Overseas Development Institute

CENTRE FOR POLICY DIALOGUE (CPD)
BANGLADESH
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Global Financial Crisis Discussion Series

Paper 12: Bangladesh Phase 2

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January 2010

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1 This paper was funded by the UK Department for International Development (DFID) and is part of a wider research project coordinated by the Overseas Development Institute (ODI) London, but it does not necessarily reflect their views.
2 The authors would like to thank all reviewers and gratefully acknowledge contributions from Mr. Tapas Kumar Paul, Research Associate, CPD, Mr. Ashiqun Nabi, Research Associate, CPD, and Hasanuzzaman, Senior Research Associate, CPD, for their capable research support. The authors remain solely responsible for the analysis in the report.

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Acronyms

ADB	Asian Development Bank
ADP	Annual Development Programme
BB	Bangladesh Bank
BBS	Bangladesh Bureau of Statistics
BGMEA	Bangladesh Garments Manufacturers and Exporters Association
BKMEA	Bangladesh Knitwear Manufacturers & Exporters Association
BMET	Bureau of Manpower, Employment and Training
BTMA	Bangladesh Textile Mills Association
CPD	Centre for Policy Dialogue
DFID	UK Department for International Development
EBA	Everything But Arms
EDF	Export Development Fund
EPB	Export Promotion Bureau
EPZ	Export Processing Zone
EU	European Union
FDI	Foreign Direct Investment
FGD	Focus Group Discussion
fob	Free on Board
Forex	Foreign Exchange
GDP	Gross Domestic Product
GoB	Government of Bangladesh
GSP	Generalized System of Preferences
HIES	Household Income and Expenditure Survey
HSC	Higher Secondary Certificate
IMED	Implementing, Monitoring and Evaluation Division
IMF	International Monetary Fund
IT	Information Technology
L/C	Letter of Credit
LIBOR	London Interbank Offered Rate
LIC	Low-Income Country
LTU	Large Taxpayers' Unit
MDG	Millennium Development Goal
MoF	Ministry of Finance
MTMF	Medium-Term Macroeconomic Framework
MW	Megawatt
NBR	National Board of Revenue
NITRAD	National Institute of Textile Training, Research and Design
ODA	Official Development Assistance
ODI	Overseas Development Institute
PFI	Portfolio Investment
PPA	Public Procurement Act
PPP	Public–Private Partnership
PPR	Public Procurement Rules
RMG	Readymade Garments
SDR	Special Drawing Rights
SME	Small and Medium-Sized Enterprises
TIN	Tax Identification Number
UAE	United Arab Emirates
UK	United Kingdom
US	United States
USITC	US International Trade Commission
VAT	Value Added Tax
y-o-y	Year-on-Year

Abstract

Although Bangladesh was initially spared the worst consequences of the global financial crisis, the lagged impacts have started to become visible, transmitted by means of various channels. Overall, export earnings have remained robust, driven by readymade garment exports, but volatility has increased. In the third quarter of 2009, there was a significant fall in exports, with apparel exports also falling victim to sluggish demand. At the same time, policies pursued by competitors have had an adverse impact on Bangladesh's competitive strength in the global market.

To address the emerging tasks of stimulating domestic demand and increasing export competitiveness, Bangladesh put in place two consecutive stimulus packages, went for a higher budget deficit and adopted a number of other countercyclical measures.

Remittance inflows have remained robust until now: the number of terminally returned workers is insignificant against the large stock of workers managing to stay working overseas. However, a lower number of outward migrants has given rise to concerns with regard to future inflows of remittances, and has also put pressure on the domestic labour market.

The gross domestic product (GDP) growth projection of 5.5% for 2009/10 is the lowest in recent years, holding consequences for jobs and incomes. The available evidence does not suggest a large number of factories being shut down as a result of the crisis, nor does it indicate significant retrenchment in apparels and other export-oriented sectors; however, overtime payments and new recruitments have suffered.

On the other hand, with the majority of the population making a living from agriculture, good harvests have meant that the poverty impact of the crisis may have been limited. An earlier fall in commodity prices has also been beneficial with regard to the real incomes of the poor. With remittance inflows holding, these factors have had a positive impact on the poverty situation in Bangladesh.

Bangladesh has been somewhat of an outlier in this crisis. However, in view of a jobless recovery, Bangladesh will need to pursue a proactive policy, one which continues with countercyclical measures and at the same time is forward looking, to exploit the advantages arising from the expected global economic recovery. Effective and timely implementation of the recently announced support measures will be of importance in this context. To do this, Bangladesh will need to improve its investment climate significantly through better power and infrastructure provisions.

1. Introduction

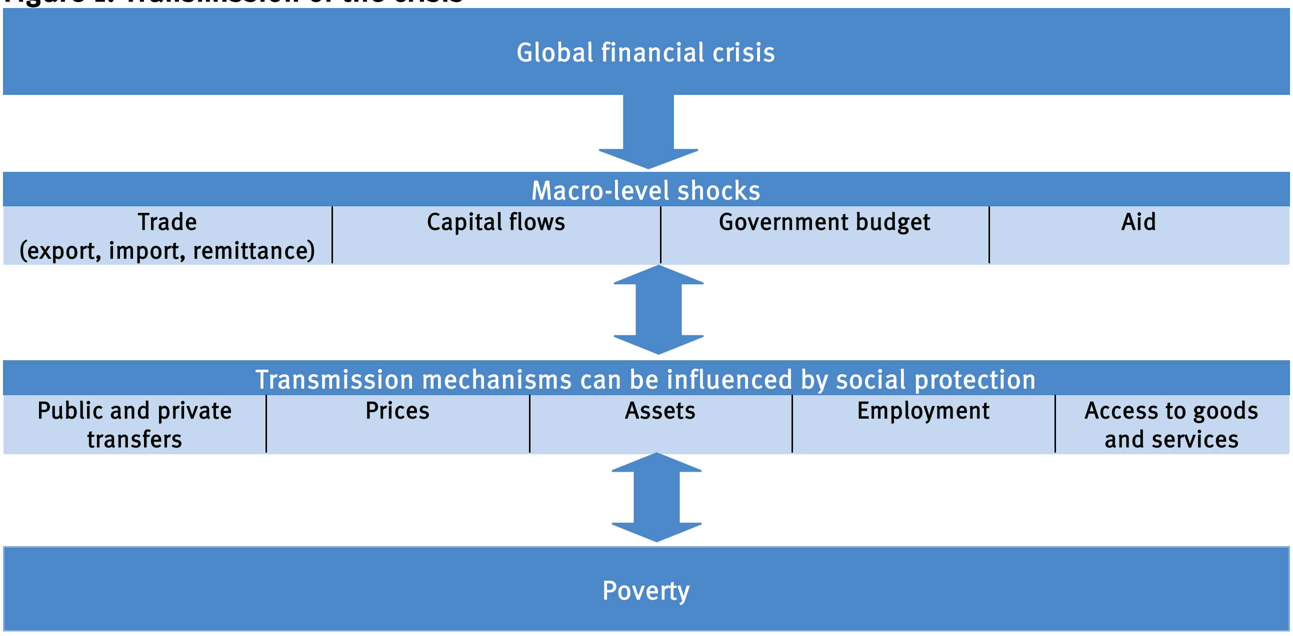
The impacts of the global financial crisis have been felt in the increasingly globally integrated economy of Bangladesh in a very distinctive manner. In a number of ways, Bangladesh has been an outlier, with some lag to the consequences. Indeed, crisis impacts were felt in a much more intense manner in the second half of 2009, when many developed countries (Bangladesh's major import sources and export destinations) were beginning to recover. This lagged response makes the Bangladesh story somewhat different from that of many other low-income countries (LICs).

The crisis has left its fingerprints on Bangladesh's externally driven economy through the various transmission channels of exports, imports, remittances and aid and foreign direct investment (FDI) flows, with consequent repercussions for the labour market, domestic resource mobilisation and gross domestic product (GDP) growth and poverty. Nevertheless, the depth of the consequences has tended to vary during different phases in the crisis. Two such phases can be discerned from an analysis of the impact of the ongoing crisis.

In the first phase, ending with the first quarter of 2009, impacts through the various channels, although present, were relatively subdued.[3] Bangladesh was one of very few developing countries not to be affected to the extent expected. Although exports of primary products suffered early shocks through falling demand, at the aggregate level export performance continued with double-digit growth, driven by steady performance of apparels exports until the end of the first quarter of 2009. At the same time, despite cases of early retrenchment of workers abroad, remittance flows continued to be robust, thanks to the large stock of workers managing to stay overseas and continuing to send money home.

However, a study on the impact of the crisis (Rahman et al., 2009a) cautioned that Bangladesh could face a lagged response, with further deepening of the crisis towards the second half of 2009. In fact, some indications of trouble began to be felt even in the second quarter of the year. This was reflected in the response of policymakers in terms of macroeconomic management, attempts at countercyclical measures and the stimulus packages put in place to address the emerging challenges.

Figure 1: Transmission of the crisis



Source: Adapted from McCord and Vandemoortele (2009).

3 A detailed analysis of the impacts of the global financial crisis on the Bangladeshi economy, through the various transmission channels, is presented in Global Financial Crisis Discussion Paper 1: Bangladesh (May 2009) (Rahman et al., 2009a), which was part of an ODI project titled 'The Global Financial Crisis and Developing Countries'.

This paper tracks and traces the impact of the crisis on the Bangladeshi economy through the different transmission channels and their economy-wide and sectoral impacts (Figure 1). It provides an analysis of the fiscal and financial policies taken and the stimulus packages put in place by the Government of Bangladesh (GoB) to address the emergent challenges, and seeks to assess the efficacy of these. It also puts forward a set of policy recommendations perceived to be important as the Bangladeshi economy emerges from the current slowdown and prepares to take advantage of a possible recovery.

The paper is based on an analysis of secondary data and literature, government policy documents, cross-country experiences and media reports. Focus group discussions (FGDs) and interviews with relevant stakeholders generated more in-depth insights and information.

The rest of the paper is divided into four sections. Section 2 revisits the various transmission channels to evaluate the impact of the crisis on Bangladesh's economy. Section 3 carries out an analysis of the policies undertaken by GoB in view of the crisis. Section 4 presents some policy recommendations. Section 5 concludes.

2. Impacts on the Bangladesh economy: Revisiting the transmission channels

Over the past couple of decades, Bangladesh has become increasingly integrated into the global economy.[4] The degree of openness of the economy rose from 16.8% to 42.5% and the extent of globalisation increased from 24.9% to 56.3% between 1990/91 and 2008/09.[5] Although increasing global integration has created an opportunity for Bangladesh to take advantage of the global economy, it has also exposed the country to vulnerabilities emanating from global shocks. Indeed, the ongoing global financial crisis encompasses many of the challenges that a low-income economy such as Bangladesh faces as it strives to become integrated into the global economy.

As is evident from the subsequent analysis, impacts on Bangladesh's economy through the transmission channels were rather limited in the first phase of the crisis,[6] but adverse consequences have become more evident in recent times (since April 2009). Despite some volatility, export performance showed resilience until March 2009, but the second and third quarters of the year saw a considerable fall in total export earnings. On the other hand, imports (in value terms) have fallen consistently during the crisis phase, in view of falling global commodity prices, resulting in a comfortable balance of payments situation. Although the outflow of migrant workers has slowed, as a result of limited scope for new jobs, remittance flows have remained buoyant throughout. New official development assistance (ODA) opportunities have been created to mitigate the crisis,[7] although these have been constrained, largely by a lack of domestic absorption capacity. Bangladesh's government revenue mobilisation structure is characterised to a large extent by import-related sources; falling imports have therefore meant that government revenue mobilisation has been particularly affected. The slowdown in exports and the lack of opportunities in job markets abroad have had adverse impacts on the domestic labour market. A detailed analysis of the impact of the crisis on the Bangladeshi economy, through the various transmission channels, is presented in the following subsections.

2.1 Export performance

With the deepening of the global financial crisis and the consequent slump in developed country demand for exported goods from developing countries, a significant slump in global exports was expected. The International Monetary Fund (IMF) estimate of global trade growth for 2008 (made in October 2008), of 15.3%, was revised downward to 11.2% (actual). Moreover, the updated projections indicated a contraction of -12.0% for 2009, alluding to a severe fall in global trade. In this context, Bangladesh's export performance in 2008/09 was quite remarkable: growth in this year was a respectable 10.3% (Table 1). It is particularly interesting to note that this record was attained against the backdrop of high growth rates of 15.6% and 15.9% in the previous two fiscal years. Export growth of apparels, which contribute about three-quarters of total export earnings, held strong. Two of the major contributors, knit and woven RMG (readymade garments), also maintained impressive growth figures: 17.4% and 13.2%, respectively, compared with the last fiscal year (2007/08).

Widespread apprehension regarding a possible slowdown in apparels exports was proven for Bangladesh only partially – in the first quarter of 2009 (January-March), total exports registered 6.0% growth (y-o-y), although the growth rate became negative (-0.6%) in the second quarter (April-June).

4 Tariff rates have been rationalised significantly, the anti-export bias has largely been removed, both exports and imports have been derestricted and a host of incentives have been put in place to stimulate and encourage export-oriented activities.
5 Degree of openness is defined as share of export and import as a percentage of GDP. Extent of globalisation is defined as export + import + official development assistance + remittance + foreign direct investment as a percentage of GDP. Bangladesh's fiscal year runs from July to June.
6 In the context of Bangladesh, the first phase of the crisis refers to the period from September 2008 to March 2009.
7 More on this issue is in Section 2.5.

This is an indication of increasing volatility in Bangladesh's export performance in view of the crisis,[8] explained by some by the so-called 'Wal-Mart effect'.[9] In fact, 2008/09 as a whole experienced some volatility: exports faced difficulties in view of falling demand in the second quarter of the fiscal year (October-December 2008). Export growth of knit and woven RMG decelerated considerably in the fourth quarter of the fiscal year (April-June 2009) (y-o-y), posting 4.0% and 3.6% growth, respectively. In contrast with RMG exports in the same quarter (total 3.8%), exports of non-RMG products declined by -14.8%, with all non-RMG exports, other than raw jute, posting negative growth rates. The leather industry was particularly affected: exports of leather declined by 46.8% compared with the previous fiscal year.

Table 1: Quarterly export growth in value of Bangladesh's major commodities, 2008/09 and 2009/10Q1 (%)

	2008/09 (Jul-Jun)					2009/10
	Q1	Q2	Q3	Q4	Jul-Jun	Q1
RMG	44.6	5.4	12.7	3.8	15.4	-9.7
Woven RMG	36.7	6.3	9.9	4.0	13.2	-9.7
Knit RMG	52.0	4.6	15.8	3.6	17.4	-9.7
Non-RMG	35.7	-22.2	-16.4	-14.8	-5.8	-13.1
Raw jute	-27.6	5.6	-38.1	22.0	-10.5	27.9
Tea	36.3	-28.5	-41.5	-56.6	-17.3	-85.6
Frozen foods	15.7	-24.3	-32.2	-21.0	-14.8	-37.9
Leather	-6.3	-50.2	-41.4	-46.8	-37.6	-24.6
Jute goods	-4.3	-32.1	-18.1	-7.2	-15.4	5.2
Chemical	195.8	-13.8	15.0	-28.4	29.7	-58.0
Engineering products	30.9	-55.8	-7.6	-8.8	-13.8	-10.5
Home textile	27.8	-3.9	38.4	-9.1	10.7	-19.6
Footwear	49.0	8.8	3.7	-13.6	10.2	-3.0
Others	54.6	-17.1	-18.9	-10.3	-2.0	-6.8
Total exports	**42.5**	**-1.6**	**6.0**	**-0.6**	**10.3**	**-11.7**

Source: Calculated from EPB (2009).

