

Recommendations for Budget 2020-21 in Light of the COVID-19 Crisis



Prepared for:



Ministry of Finance, Government of Bangladesh

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Background

The COVID-19 pandemic, which has now turned into a major global health and economic crisis unprecedented over the past 100 years since the Spanish flu of 1918. Economic activities across the world have collapsed. Most recent IMF projections show an overwhelming majority of global economies to contract in 2020. Hundreds of millions of people worldwide have lost their jobs and are confronted with survival and livelihood struggles.

Bangladesh has also started dealing with the severe consequences of COVID-19 with curtailed economic activities manifested in factory closures, massive loss of employment, cancellation of export orders, declining remittance inflows, and depressed demand for domestically produced goods and services. The World Bank projects overall economic growth in the current (FY20) and next fiscal year (FY21) to be in 2–3 per cent range. Poverty incidence is to rise dramatically—although expected to be temporary in nature—from around 20 per cent to more than 40 per cent.

The budget formulation for the next year is going to be a mammoth challenge given the uncertainty about economic activities, reduced capacity in revenue generation in the face of economywide slowdown, subdued international trade, and the need for increased resources in health and social protection that have now become priority sectors, and provisioning of stimulus packages to facilitate economic recovery.

Recommendations

In the light of this evolving situation, the Research and Policy Integration for Development (RAPID) would like to offer the following recommendations for consideration in the budget making process.

Allocation of resources

- It has been reported that a Tk 5,60,000 crore budget has been planned for FY21 compared to FY20 budget of Tk 5,23,190 crore. If this budget is formulated just by proportionally increasing the sectoral allocations, the challenges of the crisis will not be addressed effectively. The budget for FY21 should be tailored to mitigate the shocks arising from the COVID-19 crisis. With a potentially reduced fiscal space, there is a need to prioritise sectors.
- It is to be acknowledged that the finance ministry does not have much scope for discretionary spending as there are binding sector specific commitments that must be fulfilled. Therefore, some savings will have to be generated within the current sectoral allocations with the objectives of saved resources to be invested in health, social protection, and stimulus packages. Taking into account the current pandemic situation, the budget must allocate more resources to health and social security sectors.
- The health system in the country must be immediately strengthened. While health care professionals and workers are increasingly being infected, non-COVID-19 patients' not receiving treatment are now commonplace. This crisis should be regarded as an opportunity to build the national health system. Out-of-pocket expenses of Bangladeshi households are

highest amongst the global economies and it is high time to address this unfair, inequitable, and largely ineffective health care system for the mass population. As per the data in the budget documents for FY20, the share of government health expenditure in GDP is around one per cent, but for cross-country comparison World Bank's World Development Indicators (WDI) could be used. According to the latest data reported in WDI, the share of government health expenditure in GDP is around 0.4 per cent in Bangladesh as against around 2.7, 1.6, 1.0, and 0.9 per cent in Vietnam, Sri Lanka, India, and Pakistan, respectively.

- The allocation for Social Security Programmes (SSPs) must be beefed up as well. After many years' success in reducing poverty incidence and vulnerability, this crisis threatens to derail the remarkable progress made by Bangladesh. According to some estimates, 10–15 million households will now need some direct support to stave off hunger and meet their very basic necessities. The National Social Security Strategy (NSSS), adopted in 2015, considered a provision of support for covariate risks arising from natural disasters and unpredicted eventualities. It is now most appropriate to provide extended and effective support mechanism as envisaged in the NSSS.
- Currently, social security spending is just above 14 per cent of the budget and about 2.5 per cent of GDP. However, pension payments for retired government officials and honorarium for freedom fighters together comprise a substantial share of around 40 per cent of the social security budget. Ideally, SSP allocation should be considered excluding components like these that are not directly associated with the objectives of tackling poverty and addressing vulnerability. In expanding the allocation to social protection in the wake of the Coronavirus crisis, due importance should be given to a much wider coverage and deepened assistance for households directly affected (under covariate shocks) through expansion of programmes such as Open Market Sales (rice and foodstuffs at subsidised prices) and Test Relief Cash. One important issue is how to reach out to the poor and vulnerable households with emergency assistance, including the expanded support that is to be provided under social protection. It is widely regarded that cash assistance has many advantages over in-kind distribution. Cash programmes have been found to be 25–30 per cent cheaper (than in-kind transfers). Given the availability and rapid expansion of mobile financial services (MFS), money can now be sent to even remote places in Bangladesh. Even though using the MFS channel could be the most efficient option, it must be borne in mind that there is a big gender gap in mobile phone ownership.
- In the forthcoming budget, an emphasis should be given on the production and distribution of medicines, medical supplies, and potential vaccines. Production and distribution of the same by the private sector may require incentivisation. The government should consider undertaking proactive policy measures backed by budgetary resources to be part of the global value chain of medical supplies and vaccine production as there is going to be huge domestic and overseas demand for those in the near future.

