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Concessional Financing for Development in Bangladesh

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Abstract

On July 1, 2015, the World Bank re-classified Bangladesh as a lower-middle income country. Hence, Bangladesh is expected to graduate from the World Bank's International Development Association (IDA) in the next few years and will then lose access to concessional financing from IDA and subsequently from other donors as well. This article examines the impact of this loss to concessional financing on Bangladesh to finance development, especially related to poverty reduction and social sector development. Following a brief review of the aid literature, it reviews the evolution of concessional aid to Bangladesh. The analysis moves then to a forward-looking impact assessment of losing access to concessional aid. The article also examines how well Bangladesh is prepared to replace foreign aid with domestic financing. The findings provide recommendations to donors and the Government of Bangladesh.

1 Introduction

A key milestone that impacts a country's ability to finance equitable development via official development assistance (ODA)[1] is the graduation from low-income country status to lower-middle income country status. This graduation leads to the gradual loss of access to highly concessional financing, especially from the International Development Association (IDA), the concessional lending arm of the World Bank. Due to substantial increases in Bangladesh's gross national income (GNI) per capita, the World Bank re-classified Bangladesh on July 1, 2015 as a lower-middle income country, which were at that point of time countries with a GNI per capita between US$1,046 and US$4,125.

With regards to the IDA's graduation process, Bangladesh became a so-called Gap country on July 1, 2018, as its GNI per capita has been above the operational cut-off for more than two consecutive years.[2] It will become a Blend country as soon as the World Bank considers Bangladesh to be creditworthy for non-concessional financing. Based on current guidelines and current GNI growth rates, Bangladesh is likely to graduate from IDA around June 30, 2023. However, the question is if Bangladesh will be ready to graduate or if it will join the list of countries that graduated prematurely from IDA.

The remainder of this article is structured as follows. The next section provides a review of the aid literature. Section 3 examines Bangladesh's external development finance portfolio from 1971 to 2016. Section 4 reviews where most of the aid has been spent in Bangladesh during the last ten years to deduct which sectors may be hurt most by losing access to concessional financing. It also focuses specifically on the impact of losing concessional financing from IDA. Section 5 examines how well Bangladesh is prepared to replace concessional financing with domestic government revenues. The last section provides some conclusions and recommendations.

2 Review of the Aid Literature

The impact of foreign aid is a highly disputed topic, at the international level as well as in the case of Bangladesh. While most of the academic literature was critical of the effectiveness of foreign aid during the last century, the seminal studies by Burnside and Dollar (2000) and Collier and Dollar (2002) found that foreign aid is effective if the recipient country has a strong and sound policy environment. However, subsequent studies, including especially by Rajan and Subramanian (2008) have challenged those results. Despite the continuing controversy within the global aid literature, there has

been a shift recently towards explanations under what circumstances aid is effective or ineffective. A forthcoming dissertation by Ramon (2019) shows that aid is effective after controlling for conflicts, debt overhangs, disasters and epidemics. Our own regressions across 64 developing countries came to the result that net ODA[3] contributed to GDP growth (with a significance level of at least 95 percent in two regression specifications) after controlling for the volatility in the terms of trade. Our results of Granger causality tests showed that the direction of causality is unidirectional from ODA to per capita income.[4]

With regards to the aid literature focusing on Bangladesh, the first seminal assessment of the impact of aid in Bangladesh has been provided by Rehman Sobhan (1982). He concludes that the impact of aid in Bangladesh had been negative. On the other hand, a comprehensive review by Rahman (1984) came to the conclusion that aid had an overall positive impact on growth and development in Bangladesh.[5] The subsequent aid literature has not only become more focused in terms of assessing specific impacts of aid in Bangladesh, the conclusions have overall become more nuanced.

2.1 Impact on Economic Growth

The largest number of aid studies focus on the impact of aid on macroeconomic effects, especially economic growth, which is critical because the impact of Bangladesh's graduating from aid on GDP growth is a major concern. However, these studies are overall inconclusive.

Quazi (2000) concluded that aid induces indirect positive effects on GDP growth through increased consumption demand, which offset much of the direct adverse effects of aid. Five years later, Quazi (2005) concluded that aid has marginal effects on GDP growth, but when aid is disaggregated into loans and grants, it is found that loans significantly raise GDP growth, while grants do not. Hossain (2014) finds that foreign aid has a positive effect on Bangladesh's economic growth, but that aid generates decreasing returns because of capacity constraint of Bangladeshi institutions to utilize the foreign aid effectively.

On the other hand, Obaydullah (2007) indicates that there is little evidence that foreign aid alone has contributed to economic growth in Bangladesh, mainly due to the poor policy environment and institutional constraints. Khatun (2018) concluded that aid provided to Bangladesh had no significant impact on economic growth. Dristy (2016) examines the impact of foreign aid on Bangladesh's economic growth before and after the signing of the Paris Declaration in 2005 and concludes that there is almost no change in the aid-growth relationship before and after adopting the Paris Declaration.

2.2 Impact on Poverty Reduction, Health and Education

Despite the overall inconclusive aid and growth literature, there is some indication that aid has been critical to reducing poverty and promoting social development, specifically in the health and education sector. Khatun (2018) concluded that health sector projects have benefitted from ODA support. Similarly, Obaydullah (2007) finds that the sectoral allocation of foreign aid to Bangladesh has been broadly consistent with a strategy to effectively reduce poverty and increase human well-being, which is also consistent with the vast project evaluation literature. Examining the degree of Bangladesh's dependency on foreign aid, Hasan (2011) concludes that even though the flow of aid has declined as percentage of GDP or investment, the contribution of ODA is still very significant in different development projects, especially in health, education and physical infrastructure, and hence, the influence of donors in policy matters has paradoxically increased significantly.

3 Bangladesh's External Development Finance Portfolio

There are a variety of different external sources that might finance development. For analytical purposes, we divide external development finance into public and private resources. External public resources are provided to the Government of Bangladesh, independent on if they come from another government, an international organization, or external private sources (like foreign commercial banks loans). Within the category of public external resources, we differentiate between concessional and non-concessional resources.[6] We first focus the analysis of this section on the flows of public external resources, especially concessional resources (that is, ODA), before examining the flows of some private external resources.

3.1 Recent Trends in Public External Development Finance

Recent Trends in Public External Development Finance from Official Creditors

Given that IDA has been the largest multilateral development bank providing development finance to Bangladesh, we start with the examination of development finance provided by IDA. Figure 1 shows the flows of concessional funds (in terms of gross

disbursements) from IDA from 1971 to 2016. As the left panel of Figure 1 shows, despite some considerable volatility in aid disbursements from IDA, there is a clearly upward trend since 2009. In 2016, IDA disbursed US$1.05 billion to Bangladesh. The right-hand panel of Figure 1 shows IDA's disbursements as a percent of GNI. Despite the relatively high volatility, it shows a clearly declining trend since 1986, which is due to Bangladesh considerable growth. In 1986, IDA disbursements reached 1.5 percent of GNI. During 2013-2016, IDA disbursements were between 0.42 and 0.45 percent of GNI.

