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SM/84/151

Supplement 1

CONTAINS CONFIDENTIAL  
INFORMATION

July 18, 1984

To: Members of the Executive Board

From: The Acting Secretary

Subject: Bangladesh - Staff Report for the 1984 Article IV Consultation

The attached supplement to the staff report for the 1984 Article IV consultation with Bangladesh has been prepared on the basis of additional information.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Al-Eyd (ext. (5)7335).

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INTERNATIONAL MONETARY FUND

BANGLADESH

Staff Report for the 1984 Article IV Consultation  
Supplementary Information

Prepared by the Staff Representatives for the  
1984 Consultation with Bangladesh

Approved by Tun Thin and Eduard H. Brau

July 17, 1984

1. Recent economic developments

According to information received since the Staff Report (SM/84/151, June 29, 1984) was issued, the 1983/84 external current account is now estimated to have recorded a smaller deficit than that presented in the Staff Report. Due to higher prices, exports for 1983/84 are now estimated to be \$825 million, \$40 million higher than the estimate in the Staff Report. Reflecting mainly the slower-than-expected recovery in the nonagricultural sector, imports are estimated to be around \$2.4 billion, approximately \$100 million lower than the estimate contained in SM/84/151. Due mainly to a decline in the number of Bangladeshi workers abroad, workers' remittances are estimated to be \$15 million less than originally estimated. A shortfall in aid disbursements appears to have occurred but developments with respect to the other capital items are less clear. At the end of the fiscal year, 1/ gross official reserves stood at \$516 million, equivalent to approximately two-and-a-half months' of imports.

Real GDP growth in 1983/84 is now estimated at less than 5 percent, due to a lower-than-expected increase in agricultural production and a less robust recovery in the nonagricultural sector. Although inflationary pressures intensified to about 11 percent in recent months, the average rate of inflation for the year as a whole is estimated to have remained below 10 percent. This reflected higher food prices caused by flood damages to foodgrain crops harvested in late spring and higher agricultural incomes due to the rise in prices for cash crops.

On the basis of developments during this period, the growth of liquidity appears to be broadly in line with the estimates presented in SM/84/151. However, the rate of expansion in public sector credit is now estimated to be substantially less due to a smaller borrowing requirement by the Government and a significant improvement in the

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1/ The fiscal year is from July 1 to June 30.

financial positions of the major public enterprises. In contrast, the growth in private sector credit is estimated to be much stronger than envisaged, with the rate of expansion approaching 37 percent during the first 11 months. The factors responsible for the surge in private sector credit include expansion in agricultural credit and substantial increases in advances against fixed-term deposits.

## 2. The 1984/85 budget

The 1984/85 budget that was announced on June 27, 1984 aims at providing further stimulus to economic growth while containing the overall deficit. The overall deficit is budgeted at Tk 39.6 billion (10.3 percent of GDP), compared with a likely deficit of Tk 35.9 billion (10.6 percent) in 1983/84 (Table 1). Most of the deficit will be financed by external assistance through grants and concessional loans. No provision is made in the budget for domestic bank financing of the overall deficit or foodstocking operations. In the past, foodstocking operations were financed by bank credit. Thus, the decision in respect of foodstocking operations marks a departure from previous practice.

Revenues are projected to increase by 24 percent, implying an increase in the revenue/GDP ratio of about 1 percentage point to 9 percent. The bulk of this increase will come from higher import-related revenues as a result of an expected growth of about 15 percent in dutiable imports. The budget introduced a number of new tax measures as well as measures to improve tax administration. These included adjustments in customs and excise duties, introduction of taxes on shop areas and on irrigation, extension of the 2 percent turnover tax to cover certain services, increases in postal rates and railway fares, and more effective income tax collection under a new ordinance. The measures are expected to yield about Tk 1 billion in additional revenue (about 0.3 percent of GDP).