Budget financing

- In recent years, there has been a consistent shortfall in actual revenues as against the targeted collection. A more realistic approach is required to assess the revenue generation capacity to manage public expenses during the crisis.

- The crisis has caused a substantial decline in economic activities, both in the domestic and international front. This would result in substantial decrease in domestic income and international trade. With an already low tax-GDP ratio of less than 9 per cent compared to that of the average of developing countries of 15 per cent, Bangladesh might be set for substantially low tax revenues shrinking the already constrained fiscal space. This calls for searching alternative funding sources for the budget.
- By the end of FY19, close to as much as US\$ 50 billion was stuck in the aid pipeline. This potentially shows the country's weak absorptive capacity and slow implementation of ADP projects. The countries and agencies contributing to current aid pipeline accumulation should be requested for reallocation of some of the resources to the health and social security sectors.
- The second important source for resources could come from the review of the Annual Development Plan (ADP) spending. In the on-going fiscal year, ADP spending could be just about 60 per cent of the targeted amount. Implementing an ambitious ADP for the next year is likely to be difficult. It has been a pattern over many, many years that ADP spending during the first two quarters of a fiscal year is slow due to, amongst others, the monsoon and weak implementation strategies; such a trend could be spared this time round by focusing only on the most essential projects over the next few months and diverting the saved resources to most essential sectors.
- The government can also ask all its ministries and departments to slash non-essential expenses. Such expenses are likely to be quite significant and can help generate resources for the priority sectors.
- The G20 nations have agreed on a moratorium on bilateral government loan repayments for over 75 poor countries until the end of the year as a part of the initiative to tackle the health and economic crises triggered by the pandemic. It would be wise for Bangladesh to accept the moratorium. Furthermore, Bangladesh, with other poor countries, should ask for a 2-year moratorium due to suppressed global economic and trade activities caused by the pandemic, even prior to that, because of such factor as the US-China trade war. The suspension of debt servicing both from bilateral donors and multilateral agencies should be demanded. This could generate a saving of around US\$ 2.8 billion for a year.
- The Bangladesh government has sought for US\$ 2.6 billion in loans (over Tk 22,000 crore), as emergency budget support, from five development partners to tackle the impacts of the COVID-19 pandemic. This is a welcome initiative and should be seriously pursued.
- In addition, the government can create new money responsibly and within a small range. Many global economies are using much larger stimulus packages and thus the Bangladesh economy might need some additional support in returning to pre-crisis level growth trajectory and building competitiveness.

The need for reliable information and informed policy inputs

- There are some suggestions that the budget deficit would swell and cross the until recently maintained threshold level of 5 per cent of GDP. The World Bank's (WB) South Asia Economic Focus 2020 report projects that Bangladesh's budget deficit might rise to 7.7 per cent of the GDP in FY20. GDP estimates are generally subject to some upward bias, which means actual budget deficit as proportion to GDP is likely to be under reported. For a crisis year, it is vital to

have credible GDP estimates. Otherwise, many of the policy objectives could be misdirected. This is where the role of the Bangladesh Bureau of Statistics (BBS) is key.

- Traditionally, Bangladesh has suffered from quality firm-level data of various sectors of the economy. Even in the wake of the crisis, there has not been any official attempt to undertake rapid assessments of the economy. This does not help the government in considering informed policy choices. This is one area where the BBS's capacity must be strengthened.
- Even after several years, the National Household Database, as recommended by the NSSS, could not be made operational with the objective of targeting the poor and vulnerable households. This has already proven to be a missed opportunity for reaching out to the households most severely affected by the current crisis.

Implementation of stimulus packages

- Stimulus packages are very welcome initiatives to mitigate the impact of the pandemic but their success depends how effectively they are implemented. The government has to ensure transparent and accountable implementation of the packages so that the stimulus funds reach the right beneficiaries in due time.