

COVID-19 and Bangladesh

Macroeconomic Impact and Policy Choices

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12 December 2021

Conference on
**Bangladesh Emerging from the Pandemic:
*Coping Experiences and Policy Choices***

Organised by



Citizen's Platform for SDGs, Bangladesh
এসডিজি বাস্তবায়নে নাগরিক প্ল্যাটফর্ম, বাংলাদেশ

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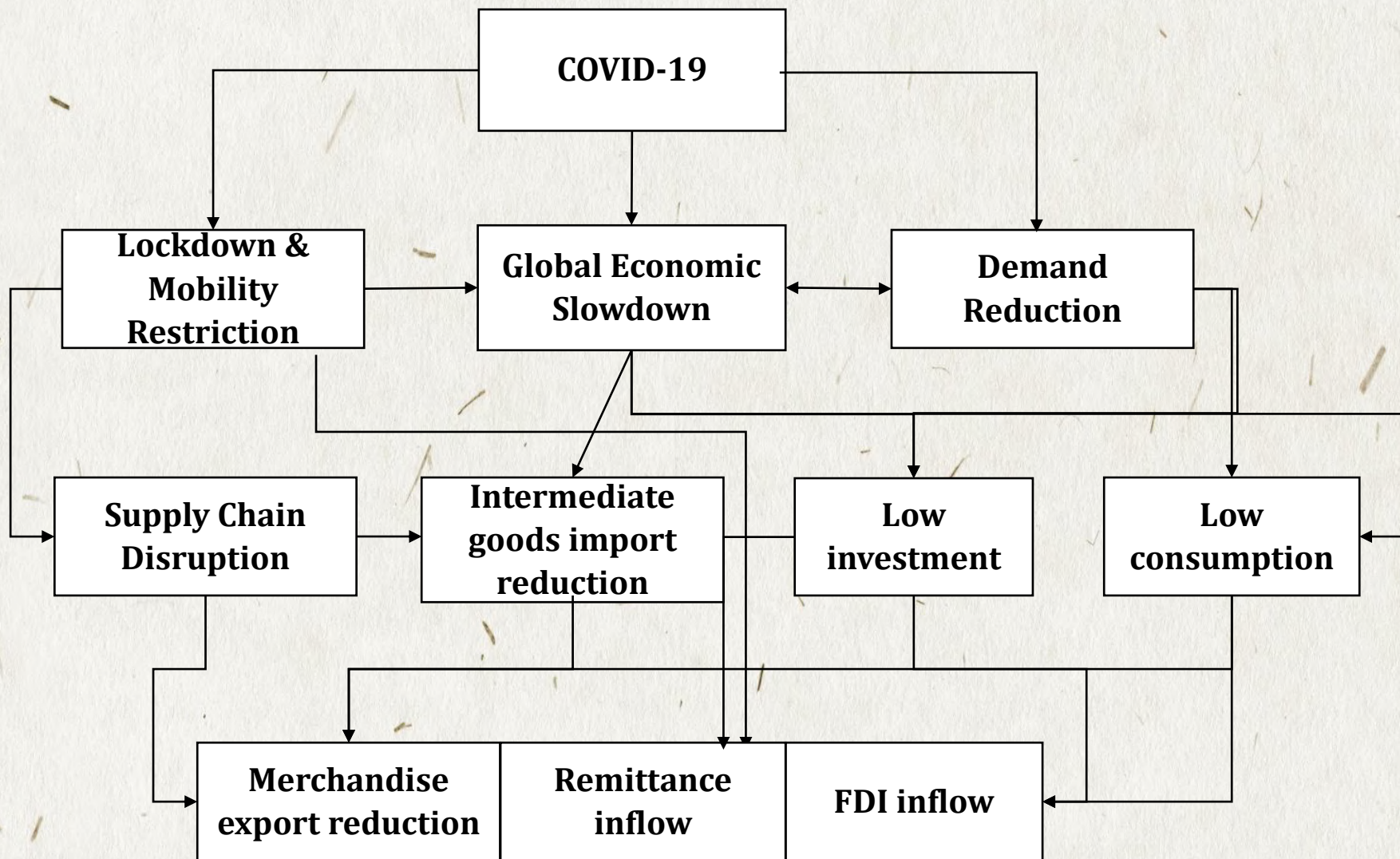