A decomposition of the growth dynamics reveals that the rise in total exports (10.3%) was more than accounted for by a rise in volume (11.9%), whereas prices had somewhat declined on average (-1.6%) (Table 2). Thus, most of the export growth in 2008/09 was volume driven, and exporters had to cope with lower prices and lower profit margins. Indeed, anecdotal information suggests that a large number of exporters continued to export at lower prices, with a view to maintaining their relationships with importers in developed countries and with buying houses (mainly in the case of apparels).

Table 2: Decomposition of Bangladeshi export growth dynamics, 2007/08-2009/10Q1 (%)

	2007/08	2008/09	2009/10Q1 (Jul-Sep)
Total export growth	15.9	10.3	-11.7
Volume index growth	14.1	11.9	- 8.4
Price index growth	1.8	-1.6	- 3.2

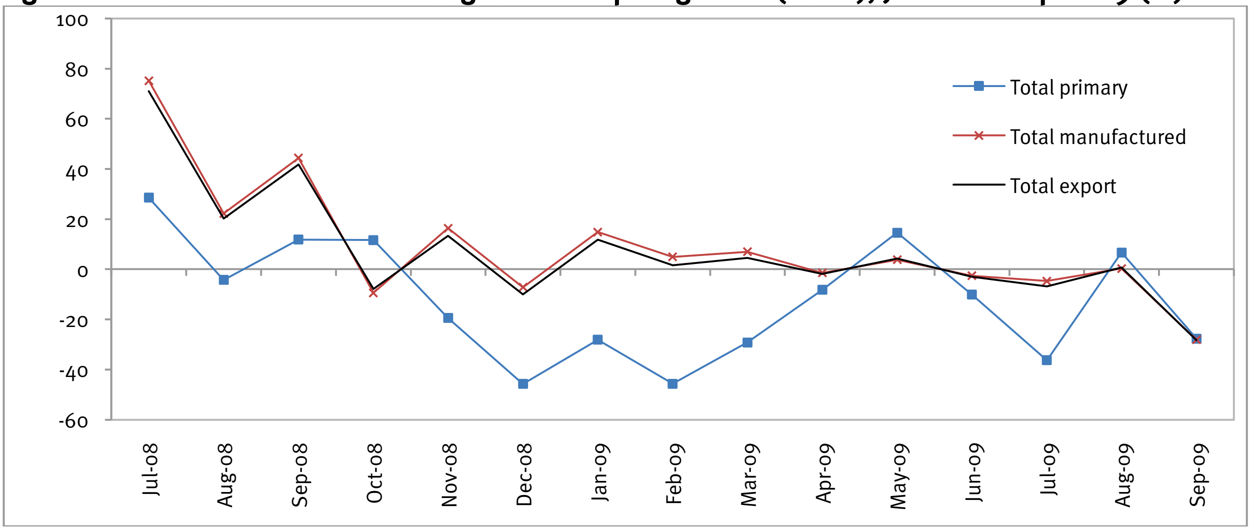
Source: Compiled from EPB (2009).

Performance of the export sector has had a concomitant impact on industrial production, particularly because export-oriented production accounts for a significant part of manufacturing sector GDP in Bangladesh. During 2008/09, the quantum index of production of medium- and large-scale manufacturing industries registered growth of 7.4%. Major primary product groups recorded relatively low production growth of 0.8%. However, higher growth of apparels meant that export-oriented manufacturing industry recorded a modest 10.6% growth during the same period (BBS, 2009a).

8 The effect of the base year's performance (compared with the corresponding months of 2008) on export growth was also a contributing factor.

9 The Wal-Mart effect refers to continued (even higher) demand for low-priced items during recession as some consumers tend to shift their demand to lower-end products in view of reduced earnings.

Figure 2: Gradual slowdown of Bangladeshi export growth (value), Jul 2008-Sep 2009 (%)



Source: Based on EPB (2009).

The resilience of the export sector tapered away towards the last quarter of 2008/09, when overall exports declined by 0.6% (Figure 2). Lower demand led to an accumulation of inventories, and rising inventories led to a further slowdown in orders. Uncertainties about whether the recession would be 'L', 'U' or 'V' shaped also added to lower business confidence. The slowdown in export earnings continued during the first quarter of 2009/10, when the lagged impact of the global downturn became more pronounced. Exports of manufactured products (in value terms) declined by a substantial amount, registering a fall of 11.7% during the first quarter of 2009/10 (y-o-y), underwritten primarily by a fall in exports of woven and knit RMG, both declining by 9.7%.[10] Exports of tea (-85.6%), agricultural products (-18.4%) and frozen foods (-37.9%) were also affected significantly. Only exports of electronics managed to record substantial positive growth, of 54.8%. All other major manufacturing items recorded a significant decline in exports in the first quarter of 2009/10. It is to be noted that, in the first quarter of 2009/10, the fall in export value (by 11.7%) was accounted for mainly by the decline in volume (8.4%) terms; however, average prices also decreased significantly compared with the corresponding period of the previous fiscal year (by 3.2%).

October 2009 saw setbacks. Total exports registered 18.0% growth over October 2008 but, taking into consideration July-October 2009 (the first four months of 2009/10), total export earnings experienced a fall of 6.7% compared with the corresponding period of 2008/09; exports of apparels had declined by 5.7%.

Table 3: Export growth in value of Bangladesh's major commodities, Jan-Oct 2008 and 2009 (%)

	2008	2009
RMG	31.1	2.5
Woven RMG	25.4	1.4
RMG	36.7	3.5
Non-RMG	22.6	-13.2
Raw jute	-0.7	11.7
Tea	26.9	-62.9
Leather	-6.6	-34.3
Jute goods	-3.5	0.8
Frozen foods	16.1	-27.5
Chemical	46.2	-57.0
Engineering products	-0.3	-2.0
Home textile	15.8	0.1
Footwear	36.9	-6.4
Total exports	29.0	-1.2

Source: Calculated from EPB (2009).

10 Table 1 provides further product-specific performance information.

Total export earnings during the first 10 months of 2008 (January-October) increased by 29% over the same period of 2007, and RMG exports posted 31.1% growth (Table 3). With the emergence of the global financial crisis, the same time period of 2009 saw total exports decline by 1.2%, compared with the corresponding period of 2008. Although exports of RMG products managed to maintain a marginal positive growth (2.5%), exports of tea, leather, frozen foods and chemicals decreased sharply.

US imports of apparels (both knitwear and woven) from most other countries have decelerated during the crisis period. Estimations based on US International Trade Commission (USITC) data show that total apparel imports to the US declined by 13.5% during January-September of 2009, over the same period of 2008. Imports declined by 0.1% from China, 4.6% from Vietnam and 24.2% from Cambodia during this period. However, US imports of apparel items from Bangladesh increased by 1.8% over the period between January and September 2009 (Table 4).

Table 4: Growth in US imports of apparel items (knit and woven) in Jan-Sep 2009 over Jan-Sep 2008 (%)

	Knit	Woven	Apparel (knit & woven)
China	5.9	-4.5	-0.1
Mexico	-23.4	-14.1	-17.8
Vietnam	-0.5	-9.5	-4.6
Indonesia	5.9	-14.9	-4.8
India	-4.1	-9.5	-7.3
Bangladesh	-5.6	4.5	1.8
Honduras	-21.3	-20.4	-21.1
Cambodia	-22.0	-28.4	-24.2
Total	-12.2	-14.8	-13.5

Source: Computed from the USITC database.

Shares of various competing countries in the US apparels market have also changed during the crisis period. China, the largest exporter in the US market, sustained and even managed to improve its share in the (shrinking) market during the recessionary period. China's market share increased by more than 5.0% in 2009 (data available up to September 2009) compared with 2007, the pre-crisis year. In the case of Bangladesh, market share of apparel items also increased, though marginally, by 1.5% in 2009 from 2007 (Table 5). During the third quarter of 2009, China's market share increased further, standing at 42.8%. Against this, Bangladesh's share in the US market reduced to about 4.9%, testifying to the lagged response.

Table 5: Value share and rank by country in US imports of apparel items (knit & woven), 2007-2009 (%)

Country	2007	2008	2009 (Jan-Sep)	Ranking (2009)
China	31.9	33.0	37.1	1
Vietnam	5.7	7.1	7.7	2
Indonesia	5.3	5.5	6.2	3
Bangladesh	4.0	4.7	5.5	4
Mexico	5.9	5.5	5.2	5
India	4.3	4.3	4.8	6
Honduras	3.4	3.6	3.2	7
Cambodia	3.2	3.3	2.9	8

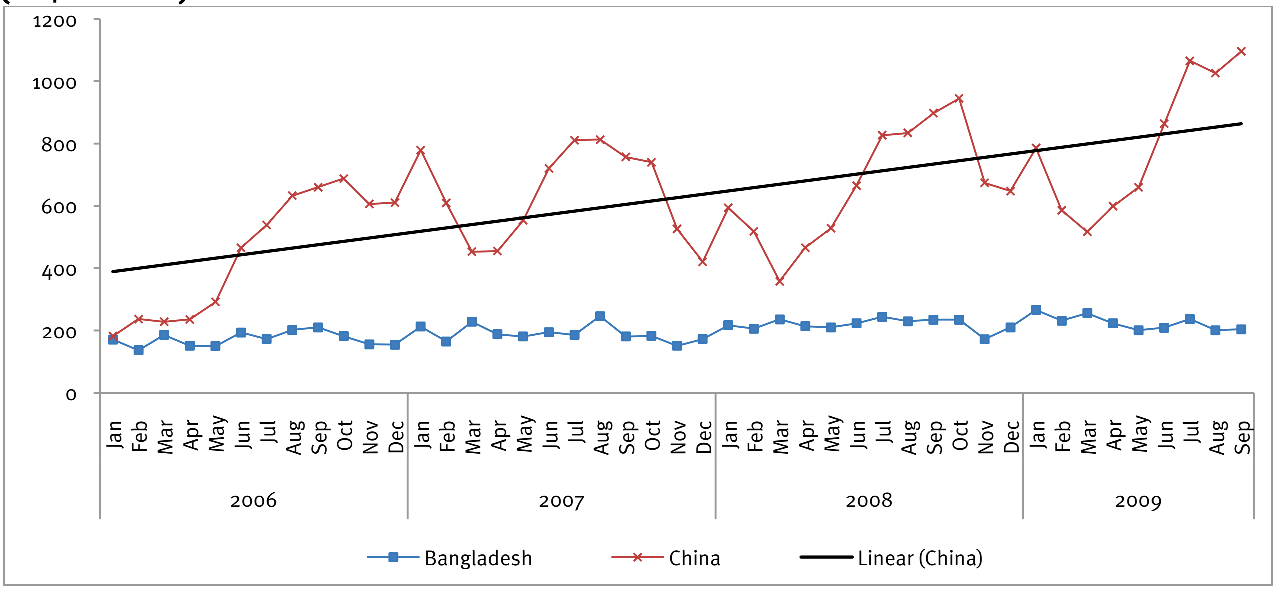
Source: Computed from the USITC database.

This gradual development has come from both weakened demand in external markets and also from some degree of erosion of Bangladesh's competitiveness. If the top 14 RMG products of Bangladesh are considered, during September 2008 to September 2009, US imports from Bangladesh decreased by 13.2%, whereas exports of the same items from China to the US increased by about 22.0% over the same period.[11] Since March 2009, China's exports (of the 14 RMG products mentioned above) to the US

11 These include eight woven items and six knit items.

have recovered considerably, whereas for Bangladesh export earnings have remained mostly unchanged (Figure 3). Withdrawal of the US quota restriction on imports from China in January 2009, coupled with China's aggressive response to the global shock (e.g. raising tax rebates on lower-end export items, in addition to other export incentives), has contributed towards a revival of China's exports to the US market. Unit price cuts by Chinese manufacturers may also have raised competitiveness and stimulated demand for China's RMG products.[12] Along with external factors, domestic supportive policies to stimulate demand have helped China's export sector, particularly apparels.[13]

Figure 3: Imports by the US – Bangladesh's major RMG export items vis-à-vis China, 2006-2009 (US$ millions)



Source: Computed from the USITC database.

As in the case of the US market, in the European Union (EU) market China remained by far the leading source of apparel products.[14] Indeed, China was able to increase its market share, while the market share of second-ranked Turkey has been on the decline in the recent past, if pre- and post-crisis periods are compared (Table 6). Despite China's dominant role in the EU market, Bangladesh and India both managed to increase their market share in a shrinking market.[15]

Table 6: Share and rank by country in the EU-27 import of apparel items (knit and woven), 2007-2009 (%)

	2007	2008	2009	Rank 2009
China	37.7	42.6	43.0	1
Turkey	15.4	13.2	12.3	2
Bangladesh	7.6	8.0	9.3	3
India	6.6	6.6	8.0	4
Tunisia	4.4	4.3	4.1	5
Morocco	4.4	4.0	3.6	6

Source: Computed from the Eurostat database

12 For the six knit products discussed above, China managed to reduce the respective price by about 22% (on average) in September 2009 compared with September 2008, whereas (on average) prices offered by Bangladesh increased by 2%. For the eight woven products, the price offered by China was about 14% lower in September 2009 compared with September 2008. For some of these products (four out of eight), Bangladesh was also forced to follow China in reducing prices.

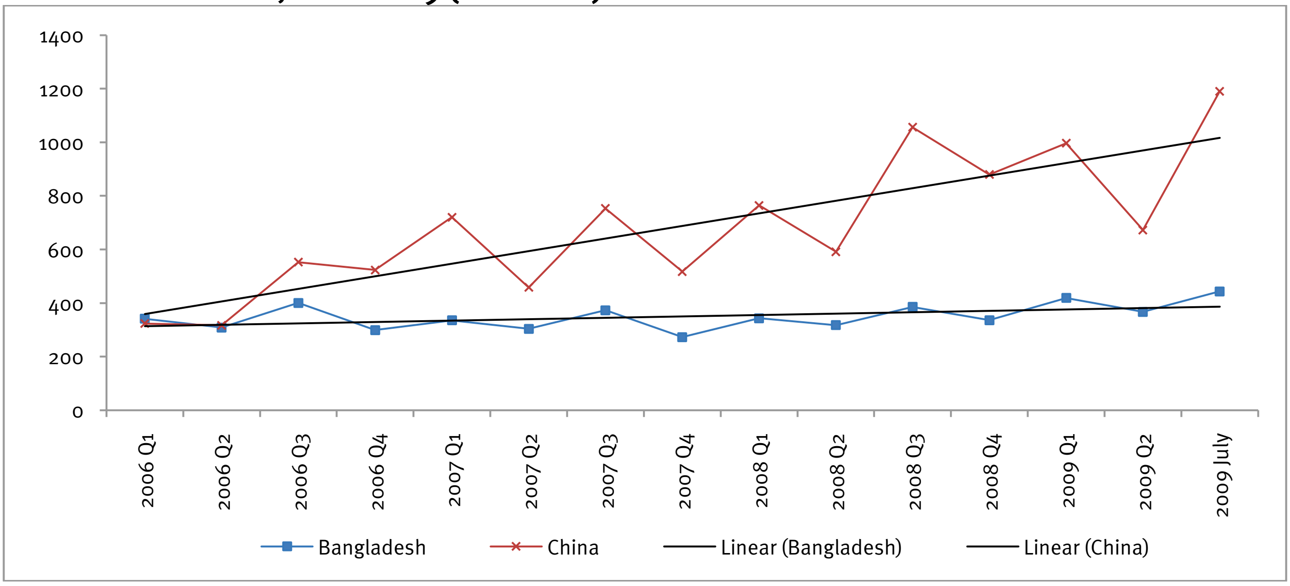
13 The Chinese textile industry benefited from the introduction of a tax rebate and a declared 15% cash subsidy on exports. China also maintained a fixed exchange rate of the yuan against the US dollar. The Chinese yuan depreciated against the euro by 6.2% between January and November 2009.

14 The analysis considers only extra-EU trade.

15 58.5% of total apparel exports from Bangladesh were destined for the EU in 2008/09.