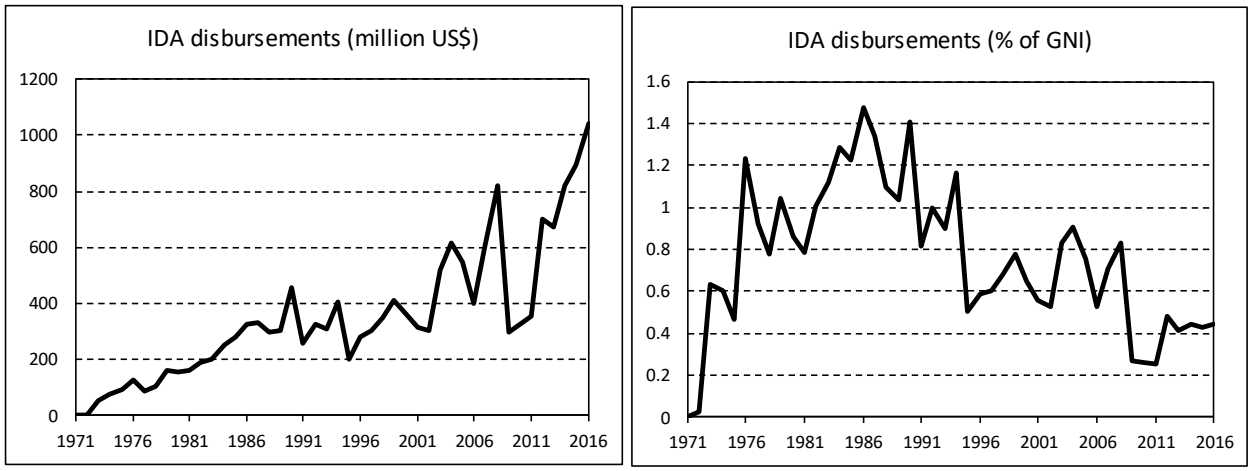

Figure 1: Disbursements of ODA from IDA

Source: Authors' estimates based on World Bank (2018a) database.

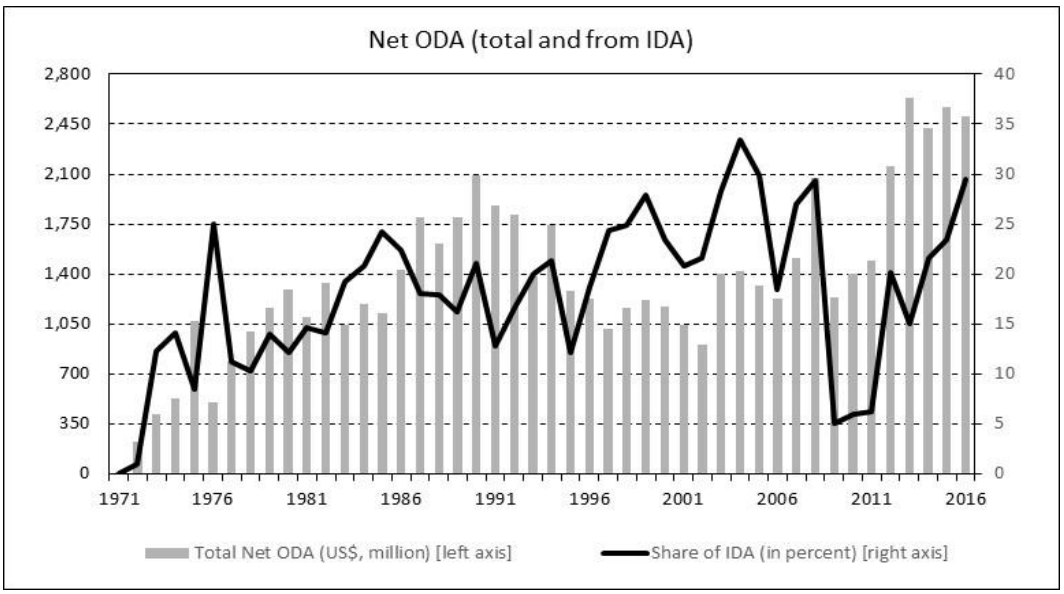

Figure 2: Total Net ODA and IDA's Share in Total Net ODA

Source: Authors' estimates based on World Bank (2018a) database.

Using the left vertical axis of Figure 2, the grey bars show total net ODA in million US$ from 1971 to 2016. Despite some volatility, total net ODA shows an increasing trend from 1971-1990; then a decreasing trend from 1990-2002, after which it shows another increasing trend from 2002-2008. It then plummeted in 2009, after which total net ODA shows once again an overall increasing trend until reaching an all-time high in 2013, and a gradual decline since 2013.

The black line of Figure 2 shows that IDA's share in net ODA has been highly volatile throughout the 1971 to 2016 period, reaching a maximum of 33.5 percent in 2004 and a minimum of 5.1 percent in 2009. IDA's share in total net ODA increased over time, until it decreased sharply in 2010, but increased subsequently, reaching 29.5 percent in 2016. The key point of Figure 2 is that ODA has been high within the last few years (in nominal terms), including from IDA, and that a forthcoming graduation from IDA would constitute a considerable shock.