Acknowledgement

The presentation is based on a CPD special publication titled *COVID-19 and Bangladesh: Macroeconomic Impact and Policy Choices*, by Debapriya Bhattacharya, Towfiqul Islam Khan, Md Mursalin Hossain Rabbi.

Bhattacharya, D., Khan, T. I, & Rabbi, M. M. H. (2021). *COVID-19 and Bangladesh: Macroeconomic Impact and Policy Choices*. Dhaka: Centre for Policy Dialogue (CPD).

Nature of COVID-19 shock on the economy



Source: Authors' illustration

Impact on macroeconomic indicators

| Indicator | FY19 | FY20 | FY21 | FY22 |
|---|-------|-------|---------------------|----------------------|
| GDP growth (%) | 7.88 | 3.45 | 5.43 (p) | n/a |
| Private investment (as % of GDP) | 25.25 | 24.02 | 23.80 | n/a |
| Public investment (as % of GDP) | 6.96 | 7.29 | 6.96 | n/a |
| Growth of revenue collection (%) | 16.3 | 4.4 | 21.5 (up to May) | n/a |
| Implementation rate of public expenditure (%) | 84.3 | 80.3 | 55.1 (up to May) | n/a |
| Budget deficit as % of GDP | 5.5 | 5.6 | 6.2 (RB) | n/a |
| Growth of export earnings (%) | 10.5 | -16.9 | 15.1 | 24.3 (up to Nov) |
| Growth of import payments (%) | 1.8 | -8.6 | 19.7 | 47.6 (up to Sep) |
| Growth of net FDI inflow (%) | 47.8 | -42.5 | 17.3 | 49.3 (up to Sep) |
| Growth of inward remittance (%) | 9.6 | 10.9 | 36.1 | -21.0 (up to Nov) |
| Debt-GDP ratio (%) | 33.1 | 36.0 | 39.0 (RB) | n/a |

Source: Authors' compilation from various official sources

Impact on macroeconomic indicators *(contd...)*

- Decade-long progress and 5 years achievement in SDG of Bangladesh in several socio-economic indicators are in jeopardy
 - Poverty
 - Unemployment
 - Health & Nutrition
 - Education (net enrolment and completion rate)
 - Gender gap
 - Climate vulnerability
- Exacerbation of earlier negative trends (income inequality and youth unemployment) and emergence of new

The role of fiscal space

- The choice and limits of counter-cyclical expansionary fiscal policy
- The need for fiscal space
 - The room for additional resources in government's budget which allows the government to allocate the resources to the desired and required sector without risking the stability of the economy
- Scope for fiscal space enhancement
 - Additional domestic resource mobilisation
 - Reprioritising public expenditure structure
 - Review of subsidy allocations
 - Domestic borrowings from bank and other sources
 - External finances – grants and loans
 - Printing new currency i.e., seigniorage

Policy responses

- Movement restrictions in phases
- Additional mobilisation of foreign assistance
- Doling out of support measures (stimulus packages) in phases
 - **Monetary easing**
 - **Relief programmes**
 - **Tax breaks**
 - **Subsidised credit packages**

Issues threatening the effectiveness of the stimulus packages

- Predominantly liquidity induced
- Inadequate fiscal support compared to credit support
- A big chunk of fiscal support is from expansion of existing programmes
- Inefficiency in resource utilisation
- Low implementation (disbursement) rates, particularly to poor and smaller entrepreneurs
- Lengthy disbursement procedures through complex banking system (particularly for new and smaller entrepreneurs)
- Limited access due to information and coordination failure
- Inadequate coordination with non-state actors (NGOs and CSOs)
- Commercial banks are the major risk takers
- Traditional banking behaviour for women entrepreneurs
- Lack of transparency and poor governance