Total expenditures are budgeted to increase by 16 percent to Tk 73.9 billion, remaining virtually unchanged in terms of GDP (19 percent). Current expenditures are expected to rise by 18 percent, mainly because of a 30 percent average increase in wages and salaries and other allowances that became effective on July 1, 1984. <sup>1/</sup> The increase in wages and salaries reflected adjustments for inflation since the last general increase and an attempt to improve the incentives for qualified personnel in the public sector. The Annual Development Plan (ADP) is targeted at Tk 39 billion, also representing an 18 percent increase over the likely outturn in the preceding year. In real terms, expenditure under the ADP is expected to increase by about 6-8 percent, the first significant real increase in several years. A core program of Tk 23.5 billion, or 60 percent of the ADP, has been approved. As in

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<sup>1/</sup> The last general wage and salary increase, which averaged 28 percent, was granted in July 1982.

Table 1. Bangladesh: Central Government Operations,  
1982/83-1984/85

	1982/83	1983/84 Staff Estimates <sup>1/</sup>	1984/85 Budget
<u>(In billions of taka)</u>			
Total revenue	25.6	27.7	34.3
Tax	20.6	22.4	27.5
Non-tax	5.0	5.3	6.8
Total expenditure	59.0	63.6	73.9
Current	19.2	21.7	25.5
Annual Development Program	29.8	33.0	39.0
Other	2.2	3.8	4.5
Food account deficit	7.8	5.1	4.9
Overall deficit	33.4	35.9	39.6
Excluding foodstocking	(33.1)	(34.3)	(...)
Net foreign financing	28.2	30.1	36.4
Project aid	13.4	16.8	20.8
Commodity aid	9.0	9.5	11.9
Food aid	6.4	6.7	6.3
Commercial food borrowing (net)	1.2	-1.0	-0.5
Debt amortization	-1.8	-1.9	-2.0
Net domestic financing	5.1	5.8	3.2
Banking system	-1.2	2.7	--
Other domestic (net)	6.3	3.1	3.2
<u>(As percent of GDP)</u>			
Memorandum items:			
Total revenue	8.8	8.2	8.9
Total expenditure	20.1	18.8	19.1
Overall deficit	11.4	10.6	10.3
Excluding foodstocking	(11.3)	(10.2)	(...)

Sources: Data provided by the Bangladesh authorities; and  
staff estimates.

<sup>1/</sup> As presented in SM/84/151, (June 29, 1984).

previous years, the core program concentrates on the completion of ongoing projects and new projects that are foreign-assisted and quick yielding.

### 3. Other measures

In conjunction with the 1984/85 budget, the Government adopted important policy measures in areas outside the budget. To encourage higher domestic food production, foodgrain procurement prices were raised by 10 percent for rice and by 15 percent for wheat on July 1, 1984. However, in order to further reduce the per unit subsidy, fertilizer prices were increased by 10 percent, effective July 7, 1984. In the monetary area, the statutory liquidity requirement for time deposits was reduced from 25 percent to 23 percent, in order to provide incentives for banks to accept fixed deposits and to increase their portfolio of medium-term lendings. Furthermore, the rate of interest on savings deposits with checking facilities in the rural areas was raised by 1 percentage point to 9.5 percent in order to encourage financial intermediation in these areas.

In the external area, Bangladesh Bank issued new regulations, effective July 7, 1984, aimed at broadening the participation in the secondary foreign exchange market and stabilizing the premium over the official exchange rate. Scheduled banks are now authorized to participate in the secondary foreign exchange market to buy foreign exchange for their own use or on behalf of their clients; they are not obligated to surrender foreign exchange so acquired. In the recent months prior to the new regulations, the premium of the secondary foreign exchange market rate over the official rate varied between 6 percent and 13 percent. Under the new regulations, the premium will be not less than 7 percent and not more than 10 percent. A committee of the major scheduled banks will establish exchange rates that will be in effect for three days at a time. The Bangladesh Bank will be ready to buy and sell foreign exchange to scheduled banks at a very small premium over the rate prevailing in the secondary foreign exchange market. Moreover, with a view to encouraging exports, the authorities introduced a 100 percent entitlement rate for leather products, jute carpets, and tea bags under the Export Performance Licensing Scheme (XPL), and raised entitlement rates for certain other items. In addition, import entitlement certificates under the XPL are now allowed to be auctioned at the secondary foreign exchange market.