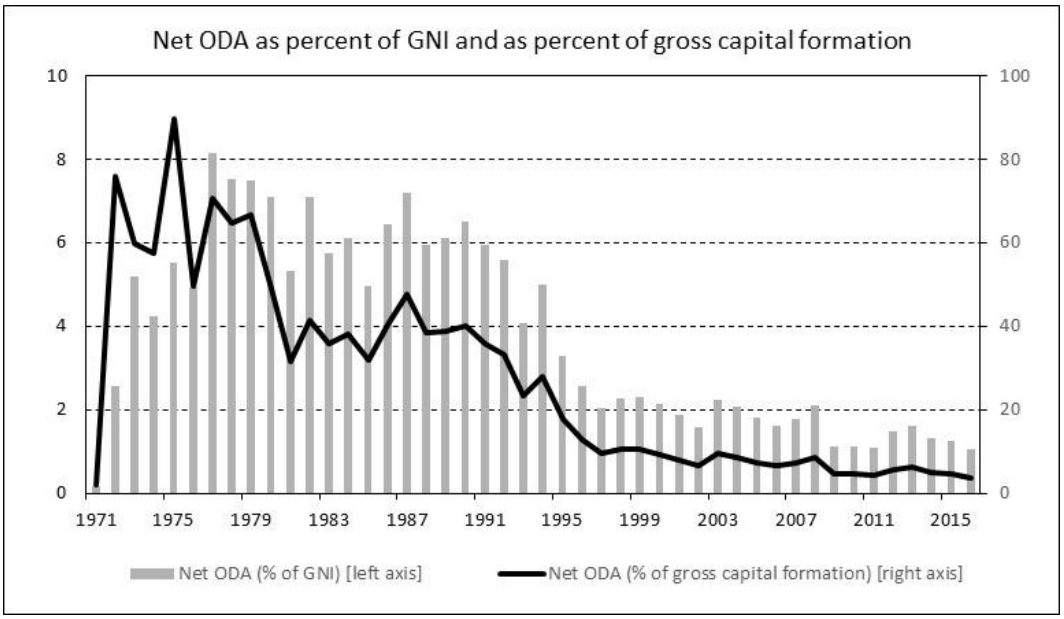

Figure 3: Net ODA as percent of GNI and as percent of Gross Capital Formation

Source: Authors' estimates based on World Bank (2018a) database.

Figure 3 shows net ODA as a percent of GNI (the grey bars) and as a percent of gross capital formation (the black line). As a percent of GNI, net ODA reached a maximum of 8.2 percent in 1977, after which it mostly decreased, reaching a minimum of 1.1 percent in 2016. As a percent of gross capital formation, net ODA reached a maximum of 89.6 percent in 1975, after which it mostly decreased, reaching a minimum of 3.8 percent in 2016. However, consistent with the assessment by Hasan (2011), it should be stressed that despite the fact that aid has declined as percentage of GNI or as a percent of gross capital formation, ODA is still very significant in different development projects, especially in health and education, as will be examined in more details in Section 4.

Comparing the data provided in Figures 2 and 3, it is clear that while net ODA is currently at about its maximum level in nominal terms, it is currently at its lowest level in percentage terms of GNI and gross capital formation. This seemingly contradiction is due to Bangladesh's high economic growth rate, which has reduced the relative importance of aid in Bangladesh since the late 1970s.

Recent Trends in Public External Development Finance from Private Creditors

Public and publicly guaranteed (PPG) debt from private creditors did – due to high interest rates and short maturity periods – not contribute to financing development in Bangladesh. The cumulative net transfer from PPG debt from private creditors amounted to negative US$173.1 million from 1971 to 2016. In addition to having been overall negative, Figure 4 shows that net transfers from private creditors have been small, ranging from a minimum of negative US$37.8 million in 1989 to a maximum of US$ 45.7 million in 1986. In comparison, net transfers on PPG debt from multilateral creditors ranged from a minimum of zero US$ in 1971 to a maximum of US$ 1.23 billion in 2016. Figure 4 also shows that net transfers on bilateral debt have been substantial from 1971 to 1990, but then turned either negative or insignificant, until turning again significantly positive since 2012.

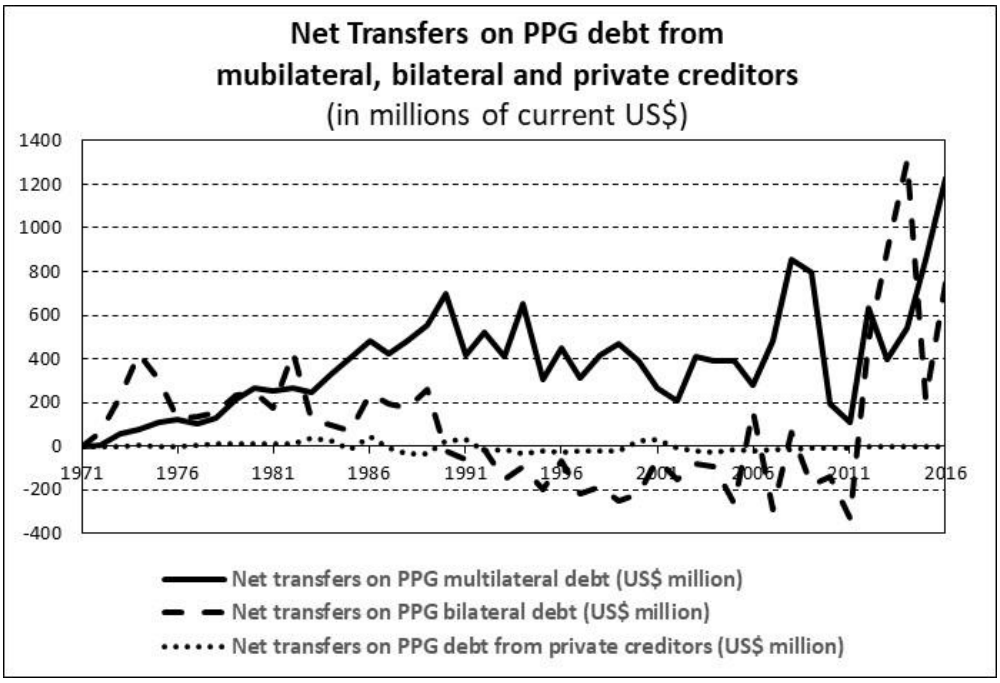

Figure 4: Net Transfers on PPG Debt from Multilateral, Bilateral and Private Creditors

Source: Authors' estimates based on World Bank (2018a) database.

It should be stressed that non-concessional debt financing is not an alternative to concessional resources as non-concessional loans have a negative impact on public debt sustainability. Tashfique (2019) provides some details on how major development partners have started to readjust their terms and conditions by either increasing the interest rate or by shortening the maturity and grace period in view of Bangladesh's recent elevation to lower-middle income country status. Although Bangladesh has gradually transformed itself from an aid-dependent to a trade-dependent economy, the transformation may well reverse if policymakers undermine the downsides of foreign aid with stringent conditionality and higher costs. Tashfique (2019) warns that foreign aid with an unmanageable loan component will not only fail to serve its development purpose but also worsen the debt situation. We are therefore not examining the replacement of aid with non-concessional debt further.

3.2 Recent Trends in Private External Development Finance

External private resources are provided to Bangladeshi individuals (like remittances or donations) and/or to the Bangladeshi private sector (like loans from foreign commercial banks, private bonds raised in foreign currency, foreign direct investment (FDI) and portfolio investment). With the exception of remittances and private donations, private external resources are typically never concessional. While all private external resources may support the Bangladeshi economy, private sector loans, FDI and portfolio investment are typically not considered to be development finance as they are not provided to the Bangladeshi government.