Policy simulations

- Economy-wide impacts are examined for two policies:
 - I. Simulation 1: Doubling government's transfers to five selected household categories:**
 - landless farmer
 - marginal farmer
 - small farmer
 - rural non-farm poor
 - low education
 - II. Simulation 2: A 50 per cent increase in government expenditure on health and education**
- The model assumes:
 - government savings, i.e. budget deficit, is flexible, and there are no changes in the tax rates
 - investment is savings driven
 - exchange rate is also considered to be fixed
 - capital and land are assumed to be fully employed but mobile
 - labour can be unemployed and mobile

Policy simulations *(contd...)*

- The paper uses the framework of a standard CGE model following Lofgren et al. (2002).
- A modified version of the Social Accounting Matrix (SAM) of 2012 for Bangladesh is used.
- The results of Simulation 1 and Simulation 2 policies are presented in three heads:
 - i. changes in macroeconomic variables**, including real GDP, fixed investment, export, import, revenue mobilisation, government expenditure and budget deficit
 - ii. changes in factor income** viz. unskilled labour, skilled labour, capital and land
 - iii. changes in real consumption** of the household groups

Policy simulation results

Results of Simulation 1 on macroeconomic variable

| Variables | Impact of Doubling government's transfers to five selected household categories |
|---|---|
| Real GDP (% change) | 0.1 |
| Export (% change) | 3.7 |
| Import (% change) | -0.9 |
| Government income (% change) | -0.5 |
| Government expenditure (% change) | 17.5 |
| Budget deficit as % of GDP (percentage points) | 1.4 |
| Fixed investment as % of GDP (percentage points) | -1.9 |

Source: Authors' estimation

Policy simulation results *(contd...)*

Results of Simulation 1 on Changes in factor income (%)

| Variables | Impact of doubling government's transfers to five selected household categories |
|------------------|---|
| Unskilled labour | 0.0 |
| Skilled labour | 0.5 |
| Capital | -0.4 |
| Land | 2.1 |

Source: Authors' estimation

Policy simulation results *(contd...)*

Results of Simulation 1 on Changes in real household consumption (%)

| Household | Impact of doubling government's transfers to five selected household categories |
|-------------------------|---|
| Landless Farmer | 5.2 |
| Marginal Farmer | 4.1 |
| Small Farmer | 2.8 |
| Large Farmer | 0.5 |
| Rural Non-Farm Poor | 3.0 |
| Rural Non-Farm Non-Poor | -0.2 |
| Low Education | 2.5 |
| High Education | 0.2 |
| All Households | 1.7 |

Source: Authors' estimation

Policy simulation results *(contd...)*

Results of Simulation 2 on macroeconomic variable

| Variables | Impact of 50% increase in government expenditure on health and education |
|--|--|
| Real GDP (% change) | 0.5 |
| Export (% change) | 0.5 |
| Import (% change) | -0.6 |
| Government income (% change) | -0.1 |
| Government expenditure (% change) | 10.9 |
| Budget deficit as % of GDP (percentage points) | 0.9 |
| Fixed investment as % of GDP (percentage points) | -1.0 |

Source: Authors' estimation

Policy simulation results *(contd...)*

Results of Simulation 2 on Changes in factor income (%)

| Variables | Impact of 50% increase in government expenditure on health and education |
|------------------|--|
| Unskilled labour | 0.1 |
| Skilled labour | 2.0 |
| Capital | -0.1 |
| Land | 0.4 |

