Index* (ASPI) of the *Dhaka Stock Exchange* (DSE) fell from 1111.55 in June 1997 to 546.79 in June 1999. The market registered some recovery during the subsequent two years, yet the ASPI in June 2001 (716.06) remained lower than the pre-boom benchmark (999.05, June 1996). Market capitalisation in \$ terms also did not recover, in spite of the fact that 43 new securities were listed on the DSE between FY96 and FY01.

The ASPI for the DSE at end December 2001 stood at 817.79 with (DSE20 at 1075.72) which is more than 27% above the corresponding figure of the preceeding year. On the other hand, market capitalisation of the listed securities in the DSE in December 2001 amounted to \$1119.00 million, which is about 1.35% higher than the matching figure for FY01.

However, it is interesting that during the last six years most of the Initial Public Offerings (IPOs) were routinely oversubscribed indicating the inclination of the small investors to invest in the primary market and their lack of confidence in secondary transactions.

The continuing paralysis of the stock market in Bangladesh, because of its lack of transparency and accountability, is depriving the economy of much need equity financing for industrialisation. Given the institutional weaknesses (including inability to launch the Central Depository System) of the self-regulatory bodies (i.e., DSE) and the oversight agencies (i.e., Securities and Exchange Commission), it is too much to expect that cuts in interest rates on public savings instruments would automatically inspire the potential small investors to move to the capital market. The confidence of small savers has yet to recover from the trauma of the losses inflicted on them through market manipulation where no one has yet been held accountable for such criminal behaviour.

V. EXTERNAL SECTOR

Import. The slow pace of import growth between FY97 (3.09%) and FY00 (4.80%) has been construed as one of the indicators of depressed economic activity, particularly in the manufacturing sector. However, it has been also been argued that modest import growth has been a “blessing in disguise” for Bangladesh given its fragile balance of payments situation. Thus, when the import growth gathered momentum in FY01 and finally recorded a 11.42% growth, it was received with mixed feelings.

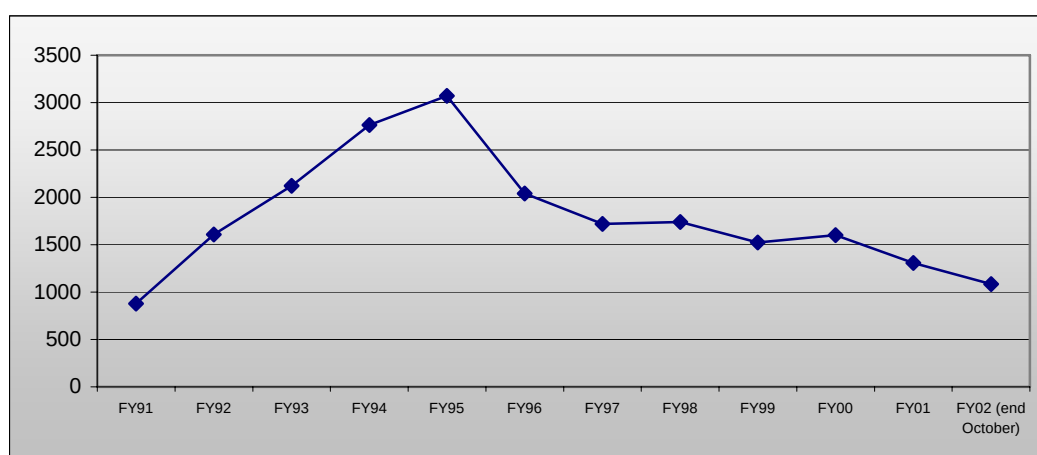
In the backdrop of depleting foreign exchange reserves, underpinned by the slowdown in export growth, deceleration in remittance flow and low off-take of foreign aid, it became imperative during the early months of FY02 to deploy some market-mediated import discouraging measures, e.g. discouraging import intensive public expenditures, increasing L/C margins, and applying *ad hoc* supplementary duties. The Caretaker Government initiated some measures in this respect and the new incumbent government proceeded further in this regard by temporally imposing a 100% L/C margin on 58 “non-essential” commodities.

Statement of the settlement of import L/Cs for the period July-December 2001 indicates a negative growth of imports, i.e. by (-)3.34% in US\$ term. Composition of the commodities imported under these settled L/Cs indicates a high growth of import of capital machineries (37.51%). Input of intermediate goods (2.73%) and machinery for miscellaneous industries (0.74%) registered only modest growth.