Figure 5 shows the evolution of private external flows that might finance development in Bangladesh, including transfers on private non-guaranteed (PNG) external debt, net foreign direct investment (FDI) inflows, net portfolio equity investments, and remittances, though we also provide the data for net ODA received to get an idea on the relative size of public and private external development finance.

- The first year the World Bank (2018a) has data on private non-guaranteed (PNG) external loans is 2007, when net transfers on PNG debt amounted to 0.14 percent of GDP. Though such flows increased in subsequent years, the maximum was reached in 2014, when net transfers on PNG debt amounted to 0.52 percent of GDP. These flows then decreased in 2015 and even turned for the first time negative in 2016.
- Despite going back to 1972, net FDI inflows to Bangladesh have remained insignificant until the

late 1990s, when they reached 0.4 percent on GDP. They then increased to 0.7 percent of GDP during 2000-2009, and finally to 1.3 percent of GDP during 2010-2016.

- Data for net portfolio equity investments exist since 1983, but the amounts have been insignificant for most of the years, reaching an all-time high of 0.31 percent of GDP in 1994.
- As Figure 5 clearly shows, the only significant private external flows to Bangladesh have been private remittances, which have increased from 0.19 percent of GDP in 1996 to an all-time high of 10.6 percent in 2012. Though the flow of remittances has continued to increase in nominal terms until 2015, they have decreased as percentages of GDP, reaching 6.1 percent of GDP in 2016.

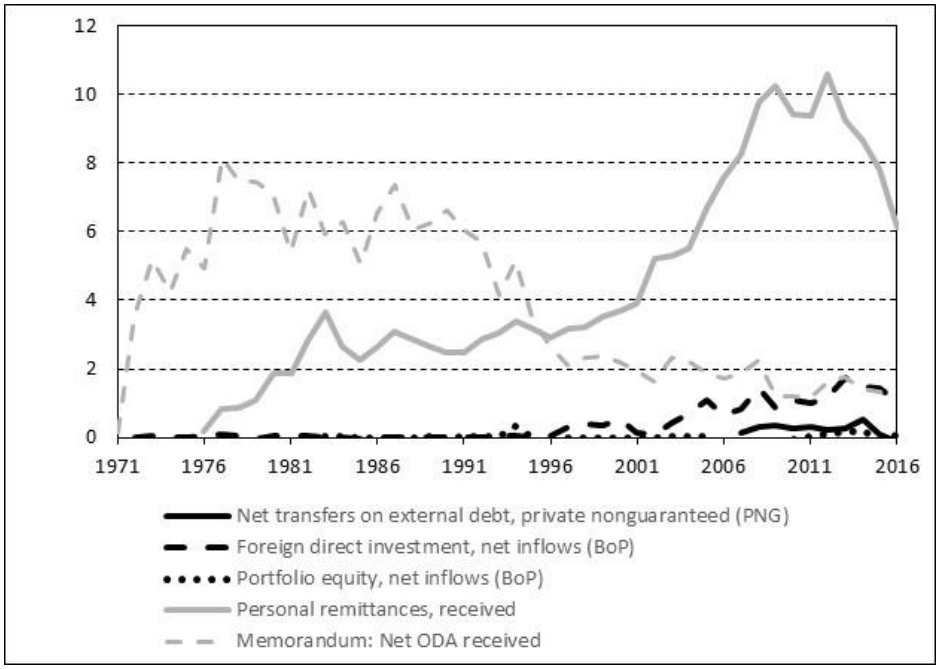

Figure 5: Net Transfers on Private Non-guaranteed (PNG) External Debt, FDI, Portfolio Equity Investment, and Remittances (percent of GDP)

Source: Authors' estimates based on World Bank (2018a) database.

Finally, even though some of the resources from so-called public-private partnerships come from domestic enterprises, the majority of Bangladesh's public-private partnerships have involved foreign investors. According to the World Bank's Private Participation in Infrastructure Database,[7] there have been 65 such projects totaling to US$5.5 billion from January 1, 1990 to June 30, 2018. The large majority of these public-private partnerships have been in the electricity sector, which accounts for 88 percent of total investment via public-private partnerships. Within the last five years (June 30, 2013 to June 30, 2018), there were 11 public-private partnerships projects, totaling to investments of US$2.0 billion, which is equivalent to about 0.14 percent of GDP. It should be stressed that not all of these funds for public-private partnerships are external and that some are provided as publicly guaranteed loans, some as FDI, and in some cases even as ODA. As detailed in Romero (2015), public-private partnerships have been controversial given that they were many times non-transparent, anti-poor, and ultimately a liability for the public sector. While public-private partnerships should be pursued, they have to be scrutinized thoroughly on their impact on poverty and inequality as well as their potential financial liability for the public sector.

4 Forward-looking Impact Assessment

This section examines some of the key consequences the reduced access to aid may have. It first reviews the sectoral allocation of ODA over time. It then examines the impact of losing concessional financing specifically from IDA on the education and health sectors.

4.1 Recent Trends in the Sectoral Allocation of ODA

Figure 6 shows the disbursements of total ODA and total sector allocable ODA, respectively as black and grey bars.[8] It shows that disbursements of total ODA have decreased marginally from 2008 to 2009, then increased from 2009 to 2013, after which it decreased again until it spiked in 2017. The percentage of sector allocable ODA[9] in total ODA (shown by a black line) jumped from 77.1 percent in 2007 to 87.1 percent in 2008, after which the percentage increased more moderately, reaching a maximum of 96.3 percent in 2013. It then declined in the subsequent years, reaching 86.2 percent in 2017. Despite the recent decline, it is clear that most ODA to Bangladesh has been disbursed either to a specific sector or multi-sector and cross-cutting, averaging at 89.9 percent during 2008-2017.