Exports of Chinese apparels to the EU, as indicated by mirror data, experienced a high degree of volatility. As is evident from Figure 4, where exports of Bangladesh's top 15 apparel items are given in a comparative setting with China, the gap between Bangladesh and China widened between 2006 and 2009 (July). Although Bangladesh is entitled to Generalized System of Preferences (GSP) facilities in the EU market, for the top seven knitwear products in the EU market it registered negative growth of 6.7% during April-July 2009 compared with the same period of 2008.[16] China registered growth of 6.4% for the same set of products during the same period. In the case of the top eight woven RMG products, during the first seven months of 2009 Bangladesh posted only 0.5% growth compared with the corresponding months of 2008, whereas China registered rather impressive growth of 7.1%.

Figure 4: Imports by the EU-27 (monthly average by quarter) – Bangladesh's major RMG export items vis-à-vis China, 2006-2009 (€ millions)



Source: Computed from the Eurostat database.

With regard to the near-term outlook for Bangladesh's export performance, much will depend on the pace at which the developed economies recover, and whether Bangladesh can face the stiff competition from its competitors, which are trying to restructure their exports in view of the crisis to address the challenges and realise emerging opportunities. Entrepreneurs will have to try to increase the productivity of both labour and capital. For its part, GoB will need to create the supportive and conducive environment required for this, particularly through availability of power and infrastructure. One promising sign is that demand for apparels is on the rise, and Bangladeshi entrepreneurs have started to receive enhanced orders from buyers and major buying houses. However, the downward push on prices appears to have been sustained. As a result, it is unclear whether higher volumes of orders will result in higher export earnings. With regard to non-RMG products, the slump in export performance has continued unabated.

2.2 Performance of remittance flows

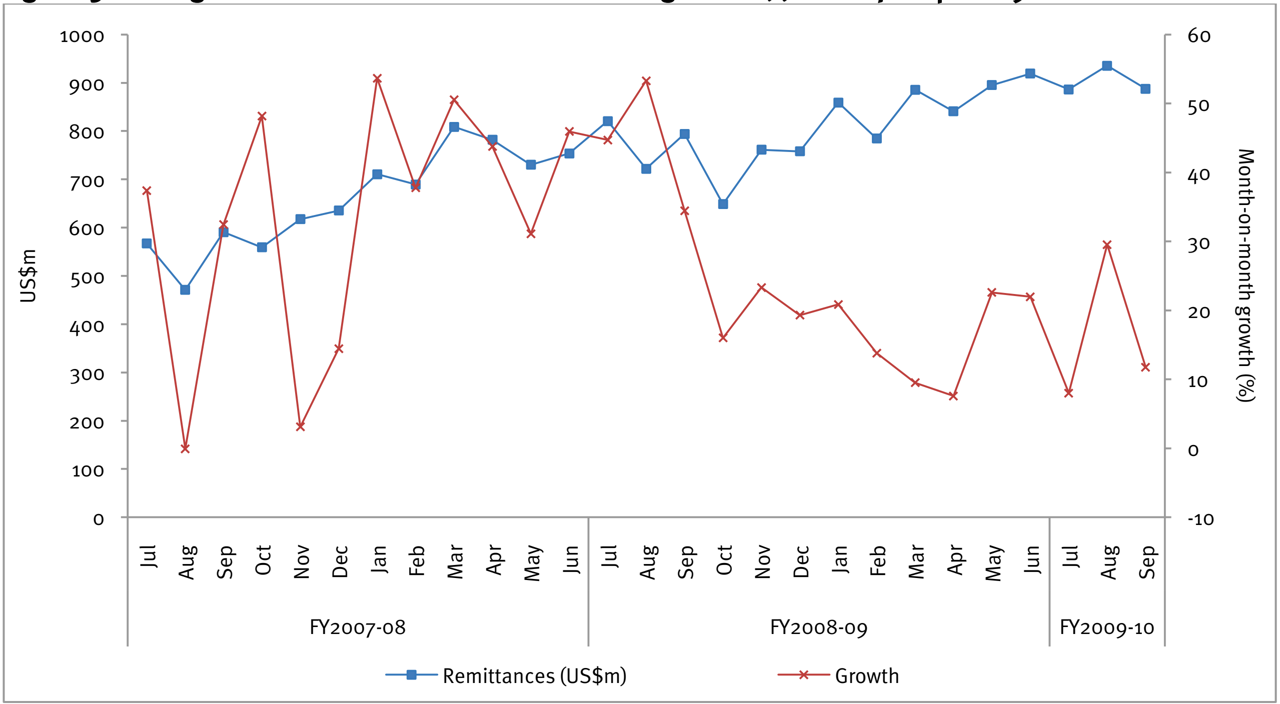
In recent times, Bangladesh has emerged as a major exporter of manpower, targeting particularly the labour-intensive sectors of the various developed and developing economies. Over the past two years (2007/08 and 2008/09), a record number of Bangladeshi workers, 1.6 million (BB, 2009a), have left the country in search of jobs abroad. Over the years, the contribution of remittances to Bangladesh's economy in terms of GDP has increased significantly (from 4.0% in 2000/01 to 10.8% in 2008/09). If remittances through informal channels were taken into account, for which no official data are available,

16 Under the EU Everything But Arms (EBA) initiative, Bangladesh receives duty-free quota-free treatment for all its exports. Since average duty on apparels in the EU is about 12.1%, this allows Bangladesh to enjoy a considerable competitive edge vis-à-vis China, which is not eligible for such preferential treatment.

this would be even higher. Setting aside the role of remittances in terms of beefing up Bangladesh's forex coffers and enhancing its ability to import, remittances sent from overseas also play a crucial role in strengthening the social security of the family members of the remitters, who often come from low-income households.

In spite of the recession, unlike exports, remittance earnings have been on the rise in recent months, albeit with some fluctuations (Figure 5). Overall, remittances during 2008/09 were 22.4% higher compared with 2007/08. However, monthly growth (y-o-y) during 2008/09 shows a slower pace, particularly since January 2009. A reduction in the number of outward migrants during recent months could explain this slowdown. Nevertheless, remittance earnings during July-October of 2009/10 ($3,619.30 million) recorded 21.2% growth. This implies that a growth rate of only 4.1% would be required over the next eight months to achieve the remittance target set by GoB for 2009/10.[17]

Figure 5: Change in the flow of remittances in Bangladesh, Jul 2007-Sep 2009



Note: The secondary axis represents the growth rate.
Source: Compiled from BB (2009a).

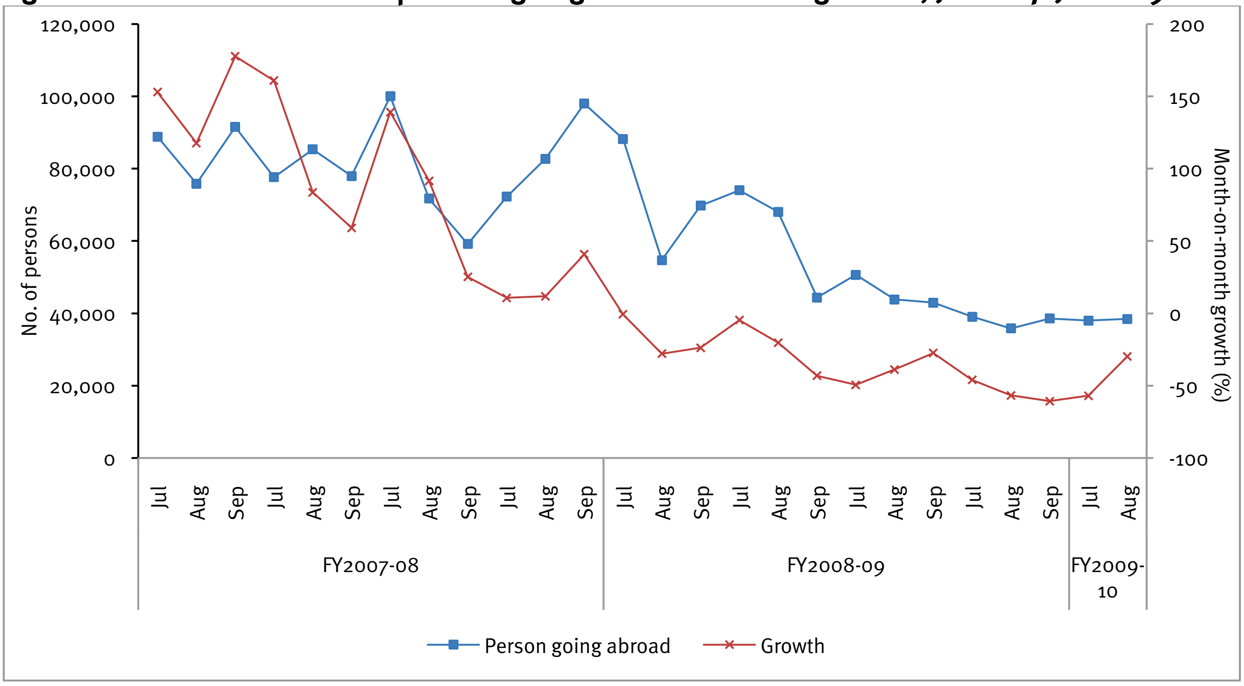
In contrast with in many other countries, performance of remittance flows has thus shown resilience in the face of the crisis. There are a number of explanations for this. First, annual outflow of workers is an insignificant part of the total stock of Bangladeshi workers working abroad (accounting for about 8% to 9%). This limits the impact of the crisis on remittance inflows from lower outflows of migrant workers. Second, part of the increase in remittances inflows could be accounted for by terminal workers bringing back their savings. Third, as a consequence of the crisis on the global financial system, a number of migrants may have shifted their savings to their home country. Fourth, in recent years Bangladesh Bank (BB) has promoted the use of legal channels (banks, money exchanges and other formal institutions) to remit foreign currency to Bangladesh. At the same time, the cost of sending remittances has fallen.

However, a disquieting development has emerged with regard to the falling number of workers leaving for abroad. As is evident from Figure 6, export of manpower from Bangladesh has been on a declining trend for some time now. During 2008/09, the number of persons going abroad for work was around

17 The target was set conservatively, at $10.6 billion, in view of the crisis (9.4% growth over the previous year). Macroeconomic performance targets are generally set in Bangladesh by keeping in line with historical trends rather than with strategic visions and policy options in mind.

0.65 million, recording a significant fall of -33.7% against 2007/08. The trend continued during the first two months of 2009/10, recording a fall of -46.5% (y-o-y).

Figure 6: Trends in number of persons going abroad from Bangladesh, Jul 2007-Jul 2009



Note: The secondary axis represents the growth rate.
Source: Compiled from BB (2009a).

The lion's share is sent back from Middle Eastern countries (62.9% in 2007/08). The other two major sources are the US (17.4% in 2007/08) and the UK (11.3% in 2007/08). Available records show that, during the crisis-affected period, the share from the Middle East increased slightly, to 65.8% in 2008/09, whereas the share of the US and the UK declined to 16.3% and 8.1%, respectively. Data on remittance inflows for the first four months of 2009/10 (July-October 2009) show a further decline in the share of the US (13.6%) but that the shares of the UK (8.1%) and the Middle East (64.5%) have remained rather steady. However, the number of workers is higher in the Middle East, where most workers enter the lower end of the job market; in the UK and the US, a significant number work as professionals or skilled workers and in the services sectors.

Bangladeshi workers going abroad in 2009 were significantly fewer compared with the previous two years, mainly because some of the major destinations (including the United Arab Emirates (UAE), Saudi Arabia, Malaysia and Singapore) were tending to be cautious with regard to allowing inward migration in the face of sluggish economic growth and lower demand for construction and other services. Initially, 12,000 Bangladeshi workers were retrenched in Malaysia, and the Maldives halted hiring Bangladeshi workers. Sudan's decision to retrench 20,000 Bangladeshi workers also contributed to Bangladesh's woes. Realising the potential negative impact of such measures on the economy, GoB decided to conclude bilateral negotiations with some of these countries. Fortunately, countries such as Saudi Arabia and Malaysia have committed to not retrenching Bangladeshi workers and have allowed these workers to change jobs, or stay on even when they lose their jobs. With economic recovery, some of the traditional destination countries have indicated that imports of workers could rise again in the near future. In view of recent negotiations, the UAE is once again considering hiring workers from Bangladesh.[18] A recent initiative to send workers to Iraq may also contribute positively in this respect, although security concerns remain.

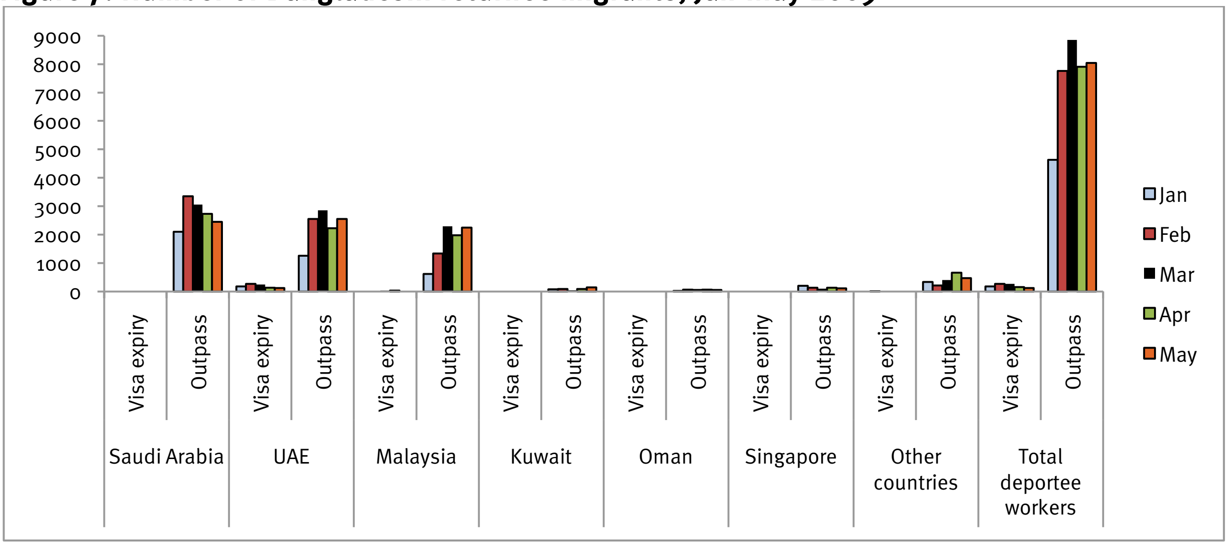
The recent debt default by Dubai has sent shockwaves through financial markets. The governments of Dubai and Abu Dhabi have already given assurance that they will provide financial support to cover

18 During November 2009, the Prime Minister visited the UAE, where this commitment was made by the latter government.

working capital and interest expenses: Abu Dhabi has already provided $10 billion as an initial support measure. It remains to be seen how Dubai can manage and overcome the crisis, and whether or not manpower exports from Bangladesh are affected.

The issue of returnee workers from abroad during the past 10 months has drawn significant attention from various quarters in Bangladesh. After the crisis started in mid-2008, Bangladesh's major manpower importing partners, including Saudi Arabia, Kuwait, UAE, Malaysia and Singapore, resorted to various retrenchment measures, and in some instances imposed restrictions on issuance of new work visas. Malaysia initially announced cancellation of 55,000 new visas for Bangladeshi workers although it withdrew this order after successful negotiations at higher levels with GoB (see above). According to Rahman et al. (2009b), as many as 38,208 Bangladeshi workers returned from overseas during January-May 2009. Out of these, about 97% returned because of retrenchment and the rest because their visas had expired (Figure 7). Most of the retrenched workers were from the two major destination countries (about 36% from Saudi Arabia and 31% from the UAE). However, in the absence of historical data on returnee workers, no comparison is possible to separate out any usual returns.