Source: Authors' estimation

Policy simulation results *(contd...)*

Results of Simulation 2 on Changes in real household consumption (%)

| Household | Impact of 50% increase in government expenditure on health and education |
|-------------------------|--|
| Landless Farmer | 0.5 |
| Marginal Farmer | 0.4 |
| Small Farmer | 0.4 |
| Large Farmer | 0.4 |
| Rural Non-Farm Poor | 0.5 |
| Rural Non-Farm Non-Poor | 0.2 |
| Low Education | 0.4 |
| High Education | 1.0 |
| All Households | 0.4 |

Source: Authors' estimation

Policy simulation results *(contd...)*

- Limits of the fiscal expansion have dictated available incremental fiscal space of 1-1.5% of GDP
- Between the two expansionary fiscal policies, the 50 per cent increase in government expenditure on health and education has a larger positive impact on real GDP growth and export
- However, doubling the government's transfers to five selected household categories despite resulting in a larger budget deficit has a much significant positive impact on the real consumption of poorer households
- It is, however, to be noted that in both cases, the impacts on GDP, export and factor income except for capital are positive
- Hence, the expansionary fiscal policy at the time of the COVID-19 pandemic is expected to bring positive results for the economy

Policy outlook

- Bangladesh needed to pursue a countercyclical policy stance during the COVID-19 period where fiscal interventions could play a more significant role than the monetary instruments – a consensus on policy stance among the policy analysts
- Regrettably, the pursued policies followed this stance only partially!
- Indeed, the government did not use all the arsenal at its disposal!
- ***How relevant is it now in view of the emerging trends – both globally and nationally?***

Policy outlook *(contd...)*

- Most of the macroeconomic correlates are in the recovery trajectory but at a different pace
- Macroeconomic stability is no longer in a comfortable state –
 - rising commodity prices fueled by both international prices and unfavorable government policy
 - significant negative overall balance of payments leading to reduced foreign exchange reserve
 - volatile exchange rate
 - apparent shrinking fiscal space (indicated by the government during the upward revision of diesel and kerosene prices, amid absence of updated fiscal data)
- The global environment is still uncertain and volatile – fragmented economic recovery and demand in the large economies (also our major export destinations), steep rise of commodity prices, the emergence of new (omicron) COVID-19 variant

Policy outlook *(contd...)*

- Unfinished support agenda needs to be delivered – loans to SMEs, implementation of programmed social protection programmes
- It is perhaps also time to pull out the placed support measures and be prepared for its fallouts –
 - ending the moratorium on bank loan recovery and classification at a time of rising non-performing loans (NPL)
 - recovery of loans under stimulus packages
 - increased cost of investment due to probable rise of interest rates, rising commodity prices (including for capital goods) and pressure on wages
 - phasing out tax incentives

Policy outlook *(contd...)*

- The economy will need a recovery package 2.0 with distributive justice (i.e. supporting the marginalised people at a time of rising prices of daily essentials and considering their struggle during the pandemic such as lost income and savings along with increased debt)
- To this end, the trade-offs among conflicting policies will need to be taken into cognisance
- As the policy space is limited, the challenges of policymaking are more acute
- Lack of data (e.g., poverty, employment, inequality, fiscal position) will continue to hurt the design of policy package – the fear is with lack of data for these critical indicators, policies will continue where data is available (e.g., GDP and per capita income)
- At these difficult times, the government will need to revitalise lost reform and good governance agenda for the sake of delivering these policy agenda

Policy outlook *(contd...)*

- A targeted flow of fiscal resources to the more vulnerable households as well as to relatively smaller (and informal) enterprises will have more 'aggregate domestic demand augmenting' effect and protect the marginalised groups
- Mobilisation of resources – domestic and foreign – for underwriting expansionary fiscal policy is a challenge but may not be the binding constraint
- Ability to implement expanded public expenditure programmes including stimulus packages effectively – in quantitative and qualitative terms seems to be the binding constraints
- The macro approach has to be complemented with dedicated resource allocation and institutional support to counteract the accentuated trends of inequalities and marginalisation
- The expansionary fiscal policy has to be coupled with institutional and policy reforms for ensuring building back better

Thank You



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