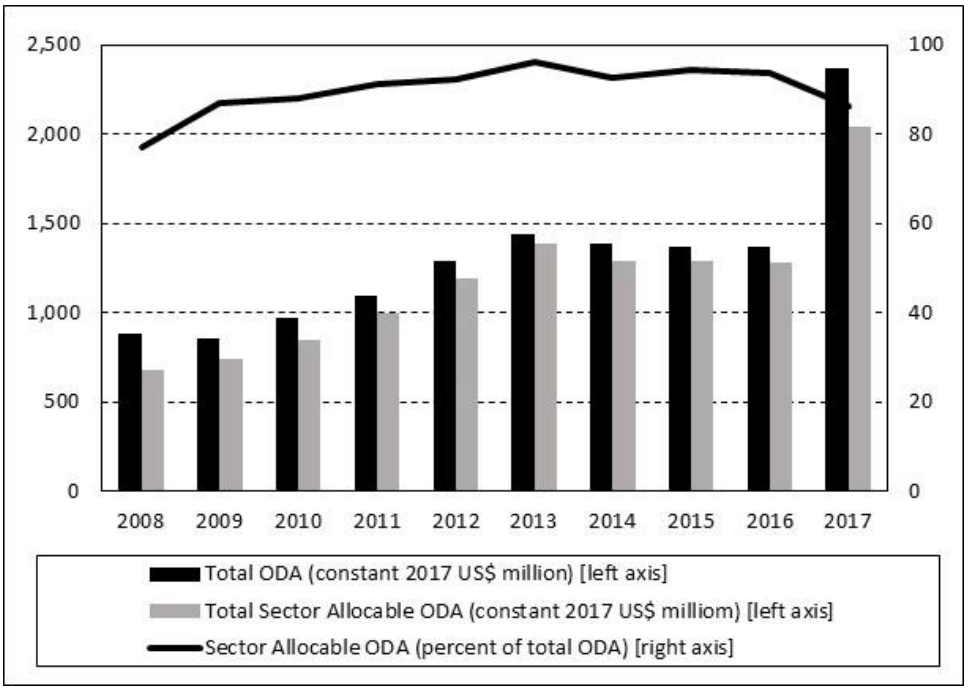

Figure 6: Disbursements of Total ODA and Sector Allocable ODA

Source: Authors' estimates based on OECDStat.org, extracted on July 24, 2019.

Following the sector classification of the Organisation for Economic Co-operation and Development (OECD), Figure 7 shows the disbursements of ODA to three specific sectors: a) social sector, b) economic infrastructure and services, and c) production sectors, as well as ODA disbursed to more than one sector (multi-sectors or across sectors). It shows that excluding the 2017 spike to economic infrastructure and services, which is also the source for the 2017 spike in overall ODA disbursements, the sectoral allocation of ODA to Bangladesh has been relatively stable during the last 10 years. Traditionally, most of ODA provided to Bangladesh has been to social sectors (further details below), which averages to US$550 million per year during 2008 to 2017, or 49.6 percent of all sector allocable ODA. And keeping in mind that 89.9 percent of all ODA has been allocable to sectors, this implies that 44.6 percent of all ODA provided to Bangladesh during 2008-2019 has been to social sectors.

The second largest amount of ODA has been disbursed for economic infrastructure and services. During 2008 to 2017, this averaged to US$356.8 million per year or 26.8 percent of all allocable ODA (or 24.0 percent of all ODA). On the other hand, during 2008 to 2017, ODA disbursed to production sectors averaged to only 6.7 percent of all allocable ODA, while the average percentage for multi-sectors or across sectors amounted to 16.9 percent. Clearly, with nearly 50 percent of all allocable ODA going to social sectors, the social sectors are likely to suffer the most due to the forthcoming reduction in ODA. The private sector may pick up some of the decline of ODA to infrastructure projects, however there is typically little appetite by the private sector to invest in education and health services for the poor.

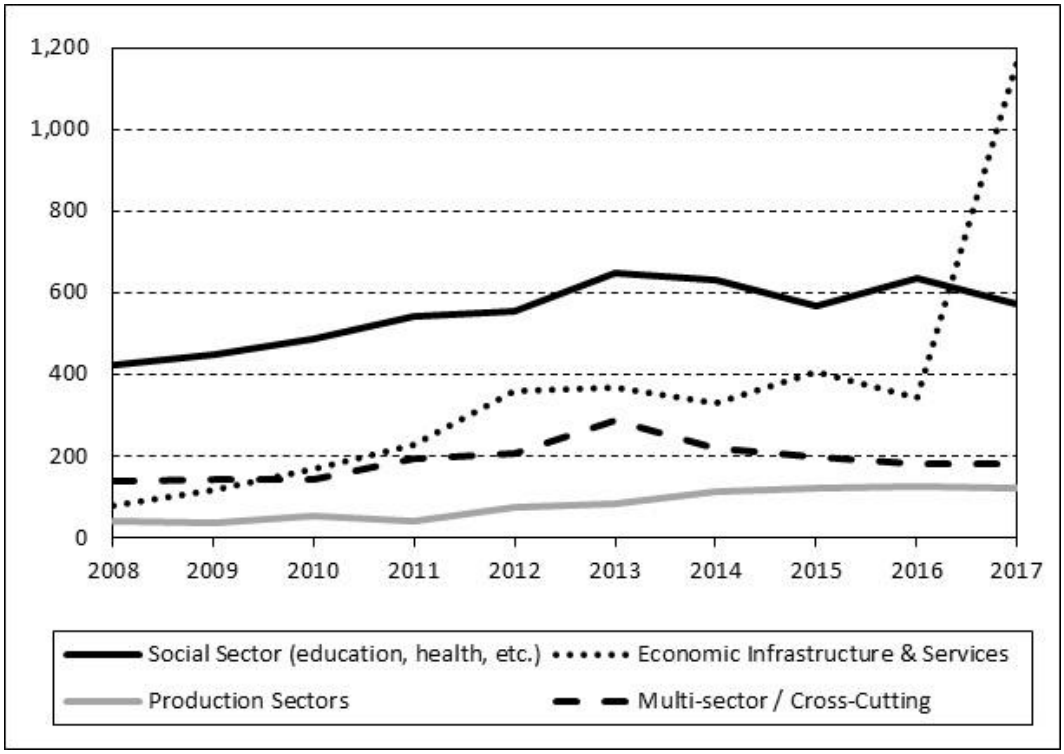

Figure 7: Sectoral Allocation of ODA (in constant 2017 US$ million)

Source: Authors' estimates based on OECDStat.org, extracted on July 24, 2019.