On the other hand, fresh opening of L/Cs during the July-December 2001 period indicates in further reduction of imports during the coming months. The L/C opening figures for the period show a fall by (-) 9.74% of imports. While most of the major categories experienced a fall in imports in real terms, import of capital machinery continues to grow at an exceptionally high rate (23.03%) during the first half of FY01.

It is heartening to note that import restraining measures of the government have been yielding some results. Nonetheless the slowdown in import growth is a “double edged sword” – in the present circumstances it will have a beneficial effect on the balance of payment, but may affect domestic economic activities in the not so distant future.

FIGURE 2: FOREIGN EXCHANGE RESERVE (IN mln. US\$)



Exports, One of the major success stories of the Bangladesh economy during the 1990s had been the accelerated growth of exports which put the country in the league of top 20 countries demonstrating the fastest export expansion. After the fall in the rate of export growth in the post-flood period (2.94% in FY99), the export growth rate bounced back to 8.23% and 12.39% in the FY00 and FY01 respectively. However, early figures on export performance in FY02 portend serious difficulties in the sector.

The drastic fall in export receipts during the first half of FY02 has imparted a strong shock to the economy. Export earnings during the July-December period was 16.45% short of the target and more than 11.47% lower than that of the matching figure of FY01. During this period both the *Export Price Index* and the *Export Volume Index* have suffered a significant erosion, recording declines by (-) 1.50% and (-) 9.97% respectively. The brunt of the export setback has been borne across the board by all major commodities of the export basket of Bangladesh. Most importantly, the country's premier export products, viz woven and knit garments, which account for more than three-fourth of our export receipts, experienced negative growth possibly for the first time since the emergence of the RMG sector in Bangladesh. During the period July-December 2001, woven and knit RMG exports fell by (-)11.28% and (-)8.23% respectively.

What is worrying is that the dent made in Bangladesh's export performance during the early period of FY02 may translate into a trend. The major factor which may make such a possibility a reality are the recession in the developed countries' market, arbitrary trade preference practiced by the USA-Bangladesh's principal market for RMG exports, our inability to raise domestic competitiveness, lack of export diversification etc.

The export shortfall is currently not only putting pressure on the balance of payment, but is also threatening a loss of livelihood for a very vulnerable section of the society, i.e. the women workers of the RMG sector. Whilst the current drive to address the situation is appropriately geared to securing "quota free and zero tariff" market access in the USA, it needs to be emphasised that in the absence of any significant improvement our trade-supportive infrastructure and enterprise level capabilities, it will be difficult to make full use of real market access opportunities.

Foreign Remittances. The annual flow of foreign remittances has steadily grown from \$758.23 million in FY90 to \$1953.19 million in FY00. As Bangladesh was getting ready to cross the \$2 billion mark in foreign remittances, it experienced a drop in flow by (-) 3.6% in FY01 – once again, a fall for the first time since the inception of the export of manpower from Bangladesh.

It is, however, heartening to note that the flow of foreign remittance recorded a robust growth of 20.36% (\$1116.91 million) during July-December, 2001. It will be interesting to observe how these early signals are maintained in the upcoming months. It has to be noted that the number of workers going abroad from Bangladesh is declining and such a trend may become more acute as recessionary symptoms engulf the non-OECD countries. Notwithstanding temporary setbacks, the flow of foreign remittances has been a significant area of promise for the Bangladesh economy as it is currently playing a predominant role in underwriting the balance of payments situation. It is worth noting that for the last three years official remittances have exceeded aid disbursements to Bangladesh so that our own citizens have now established themselves as the principal external benefactors of the Bangladesh economy.

Foreign Aid. During the recent past, Bangladesh has on average received about \$1.5 billion as foreign grants and loans. Inability to take full advantage of the committed foreign aid been one of the reasons which forced the government to resort to domestic borrowing to sustain its developmental activities. Slow progress in policy and institutional reforms have deterred the development partners in committing and disbursing foreign aid in larger volume. Such a trend in the flow of foreign aid deprived the Bangladesh economy of one of its traditional sources of support for the external account.

In FY01, Bangladesh received a commitment of \$2.3 billion worth of external assistance. Upto January 2001, actual disbursement amounted to \$650 million, i.e. only 28% of the commitment. The initial numbers for FY02 show that a total amount of \$55.5 million was committed during July-September 2001 which is only 17.3% of the comparable figure of FY01. It is expected that the commitment figure will rise as the incumbent government negotiates new projects with the development partners. However, Bangladesh's foremost immediate requirement for aid relates to the need for securing a quick disbursing, low conditionality balance of payment support. It will be interesting to observe whether Bangladesh can secure the same from the IMF keeping the preparation of the *Poverty Reduction Strategy Paper* (PRSP) in abeyance and failing to reach a stand by agreement with the Fund.