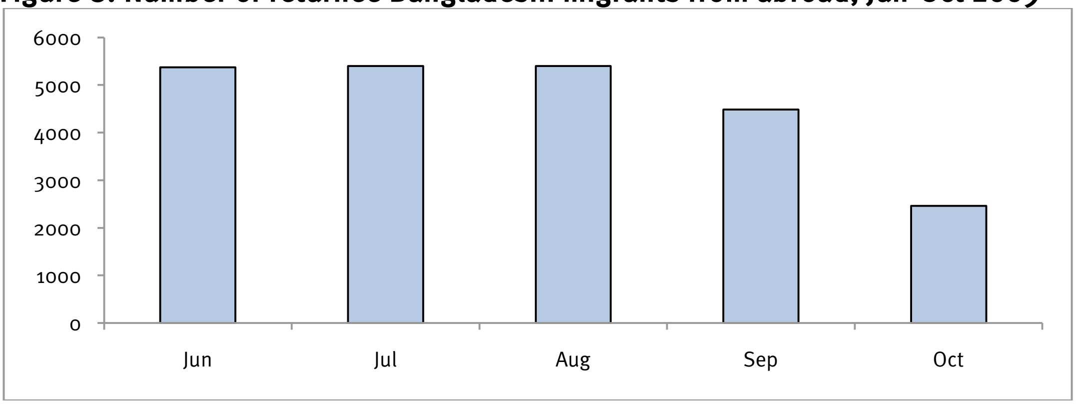
Figure 7: Number of Bangladeshi returnee migrants, Jan-May 2009



Source: Rahman et al. (2009b).

Latest data from the Bureau of Manpower, Employment and Training (BMET) suggest that, during the period June-October 2009, the number of Bangladeshi returnee workers declined to 23,000 (Figure 8). This is perhaps an indication of recovery in international job markets, particularly in the Middle East region. The rise of oil prices in international markets has played a positive role in this context. However, this information should be interpreted carefully, as one would expect normal (not crisis-related) return as well: as there are no reliable data on returnee migrants it is difficult to identify those returning as a result of the crisis as against 'normal' returnees.

Figure 8: Number of returnee Bangladeshi migrants from abroad, Jun-Oct 2009



Source: Data from BMET (2009).

Bangladeshi workers returning home since the beginning of the crisis belong to two groups: 1) those who had worked overseas for more than a year and 2) those who had stayed overseas for less than a year and had to return as a result of the crisis. Findings from Rahman et al. (2009b), based on FGDs with returnee migrants, reveal that the first group somehow managed to recover part of the cost incurred for visas and other expenses. The situation was different for those belonging to the second group who, in some instances, were unable to stay even for a month. These workers were found not only to have incurred serious financial losses as a result of their early return but also to be heavily indebted on account of the substantial loans that they had had to take in order to pay for travel and sponsorships, often at high interest rates. Some of these workers are currently unemployed; others are either working as day labourers or operating small businesses.

Rahman et al. (2009b) further report that returnee migrant workers identified a number of problems that they faced when going aboard. These related to excessively high payments for visa processing, harassment by local recruiting agencies and their commission agents after their return, misinformation/false information with regard to the availability and nature of jobs abroad and harassment by outsourcing agencies working in importing countries. Because of the higher expenditures involved for a typical Bangladeshi worker (by more than three times) vis-à-vis those of neighbouring countries (e.g. India and Nepal), length of stay abroad, level of wages, timely payment of wages and opportunity for overtime were relatively more important factors for Bangladeshi workers. Rahman et al. (2009b) note that, according to these returnee migrants, withdrawal of the sponsorship system and allowing workers to work for different employers than just the one recruiting them in the first place could help workers stay abroad, bide their time during recession and recoup the money spent in going abroad. Returnees also complain that many of the Bangladeshi diplomatic missions located in the Middle East and Southeast Asia have not been adequately responsive to the needs of migrant workers. GoB needs to adopt a stricter monitoring mechanism to ensure that government institutions carry out their service mandate to non-resident Bangladeshis in an appropriate manner, particularly during times of financial crisis and economic turmoil. While some of these points noted here are general phenomena, indications are that they have become more frequent during the crisis.

2.3 Import performance

In recent years, imports by Bangladesh have tended to experience quite robust growth. Particularly during 2007/08, import payments marked a 25.7% growth, mainly because of the then high global commodity prices (Table 7). However, import of capital machineries decelerated by 14.3% in this period, owing to a slackening of investment demand in the country.

Table 7: Import payment growth (value) in Bangladesh, 2000/01-2009/10 (%)

	Growth
2000/03 (average)	10.2
2004/07 (average)	20.5
2007/08	25.7
2008/09	4.8
2009/10 (Jul-Sep)	-19.0

Source: Calculated from BB (2009b).

During the first two quarters of 2008/09, total import payments posted 37.7% and 11.8% growth, respectively, compared with the corresponding periods of the preceding fiscal year (Table 8). But, to a significant extent, this significant growth was accounted for by high growth in imports of crude and refined petroleum products and fertiliser. A sharp fall in the prices of these items in the international market during the later parts of the year resulted in a gradual slowdown in import payment growth. During the third and fourth quarters, import payments declined by 4.4% and 16.6%, respectively. At the end of the last fiscal year (2008/09), growth of aggregate import payments came down to 4.8%, compared with 25.8% in 2007/08. With the deepening of the economic crisis, the manufacturing sector, particularly export-oriented industries, was adversely affected (which is reflected by the downward import trend of textile and articles thereof).

Table 8: Recent import growth (value) of major commodities in Bangladesh, 2007/08-2009/10Q1 (%)

	2007/08	2008/09	2008/09 Q1 (Jul-Sep 2008)	2008/09 Q2 (Oct-Dec 2008)	2008/09 Q3 (Jan-Mar 2009)	2008/09 Q4 (Apr-Jun 2009)	2009/10 Q1 (Jul-Sep 2009)
Food grain	141.4	-37.4	-44.6	-29.0	-44.2	-23.4	-23.8
Milk and dairy products	64.9	-30.2	-31.6	-28.9	-42.4	-6.9	-34.2
Edible oil	71.7	-13.8	8.2	-11.4	-8.1	-39.9	19.3
Textile and articles thereof (RMG inputs)	-0.6	11.2	11.3	18.0	12.7	3.8	-11.7
Iron and steel	18.9	27.7	38.8	18.8	50.0	9.2	-14.8
Capital goods	-14.3	-13.6	-10.8	-8.2	-13.0	-22.3	-4.1
Others	29.0	10.0	60.7	20.7	-3.5	-19.3	-23.5
Total imports	25.8	4.8	37.7	11.8	-4.4	-16.6	-19.0

Source: Calculated from BB (2009a).

During the first quarter of 2009/10, aggregate import payments declined by 19.0%. Imports of capital machineries are yet to recover from the earlier shock posed by falling global demand and bottlenecks in domestic investment. Imports of textiles and articles thereof decelerated by 4.9%: this category relates to fabrics for RMG production; perhaps the negative growth indicates lower orders being placed during the crisis period. However, lower import payments have kept the balance of payments situation at a comfortable level. Combined with record remittance flows, this has helped Bangladesh to accumulate a record high level of foreign exchange reserves.[19] With global commodity prices rising, import payments are projected to rise in the near future.[20] During the first two months of 2009/10, opening of import L/Cs registered 3.3% growth, indicating a revival in import demand. The growth in L/C opening of capital machineries has brought some promise, registering 8.7% growth in the abovementioned period. However, unless investment and export trends recover, imports are likely to register lower growth.

2.4 Revenue earnings

The global financial crisis has had concomitant implications for domestic resource mobilisation in Bangladesh, in a number of ways. First, Bangladesh's revenue is highly dependent on import duties.[21] With the onslaught of the financial crisis and the consequent decline in global demand, global commodity prices have experienced a significant fall. Combined with the depressed investment situation and lower domestic import demand (both in value terms and, in many instances, in volume terms), revenue from import-related duties has emerged as the major fiscal transmission channel of the global financial crisis. Second, deceleration in economic activities, particularly in export-oriented industries, has meant lower scope for direct tax collection at that level. Third, apprehension regarding a slowdown in foreign resource flows has highlighted the need to generate additional resources at domestic levels to finance the developmental budget. Finally, the need for higher public expenditure to service the stimulus package and public investment in social safety nets has underlined the need for higher revenue collection to maintain the fiscal balance. The need for countercyclical measures was a reality, but GoB attempted also to go for greater resource generation at domestic levels to reduce the expected higher deficit.

19 On 10 November 2009, foreign exchange reserves crossed the $10 billion mark for the first time in the country's history.

20 The oil price (per barrel) has been hovering around the $80 mark in recent times.

21 Import-related duties account for 29.2% of total domestic revenue in the budget for 2009/10.

Revenues at the import stage mostly suffered from lower collection of import duties in 2008/09. Against a target of Tk10,862 crore ($1551.7 million), Tk9351.9 crore worth ($1336.0 million) of import duties was collected. This implies a shortfall of Tk1501 crore ($215.7 million), posting a negative growth of -2.6% over the matching figure of 2007/08 (Table 9). The budget aimed for 13.1% higher import duty collection in 2008/09 over 2007/08, mostly from the anticipated global price recovery. Compared with import duties, revenues from VAT (import) suffered less from falling prices; a growth of 8.2% was recorded, although this also was lower than the target of 12.6%. VAT (import) collection missed its target by Tk375.1 crore ($53.6 million). On the other hand, supplementary duty (import) posted relatively high growth of 32.9%, surpassing its target by Tk219.4 crore ($31.3 million).[22]

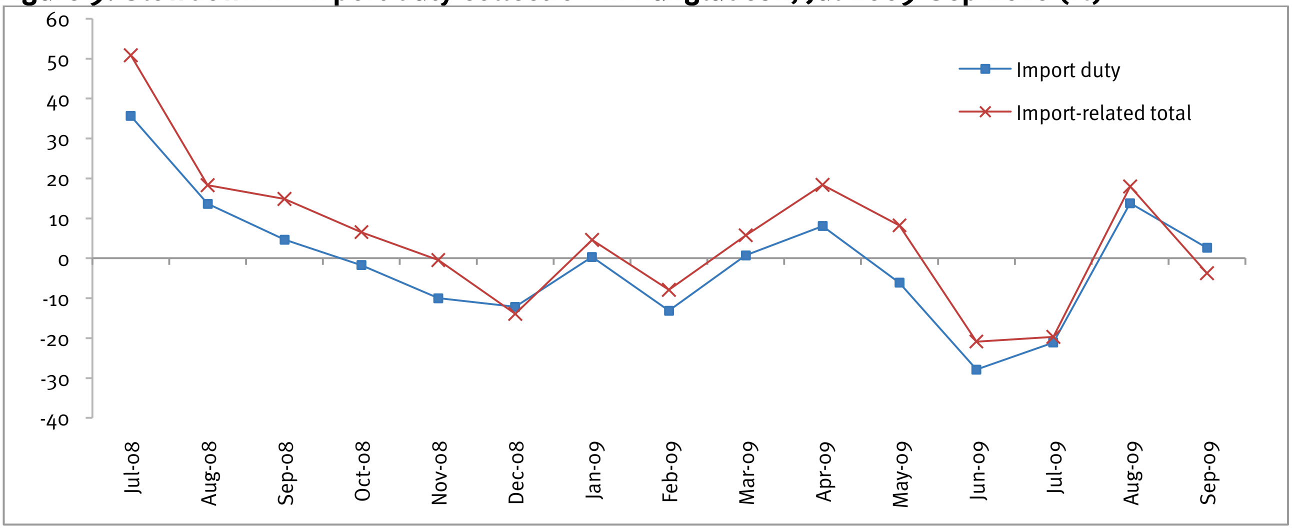
Table 9: Import-related revenue collection in Bangladesh, 2008 and 2009 (%)

	Actual growth 2007/08	Target growth 2008/09	Actual growth 2008/09
Import total	26.7	13.5	5.2
Import duty	17.7	13.1	-2.6
VAT import	34.5	12.6	8.2
Supplementary import	46.6	20.4	32.9

Source: Calculated from NBR (2009a).

Revenue mobilisation from import sources has been on the slide for some time now (Figure 9). During July-September of 2009 (2009/10), revenue earnings of the government from import-related duties declined (-2.7%) compared with the corresponding period of 20008 (2008/09). VAT (import) recorded -8.7% growth, and import duties also decreased (-2.3%). Supplementary duty achieved impressive 20.3% growth, which somewhat offset the decline of income from other sources. This owed to the proposed new duty structure announced in the budget for 2009/10.[23]

Figure 9: Slowdown in import duty collection in Bangladesh, Jul 2009-Sep 2010 (%)



Source: NBR (2009b).

The depressed global economic situation has led to lower domestic investment, eventually leading to lower than projected GDP growth in 2008/09; against targeted growth of 6.5%, 5.9% growth was achieved. Bhattacharya et al. (2009) indicate that domestic revenue mobilisation in Bangladesh is dependent to a significant extent on changes in the level of per capita income. The adverse impact on income growth affected domestic resource mobilisation negatively.

22 Supplementary duty is additional to customs duty and VAT, imposed at local and import stages under the VAT Act 1991. The tax base for VAT stands as follows. For import stage, customs assessable value + customs duty + supplementary duty. For domestic/local stage, 1) goods (manufacturing): [production cost + profit and commission (if any) + supplementary duty (if any)]; 2) services: [total receipts excluding VAT but including supplementary duty (if any)].

23 The details of the new duty structure are discussed in Section 3.

The global financial crisis has once again reinforced the need for greater emphasis on direct taxes as a source of domestic revenue mobilisation in Bangladesh. As of now, direct taxes account for only 21% of total revenue earnings (2008/09). At the same time, the crisis has also exposed the long-standing structural weaknesses of revenue mobilisation in Bangladesh. It is necessary now for the government not only to widen and deepen the domestic tax base, but also to reemphasise the need for institution-strengthening initiatives to ensure higher and more effective revenue effort.

2.5 Official development assistance

The role of ODA has been on the decline over the past decade. However, ODA still finances about one-third of the total fiscal deficit of Bangladesh (the projected share of net foreign financing in the budget for 2009/10 is 29.7%). In 2008/09, a total amount of $1726.9 million in aid was disbursed. This was approximately $335 million (15%) less than the amount disbursed over the previous fiscal year. Net receipts of foreign aid during 2008/09 decreased to $1085.91 million, against $1475.52 million in 2007/08 (-25.7%). The figures for July-August 2009/10 are also on the downside, indicating a decline (-90.3%) in net foreign aid disbursement in Bangladesh, with gross disbursement falling substantially from $315.2 million in 2008/09 (July-August) to $22.3 million in 2009/10 (July-August). Since most of the aid is project oriented, flows are often dictated by project cycles. Thus, aid tends to be volatile across months, and this declining trend should be looked at with some caution.

There was an expectation in Bangladesh that earlier aid commitments would hold and, at the same time, that new pledges in view of the growing needs in crisis-driven developing economies would also be made available. Indeed, a number of global initiatives were put in place in view of the crisis. However, Bangladesh is yet to receive any significant aid to address the consequences of the crisis. An exception has been the Special Drawing Rights (SDR) allocation by the IMF. On 1 September 2009, Bangladesh received $735 million from the G-20-supported general allocation (total equivalent to $250 billion to boost global liquidity) from the IMF, which has been made available to all 186 IMF members. This fund has helped Bangladesh boost its foreign exchange reserves. However, it is pertinent to mention here that the balance of payments situation of Bangladesh was quite comfortable even before this disbursement; during July-August 2009 the current account surplus was $1304 million.