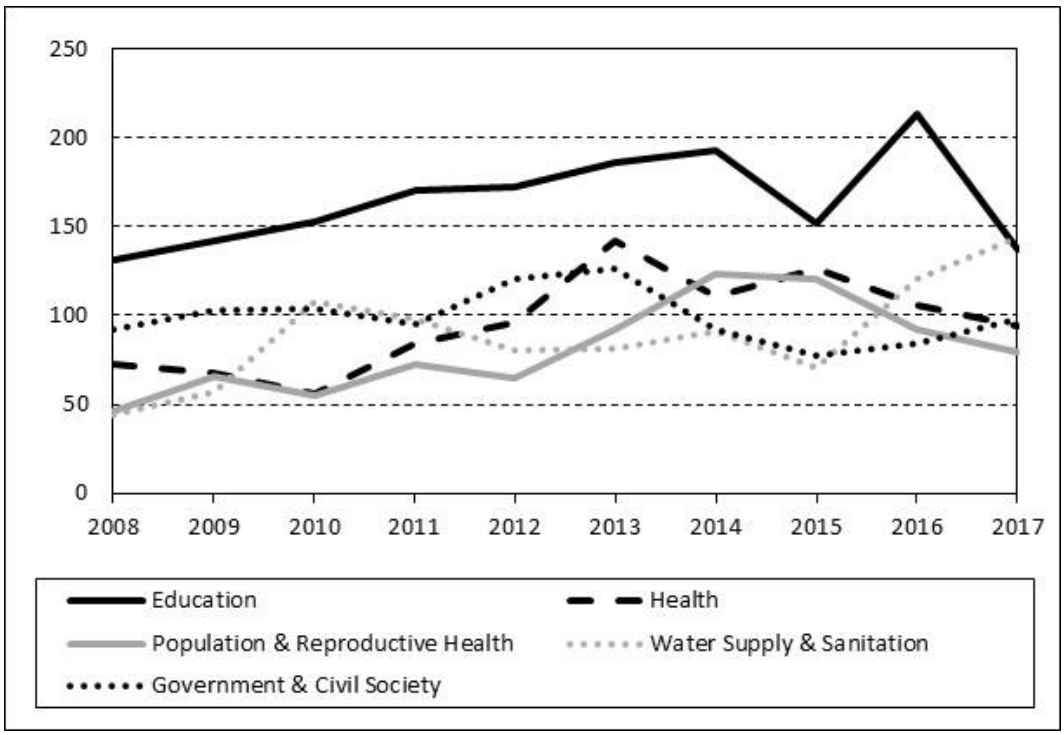

Figure 8: ODA Disbursements within the Social Sector (in constant 2017 US$ million)

Source: Authors' estimates based on OECDStat.org, extracted on July 24, 2019.

Furthermore, as is detailed in Figure 8, the education sector has consistently been the social sector to which most of the ODA has been disbursed, averaging to US$164.9 million per year during 2008 to 2017, or 30.0 percent of all ODA disbursed to social sectors.[10] The next three social sectors are relatively close to each other in terms of ODA disbursements: the government and civil society sector received an average of US$99.2 million per year (or 18.0 percent of all social sectors), the health sector received an average of US$95.5 million (or 17.4 percent), and the water supply and sanitation sector received an average of US$89.3 million (or 16.2 percent). The fifth most important sector (in terms of ODA disbursements) during 2008 to 2017 has been population policies/programs & reproductive health, for which an average of US$81.1 million (or 14.7 percent of all social sector ODA) has been disbursed.

4.2 How Important Has IDA been in Key Social Sectors?

While most of the bilateral aid provided to Bangladesh is spent in the economic infrastructure sector, most of IDA's aid to Bangladesh has been allocated more evenly between social and economic sectors.[11] As columns 2 and 3 of Table 1 show, IDA has been the largest provider of aid to Bangladesh's education sector, totaling US$108 million (based on 2016 commitments), which is equivalent to 32 percent of all donor commitments in the education sector. The United Kingdom had committed US$97 million (28 percent), while South Korea had committed US$77 million (23 percent). But given that Bangladesh is now a middle-income country, most of these donors will sooner or later reallocate their aid to poorer countries.

While IDA has been significant to fund education programs in Bangladesh, columns 4 and 5 of Table 1 shows that IDA has been even more significant in Bangladesh's health sector, contributing US$150 million (based on 2016 commitments), which is equivalent to more than half (52 percent) of all donor commitments in the health sector in 2016. The United States has been the second largest donor to Bangladesh's health sector, with a commitment of US$90 million or 31 percent of all donor commitments.

In conclusion, with IDA being the far largest donor in the education and health sectors, the loss of concessional financing from IDA may affect these sectors negatively if no compensating transition plans are made to fund these programs in the future. While some of the projects financed in the past by IDA may be financed via loans from the International Bank for Reconstruction and Development (IBRD), IBRD financing is not concessional, and there is therefore less interest by the Bangladeshi government to continue these projects.

Table 1: Donor Contributions in the Education and Health Sector (based on 2016 commitments)

Donor Contributions in the Education and Health Sectors				
	Education		Health	
	USD million	Donor's share (in percent)	USD million	Donor's share (in percent)
IDA	108	32	150	52
United Kingdom	97	28	0	0
United States	2	1	90	31
Korea	77	23	2	1
Germany	21	6	0	0
Japan	7	2	1	0
France	2	1	0	0
Canada	0	0	11	4
European Union	0	0	7	2
WHO	0	0	7	2
Other donors	27	8	17	6
Total	341	101	285	98

Source: OECD DAC (2018) Table 4.3.8 and Table 4.3.12

According to the World Bank (2018c), decades of IDA financing has contributed to the achievement of significant results across a range of sectors, including (among many others, the following items are some illustrations):

- an increase in net enrollment rate at the primary school level from 80 percent in 2000 to above 90 percent in 2015;
- a 40 percent reduction in maternal mortality from 194 deaths per 100,000 live births in 2010 to 320 deaths in 2000;
- a reduction in fertility from around 3.3 children per woman during the 1990s to 2.3 children per woman in 2014;
- 13,006 functioning community clinics in 2014, with 64 percent of pregnant women receiving Ante Natal Care (ANC) from a medically trained provider in 2014, up from 53 percent in 2007;
- 800 km of new roads paved, 4,500 km rural roads in 26 districts maintained, and 47 km of rural waterways dredged; and
- 1.1 million people gaining access to clean water in rural areas.

However, as was already detailed in the review of the aid literature above, how much of these results can indeed be attributed to ODA remains controversial.

5 Replacing Concessional Financing with Domestic Financing

There is a broad agreement that it is critical to replace concessional external financing not with non-concessional external or domestic debt, but via increasing domestic revenues. This section will shed some light on how well Bangladesh is prepared to replace concessional financing with government revenues by reviewing government revenues, especially taxes.

