

BANGLADESH

PRS IMPLEMENTATION FORUM

Dhaka, November 15, 2005

Statement by the Representative of the International Monetary Fund

Honorable Prime Minister, Honorable Ministers, delegates, ladies and gentlemen:

- 1. The IMF welcomes this opportunity to participate in the PRS Implementation Forum.** This forum is a good occasion to review Bangladesh's achievements over the last few years and highlight the main challenges that still need to be addressed. The implementation of the NSAPR also provides a good opportunity for Bangladesh to address issues in the areas of governance, social policy, and economic management that have been a constraint to economic development and poverty reduction for far too long.
- 2. The IMF has worked closely with the government of Bangladesh to help it develop and implement a reform program to achieve the goals of raising economic growth and accelerating poverty reduction.** In June 2003 the IMF's Executive Board approved Bangladesh's request for a three-year arrangement under the Poverty Reduction and Growth Facility (PRGF), later augmented to help overcome the impact of the removal of Multi-Fiber Agreement (MFA) quotas. Economic performance under the program has been broadly satisfactory so far, and Bangladesh has completed three reviews with the most recent one concluded in June of this year.
- 3. Overall macroeconomic performance has generally been supported by prudent policies.** The central government's overall deficit was contained to 3.5 percent of GDP in FY05, although it should be noted that continuing losses in the state enterprise sector are not included in these figures. Monetary policy has generally been cautious and supportive of growth while keeping inflation relatively low until early this year. The move to a floating exchange rate regime was an important step, and the government's commitment to limit nonconcessional borrowing has contributed to keeping debt ratios manageable. Despite the impact of devastating floods and higher oil prices, growth was strong at 5½ percent in FY05. The economy has withstood well the initial impact of the elimination of MFA quotas, and growth momentum appears to have been maintained this year. Implementation of structural reforms has also shown some progress with initial steps having been taken with respect to reforming tax administration and the nationalized commercial banks (NCBs), as well as in liberalizing the trade regime.
- 4. However, considerable macroeconomic challenges will need to be addressed in the period ahead.** Inflation, led by rising food prices last year, has picked up. While the impact of higher oil prices has been manageable so far as better-than-expected garment

exports and continued strong remittances have helped finance higher oil imports, more flexible and pro-active macroeconomic management will be required in the coming months.

5. **Bangladesh has already made progress toward meeting the MDGs owing to strong growth over the last decade.** However, it remains among the world's poorest countries. Faster growth will be required to reduce poverty and achieve the goals targeted in the NSAPR. Growth continues to be adversely affected by inadequate investment in human capital, infrastructure bottlenecks, and poor governance. To create an enabling environment for growth and remove impediments to investment, continued prudent macroeconomic policies and intensified structural reforms will be needed.

6. **The medium-term macroeconomic framework presented in the NSAPR represents a high growth scenario.** It aims to achieve a medium-term annual growth of 6½-7 percent, while maintaining inflation at 4½-6½ percent. To achieve this high growth, a steadfast implementation of reform policies will be needed, together with favorable economic conditions. As was done in some other countries preparing PRSs, it would have been useful to consider alternative macroeconomic scenarios. We thus recommend that future PRS documents include at least two scenarios: a baseline scenario that reflects progress toward agreed objectives but is more in line with past experience, and a more ambitious high-growth scenario. Budgeting the level of expenditure based on a very optimistic environment could undermine fiscal discipline if not supported by revenue mobilization.

7. **We support the thrust of the macroeconomic policies proposed in the NSAPR. Over the near term, however, policy adjustments are needed to keep macroeconomic performance on track.** Money and credit growth remain high. In view of this, the authorities' intention to tighten the monetary stance further to contain inflationary expectations is appropriate. With respect to exchange rate policy, we encourage the authorities to further improve the functioning of the foreign exchange market and allow the exchange rate to move, as needed, in response to changes in economic fundamentals, especially in view of recent external shocks arising from oil price increases and the phase out of MFA quotas.

8. **The authorities' commitment to protect fiscal sustainability while supporting growth and poverty reduction is welcome, but will depend crucially on better revenue mobilization.** Determined efforts to improve revenue collections are vital for funding development expenditure and social spending aimed at poverty reduction without jeopardizing fiscal sustainability. However, the government needs to do more to show its commitment to address Bangladesh's chronic revenue shortages, including by accelerating reforms in revenue administration and reducing tax exemptions. There is also scope for increasing the efficiency of existing spending to allow room for more poverty-reducing expenditure. We also call for more discussion in future PRSs of the macroeconomic impact, including substantial quasi-fiscal losses, associated with the ongoing operating losses in the NCBs and the pricing of petroleum and natural gas products. These ongoing losses (and foregone revenue) add to the contingent liabilities of the government and undermine the

sustainability of development policies. In this regard, strengthened reform of SOEs with the support of the World Bank will be needed to contain quasi-fiscal liabilities.

9. **The bank restructuring program continues to move too slowly for the financial sector to play its role in promoting growth and investment.** Moving forward with the divestment of Rupali Bank will help improve market sentiment and facilitate the implementation of the entire bank restructuring program. Determined efforts to contain nonperforming loans and implement bank-by-bank strategies will also be needed to resolve the long-standing problems in the banking sector.

10. **In its program, the government intends to restrain domestic borrowing and rely on concessional external borrowing.** Government debt and debt service payments have been manageable thus far. To maintain external debt sustainability, any new external borrowing needs to be carefully screened and any nonconcessional loans kept to a minimum. External debt monitoring and management capacity need to be considerably strengthened to support policy analysis and decision making.

11. **Improving governance remains a key challenge and a high priority, particularly to improve the investment climate.** We look forward to effective operations of the Anti-Corruption Commission, as well as steadfast political commitment to tackle governance problems. Continued reforms of the NCBs, tax administration, and the trade system to ensure transparency and accountability will also contribute to improved governance.

12. **To advance this wide-ranging reform agenda, the government has consulted widely in the development of the PRS and is giving attention to forging domestic support for reforms.** Ensuring adequate social safety nets will be equally important, to help ease the transitional costs and mitigate the political risks of reform. Notwithstanding the difficult political environment that may be affecting the authorities' ability to implement key reforms, every effort must be made to prevent policy slippages. Otherwise, the hard-won gains toward macroeconomic stabilization could dissipate with economic and social objectives being jeopardized.

13. **To successfully carry out this large agenda, Bangladesh will need the continued support of the international community,** through technical assistance and financial support on concessional terms. The IMF looks forward to continuing to support Bangladesh's efforts to attain its economic potential and substantially bring down poverty for its people, and wishes the authorities every success in their future efforts.