On the other hand, enhanced aid commitments are evident. Two separate deals with the Asian Development Bank (ADB) are expected to provide $745 million as budgetary support credit and $130 million as soft loans to help improve public and environmental health services in large cities. The ADB earlier announced that it was going to increase its annual assistance package to Bangladesh by 33%, to $800 million annually during 2009/11. The ADB is also considering GoB's request for $500 million in aid from its special fund to tackle the adverse impacts of the global financial crisis. The ADB may also provide a further $76 million to help support small and medium-sized enterprises (SMEs). Meanwhile, the World Bank has recently approved $130 million-worth of credit to increase the country's access to electricity through installation of affordable solar home systems in rural areas, and has also decided to increase aid to Bangladesh by 20%, to $1.0 billion per annum over the next three years. The overall commitment of the World Bank is estimated to be $1096.9 million. The government is also negotiating $4.7 billion of assistance in the form of project aid with the Chinese government, which is expected to be realised over the next few years if an agreement is reached. However, the recent dispute with the World Bank and ADB regarding the Public Procurement Regulations (PPR) has generated doubts with regard to the availability of such loans.

It is to be noted that the major share of aid flows to Bangladesh comes as project aid to finance various development projects under the country's Annual Development Programme (ADP). As a result, aid disbursement is related directly to the implementation status of ADP projects. Actual disbursement will depend more on Bangladesh's capacity to absorb the aid rather than on the availability of aid itself. During the first three months of 2009/10, only 9% of project aid allocations had been utilised, which is in tune with historical trends. Slow implementation of donor-funded ADP projects in the current fiscal year has yet again resulted in lower aid disbursement thus far this year. In view of the need to generate more local demand through enhanced economic activities, it is important that both quality and quantity of aid disbursement and ADP implementation be significantly improved. In order to tackle the potential deceleration in GDP growth as a consequence of the global economic contraction, GoB ought to consider foreign financing as an important source, given its non-inflationary nature, and also, more crucially, to minimise the 'crowding-out' effect of borrowing from domestic sources.

2.6 Foreign direct investment and portfolio investment

FDI inflow to Bangladesh is typically concentrated in a few sectors (e.g. telecommunications, banking, power, gas and petroleum, textiles and wearing apparel). Table 10 provides some background information on sources of FDI inflow to Bangladesh and its sectoral composition.

Table 10: FDI in Bangladesh, 2005-2008 (US$ millions)

Year	2005	2006	2007	2008
Total FDI inflows	845.3	792.5	666.4	1086.3
Sector				
Telecommunications	278.8	346.5	201.9	641.4
Banking	117.8	117.7	80.0	141.8
Gas and petroleum	181.1	187.1	190.2	73.3
Textiles and wearing apparel	96.5	70.1	102.4	126.4
Power	27.2	21.1	25.8	27.8
Other	143.9	50.0	66.2	75.8
Source				
Egypt	48.4	105.4	75.2	373.4
UK	152.8	70.5	142.6	130.6
UAE	55.5	88.0	83.3	102.2
Switzerland	2.3	2.8	13.4	69.3
Singapore	97.5	35.9	10.7	32.3
US	141.8	175.7	120.4	40.9
South Korea	29.9	53.9	27.7	44.6
Hong Kong China	53.1	47.4	55.5	39.9
Netherlands	15.4	13.0	18.7	31.7
Pakistan	25.5	5.1	3.5	12.5
Other	223.2	194.8	115.7	209.0

Source: BB (2009d).

Net FDI flows to Bangladesh increased, albeit marginally, to $941 million in 2008/09 (Table 11). However, it needs to be kept in mind that FDI in Bangladesh has always been rather low compared with in its South Asian neighbours, accounting for only about 4.4% of total investment.

Net FDI inflows of $126 million during the first two months of 2009/10 were considerably lower (by 37.3%) than in the corresponding period of the previous fiscal year. However, lower inflows of FDI during recent months are perceived to be the result of a recent power crisis and infrastructural constraints rather than a reflection of a lack of availability of sources.

Table 11: FDI and PFI in Bangladesh, 2007/08-2009/10 (US$ millions)

	2007/08	2008/09	2008/09 Jul-Aug	2009/10 Jul-Aug
Net FDI	748	941	201	126
Net PFI	47	-159	8	-25

Source: BB (2009b).

As major stock indices around the world reeled from the impact of the global financial crisis, foreign investors began to withdraw their PFI from Bangladesh's stock market. In 2008/09, $159 million-worth of PFI was withdrawn, almost equivalent to the total amount of PFI inflow ($154 million) to Bangladesh in 2006/07 and 2007/08 combined.[24] It appears that, in the short term, the negative impacts of the financial and economic crises on foreign investments will continue (CPD, 2009).

2.7 Labour market

The prolonged recession and the consequent economic downturn have resulted in considerable adverse implications for the employment and labour markets of most economies. In view of the global financial crisis, Rahman et al. (2009b) estimate the employment situation of Bangladesh and its implications on the domestic job market.[25] The resilience of Bangladesh's economy during 2008/09 contributed towards containing the adverse impacts on Bangladesh's employment situation. Relatively high growth of the agriculture sector had a positive impact from the labour absorption perspective. Growth of employment opportunities in the industrial sector is expected to slow down; only 0.4 million job opportunities are expected to be created in 2008/09. Moreover, weakening manpower exports would mean an increase in the domestic labour supply by an additional 0.8 million over the 2008/10 period. Considering these factors, the unemployment rate was estimated to be about 3.6% in 2008/09 (Table 12).[26] However, with a possible downward revision of GDP growth, the composition of the labour force in different sectors and the rate of unemployment may need to be reviewed further.

Table 12: Employment and labour market of Bangladesh, 2005/06-2009/10 (proj.) (millions)

	2005/06	2007/08 (est.)	2008/09 (est.)	2009/10 (proj.)
Agriculture	22.8	24.1	25.0	25.6
Industry	6.9	7.6	7.9	8.3
Service	17.7	19.5	20.4	21.3
Total employment	47.4	51.2	53.3	55.2
Labour force	49.5	53.1	55.2	57.3
Unemployment rate (%)	4.3	3.6	3.6	3.7

Source: Rahman et al. (2009b).

The GDP growth target for 2009/10 has been set at 5.5%. If the economy does not experience much restructuring and change, total employment is expected to be 55.2 million in 2009/10; 25.6 million in the agriculture sector and 21.3 million in services. Additional employment in industry is projected to be lower: 0.4 million additional workers are expected to be employed in 2009/10. According to the projection, the unemployment rate will marginally increase to 3.7% in 2009/10. However, since agriculture in Bangladesh is characterised by a higher level of underemployment (i.e. lower working hours), the real employment situation of the economy may be worse than what the figures in Table 12 would suggest.[27] The concern here is that a large part of this newly absorbed labour force in this sector would work at less than the optimum level, which would increase underemployment in agriculture. The declining trend in underemployment visible since 2002 would possibly slow down in 2009/10.[28] This indicates that global recession may not impose rapid job cuts, as experienced by many developed countries, but would entail adverse implications for labour market composition in Bangladesh.

FGDs with entrepreneurs from various export-oriented industries (Rahman et al., 2009b) suggest that a large number of entrepreneurs have taken various cost-cutting measures in view of the adverse impact

24 Stock markets of Bangladesh being largely isolated from the global economy (only about 2% of the market capital is sourced from foreign capital), the global crisis has had little, if not zero, effect on capital market developments.

25 It is important to note here that the study mentioned a number of underlying assumptions in carrying out the estimation. First, the projection assumes that the relationship between employment and output remains consistent over the medium term. Second, structural changes within industries are adjusted for broad sectors in the medium term. Finally, it is assumed that no change in production technology takes place during the period under consideration.

26 This is a low figure by any standard. However, there is a great deal of debate in Bangladesh with regard to the definition of unemployment. If underemployment is included, the figure would be much higher, at 28.7%.

27 The average weekly working hours (according to BBS, 2008) in modern sectors varies between 50 and 60 hours, whereas in agriculture it varies between 37 and 54 hours.

28 Underemployment in 2005-2006 decreased to 24.5%, from 37.6% in 2002-2003 (BBS, 2008).

of the crisis (Table 13). Although retrenchment of workers was not evident from the information provided, a number of entrepreneurs mentioned adopting such cost-cutting measures as increasing working hours, reduction of fringe benefits, reduction of firm's capacity utilisation or even shutting down of some production units. Entrepreneurs with multiple units shut down some of them when order volumes were not forthcoming. Over the past several years, in view of high growth rates, many apparels entrepreneurs have gone for considerable capacity building and expansion. This excess capacity has remained idle, with consequent adverse effects on current employment and potential recruitment. A large segment of sample entrepreneurs indicated that, if demand for their outputs reduces further, they may have to intensify cost/labour reduction measures. Thus, the demand slump could have further adverse consequences for the labour market. Moreover, in industries that pay workers according to production,[29] lower export demand may not necessarily result in a job cut or reduction of wages, but still can reduce the take-home pay of a worker.[30]

Table 13: Various adjustment measures considered by sample Bangladeshi entrepreneurs in view of crisis (% of respondents)

	Measures taken because of the crisis	If recession deepens, possible measures to be taken
Laying off workers	8.3	11.1
Wage cut	0.0	3.7
Increasing working hours	4.2	6.5
Reduction of workers' fringe benefits	5.6	10.2
Reducing profit margin	29.2	25.0
Reducing firm's capacity utilisation	5.6	12.0
Closing down of production units	5.6	11.1
None	41.7	20.4

Source: Rahman et al. (2009b).

The available evidence does not allude to the large number of RMG factories being shut down as a result of the crisis. FGDs with garments owners revealed that, among 4939 RMG factories, 270 were listed as 'sick' prior to the global recession and 100 garment factories were put at risk as a result of the adverse impacts of the global recession. However, it was also mentioned that 149 RMG factories entered the industry during this period. As growth in the RMG sector is volume driven, the overwhelming majority of the 2 million workers in this sector have, thus far, been spared the worst consequences of the crisis. However, with apparels exports slowing down considerably in recent months, this could have knock-on effects on employment and also on labour absorption capacity in the RMG sector, and could perhaps result in retrenchment in some cases. The Bangladesh Garments Manufacturers and Exporters Association (BGMEA) has recently claimed that at least 25-30,000 workers have faced job losses over the past eight months. Factory owners reported during FGDs that fresh recruitment of workers has slowed down significantly since mid-2008. There is demand for skilled labour, but willingness to recruit new workers and provide them with on-the-job training has suffered.

On the other hand, workers expressed willingness to work at a reduced wage rate for a temporary period rather than face retrenchment. Many employers also seemed to be considering the option of providing a low wage instead of retrenchment. However, evidence suggests that this may be difficult to implement at factory level, and a FGD with worker leaders did not indicate that wages had been lowered. Layoffs have not been uncommon and a lack of appropriate exit regulations has complicated matters.[31] It is evident that, in many cases, reduced overtime, underutilisation of production capacity and reduction of working hours, especially in textiles, jute and frozen food industries, have led to a lower take-home salary. Occasional labour unrests have also been reported as a result of reduced operations although, to date, most factories have managed to address the emerging difficulties.

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29 Piece rate is more prevalent in the sweater subsector of the knitwear industries.

30 For example, the sweater-making factories set the wage of a worker according to pieces manufactured.

31 For example, Bangladesh does not have a bankruptcy law.

2.8 Poverty situation

There is a general acceptance that the crisis has had an adverse impact on the global poverty scenario. According to Chen and Ravallion (2009), the financial collapse, combined with the food and fuel crises, was likely to drive an additional 53-64 million people below the poverty line in 2009,[32] although they admit that 'the estimates for any individual country could be widely off the mark in some cases'.

Bangladesh has achieved remarkable progress in reducing poverty in the recent past: the proportion of people below the poverty line decreased by one percentage point in the 1990s and almost two between 2000 and 2005, down to around 40%. Since no Household Income and Expenditure Survey (HIES) has been conducted in Bangladesh since 2005, it is difficult to produce reliable estimates about current poverty levels or the impact of the crisis on the poverty situation in the country. It would be safe to argue that poverty continued to decline between 2005 and 2007, in keeping with past trends, with a reversal of the trend in 2008 because of the subsequent commodity price hike, particularly of rice. According to World Bank estimates, the proportion of people living below the poverty line, expected to drop from 40% to 32% between 2005 and 2008, was likely to be about 38% (World Bank, 2008). Other estimates put the figure at much higher levels (Rahman et al., 2008). However, this refers to the pre-crisis period. The World Bank (2009a) predicts that, as a result of the global financial crisis, 2.4 million people in Bangladesh will be unable to cross the poverty threshold at the end of 2009/10. A lower number of people going abroad as migrant workers and a slowdown of growth in export-oriented sectors were said to be likely to have adverse implications for poverty reduction in Bangladesh in 2009.

In 2008/09, the national output of Bangladesh increased by 5.9%, while final consumption expenditure by households (in real terms) recorded a 6.0% growth over the previous fiscal year. Agriculture attained an impressive 4.6% growth during this period. With the majority of the population making their livelihood from agriculture, poverty impacts during the crisis period could thus be limited. Hopes of better agricultural production in 2009/10, if realised, would also provide some shield for the majority of the poor in terms of food security. The fall in commodity prices in the domestic market, influenced by the crisis-induced price slide in global commodity markets, has also been of benefit with regard to the real incomes of the poor. With continuing robust remittance inflows, households dependent on such finances have not been hard done by the crisis as yet. At the same time, absence of any evidence of large-scale labour retrenchment from the industrial sector also indicates limited impact of the crisis on the poverty situation. In view of the crisis, the growth projection for 2009/10 has been set at 5.5% (lower than the 6.2% and 5.9% in 2007/08 and 2008/09, respectively).

However, the slowdown in economic growth, declining exports and sluggish investment in recent times could lead to a reduced pace of poverty reduction in 2010. The slowdown indicates lower opportunities for new job creation and fewer opportunities for overtime work. All of these have bearings on the poverty reduction performance of Bangladesh. With the rise in global commodity prices, particularly of food prices in the global market, much will depend on Bangladesh's ability to increase domestic food grains production from the perspective of poverty reduction.

32 Based on estimates of people living on less than $2 a day and $1.25 a day, respectively.

3. The global financial crisis and Bangladesh's policy stance

As a quick response to the global crisis, in September 2008 the BB set up a Forex Investment Committee to monitor forex reserves held abroad. The BB withdrew about 90% of its total investment from international banks that were perceived to be at risk. It also advised the commercial banks of the country to be watchful about such investments. At the initial stage, this quick move helped avert the adverse impacts of the global financial crisis on the country's foreign exchange reserves. As the global crisis spread, GoB came up with various direct and indirect policy support measures aimed at safeguarding domestic industries, sustaining exports and protecting the poor and the marginalised segments of society. These policy measures to mitigate the adverse consequences of the crisis consisted of 1) direct policy support and 2) macroeconomic policy stances for economy-wide positive effects.

3.1 Direct support measures

3.1.1 The first stimulus package

In order to address the adverse affects of the global financial crisis, GoB declared a stimulus package of Tk3420 crore ($488.6 million) in April 2009. The fund, meant to be used over the last quarter of 2008/09, allocated an additional Tk450 crore ($6.4 million) in cash subsidies (a total of Tk1500 crore or $21.4 million) for export industries most affected by the crisis.[33] Of the rest, Tk1500 crore ($21.4 million) was allocated for agriculture, Tk600 crore ($8.6 million) for the power sector, Tk500 crore ($7.1 million) for recapitalisation of agriculture loans and Tk374 crore ($5.3 million) for social safety net programmes. The first stimulus package also put more money into the SME Fund, whose capital was raised from Tk500 crore ($71.4 million) to Tk600 crore ($85.7 million) (MoF, 2009a).

According to the package, cash incentives (based on actual export value) for jute and jute products were set to rise to 10%, from the previous rate of 7.5%, leather and leather goods to 17.5% from 15% and frozen foods and other fish exports to 12.5% from 10%. This was in line with the fact that exports of primary products suffered the most from the global crisis. Procedures for disbursement of funds were also simplified. Presumptive payment of 70% of the claim was proposed to be made available immediately, with the settlement of the rest of the claim to be paid after subsequent audit scrutiny.

Available information shows that, as of September 2009, Tk995 crore ($14.2 million) in cash incentives has been disbursed, in two instalments. An amount of Tk245 crore ($35.0 million) was paid out in the first instalment, with the remaining Tk750 crore ($107.1 million) disbursed in the second phase. The increased cash subsidies could not deter the decline in exports in the sectors in question, but were perhaps helpful in reducing their difficulties at a time of falling demand and falling prices with consequent implications for profitability.