One of the earliest comprehensive reviews of Bangladesh's tax system was a three-volume World Bank (1989) report, which laid out a medium-to-long term agenda for reforming Bangladesh's tax system into an elastic, efficient and equitable instrument of domestic resource mobilization. However, little if not nothing of this agenda seems to have been implemented. During 2007-2016, Bangladesh's government revenues amounted to an average of 10.2 percent of GDP, which is the lowest in the world the average government revenue for the 38 low-income countries with similar data is 17.6 percent.[12]

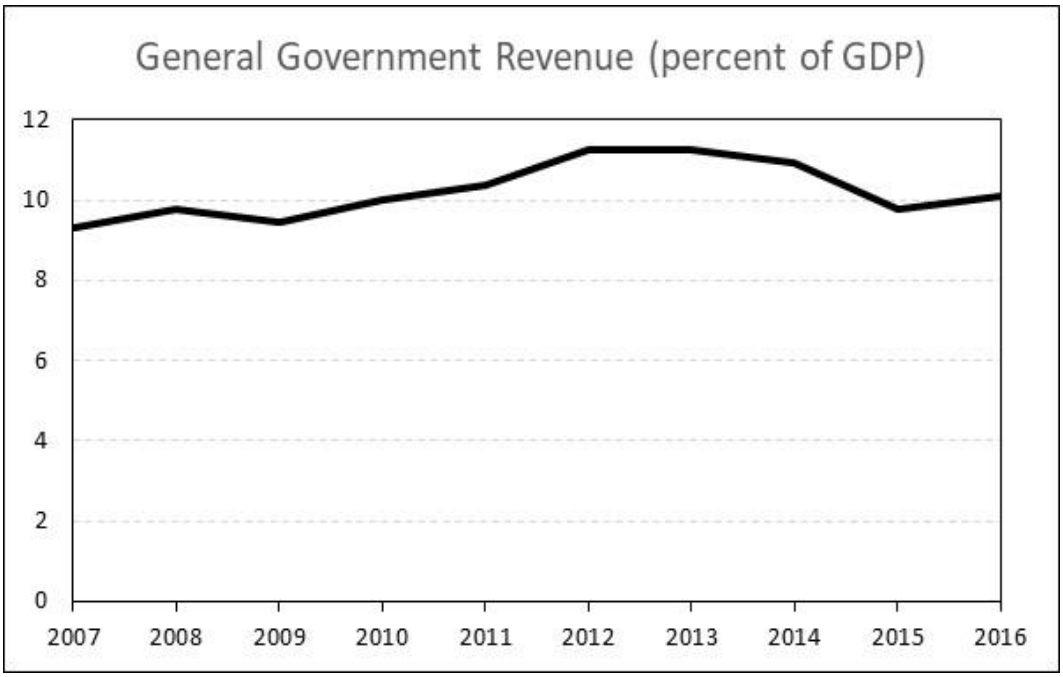

Figure 9: Evolution of General Government Revenue (percent of GDP) in Bangladesh, 2007-2016

Source: Authors' estimates based on combining data provided in IMF (2016) and IMF (2018).

As Figure 9 shows, though there has been some progress in increasing the government revenue-to-GDP ratio from 2009 to 2012, the ratio has been declining from 2012 to 2015, and it then increased only marginally from 9.8 percent in 2015 to 10.1 percent in 2016. Sushasoner Jonny Procharavizan (SUPRO) and Oxfam Bangladesh (2015) conclude that the narrow tax base, widespread exemptions, and administrative inefficiencies are the main factors behind the low tax to GDP ratio in Bangladesh. Furthermore, they stress that these factors also explain why tax reforms over the last decades have not brought about significant changes in Bangladesh's tax efficiency and productivity. The overall weakness of the policy framework, which is characterized by an enormous range of exemptions, incentives and special regimes. This directly lowers tax revenues, complicates tax administration, undermines equity in the system and introduces significant scope for officials to exercise discretion.[13]

Rahman and Yasmin (2008) estimate the revenue losses derived from different categories of taxpayers who use Bangladesh's Self-assessment System. They find that the revenue loss due to these taxpayers' noncompliance with income laws is a growing problem and that Private Ltd Companies and Public Ltd Companies contributed significantly to accelerating the problem during 2000-2004. They conclude that the tax evasion issue is critical in Bangladesh.

Besides income tax evasion, one of the main reasons for Bangladesh's low government revenue-to-GDP ratio is that Bangladesh has not yet been able to adopt a broad-based value-added tax (VAT). Saleheen and Siddiquee (2013) examine and analyze the nature of deviations and distortions in Bangladesh's VAT system. They argue that Bangladesh's VAT, which was introduced in 1991 to maximize tax revenues, has deviated significantly from standard and international best practices. Furthermore, they argue that most of the deviations have their roots in the excise system of taxation that the VAT has replaced and, while some of them produce ad hoc benefits in terms of generating revenue and easing compliance, most of them defeat the core principle of the VAT. Overall, the objective of the VAT to evolve as an efficient tool for maximizing tax revenues remained elusive.

While a new law for a broader VAT had been passed in the VAT Act of 2012, its implementation has been postponed more than once, mostly due to political resistance from the business sector and some civil society organizations that had criticized it as being a regressive tax that will hurt the poor. Hossain (1994) examines the distributional implications of different value-added tax (VAT) schemes in Bangladesh. He concludes that a uniform VAT is regressive in its impact on the income of different households. He therefore suggests an alternative policy package, consisting of a basic rate of VAT with exemptions for certain commodity groups, which would have superior welfare consequences than the uniform VAT.

Finance Minister Muhith had proposed a uniform 15 percent VAT rate in the budget for 2017-18 fiscal year, but Prime Minister Sheikh Hasina suspended it for two more years. At the IMF Annual Meeting of 2017, Finance Minister Muhith revealed the plan to implement the new VAT law with two thresholds: one from 7 to 10 percent and the other 15 percent (instead of the uniform rate of 15 percent), to be implemented in 2020.[14]

In FY2018 and FY2019, VAT tax revenues averaged to 40.0 percent of total tax revenues, while import tariffs averaged to 32.9 percent and income taxes to 27.1 percent.[15] Furthermore, due to lowering the source tax on export proceeds from businesses (excluding jute) from 1.0 percent to 0.65 percent in September 2018, and new VAT waivers to sectors such as liquified natural gas, shipping and stock brokers, the July-November 2018 tax revenue were 21.6 percent below the target.[16]

Khan (2018) examines the potential of the personal income tax in Bangladesh. One of the many findings of the study is that only about half of the about 3.4 million individuals that had a Tax Identification Number as of May 2018 have submitted income tax returns. Another key finding is that about 90 percent of the returns submitted in recent years have been self-assessed. Hence, there seems to be a considerable potential to increase revenues from the personal income tax if either more Bangladeshis come forward voluntarily to pay their due taxes or the government enforces existing personal income tax codes.

Akhand (2015) points out that several tax compliance approaches have been designed to improve the tax compliance of large corporate taxpayers. For example, in many tax administrations, specific taxpayer units have been set up to closely monitor the assessment and collection of revenues from large corporations. Using original survey data, Akhand finds that finance sector corporations achieve the highest compliance in return filing, manufacturing sector corporations achieve the highest compliance in payment, while service sector corporations achieve the highest compliance in reporting. These differences across sectors show that there are options to increase tax revenues by bringing all sectors to the same level of compliance.[17]

Even if Bangladesh will be able to increase government revenues, the question is then if these increased revenues will be focused on poverty reduction. As stated in Khatun, Khan and Nabi (2012, p. 32): "While effectively crafted fiscal policy and/or government budget certainly could reduce poverty, regrettably Bangladesh's fiscal policies emphasize more

on fiscal stability than on empowering the poor. (…) Nevertheless, the recent effort of collecting incremental tax revenue in the form of direct tax (income tax) at an accelerated rate compared to indirect tax can be considered as a positive trend."