Foreign Exchange Reserve. The fall in the foreign exchange reserve has been a major macro-economic concern in the recent past. The forex reserve started to climb in FY91 from \$880 million and reached its peak in FY95 (\$3070 million). It is a matter of interpretation as to the extent to which such a high level of reserves signified an improved balance of payment situation and to what extent it was an expression of investment stagnation. Since FY95 the forex reserve has gradually depleted and at the end of FY01 was in the order of \$1307.

Early figures on FY02 indicate that the depletion of the forex reserve continued during the months of July–December. At end December, 2001 the reserves amounted to \$1305.35 million which is almost 13.9% less than the comparable figure for FY01. The current level of reserves is equivalent to 50 days of imports.

The reserves experienced a further fall in January '02 reaching \$1173 million (as of January 24, 2002) which is 18.35% lower than the comparable amount of the preceding year.

It should be remembered that a low level of forex reserve is a symptom of a malaise, not the disease itself. Short-term management of external payment (i.e., deferring payment to ACU) may be useful, but it seems it is becoming imperative to obtain some form of balance of payments support from external sources so as to maintain economic stability.

Balance of Payments. The current account balance has witnessed some improvement since the mid-1990s due to higher export growth, modest import expansion, buoyant private transfers including workers' remittances, a reasonable flow of official transfers and steady net income from the sale of services abroad. As a result, in FY00, Bangladesh enjoyed, albeit small, a positive current account balance of \$2 million. In contrast, in FY01, Bangladesh had a negative balance of (-)\$817 million on its current account. This resulted from a slowdown in workers remittances, a sharp fall in official transfers, increase in income payments and enlargement of the export-import gap. Thus, the immediate attempts to strengthen the balance of payment should start with addressing the primary sources of the deterioration in the current account balance.

The Bangladesh economy also, enjoyed a positive overall balance of payments amounting to \$325 million in FY00. At the end of FY01, the overall balance of payments indicated a negative balance of (-) \$326 million. Such a reversal was largely dictated by the changes in the current account. Deterioration of the financial account, particularly due to an increase in the short term debt servicing liability, largely explains the weakening of the BOP situation. However, one of the positive features of the BOP situation for FY01 relates to the reduction of the missing foreign earnings as expressed through the item “Error and Omissions” (\$720 million and - \$304 million in FY00 and FY01 respectively).

VI. CONCLUDING REMARKS

The forgoing review of the state of the Bangladesh economy reveals that some of the general weaknesses of the macroeconomic balances have become more acute during the early months of FY02. These trends may not only disrupt macroeconomic stability, but also undercut the growth prospects in the real economy.

Whilst the revenue collection situation remains steady, the need for government borrowing seems to be still very high, indicating the need for a major revision of the public expenditure package.

The inflation rate although still quite low, is showing some signs of an increase in non-food prices.

In the agriculture sector, *aus* and *aman* production appear to be satisfactory as of now, although much will depend on the *boro* harvest. The manufacturing sector’s performance continues to be sluggish. Foreign investment is tapering off and the capital market remains paralysed.

The shocks in the external sector are emanating from the fall in export growth. Low off-take of foreign aid is affecting the level of development activities and the balance of payment. Depressed import growth and a high level of remittance flows have been useful in containing the strong pressures on the balance of payment.

It is time that Bangladesh prepares a short-term package for FY02 which will allow it to adjust the economy at a lower equilibrium through consolidation measures. It is being suggested that a conscious trade-off be made between economic growth and macroeconomic stability – in favour of the latter-for the current fiscal year (however it is recognised that such a trade-off may not be suitable in the medium term).

While designing such a package one should not indulge in political point scoring, otherwise it will confuse us in locating the real sources of the current problems and deflect us in identifying the appropriate remedies.

The sources of Bangladesh's emerging economic problems are of a structural nature, and may persist over a period of time unless radical remedial actions are initiated, particularly in the areas of public expenditure, privatisation, the financial sector, capital market, public utilities, industrial and export diversification and trade-supportive infrastructure.

Such an approach to structural adjustment must emerge out of an indigenous process of policy making and dialogue which will need to be underwritten by a political consensus at home. ■