GoB's response came in for some criticism, since RMG exporters complained that they were left out from the benefits of the stimulus package. The apparently contradictory picture of volume-driven good apparels performance and falling profit margins gave rise to some tension between the government (which was comforted by good overall export earnings) and businesses, mainly the dominant apparels entrepreneurs (who were complaining about increasing competitive pressure). Complaints about government complacence gathered strength in September 2009, when exports of apparels experienced

33 Cash incentives for 13 export sectors (jute goods; leather and leather products; shrimp and other fish products; local fabrics; products made of *hoogla*, straw, coir or sugar cane; agriculture and agricultural processed products including vegetables and fruits; potatoes; bicycles; crushed bone; hatching eggs and day old chicks; light engineering products; liquid glucose (only for economic processing zone (EPZ)); halal meat) were already in place for 2008/09. Three sectors (jute goods, leather products and frozen shrimp and other fishes) were selected for additional allocation in the stimulus package against their exports during April 2009 to June 2009.

a 27% dip compared with the corresponding month of the previous year. The stimulus package announced in October 2009 was thus more of a reactive one.

3.1.2 The second stimulus package

Provision of Tk5000 crore ($714.3 million) was made in the budget for 2009/10 as part of a second stimulus package. While details on the new package were not unveiled, it was announced that it would help service the incentives and policies set forth in the first package. Not much information is available on the implementation status of the second package. However, according to recent newspaper reports, the package contains an allocation of Tk3046 crore ($435.1 million) as cash subsidies to affected exporters, out of which Tk1311 crore ($187.3 million) has already been released.

3.1.3 The third stimulus package

The government has recently announced a third stimulus package, focusing mostly on the apparels sector. The following provisions are included:

1. Renewal fee (1 November 2009 to 30 June 2009) for captive generators to be used in the apparels sector will be paid out.
2. Rescheduling of overdue loans in the apparels sector without down payment will be extended from 31 October 2009 to 30 June 2010. The rate of interest will be reduced from 13% to 10%.
3. Payments time for loans defaulted on during the extension period will be increased on the basis of the bank–customer relationship at the prevailing market interest rate.
4. Cash incentives (based on actual export value) at the rate of 5% for exporters to new markets (markets other than the US, Canada and the EU) will be provided in the first year, 4% in the second year and 2% in the third year. The Bangladesh Textile Mills Association (BTMA) will receive this particular benefit for any markets for export of yarn.
5. Providing forward exchange booking facilities to home textiles for foreign exchange transactions in foreign currencies other than the US dollar.
6. SMEs in the apparels sector that export up to $3.5 million in 2009/10 may be considered for 'special incentives'. Bangladesh Knitwear Manufacturers & Exporters Association (BKMEA) and BGMEA are to provide details (name, owner and actual exports) of such industries to the committee. BKMEA has submitted its information; BGMEA is yet to do so. The following recommendations have been accepted by the committee:
    a. If actual exports in 2009/10 are higher than in 2008/09, a 5% cash incentive will be provided on the additional value of exports.[34]
    b. SMEs that do not own captive generators or diesel-run generators will receive a subsidy of 10% on their electricity usage until 30 June 2010.
    c. Only those industries that have not rescheduled their loans will be eligible for the abovementioned incentives.
    d. It must be ensured that no SMEs are under the ownership of any larger industries.
    e. The government will decide on cash incentives after it receives the accurate information.
7. The L/C advising charge, L/C amendment and transfer fees will be reduced to Tk750 ($10.7) from Tk1000 ($14.3). Commission on L/C opening will be reduced from 0.60% to 0.50% (three months). The L/C confirmation fee will be decreased to 0.20% from 0.25%. A ceiling of 0.15% is to be imposed on commission on import negotiation and collection (BB, 2009c).
8. The limit of the Export Development Fund (EDF) will be raised from $1.5 million to $10 million by combining the resources of three commercial banks; the interest rate to be charged will be LIBOR + 2.5%.
9. BTMA members will be eligible for EDF loans from their respective banks at LIBOR + 2.5% on the import value of raw materials for yarn production (cotton and other fibres). This facility will be provided on the value of yarn imported in previous years (maximum one year) or $10 million (whichever is less).

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34 However, the related business associations (BGMEA and BKMEA) demanded a revision of this provision and requested that the government relax the conditionalities. Indeed, the original suggestion from the Working Group was to provide a cash incentive of 5% on up to 10% additional exports (over 2008/09) by small and medium-sized RMG units.

10. GoB will provide Tk300 crore ($42.9 million) as seed money to create a Contributory Fund with the objective of tackling the adverse effects of the global financial crisis on the exports of textile and apparels. Textile and apparels industry owners will contribute 0.1% of their export value (fob) from January 2010 to June 2010 and 0.2% of export value from July 2010.
11. The contract for the National Institute of Textile Training, Research and Design (NITRAD) has been modified: a) The government will bear all expenses for the first year; b) the government will contribute 60% of the expenses incurred in the second year; c) for the next three years 50% of expenses will be borne by the government; and d) BTMA will take over the responsibilities of NITRAD from the sixth year onwards.

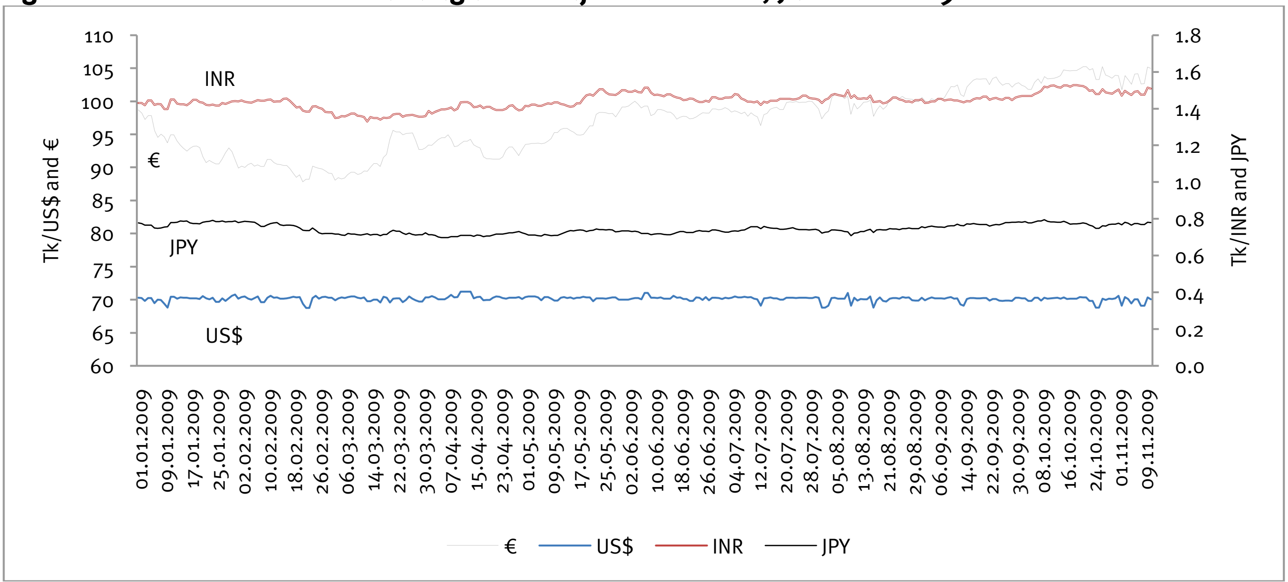
The third stimulus package also includes some benefits for the shipbuilding and crust leather industries: a 5% cash incentive to promote exports to each industry.

3.2 Indirect measures: Macroeconomic policy stances

3.2.1 Exchange rate management

Over the recent past, Bangladesh has pursued a policy of keeping the exchange rate stable vis-à-vis the US dollar, even during the crisis period. The BB has periodically been purchasing (and selling) US dollars from the open market to keep the Tk-US$ exchange rate stable.[35] However, the weakening US dollar against major currencies such as the euro, the Japanese yen and the Indian rupee throughout 2009, with the taka remaining stable against the dollar, has implied some depreciation of the taka against those currencies. Between 1 January and 11 November 2009, the taka depreciated by 6.3% against the euro, 5.4% against rupee and 0.2% against the yen, and appreciated only marginally against the US dollar, by 0.3% (Figure 10).[36]

Figure 10: Movement of the taka against major currencies, Jan-Nov 2009



Source: www.oanda.com.

35 They have been successful – the Tk-US$ exchange rate has remained about the same, at 68.8 over the past two years.

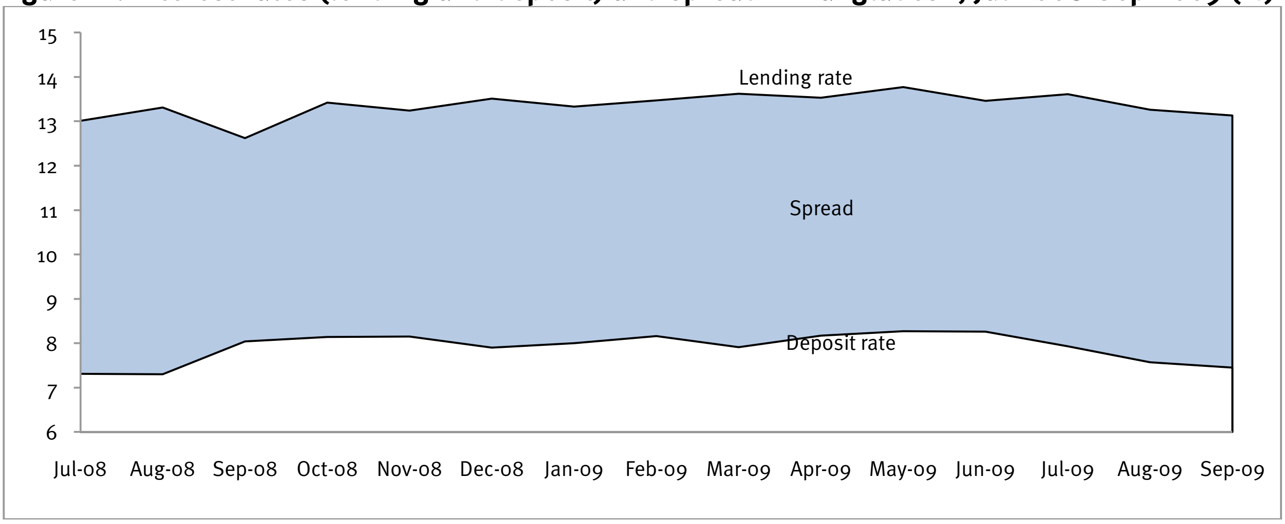
36 China, the major competitor of Bangladesh in EU and US markets (particularly for RMG), kept its currency pegged against the US dollar. Consequently, the yuan depreciated by 6.2% against the euro. Sri Lanka also announced 'exchange rate support' in its stimulus package.

In the early months of 2009 (January-March), Bangladeshi exporters to the EU suffered because of taka appreciation against the euro.[37] However, later on, when the euro appreciated against a weak dollar, Bangladeshi exporters reaped some benefit. Weak demand for US dollars in Bangladesh (from slower imports as against robust remittance inflows) perhaps led to some appreciation of the taka against the dollar supply underwritten by rising export earnings. Thus, keeping the exchange rate against the dollar stable has helped exporters. However, depreciation of the Indian and Pakistani rupee and the Vietnamese dong, and China not allowing the yuan to depreciate, has undermined Bangladesh's competitiveness quite significantly in markets where these countries are Bangladesh's major competitors, particularly in the markets for apparels.

3.2.2 Interest rate management

Generally, the commercial lending rate in Bangladesh has remained on the high side, against the backdrop of a high deposit rate underpinned by high inflation: 9.93% in 2007/08 and 6.66% in 2008/09. However, at the same time, the spread between lending and deposit rates has persisted as high. Proactive measures have been voiced by many quarters to address this issue (Figure 11).

Figure 11: Interest rates (lending and deposit) and spread in Bangladesh, Jul 2008-Sep 2009 (%)



Source: Based on BB (2009a).

Responding to demands from investors, exporters in particular, the BB put in place a ceiling of 13% on commercial lending rates on 19 April 2009 for agricultural credit and credit for large and medium industries (term loan and working capital), along with loans for the housing sector. However, despite the imposition of the cap for these selected sectors, the weighted average rate of interest on commercial lending remained above 13% (which was the usual case); from 13.5% in April 2009, the weighted average lending rate went up to 13.8% in May 2009 and marginally decreased to 13.6% in July 2009; recently, this has further declined to 13.1% (September 2009). This appears to be the result also of mounting excess liquidity in the banking sector.

The secondary objective of the ceiling, to bring down the spread, has not succeeded at all. The banks responded by offering lower rates on deposits, which came down to 7.5% in September 2009 from 8.2% in April 2009. The spread between the lending and the deposit rate increased to 5.7% in September 2009, from 5.4% in April 2009.

However, it is argued in the available literature that the interest rate has only a limited impact on private investments in Bangladesh (no response at the aggregate level in the Bangladesh context)

37 Bangladeshi exporters also suffered when the taka appreciated against the euro in 2008. Exporters in Bangladesh are generally reluctant to take forward coverage since the taka has a track record of generally depreciating against major currencies.

(Ahmed and Islam, 2006). As it appears, the move by the BB to put a ceiling on interest rates has not had any significant effect in terms of stimulating investments.

3.2.3 Budgetary support for SMEs and cottage industries

GoB has created three funds with seed money of Tk1000 crore ($144.8 million) to provide refinancing facilities to SMEs against loans disbursed by commercial banks and financial institutions. At least 15% of this allocation has been earmarked for women entrepreneurs, at an interest rate of 10%. A number of tax measures have also been taken for cottage industries. These are currently exempted from VAT and instead are required to pay a turnover tax at a rate of 4%, which has a positive impact on costs of production. In the budget for 2009/10, eligibility for exemption from VAT for cottage industries has been widened to cover relatively larger cottage units.[38] Besides, the limit on turnover has been proposed to increase to Tk40 lakh ($0.06 million) from Tk24 lakh ($0.03 million). These measures are likely to aid cottage industries by decreasing their production costs.

3.2.4 Domestic demand and investment stimulation

Public investment programme

It has been argued by many that Bangladesh should pursue policies towards stimulating domestic demand in order to counter the impact of the crisis on the domestic economy, as has been done by other affected economies. A common recommendation has been to strengthen public investment programmes that not only generate employment opportunities but also play a crucial role in stimulating private investment through improved infrastructure. The government eventually came up with an ADP[39] much bigger than those of the past years. The total size of the ADP for 2009/10 has been fixed at Tk30,500 crore ($4.4 billion), over 55% higher than the implemented ADP of 2008/09 (IMED, 2009).

However, while a larger ADP indicates the intensions of the government, it is the implementation aspect that is a major concern, considering the existing implementation capacity of government institutions. In the past, ADP implementation has hovered around 80-85% of the target. The latest available information regarding status of ADP implementation indicates similar performance for this year. On the other hand, while in percentage terms the ADP utilised for 2009/10 is rather similar to that of the previous year, in absolute terms this implies about 31% higher utilisation of funds during the first quarter. The government is also trying to remove obstacles causing slower progress in ADP projects, to improve implementation status. One critically important issue from the perspective of improving implementation has been the complexities in procurement policies, resulting in delays in setting projects in motion. The government is currently reviewing the existing Public Procurement Act (PPA 2006) and the PPR (2008) to remove delaying factors, such as lengthy tendering processes. It will be important, however, to ensure that transparency and accountability are not jeopardised in the process so that the required quality of implementation can be maintained.