On July 7, 2019, eminent Bangladeshi economists warned that failure in meeting the revenue targets could put Bangladesh into a debt trap. One of these economists, Dr. Ahsan H. Mansur, said that the government is implementing most of the mega projects through borrowing from external sources. For example, the Rooppur Nuclear Power Plant project is estimated to cost around US$13 billion, which will be borrowed from outside. This project alone would increase the foreign debt-GDP ratio by around 50 percent.[18]

Given that the VAT tax is indeed regressive (i.e., hurting the poor the most), the Bangladesh government may think of alternative progressive options, including a tax on real estate property. Given the massive increase in real estate values in recent years in Bangladesh, a real estate property tax could raise significant resources. Furthermore, instead of having a nonconvertible Taka, which pushes Taka to dollar transactions to a booming black market, an appropriately set low tax rate would eliminate most illegal currency transactions, reduce currency speculations, and still raise urgently needed tax revenues.

6 Conclusions and Recommendations

Bangladesh's IDA graduation is positive news since it reflects decades of significant GDP growth. Indeed, Bangladesh has experienced rapid economic growth in the last 16 years (averaging 5.87 percent from 2000-2016), characterized by rising average incomes and a steady and significant fall in the number of people living in poverty. From 2000 to 2010 (which is the last year such data is available in World Bank (2018a)), more than 4.8 million people have been lifted out of extreme poverty in Bangladesh, defined as living below $1.90 a day, adjusted for differences in purchasing power parity of 2011 (2011 PPP).

Bangladesh's Human Development Index increased from 0.47 in 2000 to 0.58 in 2015. Bangladesh has also achieved most of the Millennium Development Goals. However, despite all this progress, and assuming the same rate of poverty reduction as from 2005 to 2010, by the time Bangladesh may graduate from IDA, nearly 10 percent of the population will still live in extreme poverty (below PPP$1.90-a-day) and nearly 50 percent of the population will still live in poverty (below PPP$3.20-a-day).[19]

Our review of the sectoral allocation of ODA has shown that during 2008-2017, nearly 90 percent of ODA to Bangladesh has been disbursed either to a specific sector or multi-sector and cross-cutting. Among this sector allocable ODA, 49.6 percent has been disbursed to social sectors. Among social sector ODA, 30.0 percent went to the education sector, 18.0 percent to the government and civil society sector, 17.4 percent to the health sector, and 16.2 percent to water supply and sanitation. This seems to indicate that the forthcoming decrease in ODA will likely hurt the social sectors most. Further supporting this argument is the fact that IDA has been the largest donor to Bangladesh's education and health sector. Hence, the loss of access to concessional financing from IDA may cause considerable challenges and risks to these sectors in the near future.

There is an urgent need to rethink criteria for graduation from IDA due to the challenges Bangladesh will face with losing access to concessional development finance relatively abruptly and achieving the Sustainable Development Goals. The IDA graduation process should not only be much longer, the reduction in concessional financing should be more gradual. Donors like the World Bank are promoting various adjustments, including boosting domestic resource mobilization for public development projects. However, as our analysis of the recent tax revenues has shown, Bangladesh is not yet prepared to compensate the loss in donor-funding by domestic public resources.

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Endnotes

1. Official development assistance (ODA) consists of disbursements of loans made on concessional terms and grants by official agencies of the members of the Development Assistance Committee (DAC), by multilateral institutions, and by non-DAC countries to promote economic development and welfare in countries and territories in the DAC list of ODA recipients. It includes loans with a grant element of at least 25 percent (calculated at a rate of discount of 10 percent); see World Bank (2018a).
2. See World Bank (2018b).

3. Net ODA is total ODA (see footnote 2) minus repayments of principal on loans that were provided on concessional terms.
4. The details of these regressions and Granger causality tests are available upon request.
5. Further details on these and other early contributions can be found in Gunter, Rahman and Rahman (2010).
6. Concessional resources are provided either via grants or via loans with an interest rate below the market interest rate. As detailed in footnote 2, concessional resources qualify as ODA if they are provided either as a grant or as a loan with a grant element of at least 25 percent (using the rules as they have been in place the last few decades). On the other hand, non-concessional public resources are non-concessional loans (from either foreign governments, international organizations, or foreign commercial banks) or any sovereign bonds issued by the Bangladeshi government. While there have been discussions of Bangladesh issuing such bonds, no external sovereign bond has so far been issued by the government of Bangladesh.
7. https://ppi.worldbank.org/data; accessed on December 27, 2018.
8. Given that this data is only available in either gross disbursements or based on donor commitment, we examine gross disbursements of ODA, which is closer to the previous analysis. This section excludes the exceptional debt relief Bangladesh received in 2008 (amounting to US$678 million in constant 2017 dollars) in order to not distort the sectoral analysis.
9. Allocable ODA includes ODA allocated to specific sectors as well as ODA allocated to more than one sector (multi-sector) or to all sectors (cross-cutting). Non-allocable ODA includes ODA provided as commodity aid, general program assistance, and humanitarian aid (like disaster relief).
10. In order to keep Figure 8 legible, it does not display the relatively marginal ODA disbursed to the sixth social sector category, which the OECD refers to as "other social infrastructure and services". However, we have included this category in the percentage calculations.
11. See OECD – Development Assistance Committee (DAC) (2018).
12. Calculations by authors based on IMF (2016) and IMF (2018).
13. Similarly, Hassan and Prichard (2016) explain that Bangladesh's current tax system is characterized by low revenue collection and extensive informality. They conclude that Bangladesh's tax system is unusually informal, discretionary, and corrupt, but remains resistant to change because it delivers low and predictable tax rates to businesses, extensive opportunities for corruption to the tax administration, and an important vehicle for fundraising by political leaders and rent distribution to their elite supporters.
14. See https://bdnews24.com/business/2017/10/13/bangladesh-plans-to-introduce-two-slab-vat-rates-from-2020-muhith-says.
15. Based on July-November data for both fiscal years, as published by National Board of Revenue (NBR) in January 2019.
16. As reported in the *Daily Star* on January 4, 2019, Star Business, p. 1.
17. Alam and Shil (2009) focus on the performance of non-tax revenues in Bangladesh.
18. See *Financial Express* (2019) for further details.
19. Estimates by authors based on World Bank (2018a).

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