Provision for legalising undisclosed income

Apart from the larger development expenditure, GoB has also explored other measures to stimulate the domestic economy. In the national budget for 2009/10, GoB maintained a provision to legalise undisclosed money in the mainstream economy through unquestioned investment facilities in some selected industrial and service sectors on payment of 10% as tax. The provision drew criticism from different quarters on the grounds of both morality and effectiveness (particularly with regard to improving revenue), but it may benefit the capital market and the housing sector in particular, by drawing more investments into these sectors. However, it has been argued widely that perhaps it would have been better to provide the facility to selected thrust sectors, rather than maintaining its current economy-wide nature.

38 Previously, cottage units with plants and machineries with a financial involvement of up to Tk15 lakh ($0.02 million) were eligible for this exemption. The limit has now been extended to Tk25 lakh ($0.04 million).

39 The ADP accounts for the major component (over 80%) of public investment in Bangladesh.

3.2.5 Duty measures

Lower corporate tax rate

Bangladesh has maintained a high corporate tax rate of 45% for companies not listed on the stock exchange. For listed companies, the tax rate is 37.5%. It has been acknowledged that global developments may impact the income and profitability of these companies, particularly financial institutions, and in the budget for 2009/10 the corporate tax rate for financial institutions was brought down to 42.5%. It is estimated that, in doing so, the government will incur a revenue loss of about Tk550 crore ($78.6 million) in the current fiscal year (Bhattacharya et al., 2009).

Lower duty on imports of industrial raw materials

In an effort to provide support to domestic industries during the crisis, the government has decided to reduce the rate of duty on imports of industrial raw materials. The national budget for 2009/10 has brought the existing level of 7% down to 5%. However, this measure has been accompanied by increased duties on imports of luxury goods to make up the revenue loss incurred from it.

3.2.6 Measures for returnee workers

Although remittance flows are robust at present, there is a possibility of a lagged effect, given the lower number of people now leaving for jobs abroad. To keep the negative impact of the global recession on remittance flows at a minimum, GoB has announced the following strategies in the national budget: 1) training programmes for skills development of returnee expatriate workers; 2) a diplomatic initiative to prevent retrenchment of workers; 3) exploration of new labour markets abroad; and 4) strengthening the National Skill Development Council to build a skilled workforce compliant with international labour markets. The government has allocated $10.1 million for these purposes (Rahman et al., 2009b).

Although GoB has expressed its commitment to rehabilitating retrenchment-hit returnee migrants, no specific measures have been proposed yet to absorb this group of people. Nevertheless, it is expected that the policy support (both fiscal and monetary) that has been extended to various labour-intensive sectors, including SMEs, agriculture and export-oriented industries, may result in additional job opportunities, which would help to an extent to accommodate returnee migrants. The government has also strengthened its efforts to directly create new job opportunities. A new programme, titled Employment Generation for the Hardcore Poor,[40] has been announced to create new employment opportunities for 4.9 million man months with an allocation of Tk1176 crore ($170 million), along with a National Service Programme[41] introduced for Higher Secondary Certificate (HSC) or equivalent graduates with an allocation of Tk20 crore ($2.9 million).

3.2.7 Measures to minimise revenue loss from slower imports

New duty structure

Crisis-induced slower imports gave rise to concerns over possible revenue losses at the import stage. As is detailed in Section 2.4, these concerns later proved to be valid, as significantly lower import duty collection was recorded during 2008/09 and also in the early months of the current fiscal year (2009/10). At the same time, the national budget for 2009/10 marks a reduction in duties on imports of industrial raw materials, from 7% to 5%, to support domestic industries, which would imply further revenue loss at the import stage.

Responding to the issue, GoB has made some modifications to the duty structure on imports. An effort to balance the loss in import duties has been made, by increasing duties on imports of finished/luxury

40 This programme was introduced to modify the 100-Day Employment Generation Programme, launched during the past Caretaker Government, postponing the second phase of the programme.

41 The beneficiaries will get three months' training and will be provided with employment for two years in government institutions.

goods (cars, air conditioners, etc). At the same time, a 5% regulatory duty has been imposed on some luxury items with customs duty of 25%.

It is estimated that the current duty structure will result in 5.65% additional revenue (over 2008/09) in 2009/10, even with zero growth in imports. Assuming a 13% growth in imports for 2009/10, as projected in the Medium-Term Macroeconomic Framework (MTMF), it is likely that revenue earnings from imports in 2009/10 will be around 11.2% higher than in 2008/09. The new duty structure is, therefore, expected to minimise the revenue loss from potential slower imports as a consequence of the depressed global situation.

Expansion of the tax net

Apart from the new import duty structure, the government has also planned various initiatives to bring new taxpayers under the tax net through nationwide tax surveys. GoB is also considering withdrawal of the provision of tax refunds for government employees from the current fiscal year. It should be noted that currently there are only 0.76 million individual taxpayers under the tax net, of whom 0.15 million are government employees who get their tax payment refunded. Therefore, the number of effective taxpayers is only 0.61 million (2009).

3.2.8 Safety nets for the poor and the vulnerable

The possible direct and indirect adverse affects of the global economic crisis on the poor and marginalised have created a demand for GoB to take additional social protection measures. This demand is reflected in the national budget for 2009/10, in which an allocation of Tk14,320 crore ($2 billion) was made for social safety net programmes. This allocation is 26% higher than that of 2008/09 and 12.58% of the total budget (2.09% of GDP). Allocations for social empowerment were also increased, from Tk2484.0 crore ($359 million) to Tk3007.0 crore ($435 million), which is 2.64% of the total budget and 0.44% of GDP. The two employment creation programmes mentioned earlier (Employment Generation for the Hardcore Poor and the National Service Programme) have also been created as part of safety net programmes.

With regard to strengthening of food security for the poor and vulnerable, the government has allocated Tk5877 crore ($851 million) under the Food for Works Programme, Vulnerable Group Feeding, Vulnerable Group Development, Test Relief (Food) and Gratuitous Relief (Food), and also as part of food assistance to the Chittagong Hill Tracts.

4. Global recovery and possible policy implications for Bangladesh

As the recent revised growth projections (Table 14) and other visible indicators suggest, 2010 is expected to hold noteworthy improvements in terms of economic activities, leading to increased global demand. Revised upward estimates of GDP growth in the US and the EU, coupled with a favourable forecast for global output in 2010, indicate that the global economy may soon recover from the slump. At the same time, gains in the major stock market indices around the world show definite signs of renewed investor confidence. Stabilisation of oil prices in recent months also suggests a favourable outlook for oil revenue-dependent countries.

Table 14: GDP growth rate projections, 2009-2010 (%)

	2009	2010	2009	2010
IMF projection	January 2009*		October 2009*	
World	0.5	3.0	-1.1	3.1
US	-1.6	1.6	-2.7	1.5
Euro area	-2.0	0.2	-4.2	0.3
ADB projection	March 2009*		September 2009*	
Asia	3.4	6.0	3.9	6.4
South Asia	4.8	6.1	5.6	6.4
Bangladesh	5.6	5.2	5.9	5.2

Note: * Refers to the time when projections were made.
Sources: ADB (2009a; 2009b); IMF (2009a; 2009b).

Bangladesh should reposition its economy in view of the envisaged global economic recovery. It is important to understand the nature and pace of the recovery and to craft policies to take maximum advantage of emerging opportunities. Policy responses should take into account the possible structural changes that may evolve as a result of the crisis. In recent times, Bangladesh has been trying to diversify both its exports and its markets. New export-oriented industries such as shipbuilding and leather goods are perceived to have significant potential. Indeed, before the crisis, some visible interest in these items was seen from international buyers. During the crisis, for obvious reasons, interests waned. With regard to export of labour, some positive movements in skilled and semi-skilled labour are becoming visible. Once the recovery gains momentum, Bangladesh is expected to benefit from these structural changes. In the above context, the following policy initiatives and interventions will require careful consideration.

4.1 Revitalising investments

The investment scenario in Bangladesh will need to be significantly re-energised. What is rather discouraging is that, in spite of growth in absolute terms, gross investment as a percentage of GDP declined for the third consecutive year in 2008/09.[42] Investment has suffered from both a lack of infrastructure, including power and communication, and a lack of investor confidence in view of global volatility.

Inadequate power supply has been a major bottleneck deterring industrial development in Bangladesh and has severely constrained investment and business activities in the country. New investments are being discouraged because of the power crisis, and existing ones are bearing the brunt of frequent outages, leading to damage of equipment, production disruption and cost escalation from more expensive alternative sources of power. The gap between demand for and supply of electricity reached close to 2000 MW in 2008/09. A yawning gap between capacity and generation of electricity is emerging for a number of reasons, including gas shortages, ageing power plants and lack of new instalment. It is estimated that, during April 2009, for the abovementioned reasons, the average daily

42 Investment is estimated to have been 24.18% of GDP in 2008/09 compared with 24.21% of GDP in 2007/08.

shortage was to the tune of 845 MW. In view of ongoing electricity shortages, GoB has taken a number of short-term measures, including the introduction of daylight saving time, adjusting the day off in the industry sector, reducing the time span that shopping malls can remain open and encouraging small-scale private power generation.[43] Owing to gas shortages, the government recently decided to delimit/control the supply of gas to various industrial units (like the fertiliser, yarn and textile industries) during evening hours. FGDs with export-oriented industrialists (Rahman et al., 2009b) evinced that at least 100 factories are waiting for electricity and gas connections, which the government is holding back in order to meet current demand. Investors rate 'lack of electricity and gas' as the single most important constraint to investment in Bangladesh. Around 800 MW was expected to be added to the national grid by the end of December 2009, which it was thought would improve the situation to some extent, but latest statistics suggest that the reality was only 475 MW. Much more will need to be done in view of the increasing demand.

Infrastructural development, particularly in power and energy, will be critical and, in this context, the announced public–private partnership (PPP) will need to be given due importance.[44] Planned investment under the PPP initiative is around Tk7000 crore, or $1 billion (about 1% of GDP). However, the PPP has been slow to take off over the past five months. A PPP Act would be helpful to make the government's commitment more credible in this regard.

Public investment has been on the slide for the past decade,[45] with the deceleration attributed mostly to slow ADP implementation.[46] To revive private investment, higher public sector investment is critical in the context of Bangladesh. The targeted size of the ADP for 2009/10 is about 4.4% of GDP (55% higher than the implemented ADP of the preceding fiscal year). However, as pointed out, during the first quarter of 2009/10, only 10% of the announced ADP had been implemented. Thus, a renewed effort will be needed in 2009/10 to improve both the quantitative and the qualitative aspects of the ADP, which should then be able to stimulate and crowd in private sector investment. Towards this end, institutional as well as human resource capacities of relevant agencies of the government will need to be substantively strengthened and improved by putting in place adequate resources, capacity-building mechanisms and incentive structures. Quality of output and monitoring of outcomes will need to be accorded the highest priority in implementing the ADP.

To stimulate private sector investment, an interest rate policy could play a role. In this case, the BB will need to play a leading part in order to reduce the spread between the lending and deposit rates, if need be by pursuing a proactive policy in the context of both the ceiling on lending and also the floor on deposit rates.

In view of the constraints in mobilising adequate domestic resources, FDI will need to be encouraged. Net FDI inflow in the first two months of 2009/10 decreased by 37.3% (although this may not be indicative of the expected annual flow). Without improving the domestic investment situation and ensuring adequate power supply, it will be difficult to attract significant inflows of FDI. At the moment, encouraging FDI both in infrastructure and in modern sectors, focusing on both domestic and international markets, should be emphasised along with speedy implementation of development projects without compromising their quality.

43 Renewal fees on captive power plants and VAT on domestic generation of power along with domestically produced/assembled generators were withdrawn in the budget for 2009/10.

44 While a PPP component in the budget for 2009/10 is a novel initiative, PPP-led projects operating in infrastructure building, particularly in power generation, have already been there for some time now.

45 Public investment as a percentage of GDP reduced to 4.6% in 2008/09 from 7.2% in 2000/01.

46 The ADP constitutes about 80% of public investment in Bangladesh.

4.2 Supporting export growth

GoB has come up with a number of measures (including cash subsidies) to deal with the decline of exports. However, as latest data reveal, negative impacts of the global crisis on Bangladeshi exports have intensified in recent months. In consideration of the latest developments, raising efficacy of implementation of proposed policy decisions and the stimulus packages will be critical in this context. As noted earlier, the provision for presumptive payment of 70% of the cash subsidy claims made under the first stimulus has already been implemented. It will be important to settle the remaining claims (30%) quickly: their disbursement was announced to take place after audits. Speedy implementation of the support given to export-oriented sectors in the second package will also be of critical importance.

In view of the increasing competition from China, Vietnam and other countries, and against the backdrop of the incentives being provided there, Bangladesh will need to put concentrated effort into holding on to or increasing its market share. The stimulus packages are expected to help export-oriented sectors in addressing these concerns in the short run. At the same time, it is important that workers' welfare is kept at the centre of attention. As in Sri Lanka, policymakers could consider attaching anti-retrenchment conditionalities to the support packages put in place.

4.3 Sustaining aid flows

Bangladesh has managed to negotiate a higher inflow of foreign aid for the current fiscal year and for the next few years to come. As discussed earlier, both the World Bank and the ADB have promised substantially higher aid to Bangladesh in the current year; enhanced support is also being negotiated with China. However, past experiences have shown that a large part of the aid commitments remains undisbursed each year owing to low progress with regard to fund utilisation in the early stages, mostly because of a failure to achieve satisfactory implementation of ADP projects. The large aid requirement to finance the deficit projection for the current fiscal year will call for renewed emphasis on improving ADP implementation in the current fiscal year, particularly in aided projects.

As the current process of awarding projects to bidders has been one of the most critical factors hindering ADP implementation, the government has recently undertaken an initiative to simplify the procedure to facilitate speedy initiation of projects by amending the PPA 2006 and PPR 2008. However, some amendment proposals have drawn criticism from the major development partners, i.e. the World Bank and the ADB, and created uncertainties about fund release by these institutions. These include setup of a lottery for awarding projects, exclusion of experience requirement for projects not exceeding Tk5 million ($0.07 million), etc. Contentious issues will need to be settled as early as possible to avoid further delays and deterioration of the ADP implementation record (and hence to materialise aid commitments) in the current fiscal year. This will also be important in view of the relatively larger size of the ADP proposed in the budget for 2009/10. Underutilisation of ADP allocations will be costly from the perspective of creating employment, increasing domestic demand and stimulating private investments.

4.4 Sustaining remittance flow

Concomitantly maintaining outward migration and robust remittance flows will be of high importance in order to absorb the huge number of new aspirants entering the job market every year, and also from the perspective of their significance as a contributor to foreign currency reserves and as a potential source of financing investments. To address the negative impact of the global crisis on remittance flows and to sustain outward migration, the government could consider the following strategies to minimise certain longstanding issues, which are rather general in nature but have become that much more important in view of dealing with the crisis.

Lowering the cost of migration

Strict monitoring and enforcement systems need to be deployed to reduce unscrupulous recruitment practices and ensure that agent commissions fixed by GoB are implemented properly. Awareness should be strengthened about fees and service charges to be claimed by agents of recruiting agencies from aspirant workers. Recruitment and migration procedures need to involve a minimum number of intermediaries and transaction costs must be kept as low as possible. Formal channels of transaction should be rendered more flexible, accessible, fast and cost effective. The government may work with major labour-importing countries to allow transfer of jobs by migrant workers without any transfer fee. Kuwait has already agreed to provide such flexibility to Bangladeshi workers.

Training

Appropriate training to improve human resources is the most important factor to enhance market opportunities for migrant workers. Emphasis should be given to specialised training programmes with the target of meeting the needs of specific human resource importers. Some particular categories (e.g. nurses, medical technicians, caring service providers) need to be identified, for which the country has the potential to develop highly skilled manpower. Quick implementation of such training programmes will be particularly important to take advantage of the global recovery and consequent demand enhancement for migrant workers. In this context, allocation of Tk70 crore ($10.1 million) in the national budget for 2009/10 to form a Skill Development Fund is worth mentioning and much appreciated. The fund will be used for the expansion of labour markets abroad, to conduct research exploring new labour markets, to provide training for prospective workers and for retraining for returned migrants.

Loan facilities for aspirant and returnee workers

Traditional banks have not always provided adequate services to aspirant migrant workers. Thus, to offer financial services and other related support to retrenched and returnee migrants, the initiative to establish a *probashi bank* (bank for non-residents) should be geared up and implemented without delay. According to available information from the BMET, a proposal to establish such an institution has been submitted to the BB for approval. However, it may take time to finalise the *modus operandi*, even though the initiative has been approved. GoB should use the existing expatriate welfare fund to provide loans/credit to returnee migrants to help them start businesses of their own.

Diplomatic missions

GoB should strengthen the operations of diplomatic missions in the Middle East and Southeast Asian countries. Legal advisors in major labour destinations could be appointed in order to provide legal support to deprived Bangladeshi workers. Diplomatic missions need to be extended further to explore potential new markets for human resource exports, to develop strategic partnerships with them and to ensure the rights of migrant workers. With a view to expanding international cooperation on migration, international organisations can promote dialogue and encourage exchange of best practices on migration management among countries in a regional context.

4.5 Enhancing alternative sources of revenue mobilisation

In light of the growing need for development spending and to extend support measures to deal with the global crisis, there is an urgent need to stimulate revenue generation in Bangladesh without disrupting support to producers and external trade flows. It should be recalled that, in Bangladesh, public revenue is rather import dependent in the absence of appropriate measures to bring more people under the domestic tax net. In view of the crisis, revenue collection efforts in the coming year will be somewhat constrained, so exploiting the untapped reserve of direct tax sources will be seen as a major task. The major issues that need immediate attention to attain revenue targets for 2009/10 are as follows.

Tax surveys to widen the tax net

Tax authorities need to execute a drive to bring more people under the tax net. Bangladesh has around 2.3 million registered Tax Identification Number (TIN) holders, of whom only about 0.76 million submitted their tax returns this year (NBR, 2009b). The government has already announced an initiative to bring in about 0.4 million new taxpayers under the tax net, through new tax surveys, by next year, but it will be equally important to reach out to the large informal sector that exists in the economy.

Over the past two decades, the nominal income of people living in municipality and *upazila* (sub-district) areas is perceived to have gone up significantly. However, owing to an absence of tax officials at peri-urban levels, collection of taxes from these areas has not increased. Along with tapping the microeconomic tax base, expansion and supervision of the Large Taxpayers' Unit (LTU) is necessary.[47]

Settling legal disputes over NBR recruitment
Owing to legal disputes, the NBR has not been able to expand its manpower capacity adequately since the mid-1980s. These disputes need to be settled and an effective revenue administration, staffed with a well-trained and motivated workforce and adequate IT support to track the paper trail, must be developed to realise revenue objectives.

Simplification of tax laws and facilitating online tax return submission
In order to ensure clarity, transparency and predictability, tax laws need to be made taxpayer friendly. Promoting the use of a 'self-assessment system' may significantly increase the revenue of the government by bringing taxpayers in personal contact with the revenue administration without the help of intermediaries. The feasibility of online tax return submissions should also be tested.

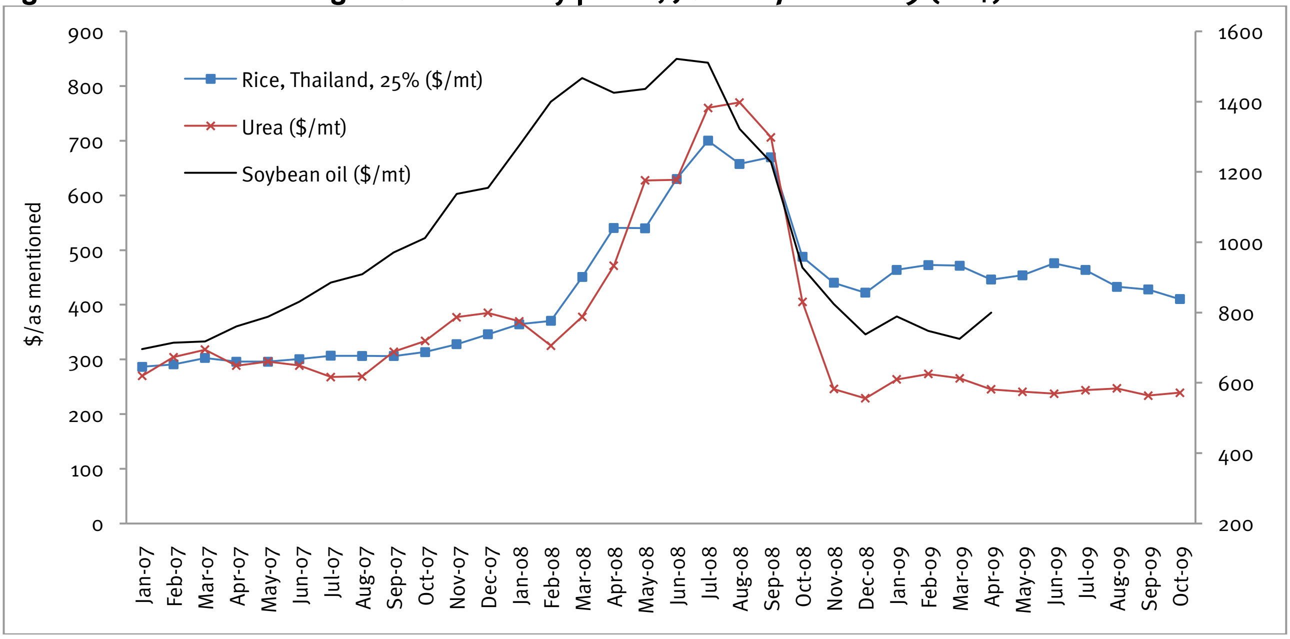
4.6 Maintaining macroeconomic balances

Bangladesh was successful in maintaining macroeconomic stability with moderate growth throughout the first half of this decade. During 2007 and 2008, macroeconomic management was directed to deal with 'agflationary' pressure as a result of the worldwide surge in food prices. During July 2007 to September 2008, inflation in Bangladesh tended to remain at two-digit level.[48] Since then, the world economic situation has changed and macroeconomic policies in Bangladesh have had to adapt to the changing reality. Prompted by the global financial crisis, policies have been redirected towards crisis management. Bangladesh, with its late entry to the crisis, has dedicated full force to addressing the adverse impact of the recession only in recent times. However, global prices may once again start to rise in view of the expected recovery. International oil prices have been rising, and are likely to continue on this upward trend as the world economy recovers in the early part of 2010.

In Bangladesh, food prices generally drive inflationary trends. The international price of rice (Thailand, 25% broken) declined to $410 per metric ton in recent times from the higher level of 2008. However, in the Bangladesh context, it is important to note that India experienced its lowest food grain production in recent history in 2009 and may need to import food this year.[57] Thus, it is important that Bangladesh be able to achieve its targets for crop production. Soybean prices have been going up and may create volatility in the domestic market; however, the price of urea has been rather stable in the global market (Figure 12).

47 The LTU has been set up specifically to examine the performance and returns of large enterprises that account for a significant share in total direct tax collection in Bangladesh.
48 Average food inflation during the reported period was even higher, at 12%.

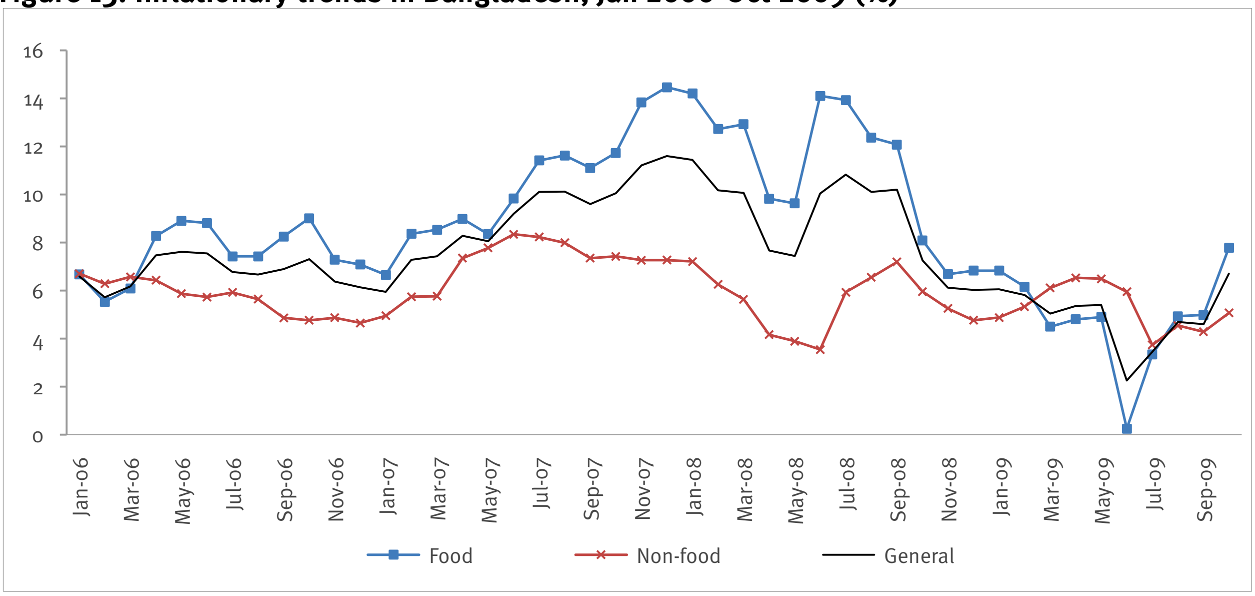
Figure 12: Movements in global commodity prices, Jan 2007-Oct 2009 (US$)



Note: The right-hand axis shows the price of soybean oil; the left-hand axis shows the price of rice and urea.
Sources: World Bank (2009a; 2009b).

These global developments, coupled with domestic contingencies, will require prudent macroeconomic management. Inflation in Bangladesh has been on the low side with the progress of the global crisis, reaching 2.3% in June 2009.[49] However, inflation has again been on the rise since July 2009 (Figure 13). A continuation of this trend could pose a threat to the maintenance of macroeconomic stability in the near-term perspective.

Figure 13: Inflationary trends in Bangladesh, Jan 2006-Oct 2009 (%)



Source: Based on BBS (2009b).

Bangladesh's budget deficit has been under control in recent times, amounting to 3.3% of GDP in 2008/09. In the face of the deepening impact of the crisis, the government had to opt for a higher deficit, which could create some inflationary pressure if budgetary expenditure targets are realised at the end of the fiscal year.[50] On the other hand, lack of import demand, coupled with buoyant remittance

49 At the same time, food inflation in Bangladesh reached its all time low (0.3%).
50 However, during the first two months of 2009/10, deficit financing was not required, thanks to sluggish implementation of the ADP.

flows, has helped Bangladesh accumulate significant foreign exchange reserves. The BB has been vigilant in maintaining exchange rate stability and has been buying foreign currency from the open market on a regular basis to maintain a balance between demand and supply for US dollars. The foreign exchange reserve is now equivalent to about 6 months of import payments.

The relief and security in the area of balance of payments is definitely a positive development. To some extent, this may also help ensure food security, i.e. using foreign exchange for food import payments. However, foreign exchange management has led to an increased flow of money supply in the domestic market, which could lead to inflationary pressure in the economy. Keeping in mind that excess liquidity with scheduled banks is already very high,[51] the central bank has actively participated by mopping up the money supply from time to time, using various monetary instruments, mainly in the form of reverse repo.

However, to ensure food security and to keep inflation in check, much will depend on whether Bangladesh can replicate its recent success in crop production.[52] In this context, balancing the apparently conflicting interests of consumers and producers will once again be the major challenge for Bangladesh's policymakers. Stimulating productivity of agriculture through prudent subsidy policy, providing incentives to promote adoption of high-yielding varieties and adoption of technology must be given due priority in policymaking (CPD, 2009). Managing the market should once again be on the policy agenda, and the government must exercise due vigilance in terms of developments on the global scene.

51 Excess liquidity with the scheduled banks doubled in the past one year owing to weak investment and import demand.
52 Production of food grains in 2008/09 was 8.0% higher than in the previous year.

5. Conclusion

In the preceding analysis, an attempt is made to capture the impact of the ongoing global financial crisis on the increasingly globalising economy of Bangladesh, by tracing the impacts through various transmission channels. Although the Bangladeshi economy has been spared the worst consequences of the crisis, particularly because its financial and capital markets are by and large isolated from global markets, there was no escaping the adverse effects once the crisis started to deepen. As the crisis evolved and developed, Bangladesh suffered from a slowdown in export earnings, a lower number of workers going abroad, lower revenue earnings and a loss of competitiveness in view of stimulus packages put in place by other countries.

The first stimulus package was geared mainly towards domestic demand stimulation, with only a limited amount of support to a number of non-RMG export sectors. In September 2009, exports of apparels experienced a 27% dip compared with the previous year. As such, the stimulus package announced in October 2009 was more of a reactive one.

Exports started to pick up again in October (18% growth), indicating increasing volatility in Bangladesh's export market. Although exporters argued that the government should have provided incentives earlier, whereas the government has tended to design policies based on market signals, there is now a general agreement that, notwithstanding volatility in export performance, a stimulus was required in view of shrinking profits, a lower migration rate, the impact of policies pursued by competitors and the need to take advantage of opportunities originating from the incipient global recovery. There is a growing feeling that, in spite of the signs of recovery, lagged negative impacts will continue to be felt in Bangladesh's job market, in prices offered for Bangladesh's exports and the consequent adverse terms of trade, in profit margins and in the trade balance, with possibility of export earnings falling behind the pace of the rise in import bills.

GoB has made an attempt to enhance its safety net and employment programmes, which will need to be strengthened further in view of the nature of global recovery (jobless growth, lower demand for migrant labour, etc). Higher allocations to agriculture and continuing support to stimulate higher crop production will be required particularly from the perspective of ensuring food security, which could become an issue in 2010 in view of the expected global food availability situation. In view of this, government's focus on agriculture both in the first stimulus package and in the budget for 2009/10 appears to be well justified. Here, the tension between the urgency to keep food prices low and providing adequate incentives to farmers to grow more food will be a challenge. Policy support to raise productivity and lower costs at farmer level will be the major tasks to be addressed in this context.

It is too early to make an assessment of the efficacy and effectiveness of GoB's stimulus packages. Additional cash incentives to apparels and other export-oriented sectors are obviously going to benefit the exporters. In the context of the emerging situation with regard to Bangladesh's competitive strength in the global market, a renewed effort will be required to enhance productivity in the export-oriented sectors. The government's stimulus package does contain additional support for encouraging access to new markets, but additional support will be required for product diversification (such as the promising shipbuilding sector, which could receive some fresh air in view of the rise in global trade).

The Bangladeshi economy suffered from higher inflation during the pre-crisis period. Indeed, the financial crisis that followed did not allow Bangladesh much leeway to take the corrective measures necessary to mitigate the adverse impacts of the rise in commodity prices and its adverse consequences for the economy. The need to pursue countercyclical policies during the ongoing crisis has meant that scarce resources have had to be diverted from sectors that are critical to achievement of the poverty-reducing Millennium Development Goal (MDG) targets. All this will require a restructuring of resource allocations once recovery sets in and the worst impacts of the crisis are over for Bangladesh.

Bangladesh has been identified as one of the most vulnerable economies in terms of climate change, and the expected fall in global food production this year could mean Bangladesh is confronted with challenges in terms of food security, which will need to be addressed through higher domestic food production. Inflation management will also be crucial, no doubt. As Bangladesh prepares for the future, there will be a need to be sensitive to these challenges.

Bangladesh's macroeconomic management over the near term will, thus, need to be crafted carefully by building on the demonstrated resilience of the economy, by addressing the emergent lagged impacts and by taking advantage of the opportunities offered by a recovering global economy.

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